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IN THE COMPETITION
APPEAL TRIBUNAL

Case No. 1166/5/7/10

Victoria House,
Bloomsbury Place,
London WC1A 2EB

6 November 2012

Before:

VIVIEN ROSE
(Chairman)
TIM COHEN
DTKCP LANDERS

Sitting as a Tribunal in England and Wales

BETWEEN:

ALBION WATER LIMITED

Appellants

– v –

DWR CYMRU CYFYNGEDIG

Respondent

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HEARING (DAY 12)

Note: Excisions in this transcript marked “[...][C]” relate to passages excluded.

APPEARANCES

Mr Thomas Sharpe Q.C., Mr Matthew Cook and Mr Medhi Baiou (instructed by Shepherd Wedderburn LLP) appeared on behalf of the Claimant.

Mr Daniel Beard Q.C., Mr Meredith Pickford and Ms Ligia Osepciu (instructed by Hogan Lovells International LLP) appeared on behalf of the Defendant.

Tuesday, 6th November 2012

(10.00 am)

Closing submissions by MR BEARD (continued)

MR BEARD: Good morning, madam and members of the Tribunal.

Yesterday I was dealing with ...

(fire alarm sounds)

As I was saying, I was dealing with what we say is the right legal test in relation to the common carriage price and, in the alternative, if you're not accepting our approach to the legal test, how the analysis of the relevant common carriage price at the time needs to be carried out rather carefully because of the perfectly proper assumptions that regional average cost pricing was appropriate. And, indeed, one needs to be very careful about the sort of knowledge, the specific pieces of knowledge that you attribute to, in particular, Dwr Cymru at the time of that settlement.

We then move on to the third question in relation to the common carriage: would Albion have accepted? Now, obviously one has to consider this question at different possible price levels given in the alternative. Now, there is no basis for any suggestion that Albion would have agreed to common carriage at 16.5p, nor on the lawful basis of 15.8p. Albion seeks only to focus on 14.4p, and we've already said why there's a problem with

1 suggesting that Dwr Cymru would have offered 14.4p.

2 But even there, working on Albion's own case, there
3 are real fundamental problems. It was pressing at the
4 time for 7p. In fact that was the absolute maximum that
5 it was pressing for. It had suggested that actually it
6 would only want a price much lower than 7p in relation
7 to the relevant common carriage elements. So why, in
8 those circumstances, would it have accepted 14.4p? We
9 say it wouldn't.

10 Now, one of the things that is said is that Albion
11 was in the accounting darkness about the relevant
12 pricing, and it says therefore it wouldn't have taken
13 this because the price wasn't justified.

14 Two points to make: first of all, in relation to
15 this allegation of accounting darkness, it's in some
16 contrast to what Albion were saying at the time, and
17 indeed had maintained subsequently. Just for your
18 reference it's document bundle 4, 164, page 1025. It
19 said it was putting forward those prices for common
20 carriage on the basis of what it called overwhelming
21 evidence in relation to what it considered it knew about
22 these matters.

23 In relation to the suggestion that it would have
24 taken the price, this is contrary to the evidence that
25 it has given and the stance it has taken in relation to

1 justification. Now, what Albion has constantly said is,
2 ah, well, the price had to be justified. It all had to
3 be spelled out.

4 There are two things to say here. First of all, no,
5 it didn't have to be justified in the way that Albion
6 suggested. There isn't a basis for that. Albion seems
7 to work in a world where everyone approaches one another
8 on a totally open book basis in relation to figures.
9 That's not the way the world works, not the way any
10 dominant undertaking is required to work.

11 But more than that, if one takes up bundle 5, at
12 tab 227, here we have the Ofwat 2004 decision. If one
13 could turn on to paragraph 379, this was the allegation
14 being made at the time to Ofwat that there'd been
15 a failure to provide sufficient information and
16 justification.

17 Now, Mr Sharpe appeared, during the course of his
18 submissions yesterday, to say Ofwat didn't really deal
19 with these points. These were specific allegations made
20 of abuse by Albion in relation to the way that Dwr Cymru
21 had conducted itself.

22 As you'll see from paragraphs 379 to 381, what Ofwat
23 is saying there is no, actually the information provided
24 was entirely adequate in relation to the FAP, it was
25 sufficiently justified. That leaves Dr Bryan and Albion

1 with a real problem. If the justification given for the
2 FAP was sufficient, and there's no subsequent
3 overturning of that, in those circumstances, his
4 evidence is, "It wasn't sufficiently justified, I wasn't
5 going to take this".

6 He was working on a different basis as to what he
7 thought he could expect from people. He wasn't
8 justified in his demand for justification.

9 So there wasn't justification, he says in relation
10 to the FAP. There is no reason to think there would be
11 more justification in relation to a non-abusive price
12 because there wasn't any need for any further
13 justification. So Dr Bryan's problem in this regard
14 isn't cured in the counter-factual world. The truth is
15 that Albion wanted a price that wasn't based on any
16 top-down methodology. It wasn't about justification.
17 They actually knew what the methodology was, the
18 underlying methodology. It wanted a bottom-up price.

19 The lines were relatively clearly drawn here, so all
20 this about justification, it was effectively Dr Bryan
21 saying, "I don't want a price based on this sort of
22 methodology".

23 As we know, there wasn't any good reason why that
24 sort of top-down methodology couldn't be used. We know
25 that because when it comes to the final judgment, the

1 Tribunal is using top-down methodologies. It uses
2 crosschecks; we quite accept that. But to suggest that
3 it didn't use a top-down methodology is just wrong.

4 So Dr Bryan has a real problem in relation to those
5 matters. But he also has a problem with what he has not
6 actually done in the real world, because in a way, one
7 of the clearest indications as to whether he accepted
8 14.4p, is what has happened since 14.4p has been set out
9 as a compromise. Because as we know, Dwr Cymru came
10 forward with an offer of 18.7p in 2009/2010 prices.

11 It's perhaps worth pulling that out. It's in
12 bundle 17, tab 73. Just to be clear, this is a letter
13 in response to Dr Bryan's letter of 22nd June in which
14 he says:

15 "In the light of the letter of today's date and your
16 observations about the expiry of your common carriage
17 offer on 7th November 2008, would you please provide
18 a common carriage price valid for the current charging
19 year."

20 That's what he's saying in tab 72. What is then
21 provided is a reiteration of the previous offer,
22 7th November 2008, but updated to 2009/2010 prices.
23 What happens then? Nothing.

24 This is the price that Dr Bryan has been burning to
25 receive. This is the price that back in 2001,

1 backdated, he says he would have accepted with alacrity.
2 July 2009, that is.

3 Just for completeness whilst we're in this bundle,
4 although I think we all probably agree that it doesn't
5 matter whether this was the last or penultimate letter,
6 it was in fact the last letter in relation to this issue
7 and there was some suggestion that Dr Bryan had sent
8 some earlier letters on 16th January 2009. It was
9 a letter that was supposed to have been copied to Ofwat.
10 A check was made with Ofwat; it had never received that
11 letter. And that is confirmed in tab 76 in that bundle.
12 But that doesn't detract, that is just completion of
13 a loop of information.

14 So there you have 14.4p, never taken.

15 But there is another problem in relation to Albion's
16 position on 14.4p. It's the indexation issue. It is
17 clear from the evidence that Dwr Cymru would only have
18 accepted an RPI indexation. There's an important point
19 here: there was no obligation on Dwr Cymru to offer
20 anything other than RPI.

21 Now, Albion's case is that it would have pressed in
22 the first instance for no indexation, and it would have
23 got that. It's just vanishingly difficult to understand
24 why that would ever be the position taken by --
25 [overspeaking] --

1 THE CHAIRMAN: One thing, in opening Mr Pickford drew
2 a distinction between the test, as I understood it, that
3 the Tribunal has to apply in the counter-factual for
4 arriving at the common carriage price, and the test that
5 we have to apply for other aspects of the
6 counter-factual, which I think was accepted was more
7 commercial behaviour.

8 MR BEARD: Yes, what would have happened.

9 THE CHAIRMAN: What would have happened.

10 MR BEARD: Yes.

11 THE CHAIRMAN: Two questions. Which side of that divide
12 does the indexation point fall into? Second question:
13 in the what "would have happened" situation, what
14 assumptions do we make about the effect on the
15 negotiating result of Dwr Cymru's dominance?

16 MR BEARD: Let's take it in stages.

17 RPI wasn't part of the abuse. It's clear from the
18 judgments that the Tribunal didn't say RPI would be
19 abusive. So RPI on the indexation, the RPI, is no part
20 of the abuse. The excess is in relation to the level of
21 price above. Therefore, RPI analysis falls into the
22 "what would have happened" category. So that's clear.

23 In relation to what would have happened, you ask
24 yourself: what would the parties have done in those
25 circumstances? What would Dwr Cymru have done?

1 Dwr Cymru says, "We would have held out for RPI because
2 that was the structure of regulation of the industry",
3 and as I'll come on to show, Ofwat was assuming that you
4 would be setting your contracts by reference to RPI, and
5 therefore if you didn't set them by reference to RPI,
6 when it came to a price control, Ofwat would have been
7 assuming that you'd have got that increase.

8 THE CHAIRMAN: Yes, that's a different point. That's
9 a point that would be relevant, I would expect you to
10 say, whether we apply a test of reasonable negotiations
11 between equals or a test of Dwr Cymru being in
12 a position to say, you know, take it or leave it,
13 basically. So which test do you say that we apply?

14 MR BEARD: I'm sorry, in relation to the second question
15 that you were asking about the impact of the dominance
16 test, I'm not sure that it assists here because there's
17 no doubt that applying RPI was non-abusive. So even if
18 you assume that we're dominant, which is later found, in
19 those circumstances we are entitled to impose RPI, and
20 the notion that the special responsibility somehow
21 attenuates that doesn't really work. I'm sorry, am
22 I answering the question?

23 THE CHAIRMAN: Yes, but then I don't really see what the
24 difference is between the two aspects of the test,
25 because in both cases you're saying the test is what

1 could we have imposed short of acting abusively, because
2 that's what we would have done?

3 MR BEARD: We say that is what we would have done. You, oh
4 Tribunal, may look at all the evidence and say actually
5 that isn't what you would have done. That is
6 a different exercise from the legal exercise of
7 stripping out the unlawfulness in relation to the
8 excessive pricing. I think those are two separate
9 issues.

10 In relation to the dominance issue, you can take
11 into account the nature of Dwr Cymru, it's scale and its
12 position, and the nature of it as a regulated entity and
13 its concerns about ensuring it was able to index at RPI
14 by reference to the industry norm, and that actually it
15 was in a good position to say in negotiations, "Yes,
16 that is what we are going to stick by". You can take
17 those factors into account because those are material to
18 what it would have done, what would have happened.

19 THE CHAIRMAN: Suppose we were to arrive at a situation
20 where we think, well, actually, if it was two
21 commercially reasonable companies with no particular
22 bargaining power on either side, just suppose we got to
23 this position, they would have agreed PPI, but these
24 weren't such companies, this was Dwr Cymru in a very
25 strong bargaining position and Albion in a very weak

1 bargaining position. And regardless of what reasonable
2 parties would have agreed, Dwr Cymru could have just
3 held out and insisted on RPI unless we think that that
4 would have been abusive. Is that where we get to?

5 MR BEARD: Yes, that's perfectly right. Dominance
6 doesn't suddenly mean that big companies are bad. It
7 means that big companies can go about their daily
8 business, you know, degrees of market power they may
9 have in negotiations. That's entirely proper. That's
10 not in breach of any special responsibility they have.
11 Indeed, if competition law started straying in that
12 direction it could have systematically adverse effects
13 on the way that major companies could operate. So yes,
14 you do take into account the realities of the situation.

15 Just on one issue, this notion of reasonableness, it
16 is one of those implicit suggestions that everyone will
17 speak in quiet voices. There isn't a sense of
18 reasonableness that means that actually, someone that
19 has market power and a commercial interest in setting,
20 for instance, RPI is being unreasonable if they press
21 for and insist upon that when it is a perfectly lawful
22 measure to impose in a contract in circumstances where
23 it is of real significance. There's nothing
24 unreasonable about that at all.

25 I don't want to get into a situation where I am

1 saying, well, the "would have done" test is no different
2 from a reasonableness test, because actually "would have
3 done" takes into account all the real factors that would
4 have occurred absent the unlawfulness.

5 MR COWEN: I'm sorry, just one small point. Would it be
6 reasonable, rational, in the counter-factual world for
7 Dwr Cymru not to supply at all, then?

8 MR BEARD: Not to supply even on bulk supply basis?

9 MR COWEN: Yes.

10 MR BEARD: Well, I think it's different because if you were
11 refusing to supply and you're in a dominant position,
12 you might be in different abuse territory. So if it
13 were non-abusive and it were reasonable not to supply,
14 yes, you're allowed not to supply. If, on the other
15 hand, refusal to supply amounted to an abuse in the
16 circumstances, that's part of the special
17 responsibility. So I think it's one of those
18 hypotheticals that's difficult to answer. But the logic
19 is there.

20 MR COWEN: Thank you.

21 MR BEARD: I should say that refusal to supply, as
22 Mr Pickford rightly says, if someone doesn't accept
23 reasonable terms then it doesn't matter whether you have
24 dominance, super-dominance, or total monopolist, it's
25 not actual abuse in those circumstances. Again, it's

1 a further wrinkle in how does one analyse those sorts of
2 hypothetical situations?

3 In any event, I just track back the Albion's primary
4 case which, as we understand it, is no indexation. We
5 just think this doesn't make any sense whatsoever. No
6 company would enter into a no indexation arrangement.
7 We heard the story yesterday of Albion would never have
8 accepted an inflationary measure in a deflationary
9 world. Well, that is a proposition that, if it were
10 true in these circumstances, where at a particular time
11 K was negative for a particular company and therefore
12 was deflationary, then suddenly you would be in
13 a situation where you couldn't insist upon, for
14 instance, positive RPI measures or, indeed, PPI
15 measures. And when pressed in relation to these
16 matters, that in a deflationary world you wouldn't have
17 inflationary measures, there was a question asked about
18 what about back to backing it with Shotton? And, of
19 course, there it was said, "We wouldn't have anything
20 there either".

21 But of course that's just unreal because we know in
22 the bulk supply agreement that Albion and Shotton have
23 in fact got arrangements that are inflationary in
24 a deflationary world. So quite why it's being suggested
25 that indexation of some sort wouldn't be used when it is

1 absolutely common throughout the industry, is just,
2 frankly, beyond us.

3 That then takes us to the question about whether or
4 not it would be PPI, which was one of the measures that
5 has been used as an inflationary measure in the Shotton
6 arrangements, albeit because of a legacy situation, or
7 RPI. As we've indicated, the only evidence is that RPI
8 would have been the way that things would have been done
9 by Dwr Cymru, and it wouldn't have resiled from that.

10 We have the remedies judgment just for your notes at
11 folder 13, tab 22, paragraph 22; confirmation that
12 there's nothing unlawful about RPI being used. We know,
13 for example, that the UU contract arrangements, although
14 they were never finally completed, those were on an RPI
15 basis as well so. The 9p contract, putative 9p contract
16 would be on an RPI basis, and that's not something that
17 has been challenged.

18 Now, it's also worth considering what Ofwat thought
19 about these sorts of matters. If we could go back to
20 bundle 17, tab 52, and this is a matter we dealt with at
21 paragraph 143 in our closing submissions. If you go to
22 page 6698, this is Ofwat guidance. I should make clear,
23 back in June 1998, on supply of demand submissions, so
24 it is going to how price control matters are going to be
25 dealt with. Under the heading "Tariff switching and

1 large users", just go down to the last couple of bullet
2 points:

3 "In respect of revenues from large users and for the
4 purpose of setting price limits:

5 "... The director will assume that revenues from
6 excluded large users and other sources of non-tariff
7 basket revenue reported in table E6 at 97 and 98 prices
8 are scaled to nominal values by assumed year-on-year
9 change in basket year RPI."

10 That's the approach Ofwat was taking in relation to
11 these matters. It was saying, "We will treat what
12 you're getting from these relevant customers", which
13 would include Albion, "as being indexed at RPI. If you
14 don't index at RPI, we're still going to treat you as
15 receiving the revenues at RPI."

16 In those circumstances, for Dwr Cymru not to have
17 ensured that it had the certainty that it was actually
18 receiving revenues at RPI, in circumstances where the
19 price control would be treating it as obtaining those
20 revenues, would just be irrational.

21 THE CHAIRMAN: Is there any evidence that the people who
22 were doing the negotiation on behalf of Dwr Cymru were
23 aware of this, that it operated in their minds?

24 MR BEARD: We'll double-check, but in his second witness
25 statement -- and I'll come on to that -- at paragraphs 8

1 to 23, Mr Edwards deals in some detail with issues to do
2 with RPI and what was understood as the position in
3 relation to Dwr Cymru in relation to RPI. And I think
4 there it is made very clear that actually RPI was
5 understood to be the proper basis on which we would
6 proceed with any dealings of this sort.

7 So you've got the Ofwat approach. There was all
8 sorts of cross-examination by Mr Cook trying to suggest
9 that because K was negative in the regulatory settlement
10 at some point Dwr Cymru would have known that PPI
11 indexation would have been a better rate than the
12 average rate for RPI, and even the no indexation would
13 be appropriate. But that really just misses the point.

14 K can be positive and K can be negative, and it
15 changes from time to time. And obviously we're dealing
16 here with much longer-term contracts and much
17 longer-term indexation and fluctuations in K across
18 particular years or, indeed, across a single price
19 control.

20 The fact that at any moment you have K at
21 a particular level doesn't tell you about how, as
22 a company, you are going to consider indexing your
23 contracts. You are going to use the index that is being
24 applied across the industry and is recognised by the
25 regulator in order to protect yourself against

1 fluctuations in relevant costs. What K is there doing
2 is ensuring that combination that is a particular
3 struggle within the water industry between ensuring that
4 there's sufficient investment -- and I say it's
5 a particular struggle because in the water industry it's
6 well recognised that the modern asset replacement value
7 is very high as compared to the stuff sitting in the
8 ground. And therefore if you want to incentivise
9 companies to actually invest you're going to need to
10 enable them to recover those costs adequately through
11 the price control. But on the other hand, you want to
12 drive efficiencies which obviously puts in place
13 a negative K.

14 But the fact you have these external considerations
15 as a regulatory structure, means that you flex K due to
16 all sorts of other considerations, doesn't mean that you
17 diverge from RPI in relation to the particular contracts
18 you're dealing with. So essentially it's a red herring
19 that is dangerous to take on, particularly because, of
20 course, K can change. So it can be positive at one
21 point or it can be negative at another, and in those
22 circumstances you'd end up with a situation where you
23 would have proper claims on Mr Cook's basis at certain
24 points for much higher indexations. That would be
25 cutting across the way in which the regulatory scheme

1 worked.

2 That's precisely what Mr Edwards sets out in his
3 witness statement at paragraphs 8 to 23. Now, that's at
4 folder 1, tab 6 in his second witness statement. I'm
5 not going to take you through it in detail, but that is
6 dealing with why Dwr Cymru cared about RPI, would have
7 stuck with RPI, and why it was thinking about RPI as
8 it did.

9 Then the final couple of points to make in relation
10 to this is when we move right through the story and come
11 up to the bulk supply determination in 2011. And I will
12 just provide you with a reference for this. It is
13 bundle 9, tab 304, tab 2699, and the relevant paragraph
14 is 12.2.2. It says:

15 "With effect from 1st April 2012 and for each
16 subsequent year commencing on 1st April, charges for
17 non-potable water shall be adjusted by the annual
18 percentage movement in prices as recorded by the retail
19 price index in the previous November."

20 So this was an assessment being carried out. In
21 particular, one that considered, for example, the costs
22 of water resources, and in those circumstances was
23 saying very plainly RPI is absolutely fine here.

24 So that of course is a matter that was raised in the
25 judicial review that is pending, but it was a matter in

1 relation to which no commission was granted. Just for
2 your references, the judicial review judgment on
3 permission, bundle 16, tab 22, page 6638, paragraph 60.

4 So lots of evidence as to why Dwr Cymru would have
5 pressed for RPI, why it would have pressed for RPI, how
6 it was entirely consistent with the industry, and that
7 is not countermanded by any real evidence on the other
8 side about this.

9 Yes, sorry. Mr Pickford, who is ahead of me on the
10 figures by some margin, points out that the K factor in
11 2005 was actually plus 14.2 per cent.

12 But just finishing off in relation to the RPI issue,
13 it gives rise to two points here. It obviously gives
14 rise to a causation point, because if Dwr Cymru was
15 perfectly legitimately going to insist on RPI and Albion
16 has made clear it didn't want to proceed on that basis,
17 there wouldn't have been a common carriage agreement, it
18 appears. And we've set that out at paragraph 155 in
19 closing.

20 The second point is even if they were able to
21 overcome that substantial difficulty in their evidence,
22 it clearly impacts on the relevant quantum calculation.

23 I'm going to move on from RPI to United Utilities,
24 if I may, because obviously that's the second agreement
25 that was necessary for there to be an arrangement for

1 Albion to supply Shotton Paper using any form of common
2 carriage. So United Utilities needed to provide that
3 supply of water. And the points here overall are
4 relatively simple: the minimum price that United
5 Utilities would have offered would have been 9p. Would
6 have been. That's the only price that United
7 Utilities's internal process would have given regulatory
8 sign-off to. There is no evidence at the time that
9 United Utilities would have done anything else.

10 The tendentious and, indeed, wrong contentions about
11 how LRMC would have been calculated, if it had been
12 calculated on what Albion says is the proper basis,
13 aren't relevant. It's straining into "should" world,
14 but in any event there weren't mistakes in relation to
15 LMRC, and I'll come back to that briefly.

16 Equally, the argument that non-discrimination
17 provisions would have meant there was no basis for 9p
18 are just wishful thinking. And again, that's "should"
19 world not "would" world. It is plain and obvious that
20 United Utilities considered that there was no breach of
21 any discrimination criteria in sticking with 9p. They
22 had given scrutiny to these issues. They thought that
23 condition E applied in relation to it and they were
24 still saying, "It will be 9p". And they were well aware
25 of the fact that actually there was a 3p cost being

1 imposed on Dwr Cymru.

2 Finally, the suggestion that this would all have
3 been a commercial carve-up ignoring Ms White is
4 a remarkable one. Ms White was absolutely clear:
5 regulatory sign-off within UU was required for any
6 price. She was not willing to countenance any price
7 lower than the 9p, and she made that absolutely clear.
8 She had no concern about Ofwat demurring on this. She
9 was confident that they would have confirmed this. So
10 the minimum price would have been 9p.

11 Obviously she carried out work -- and this is
12 referred to at bundle 4, tab 136, 891 -- that 12.1p was
13 what she thought the relevant LRMC price would have
14 been. It is perhaps just worth turning to that to
15 situate ourselves back into what was going on at the
16 time. Tab 136 at bundle 4.

17 What is clear from this, Mr Sharpe said they offered
18 12.1 and then brought it back down relatively quickly,
19 and that suggests, you know, if you had a few hours more
20 it would have been dropped by a few more pence, and if
21 you'd had days you would have been tending towards zero.
22 That just doesn't stack up as an account at all because
23 what happened was Ms White carried out the analysis
24 where she said, "I think the LRMC costs will be 12.1p"
25 and then a clear statement was made by John Lafon that

1 there was a justification for moving back down to 9p,
2 that was consistent with the regulatory analysis that
3 had been carried out.

4 Miss White somewhere in her evidence made absolutely
5 clear that she would not go any lower at all.

6 Mr Lafon's e-mail, which is earlier in this chain, makes
7 it very clear that the reduction takes into account that
8 the supply is not secure, and therefore has a lower
9 level of reliability than our supplies which are not
10 integrated into the network. And in those
11 circumstances, there was a good justification which
12 Ms White was willing to accept, but the very fact that
13 there had to be consultation with Ms White about whether
14 or not they could move away from 12.1 simply reinforces
15 the importance of that regulatory sign-off. And that's
16 not really surprising.

17 United Utilities is another very large undertaker in
18 the industry. It needs to deal with Ofwat. It needs to
19 make sure that Ofwat is content with the way that it is
20 setting prices, otherwise it is vulnerable to regulatory
21 and competition intervention in relation to these
22 matters. Ms White was very clear that she was well
23 aware of the competition concerns and the regulatory
24 guidance that was given in relation to these matters.

25 To take it in stages, it has been suggested that

1 somehow Ms White made mistakes and that left leeway in
2 relation to the regulatory process. First of all,
3 that's not what we're asking. We're asking what would
4 United Utilities have done, and none of the suggestions
5 that have been made are such that Ms White indicated she
6 would have moved away from 9p at all in relation to any
7 of the contentions about LRMC, or any other matter
8 relating to discrimination. And this hierarchy that
9 Mr Sharpe seems to want to put in place between LRMC and
10 discrimination is not one that in any event exists
11 in law.

12 Moving away from that, she didn't actually make
13 mistakes. Mr Sharpe and Mr Cook have been suggesting
14 that some how there has been a misreading of MD163.
15 Now, that is to do with common carriage, so strictly
16 speaking it didn't apply in relation to UU arrangements.
17 But the suggestion was being put that actually MD163 was
18 terribly, terribly narrow and it has only allowed you to
19 set costs on a specific asset-related basis. That
20 plainly isn't true. I'll come back to that in relation
21 to the Ofwat decision.

22 Ms White was recognising that the broader approach
23 to LRMC was entirely proper and the right way of
24 proceeding. So she was reading MD163 entirely
25 consistently with Ofwat's approach. She wasn't making

1 any errors in relation to these matters, and she was
2 alive to competition concerns.

3 Now, at one point yesterday Mr Sharpe described
4 Ms White's concerns about competition law as being
5 eccentric and suggested he was being --

6 THE CHAIRMAN: I don't think he was describing that as being
7 eccentric; I think he was describing what she understood
8 LRMC to be as eccentric.

9 MR BEARD: I think actually it was to do with predation, and
10 he suggested her concerns about predation were
11 eccentric. But check the transcript. Little turns on
12 it. But the concern about predation was not only not
13 eccentric, it was real and proper.

14 There is consistent evidence from Ofwat, including
15 specifically in the Competition Act 1998 guidance that
16 was provided by Ofwat and OFT jointly, that one of the
17 real concerns that existed was that if you were a large
18 player in the water industry and you were able to price
19 by reference to some sort of very narrow local costs
20 measure, you would effectively be able to exclude new
21 entrants. You would be able to predate. Because if you
22 only focus on your local costs and not the long-term
23 replacement costs and the broader costs incurred that
24 have to be effectively smeared across your
25 infrastructure, you would be able to cost at a lower

1 level than entrants.

2 I realise this is the opposite problem from the
3 problem that led to the finding of abuse here, but to
4 suggest it is eccentric is just plain wrong. It was
5 central to the consideration and concern that was
6 expressed both by Ofwat and by OFT.

7 So one of the concerns that Miss White quite
8 properly had in mind was actually dropping these prices.
9 That was in the forefront of her mind, and she was right
10 to have it in the forefront of her mind. It wasn't
11 eccentric. To have ignored that would have been
12 eccentric and irresponsible.

13 THE CHAIRMAN: If someone had argued that the price that we
14 have always referred to as 3p was predatory because it
15 didn't cover future replacement costs so it wasn't
16 a long-run marginal cost.

17 MR BEARD: I think some of the concerns raised by United
18 Utilities when it raised these things with Ofwat were
19 pointing in that direction, but of course you're dealing
20 with a very old agreement here.

21 THE CHAIRMAN: If you just let me finish. Wouldn't the
22 answer to that have been: this is an unusual contract
23 because in fact they agree not only to pay the 3p actual
24 costs for the water, but also to contribute their share
25 of future replacement costs, and therefore, in fact the

1 totality of the contract is long-run marginal cost, it
2 is just a lumpy contract rather than the usual long-run
3 marginal cost contracts in which you gather with each
4 metre cubed of water a little bit of money to go into
5 the kitty for when you have to replace the pumps?

6 It seemed what she was doing was a different
7 exercise, which was the opportunity cost of the water in
8 the sense of what would United Utilities have to pay to
9 get a different 36 megalitres of water into their system
10 if they didn't have the Heronbridge pump. Isn't that
11 what she was doing?

12 MR BEARD: Well, I mean, in one way I suppose one can look
13 at it like that. I think the danger is that what is the
14 proper approach to long-run marginal cost analysis in
15 the water industry may not just be appropriately limited
16 to discrete sections of particular systems, and that
17 what Ms White was doing was looking at long-run marginal
18 costs in a wider basis across the United Utilities's
19 system and she said, "Well, that's entirely appropriate,
20 that's the way it should be done, that was the way I was
21 thinking about it".

22 If you then say, well, long-run marginal costs
23 across the system then end up looking like
24 a quantification of the opportunity costs for getting
25 that amount of water, then it may well be that that will

1 be the right way of looking at it. But that doesn't
2 suggest that anything she did in relation to her
3 long-run marginal cost calculation was wrong, and nor
4 does it mean that one should just automatically treat
5 the old Heronbridge agreement as fulfilling the
6 requirements of an orthodox long-run marginal cost
7 calculation as it would be understood in the industry.

8 We know that, for instance, there are all sorts of
9 central costs. We saw that material from Chris Jones
10 that talked about how in fact the vast majority of costs
11 are not local costs in the system, and you then end up
12 with a situation where you then effectively have to
13 smear those costs across the system no matter whether it
14 is spurs on a system or central parts of the system, you
15 can end up missing those costs if you start bottom-up in
16 relation to the long-run marginal cost calculation.

17 So whilst I can understand why you say there's
18 a sort of sense of LRMC about the old Heronbridge
19 agreement, I don't think it is really capturing what
20 a proper LRMC analysis would do in relation to this
21 system or any other system, and I'd be reluctant to sort
22 of conflate the two.

23 Does that deal with the point?

24 THE CHAIRMAN: Yes.

25 MR BEARD: So she carried out perfectly orthodox LRMC

1 approach that was consistent with MD163. Her concern
2 was she was doing was Ofwat said.

3 There were also various points in cross-examination
4 about her water resource management plan and whether or
5 not there was a surplus or not a surplus. Well,
6 actually, when we look at the document that she was
7 taken to, which is at tab 21 of bundle 2, actually what
8 we saw was there would be surpluses because United
9 Utilities were going to spend money and invest and
10 ensure that those things happened.

