# Anticipated Acquisition by Macquarie Asset Management of a jointly controlling interest in Last Mile Infrastructure (Holdings) Limited

## Decision on relevant merger situation and substantial lessening of competition

**ME 7095/24**

The Competition and Markets Authority's decision on relevant merger situation and substantial lessening of competition under section 33(1) of the Enterprise Act 2002 given on 16 September 2024. Full text of the decision published on 10 October 2024.

The Competition and Markets Authority (**CMA**) has excluded from this version of the decision information which the CMA considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Some numbers have been replaced by a range, which are shown in square brackets.

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# SUMMARY

## OVERVIEW OF THE CMA'S DECISION

1. The Competition and Markets Authority (**CMA**) has found that the acquisition by Macquarie Group Limited (**Macquarie**), through its indirectly owned funds, of 50% of the issued share capital of Last Mile Infrastructure (Holdings) Limited (**LMI**) (the **Merger**), is a relevant merger situation that does not give rise to a realistic prospect of a substantial lessening of competition (**SLC**).

2. Macquarie agreed to indirectly acquire shares representing 50% of the total voting rights in LMI from Infracapital further to a share purchase agreement entered into on 16 December 2023. The remaining shares and voting rights in LMI will be retained, indirectly, by Infracapital.

### Who are the businesses and what products/services do they provide?

3. Macquarie, via Macquarie Asset Management, is active in the UK gas sector through its stake in Cadent Gas Limited (**Cadent**) and National Gas Transmission plc (**NGT**) and in the water and wastewater sector through its stake in Southern Water Services Limited (**Southern Water**).

4. LMI and its subsidiaries design, build, own and operate last mile utilities infrastructure, including gas, water and wastewater connections in Great Britain.

5. For the purposes of this investigation, the CMA has focused on the vertical relationships between:

   (a) Macquarie, via its interest in Cadent, an operator of a gas distribution network, and LMI, which is active downstream in the provision of last mile gas connections; and

   (b) Macquarie, via its interest in Southern Water, an appointed water and sewage undertaker, and LMI, which is active downstream in the provision of last mile water and wastewater connections.

6. Macquarie and LMI are together referred to as the **Parties** and, for statements relating to the future, the **Merged Entity**.

### Why did the CMA review this merger?

7. The CMA has a statutory duty to promote competition for the benefit of consumers. This includes a duty to investigate mergers that could raise

competition concerns in the UK where it has jurisdiction to do so. In this case, the CMA has concluded that it has jurisdiction to review this Merger because a relevant merger situation has been created: each of Macquarie and LMI is an enterprise that will cease to be distinct as a result of the Merger and the turnover test is met.

8. The CMA has also considered the Merger further to its duty under section 68C of the Enterprise Act 2002 (the **Act**) in connection with mergers of energy network enterprises and decided not to refer the Merger to a phase 2 investigation in a separate decision on 16 September 2024.

## What evidence has the CMA looked at?

9. To understand the impact of the Merger on competition, the CMA considered a wide range of evidence in the round. The CMA received several submissions and responses to information requests from the Parties and reviewed a number of the Parties' internal documents to understand their businesses, competitive strategies and plans, and the competitive landscape in which they operate. The CMA also gathered data on shares of supply and bidding data.

10. The CMA spoke to and gathered evidence from other sector participants, including competitors and customers, which included both written and oral submissions to better understand the competitive landscape and to get their views on the Merger.

11. Throughout its phase 1 investigation, in line with its guidance in relation to merger investigations involving regulated sectors, the CMA also engaged with the Office of Gas and Electricity Markets (**Ofgem**) and the Water Services Regulation Authority (**Ofwat**) given their sector expertise.

## What did the evidence tell the CMA about the effects on competition of the Merger?

12. The CMA considered whether the Merger would lead to an SLC as a result of vertical effects in the markets for the installation and adoption of last mile gas, water and wastewater connections. The CMA found that the Merger does not give rise to a realistic prospect of an SLC in any of these areas for the reasons below.

*Theory of harm 1: Input foreclosure in the installation and adoption of last mile gas connections in the Cadent Region*

13. The CMA considered whether the Merged Entity could use Cadent's position (upstream) to provide LMI with certain advantages to the detriment of LMI's rivals in the installation and adoption of last mile gas connections (downstream) in those

regions where Cadent has a statutory duty to connect, that is, in the North West, West Midlands, East Midlands, South Yorkshire, East of England and North London (the **Cadent Region**). For example, the CMA considered whether the Merged Entity could slow down the speed at which Cadent approves last mile gas connections by LMI's rivals to its network or quote a higher price for connections to LMI's competitors.

14. The CMA found that although Cadent holds a position of market power and provides an essential input in the Cadent Region, the Merged Entity would have only limited ability to disadvantage LMI's rivals due to (i) existing regulation enforced by Ofgem which provides some protection to competing suppliers and (ii) the fact that Macquarie only holds a minority stake in Cadent, which means that Macquarie is not able to take unilateral strategic decisions with respect to Cadent.

15. The CMA also found that the Merged Entity would not have the incentive to engage in behaviour which would disadvantage LMI's rivals. This is because the risk of enforcement action by Ofgem would act as an effective deterrent and Cadent's other shareholders would have no incentive to allow Cadent to favour LMI, especially if this risks financial penalties or other enforcement action.

*Theory of harm 2: Input foreclosure in the installation and adoption of last mile water connections in the Southern Water Region*

16. The CMA also assessed whether the Merged Entity could use Southern Water's position (upstream) to provide LMI with certain advantages to the detriment of its rivals in the installation and adoption of last mile water connections (downstream) in those regions where Southern Water is active, that is in East and West Sussex, Kent, Hampshire and the Isle of Wight (the **Southern Water Region**). For example, the CMA considered whether Southern Water could charge higher prices or set less preferential tariffs to LMI's rivals when negotiating bulk water supply agreements.

17. The CMA found that the Merged Entity may have some ability to disadvantage LMI's rivals, particularly given that: (i) Southern Water holds a position of market power; (ii) Southern Water's input is necessary for downstream players to provide their services; and (iii) existing regulation enforced by Ofwat may not eliminate all the ways in which Southern Water might disadvantage LMI's rivals in the relevant downstream markets. However, the CMA found that the Merged Entity would not have the incentive to disadvantage LMI's rivals. Despite the potential benefits from securing contracts downstream, the costs of foreclosure would be high, particularly given: (i) the likelihood that such a strategy would be detected by rivals or the developers they serve; (ii) once detected, enforcement action from Ofwat could lead to significant financial penalties; (iii) the strategy would likely result in

additional financial losses via D-MEX (Ofwat's framework that scores incumbents on their relative service levels); and (iv) given the relative shareholdings in the two companies, the Merged Entity would only enjoy half of the benefits of such a strategy yet would bear most of the costs.

*Theory of Harm 3: Input foreclosure in the adoption of last mile wastewater connections in the Southern Water Region*

18. Similarly, the CMA assessed whether the Merged Entity could use Southern Water's position (upstream) to provide LMI with certain advantages to the detriment of its rivals in the adoption of last mile wastewater connections (downstream) in the Southern Water Region.

19. The CMA found that the Merged Entity may have some ability to disadvantage LMI's rivals, particularly given that: (i) Southern Water holds a position of market power; (ii) Southern Water's input is necessary for rivals to provide their services; and (iii) existing regulation enforced by Ofwat may not eliminate all the ways in which Southern Water might disadvantage LMI's rivals in the relevant downstream market.

20. However, and for the reasons set out in paragraph 17 above (given the lack of differences in the evidence base for water and wastewater) the CMA found that the Merged Entity would not have the incentive to pursue a foreclosure strategy against rivals in the adoption of last mile wastewater connections in the Southern Water Region.

## What happens next?

21. The Merger will therefore **not be referred** under section 33(1) of the Act.

# ASSESSMENT

## PARTIES, MERGER AND MERGER RATIONALE

### Parties

22. Macquarie is a global provider of banking, financial, advisory, investment and funds management services and is listed on the Australian Securities Exchange.[1] Macquarie Asset Management (**MAM**), a division of Macquarie, is a specialist global asset manager with investments in electricity and gas distribution, gas transmission and water and wastewater utilities.[2] MAM is active in the UK gas sector through its minority stake in Cadent[3] and is active in the water and wastewater utilities sector through its majority stake in Southern Water.[4]

23. MAM manages assets on behalf of third-party investors, acting through its portfolio manager, Macquarie Infrastructure and Real Assets (Europe) Limited (**MIRAEL**). Macquarie European Infrastructure Fund 7 SCSp (**MEIF7**), in turn, is a fund that is portfolio managed by MIRAEL and has a mandate to invest into assets across Europe.[5] Macquarie's turnover (including its wider group of companies) for the year ending 31 March 2023 was [✂] worldwide and [✂] in the UK.[6]

24. Separately, Macquarie Capital (**MacCap**), a division within the Macquarie group, also holds a majority share ([✂]%) in Matrix Group (**Matrix**). Matrix installs last mile electricity, gas and water connections, and adopts last mile electricity connections, through Matrix Networks.[7]

25. In the remainder of this Decision, the CMA refers to Macquaire and/or MAM and/or MIRAEL and/or MEIF7 and/or MacCap, collectively as **Macquarie**.

26. Infracapital, headquartered in the UK, is the infrastructure equity investment business unit of M&G plc and manages funds, namely: Infracapital Partners III (Euro) SCSp and Infracapital Partners III (Sterling) SCSp.[i] These funds, acting by their respective managers,[8] [ii] indirectly own 100% of the issued share capital of

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[1] Final Merger Notice submitted to the CMA on 18 July 2024 (**FMN**), paragraph 4.
[2] FMN, paragraph 23. MAM also has an interest in NGT, which is an owner and operator of the national transmission system for gas. FMN, paragraph 30(a).
[3] MAM manages a stake of approximately 26% in Cadent on behalf of its managed funds, noting that MAM's own direct ownership is approximately 12%. FMN, paragraph 24.
[4] FMN, paragraph 24. MAM manages a stake of [✂]% in Southern Water; Parties' response to the Issues Letter, 20 August 2024, paragraph 105.
[5] FMN, paragraphs 3, 12 and 26.
[6] FMN, paragraph 42. The UK turnover of MEIF7 (including the wider Macquaire group of companies) for 2023 is not available. This figure reflects MEIF7 group's worldwide turnover, excluding its EU-wide turnover (FMN, footnote, 25).
[7] FMN, paragraphs 4 and 28(d).
[8] ie M&G Alternatives Investment Management Limited and ICP (Finch) LP acting by its manager M&G Investment Management Limited (together the '**ICP Funds**'); FMN, paragraph 3.

LMI.[9] LMI and its subsidiaries design, build, own and operate last mile utilities infrastructure, including electricity, gas, water, wastewater and heat connections in Great Britain. [10] LMI's UK turnover in the year ending 31 March 2024 was £[✂].[11]

## Merger

27. On 16 December 2023, Macquarie (through its group company Connex Bidco Limited) and Infracapital (through its managed funds) entered into a share purchase agreement, whereby Macquarie (via MEIF7) will indirectly acquire shares representing 50% of the total voting rights in LMI, through wholly owned intermediate companies, as well as [✂].[12] The remaining shareholding and voting rights of LMI will be retained, indirectly, by Infracapital.[13]

28. The Parties informed the CMA that completion of the Merger is subject to approval from the Secretary of State under the National Security and Investment Act 2021, which was received on 8 March 2024, as well as merger control clearance by the European Commission, which was received on 26 February 2024.[14]

## Merger rationale

29. The Parties submitted that the rationale for the Merger is as follows:

    (a) For Macquarie, LMI offers [✂].[15]

    (b) For Infracapital, the Merger would enable Infracapital to [✂].[16]

30. The CMA considers that the Parties' internal documents are broadly in line with their stated strategic and economic rationale.[17]

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[9] FMN, paragraphs 3 and 32–33.
[10] The LMI group of companies is made up of a number of businesses that provide last mile utility connections and metering services in Great Britain, namely (a) Energetics Design & Build Limited, UK Power Solutions Limited, and Icosa Water Ltd active in installation/construction businesses; (b) Last Mile Electricity Limited, Icosa Water Services Limited, Last Mile Gas Limited and Last Mile Heat Limited, active in adoption; and (c) Last Mile Asset Management Limited, active in in-house asset management. FMN, paragraphs 5, 17–18.
[11] Email from Clifford Chance LLP to the CMA on 28 August 2024, 14:19.
[12] Annex 8.001 to the FMN, 'Share Purchase Agreement – Executed 16 December 2023', December 2023.
[13] FMN, paragraphs 3 and 7-8 and Annex 8.001 to the FMN, 'Share Purchase Agreement – Executed 16 December 2023', December 2023.
[14] FMN, paragraph 14.
[15] FMN, paragraph 12.
[16] FMN paragraph 13.
[17] See for example, Macquarie Internal Documents, Annex 9.005 to the FMN, [✂]; Annex 9.006 to the FMN, [✂].

