Water UK

A Brief Guide to Competition Law Compliance

June 2017

WATER UK

A BRIEF GUIDE TO COMPETITION LAW COMPLIANCE

1. Introduction

Who is this guide aimed at?

1.1 This guide is intended to provide guidance on complying with competition law for the benefit of

- Water UK staff and
- Staff of Water UK member companies working with other members on subjects with which Water UK is involved, by facilitating or participating in meetings, providing technical or logistical support or in any other way.

1.2 The guide does not therefore address activities which Water UK members engage in outside the Water UK context.

What does this guide deal with?

1.3 In the UK and EU there is a range of laws intended to prevent anti-competitive conduct by businesses. In broad terms, these laws fall into three categories, namely:-

- Merger control
- Prohibition of the abuse of a dominant (or monopoly) position
- Prohibition of anti-competitive agreements and arrangements.

Water UK has no role to play in mergers and acquisitions and the prohibition of abuse of a dominant position largely affects activities by single companies. This guide, therefore, concentrates on the third of these categories. Annex 1 contains further information about the underlying legislation.

1.4 There are very serious consequences for breach of competition law including:-

- Fines on companies of up to 10% of annual worldwide turnover

- Damage to reputation
- Invalidity of agreements
- Exposure to third party claims for damages
- Costly and lengthy investigations by the competition authorities (in the UK water sector, these are the Competition and Markets Authority (CMA) and, under so-called concurrent powers, Ofwat).

In addition, individuals can be subject to prosecution and be fined or even imprisoned for seriously anti-competitive activities such as fixing prices with competitors or rigging bidding processes for goods or services.

Our exit from the EU is unlikely to make any significant difference to the obligations imposed on water companies to abide by competition law.

2. Some basic principles

The law is very broadly expressed

2.1 In the context of Water UK activities, it is important to be aware that the law targets not only formal, written agreements but also informal understandings and so-called "gentlemen's agreements".

Beyond that, the courts have held that any activity "which knowingly substitutes practical co-operation between [companies] for the risks of competition" is prohibited. Where competitors meet and afterwards implement a change in their competitive stance, the law may presume that this is as a result of an understanding between them. For example, if after one or more industry meetings, companies were seen to be boycotting a particular contractor or to be imposing identical charges for a non-regulated service, the risk is that the competition authorities would suspect that this was a result of an unlawful understanding between them.

In such cases, the companies need to be able to displace the suspicion. Given how often competitors meet under the auspices of Water UK, the risks both to companies and to Water UK as a potential participant/facilitator are clear. Ways of reducing these risks are described later in section 4 of this Guide on conduct of meetings.

There is a hierarchy of infringements

2.2 The most serious types of infringement are agreements, understandings or other broader arrangements which are aimed at:-

- Agreeing prices or charges; this can refer to an agreement on the price at which goods or services are to be sold or to an agreement between companies as to the prices at which they will buy goods or services, eg, from a prospective supplier of water
- Dividing up customers (eg, in relation to the business retail segment, if adjoining companies were to agree not to target customers in each other's area)
- Excluding third parties from the market (eg working with others to undercut competitors in competitive markets such as private drains clearance)

For such agreements, the most serious sanctions allowed by the law are likely to be imposed.

2.3 An important subject in the context of any trade association is the extent to which information exchanges may occur. Such exchanges can themselves restrict competition and may be the subject of enforcement action even if there is no other evidence of a more specific anti-competitive arrangement having been entered into. This subject is dealt with in further detail below.

2.4 For other forms of collaboration between competitors, the approach of the law is less black and white. For example, where two competitors collaborate on the development of a joint venture business, eg, in the non-household retail market, the cooperation will lead to joint activities which might otherwise have been conducted separately by the companies in competition with each other. Collaboration like this may also act to exclude third parties from the market.

