Completed Acquisition by Iberdrola, S.A., through its Subsidiary Scottish Power Energy Networks Holdings Limited, of North West Electricity Networks (Jersey) Limited

Decision on duty to refer

ME 7118/24

The Competition and Markets Authority's decision on relevant merger situation and whether the merger is likely to cause substantial prejudice to Ofgem's ability to make comparisons between energy network enterprises, under section 68B of the Enterprise Act 2002 given on 20 March 2025. Full text of the decision published on 1 May 2025.

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 Some numbers have been replaced by a range, which are shown in square brackets.

SUMMARY

1. The Competition and Markets Authority (**CMA**) has found that the acquisition by Iberdrola S.A. (**Iberdrola**) of North West Electricity Networks (Jersey) Limited (**NWEN**) (the **Merger**), is a relevant merger situation that does not cause substantial prejudice to the ability of the Office of Gas and Electricity Markets (**Ofgem**) to make comparisons between energy network enterprises of the type involved in the Merger.

2. Iberdrola is active in the UK electricity sector through its ownership of ScottishPower group (**SP**) and, in turn, SP Energy Networks Limited (**SPEN**).[i] The activities of Iberdrola and its subsidiaries include electricity generation, electricity transmission and electricity distribution. NWEN owns and operates Electricity North West Limited (**ENWL**), a regional distribution network operator (**DNO**) licensed under the Electricity Act 1989 (the **EA1989**) to distribute electricity in the North West of England. Iberdrola and NWEN are together referred to as the **Parties** and, for statements relating to the future, the **Merged Entity**.

3. The CMA has a duty to investigate energy network mergers further to the special energy network merger provisions of the Enterprise Act 2002 (the **Act**). The CMA has concluded that it has jurisdiction to review this Merger because a relevant merger situation has been created: each of Iberdrola and NWEN is an energy network enterprise of the same type that will cease to be distinct as a result of the Merger; and the turnover test is met.

4. The CMA has also considered the Merger's effect on competition in the adoption of last mile utility connections and has decided not to refer the Merger to a phase 2 investigation in a separate decision on 20 March 2025.

Assessment

5. The CMA has considered the Parties' submissions and Ofgem's opinion on the proposed acquisition by Iberdrola of NWEN, submitted to the CMA on 21 February 2025, (**Ofgem's Opinion**) for the purposes of its assessment. In line with these submissions, the CMA assessed the Merger with respect to the four criteria set out in Ofgem's approach to energy network mergers and statement of methods. Accordingly, the CMA considers that the Merger does not give rise to a realistic prospect of substantial prejudice to Ofgem's ability to make comparisons between energy network enterprises of the type involved in the Merger.

Conclusion

6. The Merger will therefore **not be referred** under section 68B of the Act.

ASSESSMENT

1. PARTIES AND MERGER

1.1 Parties

1. Iberdrola is a global energy and integrated utilities company headquartered in Spain and listed on the Spanish Stock Exchanges. In the UK, the activities of Iberdrola and its subsidiaries include electricity generation, electricity transmission and electricity distribution. Iberdrola is the ultimate owner of SPEN, a company licensed under the EA1989 and regulated by Ofgem to distribute electricity in Central and Southern Scotland, North Wales, Merseyside, Cheshire and North Shropshire.[1]

2. The turnover of Iberdrola in 2024 was approximately £42 billion worldwide and approximately £6 billion in the UK.[2ii]

3. NWEN is a Jersey incorporated company, that owns and operates ENWL, an English and Welsh incorporated company that is licensed under the EA1989 and regulated by Ofgem to distribute electricity in the North West of England, including from Cumbria to Greater Manchester. NWEN and ENWL, along with certain other group companies, form the Electricity North West (**ENW**) group.[3]

4. The turnover of NWEN in the financial year 2024 was approximately £623 million, all of which was in Great Britain (**GB**).[4]

1.2 Merger

5. On 2 August 2024, Iberdrola entered into an agreement to acquire 85.63% of the issued shares of NWEN for approximately £2.1 billion, together with a subscription for an additional 2.37% of shares in NWEN. The agreement was novated to Scottish Power Energy Networks Holdings Limited (**SPENH**) on 30 September 2024.[5]

6. The Parties also informed the CMA that the 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 7 October 2024.[6]

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[1] Final Merger Notice submitted to the CMA on 29 January 2025 (**FMN**), page 5.
[2] Annex 006 to the FMN, page 1 and FMN, paragraph 6.1. The turnover figures have been converted from euros to Great British Pounds using the Bank of England's exchange rate on 19 March 2025 (1.1884).
[3] FMN, paragraphs 2.3 and 3.1.
[4] FMN, paragraph 3.5.
[5] FMN, paragraph 2.8.
[6] FMN, paragraph 2.13, and an email from [✂] received on 7 October 2024.

2. PROCEDURE

7. The CMA's mergers intelligence function identified the Merger as warranting an investigation.[7] The CMA announced the launch of its phase 1 investigation by notice to the Parties on 29 January 2024.

8. Ofgem has a statutory role in the phase 1 assessment of energy network mergers.[8] Before the CMA reaches its decision on whether to refer an energy network merger, the CMA must request and consider Ofgem's Opinion on whether the merger has prejudiced or is likely to prejudice Ofgem's ability, in carrying out its functions, to make comparisons, and if so, whether any prejudice is outweighed by any relevant customer benefits.[9] Ofgem has provided the CMA with its opinion on the Merger, which is referenced, where relevant, below.

9. The CMA's assessment in this decision under the special energy network merger regime is independent of its separate assessment of the Merger's effect on competition in the adoption of last mile utility connections.[10] With respect to the Merger's effect on competition, the CMA decided to not refer the Merger to a phase 2 investigation in a separate decision on 20 March 2025.

3. JURISDICTION

10. Each Party holds one or more licences of the same type,[11] issued under the EA1989, enabling it to carry out licensable activities in GB. Consequently, for the purposes of the special energy network merger regime, Iberdrola and NWEN is each an energy network enterprise of the same type. As a result of the Merger, the Parties have ceased to be distinct, and the CMA therefore considers the Merger to be an energy network merger which is subject to investigation under the special energy network merger regime, which was introduced into the Act by the Energy Act 2023.[12]

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[7] Mergers: Guidance on the CMA's jurisdiction and procedure (**CMA2**), 2 January 2025, paragraphs 6.4–6.6.
[8] Energy network mergers: Guidance on the CMA's procedure and assessment (**CMA190**), 2 January 2025, paragraphs 1.8, 1.13-1.18 and 2.4-2.5.
[9] Section 68D(1)-(2) of the Act.
[10] If the businesses of both merging parties involve energy network enterprises of the same type, and also include other activities, the CMA will consider the parts of the transaction relating to the overlapping energy network enterprises under the special energy network merger provisions and the parts of the transaction relating to the parties' other activities under the general merger provisions of the Act. (CMA190, 2 January 2025, paragraph 1.3).
[11] An energy network enterprise is an enterprise carried on by a company holding a licence under section 7 of the Gas Act 1986 (gas transporter), section 6(1)(b) of EA1989 (transmission of electricity) or section 6(1)(c) of EA1989 (distribution of electricity), except in relation to the transmission or distribution of electricity, where the licence was awarded by way of a competitive tender (s.68A(2) EA02). CMA190, paragraph 1.7 provides examples of two electricity distribution licensees or two electricity transmission licences.
[12] CMA190, paragraph 2.10

11. The GB turnover of NWEN exceeds £70 million in financial year 2024,[13] so the turnover test in section 23(1)(b) of the Act is satisfied.[14]

12. The Merger completed on 22 October 2024 and the CMA was informed of this the same day.[15] Following extensions to the statutory four-month deadline as per section 25(1) and section 25(2) of the Act, the four-month deadline for this decision under section 24 of the Act is 3 April 2025.

13. The CMA therefore believes that it is or may be the case that a relevant merger situation has taken place, with respect to the special energy merger provisions of the Act.

14. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 30 January 2025 and the statutory 40 working day deadline for a decision is therefore 27 March 2025.

4. COUNTERFACTUAL

15. The CMA assessed the impact of the Merger on Ofgem's ability to carry out comparisons against the situation that would prevail in the absence of the Merger.[16] Consistent with its approach to general phase 1 merger investigations, the CMA believes the most cautious realistic counterfactual is a situation where the Merger is assumed not to have occurred and the two firms continue to operate under independent ownership.