# PROCEDURE

31. The CMA's mergers intelligence function identified the Merger as warranting an investigation.[18]

32. The CMA commenced its phase 1 investigation on 22 July 2024. As part of its phase 1 investigation, the CMA gathered a significant volume of evidence from the Parties. In response to targeted information requests, the CMA received and reviewed internal documents from Macquarie and LMI to understand the impact of the Merger in the utilities sector. The Parties also had opportunities to make submissions and comment on our emerging thinking throughout the phase 1 investigation. For example, on 19 August 2024 the CMA invited the Parties to attend an Issues Meeting, and the Parties submitted their views in writing.

33. The CMA also gathered evidence from other market participants, such as competitors and customers. The evidence the CMA has gathered has been tested rigorously, and the context in which the evidence was produced has been considered when deciding how much weight to give it.

34. Throughout its phase 1 investigation, in line with its guidance in relation to merger investigations involving regulated sectors, the CMA also engaged with Ofgem and Ofwat, given their sector expertise.

35. Where necessary, this evidence has been referred to within this Decision.

36. The Merger was considered at a Case Review Meeting.[19]

37. The CMA has also considered the Merger further to its duty under section 68C of the Act in connection with mergers of energy network enterprises and decided not to refer the Merger to a phase 2 investigation in a separate decision on 16 September 2024.

# JURISDICTION

38. A relevant merger situation exists where two or more enterprises cease to be distinct and either the turnover or the share of supply test is met.

## Enterprises ceasing to be distinct

39. Each of Macquarie and LMI is an enterprise within the meaning of section 129 of the Act. As a result of the Merger, these enterprises will cease to be distinct. The

[18] Mergers: Guidance on the CMA's jurisdiction and procedure (**CMA2**), 25 April 2024, paragraphs 6.4–6.6.
[19] CMA2, page 39.

Merger will result in Macquarie holding 50% of the issued share capital in LMI and Infracapital retaining the remaining 50%.

40. The CMA currently considers that Macquarie will be able to exercise at least material influence over LMI by virtue of:[20]

(a) its shareholding in LMI of 50%;

(b) its power, via its subsidiary MEIF7, to appoint [✂] members to the board of LMI (with the remaining [✂] to be appointed by Infracapital). Board decisions are taken by majority vote with each resolution requiring a positive vote from a Macquarie appointed director and an Infracapital appointed director; and

(c) its veto rights [✂], as well as other governance rights.

### Turnover test

41. The UK turnover of LMI exceeded £70 million in the last financial year, as referred to in paragraph 26 above, so the turnover test in section 23(1)(b) of the Act is satisfied.

### Conclusion

42. The CMA 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.

43. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 22 July 2024 and the statutory 40 working day deadline for a decision is therefore 16 September 2024.

## COUNTERFACTUAL

44. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual).[21]

45. The Parties submitted that the relevant counterfactual against which to assess the Merger is the prevailing conditions of competition.[22] In this case, the CMA has not received submissions (or other evidence) suggesting that the Merger should be

[20] This is also consistent with the Parties' submissions (FMN, paragraphs 7, 8 and 40).
[21] Merger Assessment Guidelines (**CMA129**), March 2021, paragraph 3.1.
[22] FMN, paragraph 78.

assessed against an alternative counterfactual.[23] Therefore, the CMA believes the prevailing conditions of competition to be the relevant counterfactual.

# COMPETITIVE ASSESSMENT

## Background and nature of competition

46. The Parties overlap in the installation and adoption of last mile utility connections (mainly water, gas and electricity). The CMA focused its assessment of the Merger on the vertical relationships between:[24]

    (a) Macquarie, via its interest in Cadent, an operator of a gas distribution network,[25] and LMI, which is active downstream in the provision of last mile gas connections; and

    (b) Macquarie, via its interest in Southern Water, an appointed water and sewage undertaker,[26] and LMI, which is active downstream in the provision of last mile water and wastewater connections.

47. This section provides an overview of these activities.

### The supply of utility connections

48. Utility connections enable homes and other buildings to have access to essential services such as gas, electricity, water, wastewater disposal and fibre.[27]

49. Historically, utility connections were supplied by state-owned network operators with exclusive areas of operation within the UK (also known as incumbents). Many of these operators were privatised in the 1990s in the UK and today utility

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[23] The Parties added that the CMA should assess, as part of its forward-looking assessment of the Merger, the competitive impact of expected policy and legislative changes in the relevant sectors (notably the Future Homes Standard/Future Buildings Standard) and equivalent devolved administration legislative changes. In particular, the Parties expect that as a result of the Future Homes Standard, the demand for new natural gas connections is likely to progressively decrease (FMN, paragraphs 78 and 103). The CMA has taken this into account, where relevant, as part of the competitive assessment.
[24] The Parties also overlap horizontally in the installation and adoption of electricity connections, gas connections and water connections, and in the adoption of wastewater connections. However, following initial scrutiny of these segments with the Parties and third parties, and having regard in particular to the low increment resulting from the Merger and the existence of a number of alternative players in each of these segments, the CMA does not believe that any plausible Merger-related competition concerns could arise in relation to these horizontal overlaps. Only one third party [✂] expressed concerns about the reduction in the number of independent utility infrastructure providers (**UIPs**) (which install gas connections). However, the CMA notes that there were 174 UIPs for gas across the UK, as of April 2024 (FMN, paragraph 85(a) based on the Lloyd's Register Quality Assurance (**LRQA**) database available at Find a GIRS accredited UIP | LRQA UK), and as such the CMA does not consider that the Merger would give rise to competition concerns as a result of the overlap between the Parties as UIPs. Therefore, the horizontal overlap in the Parties' activities in these areas are not considered further in this Decision.
[25] FMN, paragraph 24.
[26] FMN, paragraph 24.
[27] Anticipated acquisition by Brookfield Asset Management Inc. of a minority shareholding in Scotia Gas Networks Limited, [ME/6960/21], (**Brookfield/SGN**) paragraph 45.

connections are supplied by private operators, including new suppliers of utility connections.[28]

50. The UK government's housing targets indicate that the markets for new connections are likely to grow considerably in the medium-to-long term.[29]

**Last mile utility connections**

51. Last mile connections constitute the infrastructure that connects homes and other premises to a larger network nearby through which the essential utilities pass.[30]

52. The previously state-owned 'incumbent' suppliers of utility connections have developed (mainly owing to their monopoly status) large infrastructure networks that connect to the original source of the utilities. Suppliers of last mile connections typically connect to larger networks such as these and not the original utility source.[31]

**Installation and adoption of last mile utility connections**

53. The supply of last mile utility connections involves two stages. These are:

    (a) installation, which involves the placing of the physical infrastructure required to activate the connection; and

    (b) adoption, which involves the ownership and long-term management of the installed infrastructure. Adoption responsibilities include asset management and maintenance and charging property owners for such services.[32]

54. Some suppliers offer both installation and adoption, whilst others are involved in only one of the two stages. The process whereby a company both installs and adopts a particular connection is known as self-adoption. Suppliers that adopt a connection installed by another company (and are therefore not involved in the installation itself) are referred to as third party adopters.[33] Either way, once a connection has been installed and adopted, there is typically no further competition for the connection.[34]

55. The Parties submitted that competition takes place via a bidding process and most customers (including housebuilders and developers) procure the installation and

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[28] FMN, paragraphs 82 and 105. Also, Brookfield/SGN, paragraph 46.
[29] FMN, paragraph 12 (c).
[30] FMN, paragraph 80. Also, Brookfield/SGN, paragraph 47.
[31] FMN, paragraphs 82 and 105. Also, Brookfield/SGN, paragraph 48.
[32] FMN, paragraphs 84–86. Also, Brookfield/SGN, paragraph 49.
[33] FMN, paragraphs 88. Also, Brookfield/SGN, paragraph 50.
[34] FMN, paragraph 88.

adoption of utilities together. The choice of an installer is a commercial decision for the customer. Installers compete based on construction costs, as well as the ease of working on issues such as design approval, reputation, and speed,[35] whereas third party adopters mainly compete to win business from installers by offering higher asset payments,[36] although other factors are also considered, including quality of service.[37]

56. Some companies offer last mile installation and/or adoption for multiple utilities. These utility connections can include gas, electricity, water and/or wastewater (as well as heat and/or fibre). Many developers prefer to work with multi-utility connection suppliers due to the convenience of working with a single supplier for multiple utilities. However, some developers choose to use separate suppliers for different utilities.[38]

**Last mile gas connections**

57. The market for last mile gas connections was opened to competition in the 1990s.[39] Since then, installers, referred to as UIPs, and adopters, referred to as independent gas transporters (**IGTs**), have become more active in providing last mile gas connections alongside incumbents, as described above in paragraph 49.[40]

58. The next sections provide an overview of these players.

*Regulated gas companies (Incumbents)*

59. Pursuant to the Gas Act 1986 (**Gas Act**), Ofgem regulates Gas Distribution Network (**GDN**) operators. GDNs hold a gas transporter licence, which includes certain conditions in relation to pricing, duty to connect and others, as discussed further below in paragraphs 68 to 73.

60. GDNs are responsible for operating and maintaining a structure of pipelines in set geographic regions and transporting gas through those pipelines from the national transmission system to end customers. Where a last mile connection is adopted by an IGT in the GDN's area, that connection will need to be connected to the regional structure of pipelines run by the GDN.[41]

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[35] FMN, paragraph 100.
[36] See paragraph 66 below.
[37] Brookfield/SGN, paragraph 56.
[38] FMN, paragraphs 89–91. Also, Brookfield/SGN, paragraph 51.
[39] FMN, paragraph 82.
[40] FMN, paragraphs 85 and 87. Also, Brookfield/SGN, paragraph 58.
[41] FMN, paragraph 341.

61. As described in paragraph 13 above, Cadent is a GDN and the incumbent supplier of gas connections in the Cadent Region.

*UIPs*

62. UIPs contract with customers to construct and install new gas connections. As UIPs are not transporters of gas, they do not require a licence from Ofgem to carry out their activities. However, UIPs are required to be accredited and audited by specific schemes operated by LRQA for various credentials including health, safety, environmental and quality standards.[42]

63. As described above in paragraph 55, competition typically takes place via a bidding process, although a customer may also approach an installer directly to procure a quote.[43] Typically, installers provide a single quote for both installation and adoption services across all utilities provided at the site.

