

## SCHEDULE 2: Conditions of the Appointment

### Condition A: Interpretation and Construction

1. Unless the contrary intention appears:

- (1) words and expressions used in these Conditions and references in these Conditions to enactments shall be construed as if they were in a Northern Ireland enactment and the Interpretation Act (Northern Ireland) 1954 applied to them;
- (2) references in these Conditions to enactments shall include any statutory modification thereof after the transfer date;
- (3) words and expressions used in these Conditions shall have the same meaning as in any provision of the Order;
- (4) references in these Conditions to Articles and Schedules are references to Articles of, and Schedules to, the Order; and
- (5) references in these Conditions to paragraphs are references to paragraphs of the Condition in which the reference appears and references to subparagraphs are references to subparagraphs of the paragraph in which the reference appears.

2. In construing these conditions:

- (1) the heading or title of any Condition or of any paragraph of any Condition shall be disregarded; and
- (2) any description of the purposes of a Condition shall be construed subject to the provisions of the rest of the Condition in which that description appears and, accordingly, in the event of any conflict between such description and the provisions of the rest of the Condition, the latter shall prevail.

3. Unless the context otherwise requires, in these conditions:

"**the 1973 Order**" means the Water and Sewerage Services (Northern Ireland) Order 1973;

"**the 1986 Order**" means the Companies (Northern Ireland) Order 1986;

"**the Appointed Business**" means the business consisting of the carrying out by the Appointee of the Regulated Activities;

"**the Area**" means the area for which for the time being the Appointee holds the appointment as water undertaker, or as the case may be, sewerage undertaker;

"**Associated Company**" means any Group Company or Related Company;

"**the Auditors**" means the Appointee's auditors for the time being appointed in accordance with the 1986 Order;

"**books and records**" means any and all books, records, files, maps, plans, documents, papers, accounts, estimates, returns and other data of whatsoever nature and whether or not created, recorded or maintained in a document;

"**Charging Year**" means a year commencing on 1st April;

"**domestic customer**" means the occupier of domestic premises;

"domestic premises" means any premises used wholly or partly as a dwelling or intended for such use;

"Regulatory Price Control Period" means the period commencing on the day provided by paragraph [5A] of Condition B and continuing through any remaining part of the Charging Year in which that day falls and subsequent Charging Years;

"financial year" means a financial year of the Appointee beginning and ending on the respective dates referred to in Article 231(2) of the 1986 Order;

"the General Consumer Council" means the General Consumer Council for Northern Ireland on which functions in relation to consumer matters are conferred by Chapter III of Part III of the Order;

"Group Company" means any subsidiary or holding company (other than a Government department) of the Appointee and any subsidiary of any such holding company of the Appointee (other than the Appointee);

"Information" means information which is in the possession of the person required to furnish it or which it can reasonably obtain or which it can reasonably prepare from information which is in its possession or which it can reasonably obtain, and information which is required to be furnished under any of these Conditions shall be furnished, subject to the provisions of the Condition under which that information is required to be furnished, in such form and manner as the Authority may reasonably require;

"London Stock Exchange" means the London Stock Exchange plc;

"Official List" means the official list of the UK Listing Authority;

"Ofwat" means the Water Services Regulation Authority established under section 1A of the Water Industry Act 1991;

"PPP Contractor" means the counterparty to:

- (i) long-term arrangements with the Appointee under HM Government's private finance initiative; or
- (ii) broadly equivalent long-term arrangements with the Appointee involving the significant transfer of risk from the Appointee to the counterparty and the provision to the Appointee of capital works, both in relation to the performance by the Appointee of the Regulated Activities,

pursuant to which, in each case, the counterparty provides works (or, as the case may be, such works) whether or not together with facilities or services, which relate to the performance by the Appointee of the Regulated Activities.

"Periodic Review" means a review of the Appointed Business carried out under paragraph 10 or 12 of Condition B, and as more particularly described in paragraph 1.2 of Condition B, but so that references in Part IV of Condition B to a Periodic Review shall exclude any review carried out under paragraph 12 of that Condition and shall include the determination by the Competition Commission of the disputed determination referred to it under paragraph 17 of Condition B following the giving of Information to the Authority in accordance with paragraph 10;

"Prior Year" means the year commencing 1st April immediately prior to the relevant Charging Year;

"Reference Notice" means a notice given to the Authority under paragraph 12 or 15 of Condition B;

"the Regulated Activities" means the functions of a water undertaker or, as the case may be, a sewerage undertaker and, for the avoidance of doubt, references to the functions of a water

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undertaker or, as the case may be, a sewerage undertaker shall include references to the duties imposed on a water undertaker or, as the case may be, a sewerage undertaker;

**"Related Company"** means any company in relation to which the Appointee or any Group Company is a Related Undertaking or which is such a Related Undertaking in relation to the Appointee or any Group Company;

**"Related Undertaking"** means, in relation to any company, any body corporate (other than one which is a Group Company in relation to that company or which is a Government department) in which that company holds on a long-term basis a qualifying capital interest for the purpose of securing a contribution to that company's own activities by the exercise of any control or influence arising from that interest. For this purpose, "qualifying capital interest" means, in relation to any body corporate, an interest in shares comprised in the equity share capital of that body corporate of a class carrying rights to vote in all circumstances at general meetings of that body corporate. Where:

- (a) a company holds a qualifying capital interest in a body corporate; and
- (b) the nominal value of any relevant shares in that body corporate held by that company is equal to twenty per cent or more of the nominal value of all relevant shares in that body corporate

it shall be presumed to hold that interest on the basis and for the purpose of securing a contribution to that company's own activities unless the contrary is shown. For this purpose, "relevant shares" means, in relation to a body corporate, any shares in that body corporate comprised in the equity share capital of that body corporate of a class carrying rights to vote in all circumstances at general meetings of that body corporate.

**"the Retail Prices Index"** means the Retail Prices Index published by the Office for National Statistics each month in respect of all items or, if the said index for the month of November is not published by 31st December next following, such index for such month as the Authority may not later than 7th January next following determine to be appropriate in the circumstances, after such consultation with the Appointee as is reasonably practicable, and in such a case references to the Retail Prices Index shall be construed for the purpose of all subsequent calculations for which the value of the Retail Prices Index for that year is relevant as references to that other index;

**"Review Charging Year"** means the first of the Charging Years in respect of which any Periodic Review is carried out;

**"the Review Notice Date"** means the first day of January which is fifteen months before the first day of the Review Charging Year;

**"Sewerage Infrastructure Charge"** means such a charge as is described in Article 206(2)(b) of the Order;

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**"PE Budget and Regulatory Price Control Period" means the period commencing on 1st April 2010 (the fourth Charging Year) and ending on the day provided by paragraph [5A] of Condition B;**

**"trade effluent"** has the same meaning as in Article 199 of the Order;

**"UK Listing Authority"** means the Financial Services Authority acting in its capacity as the competent authority for the purposes of the Financial Services and Markets Act 2000;

**"Water Service"** means Water Service, an executive agency of the Department for Regional Development, of which the Appointee is the successor company (and references to Water Service include references to the Department for Regional Development acting in its capacity as, or through the agency of, Water Service);

**Deleted: "SBP Period"** means the period of three Charging Years commencing on 1st April 2007;

**"Water Infrastructure Charge"** means such a charge as is described Article 206(2)(a) of the Order;

4. [Not used.]
5. Any notification required or permitted to be given under any Condition shall be given in writing and cognate expressions shall be construed accordingly.
6. Where only one of the Appointments is terminated, so much of the provisions of these Conditions as applies or is relevant exclusively to the Appointment which has been so terminated or to the activities of an undertaker holding an appointment of the kind which has been so terminated shall cease to have effect as from the date on which the termination of that Appointment takes place.
7. The Appointee may refer to the Department for Regional Development for determination by it (having considered any representations by the Authority, the Appointee and any other water undertaker or as the case may be, sewerage undertaker) any question arising as to whether any area, island, premises or installation is, or, as the case may be, are, comprised within the Water Supply Area or as the case may be, the Sewerage Services Area as that expression is defined in Schedule 1 to this instrument.