11 Now, of course that is what responsible operators
12 do, and that is what Ofwat is there to do. It is to
13 ensure that people are spending money efficiently in
14 order that when we turn on the taps or an industrial
15 concern wants to turn on the taps, there is water
16 flowing. The fact that at the moment water flows when
17 we turn on the taps doesn't mean we can presume
18 a surplus and there isn't going to be a need for
19 substantial investment in any of these areas and that
20 somehow we should see the long-run marginal costs of
21 water as being next to nothing because at the moment
22 when we turn on the taps the water runs. That is just
23 not the right approach. And actually, that report
24 indicated that there were going to be systematic
25 deficits unless that sort of investment was undertaken.

1 There was some digression about mandatory leakage
2 and metering requirements, but in economic terms those
3 are endogenous not exogenous, because it is what you are
4 prioritising and the relevant costs of the different
5 options that have to be taken into account. And once
6 that process is gone through with the regulator, the
7 regulator will set targets in relation to it. But he
8 doesn't just pluck them out of the air.

9 What we saw in relation to that report, in
10 particular on table 18, was a very substantial deficit
11 and a range of measures that would need to be taken,
12 including metering and other steps, many of which were
13 very, very expensive indeed, and yet the regulator is
14 still saying that is appropriate for all sorts of other
15 concerns.

16 So there is a lot of investment that is required.
17 It is not right to presume somehow there was an
18 indication of consistent surplus. Surplus was only
19 going to be achieved by investment. Ms White was taking
20 that background, that water resource report, into
21 account when she carried out the LRMC calculation. She
22 was not wrong to do so.

23 In those circumstances, she'd done the right thing,
24 she had carried out the assessment. It was right to
25 reach the prices she did. It was entirely

1 understandable that she would not have countenanced any
2 lower price. And it is just worth noting, and I'll just
3 give you the reference, that bulk supply price report
4 from Ofwat, bundle 9, tab 304, page 2744 at
5 paragraph 6.123. Ofwat came to assess the water
6 resource price at Heronbridge at 15.3p in 2011, that's
7 12.2p in 2000 and 2001 prices. So far from being
8 outlandish, when a further methodology was applied in
9 relation to those issues by the regulator, that was the
10 price they came out with.

11 Yes, it is subject to judicial review. We accept
12 that. But to suggest that somehow she was getting it
13 wrong is just not justified at all. What would she have
14 done? What would United Utilities have done? They
15 would have said 9p.

16 Just to tidy up on the suggestion of 3p. It wasn't
17 ever mentioned in the negotiations between UU and
18 Albion. Indeed, when Albion was telling Ofwat it had
19 already done a deal in principle on
20 12th December 2000 -- and just for the notes, that's
21 bundle 3, tab 98 at 749 -- that was in relation to the
22 up to 9p price. In their discussion about 3p, UU had no
23 incentive to entrench a price that it strongly objected
24 to, and there is no evidence at all to support any
25 suggestion of 3p being acceptable to United Utilities.

1 I won't, therefore, go through any more in relation
2 to this, and we know that it would have been RPI
3 indexed, the 9p, as well.

4 That takes us to the question: would Albion have
5 accepted 9p? There is a relatively short point here.
6 If we turn to Albion's own skeleton argument.
7 Bundle 11, tab 1. If we could turn on to page 3440,
8 this is Albion's skeleton argument. Sorry,
9 paragraph 75:

10 "In February 2001 United Utilities put forward a new
11 proposal which was for a price of 12.1p, or 9p if Albion
12 waived its rights to challenge this price at a later
13 date. Welsh Water's case is that Albion would have
14 accepted United Utilities' offer. However, this is
15 clearly unsustainable.

16 "First, Albion was aware in June 1999 [supposedly]
17 that United Utilities did not place a value on the water in
18 question." Dr Bryan explains during his discussions with
19 United Utilities that he considered there was a surplus
20 of water resources.

21 80:

22 "It is difficult to see any logical reason why
23 Albion would have accepted a price three times higher
24 than that being paid by Welsh Water for water which
25 United Utilities had acknowledged it put no value upon,

1 given it had an excess of water, in circumstances in
2 which Albion had the ability to obtain a proper price by
3 applying to Ofwat for a section 40 determination or
4 making a competition law complaint against United
5 Utilities."

6 We move on, paragraph 85:

7 "There is, therefore, no reason to think that Albion
8 would simply have accepted United Utilities's proposal
9 in circumstances in which it would mean that Albion
10 would be paying three times the price paid by
11 Welsh Water."

12 Actually, the case put by Albion is that they
13 wouldn't have accepted 9p. Indeed, if that's being
14 resiled from, it may be a relatively serious matter
15 because the way in which Mr Pickford was cross-examining
16 in relation to these issues was obviously conditional
17 upon the way the case had been put.

18 It is also clear that Dr Bryan wouldn't have
19 accepted the 9p on a conditional basis. Mr Sharpe said
20 yesterday, ah well, it didn't matter whether it was
21 conditional, you couldn't enforce that sort of thing as
22 a matter of public policy. A funny submission, because
23 if that were true it doesn't really explain why Dr Bryan
24 was so concerned about conditionality.

25 It is worth noting in passing that Mr Sharpe said,

1 oh, it wouldn't be enforceable because of course
2 contrary to public policy for a dominant undertaking to
3 impose such an arrangement. There is no evidence that
4 United Utilities is dominant in this regard. There is
5 no finding in that regard. There is basis on which to
6 proceed, that United Utilities was dominant. That's
7 precisely the sort of collateral allegation that hasn't
8 been tested in these proceedings and can't be relied
9 upon.

10 If we just look, if we may, at our closing
11 submissions, paragraph 56, page 18, paragraph 56.

12 Dr Bryan gave clear evidence that he wouldn't have
13 entered into any bulk supply agreement with United
14 Utilities that was conditional on Albion's accepting the
15 contract price to be fair and reasonable.

16 We've quoted one particular instance, Day 3 of the
17 transcript, page 43. The core answer is that that is in
18 bold-face type at the bottom, lines 19 and 20:

19 "The short answer to this is ..."

20 Dr Bryan's short answer:

21 "... no, we wouldn't have accepted that sort of
22 conditionality."

23 Just for completeness, of course it would also not
24 be consistent with the fact that, under the arrangements
25 with United Utilities, Albion would have got a free

1 £25,000 on signing it -- the first point -- whatever
2 happened. So it is rather remarkable that if this was
3 so straightforward and would have been accepted with
4 such alacrity, all the evidence points in the other
5 direction. Although it may not be a massive sum of
6 money, free money was effectively being rejected here.

7 There's a real causation issue. We've set it out in
8 some detail in our written closings, and I've tried to
9 go through it relatively quickly. But in relation to
10 United Utilities there is particularly good reason why
11 Albion would have resisted entering into any such
12 agreement, and we know that without it you wouldn't have
13 had the arrangements to be able to supply Shotton Paper
14 under current common carriage.

15 So there's a real causation issue, and whether or
16 not there's a causation issue there's, of course,
17 a significant issue in relation to quantum calculations.
18 9p (inaudible) RPI is the minimum price you can take
19 into account as the price in relation to United
20 Utilities.

21 I'm going to deal now with a number of points. The
22 first I'm going to turn to now is back-up supply, if
23 I may. In dealing with this what I'll do is I will
24 stick with the written closing. So if we could turn to
25 page 48.

1 Now, this is under the heading "Adjustment 4",
2 because obviously back-up supply is a quantum adjustment
3 rather than a causation issue in this regard. Core of
4 this lies in the core of the Second Bulk Supply
5 Agreement as set out in paragraph 179. It is in the
6 bundle at bundle 2, tab 19, but I am fairly confident
7 this is an accurate reflection of clause 2.1, which is
8 the key clause:

9 "Dwr Cymru shall supply such quantity of potable
10 water to Albion as it may require during the term of
11 this agreement up to a maximum quantity of 8 megalitres
12 a day, which maximum quantity Dwr Cymru shall reserve
13 for such supply."

14 That's really the key issue here. At the relevant
15 time, there was a contractual requirement that there
16 would be a reservation of supply, because really the
17 only argument being deployed against there being a need
18 for a cost of back-up potable supply to be included is
19 that subsequently, much later on in the Ofwat 2011
20 decision, it was said, "Oh, actually you don't need to
21 specifically reserve that supply and no cost needs to be
22 attached to it". That's what is said by Albion.

23 But the point is that was a different situation,
24 a different contractual arrangement in 2.1. What
25 Albion can't get away from is the fact that Dwr Cymru

1 was being placed under an obligation to reserve that
2 supply. If you are under an obligation to reserve that
3 supply it is not shocking and astonishing that there is
4 a cost associated with that reservation. And that, of
5 course, is precisely what has been identified by Ofwat,
6 in particular in the referred work which came earlier
7 and was concerned with this structure.

8 As we've indicated, Dr Bryan in fact recognised that
9 there would, under common carriage arrangements, be
10 a requirement for a back-up supply of potable water. He
11 then disputes this reservation charge. But if we take
12 out the referred work in bundle 8, tab 274 and if we
13 just go on to 2464, which is actually a page that
14 Mr Sharpe took you to yesterday in relation to other
15 matters, there is a sort of summary of results for the
16 methodologies applied during the course of the referred
17 work. And what the AAC plus the top-down methodology
18 says is: back-up supply would cost 4.4p. I won't take
19 you back through the details of that.

20 THE CHAIRMAN: I would like to see where Ofwat discusses
21 whether -- what the reserved arrangement in place
22 actually was.

23 MR BEARD: I'm sorry, the arrangements in relation to the
24 contract?

25 THE CHAIRMAN: Well, not so much the contract, but where it

1 discusses what arrangements were in fact in place.

2 MR BEARD: I think perhaps the best summary is at 6.105. We
3 quoted this in our closings at 186, but it's perhaps
4 just worth reading through that paragraph. I won't read
5 it out.

6 THE CHAIRMAN: Yes, it is where they're looking at what
7 actually was it that Dwr Cymru had that cost around ten
8 [overspeaking] --

9 MR BEARD: It is not surprising. Dwr Cymru effectively has
10 to keep 8 megalitres a day of potable capacity on
11 permanent stand-by. That's the way Ofwat understood the
12 arrangements to operate.

13 "This is enough water to supply a small town of
14 around 60,000 people."

15 That's the way in which Ofwat understood the
16 obligation in relation to the arrangements that existed
17 for back-up potable supply.

18 THE CHAIRMAN: Yes, but what are the assets the cost of
19 which then equate to 4.4p spread out over all the water?
20 Does it say that anywhere?

21 MR BEARD: The costing of the back-up supply starts at 6.83.

22 THE CHAIRMAN: It may be that we just need to look at that.

23 MR BEARD: Yes. I think that's the section you may be
24 looking for, madam.

25 I think perhaps the 6.102 through to 6.104 may well

1 provide you with the best summary of those
2 considerations that were then taken into account by the
3 authority. I'm sorry.

4 THE CHAIRMAN: What I'm struggling to understand is, in your
5 skeleton, in your closing submissions, you seem to be
6 saying there was the contractual obligation, and what's
7 more, Ofwat, in the referred work, found as a matter of
8 fact, as you have said, that there was -- or are you
9 saying this -- that Ofwat in the referred work found as
10 a matter of fact that Dwr Cymru had made arrangements to
11 keep 8 megalitres a day of potable capacity on permanent
12 stand-by, and that the costs that Dwr Cymru was
13 incurring in order to do that were the 10p per cubic
14 metre which then becomes the 4.4?

15 What I'm trying to identify is whether in fact
16 that's correct or whether what Ofwat did was say, "Yes,
17 there is the contractual obligation. Assuming that
18 Dwr Cymru are actually reserving that supply, this is
19 the kind of money that it costs for water companies such
20 as Dwr Cymru to reserve that supply, to make that kind
21 of reservation. Therefore, we're going to add in the
22 4.4p."

23 Do you see difference between the two things?
24 Because Mr Sharpe's point is that regardless of the
25 contractual obligation, there wasn't in fact any

1 reservation. What I'm trying to find is whether there's
2 something in the Ofwat referred work that indicates that
3 what Mr Sharpe said is contrary to what Ofwat --

4 MR BEARD: I think what the referred work is saying is that
5 there is clearly an obligation. Should there be a cost
6 attributed to that obligation?

7 THE CHAIRMAN: Yes.

8 MR BEARD: Ofwat says: yes, there should.

9 THE CHAIRMAN: Right.

10 MR BEARD: Now, for Mr Sharpe to then come along and say
11 actually, no, there isn't really is running entirely
12 contrary to this. So I'm not sure how he blows the
13 tissue paper in that.

14 THE CHAIRMAN: The tissue paper is: was there in fact cost
15 incurred in reserving the back-up supply, or was there
16 really a back-up supply, because that may help us to
17 decide whether Albion would have thought it was
18 important to buy it separately now it's not bound up in
19 the bulk supply price because they'd moved to a common
20 carriage arrangement.

21 So the question we have to decide is would Albion
22 have paid extra for a reserved back-up supply? That
23 must depend on whether they were in fact getting it, and
24 knew that they were getting it, and thought that they
25 were getting it, regardless of what the contract says,

1 under the earlier agreement. What I'm trying to find
2 is, does the Ofwat referred work help us to come to that
3 conclusion?

4 MR BEARD: We say it does because what the Ofwat work
5 does -- if you go back to 6.92, and the bullet points
6 there, it explains how the systems that exist within
7 Dwr Cymru's network of arrangements are essentially set
8 up to ensure that this back-up supply can be provided.

9 What you've got is a description of what's going on,
10 an acceptance of an obligation, and a recognition by
11 Ofwat that there is a cost associated with making those
12 arrangements in order to fulfil that contractual
13 obligation. And that's what Ofwat is saying is 4.4p,
14 when applied to the relevant flows. Because those
15 points about how it operates using the Brecon or
16 Alwen systems to provide back-up supply are ones
17 specifically considered by Ofwat.

18 You'll recall in fact this was a section where
19 Mr Pickford cross-examined Dr Bryan, and Dr Bryan with
20 great alacrity started suggesting that Dwr Cymru had
21 been misleading Ofwat in relation to these matters. And
22 when it came to it, and it was pointed out that actually
23 it was absolutely clear that Ofwat very clearly
24 understood what was going on, how reserves were put in
25 place, what supplies were available and what alternative

1 supplies were available, Dr Bryan promptly resiled from
2 what was a very bold accusation.

3 MR LANDERS: But I can't help, having just read these again,
4 6.103, 6.104, it basically says that:

5 "The authority would not approve stand-by charges
6 except on an exceptional basis, for example ports and
7 power stations."

8 It then goes on to say:

9 "For illustrative purposes, we'd assume 15 per cent
10 of your total treatment costs are for back-up supply."

11 Dwr Cymru come back and say, "That's not enough,
12 Albion said it's too much", and then in 6.105 it's
13 talking about what could be done, and talks about the
14 figure you've just quoted as being a simple provisional
15 cost calculation. It doesn't seem, from this little
16 bit, to actually say this is what was actually being
17 reserved.

18 MR BEARD: This is carrying out the analysis of the costs of
19 the reservation, and it does then make various sorts of
20 assumptions and generalisations which are precisely what
21 you're referring to. How do you carry out that sort of
22 cost analysis? I don't think you can read from that
23 that Ofwat is suggesting actually, no, we didn't really
24 need to do anything in order to fulfil this obligation.
25 To the contrary, they're specifically saying: actually

1 you do, but the costing of it is quite high.

2 It may just be worth -- for your notes, section 5 of
3 this document is identifying the relevant services. At
4 5.37 it highlights what the dispute in relation to
5 back-up supply is and what the points that were being
6 put were. (Pause)

7 MR COWEN: Can we have the reference again, please?

8 MR BEARD: 5.37. It's three paragraphs.

9 There is one further document that isn't referred to
10 in the closing but was put in cross-examination, which
11 I would take the Tribunal to. It's in bundle 7 at 273.
12 If we could go to 2202, this is the oral hearing that
13 preceded the referred work. At the bottom of 2202,
14 you'll see Mr Musco, this is before Ofwat:

15 "Did you actually want that back-up at the time
16 though still?

17 "Dr Bryan, I think we've explained to you that our
18 view was that having negotiated a common carriage
19 agreement for non-potable, we would necessarily have to
20 re-negotiate our existing bulk supply for the potable
21 supply. No getting away from it. Albion needed
22 a potable supply. Within that, yes, we would be looking
23 to negotiate, as indeed we are today in the process of
24 negotiation with Dwr Cymru, what the terms for a back-up
25 potable supply would be. Those negotiations would look

1 at reserve volume, availability, conditionality, all
2 sorts of other things. We would make an informed
3 judgment on the service offered at the time. That was
4 never intended as part of the quite separate non-potable
5 supply arrangements."

6 Dr Bryan is there saying, "I do need a reserve
7 volume, I do need availability."

8 THE CHAIRMAN: He's saying he needs a potable supply, but no
9 doubt there was a potable supply anyway, going into
10 Shotton Paper.

11 MR BEARD: Well, madam, it says:

12 "Within that, yes, we'd be looking to negotiate, as
13 we are today in the process of negotiation with
14 Dwr Cymru, what the terms for a back-up potable supply
15 would be. Those negotiations would look at reserve
16 volume."

17 There is no other way of reading that than it is to
18 do with back-up potable supply.

19 Actually at the time, even Dr Bryan was recognising
20 that back-up potable supply was required.

21 I'm conscious of the time. Perhaps this is
22 a convenient moment?

23 THE CHAIRMAN: Yes, we'll come back at 11.25.

24 (11.18 am)

25 (A short break)

1 (11.26 am)

2 MR BEARD: Just one quick point on the non-potable back-up
3 point that we were dealing with just before the short
4 break. If you go to bundle 16, tab 19, please.

5 It is just worth recalling where we are. This is
6 also in the run-up to the referred work. One of the
7 arguments that's going on is whether or not a cost for
8 reservation of bulk supply should or should not be
9 within the FAP. Now, of course what we know is that in
10 the referred work Ofwat included it, and in the Tribunal
11 decision it was said: wrong. But actually there was no
12 dispute that the 4.4p was the relevant cost.

13 Just here at tab 19, we've got a letter from Albion
14 Water to Ofwat, and if you turn over to 6390, it says:

15 "There are of course significant uncertainties in
16 the calculation of cost of any back-up potable supply
17 because, as we've demonstrated, that supply I only
18 available when it is surplus to Dwr Cymru's prevailing
19 operational demand. There is no sense in which it has
20 ever been treated as a dedicated 24/7 resource, and
21 a short-run marginal cost approach might therefore be
22 more appropriate if Ofwat is to attempt a valuation.
23 That complexity is, however, avoided if Ofwat accepts
24 our arguments and the contemporaneous evidence that such
25 a supply was never part of the non-potable service and

1 was not required as part of the common carriage service
2 and wasn't included in the FAP."

3 So what's being said here is: there are
4 complications in relation to the calculation of that
5 reserve bulk apply. You can step around those by just
6 saying "don't include it in the FAP", which is
7 eventually what the Tribunal did. But the predicate of
8 that submission is: yes, there is an exercise to be
9 undertaken as to the relevant cost of the reservation of
10 back-up supply. So that is what is being put there.

11 So that's consistent with the approach that everyone
12 is recognising, that there is in fact a cost of
13 reservation which is what Ofwat was doing, and then
14 there is the question of how much it was and there was
15 also the argument about whether or not it should be
16 included.

17 Just for completeness for your references, if you
18 turn over to tab 20, this is the points of dispute in
19 relation to the final report. So this was put as
20 a Scott schedule, effectively. The first one is:

21 "The cost of back-up supply shouldn't be included in
22 an AAC analysis" is Albion's point of dispute. Not
23 there was no cost associated with it, but you should
24 exclude it.

25 I won't take you through all of that, but at leisure

1 the Tribunal may want to have a look at that.

2 So we say there is a cost associated with it, that
3 was identified by Ofwat, and the best figures we have
4 for it are obviously the Ofwat figures at 4.4p.

5 I'll move on swiftly to extra --

6 MR LANDERS: I'm sorry, can I just check. Is it agreed by
7 all parties that this statement on 6390, from Dr Bryan,
8 the back-up supply was not required, it was no longer
9 valid? Are all parties agreeing that it is required and
10 the question is --

11 (The tribunal discuss).

12 THE CHAIRMAN: Yes, it's now accepted that it is not
13 included in the 14.4p, or whatever, or 16.5p.

14 MR BEARD: Yes. There is no doubt about that. That was the
15 outturn of the Tribunal's approach. It chopped out some
16 of the costs that Ofwat have identified, and we're not
17 revisiting that. We're saying the fact that they're
18 chopped out of the FAP price doesn't mean they just
19 disappear as relevant costs; they've got to be covered
20 one way or another. Ofwat had identified them. It had
21 built them into the common carriage price. We recognise
22 that was the wrong way of doing it, because the Tribunal
23 has told us that, but that doesn't mean they just
24 evaporate, it just becomes costless.

25 MR LANDERS: So how are they paid for? You're suggesting

1 they be paid for as an additional element?

2 MR BEARD: Yes, they've got to be dealt with as such.

3 MR LANDERS: That's what I'm saying. It says in here that

4 they are not required. You are saying they are required

5 and they must be paid for as an additional element?

6 MR BEARD: Yes.

7 MR LANDERS: Okay.

8 MR BEARD: That's what Dr Bryan was saying when he said, "We

9 need that back-up supply", and what we're saying is

10 Ofwat was recognising that, but it was categorising it

11 in the wrong way.

12 MR LANDERS: But at the time of the document we've just

13 read, he was saying it was not required. He is now

14 saying, "We are saying that the current position is that

15 it is required"?

16 MR BEARD: No, he's saying there that it is not required to

17 be included in the FAP.

18 MR SHARPE: I wonder, just to clarify our position, back-up

19 is uncontentionous. The issue is whether it should be

20 reserved. They should put aside significant volumes of

21 water for the exclusive use when required, and just for

22 the avoidance of any doubt at all, our case is simply

23 this: that reserved capacity was never required, never

24 called upon and shouldn't be paid for.

25 THE CHAIRMAN: The back-up supply is required.

1 MR SHARPE: Back-up supply of itself is required and is paid
2 for, and under the potable rate. But the issue between
3 us at the moment rests upon whether or not they should
4 incur significant sums of money in order to reserve that
5 supply for the use of Albion. And that has never been,
6 to be absolutely clear, a part of Albion's case, that
7 there has been reserve supply. And it remains our case,
8 that this was a service on offer that was never
9 required, and therefore should never be paid. I hope
10 that's --

11 THE CHAIRMAN: Yes.

12 MR BEARD: And our position is simply that there is a cost
13 attached to ensuring that service available and that's
14 additional to the particular flow rate price. And we
15 say the best way you can quantify that cost is by
16 reference to the 4.4p which Ofwat says was the relevant
17 cost.

18 THE CHAIRMAN: So really the question for us is: if
19 Dwr Cymru had said, "What's on offer is the reservation
20 of 8 megalitres a day supply at the cost of £292,000",
21 or whatever it is, would Albion have said, "Right,
22 that's what we need and that's what we'll pay for it",
23 or would they have said, "Thanks but no thanks"?

24 MR BEARD: Yes, the issue though is that you've got
25 a contractual provision that requires that to be

1 available.

2 MR LANDERS: In the Second Bulk Supply Agreement?

3 MR BEARD: Yes.

4 THE CHAIRMAN: Yes. But the question is whether they would
5 have wanted to carry forward that contractual obligation
6 under the new arrangements if such new arrangements had
7 been entered into.

8 MR BEARD: Well, clearly we're dealing with
9 a counter-factual situation, but in circumstances where,
10 at the time, it was clearly necessary for there to be
11 that contractual provision in relation to bulk supply.
12 We don't understand why it is that you then look at the
13 situation 10 years later and say actually that's the
14 better comparator as to what it is you would have
15 actually needed at the relevant time.

16 THE CHAIRMAN: No, I am just at the moment trying to
17 identify what the question we should be asking
18 ourselves is.

19 MR BEARD: Just for your reference, in the judgment on
20 unfair pricing, what the Tribunal concluded at
21 paragraph 177 was that:

22 "The evidence leads us to conclude that the
23 provision and costs of the back-up supply would have
24 been included as part of a separate potable bulk supply
25 agreement."

1 I'm going to move on now, unless there are further
2 issues in relation to back-up, to extra capacity. Here,
3 again, I'm going to follow closely the written closing
4 which, on this topic, begins at page 51.

5 THE CHAIRMAN: Yes. We have read your written closing on
6 this point, so you really only need say additional
7 points, if there are any.

8 MR BEARD: I think what we've got is a situation where it is
9 accepted that if there are these two sets of
10 entitlements and they can be drawn down, then you would
11 need extra capacity.

12 Mr Edwards has said, "Well, look, we wouldn't just
13 sort of give this up for free, there is possibility you
14 might have to pay us but that's not being taken into
15 account". It is clear that it was important that there
16 was sufficient capacity, and that's referred to in
17 particular in that letter from Shotton Paper which we've
18 quoted at paragraph 205. If you weren't going to be
19 effectively buying out that entitlement, then you would
20 need to augment capacity.

21 Mr Sharpe says, ah no, well, there wouldn't actually
22 be any use for Dwr Cymru in relation to its entitlement.
23 It wouldn't take it, and therefore there would be no
24 reason to take that further step of incurring capacity
25 augmentation costs. And his only theory there was that

1 we'd be hanging on to the entitlement so that we could
2 then bid again for Shotton in due course.

3 We say that is not the reality, as was made clear in
4 particular by Ms White as an independent witness. When
5 you carry out a cost benefit analysis of what you would
6 do with a large supply of water, if you've got
7 30 megalitres a day available to you rather than ten,
8 the economics of what you do with it are very different,
9 and Dwr Cymru accept entirely that it didn't go into the
10 details of what it could do with that water. But it
11 doesn't accept it would be merely sitting on an
12 entitlement; it would want to be able to use those. It
13 may well have to incur some capital cost in order to be
14 able to use those resources, but those are very valuable
15 water resources to it, given the terms that it was able
16 to acquire the water.

17 The cheapness of that water is emphasised by the
18 fact that it was a take or pay agreement, and therefore
19 it is only the marginal cost that it would incur in
20 taking that and using it. Therefore, you've got some
21 cost in relation to the resource, a very low marginal
22 cost, a very large amount of water, you've got a very
23 large incentive to do something with it in those
24 circumstances.

25 THE CHAIRMAN: If you had done something with it and then

1 Albion dropped out of the picture, you would then have
2 put yourself in the position where you couldn't supply
3 Shotton Paper again, or would that have mattered?

4 MR BEARD: Well, if we'd have taken our entitlement and
5 supplied other people with it and used it elsewhere, the
6 question would be what would be happening in relation to
7 the volume of water that was abstracted, because if
8 Albion weren't supplying Shotton Paper in relation to
9 this, then they wouldn't be taking the water.

10 THE CHAIRMAN: Well, they might, they might --

11 MR BEARD: Well, they may well want to do the same sort of
12 thing, in which case there would be an argument about
13 the extent to which there were issues relating to the
14 abstraction licence and the scope for augmentation of
15 the abstraction licence.

16 As we know, the complexities about how you deal with
17 the abstraction licence depend upon where water is being
18 taken at different points as well as the absolute level
19 at Heronbridge. So in those circumstances, it would be
20 wrong to say we would have foreclosed ourselves from
21 being able to deal with Shotton, but in any event, if
22 what we'd done is invested so that we had a profitable
23 use for the water elsewhere, it may well just be an
24 opportunity foregone once those costs are sunk and we're
25 actually making money elsewhere using that water and

1 that resource. That may just be the consequence of it.

2 Then, if I move on to the £50,000 rather than
3 £25,000 adjustment which is at page 55, I'm not going to
4 go through and supplement anything you've said. I think
5 there's just a mistake there on the part of Albion.
6 When we get to benefit share, however, I am going to try
7 to untangle some of the mysteries that relate to how the
8 benefit share mechanism works.

9 If I may, in relation to benefit share, could I turn
10 to the claim form in bundle 10, tab 1, page 3329. I'm
11 very cautious to say I'm going to try to untangle some
12 of the mysteries of the benefit share because they are
13 many and multifarious.

14 If we start with paragraphs 112 and 113 of the claim
15 form, what we have is an articulation of what is being
16 said here to be possible approaches to the assessment of
17 quantum. And what is set out in annex 1 are a series of
18 tables, and what's described in 112 are what's going on
19 to some extent in those tables.

20 So option 1 is trying to quantify the damage alleged
21 to be suffered by Albion as the difference between what
22 Albion has in fact paid Dwr Cymru under the bulk supply
23 arrangements, as compared with what the claimant would
24 have paid the defendant for common carriage pursuant to
25 a non-abusive first access price, and the United

1 Utilities price for water.

2 What we see -- I won't take you to the table -- is
3 this one saying 14.4p, no indexation for the common
4 carriage, and then 3p for the United Utilities water
5 resource. So it is effectively the best case they can
6 possibly imagine.

7 Then option 2 is the same comparator, but using
8 14.4p indexed by PPI.

9 Option 3 is 14.4p for common carriage, no
10 indexation, and then 9p for United Utilities water.

11 Then option 4 is 14.4 indexed, but again by PPI, and
12 then 9p for United Utilities.

13 What is going on here is a comparison between what's
14 actually being paid by Albion and what they say they
15 would have paid in the counter-factual world.

16 Well, we disagree with the figures being used, but
17 we can see how that works as a quantum mechanism. The
18 mystery then starts happening when you look at the
19 A versions of the options, because the A versions of the
20 options are said to take into account benefit share
21 arrangements.

22 What you see under paragraph 113A are the sums
23 claimed under the options set out above. Now, option 1,
24 difference in price paid, three and something million
25 pounds. Well, that's their best case, so you'd expect

1 that to be the highest, and when you've got a benefit
2 share, you'd also expect the benefit share equivalent of
3 that to be lower.

4 Then in option 2, because it's not quite so good for
5 Albion on its pricing assumptions, you get a bit of
6 a lower difference, and again, you'd expect, if you
7 share some of those benefits, then the equivalent
8 option 2A table will be lower.