64. Matrix and LMI are both UIPs active in the installation of last mile gas connections.[44]

*IGTs*

65. IGTs, which are adoption businesses, must operate under licences granted by Ofgem (ie a gas transporter licence). They are also subject to certain duties and obligations under legislation and the regulatory framework set by Ofgem.[45]

66. Developers tend to have little to no interaction with the process of gas infrastructure adoption, which is left to the installer to either arrange with a third-party adopter or its own affiliated adoption business.[46] When an installer provides a quote to a customer, this will typically also include an adoption payment quote from the adopter. The adopter agrees an 'asset value' payment to the installer to account for future cashflows associated with managing the installed assets. This payment is generally then offset by the installer against the total costs charged to the customer, meaning the customer benefits from reduced capital.[47]

67. LMI is an IGT active in the adoption of last mile gas connections. Matrix is not licensed to adopt gas connections.[48]

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[42] FMN, paragraph 85. Also, Brookfield/SGN, paragraph 60.
[43] FMN, paragraph 96. Also, Brookfield/SGN, paragraph 52.
[44] FMN, paragraph 343. Matrix currently only supplies gas installation services when [✂] but does not [✂] (FMN, paragraph 143).
[45] FMN, paragraph 87. Also, Brookfield/SGN, paragraph 59.
[46] FMN, paragraph 98. Also, Brookfield/SGN, paragraph 54.
[47] FMN, paragraph 99.
[48] FMN, paragraphs 143 and 344.

## Gas regulation

68. Ofgem, is the energy regulator for Great Britain. It grants licences to companies under the Gas Act and ensures that those companies comply with the requirements and conditions of their licence.[49] As described above in paragraphs 59 and 65, GDNs and IGTs operate under licences granted by Ofgem.

*Duty to connect*

69. GDNs and IGTs are under a duty to provide new gas connections in accordance with the requirements of section 9 and 10 of the Gas Act on a non-discriminatory basis.[50]

70. GDNs and IGTs are required to grant a UIP a connection to their network where the UIP places the pipework needed to reach that network. Due to the reach of GDNs' pre-existing networks, it is often the case that UIPs rely on and therefore request connections to the GDNs' networks. These requests go through an application process which may vary in duration and complexity depending on different factors including the specific gas load/pressure needed by the premises in question.[51]

*Duty to avoid undue preference or undue discrimination*

71. Incumbent GDNs are subject to a number of licence conditions that are designed to prevent them from preferring certain IGTs and UIPs above others.[52] For example, Standard Special Condition A6 prevents a GDN from obtaining an unfair commercial advantage including, in particular, any such advantage from a preferential or discriminatory arrangement in connection with a business other than its transportation business.[53] The purpose of this condition is to ensure that a GDN treats all IGTs equally, including downstream IGTs owned by the GDN.

*Pricing*

72. Standard Licence Condition 4B requires that both GDNs and IGTs ensure their connection charging methodologies do not restrict, distort or prevent competition, and to ensure that no undue preference and/or discrimination is shown by the licensee. The connections charging methodology must be approved by Ofgem,

[49] Industry licensing | Ofgem
[50] FMN, paragraph 353. Also, Brookfield/SGN, paragraph 61.
[51] Brookfield/SGN, paragraphs 62–63.
[52] FMN, paragraph 354.
[53] FMN, paragraph 353.

and GDNs must report any subsequent changes to the methodology to Ofgem, explaining how the modification would better achieve the licence objectives.[54]

*Service standards*

73. Standard Special Condition D10 requires a GDN to achieve a 90% performance standard in the issuance of quotes for connections and to make connections and to complete certain works within a designated time frame. In addition, GDNs must also comply with the Gas (Standards of Performance) Regulations, which also apply to connections activities, which set out timeframes in which GDNs must respond to or complete certain actions for their customers (such as responding to a request for a quotation). Failure to comply with these conditions would require the GDN to pay a prescribed sum to the customer.[55]

**Last mile water and wastewater connections**

74. The supply of last mile water connections was opened to competition in 2017, when Ofwat introduced reforms in the sector, which came into effect in April 2020.[56] Since then, installers, referred to as self-lay providers (**SLPs**) and adopters, referred to as New Appointments and Variation entities (**NAVs**) have become more active in the provision of water and wastewater connections alongside the incumbents, as described in paragraph 49 above.

75. For installation, SLPs compete with incumbents on price and service, and for some customers, eg housebuilders that require a large volume of connections, service is often an important parameter of competition such that incumbents typically do not compete.[57]

76. For adoption, the Parties submitted that the incumbent and a NAV will compete on factors such as pricing, adoption standards and contract terms.[58] The Parties also submitted that the presence of NAVs has grown rapidly in response to reforms by Ofwat.[59] This is consistent with the views of third parties who noted that the market is moving away from incumbents, with NAVs adopting water and wastewater connections due to the difference in price for the developer/customer.[60]

77. The next sections provide an overview of these players.

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[54] FMN, paragraph 353.
[55] FMN, paragraph 353.
[56] FMN, paragraphs 115 and 286.
[57] Note of call with a third party, June 2024 [✂]. The Parties submitted that Southern Water does not compete for water installation opportunities (see FMN, paragraph 271).
[58] FMN, paragraph 119.
[59] FMN, paragraphs 115 and 292-295.
[60] Notes of calls with third parties, June & July 2024 [✂] and [✂].

*Regulated water and wastewater companies (Incumbents)*

78. Pursuant to the Water Industry Act 1991 (**Water Act**), Ofwat regulates both Water and Sewerage Companies (**WASCs**) and Water-only Companies (**WOCs**). WASCs are appointed under the Water Act to provide both wholesale and retail water supply and wastewater services in their appointed regions,[61] whereas WOCs are appointed to provide only wholesale and retail water supply services in a specified region.[62]

79. As described in paragraph 16 above, Southern Water is a WASC and the incumbent supplier of water and wastewater connections in the Southern Water Region.[63]

*SLPs*

80. SLPs install water infrastructure, before it is connected to the mains and adopted by either an incumbent regulated water company (as described above in paragraph 78) or a NAV company (as further described below in paragraph 84).[64] SLPs are, therefore, active in the installation of infrastructure only, and are not licensed to adopt connections.[65]

81. SLPs must be accredited before they can carry out work, either by applying to the relevant water company, or becoming accredited under the Water Industry Registration Scheme (**WIRS**) which is recognised by all the water companies and Water UK.[66] SLPs will submit their plans for approval to the relevant water company, and either the NAV or the incumbent that is adopting the connection will confirm that the infrastructure has met the relevant standard for the adoption.[67]

82. SLPs compete for customers, such as housing developers, typically through a bidding process. Once approached by a developer, an SLP will typically submit a one-off bid, seeking to offer a combination of the best price and best service delivery. Before submitting its bid, the SLP will undertake its own competitive selection process to secure the best asset value from a selection of NAVs for the adoption of the asset (see paragraph 88 below). The level of asset value is the

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[61] These services comprise of water abstraction, treatment and delivery, and wastewater collection, treatment and disposal. FMN, paragraph 107.
[62] FMN, paragraph 108.
[63] FMN, paragraph 391. Within the Southern Water Region, four WOCs, namely Affinity Water Limited, Portsmouth Water Limited, South East Water Limited and Bournemouth Water Ltd are also active. In the areas where these WOCs are active, the area is, therefore, a dual incumbency area, in which the WOCs provide water services and Southern Water only provides wastewater services. FMN, paragraph 117.
[64] FMN, paragraph 111.
[65] FMN, paragraph 112.
[66] FMN, paragraph 112. Water UK is the trade association for the water industry Homepage | Water UK.
[67] FMN, paragraph 112.

fundamental driver in terms of allowing the SLP to offer the lowest/most competitive price to the developer.[68]

83. LMI and Matrix are SLPs active in the installation of last mile water connections.[69]

*NAVs*

84. NAVs are independent water companies, licensed by Ofwat to adopt water and wastewater connections.[70]

85. NAVs replace the incumbent water company as the appointee and provide water and/or wastewater services to customers in a defined area. In contrast to other utilities, NAVs can supply water and wastewater services directly to household and non-household customers, in addition to operating the public water networks. Once a NAV adopts a connection, it will subsequently also provide retail water and wastewater services to end-customers.[71]

86. To ensure a specific project is financially viable for a NAV to adopt, Ofwat requires NAVs to submit project-level financial modelling and evaluation of the proposed project. Accordingly, it is not sufficient for a NAV to be appointed by Ofwat for a first project (New Appointment); it must also receive specific approval in relation to each subsequent project (Variation).[72] NAVs therefore require approval from Ofwat for each site that they adopt.

87. In practice, this means that for every site where a new appointment or a variation is granted and the NAV does not have its own water / wastewater resources, the NAV has to negotiate an agreement with the incumbent, for example to specify the point of connection and the volume of water supplied,[73] which leads to greater interaction with the incumbent.[74] Because the financial viability of the site is heavily dependent on levels of bulk supply and discharge charges, Ofwat requires the NAV to explain how their forecasts costs and revenues have been calculated with reference to these charges, with links to the charges published by the incumbent.[75]

88. NAVs may be selected for the adoption of water and/or wastewater connections either through a competitive selection process by the SLP, or by the developer. When competing for an adoption contract, NAVs offer an ‘asset value’ payment to

[68] Parties’ response to the CMA’s request for information, dated 1 August 2024 (**Annex RFI5 – MAM**), paragraph 4.
[69] Neither of the Parties is active in the installation of last mile wastewater connections. Matrix installs a small number of last mile water connections when [✂]but does not [✂]. FMN, paragraph 146.
[70] NAVs may also install connections and provide services at a site which was previously serviced by the incumbent regulated water company FMN, paragraph 113.
[71] FMN, paragraphs 119, 393.
[72] FMN, paragraph 114.
[73] Ofwat’s response to the CMA’s request for information, dated 20 August 2024, page 5.
[74] Note of call with a third party, July 2024 [✂].
[75] Ofwat’s response to the CMA’s request for information, dated 20 August 2024, page 5.

the installer to account for future revenue stream cashflows associated with managing the installed assets. Where the SLP is organising the selection process, this payment is generally then offset by the SLP against the total costs charged to the developer, meaning the developer benefits from reduced capital requirements.[76]

89. LMI is a NAV active in the adoption of water and wastewater connections (including third-party adoption). Matrix does not currently adopt water and wastewater connections but is in the process of applying for a new NAV licence to adopt water and wastewater connections in future.[77]

**Water and wastewater regulation**

90. Ofwat is the body responsible for economic regulation of the privatised water and sewerage industry in England and Wales.[78]

91. Ofwat regulates the sector to ensure, among other things, that no undue preference or discrimination is shown by water companies in fixing charges or in relation to the provision of services by themselves or by water supply licensees or sewerage licensees.[79]

*Duty to connect*

92. Incumbents have a statutory duty to connect by responding to customer enquiries and providing and adopting connections in response to customer requests, in line with regulatory obligations.[80]

*Duty to avoid undue preference or undue discrimination*

93. Incumbent WOCs and WASCs are subject to certain regulatory obligations under their instruments of appointment.

94. For example, Condition E1 of Ofwat's instrument of appointment prevents regulated water companies from showing undue preference towards (including towards itself), or undue discrimination against, any person in the provision of various services, including laying of water and wastewater connections, and provision of water and wastewater services. Under this Condition, the appointee must not disclose or use certain information received for any purposes other than the limited exemptions specified in the Condition. Further, Condition E also applies

[76] FMN, paragraphs 97 and 99 and Annex RFI5 – MAM, paragraph 14.
[77] FMN, paragraph 147.
[78] See Home - Ofwat.
[79] See Our duties - Ofwat.
[80] FMN, paragraphs 18, 310 and 392. See also Getting a connection - Ofwat

to prevent an appointee from setting its charges in a way which results in undue preference in favour of, or undue discrimination against, any of its customers or potential customers.[81]

*Pricing*

95. Water and wastewater price controls are set by Ofwat.[82]

96. WASCs and WOCs are subject to Ofwat's Price Review process, which determines the prices water companies can charge their customers over a set period. Ofwat sets allowed revenues for fixed periods using ex-ante price control frameworks.[83] WASCs and WOCs set their charges to recover the total revenues allowed by Ofwat through the price control as the combination of efficient wholesale costs and efficient residential retail costs.[84] Although retail pricing for water is no longer regulated by Ofwat further to market opening, incumbent WASCs and WOCs are still regulated and subject to certain controls, for example the residential retail costs incurred by WASCs and WOCs form part of the regulated cost base.

