



Demonstrating Financial Resilience Consultation Response  
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Dear Ofwat,

Thank you for the opportunity to respond to this consultation. We appreciate that it seeks to address the concerns raised by the respondents of the July 2015 consultation.

The water and wastewater companies essentially demonstrate financial resilience from corporate governance and a regulatory perspective. Bristol Water, for example, already complies with the UK Corporate Governance Code and our financial statements provide assurance with respect to financial resilience. In addition, our annual report includes details of principal risks and uncertainties, a statement on going concern and a commentary on outlook for the following year, all of which are audited. Finally in order to maintain investment grade ratings we are carefully monitored by the credit rating agencies. Even within the context of all this scrutiny we consider that it will be consistent with good practice to adopt the new requirements of the UK Corporate Governance Code ("the Code") around the Long Term Viability Statement.

We agree that the new requirements of the Code are beneficial, but we do not believe that additional details being sought over and above it are necessary. We also feel that there are commercially sensitivity issues with the publication of this additional information. We are happy to elaborate on our concerns and provide information which we hope you find useful beyond the details provided in our response below.

The Code requires that taking account of the company's current position and principal risks, the directors should explain in the annual report how they have assessed the prospects of the company, over what period they have done so and why they consider that period to be appropriate. We note that Ofwat consultation is aligned to the Code requirements in respect of assessing what the appropriate 'long term' period is.

Finally we would welcome clarification as to whether a cross-reference from the regulatory accounts to the statutory accounts is acceptable, as we are unclear why the first statement of this type has to

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be included in both the statutory and regulatory accounts for the 2015-16 financial year (a cross-reference is considered acceptable for other notes).

Our responses to the consultation questions are as follows:

**Q1 Do you agree that the proposed approach to companies demonstrating their financial resilience will provide an appropriate level of assurance about each company's long term financial resilience?**

We agree that compliance with the new requirements of the Code around Long-term Viability Statement is beneficial. We would appreciate if Ofwat could provide clarification regarding the following matters:

- On page 2 and in appendix 1 of the consultation document, it is suggested that directors should state why they have selected the sensitivities that they have used. In our view, stating the sensitivities and the reasons for selecting the same in the viability statement is commercially sensitive and also beyond the requirements of the Code. Some sensitivities for example may relate to a banking covenant that forms part of a confidential agreement and therefore stating those sensitivities may not be in the best interest of the companies.
- On page 2 and in appendix 1 of the consultation document, it is suggested that management should outline any actions that it would need to take in the event that the situations used for stress testing were to result in an unacceptable level of deterioration in the company's financial metrics. In our view providing details of the actions in the Long Term Viability Statement is commercially sensitive and also beyond the requirements of the Code.
- Appendix 1 refers to 'third party assurance', can it be clarified what is meant by that. In our view the audit of the annual report by company external auditors would provide sufficient assurance. We understand that any further third party assurance is beyond the requirements of the Code.

**Q2 Is there anything else that we should be recommending that companies explicitly include in their statement on long term financial viability?**

No, we do not consider there is anything else that should be included by companies.

**Q3 Are there alternative approaches to companies demonstrating their long term financial resilience that Ofwat should be considering?**

The alternatives are to use evidence the financial statements already provided, or to enhance this with a viability statement in line with the Code. We thought it would be helpful to provide an example of the latter, drawn from the Code (easyJet plc Annual report and accounts 2015, p22):

#### **VIABILITY STATEMENT**

The Directors have assessed easyJet's viability over a three-year period to September 2018. This is based on three years of the strategic plan, which gives greater certainty over the forecasting assumptions used.

In making their assessment, the Directors took account of easyJet's current financial and operational positions and contracted capital expenditure. They also assessed the potential financial and operational impacts, in severe but plausible scenarios, of the principal risks and uncertainties set out on pages 24 to 29 and the likely degree of effectiveness of current and available mitigating actions.

Based on this assessment, the Directors have a reasonable expectation that the Company and the Group will be able to continue in operation and meet all their liabilities as they fall due up to September 2018.

In making this statement, the Directors have also made the following key assumptions:

- funding for capital expenditure in the form of capital markets debt, bank debt or aircraft leases will be available in all plausible market conditions;
- there will not be a prolonged grounding of a substantial portion of the fleet; and
- in the event that the UK votes to leave the European Union, the terms of exit are such that easyJet would be able to continue to operate over broadly the same network as at present.

We would also like to make the point that different approach to different companies may be more suitable in respect of Ofwat's proposal for requirements in addition to the Code. For example, Bristol Water is almost entirely appointed business, thus our financial statements focus on the areas that Ofwat regulates. Therefore, once compliant with the Code in respect of the long term viability statement, our financial statements would provide sufficient assurance on financial resilience. However other companies with a large non-appointed business may not be in a similar position. Therefore Ofwat could word any regulatory requirement such that additional disclosure requirements are only required to the extent that audited annual reports do not cover the Code requirements.

We look forward to discussing these issues further with you in due course.

Yours sincerely,

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Regulatory Director

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