## Condition B: Charges

### Part I. Explanatory Provisions

#### 1. Introduction

The purposes of this Condition are set out in the following subparagraphs.

- 1.1 To limit the revenue receivable through increases in Standard Charges for the supply of water, the provision of sewerage services and the reception, treatment and disposal of trade effluent in the fourth Charging Year (commencing on 1<sup>st</sup> April 2010) and in subsequent Charging Years.

The limits imposed through this Condition apply in two distinct periods:

- First, in the period commencing on 1st April 2010 (the fourth Charging Year) and ending on the day provided by paragraph [5A] of Condition B, the PE Budget and Regulatory Price Control Period; and
- secondly, in the period commencing on the day provided by paragraph [5A] of Condition B and continuing through any remaining part of the Charging Year in which that day falls and subsequent Charging Years, the Regulatory Price Control Period.

The limits that had been imposed between 1 April 2007 and 31 March 2010 have been removed from this Condition

The weighted average increase in the Charging Years within the PE Budget and Regulatory Price Control Period and the Regulatory Price Control Period is limited to the sum of the movement in the Retail Prices Index, an Adjustment Factor, called K, and a Subsidy Factor, called S. The Subsidy Factor is intended to compensate the Appointee for any revenue shortfall that results from non-payment of any subsidy in respect of customers for whom special provision is made and the payment of which has been taken into account by the Authority in determining the Adjustment Factor.

Changes in metered charges are calculated by reference to actual consumption in respect of a Weighting Year (a financial year of the Appointee). Changes in unmetered charges are calculated by reference to changes in average revenue per chargeable supply calculated on the customer base as at the preceding 1<sup>st</sup> December. Changes are weighted in proportion to the contribution which each type of charge makes to total revenue in the Weighting Year.

These matters are dealt with in Part II under the heading "Maximum Allowable Controlled Revenue and control of Standard Charges."

- 1.2 To provide for Periodic Reviews the Appointed Business to be carried out by the Authority in respect of the following periods:

- (i) 1<sup>st</sup> April 2010 to 31<sup>st</sup> March 2013 (noting that these dates may change);
- (ii) 1<sup>st</sup> April 2013 to 31<sup>st</sup> March 2018 (noting that these dates may change); and
- (iii) thereafter at five yearly intervals,

so that the Authority can determine the Adjustment Factor for the periods referred to in (i) and (ii) above and thereafter whether the Adjustment Factor should be changed in relation to (iii) above.

**Deleted:** limit the revenue receivable by the Appointee in respect of Standard Charges for the supply of water, the provision of sewerage services and the reception, treatment and disposal of trade effluent in the first three Charging Years commencing on 1<sup>st</sup> April 2007 and to

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**Deleted:** will be set initially by the Department for Regional Development on the basis of key data assumptions. This limit on the revenue receivable does not include any subsidy payable to the Appointee by the Department for Regional Development in respect of the phasing-in of charges or to prevent average charges for the supply of water and provision of sewerage services to domestic customers from exceeding a maximum amount determined by the Department. Any variance between certain assumed and outturn figures for key data will result in an adjustment to the limit on revenue receivable in the Charging Year concerned or in subsequent Charging Years

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**Deleted:** within the SBP Period, as the case may be. An estimate of the outturn figure may be used initially where the final outturn figure is not available in time to set prices for a particular Charging Year. In cases where the outturn data is not available in sufficient time to be taken into account for the third Charging Year, any variance between certain assumed and outturn figures will not be taken into account in determining the limit on increases in Standard Charges for the fourth Charging Year or subsequent Charging Years. In each of the

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**Deleted:** Charging Years within the SBP Period, the Department for Regional Development may act to prevent average charges for the supply of water and provision of sewerage services to domestic customers from exceeding a maximum amount determined by the Department provided that any shortfall in the Appointee's revenue that would result from such action is met by the Department.

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Except where expressly provided in this Instrument of Appointment all such reviews will cover periods of five consecutive years. This is dealt with in Part III under the heading "Periodic Reviews."

1.3 To enable the Appointee:

- (1) [Removed]
- (2) to refer to the Authority for determination from time to time the question of (i) modifying the Adjustment Factor as provided during the PE Budget and Regulatory Price Control Period or (ii) modifying the Adjustment Factor (as appropriate) as provided during the Regulatory Price Control Period to allow for Notified Items and Relevant Changes of Circumstance;
- (3) to refer to the Authority for determination at any time the question of (i) modifying the Adjustment Factor as provided during the PE Budget and Regulatory Price Control Period or (ii) modifying the Adjustment Factor (as appropriate) as provided during the Regulatory Price Control Period where circumstances have a substantial adverse effect on the Appointed Business; and
- (4) where notice to terminate either or both of the Appointments has been given, to refer to the Authority for determination the question of what (i) the Adjustment Factor should be in the future, on the assumption that the relevant Appointment or, as the case may be, the Appointments were to continue in force, for the purpose of facilitating consideration of the terms on which a new appointee could accept transfers of property, rights and liabilities from the Appointee, as provided in Article 16(4) of the Order.

These matters are dealt with in Part IV under the heading "Interim Determinations and other reviews."

1.4 To enable the Authority to initiate changes to the Adjustment Factor, to allow for Notified Items and Relevant Changes of Circumstance. This is also dealt with in Part IV.

1.4A To provide for a framework within which the Appointee, the Department for Regional Development or the Authority may refer certain questions relating to the funding of the Appointee for determination by the Authority and the Department for Regional Development during the PE Budget and Regulatory Price Control Period.

1.5 To enable the Appointee to require the Authority to refer to the Competition Commission matters arising out of determinations by the Authority referred to in subparagraphs 1.2, 1.4 and 1.4A and references referred to in subparagraph 1.3. These matters are dealt with in Part V under the heading "References to the Competition Commission and Modification of this Condition."

1.6 To require the Appointee to give Information to the Authority to enable it to make determinations under this Condition. This is dealt with in Part VI under the heading "Provision of Information to the Authority."