97. With respect to NAVs, Ofwat has established a 'no worse off' principle, where it caps prices for NAVs so that their retail prices are no higher than they would be under the incumbents' charges.[85]

*Service standards*

98. Incumbent WOCs and WASCs are subject to certain reportable levels of service, determined by Ofwat.[86] For example, an incumbent would be expected to complete certain tasks within defined periods of time for all customers with specific service levels for NAV applications, including acknowledgement of application, provision of bulk contract offers and provision of signed bulk agreements.[87]

99. However, the target timeframes set by Ofwat are in some cases a statutory requirement (eg s45 service pipe connections) while others are non-statutory targets (eg pre-development enquiries).[88]

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[81] FMN, paragraph 399.
[82] FMN, paragraph 120.
[83] Allowed revenues are set in the first year of the price control and then adjusted for outcomes and performance during the period and indexed to a measure of general inflation. If a network company disputes Ofwat's determination following a periodic review, it can give notice of the determination, requiring Ofwat to refer the matter to the CMA for a further determination (FMN, paragraphs 121–122).
[84] FMN, paragraph 124.
[85] FMN, paragraph 128–129.
[86] FMN, paragraph 400.
[87] FMN, paragraph 401.
[88] See Water UK Developer Services (last access on 13 August 2024).

## Market definition

100. Where the CMA makes an SLC finding, this must be 'within any market or markets in the United Kingdom for goods or services'. An SLC can affect the whole or part of a market or markets. Within that context, the assessment of the relevant market(s) is an analytical tool that forms part of the analysis of the competitive effects of the merger and should not be viewed as a separate exercise.[89]

101. While market definition can be an important part of the overall merger assessment process, the CMA's experience is that in most mergers, the evidence gathered as part of the competitive assessment, which will assess the potentially significant constraints on the merger parties' behaviour, captures the competitive dynamics more fully than formal market definition.[90]

### Product market

102. For the purposes of its investigation, the CMA has focused on the vertical relationships between:

(a) Cadent, an upstream incumbent supplying gas connections, and LMI's activities downstream in the installation and adoption of last mile gas connections; and

(b) Southern Water, an upstream incumbent supplying water and wastewater connections, and LMI's activities downstream in the installation and adoption of last mile water and wastewater connections.[91]

*Parties' submissions*

103. In relation to gas, the Parties adopted a broadly consistent approach to the product market definition adopted by the CMA in its recent decision in *Brookfield/SGN*. The Parties agreed with the CMA's position that given the differing accreditation and licensing requirements as well as limited supply-side substitutability, the market for gas connections should be assessed separately from other utilities.[92]

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[89] CMA129, paragraph 9.1.
[90] CMA129, paragraph 9.2.
[91] Similar to LMI, Matrix is also active in the installation of last mile water connections (although currently it only supplies these services when [✂] but does not [✂] (FMN, paragraph 146)) and is applying for a NAV licence. However, as mentioned in footnote 24, the CMA considers that the Merger does not give rise to competition concerns in relation to these horizontal overlaps, and they are not further considered in this Decision. Further, the CMA refers throughout this Decision to LMI, but notes that the theories of harm being considered would also apply to Matrix to the extent it becomes a NAV in the future.
[92] FMN, paragraphs 153–154. Also, Brookfield/SGN, paragraphs 91–97.

104. Similarly, the Parties submitted that in line with the CMA's position, competition for the installation and third-party adoption of gas connections should be assessed separately, given there are different regulatory requirements for installation and adoption and there is limited supply-side substitutability.[93]

105. The Parties also broadly agreed with the CMA's assessment that the market should not be segmented on the basis of s10(1)(a) connections[94] and that any further segmentations for gas should be based on the size of the development (ie the number of connections), for example one-off connections and multi-unit connections.[95]

106. Consistent with the CMA's previous approach, the Parties submitted that domestic and non-domestic/I&C connections should be assessed together and that the CMA should not further segment the market for the supply of multi-unit domestic connections.[96]

107. With respect to water and wastewater, the Parties submitted that the installation and adoption of last mile water and wastewater connections shares a number of similarities with the gas and electricity connections sector and therefore proposed a broadly consistent approach to the product market definition adopted by the CMA in its recent decision in *Brookfield/SGN*.[97]

108. The Parties submitted that installation should be considered separately from adoption, noting that while installation can be carried out by SLPs, incumbents and NAVs, water and wastewater connections can only be adopted by an incumbent or a NAV.[98]

109. Within installation, the Parties also submitted that there is not a standalone market for the installation of last mile wastewater connections.[99] This is because the vast majority of developers make their own arrangements for installing wastewater connections and have not relied on the incumbents or SLPs. This is because sewers are installed before works of a new development have started and installation needs to be done in a time-efficient manner to prevent hold-up on development sites.[100]

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[93] FMN, paragraphs 153–154. Also, Brookfield/SGN, paragraphs 98–101.
[94] GDNs and IGTs must follow specific conditions set by Ofgem in setting their charges/prices for connections. One of these requirements is where a GDN's/IGT's network is within 23 metres of a domestic property for which a connection is requested, the GDN/IGT must provide the first 10 metres free of charge, ie a s10(1)(a) connection. FMN, footnote 84.
[95] FMN, paragraphs 153–154. Also Brookfield/SGN, paragraphs 103–106.
[96] FMN, paragraph 153–155. Also, Brookfield/SGN, paragraphs 107–109.
[97] FMN, paragraph 162. Also, Brookfield/SGN, paragraphs 91–109.
[98] FMN, paragraph 162(a).
[99] As noted above in paragraph 83, LMI is not active in the installation of wastewater connections.
[100] FMN, paragraph 162(b).

110. By contrast, for water connections, the Parties submitted that developers require the installation to be carried out by a WIRS accredited SLP or incumbent and the timing is less critical to the project's development. Therefore, the Parties submitted that the impact of the Merger should be considered in the market for the installation of last mile water connections only.[101]

111. With respect to adoption, the Parties noted that while NAVs are for the most part active across the adoption of both water and wastewater connections,[102] there are some regulatory differences between the two, with the adoption of water connections requiring more complex oversight. Accordingly, the Parties submitted that the CMA should consider the adoption of water connections separately from the adoption of wastewater connections.[103]

112. Finally, consistent with the approach in electricity and gas, the Parties consider that the conditions of competition (for both installation and adoption) differ between different sizes of development, with a distinction between small/one-off developments and larger multi-unit developments.[104]

113. Therefore, the Parties submitted that the most appropriate markets are the installation of last mile water connections, the third-party adoption of last mile water connections and the third-party adoption of last mile wastewater connections, each segmented by size of premises/development.[105]

*CMA's assessment*

114. The CMA considered whether the relevant product market should aggregate (i) types of utility and (ii) installation and adoption,[106] and whether the market(s) should be segmented by development size (ie between larger and smaller developments). The CMA has also considered the definition of the relevant upstream markets.

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[101] FMN, paragraph 162(b).
[102] As noted above in paragraph 89, LMI is active in the adoption of both water and wastewater connections.
[103] FMN, paragraph 162(b).
[104] FMN, paragraph 162(c).
[105] FMN, paragraph 163.
[106] As explained in paragraph 54, adoption can be either self-adoption where a vertically integrated firm undertakes both the installation and adoption; or third-party adoption where the adoption is undertaken by a different firm to the installer. While the procurement between both approaches differs slightly, the competitive conditions are broadly similar and ultimately the process of adoption, whether self-adoption or third-party adoption, is the same. Where the CMA refers to adoption, it covers both self-adoption and third-party adoption.

*Type of utility*

115. The CMA considered whether there is a single product market encompassing gas, water and wastewater connections (and possibly other utilities), or whether there are separate markets for each type of utility.

116. The CMA considers that from a demand point of view, a gas connection, a water connection and a wastewater connection are not demand-side substitutes, in that each connection serves a different purpose. A gas connection requires the installation of pipework to procure gas and connect to premises, a water connection requires the installation of pipework to procure water and connect to premises whereas a wastewater connection requires the installation of sewers for the discharge of wastewater. Moreover, although some developers prefer to work with multi-utility connection suppliers due to the convenience of working with a single supplier for multiple utilities, some others prefer to use separate suppliers for each utility.[107]

117. Where there is limited demand-side substitution, the CMA may aggregate markets based on supply-side substitution.[108] The CMA considered whether in this case there are supply-side factors which may lead the CMA to aggregate narrower markets and therefore consider gas, water and wastewater together as a single market. However, evidence available to the CMA shows that there is also limited supply-side substitutability between gas, water and wastewater connections. For example, although some suppliers such as LMI and BU-UK and its subsidiaries are active in gas, water and wastewater, there are other suppliers that are only active in a single utility.

118. Further, there are differences in the regulatory framework for each of gas, water and wastewater connections. 'Gas only' installers and multi-utility installers obtain different types of accreditation from the Gas Industry Registration Scheme (**GIRS**), which recognises and distinguishes the additional technical expertise required to be able to install multi-utility connections.[109] This is the same for water: while a company needs to be WIRS accredited to install water connections, this is not the case for wastewater connections and it is typical for a developer to install wastewater connections itself, to be adopted by WASCs or NAVs.[110] In addition, IGTs (gas) are subject to licensing regimes by Ofgem, which are different to the licensing regimes imposed by Ofwat on NAVs (water and wastewater).

[107] FMN, paragraphs 89–91. Also, Brookfield/SGN, paragraph 51.
[108] CMA129, paragraph 9.8.
[109] See Gas Industry Registration Scheme (Irqa.com). Brookfield/SGN, paragraph 96.
[110] FMN, paragraph 162(b) and footnote 90

119. Accordingly, the CMA has assessed the impact of the Merger in gas connections, water connections and wastewater connections separately.

*Installation and adoption*

120. The CMA considered whether there is a single product market for installation and adoption of last mile connections, or whether to assess the impact of the Merger on installations and adoptions separately.

121. The CMA considers that there is no demand-side substitutability between installation and adoption, as each of these relate to different stages in the supply of last mile utility connections: the former involves the placing of the physical infrastructure required to activate the connection; and the latter involves the ownership and long-term management of the installed infrastructure.

122. The CMA considers that there is limited supply-side substitutability between installation and adoption. Some companies, such as LMI or BU-UK and its subsidiaries act as both installers and adopters, whereas others do not (eg TriConnex only acts as an SLP).

123. Also, as noted above in paragraphs 81 and 84, there are different regulatory requirements for installation and adoption, in that installers (or UIPs for gas, or SLPs for water) must be accredited to carry out their work. However, they do not require a licence from Ofgem (in the case of gas) or Ofwat (in the case of water and wastewater) to install infrastructure, whereas adopters (or IGTs for gas, or NAVs for water) require a licence from Ofgem and Ofwat to adopt gas and water and wastewater connections, respectively.

124. Accordingly, the CMA has assessed the impact of the Merger in the installation and adoption of last mile utility connections separately.

*Size of development*

125. In *Brookfield/SGN*, the CMA considered that non-incumbent installers and adopters generally did not consider smaller developments to be commercially attractive as these are less profitable than larger developments, whereas incumbents were more competitive on price for one-off connections or very small developments.[111]

126. The CMA has not received any evidence to suggest that any departure from the approach adopted in *Brookfield/SGN* would be warranted. Accordingly, the CMA

[111] Brookfield/SGN, paragraphs 103–105.

has assessed the impact of the Merger on multi-unit developments in the competitive assessment, as these are the focus of LMI's activity.

*Upstream market (gas)*

127. For its assessment of vertical effects, the CMA considered it relevant to define the upstream market in which Cadent operates as the incumbent. As the regional GDN, Cadent is appointed by Ofgem and owns, operates and maintains a gas distribution network across the Cadent Region, by which it provides gas connections to its own regional network enabling the supply of gas into last mile connections to existing and new build properties.

