

Change of Control
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Dear Sir or Madam

Change of control: Consultation on change of control general policy and its application to Thames Water

Thank you for inviting Yorkshire Water to contribute to the consultation on issues arising out of the change of control of Thames Water Utilities Limited, as well as broader issues Ofwat is considering as part of its work on reforms to companies' licences.

Yorkshire Water is committed to working with our customers and the wider public about how we define our role in providing critical public services that can be trusted. We continue to work to improve the level of openness and transparency we provide to our customers and stakeholders, and are currently conducting a consultation with customers and stakeholders on a new Openness Charter.

We believe our approach also aligns with the work Ofwat is progressing to improve trust in the sector and further develop the regulatory regime, including exploration of how companies' licences can be reformed to help ensure water companies put customers' interests at the heart of what they do.

With regard to the general regulatory issues arising from changes in control and proposals for modifications to the licence of Thames Water, we wish to highlight three specific areas:

1. Notifications of change of control, identification of Ultimate Controllers and enforcement of undertakings

We think it is important for there to be openness and transparency in understanding who owns the water companies in England and Wales. We support the requirement for companies to notify Ofwat when it becomes aware of a change of, or likely change of control, and this has been our approach to date.

We agree that it is sensible for companies or investors to provide to Ofwat an appropriate level of information of a change of control and this is aligned with good and open governance.

We would welcome discussion with Ofwat on the range and depth of information that may be requested in relation to a change of control and how an Appointee can ensure it always can satisfy a new licence condition.

We understand the assessment of the Ultimate Controllers of an Appointee is not always straightforward and a number of factors are considered. We would welcome further clarification from Ofwat on how it intends to approach future assessments, and what practical mechanism it will put in place to facilitate enquires and feedback from companies and/or investors. Key will be that a defined approach can be uniformly applied, even if the outcomes may not have uniform features.

In regard to enforcement of undertakings we believe the existing provisions of the licence do provide Appointees the protections that require to operate on the basis of a standalone business and that it is in their interests to enforce undertakings where relevant. We would be happy to discuss with Ofwat scenarios where Ofwat would consider it may need to intervene and make a direction to an Appointee to enforce an existing undertaking.

2. Ring fencing provisions

We support the principles to standardise licence conditions around ring fencing to ensure the most up to date provisions are in place across the sector. We agree that Ofwat has focused on the correct priority issues that relate to change of control situations and that ensure customers remain protected beyond such events. We believe the proposals are a good starting point for discussions on how licence conditions are modified and whether any obligations change materially.

We note it is for the Board of each company to identify, assess and manage the financial risks relevant to that company, and we ask Ofwat to consider the proportionality of any new obligations. We would welcome the opportunity to work with Ofwat in resolving the priority areas.

3. Thames Water – assessment of incoming investors and licence modifications

We feel unable to comment of the specifics of the assessment of the incoming investors of Thames Water or indeed the proposed detailed licence text. However, we do welcome the opportunity to view Ofwat's thinking around licence modifications that improve and simplify elements of the ring fencing framework.

We look forward to having discussions with Ofwat on how both the Ultimate Controller assessment and potential licence modifications can be further considered and commonly applied sector wide, and not solely against one specific Appointee.

We have responded to each of the consultation questions in the attached table 1, and we would be pleased to discuss matters further should you consider this of benefit.

Yours faithfully,

A handwritten signature in cursive script that reads "Adrian Kennedy". The ink is a light grey or blue color.