2. *Defined Terms which apply for the purpose of all parts of this Condition*

In this Condition:

references to **the Appointed Business** shall be construed as if the Appointed Business included the management and holding by the Appointee of any protected land;

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**Average Charge per Chargeable Supply** means in respect of a specified Unmeasured Basket Item for a specified year, the amount  $\frac{R}{N}$ , where:

$R$  is the annual revenue (exclusive of VAT) which would accrue to the Appointee in respect of the specified Unmeasured Basket Item if all Standard Charges (other than Excluded Charges) made or to be made in respect of that Unmeasured Basket Item in the specified year were applied to all Chargeable Supplies of the Appointee which would have been subject to those Standard Charges as at 1 December preceding the specified year, and

$N$  is the number of Chargeable Supplies as at such 1 December for which the Appointee would have been entitled to make those Standard Charges, provided that, where the specified year is a Prior Year,

- (a) there shall be included in  $N$  the number of any additional Chargeable Supplies which the Appointee would have made as at such 1st December if the Standard Charges to be made in respect of the Unmeasured Basket Item in the relevant Charging Year had applied; and
- (b) there shall be excluded from  $N$  the number of any Chargeable Supplies which the Appointee would not have been entitled to make as at such 1st December if the Standard Charges to be made in respect of the Unmeasured Basket Item in the relevant Charging Year had applied;

**Basket Items** are:

- (1) unmeasured water supply;
- (2) unmeasured sewerage services;
- (3) measured water supply;
- (4) measured sewerage services; and
- (5) reception, treatment and disposal of trade effluent,

where:

- (a) a measured supply or service is one where all or some of the charges for that supply or service are based on measured quantities of volume and an unmeasured supply or service is any other; and
- (b) sewerage services includes sewage treatment and disposal and excludes reception, treatment and disposal of trade effluent;

**Chargeable Supply** means any supply of water or any provision of sewerage services for which charges are payable;

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**Excluded Charges** unless and until otherwise agreed between the Authority and the Appointee, are:

- (1) amounts payable in respect of an unmeasured supply of water by means of stand-pipes or water tanks and in respect of the erection or maintenance of stand-pipes or water tanks;

**Deleted: Domestic Base Allowed Revenue** means, in relation to each of the three successive Charging Years commencing on 1<sup>st</sup> April 2007, the base allowed revenue (exclusive of VAT) attributable to domestic customers as determined by the Department for Regional Development initially on the basis of assumptions as to key data specified (in certain cases) in subparagraph 4.3 and as shown in the relevant table in subparagraph 4.1 or as determined subsequently in accordance with Part IV or V of this Condition;

**Deleted: Domestic Maximum Allowable Controlled Revenue** means, in relation to each of the three successive Charging Years commencing on 1<sup>st</sup> April 2007, the sum calculated in accordance with the formula in subparagraph 4.1;

**Deleted: Domestic Total Controlled Revenue** means, in relation to each of the three successive Charging Years commencing on 1<sup>st</sup> April 2007, the total revenue (exclusive of VAT) receivable by the Appointee in respect of Standard Charges (other than Excluded Charges) attributable to domestic customers together with any grant or subsidy paid to the Appointee by the Department for Regional Development under Article 213(1) of the Order but excluding any grant or subsidy paid to the Appointee by the Department for Regional Development under Article 213(3) or Article 278;

- (2) charges for a supply of water provided by the Appointee under Article 98 of the Order;
- (3) charges for the reception and disposal by the Appointee, or other person specified by the Appointee or, as the case may be, Water Service, of matter delivered to the Appointee or such other person by tanker or similar means;
- (4) charges for unmeasured supplies of water to cattle troughs;
- (5) charges for unmeasured building water supplies;
- (6) amounts payable in respect of an unmeasured supply of water by means of bowzers or water tankers;
- (7) charges for unmeasured supplies of water to farm taps and other agricultural water points; and
- (7A) charges in any Charging Year for supplies of water (or for the provision of sewerage services or for the reception, treatment and disposal of trade effluent) to premises where the premises were supplied in the relevant Weighting Year with not less than such quantity of water as is specified from time to time under Article 14(5)(a) of the Order;

AND, for the avoidance of doubt, but without prejudice to the meaning of Standard Charges in respect of Basket Items, shall also include:

- (8) charges payable for any such connection as is described in Article 206 of the Order; and
- (9) charges for a supply of water in bulk to another water undertaker;

**LIBOR** means the London Inter-Bank Offered Rate for six month deposits in sterling which appears on the display designated as page 3750 on the Dow-Jones telerate monitor (or such other page or service as may replace it for the purpose of displaying London inter-bank offered rates of leading banks for sterling deposits) provided that, if for any reason that rate does not appear or the relevant page is unavailable the Appointee may request each of the banks whose offered rates would have been used for the purposes of the relevant page if the event leading to the application of this proviso had not occurred, to notify to the Appointee its offered quotation to leading banks for sterling deposits for a six month period, and in that event the rate shall be the arithmetic mean (rounded upwards if necessary to the nearest decimal place) on the respective quotations (being not less than two) notified to the Appointee;

**Measured Basket Items** means items (3), (4) and (5) in the definition of Basket Items;

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**Non-volumetric Charge** is a charge which is not based on measured quantities of volume;

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**Deleted: Ministerial Policy Limit** means, in relation to any Charging Year, the maximum amount of Domestic Total Controlled Revenue that is consistent with ensuring that the Appointee's average charges for the supply of water and the provision of sewerage services to domestic customers (taking into account for this purpose any subsidy payable by the Department for Regional Development under Article 213(3) of the Order) do not exceed the average charges for the supply of water and the provision of sewerage services to domestic customers in England and Wales or such other maximum amount of Domestic Total Controlled Revenue as is determined by the Department for Regional Development initially on the basis of the ...

**Deleted: Non-Domestic Base Allowed Revenue** means, in relation to each of the three successive Charging Years commencing on 1<sup>st</sup> April 2007, the base allowed revenue (exclusive of VAT) attributable to non-domestic customers, including in respect of the reception, treatment and disposal of trade effluent, as determined by the Department for Regional Development initially on the basis of the ...

**Deleted: Non-Domestic Maximum Allowable Controlled Revenue** means, in relation to each of the three successive Charging Years commencing on 1<sup>st</sup> April 2007, the sum calculated in accordance with the formula in subparagraph 4.2;

**Deleted: Non-Domestic Total Controlled Revenue** means, in relation to each of the three successive Charging Years commencing on 1<sup>st</sup> April 2007, the total revenue (exclusive of VAT) receivable by the Appointee in respect of Standard Charges (other than Excluded Charges) attributable to non-domestic customers, including in respect of the reception, treatment and disposal of trade effluent, ...

**Deleted: Policy Limit Shortfall** means, in relation to a Charging Year, the difference between the Appointee's Domestic Maximum Allowable Controlled Revenue as determined in accordance with paragraph 4.1 and the maximum amount of Domestic Total Controlled Revenue which the Appointee is entitled to recover if the Department for Regional Development has confirmed that the Ministerial Policy Limit ...