5. ASSESSMENT

5.1 Statutory framework

16. The intention of the special energy network merger regime is to ensure that a merger between two or more energy network enterprises of the same type in GB will not substantially prejudice Ofgem's ability to make comparisons for the purpose of carrying out its statutory functions under Part 1 of the Gas Act 1986 or Part 1 of the EA1989.[17]

17. The CMA considers that an increase in common ownership or control across one or more companies has the potential to affect the ability of Ofgem to make comparisons.[18] Ofgem's regulatory framework for network enterprises uses the

[13] Email from the Parties to the CMA dated 14 March 2025.
[14] Section 23(1)(b) of the Act, as amended, now provides for a £100 million turnover test, but the £70 million threshold continues to apply to mergers which completed before 1 January 2025. See SI 2024/1226, Schedule, paragraph 5. References to the Act in this decision include the modifications made by Schedule 5A of the Act, where relevant.
[15] Email from [✂] to the CMA dated 22 October 2024.
[16] Merger Assessment Guidelines (**CMA129**), March 2021, paragraph 3.1.
[17] CMA190, paragraph 1.6.
[18] CMA190, paragraph 4.13.

concept of a 'notional efficient' licensee. A notional efficient network licensee is a hypothetical construct that Ofgem uses as a 'yardstick' for actual network licensees when setting expenditure allowances, performances targets, and regulatory incentives that rewards licensees that move closer to (or beat) the yardstick and penalises licenses that fall behind.[19]

18. For the purposes of its phase 1 assessment of an energy network merger, the CMA has interpreted the statutory test as requiring it to assess whether there is a realistic prospect that the Merger has caused, or may be expected to cause, substantial prejudice to Ofgem's ability to make comparisons between energy network enterprises of the same type involved in the energy network merger.[20]

19. Where the CMA finds that it is or may be the case that the energy network merger has substantially prejudiced, or is likely to substantially prejudice, Ofgem's ability to make comparisons between energy network enterprises, it may decide not to make a reference if that prejudice is outweighed by relevant customer benefits (**RCBs**) relating to the merger.[21]

5.2 CMA approach

20. The CMA has considered the views and evidence provided by the Parties and Ofgem on both the likely prejudice, and the extent of such prejudice, on Ofgem's ability to make comparisons between energy network enterprises, and whether such prejudice is outweighed by RCBs. [22] Section 5.3 below discusses the Parties' submissions and Ofgem's Opinion with respect to the four criteria set out in Ofgem's approach to energy network mergers and statement of methods when assessing the likely impact of a merger on Ofgem's ability to make comparisons (**Ofgem's Statement of Methods**).[23] The four criteria are as follows.

    (i) **Criterion 1:** Could the merger lead (or has the merger led) to a loss, or a deterioration in the quality of information available to Ofgem on a) the relationship between costs and performance; and b) exogenous drivers of costs and performance such as regional factors (eg urbanity, sparsity)?

    (ii) **Criterion 2:** Could the merger lead (or has the merger led) to a loss, or a deterioration in the quality of information available to Ofgem on good performance/behaviours and efficient levels of costs?

[19] CMA190, paragraph 4.7.
[20] CMA190, paragraphs 2.2 and 4.2.
[21] CMA190, paragraph 2.3.
[22] CMA190, paragraph 2.4.
[23] See, Ofgem's Statement of Methods, part 7.

(iii) **Criterion 3:** Could the merger lead (or has the merger led) to a reduction in the diversity of management approaches and practices in a way that adversely affects the availability of information of good performance and efficient levels of costs?

(iv) **Criterion 4:** Could the merger lead (or has the merger led) to a reduction in rivalry between network enterprises in a way that adversely affects the incentive of individual licensees to pursue performance improvements and cost efficiencies?[24]

21. In assessing the impact of the Merger on Ofgem's ability to make comparisons, the CMA has further considered (including but not limited to) the following factors: the number and quality of independent observations that remain, and the loss of an independent comparator or the loss of a company with important similarities or differences.[25]

5.3 Ofgem's criteria for the assessment of the impact of a merger

22. This section addresses each of the four criteria referred to in paragraph 20 in turn below.

5.3.1 Criterion 1

23. The Parties and Ofgem made submissions on whether the Merger could lead to a loss, or a deterioration in the quality, of information available to Ofgem on: (a) the relationship between costs and performance; and (b) exogenous drivers of costs and performance such as regional factors (eg urbanity and sparsity).[26]

5.3.1.1 Parties' submissions

24. The Parties' submissions in relation to this criterion were two-fold.

(a) First, as regards the relationship between costs and performance, the Parties submitted that any loss of a data point for the assessment of core business support costs (ie the only area assessed at a group level in RIIO-ED2) would be limited.[27] These business support costs only account for approximately 2.5% of Ofgem's cost assessment approach, and by removing a small,

[24] CMA190, paragraph 4.12 and Ofgem's Statement of Methods, part 7.
[25] CMA190, paragraph 4.14.
[26] CMA190, paragraph 4.12.
[27] RIIO-ED2 is the price control for the electricity distribution network, where network companies take power from the transmission network and deliver it at safe, lower voltages to homes and businesses. The price control runs for five years, from 2023-2028.

individual DNO as a result of the Merger, would result in a more homogeneous comparator set of DNO groups.[28]

(b) Second, as regards exogenous drivers of costs and performance, the Parties submitted that the vast majority of Ofgem's performance measures are recorded at the DNO level, and not at the network enterprise level.[29]

5.3.1.2 Ofgem's Opinion

25. In terms of DNO characteristics, Ofgem submitted that the Merger brings together the two of the smallest DNO groups. As such, Ofgem found that the Merged Entity would be a median-size DNO group in the industry on several size metrics and stated that this may even improve the comparability of DNO groups for cost benchmarking purposes. Further, Ofgem found that the Parties' individual DNOs do not exhibit unique regional and company-specific characteristics. As such, it submitted that the Merger will not lead to a loss of useful regional and DNO-specific information being taken into account before Ofgem make cost comparisons.[30]

26. Ofgem concurred with the Parties that the majority of incentives are recorded at the network level and that there was no scope for within-group allocation of performance.[31]

27. Finally, under the assumption that Ofgem keeps the same cost assessment approach as at RIIO-ED2, Ofgem stated that 95% of the submitted costs would continue to be collected at the DNO level. The remaining 5% of submitted costs (ie business support costs) are collected at group level, where the Merger reduces the number of submitting groups from six to five. Notwithstanding the potential for the change in the reporting of the Parties' business support costs to result in a loss in the precision of the efficient cost benchmark modelling, Ofgem submitted that it does not believe that this change in the underlying data would be sufficient to prejudice its ability to make comparisons going forward.[32]

5.3.1.3 CMA assessment

28. In line with the Parties' submissions, and considering Ofgem's conclusions regarding the effect of the Merger outlined in Ofgem's Opinion, the CMA finds that the Merger does not affect the level of detail or quality of the vast majority of cost and performance data collected by Ofgem. The CMA also agrees with Ofgem that any deterioration in the quality of information collected as a result of the Merger is

[28] MIA, pages 41ff.
[29] MIA, pages 28ff.
[30] Ofgem's Opinion, paragraphs 3.15 to 3.16, and 3.18.
[31] Ofgem's Opinion, paragraph 3.22.
[32] Ofgem's Opinion, paragraph 3.13 to 3.14.

does not give rise to a realistic prospect of substantial prejudice to Ofgem's ability to make cost and performance comparisons going forward.[33]

5.3.2 Criterion 2

29. The Parties and Ofgem made submissions on whether the Merger could lead to a loss, or a deterioration in the quality, of information available to Ofgem on good performance/behaviours and efficient levels of costs.

30. The CMA assessment of this criterion focuses on whether the Merger leads to a loss (or deterioration of the quality) of information that would substantially diminish Ofgem's ability to implement historically comparable cost and performance benchmarking modelling in future price controls.

31. In their submissions relating to this criterion, both the Parties and Ofgem discuss whether the Merger is likely to reduce the intensity of the pseudo-competitive process embedded in the regulatory cost and performance benchmarking process, and, therefore, produce less efficient modelled costs and less stretching performance targets. Noting the close connection between the effect of the Merger on rivalry and on the intensity of pseudo-competition through benchmarking, the CMA addresses these submissions under criterion 4 from paragraph 50 below.

5.3.2.1 Parties' submissions

32. The Parties submitted that the Merger is not expected to lead to a loss or a deterioration in the quality of information on efficient levels of costs. Ofgem requires DNO-level reporting and there is a rigid cost allocation process within SPEN that will be applied post-merger.[34]

33. The Parties also submitted that only five of the 14 ODI performance targets in RIIO-ED2 applied to ENWL are informed by some form of comparative assessment.[35] As such, any risk of negatively affecting output performance targets is limited to two ODI measures where ENWL is one of the 'leading' DNOs. The Parties stated that the risk of negatively affecting output performance targets is low. This was because the targets set at RIIO-ED2 were company-specific and/or included reference to the industry average.[36]

[33] Ofgem's Opinion, paragraph 3.14.
[34] MIA, page 87.
[35] **ODI** refers to outcome delivery incentives, being the regulatory mechanism used to encourage energy network companies to deliver high-quality services and improvements that benefit customers.
[36] MIA, page 57.

5.3.2.2 Ofgem's Opinion

34. For the smaller set of cost categories that are evaluated at network enterprise level (ie, core business support costs), Ofgem submitted that there would be a reduction in the number of comparators from six to five. As such, it found that there could be, in principle, an adverse effect of the Merger on quality of information available to Ofgem to determine the efficient cost benchmark. However, Ofgem submitted that, in practice, it did not consider that the potential loss of information was sufficient to offset its ability to identity the efficient level of costs.[37]

35. Ofgem submitted that for the vast majority of cost categories, it requires that the data it uses to assess the efficient cost benchmark is collected at the DNO-level. Post-merger, it submitted that the Parties would continue to report these cost categories at the DNO-level.[38]

36. Ofgem also submitted that it will continue to have the same level of data available when setting performance targets (ie ODIs) in the price control – with one exception which is set at a network enterprise level.[39] However, given the size of this one ODI set at the network level, Ofgem did not consider that this was a major concern. It submitted that the reduction from six to five groups resulting from this Merger only had a low impact on its ability to set performance targets for this ODI.[40]

37. For the other ODIs, Ofgem found there was no scope for within-group allocation that might otherwise negatively affect performance scores. Since the DNO-level data collected to assess these ODIs is unaffected by the Merger, Ofgem did not consider their ability to set output performance targets at the licensee level to be affected by the Merger.[41]

5.3.2.3 CMA assessment

38. In line with the Parties' submissions, and considering Ofgem's conclusions regarding the effect of the Merger on its access to cost data and ODIs, the CMA finds that the Merger has limited scope to result in the loss, or deterioration of, quality of information collected to determine the efficient cost benchmark.

