



OFWAT BOARD
Emergency Meeting to discuss the performance of
Thames Water, held 29 June 2006

Members

Chairman & Acting Chief Executive:

Philip Fletcher

Non-Executive Directors:

Penny Boys (via telephone)

Jane May (via telephone)

Lord Whitty

Peter Bucks

Executive Directors:

Melinda Acutt

Keith Mason

In attendance:

Huw Brooker (Head of Legal Services)

Sue Cox (Acting Head of Consumer Affairs)

Mark Hann (Head of Comparative Efficiency Team)

Ian Stephens (Senior Leakage Analyst)

James Higgins (Minute Secretary)

Apologies:

Fiona Pethick (Head of
Corporate Affairs)

1. Did Thames' failure to meet its leakage target constitute a breach of its duties under the WIA1991, section 37?

The Board was provided with figures showing Thames leakage in 2005-06 was 894MI/d, against a target of 860MI/d set by Ofwat at the Final Determinations in 2004. This was the second successive failure by Thames to meet its annual leakage targets, following a suspension of targets for the previous two years.

The reason offered by Thames for failure to meet the target was the perceived exceptional weather conditions, however Met Office statistics indicate that the 2005-06 winter was far from exceptional in terms of temperature or other weather conditions that may have affected leakage performance. The performance of other undertakers in the South East supported Ofwat's assertion that weather conditions were not a justifiable explanation. The independent reporter also agreed with this assessment.

The executive presented its assessment that the failure to meet the leakage target represented a failure to meet Thames' obligation under section 37 of the Water Industry Act 1991 to provide an efficient and economical water supply.

We also considered whether other companies performance fell into the same bracket as Thames and concluded that they did not.

Following consideration of the issues the Board concluded that there has been a breach of the Water Industry Act 1991, Section 37. Ofwat therefore had a duty to take enforcement action, unless certain exceptions applied.

2. Ofwat's response

The Board were presented with possible actions. The benefits and risks of these actions were then discussed. A wide range of issues were explored, focussed on the need to meet our statutory duties and the appropriate response to the failure by Thames to follow its statutory obligations. The Board was mindful of the desirability of;

- ensuring that Thames met the outputs set down in its final determination, by 2010, without imposing extra cost or burden on customers; and
- mitigating the risk of water shortages in the interim period.

The Board discussed possible actions in detail. It noted that if Thames failed to fulfil the conditions outlined in its undertaking, Ofwat would once more have the full range of regulatory tools available to it including the ability to impose a financial penalty. The Board also noted that a Section 19 undertaking offered an important contribution, at no further cost to customers, towards remedying the leakage situation.

The Board noted that if it chose to impose a financial penalty it would need to observe the principles set out in 'Financial Penalties: response to the consultation on draft statement of policy and definition of turnover' carried out jointly by Defra, Welsh Assembly Government and Ofwat, and published in March 2005. The Board was also mindful to take action that would directly address the problem and of the fact that any financial penalty would go to the consolidated fund, rather than towards remedying the problems or directly to customers.

Subject to some detailed points to be agreed by the executive with Thames, the Board agreed to accept a section 19 Undertaking, guaranteeing £150 million of extra investment, more than double the maximum potential fine, and borne only by shareholders, revised leakage and security of supply targets, and the resubmission of a water resources plan.

It was agreed that Ofwat would announce its decision at a press briefing in London on Tuesday 4 July.

James Higgins

July 2006