

## **Undertakings for the purpose of section 19 of the Water Industry Act 1991**

These undertakings are given by Thames Water Utilities Limited (“**the Company**”) to the Water Services Regulatory Authority (“**Ofwat**”) pursuant to section 19(1)(b) of the Water Industry Act 1991.

### **Part 1: Contraventions to which the undertakings relate**

1. The Company is appointed as a water undertaker under the Water Industry Act 1991 (“**the Act**”) and operates pursuant to its instrument of appointment (“**Licence**”).
2. Section 37 of the Act (“**Section 37**”) requires every water undertaker to develop and maintain an efficient and economical system of water supply within its area and to ensure that all such arrangements have been made -
  - a. for providing supplies of water to premises in that area and for making such supplies available to persons who demand them, and
  - b. for maintaining, improving and extending the water undertaker’s water mains and other pipes,

as are necessary for securing that the undertaker is and continues to be able to meet its obligations under Part III of the Act.

3. Paragraph 6A.1 of Condition F of the Licence (“**Condition F6A.1**”) requires the Company at all times to act in the manner best calculated to ensure that it has adequate:
  - a. financial resources and facilities;
  - b. management resources; and
  - c. systems of planning and internal control

to enable it to secure the carrying out of the Regulated Activities including the investment programme necessary to fulfil its obligations under the Licence. These requirements must not be dependent upon the discharge by any other person of any obligation under, or arising from, any agreement or arrangement under which that other person has agreed to provide any services to the Company in its capacity as a Relevant Undertaker.

4. Ofwat has found that the Company is in contravention of Section 37 and Condition F6A.1 (“**the contraventions**”) in relation to its leakage reduction performance within the current price control period (2015-20) and its management of its leakage reduction operations, as specified in a notice under section 22A of the Act to impose a penalty dated August 2018.
5. The Company has agreed to take the steps specified in Part 2 below (“**the undertakings**”) for the purpose of securing and facilitating compliance with Section 37 and Condition F6A.1 in respect of those contraventions.
6. Ofwat considers that, to the extent the Company complies with these undertakings, it is not required to make an enforcement order under section 18 of the Act in respect of the contraventions.

## **Part 2: The undertakings**

### **Financial measures**

1. The Company accepts and will implement the following financial measures:
  - a. a reduction in its total revenue allowance for AMP7 of the greater of £46 million and its total excess expenditure on leakage management in AMP6 (as calculated in accordance with the methodology referred to in Thames Water’s proposals discussed with Ofwat on 19 March 2018).
  - b. a commitment not to reverse the Company’s attenuation of customers’ bills in 2018-19 to reflect the £10.8 million of automatic ODI penalties Thames Water incurred as a result of its leakage and SoSI performance in 2016-17.
  - c. a rebate applied to customers’ bills in 2019-20, to reflect the total amount of any expected automatic ODI penalties for leakage and SoSI performance for 2017-18.
  - d. a rebate applied to customers’ bills in 2020-21 and 2021-22 to reflect the total amount of any automatic ODI penalties for leakage and SoSI performance for 2018-19 and 2019-20 respectively.
  - e. an additional rebate applied to customers’ bills in 2019-20 to reflect an ex-gratia payment of £7 million.

- f. removal of the penalty collar in the calculation of any ODI penalty for leakage reduction performance for the years 2018-19 and 2019-20, applying this as a rebate on customers' bills in 2020-21 and 2021-22 (respectively) if they occur.
- g. identifying the rebates referred to in sub-paragraphs (c) to (f) clearly on customers' bills in wording approved by Ofwat.

Thames Water shall apply the rebates referred to above to its wholesale tariffs.

### **Leakage reduction undertakings**

2. The Company commits as part of these undertakings to reduce its leakage to 606MI/d or better by 31 March 2020 (the "**Performance Commitment**").
3. The Company commits to prepare its PR19 business plan on the basis of a commitment to reduce leakage by a further 15% (or better) from its 2019-20 Performance Commitment level and an ambition to reduce it by 50% or better from the 2016-17 level in subsequent price control periods. The specific level of leakage in MI/d will be based on whichever definition of leakage is in place at the time of calculation.

### **Leakage performance reports undertaking**

4. For every month until the later of 31 March 2020 and such time as the Company reduces its leakage to the level specified in its Performance Commitment for 2019-20, the Company will publish in a prominent position on its website a report on how its leakage performance compares with the leakage recovery plan appended to these undertakings. It will also provide these reports to Ofwat and the Company's Customer Challenge Group as soon as possible after publication.
5. The Company will ensure that each report complies with the following requirements:
  - a. it will include a comparison of the monthly volume of leaks found and fixed (expressed in MI/d) against what the Company planned to achieve, and an explanation of the reasons for any differences.
  - b. it must be easily accessible to customers (in terms of availability, style and content) and facilitate meaningful customer feedback.

- c. it will identify any material risks to the delivery of the plan and explain how the Company is addressing them.
- d. it must be certified by an appropriately qualified monitor independent of the Company that the report has been prepared in a way that is consistent with the methodology it employed in formulating its Performance Commitments for PR14.