On the other hand, there may well be economic justification for the collaboration, such as that it will reduce costs to customers or permit technical developments that would not otherwise have taken place. Where relevant justification can be demonstrated, competition law allows it to be balanced against any potential harm to competition. However, it is extremely unlikely that these criteria could ever be used

to validate serious infringements of the competition law prohibitions of the type described in paragraph 2.2.

Effects on competition that need to be considered

2.5 Whether any particular conduct might affect competition needs to be thought about both in terms of competition between the parties who are entering the agreement, arrangement or understanding and in terms of the effect on third parties. In the case of the water sector, third parties might include customers, suppliers, self-lay operators, New Appointments and Variations (NAVs) or holders of water supply or sewerage licences under the Water Act 2014 (WA2014).

Impact of water legislation

2.6 For many years there was only been limited scope for competition because the Water Industry Act did not in practice enable more extensive competition to emerge. In such circumstances, companies could legitimately consider that competition law had only a limited impact on their activities.

However, the position has changed as more competition has been introduced into water markets.

In the market for the supply of water mains, there is competition from SLPs, in the "wholesale" supply market there is competition from NAVs while the business retail market is wholly competitive.

It may be that competition will be extended further into core "upstream" markets at some future stage.

There is therefore an increasing need for companies to recognise that their arrangements may affect actual or potential competition across a much broader spectrum of activity, and to take appropriate steps to avoid competition law infringements.

Secrecy can never be guaranteed

2.7 An agreement which is unlawful will be so whether or not it is kept secret and there is in fact a high probability of secret agreements becoming public, sooner or later. Not only do parties sometimes have commercial reasons for revealing supposedly secret activities to the authorities but both the EU Commission and the UK authorities have

extensive powers to have information disclosed, and encourage applications for leniency from parties involved in cartels. Frequently, they act on information provided by “whistle blowers”. These investigatory powers are backed up by powers to conduct “dawn raids” and to interview relevant personnel.

Further advice

Further advice on the topics outlined in this note is available either from David Strang, the Water UK Legal Adviser (dstrang@water.org.uk, tel: 020 7344 1804) or from individual companies' legal and compliance teams.

3 Participation in Water UK activities

3.1 Introduction

Water UK conducts a wide range of activities, from debates on questions of broad policy questions to detailed work on technical standards. Looking across the range of these activities, most raise no potential competition law problems.

Even if companies were to align themselves completely behind a particular policy, in most cases this will have no discernible effect on competition between companies. Items such as the 21st Century Drainage project, work on consistency of performance measures or dealing more effectively with vulnerable customers fall into this category.

In many cases, the work is undertaken to enable better regulation and any impact it might have on customers is dependent on the approach of the regulator. In other cases, the work affects companies' monopoly businesses where there is no competition between companies and is well removed from the day to day commercial operations of the companies. In such cases, it can be seen to be too remote from "the market" to have any effect on competition.

A similar conclusion holds for a wide range of technical discussions between members where the outcome, while important to individual companies, does not have a material impact on costs or have any material effect on customers. Examples in this category could include exchanges of experience on meter box location and VAT treatment of particular supplies made by companies.

In between these two extremes lies a range of activities which could affect companies' competitive behaviour. This note concentrates on these activities.

3.2 Principles concerning information exchange

Principle

It is essential to avoid the exchange of information which could affect competitive behaviour. Anything which could reasonably be regarded as commercially sensitive should not therefore be discussed with competitors.

Many activities within Water UK involve the exchange of information between companies. While much of this is innocuous, it is important to be aware that even where there is no evidence of any other agreement or understanding, an exchange of information of a commercially sensitive nature that may affect the competitive behaviour of the recipient of the information is itself likely to be prohibited.

Even a unilateral disclosure of commercially sensitive information can expose the recipient to risk under competition law. The competition authorities are able to assume that the information has been acted on by the recipient unless the recipient has publicly distanced itself from the information.

Information about current and future prices, costs or commercial strategy is almost always considered commercially sensitive for these purposes. Examples could include target customers, proposed charging strategies and target sales territories in the business retail market; prices paid to suppliers, rates paid to contractors, proposals as to the sums to be charged to developers for new mains; and proposed pay rises for employees.