Adrian Kennedy
Director of Regulation

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Table 1

Yorkshire Water response to the consultation: Change of control - general policy and its application to Thames Water

Q1.	<i>What are your views on the introduction of notification requirements on change of control into the licence information requirements?</i>
A1.	<p>We think it is important for there to be openness and transparency in understanding who owns the water companies in England and Wales. We agree that Ofwat has an important role in this and that there is value in a consistent approach. We support the proposal for a requirement to be included in licences for companies to notify Ofwat when they become aware of a change of, or likely change of control, and this has been our approach to date.</p>
Q2.	<i>What are your views on the proposed obligation to provide us with information?</i>
A2.	<p>We agree that it is sensible for companies and/or investors to provide to Ofwat an appropriate level of information of a change, or possible change of control (i.e. a change of an Ultimate Controller) within a short period of becoming aware of it.</p> <p>We would welcome discussion with Ofwat on the range and depth of information required under the initial proposals, and any practical limitations on the information about a future investor an Appointee may have access to in order to satisfy a new licence condition.</p>
Q3.	<i>What are your views on the information that may be helpful for our assessment of change of control?</i>
A3.	<p>The information Ofwat may ask for in order to understand whether an incoming shareholder is an Ultimate Controller seems appropriate in general (as outlined in appendix A2).</p> <p>All UK companies must declare information on beneficial owners and controllers. We see no reason why an investor seeking to acquire a certain sized interest in an English or Welsh water company should do any less.</p> <p>We are less sure that it is as important for Ofwat to seek information about the technical proficiency of an acquirer to run a water company. There are many potential investors in the sector who may wish to invest in a water company but themselves do not demonstrate a technical capability to run a water company or a history of investing in regulated sectors. After all, it is the Appointee and its management team that must meet its licence obligations. A key function of the owner of an Appointee, is to not frustrate these obligations.</p> <p>We believe the provision of such information should not be used to become a future sector 'fit and proper' persons test for investors where a change of the Ultimate Controller is identified.</p>

	<p>We would welcome discussion with Ofwat on the information it may require to be provided by an Appointee to satisfy a new licence condition, as opposed to information Ofwat may seek from an incoming investor.</p>
Q4.	<p><i>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?</i></p>
A4.	<p>Due to the potential for an Ultimate Controller to materially influence an Appointee, we recognise the protections offered by the Ultimate Controller undertakings, and that where relevant these are enforced in the Appointees interests.</p> <p>If an Appointee is at risk of breaching obligations under its licence or the WIA91, due to the actions of an Ultimate Controller, the Appointee already has the capability to enforce an undertaking for the position to be resolved. Good Board governance arrangements also have the potential to limit undue influence of shareholders, whether they be considered as an Ultimate Controller or otherwise.</p> <p>Appointees have licence obligations to inform Ofwat if it becomes aware that an undertaking ceases to be legally enforceable, or if there has been a breach in its terms.</p> <p>The wider licence simplification activity currently being undertaken by Ofwat and the water companies includes a principle that the obligations should be proportionate. We currently do not see the need for an additional licence provision requiring the Appointee to comply with any direction from Ofwat to enforce the terms of an undertaking.</p>
Q5.	<p><i>What are your views on bringing all the licences up to the same standards, including introducing a requirement to meet the BLTG principles?</i></p>
A5.	<p>We believe it is sensible to have a consistent approach to companies' licences and have standardised obligations insofar as is practicable. In pursuit of better governance, we also welcome the opportunity to share thinking with Ofwat on the BLTG principles following its imminent review, and how to give these greater prominence.</p> <p>As Ofwat has noted, different companies are in different positions, reflecting the history of change of control in the industry. We believe it may not be feasible for all companies to be brought onto the same ring-fencing provisions or BLTG conditions within the same timeframe.</p>
Q6.	<p><i>Are there aspects of the most up to date provisions which you think we need to revisit or amend?</i></p>
A6.	<p>The 'most up to date' provisions presented as part of this consultation are the licence modifications to Thames Water's licence notified to Thames Water under section 13 of the WIA91.</p>