**Deleted: <#>PPP Legacy Contracts** mean:¶  
<#>(a) the contract dated 30 May 2006 between the Department for Regional Development and Dalriada Water Limited in respect of new and upgraded bulk treated water supply schemes for the Ballinrees, Castor Bay, Dunore Point, Forked Bridge and Moyola treatment areas (the "Alpha contract"); ¶ ...

**Deleted: Relevant Bad Debts** means, in relation to a Charging Year, the aggregate of bad debts arising from the non-payment of Standard Charges (other than Excluded Charges) relating to the supply of water or the provision of sewerage services to domestic customers to the extent that it exceeds 5% of Domestic Base Allowed Revenue provided that for the purposes of this definition "bad debts" shall be ...



**Standard Charges** means:

- (1) charges fixed under any such charges scheme as is referred to in Article 201 of the Order;
- (2) charges payable under any such agreement as is referred to in Article 200 of the Order under or for which all the charges payable are in accordance with standard charges published or fixed by the Appointee;
- (3) charges payable where a discharge is made in pursuance of a consent given by the Appointee for the purposes of the Chapter III of Part VI of the Order under or for which all the charges payable are in accordance with standard charges published or fixed by the Appointee;
- (4) charges payable under or by virtue of Article 17(4) or 53 of the 1973 Order and which, by virtue of the Water and Sewerage Services (2006 Order) (Commencement No.1 and Transitional Provisions) Order (Northern Ireland) 2007, continue to be payable on and after the transfer date to the Appointee;
- (5) charges payable under or by virtue of any consent or direction granted or made under Part V of the 1973 Order and which, by virtue of the Water and Sewerage Services (2006 Order) (Commencement No. 1 and Transitional Provisions) Order (Northern Ireland) 2007, continue to be payable on and after the transfer date to the Appointee,

Provided that no part of this definition shall apply to any charge which is for the time being an Excluded Charge by virtue of (7A) of the definition of Excluded Charges.

In this definition references to standard charges published or fixed by the Appointee or Water Service are to such charges, whether published or fixed under a charges scheme or otherwise;

**Termination Notice** means a notice given in accordance with Condition O;

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**Unmeasured Basket Items** means items (1) and (2) in the definition of Basket Items;

**Weighted Average Charges Increase** means the sum calculated as follows:

$$W_t = \sum_i \left( \frac{A_t(i)}{A_{t-1}(i)} \cdot r(i) \right) + \sum_j \left( \frac{B_t(j)}{B_{t-1}(j)} \cdot r(j) \right) - 1$$

where:

$W_t$  is the Weighted Average Charges Increase for the Charging Year;

$i$  is an index identifying the two Unmeasured Basket Items;

$j$  is an index identifying the three Measured Basket Items;

$\sum_i$  requires summation over the two Unmeasured Basket Items;

$\sum_j$  requires summation over the three Measured Basket Items;

**Deleted: <#>Unacceptably Inefficient Costs** means such costs attributable to a PPP Legacy Contract as the Authority has determined have been unacceptably inefficiently incurred by the Appointee (and should not therefore be funded by the Appointee's customers) because (and to the extent that) one or more of the following applies in respect of such costs:¶  
<#>(a) it would be more cost effective to replace the PPP Legacy Contracts with alternative arrangements, taking into account termination and other related costs; and¶  
(b) the Appointee has not taken all appropriate steps consistent with the diligent management and execution of the PPP Legacy Contracts to ensure that it benefits from any cost savings, efficiency gains or similar arrangements to which it is contractually entitled;

$At(i)$  is the Average Charge Per Chargeable Supply in respect of Unmeasured Basket Item  $i$  for the Charging Year;

$At-I(i)$  is the Average Charge Per Chargeable Supply in respect of Unmeasured Basket Item  $i$  for the Prior Year;

$Bt(j)$  is the Weighting Year Revenue in respect of Measured Basket Item  $j$  for the Charging Year

$Bt-I(j)$  is the Weighting Year Revenue in respect of Measured Basket Item  $j$  for the Prior Year; and

$r(i)$  or  $r(j)$  is the revenue (exclusive of VAT) which accrued to the Appointee in the Weighting Year from all Standard Charges other than Excluded Charges (including, in the case of Measured Basket Items, any Non-volumetric Charge) in respect of Unmeasured Basket Item  $i$  or Measured Basket Item  $j$  (as the case may be), divided by the aggregate of such revenues for all five Basket Items;

**Weighting Year** means the financial year of the Appointee ended last before 7 October in the Prior Year; and

**Weighting Year Revenue** means the revenue (exclusive of VAT) which would have accrued to the Appointee in the Weighting Year in respect of the specified Measured Basket Item, if all Standard Charges other than Excluded Charges (including any Non-volumetric Charge) made or to be made in respect of that Measured Basket Item in the Charging Year or, as the case may be, the Prior Year had applied.

3. [Not used.]

Part II. *Maximum Allowable Controlled Revenue and control of Standard Charges*

4. *Maximum Allowable Controlled Revenue*

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5. *The Charges Limit*

5.1 During the PE Budget and Regulatory Price Control Period and the Regulatory Price Control Period, the Appointee shall ensure that the Weighted Average Charges Increase in any Charging Year when expressed as a percentage does not exceed the Charges Limit.

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 $DMACR_n = DBAR_n + DC_n$   
Where:  
 $DMACR_n$  means the Domestic Maximum Allowable Controlled Revenue for the Charging Year  $n$   
 $DBAR_n$  means the Domestic Base Allowed Revenue for the Charging Year  $n$  as shown in the table below or as otherwise determined in accordance with Part IV or V of this Condition  
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**Deleted:** <#>Subject to subparagraph 4.12, the Domestic Correction Factor for a relevant Charging Year shall be an amount equal to the sum calculated by applying the following paragraphs (starting with zero):  
<#>where the actual costs of the PPP Legacy Contracts attributable to domestic customers in respect of any of the three successive Charging Years commencing on 1<sup>st</sup> April 2007 are greater (or less) than the assumed costs of those contracts attributable to domestic customers (as assumed by the Department for Regional Development for the purposes of the initial determination of the Domestic Base

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**Deleted:** In so far as the Appointee has incurred Relevant Bad Debts that exceed 5% of Domestic Base Allowed Revenue (the "Bad Debt Cap") in relation to any of the three successive Charging Years

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**Deleted:** In so far as data in respect of the three successive Charging Years commencing on 1 April 2007 required for the purpose of determining the Domestic Correction Factor or Non-Domestic

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**Deleted:** If the Domestic Total Controlled Revenue or Non-Domestic Total Controlled Revenue for the Charging Year commencing on 1<sup>st</sup> April 2009 is less than or more than, respectively, the Domestic

**Deleted:** <#>In calculating or determining the Domestic Correction Factor or the Non-Domestic Correction Factor for a particular Charging Year, such further amount sha

**Deleted:** T

**Deleted:** (beginning with the Charging Year commencing on 1<sup>st</sup> April 2010)

**Deleted:** 5.1A During the PE Budget and Regulatory Price Control Period, the Appointee shall ensure that the difference between the total revenue it receives in respect of Standard Charges in any

5.2 The Charges Limit is the percentage calculated as  $RPI + K + S$ , where:

RPI is the percentage change (expressed, in the case of an increase, as a positive number, in the case of a decrease, as a negative number and, in the case of no change, as zero) in the Retail Prices Index between that published for the month of November in the immediately preceding Charging Year and that published for the immediately preceding November;

K is the Adjustment Factor

S is the Subsidy Factor

5.3 The Adjustment Factor is, for each of the successive Charging Years commencing on 1<sup>st</sup> April 2010, such number (which may be a different number for any Charging Year and may be a positive or negative number or zero) as shall have been determined under this Condition or, if none, zero;

5.4 If the Weighted Average Charges Increase in any Charging Year is less than the Charges Limit then the Charges Limit for the following Charging Year shall be increased by the amount of such deficiency.

