



**WATER INDUSTRY ACT 1991 SECTION 13  
PROPOSALS BY THE DIRECTOR GENERAL OF WATER SERVICES FOR THE  
MODIFICATION OF THE CONDITIONS OF APPOINTMENT OF  
THAMES WATER UTILITIES LTD**

**The process**

Any representation about, or objection to, these proposals must be in writing and sent to the Director General of Water Services, Centre City Tower, 7 Hill Street, Birmingham B5 4UA (Fax 0121 625 3606) so as to be received by him not later than 5.00pm on 5 January 2001. Please quote reference LEG/34/1/8/1.

**EXPLANATION OF THE PROPOSED MODIFICATIONS AND THE REASONS FOR THEM**

Thames Water Utilities Ltd (Thames Water) is a wholly owned subsidiary of Thames Water Plc (Thames). Thames has been acquired by GBV Gesellschaft für Beteiligungsverwaltung mbH (GBV), a wholly-owned subsidiary of RWE AG (RWE), a German company which is listed on the German Stock Exchanges.

Whenever a company such as Thames Water becomes part of a larger group, the Director General of Water Services (the Director) seeks modifications of its conditions of appointment as a water and a sewerage undertaker. They are designed to preserve its viability as a comparator with the other licensed companies, to preserve the independence of action of its Board when conducting the core business and to formalise the commitment of the parent company to facilitating the proper performance of its functions. Thames Water has consented to these proposed modifications.

**Maintenance of comparisons with other water and sewerage undertakers**

The Director considers that the modifications are necessary to enable him to continue to gather information about how Thames Water carries out its statutory functions and the costs which it incurs, after Thames becomes part of the RWE group.

To that end, the Director proposes modifications of Thames Water's Conditions of Appointment, which will require it to operate at arm's length from its Group.

The modifications will -

1 (a) *prohibit payment to any Associated Company in respect of any Charging Year, of any amount on account of services received by Thames Water from its Associated Company which exceeds-*

*i) the prices ascertained from market testing carried out by the Company in accordance with arrangements previously approved by the Director and which have no prejudicial effect on the proper carrying out of Thames Water's functions; or*

*ii) if, in the opinion of the Director, market testing is not appropriate, then such proportion of the costs (including a reasonable return) actually incurred by the Associated Company as the Director agrees is appropriate and*

*(b) require Thames Water to obtain from the Associated Company information required by the Director about the latter's costs.*

**Ring-fencing of the assets of Thames Water and its ability to act separately from its parent company, RWE, and all other companies in the Group.**

At the same time, the Director wishes to ensure that Thames Water's licensed business is ring-fenced from other activities of the RWE Group. Thames Water must not, whether through its involvement in those other activities or by its dividend policy, put at risk its ability either to carry out its functions as a water and a sewerage undertaker or to finance them. Further modifications will therefore -

2 *prohibit the transfer of any asset from Thames Water to any Associated Company except with the Director's consent and in compliance with his requirements concerning the valuation of the asset and its treatment in Thames Water's accounts;*

3 *prohibit Thames Water from -*

*(i) giving any guarantee of any liability of any company within the RWE Group;*

*(ii) making to any such company any loan;*

*(iii) continuing or assuming any commitment which includes a cross-default obligation (whereby Thames Water's*

*financial liabilities are increased or accelerated because of default elsewhere within the RWE Group) -*

*in each case without the Director's consent and*

- 4 *require that Thames Water's dividend policy will not, in the opinion of the Director, impair its ability to finance the proper carrying out of its functions.*

The Directors of Thames Water are already required to certify annually to the Director that it has adequate financial and management resources. Further modifications will require -

- 5 *(i) Thames Water to inform the Director as soon as its Board becomes aware of any circumstance which causes the Board to believe that its most recent annual certificate of the adequacy of its financial and management resources could not be repeated in the light of those circumstances;*

*(ii) that every annual certificate referred to in (i) shall be accompanied by a report prepared by Thames Water's Auditors and addressed to the Director, stating whether they are aware of any inconsistencies between, on the one hand, that certificate and the statements submitted with it and, on the other hand, any information which they obtained during their work as Thames Water's Auditors; and*