*Upstream market (water, wastewater)*

128. For its assessment of vertical effects, the CMA considered it relevant to define the upstream market in which Southern Water operates as the incumbent. As the regional WASC, Southern Water is appointed by Ofwat to provide wholesale and retail water supply services, comprising water abstraction, treatment and delivery as well as the wholesale and retail supply of wastewater services, comprising wastewater collection, treatment and disposal.[112]

129. Moreover, for each of water and wastewater, the incumbent operating in the upstream market provides a connection to its own regional network enabling the supply of water into last mile connections and the discharge of wastewater into its network.

*Conclusion on product market*

130. On the basis of the evidence above, the CMA considers that the relevant markets are as follows:

(a) the installation of last mile gas connections (downstream);

(b) the adoption of last mile gas connections (downstream);

(c) the supply of gas connections to the regional network (upstream);

(d) the installation of last mile water connections (downstream);

(e) the adoption of last mile water connections (downstream);

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[112] As explained in footnote 63, within the Southern Water Region, four WOCs, namely Affinity Water Limited, Portsmouth Water Limited, South East Water Limited and Bournemouth Water Ltd are also active. In the areas where these WOCs are active, the area is, therefore, a dual incumbency area, in which the WOCs provide water services and Southern Water only provides wastewater services. FMN, paragraph 117.

(f) the adoption of last mile wastewater connections (downstream);

(g) the supply of water services and connections to the regional network (upstream); and

(h) the supply of wastewater services and connections to the regional network (upstream).

131. While the CMA is assessing the impact of the Merger in installation and adoption separately, where relevant, it considers any interactions between installation and adoption in the competitive assessment below.

**Geographic market**

*Last mile gas connections*

132. With respect to installation, the Parties submitted that most customers tender on a regional basis, and that while many utility connection providers are present nationally, others have a regional focus.

133. With respect to adoption, the Parties submitted that the appropriate geographic frame of reference is Great Britain-wide, as most adopters operate across Great Britain and there are unlikely to be regional differences in competition.

134. Although the CMA acknowledges that competition between adopters may take place across a wider geographic area, given the focus of the CMA's investigation is a vertical concern within the Cadent Region, the CMA has assessed the impact of the Merger on a regional basis, with a focus on the Cadent Region, as defined above in paragraph 13.

*Last mile water and wastewater connections*

135. The Parties submitted that given the geographic focus of the Parties' activities, the relevant geographic market should be regional, focusing on the Southern Water Region.[113]

136. Although the CMA acknowledges that competition between adopters may take place across a wider geographic area, given the focus of the CMA's investigation is a vertical concern within the Southern Water Region, the CMA has assessed the impact of the Merger on a regional basis, with a focus on the Southern Water Region, as defined above in paragraph 16. However, the CMA also recognises that across much of Southern Water's Region, it provides only wastewater

[113] FMN, paragraph 164.

services, while other entities provide water-only services.[114] This indicates that there are some differences in relevant geographic areas across water and wastewater, which have been taken into account in the competitive assessment below.

## Theories of harm

137. The CMA assesses the potential competitive effects of mergers by reference to theories of harm. Theories of harm provide a framework for assessing the effects of a merger and whether or not it could lead to an SLC relative to the counterfactual.[115]

138. In its investigation of this Merger, the CMA has considered the following theories of harm:

(a) input foreclosure of LMI's rivals by Cadent, in the installation and adoption of last mile gas connections in the Cadent Region;

(b) input foreclosure of LMI's rivals by Southern Water, in the installation and adoption of last mile water connections in the Southern Water Region; and

(c) input foreclosure of LMI's rivals by Southern Water, in the adoption of last mile wastewater connections in the Southern Water Region.

139. Each of these theories of harm is considered below.

## Theory of Harm 1: Input foreclosure in the installation and adoption of last mile gas connections in the Cadent Region

140. The concern with an input foreclosure theory of harm is that the merged entity may use its control of an important input to harm its downstream rivals' competitiveness, for example by refusing to supply the input (total foreclosure) or by increasing the price or worsening the quality of the input supplied to them (partial foreclosure). This might then harm overall competition in the downstream market, to the detriment of customers. This may occur irrespective of whether the parties to a merger have a pre-existing commercial relationship.[116]

141. The CMA considered whether Macquarie may be able to leverage Cadent's position as a GDN (upstream) to provide LMI with certain advantages to the

[114] Affinity Water Limited, Portsmouth Water Limited, South East Water Limited and Bournemouth Water Ltd. FMN, paragraph 117.
[115] CMA129, paragraph 2.11.
[116] CMA129, paragraph 7.9.

detriment of LMI's rivals in the supply of last mile gas connections (downstream) in the Cadent Region, for example (but not limited to) by:

(a) slowing down the speed at which Cadent approves last mile gas connections by LMI's rivals to its network; or

(b) quoting a higher price for connections to LMI's rivals.

142. The CMA also considered any potential effects on competition related to the sharing of commercially sensitive information (**CSI**) by competitors of LMI with Cadent. A concern would arise if following the Merger, the Merged Entity were able to gain access to CSI about the activities of its competitors (eg in this case, development plans) in the supply of last mile gas connections. Access to CSI could be used by the Merged Entity to put its rivals at a competitive disadvantage.[117] These concerns have also been considered in this section.

143. The CMA's approach to assessing an input foreclosure theory of harm is to analyse (a) the ability of the merged entity to harm the competitiveness of its downstream rivals; (b) the incentive to do so; and (c) the overall effect of the strategy on competition.[118]

*Ability*

144. The Parties submitted that Cadent will not have the ability to foreclose LMI's rivals because:

(a) Cadent has limited interactions with UIPs and IGTs that apply to connect to its distribution network. This involves the application of a set process by GDNs when dealing with connection requests;[119]

(b) Cadent is prevented from discriminating between IGTs due to regulatory protections. These include, but are not limited to, a duty to avoid undue preference and/or discrimination, a duty to achieve specified service standards and a duty to ensure that pricing/charging methodologies do not distort competition;[120]

[117] CMA129, paragraph 7.3.
[118] CMA129, paragraph 7.10.
[119] FMN, paragraph 351. The CMA has placed limited weight on the Parties' argument that Cadent has limited ability to discriminate due to the limited nature of interactions. This is because, although there are fewer interactions between gas incumbents and UIPs/IGTs compared to equivalent players in water and wastewater, these interactions are still mandatory and there are circumstances where greater levels of interaction are required (eg for more complex projects).
[120] FMN, paragraphs 352–355.

(c) Macquarie only holds a minority stake of 26% in Cadent and therefore will not have the ability to take unilateral strategic decisions or unilaterally engage in a foreclosure strategy;[121] and

(d) Macquarie has in place existing information barriers between its divisions and individual investments.[122] The barriers provide an additional segregation between LMI and Cadent and any information held by either LMI or Cadent would not be shared with the other.[123] The Parties also submitted that further to a confidentiality clause under Cadent's template connections agreements with UIPs and IGTs, Cadent is prohibited from disclosing information to third parties in connection with the agreement.[124]

145. As indicated in paragraph 52 above, GDNs hold a monopoly position in their region and continue to maintain large infrastructure networks that connect to the original source of utilities. UIPs and IGTs need to apply to GDNs to join their last-mile gas connections to the GDN's incumbent network.[125] As such, GDNs hold a position of market power and provide an essential input to UIPs and IGTs.

146. However, the ability of GDNs to act in ways which may distort competition between UIPs and IGTs downstream may be constrained by regulation. This is considered further below.

147. As described in paragraphs 69 to 73 above, the Gas Act and licence conditions set by Ofgem regulate the behaviour of GDNs. In particular, GDNs are under a duty to provide new gas connections on a non-discriminatory basis, are subject to a number of conditions that are designed to prevent them from preferring certain UIPs or IGTs above others, must follow specific conditions set by Ofgem when setting charges for connections (which include a requirement not to restrict or distort or prevent competition, and to ensure that no undue preference or undue discrimination is shown by the licensee), and are subject to quality of service standards (which includes the speed at which quotes for connections are issued and connections are made).

148. This regulation would therefore prohibit Cadent from discriminating in favour of LMI post-Merger when making connections to its network, for example, by only

[121] MAM manages a stake of c.26% in Cadent on behalf of its managed funds, noting that MAM's own direct ownership is c.12%. FMN, paragraphs 24 and 356.
[122] The CMA has placed limited weight on this argument from the Parties, as although there are currently information barriers in place, there could be some ways in which the Merged Entity could overcome these barriers and share confidential information between divisions and investments, and these information barriers could be changed in the future. As such, this is not discussed further in this Decision.
[123] FMN, paragraph 357.
[124] Parties' response to the CMA's request for information, dated 11 July 2024 (**Annex RFI4 – MAM**), paragraphs 20–21.
[125] FMN, paragraph 82.

providing point of connection information to LMI but not to its rivals, or by providing slower connections or charging connection fees to LMI's rivals without justification.

149. This is consistent with the evidence received from third parties, which suggests that existing regulation provides sufficient protection to competing UIPs and IGTs. In particular, all third parties who responded to the CMA's questionnaire noted that their ability to compete would not be affected by the Merger, with one third party qualifying that this was provided Cadent remained within the parameters of the standards of service required.[126] Other third parties explained that their ability to compete would not be affected because standards of design and technical specifications are all regulated by industry panels as opposed to being determined by Cadent alone[127] and regulated timescales would 'mitigate the risk of a reduced ability to compete'.[128]

150. With respect to the exchange of CSI, when asked whether any CSI was exchanged between Cadent and UIPs or IGTs when installing or adopting a last mile gas connection, most third parties who responded to the CMA's questionnaire indicated that no CSI was exchanged with Cadent.[129] Some third parties submitted that only very limited CSI is shared with Cadent at the time of installation or adoption of a last mile gas connection or otherwise.[130]

151. Moreover, Macquarie is part of a consortium of investors in Cadent, and the consortium only holds approximately a 26% stake in Cadent – with Macquarie's direct ownership being a 12% stake. This minority shareholding does not enable Macquarie to take unilateral strategic decisions with respect to Cadent.[131]

152. Based on the evidence above, the CMA considers that the Merged Entity would have only limited ability to disadvantage rival UIPs and IGTs, particularly given that: (i) the existing regulation would limit Cadent's ability to discriminate against rival UIPs and IGTs; and (ii) Macquarie only has a direct 12% stake in Cadent, which limits Macquarie's ability to use its shareholding in Cadent to favour of LMI.

*Incentive*

153. The Parties submitted that Macquarie will not have the incentive to foreclose LMI's rivals following the Merger because the regulatory conditions set out above and the consequences of breaching these regulations (including but not limited to financial penalties) will act as an effective deterrent.[132] The Parties also submitted

[126] Response to the CMA questionnaire from a third party, July 2024, [✂].
[127] Response to the CMA questionnaire from a third party, July 2024, [✂].
[128] Response to the CMA questionnaire from a third party, July 2024, [✂].
[129] Response to the CMA questionnaire from a number of third parties, July 2024, [✂].
[130] Response to the CMA questionnaire from a number of third parties, July 2024, [✂].
[131] FMN, paragraphs 24–27.
[132] FMN, paragraph 358-359.

that any favourable treatment towards LMI would not return a material advantage to the Merged Entity.[133] Finally, the Parties also submitted that the group structure of Cadent, and the influence of other shareholders, act as a significant constraint and limit the Merged Entity's ability and incentive to engage in any anticompetitive behaviour. In particular, the Parties submitted that Cadent's other shareholders have no economic interest in allowing Cadent to favour LMI.[134]

154. The CMA understands that any breach by a GDN of its obligations under the Gas Act or its licence may result in enforcement action by Ofgem, such as, financial penalties, modifications to the licence, and orders.[135] Such penalties and orders are also published.[136] Ofgem told the CMA that while potential breaches are assessed on a case-by-case basis, it has a broad range of powers to sanction regulated entities in breach of their licence conditions. For example, Ofgem could impose financial penalties (up to 10% of turnover), provisional orders, final orders, consumer redress order or revoke the GDN's licence.[137]

155. The CMA recognises that it may be difficult for Ofgem to detect certain breaches by GDNs[138] and Ofgem told the CMA [✂].[139] However, the CMA considers that the risk of enforcement could act as an effective deterrent, limiting the incentive for any discriminatory behaviour by Cadent in favour of LMI.

