

***Case No COMP/M.3306 -
E.ON / MIDLANDS***

Only the English text is available and authentic.

**REGULATION (EEC) No 4064/89
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 16/12/2003

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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 16/12/2003

SG (2003) D/233515

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PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the notifying party via their legal representative

Dear Sir/Madam,

**Subject: Case No COMP/M.3306 - E.ON/MIDLANDS
Notification of 17.11.2003 pursuant to Article 4 of Council Regulation
No 4064/89¹**

1. On 17.11.2003, the Commission received a notification of a proposed concentration by which the German undertaking E.ON AG ("E.ON") acquires within the meaning of Article 3(1)(b) of the Council Regulation control of the whole of the UK undertaking Midlands Electricity plc. ("Midlands").
2. After examining the notification, the Commission has concluded that the notified operation falls within the scope of the Merger Regulation and that it does not raise serious doubts as to its compatibility with the common market.

I. THE PARTIES

3. E.ON is an integrated energy services provider, whose activities are based in Germany, Sweden, the UK, the US and throughout central and Eastern Europe. Its main business is the generation, transmission, distribution and supply of electricity and the transportation, distribution and supply of gas (notably through Ruhrgas). E. ON also has interests in water, chemicals, the provision of telecommunications services and real

¹ OJ L 395, 30.12.1989 p. 1; corrigendum OJ L 257 of 21.9.1990, p. 13; Regulation as last amended by Regulation (EC) No 1310/97 (OJ L 180, 9. 7. 1997, p. 1, corrigendum OJ L 40, 13.2.1998, p. 17).

estate management. Its main activities in the UK are the generation, distribution and supply of electricity [and gas through Powergen and its subsidiaries].

4. Midlands is ultimately economically owned by Aquila Inc. and First Energy Corp. Its primary business is as an electricity Distribution Network Operator (DNO) serving 2.4 million network customers in the West Midlands area of the UK through its subsidiary Aquila Networks plc. It also operates metering services and contracting activities and has some small gas supply and shipping activities. Midlands has no interest in the supply of electricity. Midlands has an non-controlling equity interest in Teeside Power Station in the North of England, as well as equity interests in power generation plants in Turkey and Pakistan.

II. THE OPERATION

5. Aquila Inc. (through its subsidiary Aquila Europe Inc.) and First Energy Corp. own Aquila Sterling Holdings which, through Aquila Sterling Ltd. (“ASL”), ultimately owns 100% of Midlands.
6. The operation consists of the acquisition by E.ON through its subsidiary Powergen of the entire issued capital of ASL, thus acquiring sole control of Midlands. The transaction therefore constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

III. COMMUNITY DIMENSION

7. The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 billion (E.ON: EUR 37 billion, and Midlands: EUR 621 million). Each of E.ON and Midlands have a Community-wide turnover in excess of EUR 250 million (E.ON: EUR [...] billion and Midlands: EUR [...] million),² E.ON and Midlands do not achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension pursuant to Article 1 (2) of the Merger Regulation.

IV. COMPETITIVE ASSESSMENT

A. Relevant product markets

Electricity

8. The notifying party submits that there are four relevant product markets within the electricity sector: generation, transmission, distribution and supply of electricity, which is in line with previous decisions³ of the Commission. In relation to these product markets, both parties are only active in the market for the distribution of electricity.

² Turnover calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Notice on the calculation of turnover (OJ C66, 2.3.1998, p25).

³ Case COMP/M.2890 – EDF/Seeboard, decision of 25 July 2002.

9. The parties also have negligible overlapping activities in relation to electrical contracting services in that Midlands provides electrical contracting services via its wholly owned subsidiary MEB (Contracting) Ltd. Although Powergen sold its contracting business in 2000 it continues to provide, as required by the Distribution Licence, new un-metered connections and to repair existing connections. It is considered that the operation will not change the competitive situation in this market since Powergen's activities in this area are provided as part of its obligations under the licence and are not contestable.

Gas

10. The parties to the concentration have overlapping activities in the following areas: supply of gas, gas shipping and gas trading. Of these only the market for the supply of gas is affected by this transaction.
11. The notifying party submits that the supply of gas, which has been previously defined by the Commission⁴ as a separate relevant product market, could be further sub-divided into for segments: (i) the supply of gas to domestic customers, (ii) the supply of gas to small industrial customers (2,500 therms per annum to 25,000 therms per annum), (iii) the supply to large industrial customers (above 25,000 therms per annum) and (iv) the supply of interruptible gas. This sub-segmentation was considered in the case M. 3007 – E.ON/TXU, where the precise product market definition was left open. For the purposes of the present decision, the same approach can be taken since the final assessment does not change whichever definition is chosen.

B. Relevant geographic markets

Electricity

12. In previous decisions⁵ the Commission found that the relevant geographic market for the distribution of electricity coincided with the licensed distribution area for each regional electricity company. In this case, the relevant geographic markets are the East Midlands area of England and the Midlands area of England, where Powergen and Midlands respectively own, manage and operate their electricity distribution networks.

