

8 June 2018

Change of Control
Ofwat
Centre City Tower
7 Hill Street
Birmingham
B5 4UA

By email: FinanceAndGovernance@ofwat.gsi.gov.uk

Dear Sir

CONSULTATION ON CHANGE OF CONTROL – GENERAL POLICY AND ITS APPLICATION TO THAMES WATER

This is South West Water's response to Ofwat's consultation on its general policy relating to change of control and the associated proposed licence modifications.

The company is supportive of the direction of travel in which the proposed licence modifications take the industry, having already demonstrated this by working with Ofwat to include a broadly comparable Condition P in our own licence from 1 April 2016.

In this response we focus on the substantive modifications the consultation proposals would make to South West Water's current licence and have provided specific comments on these. We also provide general comment on whether standardisation is appropriate, given the varying company sizes and ownership structures.

The annex to this letter contains this information and our responses to the specific questions raised in the consultation.

We hope you find our comments helpful. Please contact us if you would like further detail.

Yours faithfully,



**Iain Vosper
Regulatory Director**

GENERAL COMMENTS

South West Water agrees that there is a real need for the industry to ensure that water and sewerage undertakers have transparent ownership, control and governance arrangements, and that they have access to adequate funding to fulfil their statutory duties. We support Ofwat's proposals in this area and the direction of travel contained in the consultation.

We have some reservations with the proposal that the licence conditions developed for Thames Water should be applied uniformly to each undertaker. Thames Water Limited is a private company with a very complicated ownership structure involving layers of UK and foreign companies and trusts. In contrast, South West Water is wholly owned by Pennon Group PLC, which is a public listed UK company that must follow strict rules relating to share ownership and governance prescribed by statute. We believe that the PLC framework provides transparency and confidence in South West Water's ownership and accountability for the industry, for our regulators and for our customers.

South West Water considers that the licence condition requirements relating to this area could be tailored to the particular ownership structure of the undertaker to ensure that the requirements are suitable and proportionate.

DETAILED COMMENTS ON THE PROPOSALS

Although the consultation document contains a list of questions for undertakers, we are conscious that some of the proposed conditions are already included within South West Water's licence condition P. In view of this, we have set out below the substantive changes that the consultation proposals would make to South West Water's current licence and have provided specific comments on these.

For ease of reference, we have then set out the relevant questions from the consultation document and indicated where we have commented on these in the South West Water Specific section.

South West Water does not have any views on the proposed changes to Thames Water's licence so has not responded to questions 8 to 12.

SOUTH WEST WATER SPECIFIC COMMENTS

Proposed Conditions P3.6 and P3.7

Substantive changes

The proposed conditions P3.6 and P3.7 would be new conditions for South West Water's licence. These would require South West Water to notify Ofwat, and to provide information, where there is a proposed change to the Ultimate Controller of South West Water. The definition "Ultimate Controller" is already used in the licence at condition P3.1 and means "*any person which, whether alone or jointly and whether directly or indirectly, is, in the reasonable determination of the Water Services Regulation Authority, in a position to control or in a position to materially influence the policy or affairs of the Appointee or any Holding Company of the Appointee*".

South West Water Comments

South West Water supports the need to the proposed conditions P3.6 and P3.7 but is concerned that the definition of 'Ultimate Controller', while appropriate for condition P3.1, is too ambiguous and uncertain for the proposed conditions P3.6(a) and (b) to operate as intended because it relies on undertakers anticipating Ofwat's 'reasonable determination'.

By way of example, South West Water would assume that the issue of a new share saving scheme for Pennon Group PLC staff would not fall within the intended scope of conditions P3.6(a) and P3.6(b) and would therefore not require notification or provision of investor information.

South West Water would favour a more objective standard for conditions P3.6(a) and (b), combined with a right for Ofwat to request information on control and ownership arrangements where it considers that it needs updated information from an Undertaker.

South West Water has not considered in detail the investor information checklist at A2 of the consultation document, as we do not believe that this is intended to capture low-level changes within the ownership of a UK listed PLC (as described above). However, South West Water is generally supportive of the proposals.

Proposed Condition P7.1

Substantive changes

It is unclear from the consultation document how the new proposals will affect companies that already have Condition P in their licence. For South West Water the proposed changes to licence condition P paragraph 7 suggest that there would be a revised condition P7.1 and that South West Water's existing paragraph P7.3 would be deleted.

South West Water comments

Current, condition P7.3 affords South West Water the option, with Ofwat's agreement, to avoid maintaining an Investment Grade Rating and instead provide evidence of the company's financial robustness.

We believe this is in the best interests of customers.

CONSULTATION QUESTIONS AND RESPONSE REFERENCES

QUESTION 1

What are your views on the introduction of notification requirements on change of control into the licence information requirements?

Please see General Comments and detailed comments on Proposed Conditions P3.6 and P3.7.

QUESTION 2

What are your views on the proposed obligation to provide us with information?

Please see General Comments and detailed comments on Proposed Conditions P3.6 and P3.7.

QUESTION 3

What are your views on the information that may be helpful for our assessment of change of control?

Please see detailed comments on Proposed Conditions P3.6 and P3.7.

QUESTION 4

What are your views on the proposed obligation to require the Appointee to comply with any direction from Ofwat to enforce an Ultimate Controller's undertaking?

No comments

QUESTION 5

What are your views on bringing all the licences up to the same standards, including introducing a requirement to meet the BLTG principles?

Please see General Comments.

QUESTION 6

Are there aspects of the most up to date provisions which you think we need to revisit or amend?

Please see detailed comments on Proposed Conditions P7.1

QUESTION 7

- a) **What are your views on how the ring fencing conditions need to be further strengthened? In particular, in relation to:**
- b) **Maintaining an appropriate credit rating and how and when the lock-up conditions are triggered?**
- c) **Whether there needs to be a more explicit requirement to inform us of particular events affecting the Appointee?**
- d) **Managing potential conflicts of interest where there are cross-shareholdings?**
- e) **Safeguarding the autonomy of the Appointee?**
- f) **Any other issues?**

Please see detailed comments on Proposed Conditions P7.1

QUESTION 8

Do you agree with our assessment of the incoming investors of Thames Water?

No comments

QUESTION 9

What are your views on the ability of the new investors of Thames Water to run a regulated water utility?

No comments

QUESTION 10

Do you have any concerns with the new investors of Thames Water that might affect the ability of Thames Water to fulfil its statutory duties and obligations under its licence?

No comments

QUESTION 11

What are your views on the proposed modifications of Thames Water's licence?

No comments

QUESTION 12

What are your views on our assessment of the Ultimate Controllers under the current arrangements?

No comments