9 Then you get to option 3, so again, the difference
10 in price paid using the ordinary or option 3 is lower,
11 because the prices aren't so advantageous to Albion.
12 But then something weird happens, because rather than
13 the benefit share generating a lower quantum, it
14 generates a higher quantum. And the same thing then
15 happens in relation to option 4, the lower figure is
16 actually in relation to the difference in price paid
17 without the benefit share.

18 Now, it doesn't, on the face of it, look entirely
19 explicable that if you've got a sensible damages
20 calculation between what you actually paid and what you
21 should have paid, but if you shared benefits in relation
22 to that, somehow you're able to claim for. That, as
23 a starting point, feels rather strange. Indeed, we were
24 a bit mystified about it. Of course, there is
25 a distinct lack of explanation as to how these tables

1 properly work.

2 THE CHAIRMAN: I thought Mr Pickford had worked that out.

3 MR BEARD: Yes, I think Mr Pickford has worked it out.

4 I was then going to go to the skeleton at bundle 11,
5 tab 2, if I may.

6 If we could go to external page numbering 3488GG so
7 here, there's an attempt by Dwr Cymru to understand
8 what's going on and why it is you get this very, very
9 odd result in the table. And if you turn on to
10 page 3488HH, 119 says:

11 "Notwithstanding the difficulty of penetrating
12 Albion's annexes, it is apparent there is a significant
13 flaw in the Option 4A calculation. The driving force behind
14 the high figures generated under option 4A is that it
15 subtracts Albion's costs under the common carriage
16 agreement in the counterfactual scenario from
17 Dwr Cymru's non-potable tariff in the counter-factual
18 scenario [which is correctly assumed to be the same as
19 in the factual scenario] and adds 30 per cent of the
20 difference as profit for Albion."

21 Just jump down to 121:

22 "Illustrated graphically below... what Albion is
23 saying is that as a result of the infringement, it lost
24 30 per cent of the share of the green and yellow areas
25 combined."

1 We have to turn over and you see the diagram there.

2 THE CHAIRMAN: Yes.

3 MR BEARD: So what the options 1 to 4 do is they look at the
4 difference between Albion costs under bulk supply and
5 Albion's costs under common carriage, which is the
6 yellow area. It makes perfect sense.

7 What the A version seemed to be doing --

8 THE CHAIRMAN: We've got here -- oh, you've got one.

9 MR BEARD: I'm sorry.

10 THE CHAIRMAN: Yes, but I think we're familiar with this.

11 MR BEARD: The triangular bit is green, the parallelogram is
12 yellow just underneath it.

13 So the non-A tables carry out an orthodox comparison
14 of the two sets of costs. What the A tables do instead
15 is, in relation to the -- take the Dwr Cymru retail
16 tariff and then look at the gap between it and the
17 bottom line in the counterfactual world and attribute to
18 Albion 30 per cent of that to their profits. So this is
19 a remarkably curious benefit-share arrangement because
20 the effect of it is that as Dwr Cymru's retail tariff
21 goes up, the price to Shotton is apparently going up,
22 and that in those circumstances, you're getting more out
23 of the equation in the counter-factual world.

24 But as is pointed out in the skeleton argument, that
25 benefit share is in a contract in the real world. What

1 is not done in the calculation is taking into account
2 the effect of that benefit share in the real world. We
3 say that is plainly impermissible. But before I get to
4 the conclusion on that, can I go to the benefit-share
5 arrangement itself in the contract and just look at one
6 or two of the clauses.

7 It's in volume 2, tab 20. If we go to page 371,
8 "Consideration and payment":

9 "The customer shall pay the charges to Albion Water
10 provided that such charges are no higher than the
11 charges which would otherwise have been levied by
12 Dwr Cymru pursuant to the DCC agreement." The customer
13 shall pay the charges to Albion Water.

14 Then we have to turn back to the definition of
15 "charges" on 368:

16 "'The charges' means the charges payable by the
17 customer to Albion Water for the supply of water in
18 accordance with schedule 3."

19 Then we have to jump forward to page 378, to
20 schedule 3. Schedule 3 specifies the price conditions
21 and it says: non-potable water, 26p. And there's an
22 indexation provision in note 1. But it set a rate, so
23 the charges to be paid are the rates specified in
24 schedule 3.

25 Then if we go back from there to 7.4, which is this

1 benefit-sharing clause that has been relied upon:

2 "Albion Water shall use all reasonable endeavours to
3 provide the customer [Shotton] with the most
4 cost-effective source of water and in particular costs to
5 the customer lower than the non-potable source of supply
6 for the alternative non-potable source of supply."

7 And that alternative non-potable source of supply is
8 an alternative source of water not using Heronbridge.

9 "And the most cost-effective treatment of waste
10 water, including the possibilities of effluent water
11 sales. The savings in the cost of supply or services or
12 incremental revenues net of financing and operating
13 costs arising from such initiatives as may be agreed
14 between the parties shall be shared between the customer
15 and Albion Water in the proportion of 70/30
16 respectively."

17 What we've got is a situation where the price being
18 paid is the schedule 3 price, and you've got
19 a benefit-share arrangement which appears to benchmark
20 off the prices charged under the contract. That's the
21 schedule 3 price, because that's the sensible way to
22 interpret savings here. It is not related to any third
23 party prices at all.

24 What Dr Bryan said -- and this makes it all the more
25 mystifying -- is that the way he would capture the

1 benefit share would be by adjusting the price on an
2 annual basis, and yet we've seen that that's not the
3 mechanism that's built into schedule 3 at all.

4 THE CHAIRMAN: Isn't it paragraph 1, subparagraph (ii):

5 "... percentage movement in the volumetric tariff
6 for potable water in DCC scheme of charges compared with
7 the previous year"?

8 MR BEARD: I'm sorry, in relation to schedule 3?

9 THE CHAIRMAN: Yes, the first subparagraph in the third line
10 there is an alternative:

11 "The percentage movement in the volumetric tariff
12 for potable water in DCC's scheme of charges for the
13 year commencing on the previous 1st April."

14 MR BEARD: That's to do with the indexation.

15 THE CHAIRMAN: DCC is Dwr Cymru, isn't it?

16 MR BEARD: Yes. It's necessary to look at note 1 because
17 note 1 has a PPI index, or 2:

18 "The percentage movement in the volumetric tariff of
19 potable water in DCC's scheme of charges for the year."

20 So 2 is referring to how you deal with little (ii)
21 in 1.

22 THE CHAIRMAN: But isn't it saying it will go up at the same
23 rate that DCC's charges go up, but then that will be
24 mitigated by the operation of clause 7(4) --

25 MR BEARD: Whichever is lower, yes. So you actually get

1 a divergence. We know you get a divergence between the
2 two over time. That's why it's represented on that
3 diagram as DCC's or Dwr Cymru's tariff, retail tariff,
4 moving above the level at which Albion was able to
5 price.

6 So if DCC's pricing was higher than PPI, then this
7 mechanism ensures that it's only the PPI move that
8 applies. But the way in which the benefit share is
9 being articulated is by reference to Dwr Cymru's retail
10 tariff, which wasn't the price that was specified in
11 schedule 3. And that is what is so bizarre about the
12 interpretation here, because effectively the
13 interpretation that has been put forward of the benefit
14 share unwinds the specific language of these provisions
15 in order to be running a comparator at a higher level,
16 and thereby take as the 30 per cent benefit share
17 a larger chunk.

18 MR LANDERS: So is the issue that the maths wouldn't work
19 unless that non-potable cost of 26p was the DC retail
20 tariff at the time this --

21 MR BEARD: That's how we read the contract. That's not how
22 it is being put forward now. It is worth bearing in
23 mind that when this case was originally pleaded this
24 benefit share argument wasn't put forward at all, and
25 certainly not in this way. It wasn't put forward at

1 all.

2 But now, this is an interpretation of a contract
3 which we find incredibly difficult to understand. It
4 has not been set out clearly and properly, and when we
5 look at the contract, we struggle to make any sense of
6 why it is you use as a benchmark for the benefit share
7 a tariff that is specifically being excluded where PPI
8 is lower than the change in the DC tariff.

9 What we say was going on here was that the
10 benefit-share arrangement was to do with reductions in
11 what it cost, effectively, Albion to supply Shotton, and
12 therefore savings that could be made to Shotton from the
13 price that was set for Shotton under schedule 3. That's
14 the straightforward reading of this and that's the way
15 it must operate.

16 So, for instance, if you find a new source of water
17 that was cheaper, a non-Heronbridge source, and
18 therefore you made savings, you then split those savings
19 as compared with the schedule 3 price 30/70. Similarly,
20 if you came up with some new whizzo scheme for
21 efficiency in relation to water supply and it is at
22 Albion's instigation not Shotton's, then you'd split the
23 benefit 30/70 vis à vis that price, not some other price
24 that you're not actually paying at Shotton, or wouldn't
25 otherwise be paying at Shotton.

1 Of course what we've set out in our closing, in
2 particular at paragraph 220, is that this approach that
3 we're articulating is actually consistent with the
4 evidence that had previously been given in these
5 proceedings and which is represented by relevant
6 documentary material.

7 If we go through 220, at 220.1, we've referred to a
8 document in folder 4 at 164, page 1026:

9 "Albion Water's contract with Shotton allows for the
10 recovery of all costs accrued to date plus 30 per cent
11 of any net benefit for improvements in supply cost.
12 These benefits will only be triggered by improvements in
13 costs."

14 And that emphasised portion runs contrary to
15 Dr Bryan's assertion that benefit share could be
16 triggered by, for example, an increase in Dwr Cymru's
17 non-potable tariff.

18 It's just worth mentioning here the indexation
19 provision that we were referring to is referencing the
20 scheme of charges which is concerned with potable
21 tariff, not non-potable. So we're talking about
22 a further remove here.

23 THE CHAIRMAN: Well, there wasn't a non-potable tariff,
24 that's --

25 MR BEARD: Well t,hat's another point we make here.

1 It's very odd, in circumstances where the document
2 at the time isn't concerned with a tariff that didn't
3 exist, that it is now being said that this is the way
4 you engineer the benefit share by reference to a tariff,
5 you calculate quantum by reference to a tariff that
6 didn't exist in relation to terms of a contract that are
7 supposedly to be carried over into the counter-factual
8 world.

9 This is also consistent with e-mails from Dr Bryan
10 to Shotton Paper. We've cited that at 220.2 in the closing statement:

11 "As soon as we get a new, definitive and fair price
12 for water, this will be reflected in a reduction in your
13 tariff to reflect the benefit-sharing agreement between
14 us."

15 So, again, it's always about reductions. It's not
16 about this move upwards by reason of what's going on in
17 relation to the Dwr Cymru non-potable tariff, which is
18 the basis on which this benefit share is supposed to
19 operate in the counter-factual world.

20 Mr Pickford took Dr Bryan in cross-examination to
21 evidence he'd given in the main hearing, where he
22 referred to, as a virtue, the savings being made as
23 being ones that "we can ascribe to our activities".
24 Again, that makes sense. If Albion are doing things to
25 reduce the cost to Shotton, then a benefit share can

1 operate. But if they're just sitting there and saying,
2 "Well, actually Dwr Cymru's price is rising, therefore
3 we should get more", there is no ascription of any
4 saving to Shotton there. In fact, Shotton is ending up
5 paying more. It is ending up paying more in the
6 counter-factual world than in the real world. And the
7 fact that that is the conclusion of this exercise just
8 indicates how preposterous it is.

9 There is no possible way that you can end up in
10 a situation where saying, "Well, because we suffered an
11 abuse and we were over-charged in relation to the FAP,
12 in the counter-factual world where we get a lower common
13 carriage price, you, oh Shotton, end up paying us more".

14 THE CHAIRMAN: Well, it's less more than they would have
15 paid if Albion had never appeared on the scene. That's
16 the argument.

17 MR BEARD: No, but its just more relative to what was being
18 paid, actually being paid in the real world.

19 MR LANDERS: Are you saying that this contract does not
20 produce the figures in the table on 3330 that we started
21 with in column A, or are you saying that it's an absurd
22 contract and shouldn't be used in a counter-factual?

23 MR BEARD: There are two things: one is it doesn't rightly
24 produce the relevant figures, but it is also important
25 for what is going on here.

1 If you're operating this benefit share, you have to
2 operate it in the correct way. We think it doesn't make
3 sense, as it has been articulated, and we don't
4 understand how the contract works. But actually, our
5 biggest concern is the fact that it's being operated on
6 this opportunistic, "Well, we'll read what we want into
7 it" approach, it doesn't fit with the language, and
8 we'll do that in the counter-factual world even though
9 the contract and the terms are in the real world. And
10 it's then being said: oh no, there's no benefit share in
11 the real world. Of course the impact of that is that it
12 widens the gap between the counter-factual world and the
13 real world.

14 THE CHAIRMAN: If you're right as to the interpretation of
15 the contract, then because Shotton in fact paid 26p
16 throughout the period, what is the real world effect of
17 the contract in the events that happened, and why does
18 that affect the calculation, given that credit has
19 already been given for the interim relief?

20 MR BEARD: The point is you can't run the counter-factual
21 against this other Dwr Cymru price. That's the wrong
22 price to be running.

23 THE CHAIRMAN: Yes. So what you would say is that in the
24 counterfactual world, once we've worked out what the
25 common carriage price would have been, what the water

1 price would have been, whether there would be these
2 other additional costs --

3 MR BEARD: Assuming there would actually have been a deal,
4 yes.

5 THE CHAIRMAN: -- assuming there'd been a deal, then we can
6 compare that price to the price under the
7 Albion-Dwr Cymru bulk supply agreement?

8 MR BEARD: Putting it in very simple terms --

9 THE CHAIRMAN: And then how does the profit share apply to
10 that?

11 MR BEARD: Effectively, what it is is the yellow
12 parallelogram in that diagram less Albion's costs, and
13 then 30 per cent of that. That's what the benefit share
14 does. And that's the way it should operate here.

15 Making up these other prices which result in
16 preposterous outcomes that are unrelated to the terms of
17 the contract is just wrong. It cannot be the right
18 approach to a quantification of damages in this case.
19 If you do it in that way, you ensure you don't get the
20 eccentricities of Shotton Paper actually paying more in
21 the counter-factual world than it would pay in the real
22 world -- than it actually did pay in the real world,
23 which is an outcome that simply cannot be one that makes
24 any sense at all.

25 THE CHAIRMAN: In the counter-factual world, benefit share

1 would be set off against the price to Shotton actually
2 increasing in the indexed way you say is set out in
3 schedule 3. So you would have to take into account that
4 the revenue in the counter-factual world would have gone
5 up by either PPI or by the alternative. In the
6 counter-factual world, Shotton Paper wouldn't have just
7 kept paying the 26p that they had paid during the course
8 of the litigation.

9 MR BEARD: I think we accept, and I don't think there's an
10 issue about the price going upwards. We recognise that,
11 but it went up in the real world ... so you've got the
12 real world price moving up. That's a parallelogram
13 rather than just a rectangle.

14 THE CHAIRMAN: What is the price increase, then, that you've
15 applied in that parallelogram?

16 MR BEARD: Oh sorry, the parallelogram is just illustrative,
17 it's stylised. We're trying to capture what was going
18 on. What I think is going on in relation to the
19 modelling exercise is trying to capture the details of
20 how you properly apply the benefit share on the various
21 different assumptions. We haven't attempted to do
22 a specific calculation model doing this. What we're
23 trying to illustrate is why there's a fundamental
24 problem with the basis on which the A table approach has
25 operated in relation to the quantification of damages,

1 because the benefit-share arrangement has been applied
2 wrongly and inconsistently, and there was some story
3 being told that somehow Albion was constrained from
4 being able to take account of the benefit share in the
5 real world and that that meant that somehow it shouldn't
6 be taken into account.

7 Well, that just is not right either. You can't rely
8 on the fact that you don't press a contractual
9 entitlement in these circumstances against Shotton in
10 order to voluntarily effectively increase the level of
11 damages claim that you have against somebody. There is
12 no basis for that approach at all. There is no basis to
13 consider they couldn't have enforced it.

14 Indeed, one of the things that would be very
15 troubling if that were the line to be followed, was that
16 this wasn't a matter that was articulated at all at the
17 time of the interim relief application, and of course
18 that would be highly material to any application for
19 interim relief because if you could come along and say
20 actually, you know, there was headroom under a contract
21 in relation to Shotton Paper, then that is something you
22 really should have made very clear to the Tribunal.

23 THE CHAIRMAN: But as I understand it, the price that
24 Shotton -- do we have the information about the price
25 that Shotton Paper in fact paid to Albion?

1 MR BEARD: Yes.

2 THE CHAIRMAN: Over the --

3 MR BEARD: I don't have it at my fingertips, but we do.

4 I think it is actually in all of the relevant
5 spreadsheets. I think those specific numerical issues,
6 there have been lots of exchanges, because Albion put
7 forward this specific material and we struggled to
8 understand it, and there were myriad requests to
9 understand what was going on. And Albion made numerous
10 corrections to its spreadsheets because of what we were
11 identifying as queries in relation to them. But in
12 relation to various of the numerical issues, there will
13 be agreement on levels of pricing.

14 Now, we heard yesterday that there are going to be
15 issues about invoices being provided and justifications
16 for the price. But leaving that to one side, we think
17 that some of those factual issues about what actual
18 prices were paid may well be well resolvable in the
19 model. So I'm not sure how much necessarily the
20 Tribunal wants to go into the details of that. That's
21 why we included the stylised diagram in the skeleton,
22 because we were trying to move away from arguing the
23 toss about particular numbers to cut through to the
24 essence of the concern we have about the way in which
25 the benefit share is being operated.

1 THE CHAIRMAN: Yes.

2 MR BEARD: I think rather than rehashing anything, I would
3 just commend to the Tribunal our closing at
4 paragraphs 215 through to, in particular, 230, setting
5 out the two sets of concerns here: One to do with
6 interpretation of the contract and how it has been put
7 forward by Albion; and the second important issue about
8 how it must operate in the real and counter-factual
9 world and affect the way in which the quantum of damages
10 is calculated. But I won't rehearse those again.

11 THE CHAIRMAN: The second point, the top triangle rather
12 than the parallelogram, is that a point that's only
13 relevant on Albion's interpretation of the agreement?

14 MR BEARD: Yes. I think that's right.

15 THE CHAIRMAN: You may want to think about it.

16 MR BEARD: I think the answer is still yes, but I think
17 there may be a series of rather technical caveats to the
18 "yes". Maybe I'll come back after the short adjournment
19 on that.

20 Unless I can assist further on benefit share at the
21 moment, I was going to move on.

22 THE CHAIRMAN: No.

23 MR BEARD: There is then the issue about grossing up, which
24 I hope I can deal with more quickly. That's dealt with
25 in the closing at 62, page 62 to 64. The position is

1 very simple: entering into an agreement about what
2 you're going to do with damages has no effect on what
3 damages you get. That's the end of this. If you've
4 agreed with someone that you're going to share some of
5 your damages with them, fine. There's no issue arises.
6 You can do that. But that doesn't mean that you change
7 the value of the damages you can claim and somehow say,
8 "Well, I'd like to put myself in the position that I'd
9 get more damages in order to be able to pay off them and
10 still be in the money, because I don't quite like the
11 way in which that agreement has panned out."

12 In the submissions we've set out what might loosely
13 be called a "money tree example" at paragraph 238, whereby
14 if this grossing up argument works, if you take it to
15 the extreme, if Albion had agreed to give almost all of
16 its damages to Shotton, it could turn up and say, "Well,
17 my total loss, the 100 per cent loss, was £1 million.
18 I've agreed to give 99.9 per cent of it away, so in
19 order to get myself into the position where I can give
20 99.9 per cent of it away but still end up with the same
21 level of damages to me as the total claim I've got,
22 well, I'm going to have to have nearly £1 billion-worth
23 of damages."

24 I mean, that's the reduction ad absurdum version, but
25 the point is pretty straightforward. It doesn't matter

1 whether it is an amendment to a strange clause in
2 a contract, or what it is. Albion may have just made
3 a legal mistake as to what they were thinking they were
4 doing there and how they thought it would operate, but
5 the law is really straightforward. There's just no
6 issue. There is no scope for grossing up here. So
7 unless I can assist the Tribunal further in relation to
8 that, I'll move on.

9 Voluntary uplift. Again, if I may, I'll just refer
10 briefly to the written closing submissions, page 64.
11 This is the idea that Shotton effectively paid Albion
12 more during a certain period, and that this shouldn't be
13 taken into account in the damages claim.

14 Well, if your downstream customer pays you more
15 during the relevant period, that does have to be taken
16 into account. Effectively, any loss you've got has been
17 passed on to them to that extent. They may have
18 a claim, an indirect effective person, but it doesn't
19 mean that you can claim on their behalf.

20 THE CHAIRMAN: But if it was really the case that Shotton
21 Paper were prepared to pay 3p more as the price of the
22 water, why was there a finding of a margin squeeze,
23 because then there was that difference between -- in the
24 margin squeeze, the top level of the squeeze is assumed
25 to be Dwr Cymru's price to Shotton Paper of 26p, because

1 it's assumed that Shotton Paper won't pay Albion more
2 than that?

3 MR BEARD: I think it's important, it's a temporal issue,
4 isn't it, here, that what was found was that the FAP at
5 the time imposed a marginal squeeze and at that time
6 there wasn't any payment coming in from Shotton.

7 So if you'd had a situation where Shotton had been
8 paying, it's possible that the assessment might have
9 been different. So there just isn't a judgment in
10 relation to that. I think it's just a timing point in
11 relation to those issues. It doesn't advance matters
12 at all.

13 I think the point that was being suggested was that
14 somehow this was a bank loan, and therefore it was
15 repayable. But that doesn't work either, because it's
16 not an orthodox loan by any manner of means. What it is
17 is a provision of money that is apparently contingent on
18 the acquisition of damages, and it then gets paid back
19 if it has been picked up in the damages.

20 Now, again, it is in a way a species of the grossing
21 up issue. You can't enter into arrangements related to
22 damages that you are seeking on the basis that if you
23 get those damages, you'll somehow pay them back, and
24 therefore that increases the level of damages you can
25 obtain. There's a circularity there.

1 So it isn't an orthodox financial arrangement by any
2 manner of means. What it is is just a reduction that
3 has to be taken into account. Yes, Shotton could claim
4 for it, if that's the law that indirect purchasers can
5 claim, and so on and so forth, and we accept that for
6 these purposes that would be the right way to consider
7 those matters and that's what's talked about in
8 Devenish. But it's not a matter that lies with Albion.

9 Sorry, yes, Mr Pickford notes that, Madam Chairman,
10 you posed a question on Day 2 about voluntary uplifts
11 and 70 per cent benefit shares and whether or not
12 Shotton could claim for both, and the answer is yes.
13 I'm not actually sure that's contentious, but that's
14 undoubtedly the answer.

15 Then I'm going to move on briefly --

16 MR SHARPE: For the avoidance of any doubt, of course it is
17 contentious because it is an erroneous legal submission.
18 I just leave it there.

19 MR BEARD: I'm sorry, I'm not suggesting that there aren't
20 contentions about the operation of the benefit share.
21 The only point I was making was that if these matters
22 fell to Shotton, it would be able to claim. But I'm
23 sure Mr Sharpe will make his case in due course.

24 Let's move on to page 66, the interim relief
25 benefit. I think this may just be a miscalculation.

1 I'm not going to go through that in any detail. You
2 have our submissions there in relation to those matters.

3 I'll instead move on to issues to do with timing,
4 and the second access price, if I may.

5 THE CHAIRMAN: We have your submissions on that. So again,
6 I'd -- [overspeaking] -- additional.

7 MR BEARD: Yes, I'm happy to move through that.

8 I think, in relation to the second access price, it
9 is just worth emphasising a couple of points in relation
10 to it. So if we could turn on to page 71, where the
11 issue arises about whether the second access price broke
12 the chain of causation or operated effectively to
13 mitigate loss.

14 I think one thing that was really helpful to note,
15 and we've set it out in paragraphs 274 and 275, is
16 actually the similarity in wording between the FAP and
17 the SAP, because if you read 275 -- and it hadn't been
18 set out that this was the FAP letter -- you might be
19 forgiven for thinking that all of those concerns that
20 were expressed by Dr Bryan and his counsel as to the
21 certainty or uncertainty of the SAP would be entirely
22 reflected in the FAP itself.

23 So the uncertainty issue is really not a good one at
24 all, minded to:

25 "... charges in FAP could be in the SAP. Concerns

1 about no charges being made for administration and these
2 being matters for further consideration ... similar
3 application should be made in the SAP ... starting point
4 for new application wouldn't include other
5 administrative or associated costs."

6 But it's more than that. We've seen through the
7 various bits and pieces of correspondence and documents,
8 the extent to which Albion was constantly trying to
9 latch on to different prices and what it suspected were
10 different prices, whether at Corus or elsewhere, and
11 immediately focusing on what was of concern to it and
12 whether they could use them and exploit them. Even if
13 they hadn't ever been sent to them, even if they were
14 speculative prices and they were essentially just
15 plucking them from what they assumed was their knowledge
16 about particular systems or arrangements.

17 So the point that was made that the SAP was
18 originally sent to Ofwat and then sent on and provided
19 to Albion in due course doesn't assist Dr Bryan and
20 Albion at all. It is completely obvious that he
21 recognised that this was the sort of price that may well
22 have been of real interest to him if he really cared
23 about common carriage. And indeed, at 277, Dr Bryan
24 acknowledged in cross-examination at the time when he
25 received the SAP letter, that he considered the price

1 therein to be sufficiently certain.

2 There's a reference there to his diary entry.

3 You'll see the quote. Mr Pickford was cross-examining
4 on the diary entry for 18 March 2004:

5 "Question: Do you see that?

6 "Answer: Yes.

7 "Question: The very first thing you say (so this
8 is the day after having received the SAP) is
9 confirmation of Dwr Cymru's reduced access charge?

10 "Answer: Yes.

11 "Question: There's nothing in your note here that
12 complains about it being far too uncertain to be able
13 to make head or tail of that, or that you just didn't
14 really know that they were up to?

15 "Answer: No, I took that letter at face value.

16 "Dr Bryan also accepted that nothing in
17 the SAP itself prevented Albion from negotiating and
18 ultimately entering into a common carriage agreement."

19 We've again quoted two extracts from the transcript,
20 and what is clear is that although they knew this was
21 a relevant price, although this is something that should
22 and could have been taken into account and must be taken
23 into account in the assessment and quantification of
24 damages, Dr Bryan was simply saying that it was a lower
25 priority than bulk supply. "That was what stopped us."

1 That doesn't mean that it isn't relevant to
2 mitigation and the relevant time over which damages
3 should be claimed. To the contrary, that suggests that
4 it is important for those purposes. That opportunity
5 was open to Albion, they knew about the opportunity,
6 they knew about that price, they knew it was a serious
7 price. They could have taken it if they had so wanted.
8 It must be taken into account in assessing the relevant
9 quantum and period of the relevant damages.

10 Indeed, although we haven't set it out in the
11 closing, Dr Bryan repeatedly refused to address the
12 question posed to him that there was nothing preventing
13 him from engaging with Dwr Cymru if he was really
14 interested in the price. There are about 12 pages of
15 that at Day 4 of the transcript, pages 108 to 120. He
16 just had no good answer in relation to those matters.

17 I will then, therefore, turn to issues concerning
18 the Corus claim, unless there are any other particular
19 questions in relation to quantum in relation to the
20 Shotton Paper claim.

21 Again, you will have seen what's set out in our
22 written closing submissions. The Tribunal has
23 previously described this claim as "somewhat tenuous",
24 and as we've emphasised, we didn't see it as improved
25 over time. There's a preliminary point: it's got to be

1 remembered that there has been no finding of abuse in
2 respect of Corus, so it follows that the Tribunal must
3 assume that had Albion in fact sought an access price in
4 respect of Corus from Dwr Cymru it would have been
5 granted a lawful price, and that no damages could in
6 those circumstances follow in respect of Corus in any
7 event. That would mean, therefore, that Albion's case
8 has to be that the FAP caused Albion not to be in
9 a position to seek an access price from Dwr Cymru some
10 three years after the FAP, and it thereby suffered loss.

11 But Albion is really unable to establish that, for a
12 number of reasons. The loss of profit claims that it's
13 making here just didn't prevent it from enquiring about
14 Corus and getting a price. Indeed, one of the
15 interesting questions that isn't really considered is it
16 could have asked for a common carriage price, it could
17 actually have asked for a bulk supply price in relation
18 to these matters. Indeed, it did ask for two bulk
19 supply prices in relation to Corus, as we will come on
20 and see.

21 One of the points that was being considered was the
22 impact of the FAP on Pennon's ownership of Albion. It
23 is a fantastically remote causal connection that is put
24 in place, stating that because of the FAP and the
25 interaction with the regulator, and because you're

1 having to deal with the regulator, Pennon no longer even
2 wanted to own Albion. All we have is Dr Bryan's
3 assertion; we have nothing from Pennon in relation to
4 this.

5 But more than that, it is hugely remote and causally
6 insubstantial because no serious capital investment of
7 cash flow was required in order for Albion to be able to
8 tender to Corus in relation to these matters. There was
9 nothing stopping Albion, even during the course of these
10 difficulties with Pennon, from actually talking to Corus
11 about the way things would work. Yes, there may have
12 been issues to do with the precise inset appointment,
13 but if there was really a proper deal to be done, the
14 fact that there was a collateral battle going on in
15 relation to other issues with Ofwat didn't prevent
16 Albion from engaging with Corus.

17 What we see is just a lack of engagement with Corus.
18 Now, it's important to bear in mind that by the time
19 we're talking about dealings with Corus in 2003, of
20 course Albion was aware that Dwr Cymru's new non-potable
21 industrial tariffs had been produced and that had
22 implications for the way that you might approach issues
23 to do with common carriage as compared with the FAP.

24 So in those circumstances, knowing that there'd been
25 a new way of looking at industrial tariffs, it is

1 perhaps all the more remarkable that, in the
2 circumstances, we didn't have a situation where Albion,
3 if it really had any chance of getting Corus, wasn't
4 pressing this point and asking for more details and
5 asking for common carriage prices or asking for bulk
6 supply prices.

7 THE CHAIRMAN: I thought Dwr Cymru have always set its face
8 against any argument that the fact that the costs of
9 common carriage should feed through into the bulk supply
10 agreement. I thought that that was something that was
11 dealt with in the remedies judgment, and that this panel
12 or the previous panel that had to hand down a ruling
13 saying that that wasn't something that could -- the idea
14 that Dwr Cymru would have read across the reasonable
15 common carriage price into the bulk supply price was not
16 something that was --

17 MR BEARD: No, but we've got to bear in mind that what we're
18 talking about is pitching to Corus, which could have
19 been in relation to bulk supply prices as well.