### **Customer engagement undertaking**

6. The Company will establish and implement a customer engagement programme (the “**customer engagement programme**”) through which it will engage meaningfully with its customers on its leakage performance and any potential risks to its improvement. Meaningful engagement includes seeking and obtaining informed feedback from customers, ensuring that the full range of the Company’s customer base is reasonably represented.
7. As part of the customer engagement programme, the Company will:
  - a. develop a dedicated micro-website prominently linked by its main website and accessible (in terms of availability, style and content) which will provide and seek customer feedback on the Company’s leakage reduction activities,
  - b. ensure that both executive and non-executive members of its Board participate personally and on a regular basis in the customer engagement programme, including meeting customer representatives to discuss the Company’s leakage performance, and
  - c. ensure that the Board maintains effective oversight of the customer engagement programme and receives and discusses customer feedback on leakage on a regular basis.

### **Executive and senior management incentives undertaking**

8. The Company will ensure that no executive or senior management incentive bonus which is dependent upon the Company’s leakage performance in the years 2018-19 and 2019-20 will be paid unless the Company meets or exceeds its Performance Commitment for the relevant year.

### **Condition F certificates assurance undertaking**

9. The Company will ensure that, in providing certificates under Condition F, its Directors will do so on the basis of their reasonable belief, formed on the basis of reasonably diligent enquiry. The Directors will provide Ofwat with evidence of that enquiry, a statement of the main factors they have taken into account in providing the certificate, and procure a report from (an) external auditor(s) on its ability to sign the certificate.
10. The auditor will perform a review of the processes, procedures and controls that operate over the main factors that the Directors take into account when considering their ability to approve and sign the F6A certificate. This review will be in addition to the standard annual procedures performed that enables the auditor to provide the annual report to the Company and Ofwat under Licence Condition F6A. The auditor will produce a 'Review and Recommend' Report (the "Report") addressed to the Company. Subject to the auditor receiving a signed 'hold harmless letter' from Ofwat, the Company will share the report with Ofwat. The report will include the auditor's findings on:
  - a. whether the Company has appropriate and effective compliance and assurance policies in place, which are regularly reviewed by appropriate and qualified individuals within Thames Water, and updated where necessary;
  - b. whether these policies are implemented and adhered to;
  - c. details of how any compliance issues identified through any of these processes have been addressed;
  - d. whether the Company's Board is regularly informed of the operation of these policies and any material potential compliance issues; and
  - e. whether the Company should adopt any improvements to these processes.
11. The Directors will also provide Ofwat with an explanation of how they have addressed any adverse findings from the external auditor(s).

### **Governance review undertaking**

12. The Company will review the governance arrangements for the Boards of Thames Water Utilities Limited and Kemble Water Holdings Limited and the committees that report to them. It will use its best endeavours to ensure the

implementation of such changes as are necessary, in consequence of that review, to ensure that the Company is able to operate efficiently and effectively, and sufficiently independently of its parent companies, to the benefit of its customers.

### **Operational oversight undertaking**

13. The Company will maintain sufficient management control over the delivery of its operational functions (whether or not they are undertaken by the Company's own employees) to ensure that it is able to meet its leakage and SOSI Performance Commitments.
14. The Company's leakage and SOSI performance commitments under the undertaking given at paragraph 13 are:
  - a. its undertaking at paragraph 2;
  - b. its performance commitments for leakage included in its business plan for PR19 as provided in accordance with its undertaking at paragraph 3; and
  - c. its performance commitment of 100 for SOSI for 2019-20.

### **Reporting on compliance with the undertakings**

15. The Company will:
  - a. provide written monitoring reports to Ofwat:
    - i. demonstrating the steps it has taken in complying with the undertakings, and
    - ii. providing assurance of its ongoing compliance with the undertakings.

The first of these monitoring reports will be provided by 1 November 2018, and then on a six monthly basis until March 2025, or such time as Ofwat agrees that this reporting frequency can be reduced or removed.

- b. provide to Ofwat any supporting information and documents which Ofwat reasonably requests in relation to, or in connection with, the undertakings (including in relation to the Company's implementation of or compliance with the undertakings).

- c. ensure independent, third party assurance of the Company's compliance with the undertakings (in addition to the assurance which the Company will procure in relation to the undertakings in paragraphs (5) and (9) above). This assurance will be reported to the Company's Board and included in the monitoring reports provided to Ofwat.
- d. designate a member of its Senior Leadership Team as the undertakings compliance officer, who will have a general responsibility for:
  - i. ensuring compliance with the Undertakings,
  - ii. preparing the monitoring reports, and
  - iii. reporting the monitoring reports to the Company's Board so that the reports have the Board's assurance before their submission to Ofwat.

By signing these undertakings the Company agrees to be bound by them.

Signed on behalf of the Company by:

A handwritten signature in dark ink, consisting of a stylized 'M' followed by a horizontal line and another stylized 'M' followed by a horizontal line.

Chief Executive Officer:

Thames Water Utilities Limited

Dated: 3.8.2018

**Appendix A1: Thames Water's Leakage Recovery Plan (June 2018)**

	<b>2015-16</b>	<b>2016-17</b>	<b>2017-18</b>	<b>2018-19</b>	<b>2019-20</b>
Leakage performance commitment (Megalitres per day (Ml/d))	649	630	620	612	606
Leakage performance commitment collar	657	649	649	649	649
Leakage recovery plan forecasts	-	677	695	672	606
SoSI performance commitment	100	100	100	100	100
SoSI performance commitment collar	97	97	97	97	97
SoSI forecasts		99	97	100	100