39. Similarly, for the ODIs set with reference to DNO-level performance data, the CMA finds that Ofgem's ability to set these output performance targets is unaffected by

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[37] Ofgem's Opinion, paragraphs 3.30 and 3.31.
[38] Ofgem's Opinion, paragraph 3.25.
[39] Ofgem state that the RIIO-ED2 Distribution System Operation (DSO) incentive is the only ODI set using group level information. Ofgem's Opinion, paragraph 3.51.[40] Ofgem's Opinion, paragraph 3.51.[41] Ofgem's Opinion, paragraphs 3.50 to 3.51.
[40] Ofgem's Opinion, paragraph 3.51.[41] Ofgem's Opinion, paragraphs 3.50 to 3.51.
[41] Ofgem's Opinion, paragraphs 3.50 to 3.51.

the Merger. In the one instance where the ODI is set at the group level, the CMA agrees with Ofgem that a reduction from six to five corporate groups only has a low impact on Ofgem's ability to set performance targets.

5.3.3 Criterion 3

40. The Parties and Ofgem made submissions on whether the Merger could lead to a reduction in the diversity of management approaches and practices in a way that adversely affects the availability of information on good performance and efficient levels of costs.

5.3.3.1 Parties' submissions

41. The Parties submitted that the Merger is not expected to lead to a reduction in the diversity of management approaches and practices in a way that adversely affects the availability of information on efficient levels of costs. They emphasised that while management performance responds to overarching ownership culture and policy setting, DNO operations directors have the autonomy and incentive to respond to very local and micro-environmental needs – factors not directly affected by the Merger. Therefore, in addition to the adoption of best practice across the three DNOs, the Parties submitted that a [✂] degree of management independence and diversity in cost and service performance would [✂] post-Merger.[42]

5.3.3.2 Ofgem's Opinion

42. Ofgem submitted that the Merger would result in a reduction in the number of corporate groups from six to five – and therefore a reduction in the number of management approaches and practices. However, Ofgem considered that the risk of losing useful information for their efficiency assessment is marginal. As such, they found that the industry will still contain a sufficient diversity of management approaches among rival DNO groups after the Merger.[43]

43. From a performance perspective, Ofgem submitted that while there may be some limited reduction in management diversity compared to the counterfactual, it had not seen evidence to suggest it will have any material impact on the availability of information indicating good performance.[44]

[42] MIA, pages 57-60.
[43] Ofgem's Opinion, paragraphs 3.54 to 3.55.
[44] Ofgem's Opinion, paragraph 3.67.

5.3.3.3 CMA assessment

44. Post-Merger NWEN's management structure will be [✂]. As a result, the number of management teams in the industry will be [✂].[45] Noting Ofgem's Opinion that the industry will still contain a sufficient diversity of management approaches among rival DNO groups to provide Ofgem with the information it needs to assess performance and the efficiency of costs, the CMA agrees with Ofgem's conclusion that any reduction in diversity of management approaches as a result of the Merger does not give rise to a realistic prospect of substantial prejudice to Ofgem's ability to perform comparisons.

5.3.4 Criterion 4

5.3.4.1 Framework

45. Criterion 4 relates to whether the Merger could lead to a reduction in rivalry between network enterprises. As set out in Ofgem's statement of methods, it is assessed by considering whether the Merger would lead to a consolidation of control in a way that adversely affects the incentive of individual licensees to pursue performance enhancements and cost efficiencies.[46]

46. The mechanism by which a merger between network enterprises could dampen such incentives is set out in Ofgem's Statement of Methods:

> 'The effectiveness of [Ofgem's regulatory mechanism] depends on the willingness of individual network licensees to pursue cost savings and associated financial rewards, at the potential cost of more challenging cost efficiency targets for all network licensees. The management of network licensees that are under common control might take a more holistic view of their financial incentives across all licensees under their ownership, taking account of the financial rewards for cost savings as well as the potential impact on expenditure allowances across all their licensees. This in turn could adversely affect the extent of rivalry in the sector and the incentive of individual licensees to pursue efficiencies, and consequently the quality of information available to us on efficient levels of costs'.[47]

47. Network licence holders are incentivised by Ofgem to invest in cost efficiency and performance enhancing schemes. For example, within the duration of a price control period, network licence holders can retain part of their gains for investment in these schemes. However, investments that lower a licensee's TOTEX in a given

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[45] Ofgem's Opinion, paragraph 3.51.
[46] Ofgem's Statement of Methods, paragraph 7.6.
[47] Ofgem's Statement of Methods, paragraph 5.12.

price control period may materially decrease cost allowances for all licensees in future price control periods through their effect on the efficient cost benchmark and, to a lesser extent, changes in predictions from Ofgem's cost regression models.[48] When two licensees merge, each licensee would be expected to take account of the negative externalities of its cost-reduction projects on the other merging party. This is because post-merger, the combined entity will maximise profits across its business as a whole. This means that some cost-reduction projects that were profitable before a merger become less profitable or loss-making after a merger. Therefore, a key consideration for the purposes of assessing criterion 4 is whether a merger of multiple licence holders could reduce rivalry in efficiency enhancing investments, thus leading to higher cost allowances at future price controls.

5.3.4.2 Parties' submissions

48. The Parties submitted that there would be no incentive to engage in a strategy which seeks to reduce efficiency enhancing investments post-Merger for a number of reasons, including:[49]

    (a) Efficient cost benchmarks are based on relative comparisons rather than absolute ones.

    (b) ENWL may not be at the threshold at RIIO-ED3 when Ofgem assesses the forecast data. This is a critical and necessary condition for there to be any possibility of an incentive, as a change in ENWL's efficiency could only impact the benchmark if ENWL is positioned near the benchmark level and has a significant influence on its determination. However, it is not possible to accurately predict or manipulate ENWL's rank.

    (c) DNOs' efficiency performances around the benchmark level are typically very close to each other, further increasing the unpredictability of how reducing efficiency enhancing investments might impact potential future cost allowances. In other words, this makes it even more difficult to target a strategy to ensure that a DNO would be ranked in a predictable position.

5.3.4.3 Ofgem's Opinion

49. Ofgem submitted that it is not credible that one DNO in a wider corporate group would reduce efficiency enhancing investments, reducing its performance for the remainder of the current price control period in order to influence targets for the

[48] **TOTEX** is a regulatory concept used by Ofgem to assess and control the total costs incurred by energy network companies. It includes both capital expenditure and operational expenditure, ensuring a balanced approach to investment and efficiency.
[49] Parties' Response to the CMA's sixth request for information, paragraph 8.

next period (to the benefit of the wider corporate group) for a number of reasons, including:[50]

(a) The precise framework for the next price control is not decided and is not therefore known in advance.

(b) Even if the same framework is used, targets are set in such a way that a change in performance of one licensee out of fourteen would have minimal impact.

(c) There has been a convergence in DNO efficiency scores over time.

5.3.4.4 CMA assessment

50. To assess the likely impact of the Merger on criterion 4, the CMA has considered whether the Merged Entity would have an incentive to reduce efficiency enhancing investments post-Merger.

51. The evidence considered by the CMA includes quantitative modelling on incentives, alongside other evidence on the likely impact of the Parties' actions on the efficiency benchmark set by Ofgem, ie whether a strategy which seeks to reduce efficiency enhancing investments to the benefit of less efficient DNOs within the same corporate group would be effective, such that there is an incentive to pursue this strategy.

5.3.4.4.1 Quantitative analysis

52. The CMA conducted quantitative analysis to assess the likely effect of the Merger on the Parties' (and in particular, EWNL's) incentives to undertake efficiency enhancing investments.

53. Ofgem's cost benchmarking model is based on a series of 'top-down' regression models (where the dependent variable is total expenditure) and bottom-up models (where the dependent variable is the expenditure for a particular function). Bottom-up models incorporate both regression and non-regression components. The results of these models are averaged, before Ofgem applies the efficiency challenge.

54. As set out in paragraphs 34 to 37, it is possible to approximate the shift in incentives induced by the Merger by evaluating the extent to which cost-reduction initiatives at one DNO induce reductions in allowances at the other DNOs owned by the Merged Entity in future price control periods. To evaluate this effect in practice, we have simulated the impact of hypothetical reductions in TOTEX for

[50] Ofgem's Opinion, paragraphs 3.86, and 3.32 to 3.33.

each of the Parties' DNOs in the context of the most recent price control (RIIO-ED2). Specifically, we have considered the following changes:

(a) a hypothetical, unilateral 5% TOTEX reduction at each of Parties' DNOs, using Ofgem's top-down regression model and simplified cost allowance calculations;[51] and

(b) a hypothetical, unilateral TOTEX reduction of 1%, 2%, 3%, 4%, 5%, and 10%, at each of the Parties' DNOs, using Ofgem's top-down and bottom-up cost benchmarking models, and Ofgem's internal cost benchmarking procedure.