20 THE CHAIRMAN: Yes, but I thought what you were saying is
21 that we have to assume that if they had asked for a
22 common carriage price, they would have got a much lower
23 common carriage price than 23.2, and that if they had
24 asked for a bulk supply price, that we have to assume
25 that that bulk supply price would have been less than

1 the --

2 MR BEARD: I'm not going as far as that. What I'm saying is
3 that what had happened was that there had been
4 a consideration of things like treatment costs in
5 relation to the non-potable industrial tariffs, which,
6 if Dwr Cymru was genuinely interested in the way that
7 Corus might deal with it, would have suggested that
8 Albion would have been back seeking further information
9 about how it could have dealt with Corus. Because of
10 course, Albion, throughout, has said the two things were
11 linked because that was the proposition that it was
12 putting to the Tribunal.

13 So what we're asking ourselves is: was Albion really
14 going after this Corus business? You had a set of
15 tariffs being produced. On its approach, they should
16 have been linked, you should have been looking at these
17 sorts of things, and yet no noise.

18 So we're looking at the way that Albion approaches
19 this, not the way that Dwr Cymru dealt with it. Because
20 what we're asking ourselves is: was Albion really
21 serious about Corus at all? We raise the question
22 whether it was really serious about Corus at all in
23 circumstances where the costs of pursuing it at least at
24 a preliminary stage were negligible. It wasn't
25 prevented by inset appointments. This account of Pennon

1 is a smokescreen in relation to these issues. There
2 were all sorts of issues going on in relation to
3 industrial tariffs which Albion thought were terribly
4 interesting and impacted upon the way that these matters
5 should be dealt with, and yet still we have silence from
6 them in relation to these matters.

7 The second point to emphasise is that Corus, when it
8 talked to Albion about these matters -- and the relevant
9 very brief letter is at bundle 5, tab 204; I won't take
10 you to it -- invited Albion to bid for the supply of
11 water to three of Corus's larger plants situated in
12 Wales, namely Llanwern, Troste and Shotton. So what
13 Corus were interested in was a negotiation to supply all
14 of them.

15 THE CHAIRMAN: Are all of them supplied by Dwr Cymru,
16 currently?

17 MR BEARD: Yes.

18 THE CHAIRMAN: And is the litigation about the price that
19 Mr Sharpe referred us to, is that in relation to the
20 price paid at all three sites?

21 MR BEARD: Yes, I understand that it is. I will come back
22 and confirm. My understanding was that all three prices
23 were at issue, whether it is with the regulator or in
24 the litigation itself. But I will confirm with those
25 that are specifically involved in that matter.

1 But yes. So they're saying, "Come on, supply all
2 three of our plants in this area" and what we know is
3 that Albion took no steps at that time in relation to
4 anything to do with, in particular, Llanwern, which is
5 the largest and most profitable, or potentially most
6 profitable, indeed, we saw Dr Bryan's diary entries in
7 the meeting the day before the letter which indicated he
8 was well aware that that was the most profitable of
9 them.

10 So the idea that Albion was really interested in the
11 Corus business when it did nothing at all about the most
12 profitable of the three plants, knowing that Corus was
13 interested in a supply for all three plants because that
14 would have substituted in for Dwr Cymru in toto, is just
15 fanciful.

16 There is no basis on which this Tribunal can find
17 that there was any real chance at all that Albion was
18 going to be able to bid for that package of plants that
19 Corus was saying, "Come on, give us an offer for it. We
20 want someone else here. We don't just want Dwr Cymru in
21 this, but we want all three plants dealt with."

22 Indeed, I'll just give you references to Dr Bryan's
23 cross-examination. Transcript Day 5, page 186, lines 11
24 to 17 and page 197, 2 to 10, where Dr Bryan is
25 recognising that all three would have been required.

1 And indeed, Dr Bryan recognised specifically not only
2 that there were no steps taken, but also that he had
3 never been able to beat Dwr Cymru's price to Llanwern in
4 2003-2004. That's Day 6, page 2, lines 5 to 9. So that
5 really is just the end of the matter.

6 I should say that when interest was supposedly
7 revived in relation to these Corus matters later on --
8 and I think we might just go to the document, bundle 7,
9 248. This is a letter sent very shortly after the
10 Competition Appeal Tribunal's judgment. If you go down
11 to the fourth substantive paragraph:

12 "May I also ask you to provide us with bulk supply
13 terms for the supply of potable/non-potable water to the
14 Corus sites at Trostre and Llanwern."

15 So when, after the judgment, Albion thought: we're
16 going to get a common carriage price we can work with at
17 Shotton, they immediately thought: well, we need to have
18 means of supplying Llanwern and Trostre in order to be
19 in a position to bid for that Corus work we interpolate.

20 Of course, what we know is that thereafter, nothing
21 happened. They didn't pursue it in any event, which
22 again illustrates just the unlikelihood and speculative
23 nature of this suggested claim for Corus. So really,
24 that disposes of matters in relation to Corus.

25 As I say, that's fatal to Albion's claim. It didn't

1 have good reason why it didn't pursue things. It needed
2 to pursue in relation to three, and it entirely failed
3 to do so. It was clear that Corus was looking for
4 three, so there was no real chance of any opportunity to
5 win business there.

6 Now, the third matter is, in these circumstances,
7 unnecessary to go into, but since it has been set out,
8 both in our closing submissions, and it was an issue
9 that was raised by Mr Sharpe yesterday in relation to
10 beating prices, Albion has failed to demonstrate that it
11 had any realistic chance of winning any contracts with
12 Corus. It has given no basis for concluding that it
13 would actually have been able to beat the prices that
14 Corus was being offered by others.

15 Now, it is perhaps just worth noting that in its
16 annex 1 calculation of quantum in its claim -- so this
17 is bundle 10/1/3345-3346, for your notes -- Albion has
18 assumed that Corus Shotton was paying the published
19 Dwr Cymru non-potable tariff for water between 2004 and
20 2009.

21 Now, that assumption is wrong, and Dr Bryan accepted
22 it was wrong, and that 2003-4 special agreement price
23 for Corus -- which is found at bundle 9A, tab 358,
24 page 3294M -- was the relevant price to beat, and that
25 was 22.5p. That's Day 6 in the transcript, page 1, line

1 19 to page 2, line 4. So even if you could somehow
2 break out the Shotton business from what Corus was
3 actually looking for, which was a bundle of supplies to
4 those three sites, it's claimed that it would have won
5 even the Shotton business in those conditions. It makes
6 no sense, with the proposed tariff and margin that it
7 has put forward in the bundle at bundle 10, tab 1,
8 3345-3346.

9 Yesterday we had some new lines about these issues
10 and what the relevant prices were. Obviously these
11 were tested in cross-examination because they weren't
12 new yesterday, but it was all to do with the cost of
13 lagoons and it was laced with accusations. The first
14 was effectively that we'd misled the tribunal about the
15 pricing numbers that had been submitted in relation
16 to -- I won't call it the "shopping list", but the list
17 of requests that the tribunal had in relation to those
18 numbers.

19 Now, Mr Sharpe may want to consider again that
20 accusation, because what was asked for was the actual
21 prices paid by Corus. It is very plain, on the face of
22 what's been provided, that we have set out the prices
23 paid by Corus.

24 He then referred to lagoon values of 4p and how
25 those should be added to those prices paid in order to

1 work out what the price to beat was. We found this
2 slightly confusing because he then referred to the Ofwat
3 decision and section 10 of the Ofwat decision, which
4 actually put the storage values at between 0p and 1.3p.
5 So we're not quite sure what's going on there.

6 Then he said that we were also misleading because
7 the unit charge that Shotton is being billed is 36p, and
8 that was therefore what he had to beat. Well, I mean,
9 that is just plainly and obviously wrong. What Corus
10 has been paying is what is set out in the table we
11 provided to you. It hasn't been paying the higher
12 price, and there is a fight going on about that.

13 Corus has made it very plain it doesn't want to pay
14 that higher price; it only wants to pay the lower price.
15 I'm sure it would like to pay a lower price still, but
16 there is no possibility at all that Corus would
17 contemplate contracting with someone at a price higher
18 than it is contending in the litigation it should be
19 paying. There's no reason to suppose that at all.
20 Corus is willing to go to the time and expense of
21 fighting about this because it thinks that that is the
22 maximum price it should be paying in these
23 circumstances. So the idea that somehow the price that
24 Dwr Cymru is contending should be paid is the one that
25 Corus would have considered was the relevant price to

1 beat, it is just completely the wrong exercise.

2 Corus is only going to be interested in deals that
3 take it under that price that it's fighting about. It
4 is perhaps striking, in these circumstances, to step
5 back. Corus is fighting with Dwr Cymru about what the
6 relevant level is that it should be paying. At no point
7 has either Albion apparently been in contact with Corus
8 about doing a different deal, nor has Corus been in
9 contact with Albion about it. We've got no material of
10 that sort. So, in terms of the realism of Albion's
11 claim, Corus prefers to have a fight with Dwr Cymru, and
12 all the expense and pain that that involves, than
13 thinking that actually there's any real point in dealing
14 with Albion in relation to these matters. There's no
15 material that we can understand that suggests that
16 either Albion would have been able to beat those prices
17 for Llanwern and Trostre and Shotton, there is no reason
18 to separate them out, it's using the wrong benchmark
19 prices in these further submissions, and it is
20 instructive the lack of contact and initiative taken by
21 Albion in relation to these matters.

22 There's also a range of other matters to do with the
23 negotiations that would have to be completed and the
24 clearances that would be needed under the Water Industry
25 Act and so on that would add further uncertainty if

1 there was any real and substantial possibility of Albion
2 winning that business. But there isn't any real and
3 substantial possibility, and therefore there are further
4 uncertainties which, under the Allied Maples assessment,
5 would at least go to reduce the level of quantum that
6 would be applicable.

7 We don't even need to get into that because there
8 are several reason why there is no real and substantial
9 chance under the first limb of the Allied Maples test.
10 That is not adopting the Mr Sharpe approach which says,
11 "If you've got a substantial chance, then it's
12 100 per cent". That's not the way that Allied Maples
13 works. You have to have a substantial chance, then you
14 assess those sorts of issues.

15 We say you never get there, for the reasons we've
16 articulated. If you did, there are bunch of other
17 uncertainties. One of them would be securing the Water
18 Industry Act exemption, and the point we make there it
19 has just never been thought about or engaged in. For
20 Dr Bryan simply to assert, "Well, yes, we could have
21 just got the Welsh Assembly to tick the box here" is a
22 presumption that he doesn't have any basis for in
23 relation to Shotton or, indeed, any of the other plants.

24 In relation to those matters we say the approach
25 adopted in Allied Maples and, indeed, Enron actually

1 results in a similar outcome to Enron, which was found
2 there wasn't a substantial chance, and therefore the
3 quantification discount that was required isn't
4 necessary. If you were thinking about issues to do with
5 quantum then obviously we've set our submissions out in
6 relation to those matters at paragraph 300 in our
7 written closings, and we would say that given the sorts
8 of uncertainties we're talking about, the discount
9 involved would have to be vast.

10 Unless I can assist this Tribunal further in
11 relation to compensatory matters, I'm going to move on
12 to exemplary damages. I just wonder whether it would be
13 more sensible to take an early break now and come back
14 at 1.50 rather than starting for ten minutes?

15 THE CHAIRMAN: That might well be advisable. (Pause)

16 Yes, very well, we'll come back at 1.50.

17 (12.52 pm)

18 (The Short Adjournment)

19 (1.50 pm)

20 MR BEARD: My intention now is to move on to deal with
21 exemplary damages claim.

22 There has been quite a lot of sound and fury in
23 relation to the exemplary damages claim, but it is
24 necessary at the outset to emphasise what we're dealing
25 with here. It's the excessive pricing abuse and the

1 finding is specific and limited, the FAP was set at the
2 wrong level, so the question in relation to exemplary
3 damages is: was that FAP set on an outrageous or cynical
4 basis?

5 We know the answer to that question. It's "no".
6 The FAP was the product of calculations carried out by
7 Paul Edwards. He plainly didn't do so with any cynical
8 disregard for Albion. To the contrary, he wanted to get
9 it right. He wanted to ensure that Ofwat considered the
10 approach he was adopting was correct.

11 We also know from Mr Edwards and Mr Williams that
12 they knew of no one within Dwr Cymru that was out to get
13 Albion in relation to the FAP; both of them were
14 concerned that Dwr Cymru did the right thing, and in the
15 eyes of Ofwat, Dwr Cymru did do the right thing.

16 In its 2004 decision, Ofwat thought that although
17 there were one or two adjustments to be made, the basic
18 approach was correct using regional average cost
19 pricing, and the outturn was correct and permissible.

20 We now know that both Ofwat and Dwr Cymru were
21 wrong, and that's what the Tribunal concluded, but that
22 doesn't mean that either of them were carrying out any
23 campaign against Albion. Indeed, we've seen that Albion
24 wanted Ofwat involved along the way, Ofwat did put
25 pressure on Dwr Cymru to produce prices and hurry up

1 their processes. Ofwat was well aware of the way in
2 which Dwr Cymru was approaching these matters, both in
3 relation to the basic methodology and in relation to the
4 consideration of the stages that it then applied. And
5 it would therefore be, quite frankly, bizarre if the
6 methodology as to the pricing, which the specialist
7 regulator had approved and was then applied by
8 Mr Edwards, who was trying to apply it accurately, could
9 give rise to any claim for exemplary damages. It would
10 be wholly unjustified.

11 I am going to take the submissions in four parts, if
12 I may: Legal background; why are regional average costs
13 pricing was an entirely acceptable methodology; the
14 process of ascertaining the FAP -- although in going
15 through that I'll go to the closings because we've set
16 it out in writing in some detail, and then I'll pick up
17 some of the particular grounds that Albion has raised
18 now as founding its exemplary claim. I say "now"
19 because it is evident from the pleadings that it is
20 sparse on suggestions as to how things should have been
21 dealt with. Then I'll deal briefly with quantum at the
22 end, albeit, again, I'll refer to the written closing
23 material we have.

24 Just starting with the first of those matters, the
25 legal background. As set out previously in Dwr Cymru's

1 skeleton at paragraphs 164 to 166, in order for conduct
2 to fall within what's referred as to the second category
3 of *Rookes v Barnard*, it must be outrageous, a situation
4 where, in cynical disregarding for the claimant's
5 rights, the defendant has calculated that the money to
6 be made out of his wrongdoing will probably exceed the
7 damages at risk.

8 It is trite that in English law, exemplary damages
9 are exceptional. On occasion during this hearing,
10 Albion seemed to say that the findings of the Tribunal
11 that there had been an abuse was somehow sufficient to
12 make out the basis of its exemplary damages case. That
13 is fundamentally wrong.

14 The finding of abuse is not a sufficient basis for
15 the position of exemplary damages in a follow-on claim.
16 It would be a serious error to seek to lower that
17 threshold. The case law is emphatic: it is a necessary
18 but wholly insufficient condition that there has been
19 a breach of law.

20 When we look at *Kuddus* -- I won't take you to it.
21 Just for your notes it's in bundle 12, tab 7. *Kuddus*
22 permitted exemplary damages being available going beyond
23 the scope of what we know as traditional cause of action
24 limitations because exemplary damages, because they've
25 been rare in English law, there was an argument that

1 they've been limited to specified causes of action that
2 had been identified in previous cases, and there was no
3 basis for exemplary damages in relation to any other
4 claims at all.

5 In *Kuddus*, their Lordships were willing to remove
6 the cause of action restriction on the availability of
7 exemplary damages, but there was very clear concern
8 expressed that the scope of exemplary damages
9 availability shouldn't be more generally extended by any
10 attenuation of the threshold test.

11 Lord Scott, just for your notes at paragraph 121,
12 specifically indicated that whilst he:

13 agreed that the restriction of cause of action
14 should not be maintained, he "[viewed] any prospect of an
15 increase the cases in which exemplaries could be claimed
16 [would be a matter of] regret."

17 That is to some extent emphasised in *Cardiff Bus*.
18 That is at bundle 13, tab 30, or 2 *Travel*, whichever is
19 being referred to.

20 At paragraph 448 of the judgment it refers to the
21 fact that:

22 "Exemplary damages are a remedy of last resort," an
23 undesirable anomaly and are essentially a means of
24 filling a gap where there is not a better means of
25 punishment, thereby vindicating the strength of the

1 law.

2 Just in this context it's worth dealing with
3 Mr Sharpe's suggestions. He mentioned them being
4 a reward for the claimant. They're not. Another focus
5 of the suggestion would be for them removing any
6 proposed claim for the claimant. They're not. Indeed,
7 a previous restitutionary claim was previously brought
8 in this case and then dropped. Exemplary damages are
9 only relevant as punishment and deterrents.

10 Three further observations on legal principles which
11 are relevant to the present case. As set out in
12 Dwr Cymru's skeleton at paragraphs 170 to 174:

13 The ability of regulatory or judicial bodies to
14 have imposed financial penalties for the conduct in
15 question is most important. In a case where both Ofwat
16 and the Tribunal had the ability to impose a fine and
17 were well aware of that fact, the absence of any such
18 public sanction should at least militate very strongly
19 against the imposition of any exemplary damages award.

20 The fine availability goes to punishment and
21 deterrents.

22 Albion actually raised this issue, but then didn't
23 pursue it. It can't have been in a better position in
24 relation to exemplary damages claims for not having
25 pursued these issues when they could have done

1 previously. We refer to its raising these matters and
2 them being adverted to, skeleton footnote 24, which for
3 your notes is bundle 11, tab 2, page 49.

4 In this respect as well as in relation to a range of
5 factual matters, the present case is saliently different
6 from Cardiff Bus, where the company in respect of whose
7 conduct exemplary damages were awarded was actually
8 subject to an immunity from public regulatory penalty.

9 Now, as a consequence, it can only be in the most
10 exceptional circumstances and on the basis of especially
11 compelling evidence that any award of exemplary damages
12 should ever be made where a public regulatory financial
13 sanction was available in relation to the conduct in
14 question.

15 Now, at the moment this leaves to one side the issue
16 that was raised on the strikeout whether or not
17 exemplary damages are available as a matter of law at
18 all here. What I'm saying is that even if, as a matter
19 of principle, you never say never in relation to
20 exemplary damages, in circumstances where a regulatory
21 penalty could have been imposed, it must be the most
22 exceptional and compelling case for exemplary damages to
23 be used where that penalty has not been imposed.

24 Now, I've resisted to going to questions about the
25 nature of compelling evidence and Lord Hoffmann's famous

1 comments about what strength of evidence you need in
2 relation to matters, but you're not looking for
3 Alsations here, you're not looking for lionesses, you're
4 looking for albino lionesses in his taxonomy of rarity
5 in relation to these matters.

6 The second point is it's clear in case law the
7 concept alleged to give rise to exemplary damages must
8 have a sort of motive mens rea element. It is a point
9 you raised in questions at the outset of closings.
10 Someone must have cynically disregarded the claimant's
11 rights in expectation that the gains of doing so would
12 outweigh the likely damages and fine risk.

13 In Cardiff Bus, the issue of intent and the
14 attribution of knowledge of unlawfulness was considered
15 by the Tribunal at paragraphs 558 to 564 for your notes.
16 Now, these are issues again unpleaded by Albion, and
17 Albion really didn't attempt to grapple with it in
18 opening. And frankly, in relation to closing we remain
19 somewhat confused. The point is important, though, as
20 the Tribunal in Cardiff Bus made clear at 561: since
21 a company is a legal, not a natural person, the question
22 of whose state of mind is to be attributed to the
23 company may be critical.

24 It is not clear who Albion are saying is the
25 directing mind. To be clear, Dwr Cymru's case is that

1 the FAP was put together by Mr Williams' team. The
2 question was what was their state of mind. There was no
3 cynical disregard for Albion's rights on their part.
4 Indeed, they were concerned not to act unlawfully and
5 were keen to ensure that Ofwat accepted their approach.

6 THE CHAIRMAN: So you're saying there was no instruction as
7 to how to go about this given to Mr Williams or his team
8 by anyone more senior than Mr Williams?

9 MR BEARD: We're not aware of any such instruction and
10 certainly no such instruction that this should be
11 pursued with cynical disregard, or the effect of cynical
12 disregard, obviously not in those words, but with that
13 motive. No.

14 THE CHAIRMAN: What do you mean when you say, "We're not
15 aware of any such instruction"?

16 MR BEARD: Well, the evidence is that no such instruction
17 was given and that the basis on which Mr Williams was
18 proceeding and the basis on which Mr Edwards was
19 proceeding was that using the regional average cost
20 pricing methodology was entirely appropriate, it had
21 been the methodology that had been used previously, and
22 then Mr Edwards took the calculations that Mr Henderson
23 had been developing and took them forward in order to
24 create the FAP.

25 In that regard, the need for the FAP to be produced

1 was clear, given the requests of Albion and the demands
2 of Ofwat, which were being communicated in
3 correspondence. But there was no instruction that
4 somehow the way in which that was to be developed was to
5 Albion's detriment or that there was an assessment of
6 the profit that would be made by using the regional
7 average cost.

8 THE CHAIRMAN: Putting those two things on one side for the
9 moment, what are you saying as regards any instruction
10 at all to Mr Williams or his team as to how to go about
11 this task?

12 MR BEARD: Well, instructions from whom? Mr Williams was
13 a board director --

14 THE CHAIRMAN: Well, I'm asking you.

15 MR BEARD: There is no indication that anyone else gave
16 instructions to the team to get on with the FAP. The
17 team knew that the FAP had to be produced, Albion had
18 asked for it. Ofwat had indicated that a price needed
19 to be produced, and indeed, had chased it up.
20 Mr Williams gave evidence that he was concerned to
21 ensure that a price was produced. That is what
22 happened, using Mr Edwards' calculations.

23 THE CHAIRMAN: Okay. Go on.

24 MR BEARD: The third point may appear trite, but it is for
25 Albion to prove that the high threshold for imposing

1 exemplary damages has been met. On numerous occasions
2 Mr Sharpe has said to Dwr Cymru's witnesses, in
3 particular Mr Williams, "I didn't call you", by which he
4 appeared to imply that an inability to answer his
5 cross-examination questions was somehow a failing on the
6 part of Dwr Cymru's case. It wasn't.

7 In the light of the fact that the exemplary damages
8 allegations concerned the ascertainment of the FAP and
9 the differences in particular between the indicative
10 price in January 2001 and the final FAP of 23.2p,
11 Dwr Cymru proffered Mr Edwards, who was the person who
12 understood the calculations and would have pulled them
13 together and could speak to those variations. It also
14 proffered the board director who had responsibility for
15 the FAP being issued, which was Mr Williams who headed
16 up the relevant team.

17 Albion now seeks to suggest that the Tribunal can
18 draw inferences from the fact that someone -- and there
19 are list of someones that have now been produced --
20 wasn't called, and in regard to that, rely on a case
21 called Kythira, which Mr Sharpe didn't take you to, but
22 I think it is relevant to have a very brief look at
23 that.

24 THE CHAIRMAN: I'm just trying to follow your line of
25 thought at the moment.

1 MR BEARD: What I was going to say was there was no basis on
2 the basis of that authority to suggest that where
3 a party has called evidence in relation to relevant
4 matters, any inferences adverse to it can be drawn in
5 relation to the fact that certain other witnesses
6 weren't also called.

7 It's no good authority for that proposition and,
8 indeed, it would be a remarkable authority if that were
9 the case because it would effectively mean that in
10 certain circumstances you'd be reversing the burden of
11 proof. All the more remarkable where you're talking
12 about an exemplary damages allegation.

13 What we have here is a situation where witnesses
14 were chosen on the basis that they were the most
15 relevant the head of the team doing the FAP and the
16 person doing the calculations. That was a proportionate
17 and sensible approach to the gathering of evidence. It
18 wasn't necessary or appropriate for anyone else to be
19 called, and I've already referred to the fact that the
20 pleadings -- there were no particulars of the exemplary
21 damages claim put forward, no indication of who was
22 accused of what in the pleadings. And I won't rehearse
23 the points made in relation to the unpleaded issues that
24 once the claimant had withdrawn section B9 of its claim,
25 there were no particulars at all of the exemplary

1 damages contentions.

2 In the circumstances, there was no reason for any
3 other witnesses to be called. It would have been
4 unnecessary and disproportionate. And just to go back
5 to the point: it's not our burden to discharge.

6 It is also just to be recalled in this regard that
7 there isn't any property in a witness. Albion can
8 approach who they like in relation to these matters. We
9 have no idea whether Dr Bryan has approached anybody
10 else, but whether or not they did, it is a matter for
11 Albion to prove its case in this regard.

12 So just turning to the people that Mr Sharpe has
13 said, "Oh, well, you should have called them" and
14 somehow inferences can be drawn against us because we
15 didn't, as we've seen and I'll come on to, it wasn't
16 Mr Henderson's work that was critical to the FAP; it was
17 Mr Edwards' work because Mr Edwards corrected errors
18 being made by Mr Henderson, and it was Mr Edwards that
19 was key to what the FAP figure was.

20 So his work was overtaken by Mr Edwards. Mr Edwards
21 was plainly the right person to call in that regard.

22 Mr Holton, now, he didn't do the figures. He wasn't
23 key to the FAP, and indeed, when it was suggested at the
24 start of the trial that he might be needed, we said,
25 look, steps can be taken to find him and make him

1 available for the Tribunal. That offer wasn't taken up.
2 Just for your notes it is transcript Day 1, page 167,
3 line 12, to 168, line 3. So how, in relation to
4 Dave Holton, any suggestion of inferences can be drawn
5 is just beyond us.

6 Dr Brooker was the overall responsible for
7 Dwr Cymru, and yes, of course he had contact with Ofwat.
8 And when the court -- the CA98, the Competition Act, was
9 being rolled out, yes, of course he was involved. But
10 the relevant board director sponsor for the FAP was
11 Mr Williams. He may not have recalled much and was
12 clearly not a man for the details, but he was the
13 responsible director. And if it's being said that
14 Dwr Cymru was running some sort of campaign against
15 Albion and was trying to target prices to damage Albion,
16 the responsible director was clearly the man to call in
17 relation to those matters.

18 In addition, in relation to Dr Brooker there was
19 a slightly strange interjection by Mr Sharpe about
20 a communication from Dr Brooker in relation to the
21 approach to common carriage when he talked about the
22 idea that in fact Dr Brooker had adopted an approach by
23 reference to domestic supply issues.

24 If you wouldn't mind, take volume 4, tab 160.
25 I just want to get this point out of way, just on

1 Dr Brooker. The reference made by Mr Sharpe yesterday
2 Day 11, page 115, line 18, through to 116, line 12. The
3 suggestion was that Dr Brooker was making suggestion of
4 average prices in the context of residential potable
5 water, and the citation given was this document.

6 It's a remarkable suggestion. As you can see, it's
7 headed "Competition Act 1998, complaint against
8 Dwr Cymru related to common carriage". What it does is
9 it says at the bottom:

10 "The proposed access prices have been determined by
11 Dwr Cymru using its whole company average costs
12 allocation methodology. Dwr Cymru has consistently
13 applied this methodology to establish pricing policy
14 since 1989. This method is fair, simple and consistent.
15 It draws primarily upon data that is disclosed by the
16 company, certified by the reporter and published by
17 Ofwat, thus achieving an open and transparent result."
18 It is neither excessive, nor predatory,
19 non-discriminatory and consistent.

20 It goes on to talk about it. We didn't really
21 understand why it was being suggested that Dr Brooker
22 was somehow engaged in some sham dealing in relation to
23 residential potable water. It is plainly not to do with
24 that at all.

25 MR SHARPE: For the avoidance of the doubt, and let me be

1 clear about it now, I didn't say anything of the sort.
2 I said yesterday, you will recall, that the overwhelming
3 volume of water supply by Welsh Water was for potable
4 water. The reference in this final paragraph deals with
5 average pricing, which plainly applied to potable water
6 supply. It plainly did not apply, given the information
7 you have seen at length from the special register,
8 having regard to the variations in price, to large bulk
9 supply agreements for non-potable water.

10 MR BEARD: We don't accept that.

11 MR SHARPE: Well, whether you accept it or not, that's what
12 I meant.

13 THE CHAIRMAN: One of the points is, as we understood
14 Mr Edwards' evidence, that at some stage somebody within
15 Dwr Cymru took the decision that there would not be a
16 separate common carriage price for non-potable common
17 carriage and a separate price for potable common
18 carriage, and that the price that they would put forward
19 would be a price for any common carriage to any part of
20 the network; is that right?

21 MR BEARD: I'm not sure that's quite right. I think what
22 Mr Edwards was saying was that he drew upon the approach
23 that had been set out by Denis Taylor in relation to the
24 previous methodology.

25 THE CHAIRMAN: Yes.

1 MR BEARD: And he knew that the previous methodology had
2 used those parameters in relation to these issues.

3 I mean, in fact we know --

4 THE CHAIRMAN: Was there a different common carriage price
5 proposed for potable common carriage, then?

6 MR BEARD: I don't think it was ever proposed separately,
7 but I'm not sure there's ever been necessarily a big
8 inquiry in relation to that. So I'm not sure it's ever
9 been engaged with. Obviously treatment issues --

10 THE CHAIRMAN: As to who within Dwr Cymru took these
11 decisions as to whether they would approach this on the
12 basis of regional averaging or bottom-up costs, whether
13 they would have separate common carriage prices for
14 potable and non-potable common carriage, you're saying
15 that Mr Edwards took those decisions?

16 MR BEARD: Well, Mr Edwards rightly encapsulated it in the
17 phrase where he said, "Approaching matters on the basis
18 of regional average cost pricing was in the DNA of
19 Dwr Cymru". That was how everyone was working. It
20 wasn't a matter that you needed an instruction in
21 relation to. That's why I said we're not aware of any
22 instructions specifically being given in relation to
23 these matters.

24 It is perfectly clear that those involved considered
25 that approaching matters on the basis on which they'd

1 been approached previously, using regional average cost
2 pricing was entirely appropriate. They did that. No
3 issue was raised against that by anyone. It proceeded
4 on that basis, and in the end Ofwat said, "Actually,
5 that's a perfectly good basis on which to proceed".