The extent of this risk should not be underestimated and in a recent case (Dole Foods, 2015) the European Court of Justice made the following comments:

"While it is correct to say that this requirement of independence [*of companies on the market*] does not deprive economic operators of the right to adapt themselves intelligently to the existing or anticipated conduct of their competitors, it does, none the less, *strictly preclude any direct or indirect contact between such operators by which an undertaking may influence the conduct on the market of its actual or potential competitors or disclose to them its decisions or intentions concerning its own conduct on the market* [our emphasis] where the object or effect of such contact is to create conditions of competition which do not correspond to the normal conditions of the market in question, regard being had

to the nature of the products or services offered, the size and number of the undertakings involved and the volume of that market"

To the extent that information is in the public domain, eg, in published tariff lists or business plans, there can be no objection to its being shared but there should be no discussion of such information before the time it is made public.

These rules do not prevent the exchange of aggregated anonymised data from which the identity of the individual parties cannot be ascertained. So, benchmarking schemes run by third parties or data gathering exercises run by external firms are likely to be permissible, especially in regard to less current data. Legal advice should always be obtained before entering into such an arrangement in order to ensure adequate anonymisation of the data.

3.3 Lobbying

Principle

Subject to compliance with the rules prohibiting the exchange of commercially sensitive information, lobbying and influencing activities through Water UK will not normally raise any competition law concerns.

Lobbying before a law or regulation is passed

It is open for some or all companies to adopt a common position towards the adoption and/or content of proposed laws or regulations as, subject to there being no prohibited information exchanges or agreements, the companies in question are merely making their views known to a third party. The third party, eg the Government or the regulator, is free to adopt or reject those views.

There is no reason for such lobbying activity to affect the competitive dynamic between companies either before or after the new law or regulation is adopted.

The critical point is that regardless of the companies' activities, the final decision is in the hands of a third party and the way in which companies will react once that decision has been taken is up to each of them individually.

The sector might for example have lobbied against the creation of a business retail market. Even though this might have been perceived as being self-interested, the important point is that the companies' activities could not affect the market-only the decision of the government/regulator could have that effect.

Once the decision has been taken by government/Ofwat to proceed in a particular policy direction, companies may no longer be free to coordinate their positions on the policy. At that point, coordination could indeed affect behaviour on the market.

3.3 Reviewing and analysing legislation applicable to the sector

Principle

Exchanges of views and opinions about the meaning of prospective and actual legislation and how it might affect the sector are permissible. In any such discussions, companies must avoid revealing their own commercial positions.

Trade body review of prospective legislation: permitted activities

Water UK frequently finds itself establishing groups to analyse and report on the application of prospective or existing legislation.

An example is provided by retail exit. There would have been nothing preventing companies from meeting in a Water UK context to discuss the pros and cons of retail exit. This might have involved considering the impact on customers, whether incumbents' duties would transfer to the acquirer of the business and how, if at all, the system of default tariffs for business customers would protect transferred customers.

Trade body review of prospective legislation: prohibited activities

In contrast, it would not have been acceptable for companies to indicate whether they would be buyers or sellers, should retail exit be permitted (even if commercially, this is something most companies would be unlikely to wish to reveal). Nor would it have been acceptable for companies to indicate the price or terms on which they might be willing to transfer their business customers. All such exchanges of information could materially affect the market for control of books of business customers being offered for sale.

Equally, any indication of the basis on which companies would offer to supply business customers would be prohibited, as it could materially affect the competitive interaction between companies in the newly liberalised market.

After a law or regulation is passed: permitted activities

The same principles apply after the law or regulation is passed and the question remains whether activity carried on by or within Water UK may affect competition.

This can be considered by reference to another Water UK activity, namely, developing an industry position towards the implementation of the provisions of the Water Act 2014 on developer charges. A group of representatives from across the industry has been considering those provisions and the subsequent Ofwat charging rules in order to give guidance to the industry as to how the new rules might be introduced.