*(iii) that the Directors record their opinion that all contracts entered into with any Associated Company include all necessary provisions and requirements concerning the standard of service to be provided to Thames Water to ensure that it is able to meet all its obligations as a water and a sewerage undertaker.*

Although Thames Water is a subsidiary, it has its own duties as the water undertaker and the sewerage undertaker for those respective areas. The Director considers it important that Thames Water should, in carrying out those functions, behave as if they were substantially its sole business and it were a separate public limited company. Further modifications will require -

- 6 *that Thames Water shall, at all times, conduct the Appointed Business as if it were substantially its sole business and Thames Water were a separate public limited company. In doing so, Thames Water should have particular regard to the following:-*

- (a) *the composition of its Board should be such that its directors, acting as such, act independently of the parent company or controlling shareholder and act exclusively in the interests of Thames Water;*
- (b) *it must ensure that each of its directors must disclose, to it and to the Director, conflicts between their duties to Thames Water and other duties;*
- (c) *where potential conflicts exist between the interests of Thames Water as a water and a sewerage undertaker and those of other companies in the RWE Group, Thames Water and its directors must ensure that, in acting as directors of Thames Water, they have regard exclusively to its interests as a water and a sewerage undertaker;*
- (d) *no director of Thames Water should vote on any contract or any arrangement or any other proposal in which he has an interest by virtue of other directorships. This arrangement should be reflected in Thames Water's Articles of Association;*
- (e) *Thames Water should inform the Director without delay when:*
  - i) a new director is appointed;*
  - ii) the resignation or removal of a director takes effect; or*
  - iii) any important change in the functions or executive responsibilities of a director occurs.*

*Thames Water should notify the Director of the effective date of the change and, in the case of an appointment, whether the position is executive or non-executive and the nature of any specific function or responsibility;*

- (f) *the dividend policy adopted by Thames Water in the light of proposal 4 (above); and*
- (g) *the principles of corporate governance which are from time to time recognised by the Listing Rules of the Financial Services Authority;*

7 *that Thames Water will publish the annual interim and final financial results information which would be required, were it subject to those Listing Rules;*

8 that Thames Water will maintain a bond and use all reasonable endeavours to retain the listing of that bond on the London Stock Exchange and

9 that Thames Water will use all reasonable endeavours to ensure that its corporate debt retains investment-grade credit rating throughout its life (being a rating awarded by reputable credit-rating agencies in the UK).

#### **The role of GBV and RWE as owners of Thames Water**

Thames Water should have the active co-operation of GBV and RWE in complying with the conditions of its Appointment and in the proper discharge of its functions as a water and a sewerage undertaker. Further modifications will -

10(a) require Thames Water to obtain from each of those parent companies a legally-enforceable undertaking in its favour and in a form specified by the Director, that it will -

i) refrain from any action which would be likely to cause or require Thames Water to breach any of its obligations under the Water Industry Act 1991 or the conditions of its Appointments as a water and a sewerage undertaker; and

ii) ensure that Thames Water's Board contains not less than three independent non-executive directors, being persons of standing who shall collectively have relevant experience, local knowledge and understanding of the interests of Thames Water's customers.

(b) require the terms of that undertaking to apply to all other companies within the RWE Group;

(c) require that the undertaking remain in force for so long as Thames Water holds its Appointments as a water and a sewerage undertaker and remains a member of the RWE Group and

(d) require the undertaking to be delivered to the Director not later than one month after this modification comes into force;

11 require Thames Water to -

(i) produce to the Director the original of the undertaking under 10 above and provide him with any certified copies which he requires and

(ii) inform the Director immediately in writing, if it becomes aware that the undertaking has ceased to be legally-enforceable, or that there has been any breach of its terms; and

12 prohibit Thames Water (except with the Director's consent) from making any contract with a member of the RWE Group which is not one of Thames Water's subsidiaries, for so long as the above undertakings have not been given or there is an unremedied breach of any of them.