6 You don't have to hunt for a specific instruction in
7 circumstances where these --

8 THE CHAIRMAN: But do we have to hunt for somebody senior in
9 the company and competent to address these issues,
10 having thought: how should Dwr Cymru respond to the
11 challenge of common carriage? No.

12 MR BEARD: No, you don't have to go hunting for people. The
13 Tribunal might sit here and say, "Well, if I were
14 running Dwr Cymru, I'm not sure that I would necessarily
15 have my directors working in precisely the way that they
16 did at the time in 2000 and 2001".

17 You might want your company run differently, but
18 that doesn't suggest that you have to hunt round to find
19 some person that is giving specific instructions. That
20 is not the exercise in relation to an exemplary damages
21 case.

22 The question you're asking yourself here is: was
23 there that animus that gave rise to the cynical
24 disregard, the outrageousness? Not: who gave an
25 instruction, because that is not necessarily how

1 a company operates in a particular situation. You have
2 very clear evidence that actually it was the default
3 approach that was being adopted because that was the way
4 things were done in Dwr Cymru in relation to price
5 calculations. The top-down regional average cost
6 approach. It didn't require a regional instruction. It
7 would be a futile exercise to go hunting for it.

8 Mr Williams made it clear that his understanding,
9 though it didn't trespass on the detail, nonetheless was
10 that regional average cost pricing was the appropriate
11 methodology, and he had no concerns about that being
12 adopted so long as Ofwat was concerned.

13 THE CHAIRMAN: I thought that was because his evidence was
14 that that had been adopted in the network access code?

15 MR BEARD: Sorry?

16 THE CHAIRMAN: That was because it had been adopted in the
17 network access code.

18 MR BEARD: No, I think he was content that was the
19 methodology that was being adopted and was adopted in
20 the network access code.

21 THE CHAIRMAN: But we don't know who decided it should be
22 adopted for the purposes of the network --

23 MR BEARD: We know the network access code was pulled
24 together by Mr Williams' team and Mr Edwards was
25 cross-examined in relation to it, that in relation to

1 those matters, reaching the default position in the
2 network access code was entirely sensible. There wasn't
3 any need for there to be separate instructions in
4 relation to these sorts of matters, and as it
5 transpired, it was entirely correct.

6 What we don't have to hunt for is some instruction
7 that if it had been given on nefarious terms with
8 nefarious intent, it might have coloured the way you
9 look at all of this. The question you're asking is: is
10 there any evidence that such an instruction was given?
11 The answer is no.

12 So it is for Albion to prove, not merely insinuate
13 that conduct was so outrageous and cynical as to justify
14 the possibility of exemplary damages. You can't draw
15 inferences about the nature and terms of evidence from
16 witnesses who weren't called when evidence has been
17 proffered. It was entirely understandable why the
18 witnesses called were called and why others were not.

19 You could always play a game, particularly a game
20 where the case and the terms of the case being put
21 against us are constantly expanding and varying over
22 time, that there were other people that should have been
23 called, could have been called, might have been called,
24 it would have been nice if they'd been around. But that
25 is not the legal test here.

1 We have proffered evidence notwithstanding the fact
2 that the burden lies on Albion. We have proffered
3 witnesses sensibly; the person dealing with the
4 calculation, the head of the team. We've also proffered
5 a witness from United Utilities to deal with that aspect
6 of the case, but again, you mustn't get away from the
7 fact the burden lies in disregard plainly on Albion.

8 Now, if the Tribunal is interested in the question
9 of drawing inferences from the absence of witnesses, I
10 think it is important that you briefly look at the
11 Kythira decision at bundle 19, tab 66.

12 This is a distinctly odd case, Bentham v Kythira.
13 What it's concerned with is what is sometimes referred
14 to as half-time submissions in proceedings.

15 "The claimant was a well-known firm of estate
16 agents, the defendants were property companies."

17 I'm just reading from the headnote.

18 "The claimants claimed they'd acted as agents for
19 the defendants in connection with certain property
20 transactions and, accordingly, became entitled to
21 commission in respect of them. The trial judge
22 dismissed the claim at the close of the claimants'
23 evidence. In doing so, he acceded to the defendants'
24 submission of no case to answer without first putting
25 the defendants to their election as to whether or not to

1 proceed. The judge accepted that although generally the
2 defendant would be put to his election, the judge had
3 a discretion not to do so in an exceptional case. He
4 thought that such an exceptional case could arise when
5 two conditions were satisfied. Nothing in the
6 defendant's evidence could affect the view taken of the
7 claimants' evidence, and secondly, that it was obvious
8 that the claimants' case must fail. The claimants'
9 appealed."

10 You've a very odd situation here where a judge has
11 unilaterally said --

12 MR LANDERS: I'm sorry, I don't actually have a 66.

13 MR BEARD: I'm sorry. (Handed) I'm just at page 7768.

14 What is said here is that:

15 "The appeal would be allowed in this case. The case
16 crossed the evidential threshold required to defeat a no
17 claims submission. If the judge had asked himself the
18 correct question with regards to the evidence adduced,
19 he would have been bound to reject the defendant's no
20 case submission."

21 What's being said here is that if the judge had
22 properly put the defendants to election, or considered
23 doing so, he would have had to conclude that it was
24 necessary for them to proceed with their case. And the
25 basis on which that's done is -- well, one can see the

1 essence of the reasoning here, which is focused on the
2 process that was followed.

3 "The question to be asked in a case such as the
4 present, where the defendants' witnesses have material
5 evidence to give on the critical issue in the action could be
6 reformulated as follows: have the claimants
7 advanced prima facie case? Is there a scintilla of
8 evidence? It may be a weak case and unlikely to succeed
9 unless assisted rather than (...read to the word...) be
10 dismissed on the 'no case' submission."

11 That's the essence of the decision. You ask
12 yourself: well, what has this got to do with inferences
13 from witnesses? What you then have to turn on to is the
14 reasoning of Lord Justice Simon Brown, as he then was,
15 in relation to these matters. In particular, at
16 7775/24.

17 "Before looking at that body of authority [which is
18 concerned with no case to answer] I now wish to
19 introduce into the debate a separate line of authority
20 to which I referred at the outset of this judgment. The
21 case is establishing the principle that in certain
22 circumstances the court is entitled to draw adverse
23 inferences from a party's failure to call evidence.

24 "Until the present appeal, no one seems to have
25 noticed that this principle might have some bearing on

1 entertaining submissions of no case. It is, I suggest,
2 relevant first as to whether a defendant seeking to make
3 such a submission should be put to his election, ie to
4 whether the court should entertain a submission, and
5 secondly, assuming he is not put to his election
6 [assuming the court does entertain it] what in those
7 circumstances should be regarded as sufficient evidence
8 to establish a real prospect of success?"

9 A real prospect of success on the part of the
10 claimant.

11 So you're in a very strange world here. The Court
12 of Appeal is considering what are the circumstances
13 where the claimant has enough of a case that a no case
14 to answer submission should be tested and should fail?
15 And then it draws on a line of cases about when adverse
16 inferences can be drawn from the party's failure to give
17 evidence.

18 "I'm in the fortunate position of being able to draw
19 on Brook LJ's leading judgment in Wisniewski , itself
20 unfortunately unreported. Brook analysed the various
21 cases and derived from them a number of principles [and
22 it lists some cases]. The principles Brook LJ derived
23 from these cases are in certain circumstances a court
24 may be entitled to draw adverse inferences in the
25 absence or silence of a witness who might be expected to

1 have material evidence to give on an issue in the
2 action. If a court is willing to draw such inferences
3 they may go to strengthen the evidence adduced on that
4 issue by the other party, or weaken the evidence, if
5 any, adduced by the party who might reasonably have been
6 expected to call the witness.

7 "There must, however, have been some evidence,
8 however weak, adduced by the former on the matter in
9 question before the court is entitled to draw the
10 desired inference. There must be a case to answer" on
11 the matter. And if the reason for that witness's
12 absence or silence satisfies the court, no such adverse
13 inference may be drawn.

14 "If, on the other hand, there's some credible
15 explanation given, even if it is not wholly
16 satisfactory, the potentially detrimental effect of his
17 or her absence or silence may be reduced or nullified.
18 The fourth of those principles doesn't apply in relation
19 to no case submissions."

20 Then the judge goes on, Lord Justice Simon Brown, to
21 talk about the test to be applied by the judge if he
22 does entertain a no case submission. In 28:

23 "It is at this stage the relevance and the
24 principles stated in (...read to the word...) by some
25 evidence, however weak."

1 So what you've got here is a situation where the
2 court is considering a no case to answer submission.
3 There's the possibility that if the defendant is pressed
4 to put forward a case, they may adduce no evidence. At
5 which point you do have an issue where you can say,
6 "Well, hang on a minute, if you're adducing no evidence
7 at all in circumstances where you could adduce evidence,
8 there may be grounds for drawing some sort of adverse
9 inference against you, albeit that it's a very tentative
10 suggestion because, of course, there might be all sorts
11 of reasons why someone doesn't present a witness", and
12 it's very clear that this is will defeat the inference
13 relatively readily.

14 That of course is highly understandable because if
15 you could readily draw these sorts of inferences, you
16 would end up in a situation where, unless you called
17 upon all possible witnesses that could be relevant to
18 a case, you would end up in a situation where,
19 notwithstanding that you're a defendant, you'd end up
20 having inferences drawn against you, which is in effect
21 reversing a burden against you in relation to such
22 matters. And it is for that reason that you don't see
23 lots of authority in relation to these sorts of matters
24 and the reason it comes up in obscure corners such as
25 this.

1 If you go forward to the court and put forward
2 witnesses on a sensible basis, there is no good basis at
3 all for drawing broader adverse inferences because there
4 might have been other witnesses that could be called.
5 So the Kythira case that is relied upon is not a broad
6 proposition that if you don't turn up with someone that
7 is now mentioned in the course of a skeleton argument,
8 which has never been mentioned in pleadings before, who
9 may or may not work for the company, that in those sorts
10 of circumstances some sort of adverse inference may be
11 drawn against you.

12 THE CHAIRMAN: You say the test is whether we consider that
13 Dwr Cymru put forward witnesses on a sensible basis?

14 MR BEARD: Yes. If we've put forward witnesses on
15 a sensible, proportionate, reasonable basis, having in
16 mind the pleadings, because of course, we proffered our
17 witnesses in the light of the pleaded case, which is --

18 THE CHAIRMAN: But we have to assume that you knew what your
19 witnesses were going to say and the limits of what they
20 were going to be able to give evidence about in relation
21 to expected lines of cross-examination?

22 MR BEARD: Well, no, I don't think you can go that far.
23 Plainly, we don't know what witnesses are going to say
24 in relation to all matters. We don't know to what
25 extent a director does or doesn't recall stuff in

1 relation to events taking place in the past. Our
2 selection is based on the case as pleaded against us,
3 who are the relevant people that we think it is
4 proportionate and sensible to call as witnesses.

5 Calling the person who we knew was the person that
6 carried out the calculations that were found to result
7 in a price that was abusive was obviously sensible.

8 THE CHAIRMAN: Yes.

9 MR BEARD: I mean, if we'd called Mr Henderson instead of
10 Mr Edwards, for example, it would be said, "But you
11 haven't called the person that actually did the outturn
12 calculations". We called the person that did the
13 outturn calculations.

14 THE CHAIRMAN: I don't think anyone is querying the
15 usefulness of calling Mr Edwards.

16 MR BEARD: No, but it is the additionality. It's the idea
17 that somehow if we'd called Mr Henderson, he would have
18 somehow given evidence that, as Mr Sharpe put it, you
19 should presume was against us.

20 THE CHAIRMAN: Just focusing for a moment on more senior
21 people -- I think what Mr Sharpe was indicating was that
22 when they saw that Mr Williams was the member of the
23 board who was the sponsor for this project, they would
24 have assumed that he was the person who would have taken
25 the decisions as to how the project was handled and how

1 it should be done, and he was the person who had
2 reported back to the board and led the discussions at
3 board level, such as they were, and to whom, then,
4 questions about what had happened at the board level,
5 given the absence of board papers and minutes in the
6 disclosure, that he would be able to answer those
7 questions.

8 Now, as it turned out, he was wholly unable to
9 answer those questions, and the question for us is:
10 ought you to have known that, and ought you to have
11 proffered an additional witness or a different witness,
12 someone who was more responsible for the project that
13 you say, well, there was no other person, it was all in
14 the hands of Mr Williams and his team?

15 MR BEARD: No, there are two things to deal with here.

16 Mr Williams was the responsible director for this
17 project and answerable at the board. The fact that he
18 didn't remember things --

19 THE CHAIRMAN: It is not just the fact that he didn't
20 remember things, Mr Beard.

21 MR BEARD: Well, he didn't remember and he didn't know about
22 the details of the matters. As I say, it may be
23 something that if you are running a company you might
24 say, "Well, I would prefer my directors to know more
25 about these things when they're presenting stuff to the

1 board --

2 THE CHAIRMAN: It was clear from his evidence, Mr Beard,
3 that he had not been actually -- and this was his
4 evidence -- that it was Dr Brooker or Mr Holton, if he
5 had attended meetings, who was able to respond to
6 questions, if there were questions from the board,
7 because he was wholly unable to respond to those
8 questions because he didn't have a grip of the detail,
9 as he put it.

10 MR BEARD: No, he didn't have a grip of the detail.

11 THE CHAIRMAN: Now, the question is that, as
12 I understand it, was not what Mr Sharpe and Mr Cook had
13 been expecting, and if it was what you were expecting,
14 then the question is: is there anything that the
15 Tribunal should conclude about the fact that nonetheless
16 Mr Williams was the person that you put forward to give
17 evidence as to what senior management involvement there
18 had been in this decision-making process?

19 MR BEARD: I think it is important first -- the answer to
20 that is no, there isn't anything. But the first point
21 to make is Mr Williams put forward a witness statement,
22 a written witness statement, talking about what he could
23 speak to. There is no suggestion in his witness
24 statement that he descended into the details of anything
25 to do with the specific calculations. What he talked

1 about was how his team, and in particular Paul Edwards,
2 dealt with the calculations, and that that was how the
3 FAP was produced.

4 In doing that and providing that evidence, he dealt
5 with the question of whether or not there was, within
6 his knowledge, anyone involved in his team or otherwise
7 at the board in Dwr Cymru who was trying to operate, or
8 intending to operate, or even being reckless in relation
9 to the way that the FAP should be produced. And he
10 plainly says no. And that's his evidence. That is
11 highly relevant. That is core evidence in relation to
12 this case.

13 If Mr Williams can't speak to a range of more
14 detailed questions that the claimant's counsel put to
15 him, that is not Mr Williams' fault. He proffered
16 absolutely relevant key evidence. It was set out in his
17 statement. He doesn't at any time suggest that he
18 understood all the details of these matters. The fact
19 that Mr Sharpe engaged in the game of putting more and
20 more detailed matters to him until it reached a point
21 where it was just a matter of a degree of embarrassment,
22 that doesn't change anything. The witness evidence was
23 rightly proffered and is highly relevant. It is
24 limited, but it is limited to focus on the key issues in
25 this case so far as the responsible board director was

1 concerned. To suggest that that was wrong, to call that
2 person, and someone else should be called in his place
3 is quite unjustifiable.

4 I don't know whether I can assist further in
5 relation to Mr Williams. I can take the Tribunal
6 through his witness statement. It is relatively brief
7 in relation to these matters.

8 Insofar as it is being suggested other people should
9 be called, there isn't any good basis, there are no
10 inferences that should be drawn from that. Indeed, it
11 would be a matter of an area of law, and Mr Sharpe's
12 suggestion that in the circumstances you should somehow
13 presume that these people were going to give evidence
14 adverse to Dwr Cymru is just outlandish. If they wanted
15 to call these people, they could have approached them in
16 any event. You can't circumvent that issue at all.

17 On that basis, I was going to move on to regional
18 average pricing, if I may, unless there are particular
19 questions relating to law, inferences, witnesses and
20 so on, because it might be sensible to pick them up now.

21 THE CHAIRMAN: No, I think go on.

22 MR BEARD: Thank you.

23 If I may, what I'll try to do is track the written
24 closing a little bit so we can, I hope, speed the
25 plough, and I'll commence at paragraph 349, which starts

1 on page 91. So I'll deal for the average pricing stuff
2 before I get into the FAP material.

3 Now, I think the reasons why Dwr Cymru proceeded to
4 offer the FAP on the basis it did are clear and
5 straightforward. Dwr Cymru has considered that it was
6 entitled to approach the assessment using the regional
7 average pricing basis, and Mr Edwards made clear that
8 that doesn't mean everyone ends up paying the same; it
9 means effectively there's a top-down methodology being
10 used, and an average cost of water provision is
11 ascertained. And then, from that, various subtractions
12 are made to ascertain a final price. Those subtractions
13 are obviously aimed at removing elements of the average
14 cost that pertain to service components which aren't
15 being encompassed by the product being provided.

16 We know that regional average cost pricing had been
17 used previously. It had been used, for example, back in
18 1996 and 98, as Mr Edwards made clear in paragraph 28 of
19 his first witness statement, in relation to setting up
20 large industrial tariffs. It was also the basis on
21 which Dwr Cymru had approached post-privatisation
22 special agreements. That didn't mean every special
23 agreement was priced at precisely the same level. That
24 was well accepted by Mr Edwards.

25 The fact that regional average cost pricing was the

1 approach that the industry was using prior to 2000 and
2 2001 and, indeed, subsequently was repeatedly recognised
3 by Ofwat. And in that regard, if I may, I'll just turn
4 to bundle 5/227, the 2004 decision at 1496.

5 This is a section of the decision that the Tribunal
6 has been taken to previously. It starts under the
7 heading on the previous page, 1493, "Accessing price in
8 the water industry" where there is a discussion of
9 MD163. And then "Average accounting cost method used by
10 Dwr Cymru" at 245.

11 "Dwr Cymru based the first access price on an AAC
12 method or, as Dwr Cymru called it, on a whole company
13 average basis."

14 So the point has been made previously: Ofwat knew
15 fully what was being done by Dwr Cymru here, and there's
16 no suggestion that anything in relation to what
17 Dwr Cymru told Ofwat somehow blinkered Ofwat in the way
18 that it approached and understood these matters.

19 Then over the page at 1495 we have the heading
20 "First access price". It's already noted by Ofwat in
21 248 that Dwr Cymru's approach to the first access price
22 and its approach to the new tariff was similar.

23 Then we're into this section of the decision where
24 there's a detailed discussion about the first access
25 price and the methodology, but I just ask you to read

1 again 252 to 253. (Pause)

2 I'm not going to take the Tribunal back through all
3 elements of this decision, but what is important is the
4 cognisance that Ofwat has of the methodology and the
5 reasons for that methodology. Then, when it comes on to
6 its scrutiny of the calculation of the first access
7 price, obviously step one that is adopted by Dwr Cymru
8 in this regard is using that average unit price for the
9 supply of water, that Ofwat is entirely content with.

10 Now, of course there are adjustments along the way,
11 and in particular, there were adjustments in relation to
12 what should be counted within that. But the
13 methodology, the approach that was being adopted, was
14 being recognised as the industry standard approach to
15 dealing with these sorts of issues. So, again, it goes
16 back to this question of whether you ever needed an
17 instruction. This was what was understood.

18 The only reason that any query is ever really being
19 raised about this is in part because, I think, there's
20 been this reference to an alternative reading of MD163,
21 but actually that doesn't take matters further forward.

22 THE CHAIRMAN: Isn't it also in part because we now know
23 that actually a great deal of work was done to do
24 a bottom-up assessment of the non-potable assets?

25 MR BEARD: I think we're jumping ahead. There has been

1 further material in relation to -- there having been
2 a study by Hyder in relation to these issues. But the
3 idea that that meant that (a) regional average cost
4 pricing was wrong, inappropriate, being adopted
5 cynically, whatever else is being alleged against
6 Dwr Cymru, it doesn't take Albion anywhere because what
7 is plain from this and, indeed, other material that the
8 Tribunal has seen is that regional average cost pricing
9 is an appropriate way of dealing with these matters. It
10 is the right way, Ofwat is saying, of approaching these
11 issues.

12 Even if we jump right forward to the end game of the
13 Tribunal judgment, the unfair pricing judgment, the key
14 methodology was a top-down methodology. Yes, it was
15 more granular and more refined, AAC plus, but actually
16 it was another top-down methodology. What the Tribunal
17 then said was you needed to do some crosschecks. Now,
18 there was no suggestion that could ever be sustained,
19 that somehow not doing local crosschecks in these
20 circumstances was itself cynical, outrageous,
21 inappropriate.

22 I know this is a line that has been maintained in
23 the closing submissions, but it is one without any merit
24 at all. The industry at the time was proceeding that
25 the regional average cost pricing was the appropriate

1 the methodology.

2 In relation to that other information that has be
3 referred to, the Hyder report, I'll come on to it, but
4 the key issue there is it doesn't tell you the answers
5 in relation to local cost pricing. Actually, there's
6 a whole heap more material that you would need to gather
7 and pursue in order to get any sort of sensible local
8 cost pricing assessment out. That was what those three
9 statements from Chris Jones were all to do with in the
10 previous proceedings, which just illustrated how
11 complicated this exercise was. Indeed, that's what
12 Ofwat is in part talking about here. It is just not
13 straightforward.

14 Dr Bryan might wish it was. That is not the way the
15 water industry works and it is not the way it works for
16 justifiable reasons to do with the common elements of
17 cost, the importance of ensuring you have proper
18 investment in relation to your infrastructure over time,
19 and Ofwat is highly aware of these matters. There is no
20 suggestion that anything that Dwr Cymru did somehow
21 prevented Ofwat from understanding these matters, and it
22 clearly did so on an entirely appropriate basis.

23 As Mr Edwards explained quite clearly in the course
24 of the transcript, Day 9, page 141 to 142, that regional
25 average pricing approach was adopted whether or not

1 a customer was on some sort of discrete spur of the
2 network or part of the wider integrated network, because
3 that was the way that these matters had been approached
4 and were approached generally within the industry. And
5 of course, that makes sense because there is a great
6 deal of common cost in relation to the way in which the
7 cost act(?) for any of these major water companies is to
8 be calculated.

9 That means, of course, that the costs across the
10 wider business were being recovered. It was intended to
11 ensure that customers were treated fairly. It took
12 account of the difficulty of identifying and allocating
13 costs of components of systems as well as ensuring that
14 the proper cost measures were used, in particular modern
15 equivalent asset values for replacement were being used.

16 As I say, we saw in the evidence of Mr Jones that
17 was referred to in the course of proceedings that even
18 when local costs were pulled together and analysed in
19 a good deal of detail in 2006, what it revealed was the
20 vast majority of costs weren't local at all, and
21 actually the exercise was extremely complicated.

22 In relation to the Hyder material, what we do know
23 from Mr Edwards, who was the person that identified it,
24 was that although he hadn't had it and hadn't used it at
25 the time, in relation to those matters you had

1 a situation where the material in the Hyder report
2 wouldn't have provided you with the relevant local cost
3 estimates that were then used as a cross-check by the
4 Tribunal in any event.

5 So that's the relevant material. As I say,
6 Mr Edwards simply didn't take into account that
7 alternative Hyder material and he was justified in
8 proceeding on the basis of the regional average cost
9 background.

10 It's worth just recalling, of course, the general
11 background here, the fact that we were moving into
12 a world where competition law was coming into force in
13 the domestic arena for the first time in relation to an
14 industry that hadn't had competition law previously but
15 had only had regulatory schemes. It was recognised that
16 that was creating effectively a state of flux.

17 There were all sorts of consultations going on,
18 Ofwat consultations, MD letters coming out, guidance
19 from OFT and Ofwat and, indeed, Government
20 consultations, during the course of which issues to do
21 with regional average cost pricing and the extent to
22 which companies could actually diverge from it for their
23 own purposes -- I mean, this goes back to the predation
24 point that I was referring to earlier -- that actually
25 one of the real concerns was about the extent to which

1 there could be either cherrypicking by new entrants of
2 the most profitable business thereby lumbering residual
3 customers with higher costs, or reactions from incumbent
4 companies who were effectively able to predate if they
5 moved away from regional average cost pricing.

6 So there was a whole deal of material that was at
7 issue at the time, and we referred to it in some detail
8 in our written closing, so I won't go through it now.

9 What was clear was that Ofwat, in carrying out its
10 consultation process, was airing what it thought were
11 the issues that arose in relation to these matters. And
12 as we've seen, in particular, the MD154, which just for
13 your notes is at bundle 3, tab 31, raised various issues
14 pertaining to the development of common carriage.

15 In relation to charges, it emphasised the need to
16 avoid unlawful discrimination and specifically referred
17 to the possibility of charging on the basis of average
18 costs. That's page 414. And in particular, of course,
19 what it put in place was an expected scheme of statement
20 of principles and then network access code being
21 developed.

22 What we've seen and heard from Mr Edwards was how
23 Dwr Cymru was concerned to properly comply with that
24 approach that Ofwat had adopted, and that there was the
25 promulgation of both the statement of principles and the

1 network access code by Dwr Cymru. in the course of the
2 relevant period in 1999/2000.

3 So I think it's also important to bear in mind that
4 Dwr Cymru wasn't simply sitting back and staying quiet
5 during this process. It wasn't. It was engaging
6 actively with Government and it sought out Ofwat to
7 highlight its concerns about issues arising concerning
8 the implementation of competition law, and in particular
9 common carriage. And it very clearly set out in its
10 response to Ofwat how it understood these sorts of
11 issues would be dealt with in its response to MD154,
12 which is at bundle 3, tab 32. Dwr Cymru set out
13 explicitly the principles it was assuming would apply in
14 relation to common carriage.

15 So that included, in particular at point 9, which is
16 page 419, the principle that charging would be on an
17 average pricing basis save where there was an
18 Ofwat-approved large user tariff already in place.

19 What we, therefore, have is an approach being
20 adopted early on in this period of consultation and
21 change where Dwr Cymru was making clear that that was
22 how it was thinking about things. Not surprising, given
23 that that is the approach that had been adopted
24 previously, the DNA, but it wasn't pretending otherwise.
25 It was making clear how it saw --

1 THE CHAIRMAN: That's what I find so curious, that there is
2 this involvement of senior managers in receipt of the MD
3 letters from Ofwat engaging with Ofwat as to what does
4 this mean, what's expected of us. Then there's
5 Mr Edwards and Mr Henderson in their team working out
6 how to do this. But yet, according to you, the evidence
7 shows that there was no interaction between those two
8 levels; that Mr Edwards wasn't given any instruction or
9 guidance, or his team weren't given any instruction or
10 guidance as to how to go about it. They just decided it
11 themselves, even though it seems that, for other
12 purposes, senior members of the board were interested in
13 the exercise.

14 MR BEARD: Well, let's go to 3/32, perhaps, just to look at
15 what was said. The relevant page is 419. Volume 3,
16 tab 32.

17 This is at the back of the response to 154. This is
18 the assumed principles on the basis of which Dwr Cymru
19 is operating. This is an articulation of what the
20 company thinks is the right way of doing things. That
21 is going to be the ambient climate, that is the way the
22 company was thinking about these things. It was
23 saying -- and in particular in relation to
24 principle 9 -- average pricing remains the charging
25 principle. You don't need instruction or any

1 specification when the assumed basis is the one that has
2 been in place and is rolling forward.

3 The fact that whilst this state of flux is in play,
4 people are going to Ofwat and saying, "Look, this is the
5 way we've been doing things for a long time, this is the
6 way we're going to be continuing to do things. If you
7 have any objection to this, you know, you should signal
8 it because this is the way we're continuing", that
9 doesn't mean that there needs to be specific
10 instructions fed in to anybody in relation to these
11 processes. To the contrary, because it is maintaining
12 the approach that has been applied previously, there is
13 no need for there to be specific instructions.

14 What is being said here is very clearly to someone
15 in Ofwat, "Look, this is the way we're doing things,
16 it's the way it's been, it's the way it's going to be.
17 We're making clear that these are the assumed
18 principles. If you don't like them, Ofwat, you should
19 tell us."

20 That, on the other hand, does not mean that there is
21 any requirement for there to be any sort of instruction
22 within Dwr Cymru to specify reasonable average pricing
23 in relation to any pricing methodology, because that was
24 the assumed basis on which people were operating.

25 Now, I'm conscious we started before two o'clock,

1 and I do have a little bit of a way to go. I wonder
2 whether now might be a convenient moment.

3 THE CHAIRMAN: Yes, we'll come back at --

4 MR LANDERS: I think what the Chairman was getting at was
5 that this was obviously a major issue for the board, and
6 they're talking to Ofwat and everybody else about it.
7 But we're asked to believe that Mr Williams' response,
8 for example, came to the board and said, "This is the
9 indicative price" and then a month later came and said,
10 "This is the final price, which is 20 per cent more" and
11 that he never asked himself why it changed, and nobody
12 on the board asked why it changed. They weren't
13 interested at all in the very first case that comes up
14 on a matter which you've just said was consuming them
15 and they were lobbying on. It just doesn't seem
16 credible.

17 MR BEARD: No, they weren't consumed by this case; they were
18 concerned about the Competition Act more generally, and
19 the issues arising in relation to it. This was one part
20 of it.

21 Obviously a magnifying glass, a forensic magnifying
22 glass is cast upon this aspect of it because this is the
23 for focus of this litigation. But in relation to what
24 was going on at the board, the idea that there was some
25 sort of nefarious scheme --

1 THE CHAIRMAN: Just putting aside the thought of a nefarious
2 scheme at the moment, just any scheme, any in
3 consideration at a senior level not including
4 Mr Williams, as to how would be the right way to go
5 about pricing a common carriage contract is just, you
6 say, an assumption that they would carry on with what
7 you say they had previously been doing, which was
8 average cost pricing and everyone assumed that was no
9 reason to tell Mr Edwards to do that because he would
10 have known that, and there was no debate of any kind
11 that anyone has ever referred to --

12 MR BEARD: Not -- [overspeaking] -- no.

13 THE CHAIRMAN: -- as to how that would work.

14 MR BEARD: No.

15 THE CHAIRMAN: Okay. I think that is probably a good point.

16 We'll come back at 3.10.

17 (3.02 pm)

18 (A short break)

19 (3.10 pm)

20 MR BEARD: During the short break, I was considering the
21 question that Mr Landers posed, the issue raised.

22 What we can see is plainly the default approach, the
23 assumed principle, regional average. That was the
24 company's DNA. Insofar as the board has strategic
25 input, that is clearly what's being accepted and what is

1 made manifest in the network access code. The fact that
2 there isn't a specific decision evidenced here, it may
3 be that it is simply a lack of memory, it may be that
4 any specific decision is just not a document that
5 continues to exist.