The group could lawfully consider items such as

- the range of options for implementing the broad framework provided for by the Ofwat rules;
- a common understanding of the meaning of the new rules;
- whether one method of implementation might be simpler/better than another; and
- whether implementation might give rise to legal problems due to a failure to deal equitably with NAVs.

After a law or regulation is passed: prohibited activities

On the other hand, companies would need to take decisions independently about how to implement the new charging regime and would not be able to exchange information in advance of publication about the charges that they might levy for particular developer services activities.

Summary

The dividing line is between discussions about how the market might operate in general and how individual companies might compete in that market. Care should be taken to avoid the risk that discussions on how the market might operate reveal the stance of individual companies towards that market. This could occur if companies used situations which were, theoretically, hypothetical to signal what their competitive stance was likely to be and/or how they might react to what others are doing in the market.

Technical topics

Many activities undertaken by Water UK's networks raise no difficulty, for example where they involve the exchange of technical information or of individual companies' experiences of practical problems. A useful test is to ask whether it would be normal for companies in fully competitive sectors to exchange the information in question.

Exchange of information about individual companies' policies on matters such as laying pipes in contaminated ground or placement of meter boxes is not likely to have a material effect on the companies' costs or on competition between them, provided that this does not involve sharing information about terms of supply or other commercially sensitive matters.

Technical information can however sometimes give an insight into material areas of costs and if this seems possible, advice should be taken before the information is exchanged. Information on, for example, the length of mains laid by a company and its costs of so doing would allow average cost information to be produced. Such detailed cost information is not something that companies should be exchanging, other than through an appropriate benchmarking process (see above).

3.5 Standard Setting

Principle

Standard setting can have anti-competitive effects where standards are established in a way which excludes competing or potentially competing technologies or approaches. This note applies to standard setting which is not under the auspices of groups such as CEN or ISO. These bodies have their own compliance policies.

In general, the law considers standards activities to be benign provided that certain safeguards are adopted.

The group establishing the standards should have a policy that ensures that all parties with an interest in the standard can make their views known. This applies to companies other than members of Water UK who could, for example, be invited to sit on relevant groups as observers. It may be prudent to formalise the rules of the group considering the standard and to make these public.

The same approach applies to groups establishing standard form agreements for use across the industry.

It will not always be essential for all potential interested parties to be part of the process at all stages but robust consultation procedures will need to be considered to avoid accusations that a “club” of Water UK members has adopted standards which might harm the interests of non-members.

For example, the current work to revise Sewers for Adoption to take account of SuDS has been entrusted to a third party, WRc, and mechanisms have been established to consider the views of a broad range of stakeholders. It will be for companies to decide whether or not they wish to implement the standards that emerge from the process.

Even if some parties choose not to participate or are overruled by the majority of the group establishing the standard, this need not affect the validity of the standard adopted. However, requiring compliance with only one standard and refusing to admit the validity of alternative

standards offering equivalent protection is likely to be problematic and needs further analysis.

In relation to standard form agreements prepared on an industry-wide basis, these can only ever be models which individual companies can choose to follow or not, depending on their individual policies. It will not be possible to require any company only to use the model form although use of models to improve efficiency can be encouraged.

4 Conduct of Meetings

Principle

In any trade association, a proper approach to the conduct of meetings is essential, both to guard against anti-competitive activity taking place and to allay any suspicion that such activity might have taken place.

Recommendations

Those chairing meetings need to understand the areas of discussion to be avoided and should intervene to stop any such discussions.

Meetings should have agendas and minutes, and discussions outside the agenda should be especially carefully monitored by the chair of the meeting.

There is no absolute prohibition on generic agenda items such as “any other business” as the key issue is what actually happens at the meeting rather than the nature of the formal agenda.

Where there are such open-ended agenda items, the safe way to proceed is to minute each item discussed under that heading, so providing evidence of compliance.