5.5 Subject to subparagraphs 5.6, the Subsidy Factor is:

- (1) for each of the two successive Charging Years commencing on 1<sup>st</sup> April 2010, zero;
- (2) for each of the successive Charging Years commencing on 1<sup>st</sup> April 2012 such number (which may be a positive number or zero but not a negative number) as shall be determined by the Authority on or before 30 April of the preceding Charging Year, and represents the difference (if any) between:
  - (a) the amount which the Department for Regional Development had undertaken to pay under Article 213(1) of the Order in respect of the Charging Year commencing two years before the Charging Year to which the Subsidy Factor relates and which was relied on by the Authority for the purposes of determining the Adjustment Factor for that earlier Charging Year; and
  - (b) the amount in fact paid under Article 213(1) by the Department for Regional Development in respect of that earlier Charging Year

5.6 Where:

- (i) any determination is made by the Authority under subparagraph 5.5 above and the Appointee disputes the determination so made; or
- (ii) in relation to any Charging Year in respect of which the Department for Regional Development had undertaken to pay an amount under Article 213(1) of the Order, the Authority fails to make any determination under subparagraph 5.5 within 1 month of the end of that Charging Year

the Appointee may refer the matter to the Department for Regional Development for re-determination or, as the case may be, determination by it (or any person appointed by it for that purpose), in which event the Subsidy Factor shall be such number (which may be a positive number or zero but not a negative number) as may be determined by the Department for Regional Development to represent the difference (if any) referred to in subparagraph 5.5.

5A.1 The final day of the PE Budget and Regulatory Price Control Period shall be the 31 March 2013 and the Regulatory Price Control Period shall begin on the 1 April 2013 or such other dates as the Authority may notify to the Appointee from time to time for these purposes (following such consultation as the Authority considers appropriate) and this Condition shall be modified by such change (if any) as is necessary in consequence of such notification and which is also so notified by the Authority.

6. *Matters affecting the Charges Limit and the calculation of the Weighted Average Charges Increase*

6.1 Where the Appointee determines:

- (1) to make a material change (other than one which relates solely to the amount of a charge) to the basis on which it makes or calculates any Standard Charge, or Standard Charges taken as a whole (other than Excluded Charges) for the supply of water, the provision of sewerage services or the reception, treatment and disposal of trade effluent;
- (2) to make a material change to the scope of any such scheme, agreement or consent as is referred to in the definition of Standard Charges (insofar as such change relates to charges, other than Excluded Charges, for the supply of water, or the provision of sewerage services or the reception, treatment and disposal of trade effluent); or
- (3) to change the basis on which the Appointee treats supplies of water or provisions of sewerage services as separate supplies or provisions for the purpose of making Standard Charges (other than Excluded Charges) which affects the calculation of Average Charge Per Chargeable Supply

it shall:

- (i) notify the Authority; and
- (ii) furnish to the Authority such explanations and Information relating to such change as the Authority considers requisite or expedient having regard to the purposes of this Condition.

6.2 Where there is a material change to the basis of compiling the Retail Prices Index which affects the Maximum Allowable Controlled Revenue determined under this Condition or which is relevant to the calculation of the Charges Limit, this Condition may be modified in such manner as the Authority, after prior consultation with the Appointee, determines to be appropriate in order to take account of such change.

7. *Verification of Compliance with the Charges Limit*

7.1 Statements

The Appointee shall deliver to the Authority the following statements:

- (1) [Removed]▼  
▼  
▼  
▼
- (2) not later than two months before the start of each Charging Year commencing on or after 1 April 2010 a statement in writing (a **Principal Statement**) of:

**Deleted:** not later than two months before the end of each of the three successive Charging Years commencing on 1 April 2007 a statement in writing (an **Interim Principal Statement**) of:

**Deleted:** <#>the aggregate revenue which accrued in (a) the Prior Year and (b) the first six months of the Charging Year from all Standard Charges, other than Excluded Charges; ¶  
the revenue which accrued in (a) the Prior Year and (b) the first six months of the Charging Year in relation to each and every type or category of charge for the supply of water, the provision of sewerage services or the reception, treatment or disposal of trade effluent which the Appointee imposes of a kind specified in the definition of Standard Charges which are not Excluded Charges (and for this purpose where the Appointee charges different prices per cubic metre of water supplied depending upon the volume of water supplied or the time of supply or the category of customer or any other variable factor then each such price shall be treated as a different type or category of charge);

**Deleted:** <#>an estimate of the expected Domestic Total Controlled Revenue and Non-Domestic Total Controlled Revenue to be accrued in the Charging Year;¶  
<#>an estimate of the revenue which the Appointee expects to accrue in the Charging Year in relation to each and every type or category of charge for the supply of water, the provision of sewerage services or the reception, treatment or disposal of trade effluent which the Appointee imposes of a kind specified in the definition of Standard Charges which are not Excluded Charges (and for this purpose where the Appointee charges different prices per cubic metre of water supplied depending upon the volume of water supplied or the time of supply or the category of customer or any other variable factor then each such price shall be treated as a different type or category of charge);¶  
an estimate of the Domestic Correction Factor and Non-Domestic Correction Factor for the subsequent Charging Year; and

**Deleted:** the amount of each and every type or category of charge for the supply of water, the provision of sewerage services or the reception, treatment or disposal of trade effluent which the Appointee proposes to impose of a kind specified in the definition of Standard Charges as at the commencement of the subsequent Charging Year which are not Excluded Charges (and for this purpose where the Appointee proposes to charge different prices per cubic metre of water supplied depending upon the volume of water supplied or the time of supply or the category of customer or any other variable factor then each such price shall be treated as a different type or category of charge);

- (i) the revenue which accrued in the Weighting Year from all Standard Charges (including, in the case of Measured Basket Items, any Non-volumetric Charge), other than Excluded Charges, in respect of each Unmeasured Basket Item i and each Measured Basket Item j;
  - (ii) the aggregate revenue which accrued in the Weighting Year from all such Standard Charges; and
  - (iii) the amount of each and every type or category of charge for the supply of water, the provision of sewerage services or the reception, treatment or disposal of trade effluent which the Appointee proposes to impose of a kind specified in the definition of **Standard Charges** as at the commencement of that Charging Year which are not Excluded Charges (and for this purpose where the Appointee proposes to charge different prices per cubic metre of water supplied depending upon the volume of water supplied or the time of supply or the category of customer or any other variable factor then each such price shall be treated as a different type or category of charge);
- (3) not later than two months, or such later date as the Authority may allow, before the date during any Charging Year as from which the Appointee proposes to impose or fix a new Standard Charge (which is not an Excluded Charge) for the supply of water or the provision of sewerage services or the reception, treatment or disposal of trade effluent or to increase or decrease the amount of any such charge a statement in writing (a **Supplemental Statement**) of the new charge or the amount by which the Appointee proposes to increase or decrease the amount of that charge.