6 But what we do have is a very clear position for the
7 company in relation to this, a strategic position, one
8 that is being clearly articulated to Ofwat.

9 I also was just asking myself, apart from this, what
10 would have been the position if there had been
11 a specific broad statement that we had identified in
12 a document that said "applied regional average cost
13 pricing"? The outturn would have been the same. You
14 would still have had a situation where you were applying
15 regional average cost pricing which Ofwat then says is
16 perfectly proper and is the way the industry has been
17 working. So the fact that it is not specifically
18 articulated doesn't alter any of that.

19 THE CHAIRMAN: No, the inference that you're being invited
20 to draw is the fact that these documents don't exist
21 indicates they said something different, or might have
22 said something different.

23 MR BEARD: You can infinitely speculate about documents that
24 don't exist and you can say all sorts of things, but
25 there is not any good basis for that. You can't weave

1 this web of insinuation and speculation and suddenly
2 have a tapestry of conspiracy. It just doesn't exist.

3 I go back to the point I made earlier about this is
4 exemplary damages. You need clear and compelling
5 evidence in relation to these matters and you don't have
6 it. It is maybe frustrating that documents don't exist.
7 It is also a long time ago that these matters were dealt
8 with, and there is a lapse of memory, and it is plain,
9 indeed on both sides, that there are all sorts of
10 documents that must have existed at some point, but are
11 not included in the disclosure in the bundles.

12 Dr Bryan's diaries, for example, they have all sorts
13 of admissions. He had problems with the server and
14 recognised that there was a whole bunch of documentary
15 material that wasn't available to him. These things
16 happen. We recognise that. It doesn't mean that
17 somehow every sort of missing document is some sort of
18 smoking gun. You can't make that sort of inference
19 at all.

20 I've talked a little about MD163, and I've taken the
21 Tribunal back to some parts of the Ofwat 2004 decision.
22 The point to be made here is the suggestion that MD163
23 said you can't go forward on this sort of broad top-down
24 basis, regional average cost basis that was being put to
25 witnesses, is just plainly wrong. Mr Sharpe reiterated

1 the point in closing: it is still wrong.

2 The MD163 approach was an approach being articulated
3 by Ofwat, who clearly understood it as encompassing
4 regional average cost pricing. The fact it refers to
5 specific assets when you talk about the average
6 accounting cost is clearly focused upon the types of
7 assets that are being used, the point in the service
8 provision that you're talking about, rather than some
9 particular localised costing methodology focused on
10 a local identification of assets.

11 If it were any other way, the whole of the 2004
12 decision makes no sense whatsoever. I'm not going to
13 deal with that any further.

14 The truth of the matter was that Albion and
15 Dwr Cymru were both keeping Ofwat well apprised of the
16 approaches they were adopting. The negotiations between
17 the two of them were being copied into Ofwat. When
18 Ofwat became frustrated with the speed at which
19 Dwr Cymru was operating, Ofwat didn't hesitate to put
20 pressure on Dwr Cymru. Indeed, that was what generated
21 the initial indicative price, was that sort of pressure.
22 Now it is being suggested that there wasn't enough work
23 done in relation to the indicative price and it
24 shouldn't have been provided in that way. But, of
25 course, that is part of the picture here: that that 20p

1 price or 19.94 price was being generated at a time when
2 Ofwat was chasing --

3 THE CHAIRMAN: Just slow down a little bit because we have
4 to make sure the transcript catches your.

5 MR BEARD: I apologise to the transcript writer.

6 It is clear that Albion and Dwr Cymru knew that
7 there were differences of view in relation to these
8 matters, but as Mr Edwards and, indeed, Mr Williams have
9 emphasised throughout, the essence of what Dwr Cymru
10 were concerned about was not putting in place anything
11 unlawful. Because if Ofwat were to find that they were
12 doing something unlawful and wrong in the way that they
13 approached it, their relationship with Ofwat would be
14 damaged and their relationship with Ofwat was what was
15 so crucial to them, not because of this but because of
16 the relationship between Dwr Cymru and its regulator in
17 relation to a vast number of issues pertaining to its
18 price control and other regulatory interactions.

19 It's clear that Mr Edwards, in late 2000, was very
20 much focused on the iDok issue. The amounts of money
21 involved in the iDok discussion dwarfed anything that
22 was at issue in relation to anything concerning common
23 carriage at all. That was the focus. It is maintaining
24 a good regulatory relationship. That was very important
25 to Dwr Cymru, and that came across very clearly from

1 Mr Williams and Mr Edwards.

2 In our written closing submissions we've set out the
3 fact that it was plain from Albion's side that they
4 understood there was a debate about what methodologies
5 might be used in the negotiations between Albion and
6 Dwr Cymru, and that obviously Albion then escalated
7 these matters by way of a complaint to Ofwat. And it's
8 clear, both from the initial reaction to that complaint,
9 the initial thinking in the letter of 31st May 2001,
10 bundle 4, tab 152, and indeed subsequently in the final
11 decision, that Ofwat well understood these issues and
12 was concerned in relation to them.

13 When Ofwat wrote on 13th November 2001, which is,
14 just for your notes, at bundle 4, tab 162, it was very
15 clear, in particular on the following points relating to
16 the pricing methodology, and I won't go to the letter,
17 but first of all in its first bullet it says:

18 Dwr Cymru's approach was consistent with the
19 long-standing policy of charging customers on an average
20 price basis. There was no evidence of excess profits
21 being made by Dwr Cymru. Dwr Cymru was reasonable in
22 wanting to use average costs to set prices when charges
23 to its own customers were on an average cost basis.
24 Moving to calculate in particular charges on an actual
25 cost basis would result in the need for re-evaluation of

1 charges to a large number of customers, and such a move
2 could create winners and losers amongst customers
3 served.

4 So that range of considerations was at the forefront
5 of Ofwat's mind right at the beginning of the situation
6 of the complaint, and of course that's later reflected
7 in the outturn of the 2004 decision. Of course, that is
8 also reflected in that part of the decision where the
9 seven-step approach to the FAP was carefully scrutinised
10 by Ofwat.

11 So, in relation to those matters, it is clear that
12 Ofwat, just like Dwr Cymru, well understood that the
13 assumed approach, the basic approach, the default
14 approach that should be taken in relation to these
15 pricing issues was a regional average cost pricing
16 approach.

17 When the company thinks like that, when the company
18 has acted like that in the past, when the regulator is
19 thinking like that, you don't need instructions of any
20 specific sort. The strategic direction was clear. The
21 board was effectively able to allow the team to get on
22 with it, knowing that that strategic direction was
23 appropriate.

24 I'll move on to briefly dealing with the specific
25 FAP calculations because, of course, what is alleged is

1 that these calculations somehow manifest a cynical
2 disregard for Albion's right. In doing this, I will
3 spin through the closing at paragraph 310 onwards.

4 In summary, the evidence of Mr Edwards who is
5 responsible for the calculations which led to the FAP,
6 made clear the way in which those calculations were
7 developed and the reasons for them. There is no basis
8 for suggesting the calculations were carried out on
9 anything other than a basis of an intent to establish
10 a lawful price on the basis of methodology which was
11 acceptable to Ofwat. Neither Mr Edwards nor
12 Mr Williams, the responsible director, had any intention
13 of allowing an unlawful or abusive price to be issued,
14 nor were they reckless as to the price's lawfulness. It
15 was throughout their intention to ensure that the price
16 was lawful and acceptable to Ofwat for understandable
17 reasons.

18 The first access price process is described in some
19 detail, we heard extensive cross-examination of
20 Mr Edwards on this and what we know from both the
21 documentary material and the cross-examination and the
22 evidence-in-chief of Mr Edwards is that Mr Henderson
23 carried out a first calculation dated 29th November
24 where he considered the feasibility of applying the same
25 methodology which had been used by Dwr Cymru to derive

1 its large industrial user tariff for potable water.

2 As I say, I'm not going to go through these matters
3 in detail. They're set out in relation to
4 Mr Henderson's first calculations, paragraphs 318 to 322
5 in our closing.

6 Then there was an adaptation of further work by
7 Mr Henderson in relation to the relevant pricing, and
8 what we have was the second pre-FAP calculations from
9 Mr Henderson, which are contained in the document that's
10 found in 9A, bundle 9A, 354. This is dealt with in
11 paragraphs 323 to 327 in the closing, where Mr Henderson
12 was pulling together methodology using regional average
13 cost pricing in order to get some sort of common
14 carriage price generated.

15 But of course, what we know is that Mr Edwards then
16 reviewed those materials and looked at them, and we were
17 taken through his handwritten notes in much more detail.
18 And he recognised that Mr Henderson had made mistakes in
19 relation to that analysis. Of course, Mr Henderson's
20 analysis came out with two possible common carriage
21 access prices for non-potable water: one at 17p and one
22 at 27p.

23 What Mr Edwards did was look back at the material
24 that had been used by Mr Henderson, and in Mr Edwards'
25 first pre-FAP calculation he reviewed these matters and

1 it's considered at paragraphs 330 at 333. He looks at
2 those matters and he found that there was a salient
3 error in relation to those matters.

4 This is was explained in transcript Day 9, page 126,
5 line 24, to 127, line 20. He explained that
6 Mr Henderson had fundamentally erred in his allocation
7 between cost resources and treatment because he'd done
8 this on the basis of figures that summed operating costs
9 and gross capital values on an MEAV basis rather than
10 the return on those values. And it is that error that
11 Mr Edwards corrected in his first pre-FAP calculation.
12 It was that calculation that led to the access price of
13 19.94, the indicative access price.

14 As far as we understand it, there is no challenge to
15 the fact that that was an error by Mr Henderson in that
16 methodology of calculation, and Mr Edwards was
17 absolutely right to make that correction. He still,
18 however, didn't feel that the price was sufficiently
19 robust. It had been issued at a time when Dwr Cymru was
20 coming under pressure from Ofwat to issue a price. The
21 indicative price was put out, but Mr Edwards made clear
22 that it was only indicative and it needed to be taken
23 forward. That led on to the second pre-FAP calculation,
24 which is dealt with in the written closings at
25 paragraphs 334 to 341.

1 As we know, in relation to that certain
2 modifications were made in relation to the process that
3 was followed, and it's been suggested that the key
4 modification -- there was more than one modification
5 undertaken by Mr Edwards -- but it was said that
6 Mr Edwards engaged in financial or accounting trickery
7 by using the whole company water cost in this
8 calculation. He denies that. He says that he wasn't
9 engaged in any such process. What he was doing, he
10 said, was approaching the basis in the same way as he
11 had understood that it had been approached previously by
12 Denis Taylor in working in relation to these matters,
13 and certainly he --

14 THE CHAIRMAN: So you accept, then, that he approached this
15 with the aim of getting to the 26p figure that Mr Taylor
16 had got to, because that was approved by Ofwat?

17 MR BEARD: No, in relation to using the whole company cost
18 he was using something that he understood was a starting
19 point that Mr Taylor had used. That was what he was
20 saying. No, there was no target. There was no target
21 at all. Mr Edwards was very clear he wasn't trying to
22 seek any target whatsoever. There has at no point been
23 any evidence from anyone that Dwr Cymru was trying to
24 seek to achieve any particular target price at all.

25 I'm sorry, there is obviously a submission by

1 Dr Bryan in that regard that is different.

2 What was being suggested was that the whole company
3 cost suggested by Mr Cook and, indeed, Mr Sharpe was
4 a matter of trickery, although at one point Mr Cook said
5 although it was trickery, it wasn't wrong. I'm not
6 quite sure that I understand those moral differences.

7 If we go to Ofwat, bundle 5, tab 227, and turn up
8 paragraph 255, just a note, 255 says:

9 "First, Dwr Cymru began with its revenues from both
10 potable and non-potable supplies and then made an
11 adjustment to reflect the fact that this case involved
12 the treatment and distribution of non-potable water
13 only."

14 So there, Ofwat is setting out what it understands
15 is the basic starting point in relation to these
16 matters, and that's reiterated at 258, step one,
17 estimate of an average unit price for the supply of
18 potable water.

19 "In step one, Dwr Cymru estimated an average unit
20 price for the supply of potable and non-potable water."

21 So what has Ofwat understood in this regard? If one
22 turns back to paragraph 52, we can see that Ofwat had
23 specifically directed its mind to what was constituted
24 by potable and non-potable water that was then going to
25 be taken into account by the methodology that was

1 adopted by Dwr Cymru.

2 "Abstracted water can be supplied in one of three
3 forms: raw water, partially treated water and potable
4 water. Raw water and partially treated water can both
5 be described as non-potable water."

6 So Ofwat clearly knew what was being described in
7 relation to this methodology. It described it as the
8 whole company average methodology and it knew that it
9 involved potable and non-potable water, including raw
10 water. It was content with that approach. It was well
11 aware of that approach. It did not demur in relation to
12 that approach being adopted in relation to step one.

13 So going back to the whole company cost issue, Ofwat
14 knew what Dwr Cymru had done. Again, it wasn't anything
15 that was hidden. Ofwat was not troubled about it.

16 So to turn this into some issue of financial
17 trickery in circumstances where Mr Edwards quite plainly
18 said that wasn't how he was thinking about these things,
19 he wasn't looking at targets, he wasn't trying to engage
20 in any achievement of a higher price, he was
21 conscientiously doing what he thought was appropriate.
22 What we know is that Ofwat, with its eyes open,
23 considered that was an entirely appropriate way forward.

24 It may, just to complete the circle, be useful to
25 refer to a document that Albion itself had put in the

1 bundle. What we have there is a very clear indication
2 as to how the whole company cost was being dealt with
3 and, indeed, approved by Ofwat in those circumstances.

4 So it is obvious from Mr Edwards' evidence that far
5 from seeking to engage in any of the financial trickery
6 of which he was accused, Mr Edwards was working
7 diligently and in good faith to produce an access price
8 that was robust, supported by clear calculations that
9 could be understood and would be acceptable to Ofwat.

10 And just for notes: transcript Day 9, page 21, lines 14
11 to 21; page 34, 21 to page 35 line 1; page 89, 20 to 25; page 143, 5
12 to 17; 145, 15 to 19; 153, 16 to 22; and finally,
13 page 158, 7 to 9.

14 So in the light of Mr Edwards' explanation of each
15 of the pre-FAP calculations undertaken by Dwr Cymru, it
16 is also obvious that the purpose of Mr Edwards' pre-FAP
17 calculations was to rectify what he considered to be
18 errors in Mr Henderson's earlier calculations, not to
19 achieve a target price or revenue neutrality, as Mr Cook
20 and Mr Sharpe have suggested. Mr Edwards has also
21 explained why he undertook those corrections very
22 clearly and fully.

23 He explained in particular the indicative price
24 being issued under internal pressure and pressure from
25 Ofwat to get at least an indicative price out to Albion.

1 In January he didn't have time to devote to an immediate
2 review of Mr Henderson's work alongside his iDok
3 commitments, and in those circumstances, a less than
4 robust indicative price was better than no price at all.

5 Indeed, Mr Edwards' attitude to his pricing work in
6 this case is just the polar opposite of the state of
7 mind that's required as the basis for any exemplary
8 damages. He wasn't cynical; he was being conscientious
9 and scrupulous.

10 As it was, the regulator both understood the
11 approach that Dwr Cymru was taking and considered it
12 appropriate. In the end, the Tribunal concluded that
13 such an approach gave rise to an abusive price, in
14 essence, because a more granular approach led to lower
15 cost estimates, but that doesn't remotely suggest that
16 the approach adopted by Dwr Cymru at the time was
17 cynical or outrageous. And, of course, we've already
18 dealt with the fact that Mr Williams, as the director
19 who was responsible to Dwr Cymru board in relation to
20 these matters, does not believe that anyone within
21 Dwr Cymru undertook the FAP calculation with malicious
22 or improper motive. You can see that particularly in
23 his evidence at paragraphs 15 and 16.

24 He considered it was important that any price
25 offered should be lawful and acceptable to Ofwat. It is

1 clear he didn't recall details of the pricing
2 calculations, but he was emphatic that had anyone been
3 considering issuing an unlawful or even potentially
4 unlawful price in order to undermine Albion or indeed to
5 profit Dwr Cymru, he would have known about it and
6 recalled it.

7 That is entirely plausible. It may not be that he
8 understood all the details of what was going on, if
9 there was any project to run an unlawful price or,
10 indeed, a potentially unlawful price, that was a matter
11 that would clearly have concerned him.

12 This of course was consistent with the evidence we
13 have heard about the concerns at the relevant time about
14 the takeover of Dwr Cymru, and the risks that that would
15 have created for the then current owners and the
16 incoming owners in circumstances where approval was
17 required by Ofwat in relation to the takeover.

18 So we have a clear account of why an average price
19 was adopted, why it was reasonable for it to be adopted,
20 why Ofwat accepted it and why Dwr Cymru was seeking to
21 provide a lawful price.

22 Against that, of course, it is relevant. If it is
23 being suggested that Dwr Cymru would have run the risks
24 of seeking to put in place an unlawful or potentially
25 unlawful price, those risks would have been huge for

1 Dwr Cymru. There was the takeover requiring approval,
2 there was the important regulatory relationship with
3 Ofwat upon which vast sums of money turned. There was
4 the more general reputational risk particularly into
5 Dwr Cymru which was coming in on the basis that it was
6 to be established to the benefit of customers to trade
7 fairly and ethically. It was clear, fourthly, that
8 there was every prospect of Albion pursuing the matter
9 with Ofwat, which of course was able to impose fines.

10 So there was no sense that Dwr Cymru could ever
11 expect a sort of stay below the radar in relation to
12 these matters. Fifthly, the involvement of Ofwat would
13 have risked a financial penalty which, understanding the
14 fine guidance, could have been up to 10 per cent of
15 turnover, and therefore could have been very large if an
16 abuse had been found by the regulator.

17 Sixthly, in addition to all of those considerations,
18 there was every chance that if Dwr Cymru would have been
19 found to breach competition laws, in addition there is
20 a risk of damages claim against it.

21 Therefore, quite apart from the proper desire to act
22 lawfully, there was every reason for Mr Edwards and
23 Mr Williams and all at Dwr Cymru not to engage in
24 conduct that would amount to an abuse because of the
25 very high risks involved.

1 I will now move briefly on to one or two other
2 issues that Albion have raised in relation to matters
3 pertaining to exemplary damages. There has been all
4 sorts of references to the risk of competition and the
5 documents prepared for board meetings, or discussion
6 documents, refer to risk from competition and the fact
7 that competition has potential to put some or all of
8 large user customary income at risk. That's absolutely
9 true, but it's also a statement of fact. It would be
10 entirely appropriate that a management board should be
11 aware of such matters. The fact that they're written
12 down doesn't suggest anyone within the organisation
13 would seek to engage in nefarious activity to protect
14 that revenue. There is just no basis for such an
15 inferential leap.

16 The paper referred to on numerous occasions fairly
17 recognises that with the advent of the Competition Act
18 1998 there were both threats and opportunities in
19 relation to Competition Act, and we note bullet 2 on
20 page 562, bundle 3, tab 52, that talks about the
21 opportunities.

22 In relation to the threats identified in the tables
23 which Mr Sharpe has taken the Tribunal -- I won't take
24 you back unless you specifically want to. It's the one
25 that goes through all the various arrangements and talks

1 about the total value of them -- it is striking that the
2 consideration isn't just -- it's not in relation to
3 common carriage, particularly. In fact, in relation to
4 Albion, the threat is said to be by bulk supply,
5 ie inset appointment for common carriage.

6 So the focus even then, it's not about common
7 carriage, it's about how competition is developing more
8 generally. It is not a suggestion of some targeted
9 focus on common carriage at all.

10 The fact that those matters are being looked at
11 doesn't suggest that Dwr Cymru was focused on providing
12 common carriage or other prices that were abusive,
13 whether to Albion or, indeed, to anybody else. In fact,
14 the accurate appraisal and risks and opportunities in
15 this paper doesn't suggest any project to undermine
16 Albion. To the contrary, it suggests a company that was
17 responsibly considering the potential impact of new
18 legislation in the area.

19 There have been new documents or further documents
20 that have been disclosed as a result of searches carried
21 out at the request of Albion following the disclosure of
22 the Hyder report. Mr Sharpe referred to them in his
23 closing. They are all of a part, the documents
24 concerned with the Competition Act being rolled out
25 dated 1999 are all of a part with a company

1 conscientiously considering up and coming regulatory
2 changes. There's no indication or basis there for
3 saying they are specifically seeking target arrival or,
4 indeed, act unlawfully in any way.

5 In relation to the use of potable costs to calculate
6 a non-potable price, that's suggested as being another
7 basis on which Dwr Cymru was acting cynically. But
8 there's no basis for suggesting at the relevant time
9 Dwr Cymru was taking an inappropriate approach to that
10 sort of distribution costing analysis in the FAP, let
11 alone one that somehow amounted to cynical conduct.

12 If I may, I'll just turn back to the Ofwat decision,
13 bundle 5, tab 227, paragraph 298. Turn to paragraph 297 on
14 page 1507. This is consideration of step six in the
15 methodology that was being analysed by Ofwat.

16 "Estimate the unit cost of non-potable bulk water
17 distribution:

18 "Dwr Cymru estimated the unit cost of non-potable
19 bulk water distribution. It assumed that the cost of
20 transporting non-potable water in bulk was the same cost
21 of transporting ..."

22 So Ofwat are very well aware of this. Nothing
23 hidden, nothing misled.

24 THE CHAIRMAN: Isn't -- well, maybe you're coming to it.

25 Go on.

1 MR BEARD: Albion are arguing that actually there were lower
2 costs associated with non-potable bulk transport and
3 much higher costs associated with bulk potable
4 transport. So that was the allegation that was
5 foursquare before Ofwat. It then considered those
6 matters in a meeting with Dwr Cymru and the officials of
7 the regulator.

8 At 300, the conclusion was reached that it was
9 reasonable in relation to these matters to consider that
10 the cost drivers for transportation were relevantly
11 similar.

12 THE CHAIRMAN: Just wait a moment. (Pause)

13 Is it right to say that in coming to this
14 conclusion, this conclusion and the reasoning behind it
15 that Ofwat was explaining, was on the basis that one
16 couldn't actually work out whether the costs for bulk
17 distribution were different for non-potable water as
18 compared with potable water, whereas what the
19 information that has been recently disclosed shows is
20 that actually it was possible to work out what the costs
21 of bulk distribution of non-potable water were, so that
22 one didn't actually have to go through this whole
23 process of trying to adjust the whole company costs to
24 get to the non-potable costs?

25 MR BEARD: No, I don't think that's right. What you see at

1 299, there's an outline of some of the issues discussed
2 in the meeting and Dwr Cymru was saying a pipe is a pipe
3 irrespective of what it's carrying.

4 Then it referred to an agreement it had with United
5 Utilities in relation to these matters, which sets out
6 the terms under which water supply services are operated
7 and maintained and which itself doesn't distinguish
8 between the costs associated with potable and
9 non-potable mains. It is just referred to as trunk
10 mains.

11 So, actually, there it's referring not to the
12 absence of information but the way in which Dwr Cymru
13 and United Utilities are conducting themselves in their
14 dealings and attributing costs under these agreements to
15 these matters. So, no, it's not saying that at all;
16 it's actually looking at what's going on.

17 MR COWEN: Perhaps we can refer to page 1526, paragraph 381.

18 MR BEARD: I don't think there's any dispute about the
19 contents of 381. What's being said there is that the
20 basis on which the first access price was provided was
21 on the regional average cost basis.

22 If you're providing calculation on a regional
23 average cost basis you're not there looking to provide
24 local cost data. This is obviously in the context of
25 the allegation that there wasn't a proper justification

1 of the first access price, and what was being said there
2 was actually there was. It didn't produce local cost
3 data because that wasn't material to the methodology
4 actually being applied, and we're happy with the
5 methodology being applied, therefore there was
6 sufficient justification. So I don't think it is
7 suggesting anything of the sort.

8 I know Albion was trying to suggest that Dwr Cymru
9 were constantly trying to withhold information, but the
10 point is that Dwr Cymru was going ahead with the
11 regional average cost methodology basis, he made clear
12 how it was approaching that. The local costs
13 information just wasn't material to the assessment of
14 whether or not that was right, or that was the
15 understanding at the time.

16 We now know, when we swing forward X number of
17 years, that the Tribunal says you should have done
18 a cross-check, and indeed it says you should have done
19 a more granular approach. But that is not some sort of
20 wilful withholding of relevant material at all, and
21 there's no suggestion of that from Ofwat.

22 As I say, when we go back to the point which was
23 just being raised in relation to potable and non-potable
24 distribution costs, there's not a suggestion that there
25 is material being withheld. Instead, Dwr Cymru is

1 actually providing concrete evidence with a third party
2 and saying, "Look, this is how we actually treat this in
3 practice. You should take this into account because
4 this is what we're doing. We're not just telling you
5 what we do; we're actually showing you what we do in
6 relation to these matters."

7 At 300 it is concluded that it is not a wrong
8 approach.

9 I think it is also worth in passing just touching on
10 the referred work, because Mr Cook sought to suggest in
11 cross-examination, and Mr Sharpe in closing, that it was
12 self-evident that there was a cost difference. We say
13 that's not the case. When it came to the referred work,
14 which was a different discrete exercise carried out
15 specifically on the terms the Tribunal had considered,
16 there was a different outturn analysis of the transport
17 and distribution costs in relation to potable and
18 non-potable.

19 We can see that if we turn very quickly to tab 274
20 in bundle 8. I'm just going to go to one or two matters
21 in relation to this. If we could go to 2397, this is
22 consideration of water mains. There is just a paragraph
23 I do want to highlight. 7.79:

24 "The authority understands that the FAP and the
25 director's decision on fairness of that price was

1 actually based on the use of larger pipes of
2 600 millimetres and over."

3 Now, Mr Cook, in cross-examination, talked about, in
4 particular, paragraphs 7.85 and 7.86 and highlighted
5 that, in relation to pipes of 300 to 600 millimetres,
6 a weight of only 10 per cent of the relevant costs,
7 capital costs, should be attributed in this calculation,
8 and in 7.86, only 50 per cent of the costs of greater
9 than 600 mm pipes.

10 He was then saying this shows there's actually
11 a vastly different approach.

12 First of all, turning on to 7.88:

13 It is worth emphasising this referred work was
14 a very different stand-alone exercise in the context of
15 the particular case, and Ofwat were very concerned to
16 say, as such, it has no automatic consequences for
17 general tariff setting.

18 So it was putting down a marker there that actually
19 this was somewhat of an unusual approach to be
20 undertaken.

21 Yes, it is quite right that the outturn assessment
22 of distribution costs and comparative distribution costs
23 for potable and non-potable mains was reached here after
24 that very different exercise had been undertaken. But
25 actually, Mr Cook rather oversold the issue in this

1 regard because, of course, the FAP, as 7.79 indicates,
2 was based on the costs of larger pipes above
3 600 millimetres. What this is saying is you only take
4 half the cost of the above 600 millimetres pipes, but
5 you actually take 10 per cent of the costs of the 300-
6 to 600-millimetres pipes into this equation. So you're
7 taking something away in relation to the overall
8 weighting in relation to over 600-millimetre pipes, but
9 you're actually adding something in relation to the
10 under 600-millimetre pipes in relation to this analysis.

11 So it is just a very different analysis and
12 a different approach being adopted. And to suggest that
13 it all moved in one direction away from the position
14 that was being adopted previously and Ofwat had adopted
15 previously is just wrong in these circumstances.

16 The next topic I'm going to move briefly on to is
17 the use of the 30 per cent multiplier for non-potable
18 treatment.

19 THE CHAIRMAN: I think we've probably got everybody's
20 submissions on that.

21 MR BEARD: Can I pick up two points, if I may?

22 THE CHAIRMAN: Yes.

23 MR BEARD: Bundle 2, tab 6. This was a document put into
24 the bundle, as I say, by Albion. It is document from
25 1996, it's a Dwr Cymru document concerning non-potable

1 supplies and the bulk supply by Albion.

2 There are two things I wanted to refer you to. The
3 first is on 153. This is material from Denis Taylor,
4 DS Taylor. If you go on to 155, there's a table setting
5 out the non-potable tariff calculation, appendix 2.

6 There we have, second line in that table:

7 "Treatment for non-pot, 30 per cent."

8 Here we have a Denis Taylor analysis setting out
9 that split.

10 Now, as we know, that split was used by Dwr Cymru in
11 its FAP calculations. When it came to dealing with
12 Ofwat, it said, "Actually, we've looked at this again
13 and we think it should actually be 15.2."

14 So it was Dwr Cymru who said, "Actually, we think it
15 may be too high". Just for your notes, that is
16 recognised in the 2004 decision, paragraphs 294 to 296,
17 bundle reference 5, tab 227, page 1506.

18 But it's actually just worth noting, if we may go
19 back to bundle 8/274 and the referred work, now
20 obviously, again, this is a different exercise being
21 carried out, but an analysis was carried out in relation
22 to water treatment at page 2389 onwards. I won't invite
23 the Tribunal to read all of this section, but what is
24 going on here is consideration of water treatment. And
25 it might be worth just noting actually that, at 7.37:

1 "Dwr Cymru (...read to the word...) the Director adopted
2 15.2 per cent as the non-potable water treatment weight
3 ..."

4 This was the one that Dwr Cymru had suggested would
5 be more appropriate.

6 Then there was a concern expressed as to whether or
7 not that was right, and further work was done in the
8 course of the referred work.

9 What we see is that a more refined approach is
10 taken. But actually, in 7.47, the AAC plus model comes
11 out with conclusions -- it is relevant for the AAC plus
12 model -- which actually put in place a higher weighting
13 back towards 30 per cent in relation to capital cost and
14 15 per cent in relation to operating cost.