As the sector moves towards the introduction of greater competition, there is an increased need to consider whether meetings of the PAGs, Board and Council should be attended by the Water UK legal adviser. Good governance suggests that this should be the norm for Board and Council meetings, given the seniority of those attending. For PAGs, this will depend on the topics under discussion.

Given the technical nature of many discussions within Task and Finish Groups, it is unlikely to be appropriate for a legal adviser to be regularly in attendance although the principles outlined in this guidance apply equally to such groups' activities.

The presence of a legal adviser where appropriate to the topics under discussion, together with a practice across the organisation of taking proper minutes, will help not only to ensure that discussions remain within appropriate limits but also to give assurance to external parties including Ofwat that correct procedures are being followed and inappropriate discussions avoided.

Depending on the nature of the meeting, it is sensible for reminders about competition law compliance to be given on a regular basis such as once a year. A statement which can be used for these purposes is set out in Annex 2.

These rules apply equally to email networks. Network chairs need to monitor network traffic to ensure that the network is not used for illicit exchanges of information or other anti-competitive activity. Guidance on this topic is also included in Annex 2.

Annex 1

1 *The legislation*

1.1 The legislation aimed at preventing anti-competitive practices is as follows:-

(a) Articles 101 &102 of the Treaty on the Functioning of the European Union (TFEU);

(b) Chapters I & II of the Competition Act 1998; and

(c) Enterprise Act 2002

1.2 Although the UK prohibitions are modelled on the TFEU provisions, the TFEU is unlikely to be applicable to the UK water sector as EU law only applies where activity "may affect trade between member states [of the EU]".

2 ***The Chapter I Prohibition*** –

Chapter I of the Competition Act 1998 prohibits –

- agreements between undertakings (that is, businesses),
- decisions by associations of undertakings (in particular trade associations), and
- concerted practices (including parallel behaviour),

which –

- may affect trade within the United Kingdom,
- and have as their object or effect,
- the prevention, restriction or distortion of competition within the United Kingdom.

3 ***The Chapter II Prohibition*** –

Chapter II of the Competition Act 1998 prohibits conduct by one or more undertakings amounting to abuse of a dominant position if it may affect trade within the UK.

4 ***Guidance***

4.1 Because UK law in this area derives from EU law, useful guidance can also be found in the EU Commission's Horizontal Co-operation Guidelines (OJ 2011 C11/1)

<http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=OJ:C:2011:011:FULL&from=EN>

Annex 2: Guidance for Water UK meetings and networks

All participants in Water UK activities are responsible for ensuring that those activities are carried out in compliance with competition law.

Meeting chairs and those responsible for networks have an additional responsibility to guard against breaches of competition law and the following guidelines may be useful.

1 On a regular basis, and no less than once a year, a copy of this guidance document should be sent to all network members.

2 A statement of the need to comply with competition law, which should include a reference to this guidance document, should be given when any group is established and at yearly intervals. This applies to all groups which may be established using Water UK facilities or involving Water UK personnel.

3 As noted in this guidance, agendas and minutes should be kept for all meetings and express reference should be made to the competition law compliance statements in those documents. Consideration should be given in the light of topics arising on the agenda to ensuring that a legal adviser is on hand where appropriate.

4 Sample wording that a meeting chairman might use is as follows:

> "I would like to remind everyone of the need to comply with competition law. This means that we need to avoid any discussion within this meeting/network/group etc of any subject which involves commercially sensitive information. This could include information relating to prices, costs, customers and future business plans. It goes without saying that it is also not permitted for companies to enter into agreements fixing prices to be charged or paid for particular activities or dividing up customers between them. Further detail on these subjects can be found in the latest edition of the Water UK competition law guidance which I would ask everyone to familiarise themselves with. The guidance can be found on the Water UK website"

5 Where the chairman of a meeting or convenor of a network considers there is a risk of competition law being breached, it is his or her responsibility to end the meeting or network conversation and to make it clear why this is being done.