55. One important limitation of this analysis is that it does not account for any uncertainty in the future expenditure paths of the DNOs, and therefore any uncertainty in which DNOs will set the benchmark in future price control determinations. Put differently, if a DNO sets the benchmark in RIIO-ED2, in the analysis this DNO is assumed to set the benchmark with probability 1 in the next price control period.

56. Generally, for simulations where the DNO sets the benchmark, this approach is likely to have the effect of overstating the expected effect on cost allowances (because they might not set the benchmark in future price control periods). Conversely, for simulations where the DNO does not set the benchmark but is close to doing so, this approach may understate the expected effect on cost allowances (because they might conceivably do so in future price control periods).

57. Nevertheless, the CMA considers that this analysis provides a useful starting point for the assessment of Criteria 4 and has considered the results of this analysis alongside other evidence.

58. The results of the quantitative analysis (the framework for which is in the Annex) show that:

(a) SPMW is among the [✂] DNOs in RIIO-ED2, such that only [✂] TOTEX changes can [✂] cost allowances for all DNOs. Accordingly, there may be [✂] in incentive for the Merged Entity to invest in [✂] and [✂] TOTEX projects, but there may be [✂] incentives to implement [✂] TOTEX saving projects.

(b) SPD is [✂] than the cost benchmark threshold in RIIO-ED2, but [✂] TOTEX changes can [✂] cost allowances for all DNOs. Accordingly, there may be [✂] in the Merged Entity's incentive to invest in [✂] TOTEX projects, but

[51] These calculations were modelled by [✂], on behalf of the Parties. See Annex 357 to the FMN, 'Follow-up response to Q3 of the CMA's Request for information dated 10 December', 6 January 2025.

there may be [✂] incentives to implement [✂] and [✂] TOTEX saving projects.

(c) For ENWL, even modest TOTEX changes materially reduce cost allowances for the Parties' DNOs. This is because ENWL is at the benchmark in RIIO-ED2. In and of itself, this indicates that EWNL may have weaker incentives to invest in TOTEX savings post-Merger.

5.3.4.4.2 Other evidence

59. The CMA has considered other evidence relating to the structure of the electricity distribution sector and Ofgem's approach to regulation, where this is relevant to the likely effect of any strategy by the Merged Entity to reduce efficiency enhancing investments post-Merger. The CMA notes that the likely effect of such a strategy may also impact the expected costs and benefits of such a strategy for the Merged Entity.

5.3.4.4.2.1 Ofgem's approach to the appropriate efficiency benchmark

60. As submitted by Ofgem, many factors affect the selection of an appropriate efficiency benchmark, including the robustness of the model, the range of efficiency scores, historical performance and wider policy considerations.[52] The starting point for the efficiency benchmark may therefore change between price control periods, and it is not necessarily true that the 85th percentile will be the starting point for the efficiency benchmark in RIIO-ED3.[53]

61. A change in the appropriate efficiency benchmark between price controls may therefore change the expected identity of the DNO which sets the benchmark, reducing the effectiveness of any post-Merger strategy to decrease efficiency enhancing investments.

5.3.4.4.2.2 Relative comparisons

62. Ofgem's efficient cost benchmarks are based on relative comparisons of DNO efficiency scores, rather than absolute ones.[54] While the Merged Entity will own three of the 14 DNOs operating in the electricity distribution sector, post-Merger there will remain 11 DNOs that are owned by four other corporate groups, all of whom are being incentivised by Ofgem to undertake efficiency enhancing investments.[55] Accordingly, there will be some degree of uncertainty on the relative position of each of the Parties' DNOs at each price control, and any

[52] Ofgem's Opinion, paragraph 3.32.
[53] Ofgem's Opinion, paragraph 3.32.
[54] Ofgem's Opinion, paragraph 3.31.
[55] Ofgem's Opinion, paragraph 3.70.

quantitative modelling which seeks to predict this relative positioning will be subject to some margin of error.

63. Further, the Parties' submitted that the relative position of a given DNO can change between Ofgem's initial business plan assessment and the final determination, as was the case for example for EWNL at RIIO-ED2.[56] The DNO's own view of their modelled costs (as well as Ofgem's view of the DNO's modelled costs) can also change between draft and final determinations.[57] Changes in the level of modelled costs, and therefore the relative rankings of individual DNOs, between draft and final determinations may increase the level of uncertainty over the likely impact of a strategy to reduce efficiency enhancing investments post-Merger.

64. While the presence of multiple competitors in the market has the potential to enhance the level of uncertainty, the CMA notes that if the electricity distribution sector becomes more concentrated in the future, and the 14 DNOs active in the sector are owned by a smaller number of corporate groups, this level of uncertainty is likely to be reduced.

5.3.4.4.2.3 Convergence in efficiency scores over time

65. Ofgem has observed that between RIIO-ED1 and RIIO-ED2 there has been a convergence in efficiency scores across DNOs, with a more compact distribution of efficiency scores at RIIO-ED2.[58] While future industry changes such as infrastructure changes to connect new renewable energy sources may impact this trend in the future, Ofgem's experience is that there is a general convergence in the efficiency scores of DNOs active in the electricity distribution sector over time.[59]

66. This convergence of efficiency scores around the benchmark has implications for our analysis of the incentives and effectiveness of a strategy to reduce efficiency enhancing investments post-Merger. Put simply, if DNOs are expected to have very similar efficiency scores and therefore 'bunch' around the benchmark, the probability that any single one of them will set the benchmark in the future is lowered.

5.3.4.5 Criterion 4 conclusion

67. Considering all the factors outlined above in the round, and in particular, Ofgem's ability to flex its approach to the benchmark, and its input on its experience with

[56] Parties' Response to the CMA's Sixth request for information, paragraph 26.
[57] See for example Ofgem's draft and final determinations for ENWL at RIIO-ED2. Specifically, Ofgem, Table 26 RIIO-ED2 Draft Determinations ENWL Annex and Ofgem, Table 20, RIIO-ED2 Final Determinations ENWL Annex.
[58] Ofgem's Opinion, paragraph 3.33.
[59] Ofgem's Opinion, paragraph 3.33.

and expectations regarding efficiency scores, the CMA considers that, on balance, the Merger does not give rise to a realistic prospect of substantial prejudice to Ofgem's ability to perform comparisons through a reduction in rivalry between network enterprises.

5.3.5 Conclusion on the impact of the Merger

68. In reaching its decision at phase 1, the CMA places significant weight on Ofgem's Opinion.[60] This is because Ofgem has substantial experience in regulating the sectors relevant to special energy merger regime.

69. The CMA notes in particular that Ofgem's conclusions on the likely impact of the Merger on its ability to perform comparisons between network enterprises are based on Ofgem's experience to date of regulating the electricity distribution sector, in which 14 licensed DNOs are currently operated by six corporate groups, and there has been a convergence in DNO's efficiency scores over time.

70. The CMA has considered the Parties' submissions and Ofgem's Opinion as set out above in relation to all four criteria. Overall, the CMA concludes that the Merger does not give rise to a realistic prospect of substantial prejudice to Ofgem's ability to carry out its functions under the EA1989 to make comparisons between network enterprises of the type involved in this Merger.

5.4 Relevant customer benefits

71. As the CMA has concluded that the Merger does not give rise to a realistic prospect of substantial prejudice to Ofgem's ability to make comparisons, it is not necessary to consider RCBs in this decision.

[60] CMA190, paragraph 4.17.

DECISION

72. Consequently, the CMA does not believe that it is or may be the case that the Merger has caused, or may be expected to cause, substantial prejudice to the ability of Ofgem to make comparisons between energy network enterprises.

73. The Merger will therefore not be referred under section 68B(1) of the Act.

Jenny Sugiarto
Director, Mergers
Competition and Markets Authority
20 March 2025

ANNEX

1. This annex contains an empirical analysis of the possible effect that the Merger may have on the incentives for the Merged Entity to engage in cost efficiency enhancing investments, ie whether the Merged Entity will reduce efficiency enhancing investments post-Merger.

2. We find that:

   (a) the Merged Entity is likely to have [✂] incentives to invest in TOTEX savings at ENWL.

   (b) there is no change in the Merged Entity's incentive to invest in [✂] TOTEX projects. However, the Merger has some potential to [✂] incentives to implement [✂] and [✂] TOTEX saving projects at SPD.

   (c) there is [✂] in incentive for the Merged Entity to invest in SPMW's [✂] and [✂] TOTEX projects. However, the Merger may [✂] incentives to implement [✂] TOTEX saving projects at SPMW.

3. The rest of this annex outlines our methodology for assessing this criterion and presents the detailed results of our empirical analysis.

Assessing the effect of the Merger on rivalry through efficient cost benchmarking

Theoretical framework

4. By bringing existing DNOs under the control of a single firm, the proposed Merger between the Parties' DNOs may lead to lower investments in cost reducing technology over time. In turn, the efficacy of Ofgem's pseudo-competitive process embedded in the cost benchmarking process may be reduced and consumers might expect to pay higher prices over time as a result of the Merger.

Methodology

5. We consider a DNO at the beginning of the ED2 period who is evaluating whether to invest in some cost-reducing projects and wants to understand the impact on future allowances. To assess this, we can simulate how a hypothetical, unilateral reduction in TOTEX by each of Iberdrola's and NWEN's DNOs would affect *all* DNOs cost allowances if applied to Ofgem's cost benchmarking model in the most recent RIIO-ED2 price control.