	<p>Naturally we have not been involved in the development of the proposed modifications to Thames Water's licence, and whether these become a template for standardised conditions for all companies' licences. At this stage we are unable to provide detailed comments on the drafting, as presented in appendix A3. We look forward to the opportunities to share thinking with Ofwat on licence modifications around ring-fencing, change of control and the BLTG principles.</p>
Q7.	<p><i>What are your views on how the ring fencing conditions need to be further strengthened? In particular, in relation to:</i></p> <ul style="list-style-type: none"> • <i>Maintaining an appropriate credit rating and how and when the lock-up conditions are triggered?</i> • <i>Whether there needs to be a more explicit requirement to inform us of particular events affecting the Appointee?</i> • <i>Managing potential conflicts of interest where there are cross-shareholdings?</i> • <i>Safeguarding the autonomy of the Appointee?</i> • <i>Any other issues?</i>
A7.	<p>We welcome the opportunity to discuss potential licence modifications in relation to the financial ring fencing framework.</p> <p>Regarding the four areas highlighted in the consultation, we would be pleased to work with Ofwat and the sector as a whole, to develop standardised provisions that improve financial resilience and ensure customers remain protected.</p> <p>As part of this future work we would welcome an approach that simplifies the licence conditions and removes possible ambiguities to ensure Appointees understand the requirement for reporting to Ofwat, and that Appointees and shareholders equally understand that the appointed business has the autonomy to operate on a standalone basis.</p> <p>We require further time to review the modified Thames Water licence text where Ofwat propose this reflects the current highest standard.</p>
Q8.	<p><i>Do you agree with our assessment of the incoming investors of Thames Water?</i></p>
A8.	<p>We do not have any information with which to inform a view on the assessment Ofwat has undertaken of the incoming investors of Thames Water.</p> <p>We would welcome a wider explanation of the internal assessment methodology used in the Thames Water change of control case. For example, what assessment options were considered and discounted.</p> <p>In this way we can establish if this methodology would be flexible enough to adapt to all anticipated future change of control situations and Appointees different corporate structures, and to be considered an effective 'common methodology'.</p>
Q9.	<p><i>What are your views on the ability of the new investors of Thames Water to run a regulated water utility?</i></p>
A9.	<p>We do not have any comments to make on the abilities of the new or existing investors to run an English or Welsh regulated water utility.</p>

Q10.	<i>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?</i>
A10.	We have no comments to make regarding the new investors of Thames Water.
Q11.	<i>What are your views on the proposed modifications of Thames Water's licence?</i>
A11.	<p>We note the proposed modifications to Thames Water's licence is considered by Ofwat as the current highest standard. At this time, we have no specific comments to make in regard to the proposed modifications text, as detailed in appendix A3.</p> <p>We would request that whilst modifications are being proposed for Thames Water's licence, should these subsequently be considered by Ofwat appropriate for other Appointees licence following a change of control, the principles used in Ofwat's licence simplification programme should apply, namely:</p> <ul style="list-style-type: none"> • Clarify existing obligations on Appointees (and only change these where new provisions are being proposed); • Remove elements that are redundant; • Make the licence text easier to understand; and, • Be proportionate.
Q12.	<i>What are your views on our assessment of the Ultimate Controllers under the current arrangements?</i>
A12.	<p>We have no specific comments to make in regard to the findings of the assessment of the Ultimate Controllers of Thames Water under the recent ownership changes. We note that the exact approach taken to change of control situations may be affected by the specific governance arrangements of an Appointee, such as prevailing shareholder arrangements in respect of director nominations.</p> <p>We would welcome further clarity from Ofwat on how a consistent and proportionate Ultimate Controller assessment methodology will be applied, given this may not be a one-size fits all approach.</p> <p>We would also welcome a discussion with Ofwat on how such assessments will be deployed to the sector as a whole over time, and the practical mechanisms that may be put in place to accommodate any Appointee or investor challenges or revisions of such assessments.</p> <p>We understand Ofwat proposes to conduct a public consultation where it considers the identification of Ultimate Controllers is complex, or it has concerns with the current licence conditions of the Appointee or other matters. We believe this consultation stage should have limited influence over how a change of control proceeds in practice, or where a change has already concluded. Rather, the consultation stage may result in additional information being captured by Ofwat with which to inform its Ultimate Controller assessment and its findings.</p>

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