15 So again, it is an illustration of the fact that
16 when you take different approaches to these matters and
17 you refine the approach, or change the approach, you
18 come out with different answers. Dwr Cymru was acting
19 conscientiously in going back on the 30 per cent. The
20 30 per cent was a sensible starting point and it had
21 been used reasonably. It was used in the context of
22 a price being pulled together so that a price could be
23 offered to Albion. When further consideration was given
24 to these issues, Dwr Cymru was forthcoming and explained
25 that actually it thought a lower figure was appropriate.

1 But actually, when it came to the referred work, there
2 was less to see because, in fact, the measures in
3 question should have been higher.

4 Then we've already touched on irrelevance and
5 unavailability of local cost information. I've
6 explained why it is that Dwr Cymru approached matters on
7 a regional average cost pricing basis. It wasn't
8 withholding information in relation to those matters; it
9 wasn't seeking to, or indeed misleading, Ofwat. The
10 relevance of that to the FAP calculations itself is
11 difficult to understand in circumstances -- in any
12 event, difficult to understand in circumstances where
13 the calculations have been properly explained.

14 We've been to some of the witness evidence of
15 Christopher Jones, but in particular that's found in
16 bundle 6/240 and bundle 6/241, those tabs which talk
17 about the limitations of the information available and
18 the ability to use and rework these limited materials.

19 Now, much play has been made of the Hyder report --

20 THE CHAIRMAN: Are you saying that Mr Jones in his witness
21 statements was referring to this Hyder --

22 MR BEARD: No, what I'm saying is that in relation to
23 Mr Jones -- I'm dealing with this rather quickly -- he
24 had access to the relevant databases and had gathered
25 material and looked at it. What he explains in his

1 witness statements is even when you gather all of this
2 material, you still have a big exercise to do in order
3 to assess what the relevant local costs are, and it is
4 just not a straightforward exercise at all. So this
5 idea that, you know, you could just type something in,
6 pull up a couple of costs and away you go, is just
7 wrong. And Christopher Jones deals with that in some
8 substantial detail.

9 MR COWEN: I thought it was in a slightly different point,
10 but I just want to make sure I have it clear. The local
11 costs are what they are; I thought Christopher Jones's
12 evidence was that in a water company, there is
13 a tremendous amount of fixed and common costs that need
14 to be allocated or, in your language, smeared across,
15 rather than, you know, in some way to the -- so the work
16 that needs to be done isn't really in relation to the
17 local costs; it's in relation to the fixed and common
18 costs.

19 MR BEARD: That's undoubtedly part of it, but he also says
20 that there are difficulties in identifying what the
21 relevant values for local costs are as well and the
22 difficulties that are used in relation to that. We can
23 go to those witness statements if it is of assistance,
24 but I mean, there's quite extensive discussion of these
25 matters because a series of points was put by the

1 Tribunal that he was effectively answering in relation
2 to those issues.

3 What it shows is that trying to calculate local cost
4 is not that straightforward, whether or not you have
5 these databases available to you. The reason I connect
6 it to the Hyder report is because of the evidence given
7 by Mr Edwards in relation to the Hyder report. He said,
8 well, that's jolly interesting, but it wouldn't take you
9 far enough to be able to actually ascertain these
10 relevant local costs.

11 THE CHAIRMAN: Why doesn't Mr Jones's evidence refer to the
12 Hyder report?

13 MR BEARD: That's not something I can answer. I assume
14 because Mr Jones didn't have the Hyder report in
15 relation to those matters, but I'd have to go back and
16 check that.

17 MR LANDERS: But Mr Jones didn't suggest that the working
18 from local costs and smearing the other costs on top
19 of it was anything like as complicated as the process
20 that actually went through to start off with, potable
21 prices and then cascade down, did he?

22 MR BEARD: I think he does, yes. In fact, I think he says
23 it's more complicated.

24 I think that's precisely what he's saying. He's
25 saying that bottom-up methodologies are more complicated

1 than top-down in the water industry. That's precisely
2 what he's talking about.

3 THE CHAIRMAN: But if he didn't know about the Hyder report,
4 then that must cast a bit of doubt on his conclusion,
5 because he obviously didn't know that quite a lot of
6 work had been done --

7 MR BEARD: I'm not sure one can go that far because I think
8 it presumes to some extent the submission that's been
9 made on the Hyder report without it being further tested
10 in circumstances where Mr Edwards said, "Actually, that
11 doesn't take you very far". What the Hyder report --

12 THE CHAIRMAN: When did Mr Edwards say that?

13 MR BEARD: It was in re-examination at the end of his --

14 THE CHAIRMAN: But we hadn't seen the Hyder report by that
15 point.

16 MR BEARD: Yes, we had. The Hyder report was disclosed the
17 day before his evidence.

18 THE CHAIRMAN: Oh, yes.

19 MR BEARD: I can find the reference in the transcript, but
20 we were concerned to ensure that the document that had
21 been referred to by Mr Edwards was made available so
22 that he could be cross-examined in relation to it. We
23 made efforts to make sure that was the case.

24 MR SHARPE: I wonder if my friend could take you to the
25 transcript here because I'm afraid his recollection

1 differs significantly from mine in relation to Mr Cook.
2 And rather than misrepresent Mr Cook, it might be
3 sensible to just conclude the point by looking at the
4 record.

5 MR BEARD: Let's go to Day 10, page 177, I think.

6 I don't know if the Tribunal has that. Turn to
7 page 177. (Handed)

8 THE CHAIRMAN: Yes.

9 MR BEARD: Just read line four down to line 18. I won't
10 read it out.

11 THE CHAIRMAN: Yes.

12 MR BEARD: There, Mr Edwards was considering whether or not
13 he'd be able to create a sort of stand-alone price for
14 common carriage just using that Hyder data. He's
15 saying, "No, that's not what I could do. I'd need other
16 information in order to be able to do it. That isn't
17 what I'd be able to create."

18 He refers to some of the sorts of other data that he
19 would need apart from the capital value; so operating
20 costs, maintenance costs, infrastructure renewals. So
21 those are costs and matters that would have to be taken
22 into account even if you're doing a bottom-up
23 calculation, is what Mr Edwards is saying here.

24 THE CHAIRMAN: Yes.

25 MR BEARD: I think that maybe echoes the point I was making

1 about Mr Jones's evidence that not only are there common
2 costs issues that require attribution, but there are
3 also local costs issues that go beyond what you can pull
4 off a particular database.

5 Going beyond the Hyder report to some of the other
6 documents very briefly, obviously those documents
7 haven't been put to a witness. We recognise that they
8 were provided after searches were conducted following on
9 from Mr Edwards' reference to the Hyder report and
10 requests being made. But with respect, Mr Sharpe's
11 speculations about their interpretation are simply not
12 sufficient.

13 We know that they didn't feed into Mr Edwards'
14 approach to the FAP, and the fact that communications
15 and e-mails does peter out doesn't suggest anything
16 about a putative conspiracy. There might be all sorts
17 of reasons why further work wasn't pursued.

18 Fifthly, it's just not accepted that this documents
19 were wrongly not provided to Ofwat, and I'm instructed
20 that on review in fact the Hyder work is considered to
21 be deeply flawed, but that is a separate matter.

22 Indeed, a passing comment on disclosure more
23 generally is warranted. The disclosure exercise was
24 done properly and conscientiously. A disclosure
25 statement was provided. There were various exchanges

1 about additional disclosure. Some requests came from
2 Dwr Cymru, some from Albion, and I can take you through
3 the correspondence, but it is perhaps not necessary.

4 The fact that later on, on the basis of the
5 statement made by Mr Edwards, who is supposed to be
6 concealing and dissembling, further document searches
7 were then pursued and further documents identified
8 doesn't in any way suggest that there is some sort of
9 conspiracy to conceal or dispose of material. Quite the
10 opposite.

11 So concluding on exemplary damages on the substance,
12 what we have is a situation where there is simply no
13 basis for a finding of exemplary damages to be made.

14 Mr Sharpe very skillfully has tried to spin a web of
15 inference and speculation, but it does not make for a
16 basis for an exemplary damages finding. After numerous
17 hearings and two occasions on which the specialist
18 regulator found there was no infringement, the Tribunal
19 did finally conclude that Dwr Cymru had imposed an
20 excessive price, but this was far from a straightforward
21 case. Even Dr Bryan recognised that these pricing
22 issues involved complexity and uncertainty.

23 In order to make its findings, the Tribunal had to
24 consider carefully complicated and contentious issues as
25 to cost allocation and price calculation. That's

1 precisely the sort of chapter 2 case where exemplary
2 damages would be wholly inappropriate in any event.

3 Indeed, the very fact that privy to all of the
4 relevant material, Ofwat was able, in its 2004 decision,
5 and later in the referred work to conclude that the
6 method by which the FAP was proceeded on didn't
7 constitute an unfair excessive pricing abuse, and indeed
8 did so in relation to the specific figures involved,
9 simply emphasises how misguided Albion's approach to
10 exemplary damages is.

11 In circumstances where, after a long process of
12 hearing detailed information and the specialist
13 regulator concluding price wasn't abusive, the
14 suggestion that the infringement was somehow outrageous
15 or cynical when there was such a level of uncertainty on
16 the fair pricing and the methodology was clearly being
17 adopted as to regional average cost pricing, in
18 circumstances where it had been long in place -- see
19 bundle 3, tab 32, page 419, point 9 -- that the powers to develop the
20 access code were delegated, and in bundle 3, tab 52,
21 page 562, that in those circumstances no decision was
22 needed by Albion specifically because the approach to
23 average pricing had already been taken in the access
24 codes in particular cross-examination of Williams, Day
25 7, page 152 line 9 to 153 line 8, and page 154 line 19 to 155 line 11.

1 We know that Mr Edwards was involved in the access
2 code. He dealt with these matters at transcript Day 8,
3 154, lines 11 to 15, and page 176 line 24 to page 178 line 9 in
4 particular, as

5 well as in his first witness statement, there is simply
6 no basis upon which it would be appropriate to proceed
7 to any finding of exemplary damages.

8 Now, in our closing submissions, we have set out at
9 paragraphs 409 to 422 some submissions in relation to
10 quantum on exemplary damages. We hope that assists the
11 Tribunal, and the understanding of the topic which we
12 say in the circumstances is entirely irrelevant to the
13 Tribunal's decision in relation to these matters.

14 Perhaps the last comment to make is just in relation
15 to interest. We don't understand any issue in relation
16 to interest is pursued. We've heard no evidence or
17 submission in relation to it. Orthodox principle of
18 simple interest plus 1 per cent is the way forward.

19 In those circumstances, unless I can assist the
20 Tribunal further, those are the submissions of Dwr Cymru
21 in closing.

22 THE CHAIRMAN: Thank you very much.

23 MR BEARD: I'm grateful.

24 THE CHAIRMAN: Mr Sharpe?

25 MR SHARPE: I'm happy to start, but should we give the
26 transcribers a moment or two?

1 THE CHAIRMAN: Yes, we'll take five minutes until 4.20.

2 (4.15 pm)

3 (A short break)

4 (4.20 pm)

5 Submissions in Reply by MR SHARPE

6 MR SHARPE: Madam Chairman, members of the Tribunal, I rise
7 for the last time in this saga. I'm very conscious that
8 there are limits to endurance even for this Tribunal,
9 and I suspect Mr Beard may well have strained them
10 already. I don't intend to keep you very long, and just
11 have a few remarks properly in reply.

12 As we've heard most recently in relation to
13 exemplary damages, may I start there and then work
14 through some of the necessary foothills in the
15 compensatory side.

16 First of all, Mr Beard suggested there was no
17 instruction to Mr Williams or his team. He linked that
18 to Mr Edwards' evidence that Welsh Water simply carried
19 on the averaging pricing because it was in their DNA.
20 Now, I made some submissions on this yesterday, but in
21 our submission that can't be true, certainly when it
22 comes to non-potable large industrial contracts; in
23 particular, pricing non-potable water by reference to
24 average potable costs, the treatment equality which
25 we'll come on to, and the distribution equality we'll

1 come on to later.

2 First of all, you heard Mr Williams. We were
3 surprised by the quality and depth of his evidence. He
4 was a director, a main board director, a member of the
5 LCE. He professed at paragraph 14 of his witness
6 statement to have a broad view, and he was designated to
7 be the sponsor of these documents. And we assumed --
8 reasonably, I think -- from that that he would be their
9 champion in the LCE and on the board.

10 Put at its most charitable, that seems most
11 unlikely, but somebody had to understand what was going
12 on and explain it to the board. And when I put it to
13 Mr Williams, he readily agreed: it was Dr Brooker. And
14 you'll recall the exchange. He wasn't sure, but it was
15 very likely, I think he put it very emphatically, that
16 it was Dr Brooker.

17 So I think we're entitled to draw the attention of
18 the court to Dr Brooker's absence in this saga, and also
19 his man, Mr Holton. And I don't think it is entirely
20 necessary, but I'll go back to the Pennon case later on
21 briefly. I think you probably don't need any further
22 submissions, but I'll give you two minutes on it anyway.

23 We go back to the DNA. This was all in the DNA and
24 all they were doing is what they've always done, and
25 what could be simpler than that? Ofwat understood that

1 as well, so what are you complaining about?

2 We know that is not true, and we know it from three
3 things: first, the detailed and, presumably, expensive
4 work that Welsh Water undertook to determine non-potable
5 costs in the Hyder study. Now, we know specifically
6 from the introductory paragraphs, to which I took you in
7 my attempted and very hurried overnight analysis of that
8 document, that it was created specifically for the
9 purpose of creating a non-potable tariff. And it was
10 part and parcel of a programme of work which I think the
11 Chairman identified on the first page, a non-potable
12 asset study calculating non-potable by reference to
13 either average non-potable costs or, as you'll recall,
14 what they call bespoke systems, which were technically
15 discrete, we submit Heronbridge, and by reference to the
16 costs of that system.

17 That work continued for several months and then it
18 stopped. Now, the e-mail underlying exchange, which of
19 course we did not get and my learned friend Mr Cook did
20 not have that when he was cross-examining Mr Edwards,
21 emerged under pressure and we got it at noon on
22 Wednesday, 24 hours or so before we had to submit our
23 submissions to you. And in the circumstances, I don't
24 think we did a bad job in trying to understand what was
25 going on.

1 If we'd had it, I am certain we would have asked
2 Mr Edwards a different question. He was asked: would
3 this be useful or enough for a pricing study for
4 non-potable assets? And he said, well, its only half
5 the story, it's only part of the story. But I think we
6 might have put it to him: what happens if you'd had
7 Mr Brotherton's operating costs and above-ground data?
8 Would he have got the same answer?

9 I can't, unlike my learned friend, give any evidence
10 on that, but it would have been very nice to be in
11 a position to ask it. I note at this late stage we've
12 not had any expression of -- well, first of all, any
13 explanation as to why these documents should have
14 appeared so late, still less an apology. But in any
15 event, we know that study existed, we know it was
16 accompanied by parallel work undertaken by
17 Mr Brotherton. We know Mr Edwards was involved in that,
18 as was Mr Henderson, deeply involved, and in fact
19 Mr Henderson seems to be the lead man on the project,
20 but always reporting onward.

21 What is important, what my friend doesn't really,
22 and cannot explain, is why it stopped. There is an
23 abrupt rupture in November, after which there are no
24 further e-mails to Mr Brotherton saying, "Can we have
25 this work refund?" No further exchanges obviously with

1 Hyder because they'd submitted part one, I suppose, of
2 their report, and it comes to an end.

3 My friend says you can't possibly draw any
4 inferences from what's not there. In this case, of all
5 the cases I've ever been in, it is one case where
6 I think we are entitled to submit that we can draw
7 inferences from a highly selective and incomplete
8 recording. And we were right to be deeply sceptical
9 throughout this case, that the quality of disclosure has
10 been lamentable. It is a great pity that what has been
11 disgorged at the very last minute, which has actually
12 proved so valuable to our understanding of the case, has
13 come so late and after, essentially, we were in
14 a position, meaningfully, to cross-examine their
15 witnesses.

16 Now, in our submission, not merely did the work come
17 to an end, but that also indicates that a clear decision
18 had been made to reorientate the nature of the work that
19 was being done. To some extent, we can carbon date that
20 no later than 6th November 2000, because you will recall
21 the board minute, that slender two or three lines in the
22 board minute, which we've been shown, made it very clear
23 how important averaging had become.

24 In our submission, it is as plain as day, they had,
25 as it were, done the maths and they'd come to the

1 conclusion, which was only ultimately evident many years
2 later, that the access charge would actually be
3 significantly low enough to afford Albion a significant
4 profit, and thus leach their profits away, both at
5 Ashgrove and possibly elsewhere.

6 I can't be certain about that, but the inference,
7 the strong inference, that I make and ask you to accept,
8 is that the world had changed within Welsh Water, and by
9 the 6th November they'd come to the conclusion that an
10 alternative strategy was needed in order to maintain
11 revenue neutrality.

12 That's my first point in relation to the DNA.
13 Secondly, let's take the argument head on. Welsh Water,
14 when they continued the work, did not follow established
15 methodology. We see from Mr Henderson's e-mail of
16 29th November -- for your note, bundle 3, tab 90 -- but
17 if I said this is the "eat me" e-mail, you will
18 remember, I think. He didn't say, "I'm just carrying on
19 from Denis Taylor in the old days". He was working out
20 a new methodology from scratch. And what was he doing?
21 He was starting with a target price for 26p, the "minded
22 to" price that Albion had paid for bulk, and trying to
23 find a methodology, working back to justify an access
24 price, because if you know what the resource price was
25 and you can deduct the resource price from the 26p,

1 that's your target.

2 In our submission, that is a clear link, and that
3 date was 29th November, three weeks after the board
4 meeting, that revenue neutrality was the objective
5 within Welsh Water. It is a fair bet, a reasonable
6 inference, that Dr Brooker, either through Mr Holton or
7 through Mr Williams, made it clear to Mr Henderson,
8 "This is what you've got to do for us in order to
9 maintain revenue".

10 We've no record of that, of course, and I'd die of
11 shock if we saw it. And Mr Holton and Mr Henderson are
12 not here to tell their story. Mr Williams, he has
13 probably forgotten, so we didn't really get to it.

14 That's the second submission in relation to the fact
15 that it wasn't in the DNA. The first one, new work,
16 Hyder. Second one, Henderson starting new methodology.
17 Thirdly, we can look at the work that he did. In
18 particular, once again, newly disclosed documents, and
19 I'm referring for your note to bundle 19, tab 58.

20 Here, he analysed non-profitable prices --
21 Henderson -- I'm so sorry -- he analysed the non-potable
22 prices and said they were based upon the Albion price,
23 and cost allocations for which there was no supporting
24 information. You may recall I took you to this document
25 yesterday. In an appendix, he's very frank: "DT did

1 this work. Albion price." Probably 1996 in the
2 submissions to Ofwat.

3 I don't want to give evidence, but that's my
4 reasonable inference when he did the work because that's
5 where the 26p eventually came from.

6 We know now, from his 2000 -- this document, that
7 there was no supporting information. We also know from
8 another Henderson document -- for your note, it's
9 bundle 9A, 354 -- you may remember this is his analysis
10 looking at height, widths, 10p price for the largest
11 users, 22 to 26p for the medium users and 30p for the
12 smallest user. You may remember that, and he was
13 looking at the costing structure. And of course, again,
14 the special register itself. We know from these three
15 pieces of evidence that Welsh Water had not carried out
16 its existing non-potable pricing on the basis of average
17 costs; it was looking at it first from a situation where
18 he acknowledged there was no supporting information, so
19 how on earth can it be an average cost if there's no
20 evidence? Secondly, he's looking at it from a cost base
21 of prices of pipes, pipe size. Then I took you to --
22 and you've been taken several times -- to the special
23 agreements register, which, however you look at it, does
24 not betray any uniform of any application of cost
25 methodology.

1 What it does do is betray bargaining power between
2 Welsh Water and large customers who were naturally
3 favoured necessarily at the expense of smaller customers
4 who paid more, as you would expect.

5 Rather than (inaudible) through all that, Mr Beard
6 was at pains to suggest that Welsh Water was simply
7 doing what they'd always done. But in our submission,
8 that could not be further from the truth.

9 Now, early November we have the new situation. We
10 think there was a clear and deliberate decision to price
11 Albion's non-potable common carriage application on the
12 basis of something called average distribution costs.
13 Now, even that's a misnomer, as we now know, because
14 they weren't average distribution costs; they were
15 potable distribution costs.

16 We also know why that decision was made. It was to
17 produce revenue neutrality. Incidentally, a point my
18 friend did not avert to: We see from the board minute
19 itself and from Mr Henderson's e-mail, that he starts
20 from that 26 price and tries to justify it.

21 To move on, in terms of how they got to the first
22 access price, we've put out in our written submissions,
23 and respectfully, you're on top of that, but
24 nevertheless I'm still going to spend a moment or two
25 dealing with the key elements. Well, the 30 per cent

1 treatment figure. We're aware of that. We're also
2 aware, aren't we, that Ofwat were told -- and this is in
3 the document you saw this afternoon -- that it was done
4 on the basis of cost studies. We know later it was done
5 on the basis of conversations with local managers. We
6 also know it was a mere 100 per cent wrong, inaccurate.

7 The second point is what we've come to call the
8 final accounting twist. You see, in a sense what we've
9 been hearing this afternoon is something of an
10 Aunt Sally, because as Dr Bryan actually admitted in
11 a document, there is no issue between average costs
12 against local costs. Indeed, my submissions yesterday
13 tried to make that point. If average costs are done
14 properly with proper regard to the class of customers
15 you're dealing with and the accounting allocations are
16 done properly and the verification is done properly, you
17 can trickle down, and you arrive at an answer which
18 might well be justified, perhaps even cross-checked, by
19 reference to bottom-up numbers. It is not rocket
20 science, at least it shouldn't be.

21 What we have seen in the crab-like progression from
22 Mr Henderson in November through to Mr Edwards in
23 February was this movement gradually to move the access
24 price as high as convenient in order to keep out Albion,
25 in our view. But what we have seen in that last

1 movement from what I'll call the Henderson paper to the
2 Edwards paper, the one fundamental difference which I've
3 drawn to your attention, and you've seen often enough,
4 is that Henderson takes potable treatment, a figure for
5 potable treatment, and then deducts that from the large
6 industrial tariff for potable water. So he's taking one
7 from the other and they're both dealing with exactly the
8 same thing.

9 Now, that might be an acceptable way, a reasonable
10 way, possibly. I beg your pardon, potable -- to arrive
11 at potable distribution. I think you've got my point.

12 Now, I make no point on that, but the importance of
13 this submission is that when we move to Mr Edwards, what
14 does he do? He takes a figure which does not relate to
15 potable treatment, but it relates to the cost of the
16 treatment of all water. So there can be no objection
17 hypothetically in this case -- it is not my submission
18 at the moment -- to talk in terms of company averages of
19 potable water, better still non-potable water, but there
20 can be no justification for taking an all-company
21 average for all water and then deducting that from
22 a potable water value.

23 That's the mischief he got up to.

24 THE CHAIRMAN: But did he deduct it from potable water
25 value?

1 MR SHARPE: He deducted --

2 THE CHAIRMAN: He deducted it from a company average --

3 MR SHARPE: No, he didn't. He took it from the LIT, the
4 large industrial tariff, which as you know only related
5 to potable water.

6 THE CHAIRMAN: That stack only adds up to 72p, or something,
7 rather than the 83.4p.

8 MR SHARPE: What he did is he took it from the potable LIT,
9 okay.

10 THE CHAIRMAN: Oh, the potable LIT, rather than the --

11 MR SHARPE: Yes. Now you can begin to understand how you
12 take a figure for potable treatment, even an average
13 figure for potable treatment from the potable LIT,
14 although we don't accept that was a sensible and
15 realistic way of doing it, of course. But what he did
16 was simply take a figure for the cost of all the
17 treatment of all water in the sure and certain knowledge
18 that that would have covered raw water, partially
19 treated water, which of course served to reduce fairly
20 significantly that valuation.

21 Then you deduct that from these global large
22 numbers, you inflate the cost of bulk distribution,
23 which you'll recall is potable bulk distribution, and
24 you arrive at a figure which, hey presto, moves the
25 number above 19.9 or so to 23.2. We call that the final

1 accounting twist.

2 When you come back to that in cross-examination --
3 you must go back and refresh your memory with the
4 cross-examination -- but he was remarkably unfluent for
5 somebody who had obviously considered that as the right
6 way to go forward. He almost gave the impression of not
7 really quite understanding the impact it had, or
8 professing not to understand the impact it would have on
9 bulk distribution.

10 Then the third point, going ahead, treating potable
11 distribution costs as applicable to non-potable
12 distribution costs. I made my submissions on this
13 yesterday. It beggars belief that somebody in the
14 industry should accept that. It was an assumption they
15 put forward. This can't be justified by any -- all
16 regional averaging, it was an assumption that was made
17 that the figure derived for potable bulk distribution
18 should equate to the figure for non-potable
19 distribution, and a mighty convenient assumption it is
20 too.

21 In the same way that the 30 per cent treatment cost
22 represented 100 per cent overvaluation, so too this
23 represented a 100 per cent overvaluation.

24 There was a moment in my friend's submissions -- and
25 if I were to go back to everything with which

1 I disagreed, we'd be here all night and you'll be
2 relieved to hear I'm not planning that. But just one
3 point. He took you to the Ofwat decision. He actually
4 said in terms Ofwat had endorsed the treatment here
5 of --

6 THE CHAIRMAN: Yes, that Ofwat had agreed that potable bulk
7 distribution was the same as non-potable bulk
8 distribution.

9 MR SHARPE: But put yourself in the position of Ofwat at
10 that time. What information did they have? If they had
11 had the Hyder report, they'd have had clear accurate
12 MEAV asset values for non-potable underground
13 distribution assets. Faced with that, they could not
14 possibly have concluded that there was an equality
15 between potable distribution and non-potable
16 distribution.

17 Of course, even without the Hyder study in the
18 referred work, Ofwat was able -- with the benefit of
19 more time and greater and more intensive study, they
20 were to come to a 50 per cent conclusion. But the point
21 is the obvious point: they could have had that
22 conclusion with the Hyder study.

23 My friend -- and this is simply for your reference
24 again -- he took you to bundle 5 at 227 at 1495. This
25 is in relation to treatment, as if in some sense Ofwat

1 had endorsed the treatment by Welsh Water and what I'll
2 call the trickery that they've engaged in.

3 I revert now to the average costs point and perhaps
4 I'm out of order, but nevertheless. If you go to
5 bundle 5 in your own time, at 227, page 1504, Ofwat here
6 refers to the adjustment, the step two adjustment. This
7 would have an impact on the step four figure, increasing
8 it from 16 to 16.6, and you'll remember the numbers, the
9 11 and then, by result of the sleight of hand at the
10 end, going up to 16.

11 "In simple terms the reduction of the step two
12 figure means a lower figure is deducted from the large
13 industrial tariff, which results in a higher step four
14 figure."

15 You have that.

16 "However, Dwr Cymru's large industrial tariff
17 relates only to potable water, whereas the amount
18 deducted by Dwr Cymru for resources and treatment
19 includes both potable and non-potable supplies."

20 So they were right on top of the point four years
21 later.

22 "We have concerns about this inconsistency in
23 Dwr Cymru's approach which appears to compromise that
24 approach."

25 So far from endorsing it, as my friend tried to show

1 you with his two citations, he, I'm sure, overlooked
2 this qualification at paragraph 284. And I move on.

3 So I started with a 30 per cent figure, I've dealt
4 briefly, but I hope enough, in relation to the
5 accounting twist and its perversity, wilfully treating
6 potable distribution costs as applicable to non-potable
7 distribution costs, and arguably when they had a good
8 deal of data at the time on the Hyder study on precisely
9 that point, yet persisting with this assumption of
10 equality right through until the referred work.

11 And then lastly, using average costs -- fine -- but
12 failing to do what I think any sensible company would
13 have done, anxious not to mislead either Albion or the
14 regulator, to attempt some sort of internal verification
15 based upon the bottom-up numbers which, as we now know,
16 they seem to have.

17 In relation to each category, there are strong
18 reasons to conclude that Welsh Water took those steps
19 either knowingly, either knowing they would lead to an
20 excessive price, or at the very least reckless as to
21 whether they would create an excessive price.

22 The evidence essentially supports both, though we're
23 content with recklessness because that will satisfy the
24 test for exemplary damages. Now, we set out at length
25 in our written submissions that the extent of the

1 problem was so manifest, especially when they had
2 admitted internally flakiness in the 30 per cent data,
3 for example, they were well known internally and they
4 must either have known, or at the very least have been
5 reckless about the problems they faced. To that I can
6 add the Hyder study in relation to potable/non-potable
7 assets.

8 Each of these conclusions is strongly supported by
9 the fact, as we analyse in relation to each category,
10 that Welsh Water either did not give Ofwat and Albion
11 a full explanation of what had been done, or withheld it
12 and withheld the data despite express requests from
13 Ofwat. They withheld data that was clearly within their
14 possession, and I am bound to say perhaps I'm not alone
15 in not finding my friend's explanation as to why the
16 Hyder study and, indeed, anything that was produced by
17 Mr Brotherton was not supplied promptly to Ofwat in
18 answer to questions, at least questions 1 and 14 of the
19 section 26 request.

20 I make no comment on what was not referred, not
21 given in the referred work to the Pinsent Mason study,
22 but it does seem to me that the same applies there.

23 Now, of course, I can make these points about
24 information that Ofwat didn't have. It should have been
25 given to Ofwat, in all candour, even if hadn't been

1 requested. But it was requested and it wasn't given to
2 them. I ask myself the question: well, if the
3 information was there and was valuable, and they knew
4 what it meant and they governed their internal strategy,
5 it seems, as a reaction to it, why didn't they give it
6 to Ofwat? It begs the further question: what did they
7 have to hide?

8 If they had nothing to hide, these documents would
9 have been passed over in the ordinary way, and they
10 could have taken their chances. In my submission, they
11 knew very well indeed what the consequences of those
12 documents would be in the wrong hands, namely Ofwat and
13 perhaps even Albion, ultimately, still less this
14 Tribunal, until the very last minute.

15 Now, it's perhaps not sensible to dwell on the
16 detail here, the data that was given was out of date
17 and that goes for the 30 per cent figure. We know about
18 Mr Brotherton's work, we know about their knowledge of
19 the work and we also know that none of these things were
20 disclosed. I'll leave that. That is the story
21 essentially on treatment costs.