6. Ofgem's cost benchmarking model is based on:

   (a) a top-down regression model; and,

(b) a bottom-up model incorporating both regression and non-regression components.

7. After efficiency challenges are applied to both the top-down and bottom-up cost models, Ofgem averages the resulting efficient modelled costs and applies a series of further adjustments to produce cost allowances for each DNO in the next price control.

8. We asked [✂] to show how a hypothetical, unilateral 5% TOTEX reduction at each of the Parties' DNOs would have affected all DNO cost allowances if applied to the most recent RIIO-ED2 price control. To simplify the calculations, [✂] only reduced TOTEX costs in the [✂] calculations.[61]

9. The results of [✂] simplified simulation analysis demonstrated that the hypothetical 5% TOTEX savings at ENWL and SPD, may [✂] all the Merged Entity's DNO cost allowances. In turn, raising the possibility that Merger may, in principle, [✂] the intensity of rivalry being implemented through the regulatory cost benchmarking process.

10. Following feedback on the analysis from Ofgem, the CMA conducted further analysis which expands [✂] approach, to provide a more in-depth examination of the potential for the Merger to diminish the incentive to implement efficiency enhancing investments post-Merger. The CMA's methodology expands on [✂] approach in three ways:

(a) to capture the broader scope of investment opportunities, we simulate a range of hypothetical % TOTEX in line with savings made in RIIO-ED1.

(b) we adjust both the top-down and bottom-up cost models for TOTEX savings.[62]

(c) we use Ofgem's internal cost benchmarking procedure to produce cost allowances for the revised cost modelling outputs.

11. To help determine a range of percentage TOTEX reductions to include in our analysis we have used historical data on DNO's underspend (overspend) on RIIO-ED1 TOTEX allowances. Figure 1's box plots show the distribution of the realised cumulative percentage TOTEX savings in each year of the RIIO-ED1 price control across DNOs.

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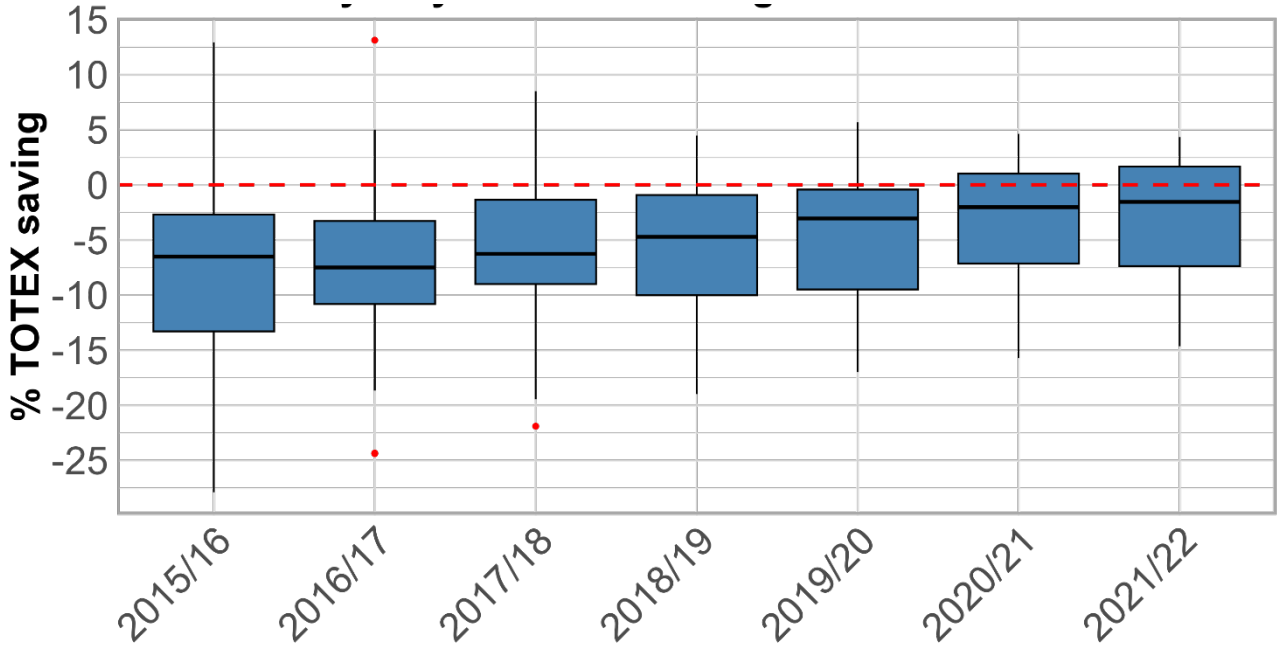
[61] Rather than reproduce Ofgem's detailed adjustments to produce new cost allowances, [✂] directly add the change in the efficient modelled costs to the original cost allowances from the ED2 price control. [✂] also use harmonised consumer price indices to update the base year for cost allowances from 2020/21 to 2022/23.
[62] Like [✂], we apply the hypothetical TOTEX reduction percentage in each year between 2016 and 2028 to the top-down regression model cost inputs. We also apply the hypothetical TOTEX reduction percentage in each year between 2016 and 2028 to the bottom-up regression and non-regression model cost inputs. Both the top-down and bottom-up models are re-run following the same internal procedure as used by Ofgem in the price determination process.

12. The figure shows that the cumulative median TOTEX savings increase from -6% to -2% over RIIO-ED1.[63] It also shows that, as DNOs approach the beginning of RIIO-ED2 price control, the range of cumulative TOTEX savings across DNOs contract. By 2022, the interquartile range of TOTEX savings over RIIO-ED1 lies between -7.5% and 2%. Broadly in line with the historic realised TOTEX saving data, we use hypothetical TOTEX savings of 1%, 2%, 3%, 4%, 5%, 7.5% and 10% in our empirical analysis.[64]

Figure 1 Realised cumulative yearly percentage TOTEX saving distribution in RIIO-ED1



Source: CMA analysis of Ofgem's RIIO-ED1 Annual Report 2021-22 Supplementary Data File

Source: CMA analysis of Ofgem's RIIO-ED1 Annual Report 2021-2022 Supplementary Data File

13. For each DNO, we compare recalculated cost allowances with the original RIIO-ED2 determination. This difference estimates the effect of a hypothetical unilateral X% reduction in the chosen DNO's TOTEX on all DNO cost allowances.

Pseudo Diversion Ratios

14. To measure the effect that a unilateral X%TOTEX saving at one of the Parties' DNOs may have on the Merged Entity's overall investment incentives, we calculate a pseudo-diversion ratio (**pseudo DR**). Pseudo DRs provide a simple, but useful way to assess how TOTEX savings can affect incentives to invest in cost reductions.

[63] For example, if a firm's TOTEX allowance was £100 million but it only spent £95 million, then its TOTEX saving is -5%. If on the other hand, the firm had spent £103 million, then it would have a TOTEX overspend of 3%.
[64] Note, for ENWL, we do not run a simulation for a TOTEX reduction of 7.5%.

15. To illustrate how pseudo DRs between the Parties' DNOs are calculated, suppose we have simulated the effect of an $X\%$ TOTEX saving at ENWL on all DNOs cost allowances. The pseudo DR from ENWL to SPD expresses the resulting change in SPD's cost allowance from 2024 to 2028 as a share of ENWL's $X\%$ TOTEX savings over the same period.[65]

16. More generally, for an $X\%$ TOTEX reduction the pseudo DR from DNO i to DNO j is defined as the ratio of the change in DNO j's cost allowance from 2024 to 2028 to DNO i's $X\%$ TOTEX savings over the same period.

$$DR_{ij}(X\%) = -\frac{Sum\ of\ the\ change\ in\ DNO\ j's\ cost\ allowance\ over\ 2024\ to\ 2028}{Sum\ of\ X\%\ TOTEX\ savings\ at\ DNO\ i\ over\ 2024\ to\ 2028}$$

17. All else equal, a higher pseudo DR indicates that the reduction in cost allowance associated with an $X\%$ TOTEX saving reduces the profitability of the associated investments.[66]

Analysing the effect of the merger on rivalry

18. Next, we describe how we combine our simulated cost allowance changes with pseudo DRs to analyse the possibility that the Merger may reduce the intensity of rivalry through its effect on the pseudo-competitive forces built into the cost benchmarking process.

19. First, we use the simulated cost allowance to identify where, if at all, an $X\%$ TOTEX saving at the chosen DNO directly affects the setting of the efficient cost benchmark. Second, we compare pseudo DRs pre- and post-Merger to assess whether the Merger substantially weakens the Merged Entity's incentive to invest in cost efficiencies at its DNOs.[67] Specifically, we focus on the increment in the pseudo DR arising from the Merger and its size compared to the DNO group's own internal pseudo DR (ie. the ratio of a DNO's TOTEX savings to the sum of the group's DNO cost allowances).

