NON CONFIDENTIAL VERSION

IN THE COMPETITION APPEAL TRIBUNAL

Case No. 1046/2/4/04

Case No. 1034/2/4/04 (IR)

BETWEEN:

ALBION WATER LIMITED

Appellant

and

WATER SERVICES REGULATION AUTHORITY

(formerly THE DIRECTOR GENERAL OF WATER SERVICES)

Respondent

and

(1) DŴR CYMRU CYFYNGEDIG

(2) UNITED UTILITIES WATER PLC

Interveners

SKELETON ARGUMENT OF THE AUTHORITY FOR THE HEARING ON 13 FEBRUARY 2009

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1. The Water Services Regulation Authority ("the Authority") sets out below its submissions on the various matters raised by the applications of Albion Water Limited ("Albion") and Dŵr Cymru Cyfyngedig ("Dŵr Cymru"), both dated 24 November 2008.

Remedy in relation to unfair pricing

2. In the light of the Tribunal's judgment of 7 November 2008, Albion is entitled to declaratory relief to the effect that Dŵr Cymru has abused its dominant position within the meaning of the Chapter II prohibition by quoting a First Access Price which was both excessive and unfair in itself.

3. As to the setting of a common carriage access price, the Authority considers that a prospective price which is agreed by negotiation between the parties (and if necessary, mediation) is by far the preferable solution. Given the volume of detailed costing information which has been produced during the course of the proceedings, as well as the clear findings of the Tribunal in its judgment of 7 November 2008, it should be possible for Dŵr Cymru and Albion to reach a relatively swift settlement.

4. The Authority welcomes the steps already taken by the parties in order to agree a price. Indeed it is understood that a price has in principle been agreed at around [ ]p. The outstanding issue appears to be indexing of the price for the future. The Authority submits that the appropriate way forward is for this issue to be addressed by way of agreement, failing which the Tribunal can determine the matter.

5. The parties do not appear yet to have reached agreement in relation to services which are additional to the common carriage services. So far as a potable back-up supply is concerned, the price for that service is being determined by the Authority in the course of its current *potable* section 40 Water Industry Act 1991

(WIA91) determination. In its judgment of 7 November 2008, the Tribunal found that the back-up supply was not a relevant cost for its assessment of the legality of the First Access Price (paragraph 188). Accordingly, there is no need for the Tribunal to determine the quantum of the cost of the back-up supply in these proceedings.

Margin squeeze

6. No declaration is necessary in respect of Dŵr Cymru's breach of the Chapter II prohibition by imposing a margin squeeze: the Tribunal has already declared that the abuse took place (see judgment of 18 December 2006, at paragraph 360(iv)).

7. Moreover, given that the Authority has suggested a way forward in relation to the access price, the setting of such a price, with an appropriate mechanism for indexation, will in practice address any issues of margin squeeze. No additional order in relation to margin squeeze is therefore needed.

8. In any event this case does not lend itself to an order such as that in *Genzyme*, where a specific level of margin was set by the Tribunal. This is because the Tribunal has made no findings as to the minimum margin needed in order to provide a profitable retail service (see the judgment of 18 December 2006, at paragraphs 282 to 313). The necessary margin depends on whether, on the basis of properly allocated costs, Dŵr Cymru's own retail activities could make a normal profit in the downstream market at the particular margin in question, for the supply in question. This is not a matter which it would be appropriate to reopen for further determination: as the Tribunal noted, the parties were "*amply*

heard on the issue of margin squeeze, not least during the 6 day hearing in May/June 2006" and the Tribunal did "*not consider that there are any further factual investigations which are necessary*" before reaching its decision on margin squeeze (paragraph 284).

Interim relief

9. The Tribunal's interim relief order of 20 November 2006, reducing Dŵr Cymru's existing Bulk Supply Price to Albion by 3.55 p/m^3, was continued until further order by the Tribunal's judgment of 18 December 2006 (paragraph 360(v)). The Tribunal considered those measures "*necessary to protect Albion's position pending the outcome of the Authority's further investigation, and the ultimate determination of this appeal*": see the Tribunal's decision refusing permission to appeal, of 2 February 2007. Those measures will no longer be necessary once the common carriage price has been set, either by consent of the parties or by further order of the Tribunal. The Authority therefore proposes that the order remain in place until the common carriage price has been either agreed or set by the Tribunal, at which point the interim relief order can cease and Case No. 1034/2/4/04 (IR) be brought to a close, along with Case No. 1046/2/4/04.

Bulk Non-Potable Supply Agreement

10. In the draft order Albion seeks a remedy both in respect of common carriage and in respect of bulk supply services. This case, however, concerns common carriage not bulk supply. Once a common carriage price has been set as above, the need

for any bulk supply price falls away. A common carriage price will provide Albion with a final remedy in respect of its complaint.

11. In any event the Tribunal does not have jurisdiction to determine a bulk supply price in the manner proposed by Albion in its draft order (paragraph 3 of the draft attached to Albion's letter of 24 November 2008). The issue of the price for the bulk supply of non-potable water was not the subject of Case No. 1046/2/4/04, which concerned the First Access Price.

12. At this stage it is by no means clear that it will be necessary to resolve the issue of a future bulk supply price for non-potable water in this case. Once a common carriage price has been set, the dispute has been resolved. It is premature at this stage to seek to address the hypothetical situation of any change in Albion's plans such as might require any future determination of a bulk supply price. In that event it would be necessary to consider Albion's proposals, including its desire to extend its services to include the neighbouring Corus plant, to determine the best way forward. Were the Authority called upon to consider any such plans, if the parties could not agree terms and conditions such as price, it would address the situation then arising. Of course any determination under section 40 WIA91 would require the Authority to have appropriate regard to the findings of the Tribunal and its statutory duties, and it may not involve a simple read across from this case to any new proposals advanced by Albion. But at this stage these issues do not arise.

Costs

13. The Authority agrees that Albion's reasonable legal costs should be borne by the Authority and Dŵr Cymru, with the proportions to be set by the Tribunal if not agreed and the costs to be subject to detailed assessment if not agreed.

3 February 2009