Any Principal Statement or Supplemental Statement shall be accompanied by the information necessary to calculate At(i) and At-1(i) and Bt(j) and Bt-1(j) in the definition of Weighted Average Charges Increase and a written statement of those calculations.

## 7.2 Auditors Report

Any Principal Statement, shall be accompanied by a report by the Auditors as to whether, in their opinion, the information (if any) included in that Principal Statement under subparagraphs 7.1(2)(i) and (ii) has been properly extracted from the relevant accounting statements prepared and delivered by the Appointee under paragraph 4 of Condition F and from the Appointee's accounting records and such other records of the Appointee as the Auditors consider relevant for the purpose of making their report and as to whether, in their opinion, the calculations delivered by the Appointee with that Principal Statement are in accordance with this Condition and with the Appointees accounting and such other relevant records.

**Deleted:** (including for this purpose an Interim Principal Statement)

## 8. [Removed]

## Part III. Periodic Reviews

## 9. [Removed]

## 10. Periodic Reviews of the Appointed Business at Regular Intervals

10.1 The Appointee shall furnish to the Authority such Information as the Authority may reasonably require to enable it to carry out a Periodic Review for the purpose of determining:

- (i) the Adjustment Factor for each of the three consecutive Charging Years commencing on 1<sup>st</sup> April 2010 or such other number of years as the Authority may notify to the Appointee from

time to time for these purposes (following such consultation as the Authority considers appropriate); and

- (ii) the Adjustment Factor for each of the five consecutive Charging Years commencing on 1<sup>st</sup> April 2013 or such other date as the Authority may notify to the Appointee from time to time for these purposes (following such consultation as the Authority considers appropriate); and
- (iii) in relation to consecutive Charging Years in any successive five-year periods, the question whether the Adjustment Factor should be changed (and if so, what change should be made to it),

in each case having regard to all the circumstances which are relevant in the light of the principles which apply by virtue of Part II of the Order in relation to the Authority's determination, including, without limitation, any change in circumstance which has occurred since the transfer date or last Periodic Review (as appropriate) or which is to occur.

10.2 The Appointee shall furnish to the Authority such Information (including further detail about or explanation of Information previously supplied, whether or not under this subparagraph 10.2) as the Authority may by notice reasonably require to enable it to carry out the Periodic Review.

11. *[Removed]*

12. *Periodic Reviews of the Appointed Business where a Termination Notice has been given*

12.1 Where a Termination Notice has been given by the Department to the Appointee, the Appointee may refer to the Authority for determination by it the question, on the assumption that such a Termination Notice had not been given, of what the Adjustment Factor should be for the ten consecutive Charging Years starting with the Charging Year commencing on 1<sup>st</sup> April last before the Termination Notice is to expire.

12.2 A reference to the Authority under this paragraph 12 shall be made by notice given to the Authority not earlier than 1<sup>st</sup> July and not later than 14<sup>th</sup> July in the Charging Year next but one before that commencing on the said 1<sup>st</sup> April.

13. *Effect of Termination of the Appointments (or either of them) on Periodic Reviews*

Subject to paragraph 12, if the Department for Regional Development shall have served a Termination Notice on the Appointee then this Condition shall have effect as though, in the case of the Appointment in respect of which the Termination Notice has been given, references to a Periodic Review being carried out in respect of an initial three consecutive charging years or subsequently a period of five consecutive Charging Years were references to a Periodic Review being carried out in respect of the relevant Appointment in respect of a period of that number of consecutive Charging Years which is the lesser of:

- (1) In the case of a Termination Notice which is to expire on or before 31 March 2010, three years or in any other case five years; and
- (2) the number of consecutive Charging Years (including that in which the day on which the Termination Notice is to take effect falls) in the period starting on the first day of the first of the Charging Years in respect of which that Periodic Review is to be carried out and ending on the day on which the Termination Notice is to expire.

Part IV . *Interim Determinations and other reviews*

14. *Matters of Interpretation and Construction which apply for the purposes of this Part IV*

14.1 In this Part of this Condition:

**the Appropriate Discount Rate** means such rate of return as, at the time at which the Appropriate Discount Rate falls to be applied from time to time under this Condition, investors and creditors would reasonably expect of a properly managed company holding the Appointments whose sole business consists of being a water undertaker and a sewerage undertaker and, without excluding other considerations which may also be relevant, having its equity share capital admitted to the Official List and to trading on the London Stock Exchange's market for listed securities, and the same Appropriate Discount Rate shall be applied for all purposes in determining questions the subject of the same reference (including questions determined by the Authority under paragraph 16 when it determines questions referred to it by the Appointee under paragraph 15);

**equity share capital** has the same meaning as in the 1986 Order;

**Interim Determination** means the determination by the Authority of the relevant questions the subject of a reference by the Appointee under paragraph 15 or pursuant to paragraph 16 or, as the case may be, the determination by the Competition Commission of the relevant questions or of the disputed determinations the subject of a reference to it pursuant to subparagraph 17(2) or 17(3), which relates to a reference by the Appointee under paragraph 15 or a determination pursuant to paragraph 16;

**making a Relevant Determination** means determining the Adjustment Factor initially or determining, in carrying out the most recent Periodic Review, or making any subsequent Interim Determination (or, where there has been no Periodic Review, in making any Interim Determination) whether the Adjustment Factor should be changed (and if so, what change should be made to the Adjustment Factor), and **Relevant Determination** shall be construed accordingly;

**Net Present Value** means the net present value calculated as at 30 September in the year in which the relevant Reference Notice is given or, where in any year no Reference Notice is given under paragraph 15 but the Authority gives a notice to the Appointee under paragraph 16, as at 30 September in the year in which the Authority gives the notice, by discounting subsequent cash flows and inflating earlier cash flows at the Appropriate Discount Rate, assuming all cash flows in any Charging Year occur on 30 September in that Charging Year;

a **Notified Item** is any item notified by the Authority to the Appointee (or, as the case may be, Water Service) as not having been allowed for (either in full or at all) in making a Relevant Determination; and for the purpose of this definition:

- (a) where any such item was not allowed for in full then it shall only be a Notified Item to the extent that it was not allowed for; and
- (b) where, in determining whether the Adjustment Factor, as the case may be, should be changed (and if so what change should be made to the Adjustment Factor), the Authority, or, as the case may be, the Competition Commission, allows for any such item as was previously so notified by the Authority (or, as the case may be, the Department for Regional Development) then references in this Condition to Notified Items and Relevant Items shall be taken, for the purposes of any subsequent Interim Determination, to exclude such item to the extent that the Authority, or, as the case may be, the Competition Commission, allowed for it as aforesaid;

a **Relevant Change of Circumstance** is any of the following:

- (1) (i) the application to the Appointee of any legal requirement; and

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**Deleted:** Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue or, as the case may be, the

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**Deleted:** (or, in relation to the three successive Charging Years commencing on 1 April 2007, the Department for Regional Development)

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- (ii) any change to any legal requirement which applies to the Appointee (including any legal requirement ceasing to apply, being withdrawn or not being renewed);
- (2) for any Charging Year in respect of which (i) no grant or subsidy is paid to the Appointee under Article 213(3) or 278 of the Order and (ii) the Authority notified Water Service or, as the case may be, the Appointee that variations in value received or expected to be received from Relevant Disposals of Land shall constitute a Relevant Change of Circumstance, either of the following circumstances:
- (a) where for that Charging Year the value received or expected to be received from a Relevant Disposal of any Identified Land is, or is expected to be, different from the value which the Authority notified Water Service or, as the case may be, the Appointee was the value attributable to a Relevant Disposal of that Identified Land for that Charging Year which had been allowed for in making a Relevant Determination; or
- (b) where for that Charging Year, and to the extent not taken into account under (a) above, the aggregate value received or expected to be received from Relevant Disposals of Non-identified Land is, or is expected to be, different from the value which the Authority notified Water Service or, as the case may be, the Appointee was the value attributable to Relevant Disposals of Non-identified Land for that Charging Year which had been allowed for in making a Relevant Determination,
- and so that any notification by the Authority for purposes of this subparagraph (2) shall be relevant for the purposes of this subparagraph (2) to the exclusion of any earlier notification it for the purposes of this subparagraph (2) to the extent that the first-mentioned notification is made in respect of matters in respect of which that earlier notification was made.

For the purposes of this subparagraph (2):

- (i) **"Identified Land"** means any piece or parcel of protected land identified in any such notification referred to in (a) above as is relevant for the time being for the purposes of this subparagraph (2) as being included in that notification;
- (ii) **"land"** includes any interest or right in or over land;
- (iii) **"Non-identified Land"** means any piece or parcel of protected land, not being, or being part of a piece or parcel of protected land identified in any such notification referred to in (a) above as is relevant for the time being for the purposes of this subparagraph (2);
- (iv) **"protected land"** and **"disposal"** have the meanings respectively given to them in Article 2 of the Order;
- (v) a **"Relevant Disposal"** means and includes any disposal by the Appointee;
- (vi) a **"Relevant Disposal of Land"** means and includes a Relevant Disposal of Identified Land and a Relevant Disposal of Non-identified Land;
- (vii) **"value"** includes value of any kind including, without limitation, cash, the value of real or personal property or any interest in such property, the value of any right or benefit (actual or prospective) and the value of any release, in whole or in part, of any obligation or claim, provided that to the extent that any property, right or benefit shall consist of a right to receive cash or any other asset then no value shall be attributed to that property, right or benefit but the cash or other asset the subject thereof shall be included and treated as value received or expected to be received in the Charging Year in which it is received or expected to be received;

**Deleted:** Department for Regional Development (in relation to the three successive Charging Years commencing on 1<sup>st</sup> April 2007), or the

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**Deleted:** Department for Regional Development (in relation to the three successive Charging Years commencing on 1<sup>st</sup> April 2007), or the

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**Deleted:** Department for Regional Development (in relation to the three successive Charging Years commencing on 1<sup>st</sup> April 2007), or the

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**Deleted:** Department for Regional Development or the



- (viii) references to "**value received or expected to be received**" shall be construed so as to include receipts by, and grants to, the Appointee, any Associated Company or any other business in which either the Appointee or any Associated Company has a material direct or indirect interest;
  - (ix) in the case of a right or benefit, but subject to the proviso to (vii) above, value shall be deemed to have been received at the time the right is granted or the benefit arises;
- (3) where:
- (i) in making a Relevant Determination, an amount has been allowed for on account of steps taken or to be taken for the purpose of securing or facilitating compliance with a legal requirement (not being one to comply with which Water Service or the Appointee has determined to make a change to the basis on which it charges customers for water supply or sewerage services) or achieving a service standard adopted or to be adopted by the Appointee; and
  - (ii) in any such case:
    - (A) the Appointee has not taken (by the date by which it was assumed for the purposes of assessing the amount allowed for as aforesaid it would take those steps) any or all of those steps which, for the purpose of assessing the amount allowed for as aforesaid, it was assumed it would take; and
    - (B) as a result, the amount allowed for as aforesaid is substantially greater than the sum of (a) the costs (if any) actually incurred by the Appointee for the relevant purpose specified in (i) above and (b) so much (if any) of that amount as has been otherwise offset by prudent management of the capital programme; and
    - (C) that purpose has not been otherwise achieved;
- (4) where:
- (i) in making a Relevant Determination an amount has been allowed for on account of capital expenditure to be incurred by the Appointee; and
  - (ii) for any Charging Year ended before the making of the relevant reference under paragraph 15, or, as the case may be, the giving of the relevant notice under paragraph 16, the Notified Index is at a different level from that which the Authority last notified the Appointee in connection with a Relevant Determination was the level which it had been assumed would pertain in that same Charging Year in which it was assumed for the purpose of assessing the amount allowed for as aforesaid that capital expenditure would be incurred by the Appointee.

For the purposes of this subparagraph (4) and subparagraph 15.2:

- (A) **the Notified Index** means the index of national construction costs notified by the Authority to the Appointee for the purposes of this condition, or such other index as the Authority, after consultation with the Appointee, determines to be appropriate and reasonable for those purposes as being the index which is to apply for the purposes of the relevant Charging Year;
- (B) where:
  - (x) the Notified Index is not available by 1 September in any year;

- (y) there is a material change to the basis of compiling the Notified Index; or
- (z) the level of the Notified Index is revised after the determination of the questions in respect of a Relevant Change of Circumstance falling within this subparagraph (4),

then the question as to how changes in construction costs in the relevant Charging Year should be allowed for as a Relevant Change of Circumstance shall be determined by the Authority in such a manner as the Authority, after prior consultation with the Appointee, determines to be appropriate and this condition shall be modified accordingly; and

(C) **the Indexed Capital Costs Amount** is the amount found by multiplying A by B, where:

A is the aggregate amount of capital expenditure which, for the purpose of assessing the amount allowed for as described in (i) above, it was assumed would be incurred by the Appointee in the relevant Charging Year; and

B is the percentage difference between the level of the Notified Index for the relevant Charging year and the level notified for that same Charging Year by the Authority, as described in (ii) above;

a **Relevant Item** is any of the following:

- (1) a Relevant Change of Circumstance (other than a Relevant Change of Circumstance falling within subparagraph (2) of the definition);
- (2) a Notified Item; and
- (3) a Relevant Disposal of Land

and references to a Relevant Item are to a Relevant Change of Circumstance (other than a Relevant Change of Circumstance falling within subparagraph (2) of the definition), a Notified Item or a Relevant Disposal of Land as the context may require.