156. The CMA also considers that Cadent's other shareholders have no economic interest in LMI and therefore no incentive to allow Cadent to favour LMI, especially if this risks financial penalties or other enforcement action.[140] The CMA therefore considers that these shareholders would have a strong incentive to prevent Cadent from discriminating against LMI's rivals.

157. Based on the evidence above, the CMA therefore considers that the Merged Entity will not have the incentive to engage in discriminatory behaviour to the detriment of LMI's UIP and IGT rivals.

*Effect*

158. In light of our conclusion that the Merged Entity would not have the incentive to pursue a foreclosure strategy, we have not considered its effects on competition.

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[133] FMN, paragraph 360.
[134] FMN, paragraph 361.
[135] See Sections 28 and 30A of the Gas Act.
[136] See sections 29(2) and 30A(7) of the Gas Act.
[137] Ofgem's response to the CMA's request for information, dated 27 June 2024.
[138] Response to the CMA questionnaire from a third party, July 2024, [✂].
[139] Ofgem's response to the CMA's request for information, dated 27 June 2024.
[140] FMN, paragraph 361.

### Conclusion on Theory of Harm 1

159. For the reasons set out above, the CMA believes that the Merger does not give rise to a realistic prospect of an SLC as a result of vertical effects in relation to the installation and adoption of last mile gas connections in the Cadent Region.

## Theory of Harm 2: Input foreclosure in the installation and adoption of last mile water connections in the Southern Water Region

160. As set out in paragraph 140, the concern with an input foreclosure theory of harm is that the merged entity may use its control of an important input to harm its downstream rivals' competitiveness.[141]

161. In the present case, the CMA considered whether Southern Water could leverage its position as the incumbent in the Southern Water Region to provide LMI with certain advantages to the detriment of its rivals in the supply of water connections. Third parties told the CMA that Southern Water could use a range of price and non-price foreclosure mechanisms to discriminate against rival SLPs and NAVs. Several third parties submitted that Southern Water could charge higher prices or set less preferential tariffs to its downstream rivals,[142] for example, when interfacing with the installer or negotiating bulk water supply agreements. Some third parties submitted that Southern Water could deteriorate the services it provides downstream rivals, for example by engaging with its downstream rivals more slowly, including when responding to connection requests, entering into bulk water supply agreements or processing NAV applications.[143]

162. The CMA also considered whether Southern Water might share certain information with only LMI, which would give it a competitive advantage over rivals. This could include information that would allow LMI a greater understanding of opportunities, market developments or more efficient pipeline designs that other third parties do not have access to when competing for and completing connections. Such information could enable LMI to implement more efficient connection designs and enable it to make more accurate predictions on future costs and revenues for water connections. These concerns have also been considered in this section.

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[141] CMA129, paragraph 7.9.
[142] Note of call with a third party, July 2024, [✂]. Responses to the CMA questionnaire from a number of third parties, July 2024, [✂].
[143] Note of call with a third party, July 2024, [✂]. Response to the CMA questionnaire from a third party, July 2024, [✂].

163. As set out in paragraph 143 above, the CMA's approach to assessing an input foreclosure theory of harm is to analyse the ability and incentive to foreclose, and the overall effect of the foreclosure strategy on competition.[144]

**Ability**

164. When assessing whether the merged entity would have the ability to foreclose its rivals, the CMA will typically focus on two issues: first, whether there is market power upstream; and second, the importance of the input.[145]

165. As explained in paragraph 79, Southern Water holds a monopoly position in the Southern Water Region, and SLPs and NAVs need to apply to Southern Water to join their last mile water connections to Southern Water's incumbent network in this region. As such, Southern Water holds a position of market power and provides an essential input to SLPs and NAVs.[146] However, the ability of Southern Water to act in ways which may distort competition between SLPs and NAVs downstream may be constrained by regulation. The CMA considers the impact of regulation in the section below.

*Regulation*

166. The Parties submitted that Ofwat's regulatory framework would prevent Southern Water from discriminating against rival SLPs or NAVs, including via price controls and minimum service standards that in effect require the provision of equivalent services to all SLPs and NAVs.

(a) First, Southern Water is subject to certain regulatory obligations under its instrument of appointment.[147] For example, Condition E1 prohibits Southern Water from showing undue preference or discrimination towards any player when setting charges, laying connections, or providing water services.[148]

(b) Second, Southern Water has no ability to discriminate on price because charges and tariffs are fixed, published online and applied to all SLPs and NAVs on an equivalent basis.[149]

[144] CMA129, paragraph 7.10.
[145] CMA129, paragraph 7.14.
[146] The Parties submitted that Macquarie holds a stake of 87% in Southern Water (see Parties' response to the Issues Letter, 20 August 2024, paragraph 105). The CMA considers that Macquarie exercises strategic control of Southern Water and would not need to be reliant on other shareholders when instructing it to pursue a foreclosure strategy.
[147] See https://www.ofwat.gov.uk/wp-content/uploads/2021/04/Southern-Water-Consolidated-Appointment.pdf
[148] Parties' response to the Issues Letter, 20 August 2024, paragraph 30(c).
[149] Parties' response to the Issues Letter, 20 August 2024, paragraph 6(a).

(c) Third, Southern Water is subject to certain reportable levels of service which are determined by Ofwat.[150] Southern Water's monthly reporting of its performance of these set tasks within the periods defined by Ofwat is publicly available.[151] The Parties also submitted that compliance with Ofwat's D-MEX framework, that scores incumbents on their relative service levels, reduces its ability to foreclose.

(d) Fourth, Southern Water has no ability to share sensitive information due to regulatory ring-fencing under licence conditions and confidentiality provisions in agreements with third parties. Furthermore, no sensitive information is shared with Southern Water during the competitive bidding process with a developer such that it has no ability to self-preference in any event.[152]

167. While the Parties referred to Ofwat's D-MEX as a factor that would limit the Merged Entity's ability to foreclose rivals, the CMA considers that the penalties under D-MEX impact the Merged Entity's incentives rather than ability. The CMA also considers that the existence of a relative ranking for service levels of itself suggests that some differences in service levels across incumbents and over time are expected, indicating that the regulatory regime does not prevent any variability in service levels. The CMA assesses the impact of D-MEX in paragraph 197 below.

168. Ofwat told us that its enforcement powers and level of penalties would likely constrain the ability of incumbents from engaging in anticompetitive behaviour.[153] In particular, it noted that incumbents are required to comply with their licence conditions, such as Condition E and E1 that together prohibit discrimination on charges, services, and the use of information; Condition F which requires them to produce accounts in line with its Regulatory Accounting Guidelines (**RAGs**); and Condition P which prohibits cross-subsidy between the incumbent and other entities in its group. Moreover, the RAGs themselves also require incumbents to operate on an arm's length basis.[154]

169. The CMA notes that the regulations covering the supply of last mile water connections are different to those in gas. In water, downstream rivals must interact with the incumbent on a site-by-site basis, for example to negotiate bulk supply agreements. This means that SLPs and NAVs must interact more frequently with the incumbent than is the case in gas. One third party considered that this

[150] See https://www.ofwat.gov.uk/regulated-companies/company-obligations/customer-experience/; https://developerservices.water.org.uk/
[151] Parties' response to the Issues Letter, 20 August 2024, paragraph 21. See also https://www.southernwater.co.uk/building-and-developing/help-and-resources/levels-of-service/
[152] Parties' response to the Issues Letter, 20 August 2024, paragraph 6(c).
[153] Ofwat's response to the CMA's request for information, dated 20 August 2024, page 16.
[154] Ofwat's response to the CMA's request for information, dated 20 August 2024, page 13.

introduced additional risk in terms of the potential effects on competition of the Merger due to the higher frequency of interaction with the incumbent.[155]

170. Some rival SLPs and NAVs told the CMA that Ofwat's regulations would prevent discriminatory behaviour while others were concerned that the regulations would not prevent all forms of preferential treatment towards LMI.[156] One third party submitted that incumbents have free reign over how they interpret the Water UK templates, and that Ofwat provided limited guidance with respect to its framework and relied to a significant extent on independent providers having sufficient knowledge to be able to negotiate terms with the incumbent.[157] Some third parties indicated that they had observed differences in pricing or service levels between incumbents.[158, 159]

171. Aside from observed variations in pricing and service levels between incumbents, one third party also submitted that there were inevitable difficulties in the detection of discrimination and gathering of supporting evidence that demonstrated that an incumbent was acting anti-competitively. It cited a lack of a common methodology for pricing, information asymmetry, and a lack of transparency on agreements negotiated with other independents as contributing factors to this outcome.[160]

*CMA's assessment*

172. As described in paragraphs 166 to 168 above, regulations and licence conditions enforced by Ofwat regulate the behaviour of incumbents. In particular, incumbents have a general duty to grant connections to their network, have a duty to avoid undue preference or undue discrimination in the connection of premises or pipelines operated by SLPs/NAVs to their network, are subject to quality of service standards (which cover the speed at which connections are made) and must follow specific conditions set by Ofwat when setting charges for connections (which include a requirement not to restrict or distort or prevent competition, and to ensure that no undue preference or undue discrimination is shown by the licensee). This means that Southern Water will, in principle, be prohibited from discriminating in favour of LMI post-Merger when making connections to its network and will be prohibited, for example, from only providing point of

[155] Note of call with a third party, July 2024, [✂].
[156] Response to the CMA's questionnaire from a number of third parties, July 2024, [✂].
[157] Note of call with a third party, July 2024, [✂].
[158] For example, some third parties had observed differences in how they were billed, how their NAV licences were progressed, whether the incumbent provided installation designs, and the scope of the 'value added' provisions such as emergency services. Notes of calls with third parties, June and July 2024, [✂] and [✂].
[159] The Parties internal documents also acknowledge that Ofwat guidance may be open to different interpretations, and there have been differences in the way the guidance has been implemented across incumbents. See for example LMI, Internal Document, Annex 09.0001 to the FMN, page 57.
[160] Note of call with a third party, July 2024, [✂]. Response to the CMA's questionnaire from a third party, July 2024, [✂].

connection information to LMI, providing slower connections or charging higher connection fees to LMI's rivals without justification.

173. The CMA, however, notes that not all of the applicable regulation specifies the precise service levels that Southern Water must provide. Rather in certain instances Ofwat has left it open to the incumbents to determine how best to fulfil their obligations, and mechanisms such as D-MEX have been developed to incentivise good performance. Evidence from third parties suggests that Southern Water may have the opportunity to interpret the guidance, targets and codes differently and there may be scope within the regulations for Southern Water to provide different levels of treatment to rival SLPs and NAVs.[161] Further, the existence of Ofwat's D-MEX rankings indicates that some variation in performance across service quality metrics is expected. Given the frequency and repeated nature of interactions that take place between the incumbent and SLPs and NAVs, the CMA considers that the risk of potential breaches is higher for water connections than for other utilities.

*CMA's conclusion on Merged Entity's ability to foreclose*

174. Based on the evidence above, the CMA considers that the Merged Entity may have some ability to foreclose rival SLPs and NAVs, particularly given that: (i) Southern Water has the market power to engage in a foreclosure strategy; (ii) Southern Water's input is necessary for SLPs and NAVs to provide their services; and (iii) existing regulation may not eliminate all ways in which Southern Water might disadvantage rival SLPs and/or NAVs and thereby impact their competitiveness downstream.