20. When the increment in the pseudo DR arising from the Merger is material, in absolute and/or relative terms, then some of the least profitable investments may switch from being NPV positive to NPV negative. If so, those investments may be deferred or abandoned. The larger the increment in the pseudo DR arising from

[65] All cost allowances and savings are measured in 2020/21 prices.
[66] Since we do not specify the cost of making different sized hypothetical investments, we do not have enough information on whether or not they would be NPV positive.
[67] Where TOTEX savings do not directly affect the cost benchmark, pseudo DR's can be affected by small changes to regression modelled outputs and non-regression bottom-up benchmark procedures. In particular, small TOTEX savings may cause shifts in allowances due to changes in the underlying regression model or non-regression calculations, resulting in substantial variations in pseudo DR estimates. For this reason, unless there is evidence that TOTEX savings affect the cost benchmark, we do not link pseudo DRs to investment incentives.

the Merger, the more likely it is that X% TOTEX saving investment will become unprofitable.

Limitations of our approach

21. Before discussing the results of our analysis, we highlight some limitations of our approach.

22. First, the analysis does not account for the uncertainty DNOs face in predicting how TOTEX savings will affect future cost allowance reductions.[68] In practice, DNOs are unlikely to be able to definitively know their position in the cost benchmark. Furthermore, Ofgem do not disclose its chosen cost benchmark before the price control and this benchmark may be subject to change.

23. Second, the analysis does not account for potential investment cost synergies between the DNOs. Efficiency investments may lower costs across all DNOs within the Merged Entity, potentially enhancing the overall benefits of these investments. Where the Merger gives rise to efficiencies, this may more than offset any losses incurred by reduced cost allowances.

Results

24. In this section, we present the results separately for each of the Parties' DNOs, showing the change in cost allowance and the pseudo DR for a range of hypothetical TOTEX savings up to 10% per year.

ENWL

25. Figure 2 shows how cost allowances at ENWL, SPD, and SPMW would have been affected in RIIO-ED2 by a hypothetical X% TOTEX cost saving for ENWL in each year from 2016 to 2028.

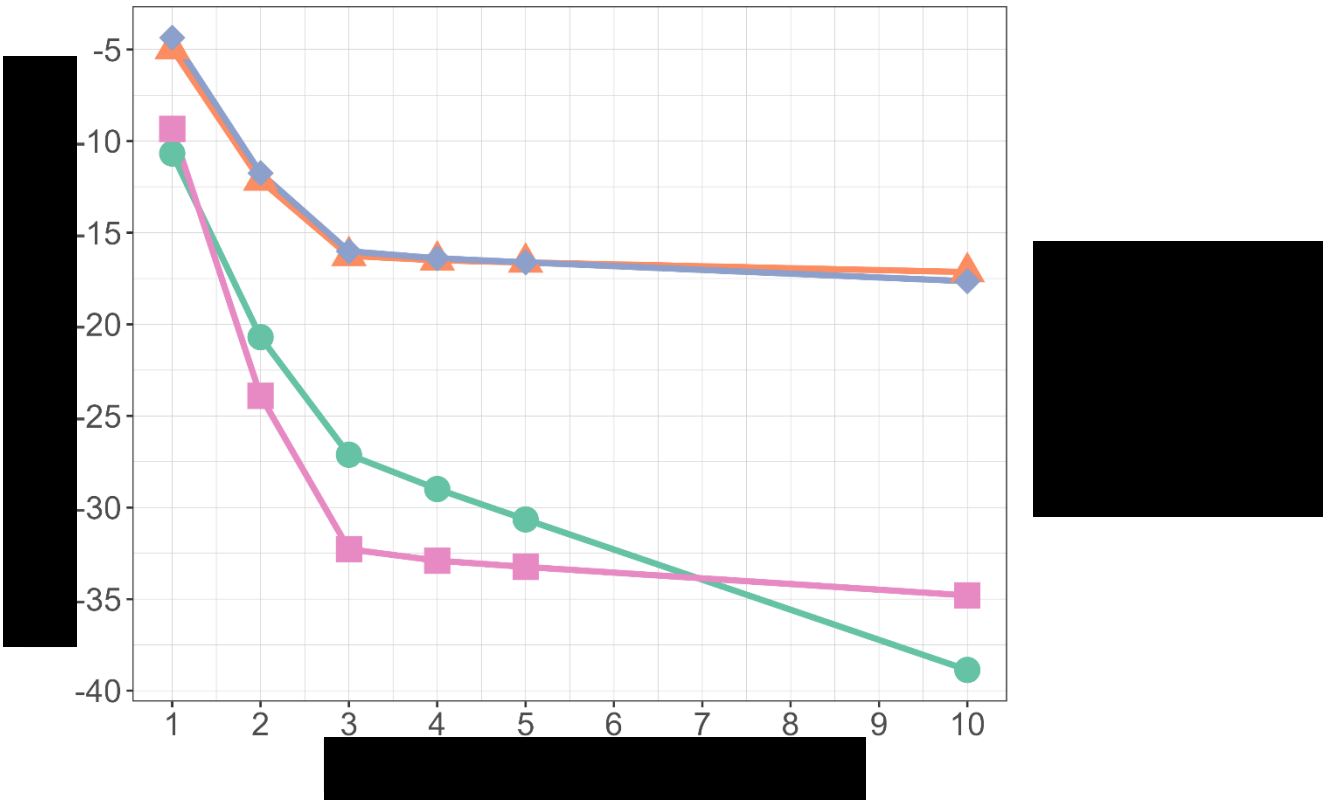
26. The figure shows that even for small percentage TOTEX savings, the combined future cost allowances for ENWL, SPD, and SPMW [✂] over 2024-2028.[69] This is because ENWL is on the efficient cost benchmark threshold in RIIO-ED2. As a result, even modest TOTEX changes [✂] cost allowances for the Parties' DNOs.

27. Beyond [0-5]% TOTEX savings, the figure shows [✂] further [✂] at SPD and SPMW's future cost allowances.[70] This suggests that beyond [0-5]% TOTEX savings for ENWL there is no further impact on the efficient cost benchmark from

[68] While it is theoretically possible to incorporate uncertainty into our analysis, it would be computationally intensive and is unlikely to be feasible in the time available in Phase 1.
[69] The combined cost reduction for the Parties' DNOs goes from £[✂] at a 1% TOTEX saving to £[✂] for a 3% TOTEX reduction.
[70] The combined cost allowance reduction over 2024-2028 at 5% TOTEX savings and £[✂] and £[✂] at 10%.

changes to the level of investment in efficiency enhancing investments post-Merger.

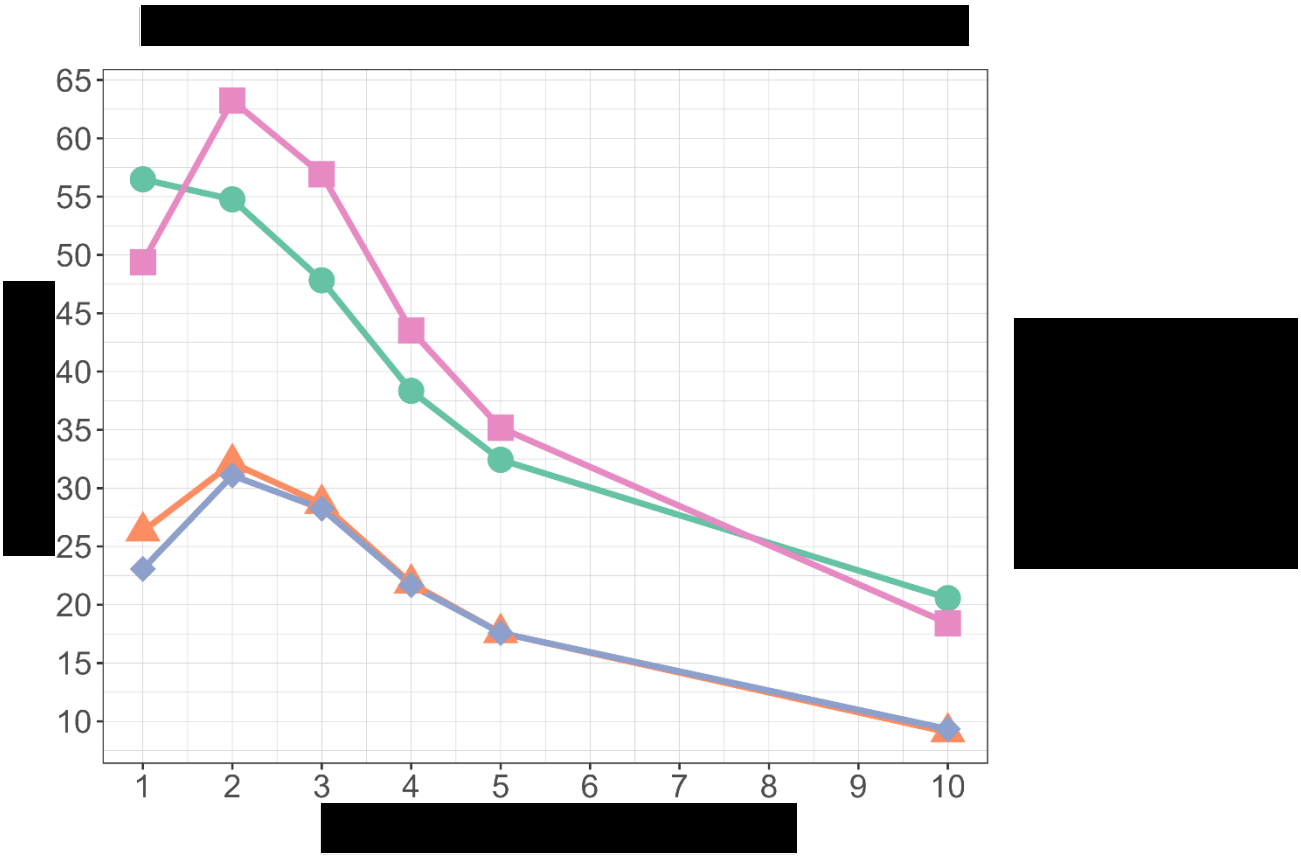
Figure 2 [redacted]



28. In the range of ENWL's TOTEX savings that directly affect the efficient cost benchmark (ie. between [✂]), Figure 3 shows that the combined pseudo DR for ENWL, SPD, and SPMW exceeds [✂]. This means that the Merged Entity's future cost allowance [✂] by [✂] over 2024–2028. The incremental pseudo DR for SPD and SPMW is at least [✂] percentage points (pp) and is often [✂] than ENWL's own internal pseudo DR – indicating a [✂] to cost allowances post-Merger.