Gas

13. The parties submit that the relevant geographic market comprises the territory of Great Britain. In its decision in E.ON/TXU-E the Commission found that the geographic scope of the market for the supply of gas to domestic and industrial customers should be considered to encompass Great Britain. This is on the grounds that the vast majority of the population of Great Britain is served by the natural gas pipeline network operated by Transco; that there are no significant differences in the regulatory regime applying to England and Wales as compared to Scotland; and no differences in the number of

⁴ Cases COMP/M.2890 – EDF/Seeboard, decision of 25 July 2002, and COMP/M.3007 – E.ON/TXU, of 18 December 2002.

⁵ For example COMP /M.2890 – EDF/Seeboard *ibid*, Cases COMP/M.2675 - EDF/TXU Europe/West Burton Power Station and COMP/M.2679 – EDF/TXU Europe/24Seven, of 20.12.2001

supply companies competing in Scotland. This market definition is valid also for the purposes of the present decision.

C. Assessment

Electricity

14. With respect to the distribution of electricity, after the operation, E.ON will own two regional distribution networks in the UK, one at East Midlands which it already owns and Midlands. However each distribution network is considered to be a separate market on which the operator has a monopoly position. These networks are regulated by OFGEM the UK regulator. There is therefore no change to the competitive situation as a result of this transaction.

Gas

15. Two product markets are affected by this transaction: the market for the supply of gas to small industrial customers and the market for the supply of large industrial customers. In all the other markets, the operation gives rise either to small market shares due to horizontal overlaps or to no overlap at all: (i) supply of gas to domestic customers, no overlap since Midlands is not active in this segment; (ii) supply to interruptible customers, combined market share below [0-10]% (E.ON: [0-5]%; Midlands: [0-5]%;); (iii) gas shipping, combined market share [10-15]% (E.ON: [10-15]%; Midlands: [0-5]%;); and (iv) gas trading, combined market share below [5-10]% (E.ON: [0-5]%; Midlands: [0-5]%).

Horizontal effects

Small industrial customers

16. As mentioned above a separate market for the supply of gas to small industrial customers could be identified, with a demand between 2,500 therms per annum to 25,000 therms per annum. On this market the parties' combined market share⁶ would be between [25-30], (E.ON [20-30]%, Midlands [0-5]%) the increment to this share resulting from the merger being less than 2%. The parties face competition from a number of strong competitors such as British Gas which has a market share of [20-25]% as well as from Shell Gas Direct [15-20]%, TotalFinaElf [10-15]% and Innogy [5-10]%, as well as a number of smaller competitors. Given the insignificance of the increment to E.ON's market share and the existence of strong competitors it can be concluded that the transaction does not give rise to any significant competition concerns in this market.

Large industrial customers

17. On the product market for the supply of large industrial customers with a demand above 25,000 therms, the parties would be the second largest player with a [15-20]% combined market share (E.ON/Powergen [15-20]% and Midlands [0-5]%). The increment to this share resulting from the present transaction is estimated to be less than [0-5]%. The new entity would face competition from TotalFinaElf Gas ([20-30]%),

⁶ All market share figures are for the year to August 2003.

Shell Gas Direct ([10-15]%), British Gas ([10-15]%), Gaz de France ([10-15]%) and a number of smaller competitors. Given the insignificance of the increment to E.ON's market share and the existence of strong competitors it can be concluded that the transaction does not give rise to any competition concerns in this market.

Vertical effects

18. As regards gas production, only E.ON, through Ruhrgas, has any interest in gas production by way of equity stakes in certain gas fields. The notifying party estimates that Ruhrgas produced in total [0-5]% of the natural gas produced in the UK in 2002. Midlands does not have any gas production interests. At present Ruhrgas does not provide Powergen with any gas.
19. As regards gas distribution E.ON, again through Ruhrgas, has a [0-5]% stake in the SEAL pipeline that transports gas from North Sea gas fields. Powergen Gas Ltd. also transports and delivers gas from the Theddlethorpe beach terminal to a number of directly connected sites, including two power stations. Midlands does not have any interests in gas pipelines.
20. Midlands is not vertically integrated in relation to gas and has only very limited gas supply interests, and there are a number of large, vertically integrated competitors operating in the UK such as British Gas, Shell, BP, and Total Fina Elf. It can be concluded therefore that this transaction will not significantly affect or give rise to concerns as to the level of vertical integration in the sector.
21. It can therefore be concluded that the concentration does not give rise to serious doubts as to the creation or strengthening of a dominant position as the result of which competition would be significantly impeded in the common market or in a substantial part of it.

V. CONCLUSION

22. For the above reasons, the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement.

This decision is adopted in application of Article 6(1)(b) of Council Regulation (EEC) No 4064/89.

For the Commission, signed,
Mario MONTI
Member of the Commission