*Incentives*

175. In this section, the CMA considers whether the Merged Entity would have the incentive to foreclose rival SLPs and NAVs active in the installation and adoption of last mile water connections in the Southern Water Region. To assess incentives, the CMA considers the magnitude and likelihood of the costs and benefits of any foreclosure strategy.[162]

*Parties' submissions*

176. The Parties submitted that the Merged Entity would have no incentive to foreclose rivals because it would face costs for breaching Ofwat's regulations. Any breach by a WOC or WASC of its obligations under the Water Act, or its licence, may

[161] Note of call with a third party, July 2024, [✂].
[162] CMA129, paragraph 7.16.

result in enforcement action by Ofwat, including, among other things, enforcement orders to the incumbent to ensure its compliance, acceptance of enforceable undertakings in which the incumbent would commit to take forward actions to ensure compliance, and financial penalties of up to 10% of its annual turnover.[163]

177. The Parties told the CMA that rivals have accessible and low-cost mechanisms to alert Ofwat of any breaches of law or regulation. They cited a recent investigation into Bristol Water as an example of Ofwat responding to complaints from SLPs about discriminatory treatment.[164] They also submitted that SLPs and NAVs are well placed to identify discriminatory behaviour, given that prices and expected service levels to both are typically published by the incumbent. The Parties also submitted that SLPs bid on an 'open book' basis[165] meaning that developers could readily identify differences in the bids they receive (including differences in the location or costs of connecting to the incumbent network) and could raise this with the incumbent and Ofwat.[166]

178. The Parties submitted that a foreclosure strategy would also result in low D-MEX scores, which would in turn have significant financial and reputational consequences, particularly as the financial consequences are set to increase from April 2025 following changes introduced in Ofwat's 2024 Price Review.[167] In addition, they said that the D-MEX scores introduce another layer of transparency to the incumbent's service levels, given that they are reported monthly and are published.[168]

179. The Parties also submitted that even if there was theoretically a narrow timeframe in which Southern Water could favour LMI on service standards (notwithstanding the fact that any discrimination would be in breach of its licence conditions and that poor performance would be penalised under D-MEX), it would have no incentive to do so as there is no material advantage that such a marginal change in service would bring.[169]

*Ofwat's submissions*

180. Ofwat submitted that SLPs and NAVs are able to compare the prices and service levels they have received against those received by their rivals given that these are published online by the incumbent itself (for prices) and by Water UK and

[163] Annex RFI5 – MAM, paragraph 38.
[164] Parties' response to the Issues Letter, 20 August 2024, paragraph 9(c). See also Bristol-Water-CA98-commitments-Final-decision.pdf (ofwat.gov.uk).
[165] Where developers can see the components and other details of the total cost.
[166] Parties' response to the Issues Letter, 20 August 2024, paragraph 9c(i) to 9(cii).
[167] Parties' response to the Issues Letter, 20 August 2024, paragraph 9(a).
[168] Parties' response to the Issues Letter, 20 August 2024, paragraph 9(ciii).
[169] FMN, paragraph 404.

Ofwat (for service levels, averaged across all NAVs and/or SLPs).[170] In addition, it submitted that it regularly meets with stakeholders, enabling them to raise any concerns, and that in any case companies could make complaints about an incumbent's behaviour.[171]

181. Ofwat submitted that it would investigate if it saw a pattern in the complaints it was receiving from SLPs/NAVs, which may lead to enforcement action.[172] Ofwat added that under section 18 of the Water Act, it has a duty to pursue enforcement action against potential breaches of licence conditions and has in the past considered and taken action against incumbents.[173]

*Third-party views*

182. A foreclosure strategy will give rise to benefits if the Merged Entity obtains additional profits downstream (for example as a result of additional downstream sales due to weaker competition in the downstream market). The CMA therefore approached third parties to understand to what extent their competitiveness may be impacted by a foreclosure strategy. The majority of third parties that responded to the CMA said that they had either no view or a neutral view on the impact of the Merger, with some citing regulatory protection as a reason for why competition would be unaffected. Only a minority expressed the view that the Merger would have an impact on competition.[174]

183. Nonetheless, several third parties submitted that, if breaches of regulations went undetected, a deterioration in the quality or timing of interactions with the incumbent would impact their ability to compete. Some third parties submitted that delays by the incumbent could inhibit their ability to deliver quotations and projects in a competitive timeline.[175] Some third parties also submitted that the incumbent could impact their ability to deliver a good level of service to the developer,[176] with one stating that uncertainty about the service levels that they receive from an incumbent would make it difficult to manage relationships with their customer.[177] Some third parties also submitted that commercial terms (for example, the prices set in bulk supply agreements) could impact their ability to compete effectively,[178]

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[170] Ofwat's response to the CMA's request for information, dated 20 August 2024, page 9.
[171] Ofwat's response to the CMA's request for information, dated 20 August 2024, page 10.
[172] Ofwat's response to the CMA's request for information, dated 20 August 2024, page 10.
[173] Ofwat's response to the CMA's request for information, dated 20 August 2024, page 13 and 15.
[174] Note of call with a third party, July 2024, [✂]. Response to the CMA questionnaires from a number of third parties, July 2024, [✂].
[175] Note of call with a third party, June 2024, [✂]. Responses to the CMA questionnaire from a number of third parties, July 2024, [✂].
[176] Note of call with a third party, June 2024, [✂].
[177] Note of call with a third party, July 2024, [✂].
[178] Note of call with third party, July 2024, [✂]. Responses to the CMA questionnaire from a number of third parties, July 2024, [✂].

with one competitor submitting that this would have a significant impact.[179] Another third party said that the choice and design of pipes by an incumbent could cause an SLP to be more expensive than its rivals.[180]

184. As an example of the impact that incumbents may have on a downstream supplier's ability to compete, one third party said it has reduced its activity in one incumbent's area due to the difficulties it faced working with the incumbent arising from some of the issues highlighted in paragraph 161.[181]

185. Some third parties also provided views on the likelihood of discriminatory behaviour being detected, leading to enforcement action by Ofwat, which is relevant to the potential costs of a foreclosure strategy. One third party said that it had raised issues it experienced with the incumbent via feedback to both the incumbent and Ofwat, but did not see any improvement in the incumbent's conduct, and was not aware of any investigation by Ofwat, although the CMA did not receive details on the nature of these complaints or the extent of any potential breach by the incumbent.[182] Another third party submitted that, because SLPs and NAVs did not have sight of agreements between the incumbent and other third parties, it may be difficult for a rival SLP or NAV to detect discriminatory behaviour, and to gather evidence to prove such behaviour.[183]

*CMA's assessment*

186. The CMA considered a range of factors when assessing whether the Merged Entity would have the incentive to foreclose, including whether it is positioning itself strongly in high-growth markets, competes closely with rivals in the downstream market and whether it could minimise the loss of upstream sales.[184]

*Benefits of foreclosure*

187. In the present case, the main potential benefit of foreclosure would be LMI winning installation and adoption contracts downstream from its rivals. The CMA considers the likelihood of and benefits of winning contracts in more detail below.

188. First, to understand the likelihood of the Merged Entity recapturing sales from its downstream rivals as a result of foreclosure, the CMA considered the current

[179] Response to the CMA questionnaire from a third party, July 2024, [✂].
[180] Response to the CMA questionnaire from a third party, July 2024, [✂].
[181] Note of call with a third party, June 2024, [✂].
[182] Note of call with a third party, June 2024, [✂].
[183] Note of call with a third party, July 2024, [✂]. Response to the CMA questionnaire from a third party, July 2024, [✂].
[184] CMA129, paragraph 7.19.

market structure to assess whether the Merged Entity's downstream offering is successful and how closely it competes with other downstream suppliers.

(a) For the adoption of last mile water connections, the Parties estimated[185] that in FY2023-24 IWNL held a share of supply of [60-70]%, Leep held a share of [0-10]% and Advanced Water did not adopt in that time, with the remaining [30-40]% held by LMI ([20-30]%) and Southern Water ([10-20]%).[186,187] The Parties submitted that IWNL [✂].[188]

(b) Although the Parties were not able to provide shares of supply for the installation of last mile water connections, the CMA notes that IWNL is an integrated supplier (ie undertakes both installation and adoption) and is likely to be a strong supplier in installation, given its strong position in adoption. In addition to IWNL, the CMA notes that there are [more than 15] SLPs that are active in the Southern Water Region, including Connect It, Goyal, Amjutan and TriConnex.[189]

189. The shares of supply analysis shows that the markets are concentrated, although they may be less concentrated in installation. The evidence shows that the Parties have a successful downstream offering and that they are likely to compete closely with at least IWNL,[190] which may be the main target of any foreclosure strategy by the Merged Entity, although all SLPs and NAVs active in the Southern Water Region are plausible targets.

190. Second, the nature and maturity of the markets suggest that the benefits of foreclosure may be material. The downstream markets for installation and adoption of last mile water connections have recently opened to competition and are expected to grow in the coming years.[191] Winning contracts for adoption would provide the Merged Entity with long-term, non-contestable, stable revenues given that there is typically no further competition once the assets are installed and adopted.[192]

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[185] Based on a count of connections adopted at sites with more than 25 connections in FY23-24.
[186] As Southern Water was not able to distinguish between installation and third-party adoption opportunities for third party connections, the CMA is not able to estimate what proportion of these adoption opportunities were won at the installation or third-party adoption stage. Parties' response to the CMA's request for information, dated 12 June 2024 (**Annex RFI2–MAM**) paragraph 93 and Annex RFI2 - MAM.RFI2.26.1.
[187] The Parties submitted information on NAV applications since the beginning of 2023 that showed Advanced Water had made a NAV application, but Advanced Water did not appear in the Parties' share of supply estimates calculated using the count of adoptions between FY2023-24.
[188] FMN, paragraph 315.
[189] Parties' response to the CMA's request for information, dated 8 August 2024 (**Annex RFI6 – MAM**), paragraph 5.
[190] For example, the Parties' internal documents highlight LMI and BUUK (which owns IWNL) as the only two large players. LMI Internal Document, Annex 09.001 to the FMN, page 24.
[191] FMN, paragraph 12(c).
[192] This is consistent with the Parties' internal documents. See for example, LMI Internal Document, Annex 09.0001 to the FMN, page 19, which notes that there are 'High barriers to entry once connections are installed and adopted by LMI'.

191. Third, the Parties acknowledge, and third-party evidence indicates, that an SLP's or NAV's reputation plays an important role in competition for last mile installation and adoption opportunities.[193] Given that some of the Parties' customers are large developers that procure multiple utilities together in one contract,[194] the CMA considers that damaging an SLP's or NAV's reputation may also harm its competitiveness for multi-utility contracts (ie for multi-utility contracts the gains may be wider than the installation and adoption of water connections).

*Costs of foreclosure*

192. Given Southern Water is a monopolist upstream, the CMA considers that there is no risk of losing upstream sales, as LMI's rivals cannot switch to alternative suppliers. The costs of foreclosure are likely to be predominantly related to regulatory enforcement. The evidence shows that the costs of foreclosure in this context are likely to be high. The CMA considers these regulatory costs in more detail below.

193. First, as noted by the Parties, Ofwat can issue financial penalties and take other enforcement action, if the Merged Entity is found to be in breach of its licence conditions. The CMA notes that the likelihood of this is dependent on the SLP, NAV, or Ofwat identifying discriminatory behaviour and Ofwat taking enforcement action against any discriminatory behaviour.

194. The CMA considers that the likelihood of any discriminatory behaviour by an incumbent being identified is likely to be high, although this may vary to some degree between the different foreclosure mechanisms.[195] This is because prices to SLPs and NAVs are largely set by reference to published methodologies, which would enable SLPs and NAVs to identify any material differences between the price they receive and what they should be charged.

