

Completed acquisition by RREEF Pan-European Infrastructure Fund LP of a minority interest in Kelda Holdings Limited

ME/4519/10

The OFT's decision on reference under section 32(b) of the Water Industry Act 1991 given on 21 June 2010. Full text of decision published on 30 June 2010.

Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

PARTIES

1. **RREEF Pan-European Infrastructure Fund LP** (RREEF Fund) is a limited partnership whose partners are institutional investors. RREEF Fund provides a means for these investors to invest in various European infrastructure assets. RREEF Fund is managed by RREEF Limited which is a wholly owned subsidiary of **Deutsche Bank AG** (Deutsche Bank). However, RREEF Limited does not own (or have any economic links) to RREEF Fund and Deutsche Bank's only financial interest in RREEF Fund is a financing commitment which accounts for less than two per cent of the total financing commitments of RREEF Fund. [See End note 1]
2. RREEF Fund has a wholly owned subsidiary, **Infrastructure Saxon sarl** (Saxon).
3. **Kelda Holdings Limited** (Kelda) is the ultimate parent company of the water company **Yorkshire Water Services Limited** (Yorkshire Water).

BACKGROUND AND TRANSACTION

4. On 23 March 2010 Saxon acquired an additional shareholding in Kelda to take its total (voting and economic) ownership of Kelda to 23.37 per cent

('the Transaction').¹ Therefore it may be the case that, through its management of RREEF Fund, Deutsche Bank is able to control or materially influence the policy of Yorkshire Water.

5. Further, Deutsche Bank holds interests in a number of companies that ultimately own shares in Sutton and East Surrey Water Company (SESW). Therefore, it may be the case that the Transaction brings two water enterprises, Yorkshire Water and SESW, under common control. If it believes that this is or may be the case that a merger of two water enterprises has taken place, the Office of Fair Trading (OFT) is required to refer the Transaction to the Competition Commission for further investigation if both water enterprises have turnover of more than £10 million (which they do in this case).²
6. The parties (RREEF Fund, Saxon and RREEF Limited) notified the Transaction to the OFT on 28 April 2010. The OFT's administrative deadline in this case is 25 June.

JURISDICTION

7. The merger provisions of the Enterprise Act 2002 (the Act) state that a relevant merger situation (that is, one which the OFT has jurisdiction to examine) is created if two or more enterprises are brought under common ownership or control as a result of the transaction and either the turnover test or share of supply test is met (sections 26 and 23 of the Act). In the special case of water mergers, the jurisdictional thresholds are different in that both parties must have turnover of more than £10 million (section 33 of the Water Industry Act). However, the concept of common ownership or control in water mergers is the same as for other mergers.
8. A water merger will have taken place only if Yorkshire Water and SESW have come under the common control of Deutsche Bank. Given the level of the shareholding acquired by Saxon in Kelda (see paragraph 4 above), the OFT has first considered whether Deutsche Bank might hold the lowest level of control, known as material influence, over Yorkshire Water.

¹ Saxon had a pre-existing shareholding in Kelda of around two per cent before the Transaction.

² This requirement is pursuant to the Water Industry Act 1991 as amended by section 70 Enterprise Act 2002. See paragraphs 10.1–10.3 of the OFT's 'Mergers: jurisdictional and procedural guidance', 2009, OFT527.

9. The OFT's Jurisdictional and Procedural guidance states that the key factors to take into account when considering material influence are the size of the acquired voting shareholding (both itself and also in relation to typical attendance/voting of other shareholders at shareholder meetings), board representation and other factors such as production agreements or financing agreements.³ The OFT makes its assessment on substance and not on legal form.
10. In this case, Saxon has a voting interest of 23.37 per cent in Kelda (which effectively equates to a 23.37 per cent stake in Yorkshire Water). As a result Saxon has the right to appoint two of the 12 directors on the board of Kelda, in line with its equity stake in Kelda.⁴ Six director posts in Kelda are reserved for the three other investors in Kelda with the remainder being appointed by vote.⁵
11. Since the original consortium (comprising the other three shareholders) acquired Kelda (in February 2008) there have not been any general meetings of the company since there is currently a general meeting waiver in place. Instead, matters which would otherwise be put to a general meeting are decided at board level. As such the effective management of Kelda takes place through the board of directors through a simple majority vote. The parties submitted attendance records for the past 15 board meetings of Kelda. These figures show that, for Kelda, directors from each of the other three investors attended all of the meetings apart from one in which no director attended from one of the investors. Based on these attendances the Saxon directors would not be able to out-vote or block motions voted for by the other directors at board meetings.
12. Notwithstanding this, the agreement between the four Kelda shareholders specifies that some decisions require specific levels of shareholder, not just board, approval. Such matters are divided into Part A matters and Part B matters. Part A matters (strategic commercial decisions⁶) require approval

³ Paragraphs 3.15–3.28.

⁴ The parties submitted that there are currently nine directors of Kelda but the additional two Saxon directors takes the total to 11. When the currently vacant finance director post is filled the eventual number of directors will be 12.

⁵ Each shareholder has the right to appoint one director for each 10 per cent of Kelda that it owns. Therefore, Saxon, with over 20 per cent but less than 30 per cent has the right to appoint two directors whereas one shareholder has over 30 per cent but less than 40 per cent and therefore has the right to appoint three directors.

⁶ For example, acquisitions and disposals, financing structures, appointing and dismissing directors and approval or adoption of the Business Plan.

of at least 60.6 per cent of votes and Part B matters (minority shareholder protection matters⁷) require at least 90.1 per cent approval. To date, no investor meetings have been called to consider Part A or Part B matters since decisions have been taken at board level (see preceding paragraph). However, any Kelda director can call a meeting of investors and, if this were to occur, Saxon's shareholding is such that it is unable to pass or to block any Part A matters (if all shareholders' representatives attend the meetings).⁸ Although each shareholder can unilaterally block Part B matters, these are investor protection matters rather than matters concerning the company's commercial behaviour in the marketplace. A representative of each investor must be present at investor meetings in order for a quorum to be achieved.

13. Finally, no director of Saxon, Kelda, Yorkshire Water, RREEF Fund or RREEF Limited is on the board of SESW or the board of any of SESW's parent and associated investor companies. Nor, given the fact that the shareholders other than Saxon in Kelda are also significant financial investors, does the OFT believe that the Saxon directors would have any particular influence in board discussions beyond their proportionate voting ability.
14. Given the above evidence, the OFT does not consider that Saxon has acquired the ability materially to influence the policy of Kelda and therefore of Yorkshire Water. The OFT therefore has not found it necessary to decide whether Deutsche Bank controls RREEF Fund through the management (but not ownership) of it or whether Deutsche Bank controls or materially influences SESW.

DECISION

15. The OFT therefore considers that a merger of two water enterprises has not taken place for the purposes of section 32(b) of the Water Industry Act 1991 since two water enterprises have not ceased to be distinct.

⁷ For example, insolvency proceedings, fundamental changes to the company's existing lines of business and changes to the dividend policy.

⁸ The shareholdings of the other three shareholders in Kelda are 37.15 per cent, 26.32 per cent, and 13.16 per cent. Thus, even if Saxon were to vote in concert with the largest shareholder, together they could not pass a Part A matter if all shareholders attended.

END NOTES

1. RREEF Limited receives a management fee from the general partner of RREEF Fund.