29. Taken together this analysis suggests that the Merged Entity is likely to have [✂] incentives to invest in TOTEX savings at ENWL.

Figure 3 [redacted]



SPD

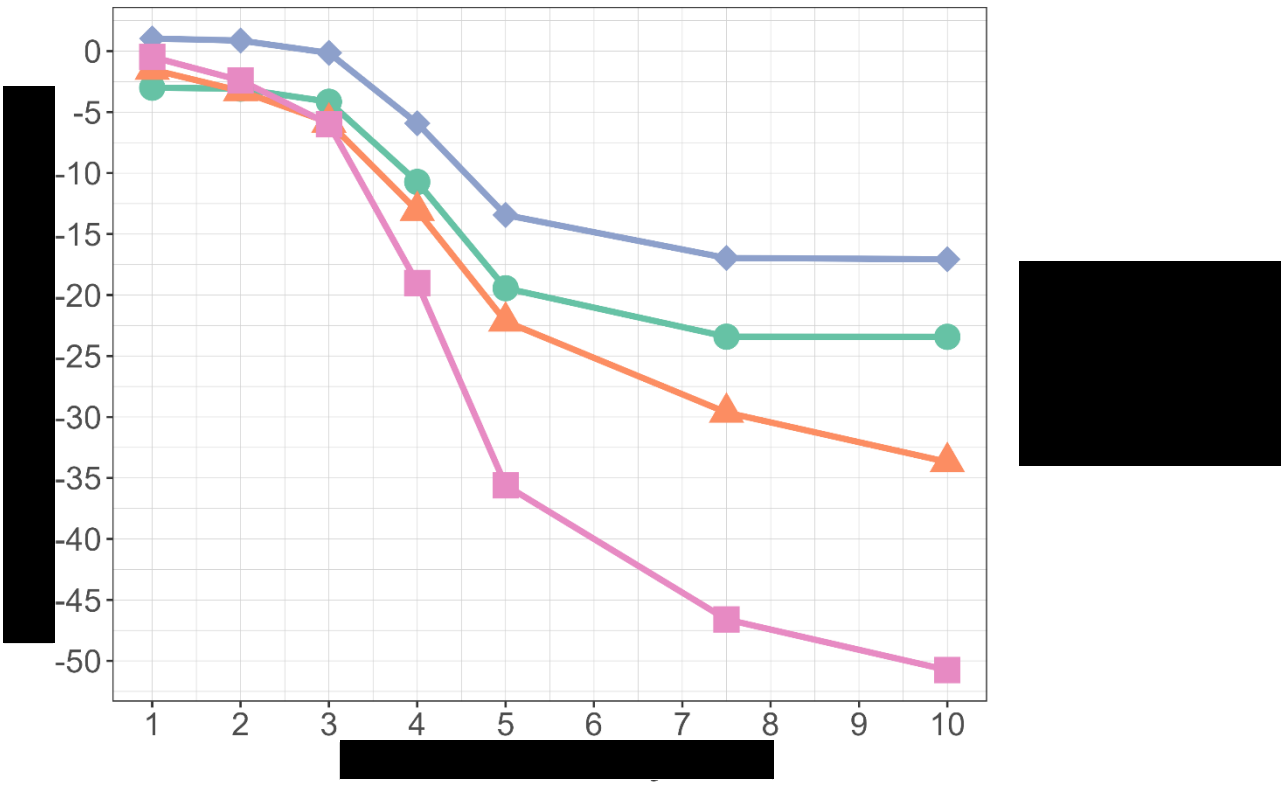
30. Next, we analyse the effect of TOTEX saving reductions at SPD. Figure 4 shows how cost allowances at ENWL, SPD, and SPMW would have been affected in RIIO-ED2 by a hypothetical X% TOTEX cost saving for SPD in each year from 2016 to 2028.

31. In RIIO-ED2, SPD is [✂] than ENWL and is not [✂]. In line with this observation (and as shown in Figure 4 for TOTEX savings of less than 3% at SPD) there is [✂] in the future cost allowances for ENWL, SPD, and SPMW.[71]

32. However, for TOTEX savings of 4% at SPD, the combined future cost allowances for ENWL, SPD, and SPMW [✂] by £[✂] over 2024-2028. For a 7.5% TOTEX saving, this figure [✂] to £[✂]. These substantial [✂] in cost allowance indicate that SPD directly affects the [✂] in the RIIO-ED2 price control for TOTEX savings in the range of 4% to 7.5%. For hypothetical 10% TOTEX savings at SPD, only [✂] additional [✂] in combined future cost allowances totalling £[✂] over 2024–2028 result.

[71] SPMW has a [✂] cost allowance increase. This is likely to be the result the [✂] changes in the top-down regression model's projections.

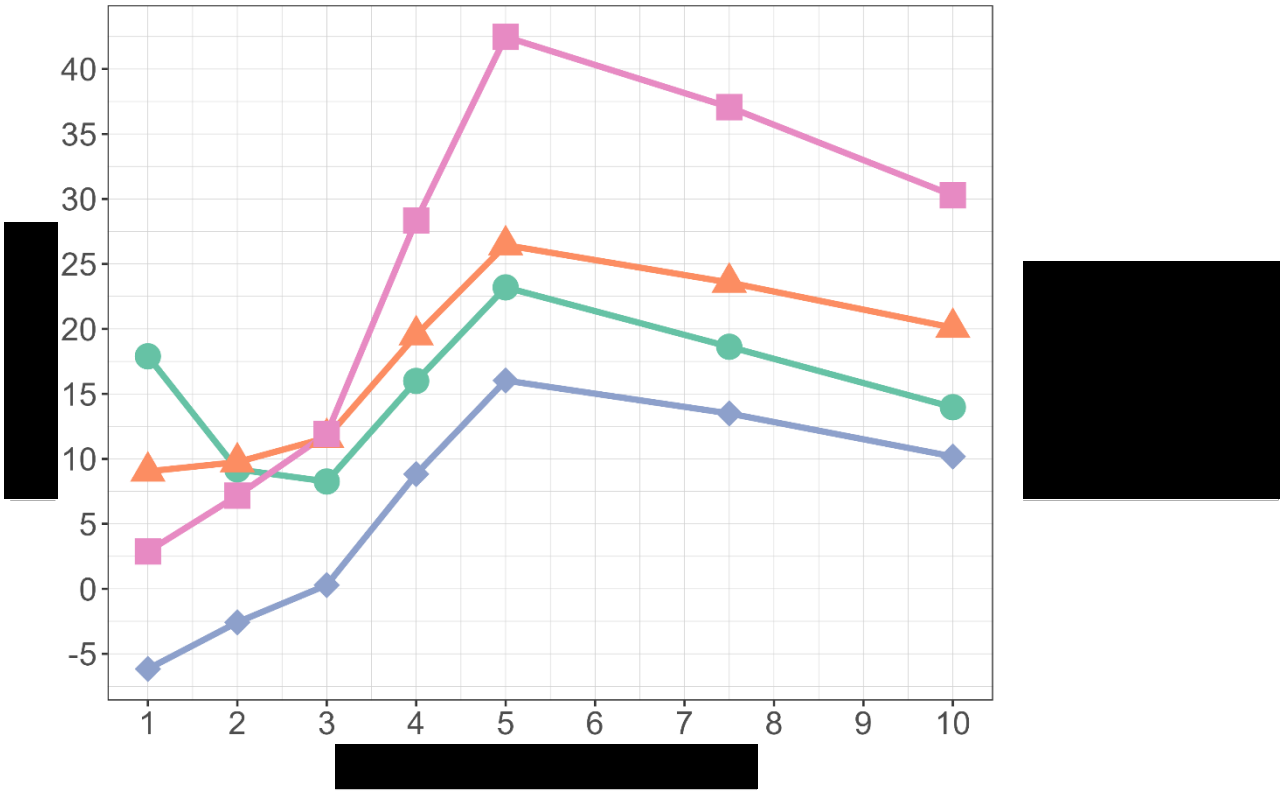
Figure 4 [redacted]



33. Focussing the analysis of pseudo DR on the region where SPD's TOTEX saving directly affects the cost benchmark, Figure 5 shows the combined pseudo DR for ENWL, SPD, and SPMW is at least [✂]%. The incremental pseudo DR from ENWL is at least [✂] – around [✂] the Merged Entity's own internal pseudo DR.