22 But exactly the same story emerges in relation to
23 potable and non-potable distribution assets, as I've
24 just described. That information should have been
25 given. Of course, just to add insult to injury we knew

1 already that the asset register that was in their
2 possession was not handed over -- I don't think it was
3 until 2006, rather late in the day. We know that what
4 was put in reply to Ofwat, the so-called D21, well,
5 five years old and acknowledged to be inaccurate.

6 What sort of response is that for a responsible
7 company to make? A company that wasn't frightened of
8 the outcome? In our view, this is all part and parcel
9 of the evidence that we submit you should take into
10 account and give big weight to, that this company was
11 really doing its best to keep Albion out of the market,
12 and it wanted to make sure that neither Albion nor Ofwat
13 knew anything about it.

14 Now, I've already made some submissions in reply as
15 to what Ofwat knew. I think it is sensible actually to
16 regard almost any information derived from Ofwat at this
17 time with some caution, because they were kept in the
18 dark. (Pause)

19 Forgive me, I'm trying to edit on the hoof and I'll
20 no doubt be told I shouldn't, but I think I will.

21 But there is I think one rather important and
22 central obvious point, and that deals with the average
23 treatment of potable water. Now, Mr Beard said this was
24 wrong. Forgive me, I've dealt with that.

25 Anyway, they didn't conclude that Ofwat regarded it

1 as legitimate for there to be this equivalence, and
2 I simply repeat the submissions I made earlier that
3 there was no basis for equality of treatment.

4 Now, it's perhaps sensible to wind this point about
5 average pricing as yet another explanation. As I said
6 in opening, we've no particular objection to average
7 cost pricing and company averages, regional averages.
8 It is true that Dr Bryan took exception to that because
9 he couldn't believe the numbers being put forward, but
10 leaving that to one side, I repeat my opening
11 submission: average of what?

12 If you look at whole companies you're going to get
13 distorted and inaccurate figures. Deriving data from
14 1.4 million customers and then cascading down
15 essentially to one, there are bound to be major
16 methodological flaws. The correct way is obviously to
17 take the average costs of the -- class of the assets
18 involved, non-potable large industrial supply, possibly
19 with allowance for partial treatment as, indeed,
20 eventually happened.

21 A brief word on Benham v Kyritha. I don't quite
22 understand my friend's submissions. Of course this was
23 a case in its own specific context in relation to
24 whether there was a case to answer. That's neither here
25 nor there. The important point and the only reason we

1 brought it to your attention were those very important
2 remarks from Lord Justice Simon Brown, as he then was.
3 They set out what I had actually thought was a fairly
4 conventional approach when assessing the weight to be
5 given to a party's case, and you are perfectly entitled
6 to make your own view as to the reasons why key movers
7 in this case, guiding minds, if you like -- who can be
8 more guiding than a managing director? -- were denied
9 the opportunity to come in and advance Welsh Water's
10 case. As I said, they're alive and well and it is
11 extraordinary they weren't brought here.

12 I can make a submission and ask you to accept it
13 that if they were to come here they would not be
14 advancing their case. There are great limits as to how
15 far Albion can have demanded their presence, as you well
16 know, but it is extraordinary that they should not have
17 been called, and you are entitled to draw what
18 appropriate inferences, namely that there was something
19 that they would have said, giving evidence, as I know,
20 truthfully, that would not have advanced Welsh Water's
21 case.

22 Probably the same is true of Mr Henderson and
23 certainly we were very glad to see Mr Edwards here.

24 Perhaps one final point on exemplary. At no point
25 in my submissions yesterday did I say you should

1 approach the quantum on the basis of restitutionary
2 principles. I'm very much aware of the law of exemplary
3 damages, and it has a primary function to punish.
4 Deterrence probably has a secondly provision, but its
5 primary function is to punish.

6 I drew attention to the vast rewards that
7 Welsh Water appeared to have been earning and the
8 evidence has not been contested, not in the sense that
9 you should equate a damages award to such awards. But
10 in your assessment of what it would be appropriate to
11 punish them for, you should have due regard to the
12 reviews that they have enjoyed by virtue of their
13 cynical disregard of the law. I am saying that an
14 appropriate level of damages would reflect the revenue
15 profits they were seeking, they earned, and perhaps even
16 further, what they were seeking to protect. And that,
17 you'll recall, was up to about 23.8 million.

18 Set over the period of the time of this claim, that
19 is a very significant number, and in our view it would
20 be unconscionable for them not to be punished
21 appropriately by reference to, in part, the reviews
22 they've garnered as a result of their cynical disregard,
23 otherwise they'd have got away with it. And the whole
24 point of this is to punish and then, secondly, to deter.
25 And what sort of deterrence is it if you can take the

1 money and give a trivial proportion of it back?

2 Now, those are my submissions on exemplary damages.
3 If I can turn briefly to a couple of points in relation
4 to compensation. I apprehend the Tribunal is well on
5 top of these issues, the counter-factual. You heard my
6 friend's submissions. He seems to have overlooked the
7 order of the Tribunal.

8 The Tribunal simply states that a price of 14.4
9 would not be abusive. The Tribunal made no findings at
10 all in relation to 15.8, no findings at all. My friend
11 was quite wrong to submit that in some sense that was
12 not an abusive price. It is what he would like to
13 charge, of course, but there was no finding. He gets no
14 assistance from the Tribunal whatsoever.

15 I'll leave that point.

16 As for the proper basis, this is a hypothesis that
17 one can go up to the outer limit of legality, whatever
18 that may be. In our submission, this is a hopeless
19 submission, a hopeless argument. It posits 20/20 vision
20 in reverse, what would have been the price. It posits
21 a riskiness on the part of Welsh Water to pitch their
22 case right at the absolute maximum. It is also
23 curiously contrary to the documents they're running in
24 relation to United Utilities.

25 It's not the case that they say United would price

1 up to an abusive price. They set the price at what had
2 been offered, and that, in our submission, is precisely
3 the exercise that the Tribunal should do now. What
4 would the parties have agreed in the shadow of the
5 abuse, and then take it on from there. What could be
6 more reasonable than the price that Welsh Water itself
7 offered?

8 Now, of course I lapsed into saying that United
9 Utilities was in a dominant position, and I'm well aware
10 at least in these proceedings there has been no finding
11 to that effect. I simply remind my friend of Ms White's
12 evidence that nothing could have been clearer. She was
13 basing her evidence on the very firm understanding that
14 she felt United Utilities was in a dominant position,
15 otherwise issues of degradation and discrimination under
16 the Competition Act simply don't apply. So we move on
17 from that.

18 If it is necessary to debate the 7p issue, my
19 friend, I'm afraid --

20 THE CHAIRMAN: I think the point that we want to hear you on
21 particularly, Mr Sharpe, is this question of how the
22 benefit share agreement works in the interpretation of
23 clause 7(4).

24 MR SHARPE: Right, but just the 7p, my friend took you to
25 that. The 7p issue related to the 1996 bulk supply

1 price and had nothing to do with common carriage.

2 Let me correct it.

3 THE CHAIRMAN: 7p, as I understand it, was the price that
4 Dr Bryan was putting forward as the possible common
5 carriage price, both in his negotiations with Dwr Cymru
6 and in his discussions as an assumption with United
7 Utilities, based on his reading of the third-party
8 supply aspects of the regulatory accounts, or something
9 along those lines. And it is put forward by Mr Beard as
10 saying, well, he would have stuck to that and would
11 never have accepted 14.4p, so we never get off the
12 ground in the compensatory claim. That's why --

13 MR SHARPE: Well, the evidence simply does not support that
14 view. At that time he thought there was overwhelming
15 evidence.

16 THE CHAIRMAN: He said he thought there was overwhelming
17 evidence.

18 Well, we have his evidence on that point. I don't
19 think we need to dwell on that point.

20 MR SHARPE: I think I've now understood it, thanks to my
21 learned friend, not for the first time in this case.

22 My friend just took you to the wrong reference and
23 I'm not going to detain you, but may I just give you
24 a reference.

25 THE CHAIRMAN: Yes.

1 MR SHARPE: Bundle 4, tab 164, 1025.

2 That was a reference, as I said earlier, to the 1996
3 bulk supply price. What he was doing was simply
4 referring to that and the evidence surrounding that.
5 And therefore, it was inappropriate to try to transfer
6 that to a statement that he was saying that 7p would
7 have been appropriate in the context of common carriage.
8 It is not a big point, but I think I don't particularly
9 want you to be misled.

10 I was going to address you on indexation.

11 THE CHAIRMAN: I think we've heard enough on indexation.

12 MR SHARPE: Well, have you?

13 THE CHAIRMAN: Before we all get completely past it, can we
14 deal with the point, as I said, on which we do want to
15 hear you, which is the interpretation of the clause 7(4)
16 and how it is that Albion say that the compensation
17 should be calculated in accordance with the difference
18 between the Dwr Cymru price under the bulk supply
19 agreement to Shotton for as long as it lasted, and
20 thereafter the price of the non-potable large industrial
21 user tariff, once that came into existence in 2003,
22 having regard to the wording of the clause in schedule 3
23 to the agreement.

24 MR SHARPE: All right. What I'm going to do --

25 THE CHAIRMAN: If you want to have a moment, we can --

1 MR SHARPE: What I'm going to do is we've practised a minor
2 division of labour in this case, and in the same way as
3 my friend was happy to correct me in relation to the 7p
4 figure, I'm going to ask Mr Cook to deal with this
5 particular point because he's been assigned
6 responsibility for that. But I don't want to detain you
7 overlong, but there are one or two things that were said
8 in relation indexation which were simply unsustainable.

9 Now, I lay a marker. If you're uncomfortable --

10 THE CHAIRMAN: Well, you had better say what they are, then.

11 MR SHARPE: Let me just deal with it quickly. We've got
12 a couple of minutes.

13 First of all, there was no mandate at all for the
14 RPI. What we're concerned about is what the parties
15 would have agreed in 2001. We've taken you to the
16 figures, which show cost reduction. My friend hardly
17 addressed that. He relied upon the Edwards evidence
18 that there was a vast number of agreements calculated by
19 reference to RPI, and we took him to the evidence to
20 show that it wasn't.

21 THE CHAIRMAN: We now seem to be majoring on the point that
22 because Ofwat seems to assume that contracts outside the
23 basket rise by RPI, that means that Dwr Cymru would have
24 insisted on RPI, otherwise they would have --

25 MR SHARPE: No, any more than they would have insisted on it

1 in any other agreement. All the other so-called special
2 agreements were subject to that Ofwat explanation, and
3 we saw that some are RPI, some are volumetric and some
4 PPI.

5 So there is no mandate to say that simply because of
6 the Ofwat point, that would of necessity have meant they
7 would have negotiated hard and not come to an agreement
8 but for that. I think that must be right.

9 Moreover, and if my friend was suggesting the
10 Tribunal earlier in these proceedings had in a sense
11 endorsed RPI, as he perhaps got rather near to, can
12 I just merely give you the reference: bundle 13, tab 22,
13 paragraph 22. The Tribunal did nothing of the sort. It
14 was actually asked to deal with the indexation by
15 Dr Bryan and it was nothing to do with us. Didn't have
16 the basis to do so and did not do so.

17 The issue here, it is really not what an undertaking
18 in a dominant position can extract out of Albion in
19 relation to indexation. As I pointed out, if there is
20 a marked divergence between price and cost, even if one
21 starts from a non-abusive level, it can readily become
22 abusive. So the test is potentially one of legality,
23 that is to say, looking at the parties, what would they,
24 in the shadow of the law, have agreed? The only
25 information we've got about that time actually rests

1 upon what Ofwat actually did in relation to its
2 determination, and we saw the direction of costs going
3 down. In our submission, not merely would that have
4 been what Dr Bryan would have insisted upon, it would
5 have been the legal answer to the question of what
6 indexation would be lawful. In our submission, that's
7 exactly what would have happened.

8 It's interesting, you know, apart from Mr Edwards --
9 and I hesitate to say this -- but discredited evidence
10 in relation to the vast number of other agreements,
11 there is no other evidence to suggest that indexation by
12 reference to RPI would have been appropriate for this
13 type of industrial contract. It wasn't industry
14 practice, it wasn't approved by Ofwat and hadn't been
15 endorsed by the Tribunal and, in our submission, would
16 have been unlawful in any event by virtue of the fact it
17 would have led to an abusive situation fairly early on.

18 The contract itself would never have lasted forever.
19 If the would had changed after X years -- and we haven't
20 talked about duration -- it would no doubt have just
21 been modified in exactly the same way as any other
22 contract would have been.

23 Those are my submissions on indexation, nothing on
24 capacity or augmentation.

25 Back-up potable supply.

1 THE CHAIRMAN: Mr Sharpe, it's up to you to decide what --

2 MR SHARPE: No, at this time I'm prepared to be led by the
3 Tribunal.

4 THE CHAIRMAN: Well, I think we've probably heard enough on
5 those issues.

6 MR SHARPE: What I'll do --

7 THE CHAIRMAN: I don't think we need to hear anything
8 further on those issues. As I said right at the
9 beginning, nothing is to be read into that as to any --

10 MR SHARPE: But you'll understand the back-up. It is really
11 what the parties would have agreed to.

12 THE CHAIRMAN: Yes, we understand now the distinction
13 between paying for the supply and paying for the
14 reservation of the supply. We will go back and look at
15 what Ofwat actually said in the referred work --

16 MR SHARPE: And the evidence that shows that since 1998
17 Albion had not been paying for this, and in 2001
18 Dr Bryan would never readily have paid such a huge sum
19 for a service he didn't want, never wanted and didn't
20 want.

21 I'll reserve the right, if I may, to come back.

22 Submissions by MR COOK

23 MR COOK: Madam Chairman, just briefly one point in relation
24 to indexation.

25 You asked about the Ofwat documentation indicating

1 it would assume that (inaudible) prices would have gone
2 up by RPI for the purpose of the 2000 price review. We
3 have checked, and as far as we can see, firstly
4 Mr Edwards makes no reference to that document in his
5 evidence and there is no reference anywhere in the
6 documentation to that document being looked at by those
7 people involved.

8 It is a thought that has occurred after the events
9 to Welsh Water. As far as we can see it was not
10 something that was in the minds of those involved at the
11 time.

12 We also repeat a point: there is no way that Ofwat
13 could mandate by making such a suggestion that
14 Welsh Water could charge RPI, whether that was an
15 appropriate level of indexation to charge or not.
16 Clearly, if the costs were not going to go up, and in an
17 inflationary world the costs were not going to go up,
18 Ofwat could not have said in that guidance, "Please now,
19 as the dominant undertaking, abuse your position by
20 overcharging those customers" simply by making that kind
21 of statement in its price review.

22 Quite frankly, if Welsh Water thought that was
23 inappropriate in some way it would have come back on
24 that and had the opportunity to come back.

25 Turning then to the benefit share arrangements and

1 how those operate, just briefly to explain how we
2 understand and how this should be understood as a matter
3 of contractual construction, you of course have the
4 basic prices set out in the agreement, which are set at
5 26p, which is indexed in accordance with schedule 3 by
6 reference to the lower of two cost measures, PPI and the
7 volumetric potable charge.

8 It is important to recognise the word "potable" in
9 there because, of course, they're looking at a potable
10 price not a non-potable price. So they're using
11 a benchmark of the lower of two measures --

12 THE CHAIRMAN: Just remind me what the volumetric thing is.

13 Is that the without the standing charge?

14 MR COOK: Yes, simply looking at the per metre cubed price.

15 So the cross-check is to the volumetric charge. So they
16 benchmarked it against two possibilities, neither of
17 which is -- well, that's not a non-potable price, it is
18 a potable price and it is only the volumetric element.

19 So at that stage, at least -- and the reason of
20 course why those measures were in there is that was what
21 previously had been offered by Welsh Water in the
22 Shotton Paper agreement previously.

23 That sets the basic way, the basic price, and of
24 course, overlaid on top of that, we then have
25 clause 7(4) and the benefit-sharing arrangements that

1 one gets within that.

2 We do say that that is something that is capable on
3 its face of leading to additional payments being made by
4 Shotton Paper, and therefore effectively an increase in
5 the price Shotton Paper was paying on a volumetric
6 basis.

7 Now, just to avoid confusion here, because I think
8 Dr Bryan did say it would be dealt with at the end of
9 the year, and clearly that would be the way in which
10 clause 7(4) would operate because at the end of the year
11 there would be an adjustment of the total amount being
12 paid.

13 But that doesn't alter the fact that 7(4) would be
14 adding or subtracting from that basic volumetric charge
15 by reference to the way in which it operates. And to
16 give an obvious example of the situation where the
17 volumetric charge will clearly go up is if Albion is
18 successful in some way in reducing the volume of water
19 that Shotton Paper uses, because it manages to find some
20 way to make the process more efficient, which is the
21 added value service that Albion provides. Then there
22 will be that level, that will be a saving. And that
23 will then be split. After Albion's costs for whatever
24 it has done in relation to that process, it gets its
25 costs back and then 30 per cent of the remaining net

1 benefit.

2 That would undoubtedly lead intrinsically to an
3 additional payment by Shotton to Albion, on top of the
4 volumetric charge. So the overall payment would exceed
5 simply the volumetric charge. So there is certainly
6 scope within this provision for the average amount of
7 money paid by Shotton to exceed the volumetric charge
8 that one gets under the basic 26p plus indexation. So
9 as a starting point the notion of this price can't go up
10 is simply wrong.

11 THE CHAIRMAN: Sorry, let me make sure I have understood.

12 So it can go up not only by the lower of PPI or the
13 Dwr Cymru volumetric charge, but you're saying that if,
14 by reason of efficiency savings, the amount of water
15 that's used goes down substantially, or at all -- I
16 wasn't positing a cost sum -- it's not that they then
17 just pay that amount less because they're buying less
18 water, because Albion has to get 30 per cent of the
19 benefit of that saving.

20 MR COOK: And its costs. Its costs are very important --

21 THE CHAIRMAN: And its costs, and then 30 per cent of the
22 benefit of that saving, and that is then spread over
23 that smaller number of cubic metres and the pricing goes
24 up.

25 MR COOK: I mean -- it probably doesn't matter too much. At

1 the end of the year there will be an additional payment
2 and the parties could have treated that as being 26p
3 plus an additional one penny per metre cubed, or they
4 could simply have said, "You've paid 26p all year and
5 now you owe us an extra £200,000". Either way it is
6 viewed --

7 MR BEARD: I'm not sure we understand the basis for the
8 evidence in relation to any of this at all.

9 MR COOK: It is not evidence; it is contractual
10 construction.

11 MR BEARD: I'm not sure it is contractual construction about
12 how these things pan out.

13 THE CHAIRMAN: Well, Dr Bryan was in the witness box for a
14 number of days. Was he asked questions about this, in
15 construction of this?

16 MR BEARD: I'm sorry, I should let Mr Pickford, since he was
17 the one who did the cross-examination.

18 THE CHAIRMAN: Let us just try and --

19 MR COOK: I'm dealing with this, to be clear, purely as a
20 matter of contractual construction and how the contract
21 operates properly in accordance with its terms. So I'm
22 saying in practice one could deal with the addition of
23 an extra sum of money under 7(4) by saying either,
24 "We'll add one penny to the price" or simply that was an
25 extra X hundred thousand pounds payable annually year on

1 year going forward. It doesn't matter; the end result
2 is Shotton ends up paying more than simply 26p
3 volumetric charge.

4 To start with, it's simply wrong to say, as Mr Beard
5 does, that one can't come up above 26p. Clearly that
6 can operate.

7 The question then is to understand within 7(4) what
8 are savings in the cost of supply in this context. Now,
9 a question we simply say in relation to that is it is
10 right to say that that is not a phase which is defined
11 within this agreement. So what it's saying is savings
12 in this cost of supply, and whatever that is going to
13 be benchmarked against will turn out, during the course
14 of the agreement, by reference to whatever you can say
15 you have managed to successfully save the costs of
16 supply. We would say in relation to that, you know, an
17 obvious example would be if Albion is able to get
18 a lower level of indexation. That is clearly a saving
19 in the cost of supply, compared to the supply of cost
20 that would otherwise have applied.

21 The benchmark is what the cost of supply would be,
22 absent Albion being there. The reason there is no
23 problem with using the DC retail tariff that comes into
24 effect in 2003/2004 is because it is simply left at the
25 level of savings in the cost of supply, and the

1 benchmark is whatever is the applicable cost of supply
2 whenever you're looking to do this calculation.

3 And if the alternative that Shotton Paper would be
4 in turns out to be a new tariff bought in by DC, then
5 that is what Albion has managed to achieve savings
6 against. It is not a situation where Shotton Paper can
7 be upset, if the end result of that is it ends up paying
8 a higher price because it's still in a situation where,
9 as a result of Albion's presence, Shotton Paper is
10 paying significantly lower than whatever it could get
11 from Welsh Water. And the context of a retail tariff
12 only becomes relevant when that becomes a tariff that
13 would apply to Shotton Paper in the absence of Albion
14 being there. That's why an LIT tariff is critical
15 because that's therefore applicable to everybody, and so
16 is what Shotton would have to apply otherwise.

17 We say that's why the clause uses a benchmark that
18 can appear some years later because it's left the
19 benchmark undefined, recognising it is designed to apply
20 to an extended period, not simply what's there at the
21 start, and it is intended to operate in a way that
22 allows a fair balance between the benefits that are
23 arising from Albion being present.

24 That's why we say the construction of clause 7(4)
25 operates or becomes in 2004, when the DC non-potable

1 tariff LIT comes into effect, that's the point when you
2 start to look at that as to being an applicable
3 benchmark as to what the cost of supply would be in the
4 absence of Albion being present. (Pause)

5 I was waiting to see if you had questions arising
6 from that. If not, Mr Sharpe has a couple of additional
7 points.

8 THE CHAIRMAN: So what you're saying is the cost of supply
9 there, or a saving in the cost of supply, arises not
10 only when Albion manages to deliver the water to Shotton
11 Paper's premises more cheaply than it had previously
12 been able to deliver the water, but also when savings
13 were made in the amount of water that Shotton Paper
14 uses. And also it's still a saving in the cost of
15 supply as and when the Dwr Cymru tariff rises, even if
16 nothing has changed in the relationship between --

17 MR COOK: Yes, we say that is obviously a saving in cost of
18 supply. We can understand why it is, by reference to --
19 if a situation happens where the costs of this system,
20 the costs of non-potable water goes up substantially for
21 some reason, whether simply due to inflation or not, and
22 as a result, Welsh Water comes back and says, "Well,
23 now, by reference to the retail tariff or otherwise, we
24 think the bulk supply price should be -- previously 26p,
25 we now think it should be 35p". If Albion is

1 successfully battling that down to 26p, it is as a
2 result of Albion's efforts that he has managed to keep
3 the price down to that level when we managed to
4 successfully persuade, through whatever process, that
5 Welsh Water's retail tariff is applicable -- the rises
6 in that retail tariff are applicable.

7 So it's Albion's ongoing presence which ensures that
8 the retail tariff that would otherwise be applicable
9 does not apply to Shotton Paper. And that was what
10 Albion was doing by fighting for common carriage. But
11 equally, it is what Albion effectively carries on doing
12 by being there as the bulk supplier of water (inaudible)
13 period.

14 So the retail tariff is what's applicable otherwise
15 and Albion is preventing that being applicable by being
16 there. So it is very much from Albion's existence, and
17 it is not something -- there are times when Albion has
18 already done the work in the sense that by being there
19 it is ensured that rises in the retail tariff do not
20 apply to Shotton Paper. But it is all down to Albion's
21 presence.

22 THE CHAIRMAN: I see that clause 5.1 provides that the
23 Dwr Cymru price is, in any event, a cap on the price
24 under the agreement.

25 MR COOK: It is a cap, but it is possible (inaudible) shall

1 pay the charges (inaudible) otherwise levied by
2 Welsh Water. The charges are defined as that in
3 schedule 3, so the benefit share is strictly outside
4 that cap, in any event.

5 It is outside that cap, you know, for the logical
6 reason that one of the, you know -- the paradigm example
7 of benefit share would be Albion Water managing to
8 decrease the total of volume of water that Shotton Paper
9 was using, and in those circumstances it is certainly
10 not a problem that Albion is going to get some of that
11 back as an additional lump sum under 7(4), because the
12 end result is that Shotton Paper is using a lot less
13 water and so paying a lot less for water. But the
14 charges are being defined by reference, charges are
15 defined terms. It is that pursuant to schedule 3, and
16 we see that at page 368. It is the reason why
17 clause 7(4) is effectively an additional provision.

18 THE CHAIRMAN: Yes, thank you.

19 Further submissions in reply by MR SHARPE

20 MR SHARPE: One final submission on Corus, then I'm done.

21 My friend made submissions in relation to Corus.
22 The essential point here is the impact of the dispute,
23 the prolonged dispute with Ofwat in relation to the
24 first access price decision. That was in the
25 unchallenged evidence of Dr Bryan, the reason why Pennon

1 withdrew its support for Albion, thus placing Albion at
2 a distinct disadvantage in relation to its dealings with
3 Corus.

4 There's nothing indirect and remote about that, it
5 was cause and effect. But for the abuse of dominant
6 position and the need to challenge it, and the
7 protracted proceedings, and recalling also that Albion
8 is a very small company, it is not quite a one man band
9 but it may seem so at times. It was quite reasonable to
10 expect that they should have engaged in further
11 discussions in relation to consider Corus at that time.

12 The only question, with respect, for the Tribunal to
13 ask is: would Albion have made a bid if it had received
14 a lawful common carriage price in the year 2001? In our
15 submission, the answer is plainly yes. It has been
16 invited to do so in relation to not one plant, but
17 three, and there is no reason to think it will not have
18 had a substantial chance of winning. After all, they
19 were invited, they were disaffected with Welsh Water and
20 they would have proceeded.

21 Indeed, as was pointed out to you this morning by my
22 friend Mr Beard, correspondence was entered into in 2006
23 between Albion and Welsh Water in relation to that.
24 There is no reply by Welsh Water in the bundle to that.
25 So the issue, as far as we are concerned, just goes

1 away.

2 We say no reason to think that Albion could not have
3 a substantial chance of winning, or a substantial
4 prospect of success. There was a substantial chance of
5 winning and the prospect of success would have been
6 high.

7 Now, my friend says that's not true. First, you had
8 to bid for all three. There's not the slightest
9 evidence to suggest that Corus made that a precondition.
10 It's true they invited all three bids, but it was never
11 a pre-condition. And it stands to commercial reason, if
12 they could save money at Shotton, why would they require
13 supply elsewhere? There is no evidence for that, but it
14 seems on the face of it a bad point, and secondly, that
15 in some sense Albion couldn't beat Corus's price. What
16 price?

17 Reference was made in the skeleton and also, I think
18 in submission, to the 2003/2004 price of Welsh Water,
19 but the record shows that Albion was being asked to bid
20 for the years 2004/2005. So the 2003/2004 price would
21 have been irrelevant. Of course as we showed you
22 yesterday in our chart, the large industrial non-potable
23 tariff had come into force then.

24 My friend, I'm sure unwittingly, but certainly in my
25 mind, did create confusion about the Corus lagoons

1 discount. Now, he tried to create a confusion in
2 that -- well, he did create confusion in my mind -- when
3 he pointed out the element in common carriage was 1.3p.

4 Well, we've got to see what we're doing here. That
5 figure reflected 4 per cent on Corus volumes, 4p on
6 Corus volumes. That was being equal to 1.3 per cent --
7 3p on Shotton volumes. In other words, he had failed to
8 distinguish between the incidence of this payment on
9 common carriage in relation to the two customers.

10 THE CHAIRMAN: Because the Shotton volume is much higher
11 than the Corus?

12 MR SHARPE: Yes. Well, it's three times higher and that's
13 reflected in the differential.

14 As for the benchmark, I think I heard my friend say
15 that as the Tribunal only asked for how much was being
16 paid, that's what you've got. In fact, you weren't told
17 that actually that's not what we asked for. And you'll
18 see the distinction between what they were seeking to
19 recover and what they were actually paid.

20 In my view, in my submission, that showed a distinct
21 lack of candour with the Tribunal because plainly you
22 were asking a question, I think, of what was invoiced
23 and what was received, when in fact in this case, in the
24 light of the dispute which has been ongoing, there is
25 significant difference between the two. And that

1 difference is quite critical in relation to Albion,
2 because Albion obviously is going to pitch at a price
3 below and offer them as price certain below the price
4 that they're arguing about. Whereas Welsh Water, by
5 their own actions in seeking to demand a higher price,
6 are plainly resolute in achieving that.

7 Why fight Welsh Water when you can get a lower price
8 from Albion? In our submission, there is a direct
9 causal relationship between the abuse and the loss and
10 the loss itself, the benchmark which Albion would have
11 met. And therefore to repeat my submission: the chances
12 of getting that from any rationally commercial world
13 would be 100 per cent.

14 Now, unless I can assist you further, those are my
15 submissions on behalf of Albion Water.

16 THE CHAIRMAN: Thank you.

17 I think we've had about all the assistance we can
18 cope with, but that's been a very long day, but very
19 helpful as far as we're concerned. And many thanks to
20 you all. We very much appreciate how hard everyone has
21 had to work to prepare not only the written closing
22 submissions, but to prepare all the submissions over the
23 last couple of days, particularly having regard to the
24 new information that came to light. And we're very
25 grateful to everybody for the analysis of that, that

1 you've been able to do and we very much recognise all
2 the long hours that must have gone into making sure that
3 that was presented to us as clearly and helpfully as it
4 has been.

5 Many thanks also to the transcript writers, who have
6 been diligently following everything that's being said.

7 We will now retire to consider what we're going to
8 do, and we'll let you know through the usual channels
9 when we're ready to hand down judgment.

10 As to when that will be, I can't say anything
11 definite, but just to manage your expectations, members
12 of the Tribunal panel have a lot of other commitments
13 between now and the end of the year, so it may not be
14 for the end of the year, unfortunately. But we would
15 hope that pretty soon after that, we will --

16 MR SHARPE: I'm most grateful for the indication, thank you.

17 MR BEARD: I'm most grateful. Thank you for sitting ...

18 THE CHAIRMAN: Thank you very much.

19 (5.34 pm)

20 (The hearing adjourned)

21

22 Closing submissions by MR BEARD1

23 (continued)

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25 Submissions in Reply by MR SHARPE172

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Submissions by MR COOK201

Further submissions in reply by211

MR SHARPE