195. Changes in services levels are also likely to be detectable. Water UK collects monthly data, published quarterly, on service levels across a wide range of metrics.[196] Any deterioration in the service level performance of Southern Water against these metrics would therefore be visible to SLPs, NAVs, developers and Ofwat. Further, the underlying data used to generate these metrics could be used to identify any patterns in the service levels offered to LMI and its rivals, providing a route for Ofwat to investigate any complaints received.

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[193] Annex RFI5 – MAM, paragraph 2.
[194] FMN, paragraph 101.
[195] See paragraph 171 above where the evidence from one the third party suggests that the likelihood of detection may be low. See paragraphs 161 to 162 where we set out the potential mechanisms of foreclosure.
[196] See Water UK Developer Services

196. As noted above, Ofwat told us it regularly meets with stakeholders, enabling them to raise any concerns and that it would investigate if it saw a pattern in the complaints it was receiving from SLPs/NAVs, which may lead to enforcement action.[197] We note the recent example of Ofwat taking enforcement action against incumbents, including against discriminatory behaviour in the case of Bristol Water.[198]

197. Second, Ofwat's published D-MEX scores incentivise water companies to improve service quality and penalise them for poor performance. The results of the 2021-2022 and 2022-2023 D-MEX rankings show that Southern Water ranked 15th out of 17 in both sets of results, receiving a negative financial payment of £936,000 and £1,817,000 in the two years respectively.[199] From April 2025, the size of the rewards and penalties under the D-MEX regime are set to increase and this should, in principle, increase the incentives of incumbents to improve performance.[200] The D-MEX scores also introduce a degree of transparency with respect to an incumbent's service levels as they provide for detailed monthly reporting covering interviews with SLPs, NAVs and developers and a large range of quantitative metrics, which further increases the likelihood of detection of discriminatory behaviour and enforcement by Ofwat.[201]

198. To the extent that any discriminatory behaviour by the Merged Entity was identified and enforced by Ofwat (either through direct enforcement or through its D-MEX regime), the CMA notes that Macquarie would bear most of the costs of a foreclosure strategy (eg financial penalties) as it holds an [✂]% interest in Southern Water, but would only stand to benefit from half of the increased sales enjoyed by LMI if the strategy were successful (as it will hold a 50% interest in LMI post-Merger).

*CMA's view on Merged Entity's incentive to foreclose*

199. Based on the evidence above, the CMA considers that the Merged Entity does not have the incentive to pursue a foreclosure strategy against rival SLPs and NAVs. Despite the potential benefits from securing contracts downstream, the costs of foreclosure are high, particularly given: (i) the likelihood that any foreclosure strategy would be detected by rivals or the developers they serve; (ii) once detected, enforcement action from Ofwat could lead to significant financial penalties; (iii) foreclosure would likely result in additional financial losses via D-

[197] Ofwat's response to the CMA's request for information, dated 20 August 2024, page 10.
[198] See Bristol-Water-CA98-commitments-Final-decision.pdf (ofwat.gov.uk).
[199] See C-MeX and D-MeX - 2021-22 results - Ofwat and C-MeX and D-MeX - 2022-23 results - Ofwat.
[200] Parties' response to the Issues Letter, 20 August 2024, paragraph 9(a), see also 2024 price review - Ofwat.
[201] Parties' response to the Issues Letter, 20 August 2024, paragraph 9(ciii),

MEX; and (iv) the Merged Entity would only enjoy half of the benefits of foreclosure yet would bear most of the costs.

*Effect*

200. Given the CMA considers that the Merged Entity would not have the incentive to foreclose LMI's rivals, the CMA has not considered effects in its assessment.

**Conclusion on Theory of Harm 2**

201. For the reasons set out above, the CMA believes that the Merged Entity does not have the incentive to pursue an input foreclosure strategy against rival SLPs and NAVs in the markets for the installation and adoption of last mile water connections in the Southern Water Region. Accordingly, the CMA considers that the Merger does not give rise to a realistic prospect of an SLC as a result of input foreclosure in the (i) installation; and (ii) adoption of last mile water connections in the Southern Water Region.

## Theory of Harm 3: Input foreclosure in the adoption of last mile wastewater connections in the Southern Water Region

202. To assess input foreclosure in the adoption of last mile wastewater connections, the CMA has applied the ability, incentive and effect framework set out in paragraph 143 above.

203. The Parties submitted that LMI is not active in the installation of last mile wastewater connections and that over 98% of developers make their own arrangements for the installation of wastewater infrastructure,[202] citing data published by Ofwat to support this point.[203] As the CMA has not received evidence to suggest otherwise, its assessment addresses only the interactions that take place between Southern Water and NAVs when competing for and adopting last mile wastewater connections in the Southern Water Region.

*Potential foreclosure mechanisms*

204. The Parties submitted that the interactions that a NAV has with the incumbent and the developer for last mile wastewater connections are very similar to those for water connections, and that any differences are minimal.[204] This is also consistent with the evidence received from third parties, as none of them highlighted any

[202] FMN, paragraph 162(b).
[203] Ofwat, PR24, Final Methodology, Appendix 3, p.25; see https://www.ofwat.gov.uk/regulated-companies/price-review/2024- price-review/framework-and-methodology/final-methodology/
[204] Annex RFI5 – MAM, footnote 3.

material differences between the interactions they have with an incumbent when competing for and adopting last mile water and wastewater connections.

205. Accordingly, the CMA considers that there are a number of mechanisms the Merged Entity could use to foreclose downstream rivals as set out in paragraphs 161 and 162 above for the adoption of last mile water connections. In this context, the CMA is considering whether the Merged Entity could engage in a partial foreclosure strategy against rival NAVs in the Southern Water Region by increasing the price, reducing the quality and services supplied to them or sharing CSI.

206. The CMA assesses the ability and incentive of the Merged Entity to pursue a foreclosure strategy against rival NAVs, as well as its effect on competition, below.

*Ability*

207. For the reasons set out in paragraph 165 above, the CMA considers that Southern Water has the market power to engage in a foreclosure strategy, and that its input is critical to downstream rival's ability to compete in its area.

*Regulation*

208. The Parties did not distinguish between water and wastewater in their submissions regarding the protection that existing regulations provide rival NAVs against a potential foreclosure strategy. Therefore, the CMA refers to the Parties' submissions set out in paragraph 166 above.

209. Similarly, no third parties highlighted material differences between the protections that regulations could afford them when competing for and adopting last mile water connections versus wastewater connections. Therefore, the CMA refers to the third parties' views set out in paragraphs 169 to 171 above.

210. Equally, Ofwat's D-MEX rankings measuring the quality of services that developers and other third parties receive applies to both water and wastewater.[205]

211. Therefore, for the reasons set out in paragraphs 172 and 173 the CMA considers that the existing regulation may not eliminate all ways in which Southern Water might disadvantage rival NAVs and thereby impact their competitiveness downstream.

[205] Further detail is set out in paragraph 197 above.

*CMA's view on Merged Entity's ability to foreclose*

212. Based on the evidence above, the CMA considers that the Merged Entity may have some ability to foreclose rival NAVs, particularly given that: (i) Southern Water has the market power to engage in a foreclosure strategy; (ii) Southern Water's input is necessary for rival NAVs to provide their services; and (iii) existing regulations may not eliminate all ways in which Southern Water might disadvantage rival NAVs.

*Incentives*

213. In this section, the CMA considers whether the Merged Entity would have the incentive to foreclose rival NAVs active in the adoption of last mile wastewater connections in the Southern Water Region. To assess incentives, the CMA considers the magnitude and likelihood of the costs and benefits of any foreclosure strategy.[206]

*Parties' submissions*

214. In their submissions on incentives, the Parties did not distinguish between water and wastewater. In summary, the Parties submitted that the Merged Entity would not have the incentive to foreclose rivals because it would face costs for breaching Ofwat's regulations in the form of enforcement action, financial penalties and financial losses via D-MEX, that discriminatory behaviour is in breach of its licence and is readily detectable, and that there are no material benefits to a foreclosure strategy. The Parties' submissions on this are set out in full in paragraphs 176 to 179 above.

*Third-party views*

215. The CMA approached NAVs to gather their views on the costs and benefits that the Merged Entity may face when pursuing a foreclosure strategy, but no third party highlighted material differences between water and wastewater in this regard. Therefore, the CMA refers to the third parties' views set out in paragraph 182 above.

216. The CMA also sought views from NAVs on how an incumbent may affect their ability to compete, but no third party highlighted material differences between how they may be impacted when competing for and adopting last mile water connections versus wastewater connections. Accordingly, the CMA refers to the third parties' views set out in paragraphs 183 to 184 above.

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[206] CMA129, paragraph 7.16.

*CMA's view on the Merged Entity's incentive to foreclose*

217. To understand the likelihood of the Merged Entity recapturing sales from its downstream rivals as a result of foreclosure, the CMA considered the current market structure to assess whether the Merged Entity's downstream offering is successful and how closely it competes with other downstream suppliers.

218. For the third-party adoption of wastewater connections, the Parties estimated[207] that in FY2023-24 IWNL held a share of [20-30]%, Leep held a share of [0-10]% and Advanced Water did not adopt in that time, with the remaining [70-80]% held by LMI ([40-50]%) and Southern Water ([20-30]%).[208,209] The Parties submitted that IWNL [✂].[210] The CMA therefore considers that IWNL is a close competitor to LMI.

219. Based on the evidence above and the reasons set out in paragraphs 187 to 198 (given the lack of differences in the evidence between last mile water and wastewater connections), the CMA considers that the Merged Entity does not have the incentive to pursue a foreclosure strategy against rival NAVs in the adoption of last mile wastewater connections in the Southern Water Region.

*Effect*

220. Given the CMA considers that the Merged Entity would not have the incentive to foreclose LMI's rivals, the CMA has not considered effects in its assessment.

**Conclusion on Theory of Harm 3**

221. Based on the evidence above, the CMA considers that the Merged Entity does not have the incentive to pursue an input foreclosure strategy against rival NAVs in the market for the adoption of last mile wastewater connections in the Southern Water Region. Accordingly, the CMA considers that the Merger does not give rise to a realistic prospect of an SLC as a result of input foreclosure in the adoption of last mile wastewater connections in the Southern Water Region.

[207] Based on a count of connections adopted at sites with more than 25 connections in FY23-24.
[208] As Southern Water was not able to distinguish between installation and third-party adoption opportunities for third party connections, the CMA is not able to estimate what proportion of these adoption opportunities were won at the installation or third-party adoption stage. Annex RFI2 – MAM, paragraph 93 and Annex RFI2 - MAM.RFI2.26.1.
[209] The Parties submitted information on NAV applications since the beginning of 2023 that showed Advanced Water had made an NAV application, but Advanced Water did not appear in the Parties' share of supply estimates calculated using the count of adoptions between FY2023-24.
[210] FMN, paragraph 315.

# ENTRY AND EXPANSION

222. Because the Merger will not result in an SLC under any theory of harm considered, the CMA has not carried out a separate assessment of whether entry or expansion could function as a countervailing factor against a potential SLC.

# DECISION

223. Consequently, the CMA does not believe that it is or may be the case that the Merger may be expected to result in an SLC within a market or markets in the United Kingdom.

224. The Merger will therefore not be referred under section 33(1) of the Act.

**Naomi Burgoyne**
**Senior Director, Mergers**
**Competition and Markets Authority**
**16 September 2024**

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[i] Following clarification from the Parties, Paragraph 26 should read 'Infracapital, headquartered in the UK, is the infrastructure equity investment business unit of M&G plc and manages funds, namely: Infracapital Partners III (Euro) SCSp, Infracapital Partners III (Sterling) SCSp, and ICP (Finch) LP. These funds, acting by their respective managers, indirectly own 100% of the issued share capital of LMI.'

[ii] Following clarification from the Parties, Footnote 8 should read 'ie M&G Alternatives Investment Management Limited and M&G Investment Management Limited; FMN, paragraph 3.'