34. Combined, this analysis suggests that the Merged Entity has [✂] to invest in [✂] TOTEX projects at SPD and has some potential to [✂] for [✂] and [✂] TOTEX savings at SPD.

Figure 5 [redacted]



[redacted]

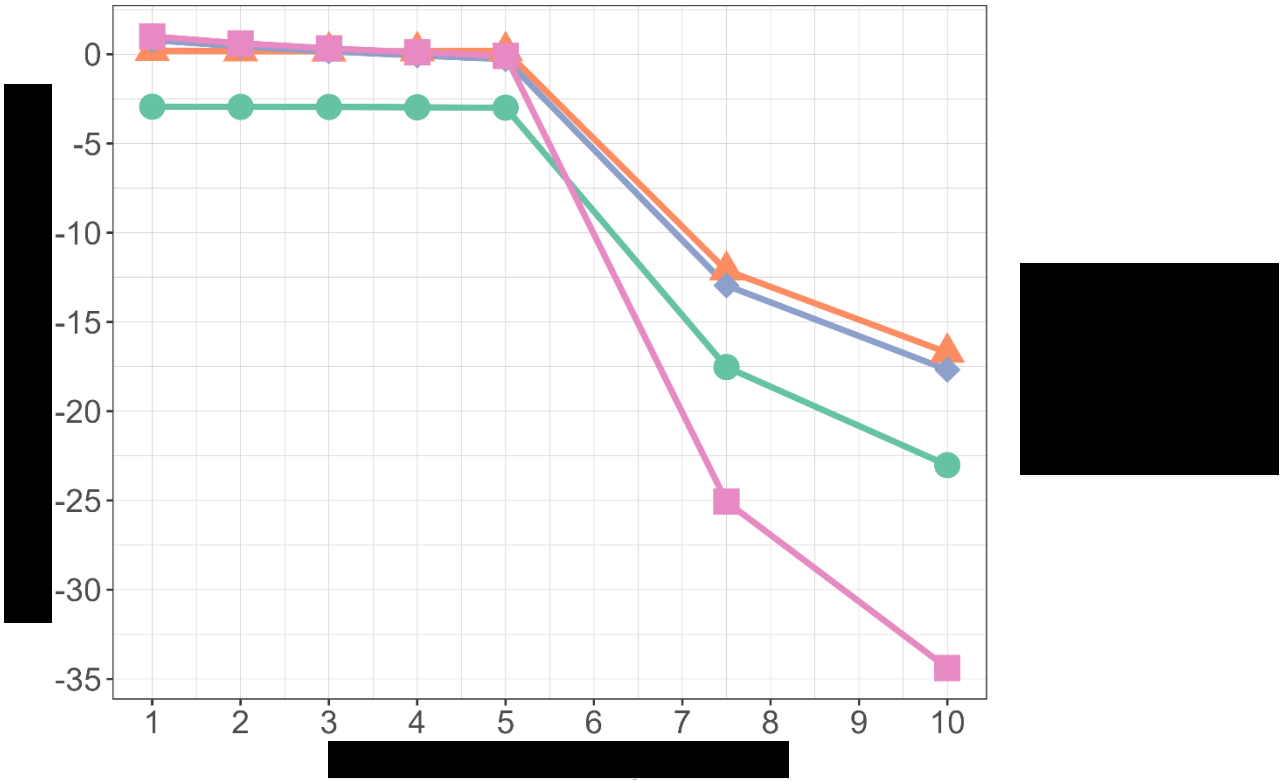
SPMW

35. Figure 6 below shows how cost allowances at ENWL, SPD, and SPMW would have been affected in RIIO-ED2 by a hypothetical X% TOTEX cost saving for SPMW in each year from 2016 to 2028.

36. Reflecting the relative [✂] of SPMW, for TOTEX savings of 1% to 5%, the future cost allowance change is relatively [✂] for ENWL, SPD and SPMW.[72] However, for TOTEX savings of 7.5% and 10%, the combined cost allowance reductions for ENWL, SPD, and SPMW [✂] over 2024 to 2028, at £[✂] and £[✂], respectively. These [✂] in the combined future cost allowance show that for [✂] TOTEX savings SPMW directly affects the efficient benchmark in the RIIO-ED2 price control.

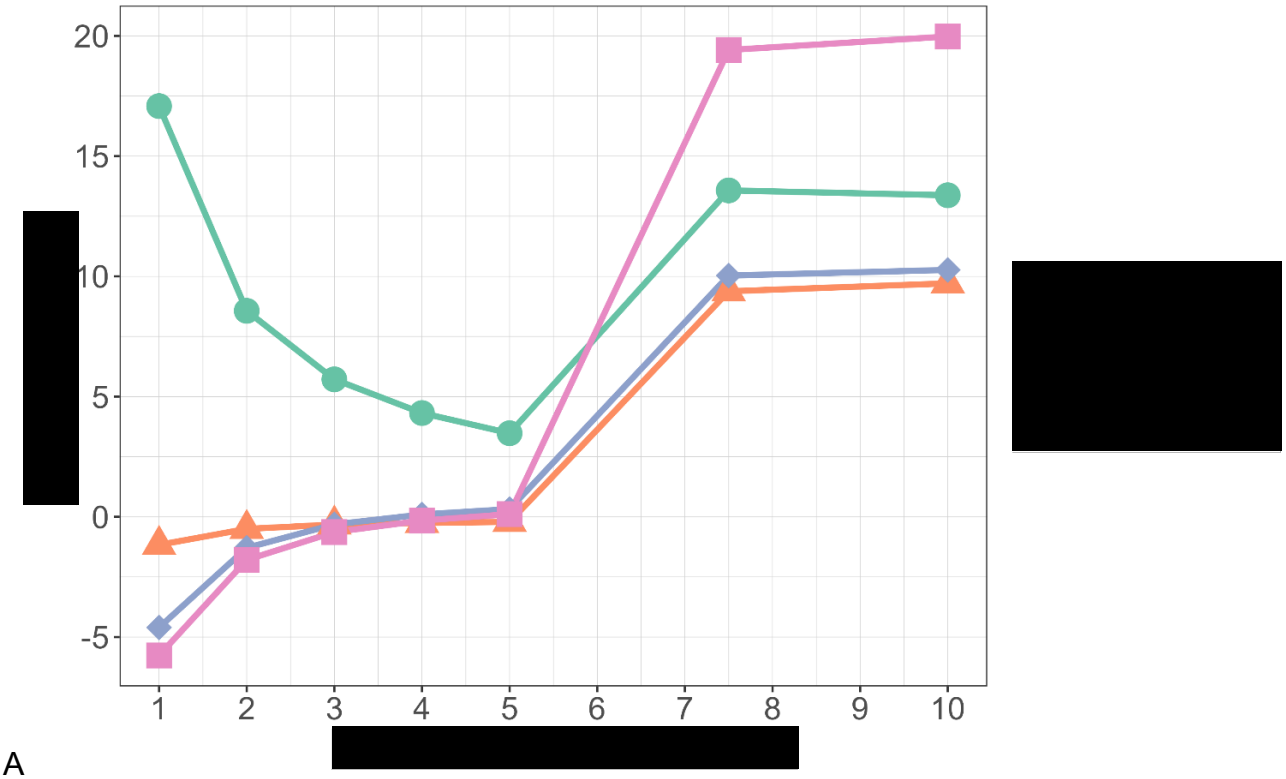
[72] Each of the Parties' DNOs experiences a [✂] of less than £[✂] or an [✂] of less than £[✂] for each TOTEX saving between 1% and 5% over 2024–2028. As was the case for SPD, the reason SPD and SPMW cost allowances [✂] following a TOTEX saving is likely to be caused by noise from the top-down regression modelling predictions.

Figure 6 [redacted]



37. Figure 7 shows, for SPMW's hypothetical TOTEX savings of 7.5% or more, the combined pseudo DR for ENWL, SPD, and SPMW [✂] to [✂]%. The incremental pseudo DR from ENWL is at least [✂] - this is approximately [✂] of the Merged Entity's own internal pseudo DR.

Figure 7 [redacted]



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38. Taken together, this analysis suggests that the Merged Entity has [✂] in incentive to invest in [✂] to [✂] TOTEX projects. However, the Merger may [✂] incentives for the Merged Entity to implement [✂] TOTEX savings at SPMW.

Conclusion

39. The empirical analysis suggests that the Merged Entity is likely to have [✂] incentives to invest in TOTEX savings at ENWL. In large part, this is can attributed to the fact that the Merger brings together Iberdrola's two DNOs, SPD and SPMW, with ENWL – a DNO [✂] to the threshold setting the efficient cost benchmark in RIIO-ED2.

40. We also find that the Merger may affect [✂] incentives at SPD and SPMW for [✂] TOTEX saving projects. This is because [✂] TOTEX investments have no [✂] on cost allowances through the cost benchmarking process.

41. We note that these findings rely on the use of RIIO-ED2's cost benchmarking as a model of future pseudo-competition through yardstick regulation. As such, it does not account for uncertainties over future costs and technological changes. Nor does it consider the potential for investment cost synergies.

ENDNOTE

[i] This sentence should be read as 'Iberdrola is active in the UK electricity sector through its ownership of ScottishPower group (SP) and, in turn, SP Energy Networks group (SPEN).'

[ii] This sentence should be read as 'The turnover of Iberdrola in 2023 was approximately £42 billion worldwide and approximately £9 billion in the UK.'