14.2 In the definition of a **Relevant Change of Circumstance** and for the purpose of that definition:

- (1) a **legal requirement** is any of the following:
  - (i) any enactment or subordinate legislation to the extent that it applies to the Appointee in its capacity as a water undertaker or sewerage undertaker (and for this purpose, but without prejudice to the generality of the foregoing, "subordinate legislation" includes any order made under Article 30 of the Order, and any authorisation granted, approval given, or prohibition imposed, by the Department of the Environment under the Water Supply (Water Quality) Regulations (Northern Ireland) 2002;
  - (ii) any regulation made by the Council or the Commission of the European Communities to the extent that it applies to the Appointee in its capacity as a water undertaker or sewerage undertaker, or decision taken by the said Commission which is binding on the Appointee in its capacity as a water undertaker or sewerage undertaker and to the extent that it is so binding;
  - (iii) any licence, consent or authorisation given or to be given by the Department for Regional Development, the Department of the Environment, the Authority or other body of competent jurisdiction to the Appointee, or given to the Department for

Regional Development and transferred to the Appointee by virtue of a transfer scheme made under Article 270 of the Order, for the purpose of carrying on any of the functions of a water undertaker or sewerage undertaker;

- (iv) any undertaking given by the Appointee to, and accepted by, the Department for Regional Development or, as the case may be, the Authority for the purposes of Article 31 of the Order;
- (v) other than any such undertaking as is referred to in (iv), any undertaking given by the Appointee to any enforcement authority, and accepted by that enforcement authority, to take all such steps:
  - (i) as are specified by that enforcement authority to be necessary or appropriate for the Appointee to take for the purpose of securing or facilitating compliance with any legal requirement in relation to which that enforcement authority is the enforcement authority; or
  - (ii) the taking of which is specified by that enforcement authority to be a condition or requirement of granting or renewing any such licence, consent or authorisation as is referred to in (iii) above or agreeing not to withdraw the same;
- (vi) the Conditions of these Appointments; and
- (vii) any interpretation of law, or finding, contained in any judgment given by a court or tribunal of competent jurisdiction in respect of which the period for making an appeal has expired which requires any legal requirement falling within (i) to (vi) above to have effect in a way:
  - (i) different to that in which it previously had effect; or
  - (ii) different to that in which it was taken to have effect:
    - (A) for the purpose of determining the Adjustment Factor; or, as the case may be,
    - (B) in determining whether the Adjustment Factor should be changed (and if so what change should be made to the Adjustment Factor),

but so that nothing in subparagraphs (i) to (vii) above shall apply so as to include:

- (i) any such legal requirement as is referred to in Article 11 or 21 of the Water (Northern Ireland) Order 1999 or in a scheme made under either of those Articles;
- (ii) those Articles or any such scheme,

to the extent in either case that they require the Appointee to pay fees or charges to the relevant enforcement authority; and

- (2) **enforcement authority** means any person or body having jurisdiction to enforce or to take action under or in respect of the relevant legal requirement.

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**Deleted:** Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue or, as the case may be,

**Deleted:** Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue or

- (1) references to costs include references to expenditure and loss of revenue and references to costs being incurred include references to expenditure being made and loss of revenue being suffered;
  - (2) references to receipts include references to receipts, cash or other assets of any sort, whether of a capital or revenue nature and including receipts of grants, contributions, gifts and loans; and
  - (3) without prejudice to subparagraph (1) above, **Operating Expenditure** in subparagraph 15.2(6) includes those items currently so identified in Ofwat's Regulatory Accounting Guidelines 3 and 4 and in the June Return 2006 Reporting Requirement, line 22 in table 21 and line 21 in table 22 or any substitute which the Authority may from time to time specify for the purposes of this Condition. For the avoidance of doubt, depreciation, the write-down/off of assets, the profits/loss on disposal of assets and infrastructure renewals expenditure or charges are excluded.
- 14.4
- (1) For the purposes of subparagraphs 15.2(1) costs, receipts and savings shall be ascertained at the general price level prevailing, or expected to prevail, on 30 September in the year in which the Appointee gives notice under subparagraph 15.1, or the Authority gives notice under paragraph 16.1(1).
  - (2) In subparagraphs 15.2(8) and 15.2(9) and subparagraph (3) below **at Outturn Prices**, in relation to the amount of any Base Cash Flow or depreciation, means that amount as adjusted to take account of the actual or expected cumulative percentage change in the Retail Prices Index from that prevailing, or expected to prevail, on 30 September in the year in which the Appointee gives notice under subparagraph 15.1 or the Authority gives notice under subparagraph 16.1, up to and including that prevailing, or expected to prevail, on 30 September in the year in which the Base Cash Flow or depreciation occurred, or is expected to occur.
  - (3) In subparagraph 15.2(8) **Current Value**, in relation to any Base Cash Flow or depreciation at Outturn Prices, means that amount, as adjusted to take account of the actual or expected cumulative percentage change in the Retail Prices Index from 30 September in the year in which that Base Cash Flow or depreciation occurred or is expected to occur, up to and including 30 September in the relevant year.
- 14.5 For the purpose of Article 20(5)(b) of the Order, the provisions of this Condition, to the extent that they relate to a Relevant Change of Circumstance falling within sub-paragraph (2) of that definition, are provisions of the Appointments which cannot be modified. This subparagraph shall cease to have effect if, but only if, this Condition ceases to contain any provision relating to changes to the Adjustment Factor to allow for Notified Items and Relevant Changes of Circumstance.

#### 14A Application of Part IV

14A.1 Paragraphs 15 and 16 of this Part IV of Condition B shall, save to any extent notified by the Authority to the Appointee from time to time for these purposes (following such consultation as the Authority considers appropriate), have no effect during the PE Budget and Regulatory Price Control Period.

14A.2 Paragraph [14B] of this Part IV of Condition B shall, save to any extent notified by the Authority to the Appointee from time to time for these purposes (following such consultation as the Authority considers appropriate), have no effect during the Regulatory Price Control Period.

#### 14B Reviews during the PE Budget and Regulatory Price Control Period

Deleted: SBP Period or the

14B.1 Subject to subparagraphs [14B.2] and [14B.10] the Appointee may from time to time refer to the Authority and the Department for Regional Development for determination by them (having considered the proposals of the Appointee) the questions set out in subparagraph [14B.6].

14B.2 The Appointee may only make a reference under subparagraph [14B.1] where such a reference relates to a request for an amount of at least the PE Budget and Regulatory Price Control Period Materiality Amount.

14B.3 For the purposes of this paragraph [14B]:

14B.3.1 'PE Budget and Regulatory Price Control Period Materiality Amount' means the amount of £500,000 or more (calculated as provided in subparagraph [14B.3.2]).

14B.3.2 The PE Budget and Regulatory Price Control Period Materiality Amount shall, in any Charging Year within which the Appointee makes a reference under subparagraph [14B.1], be calculated by deducting from the costs reasonably anticipated or reasonably incurred in relation to any particular event or events within that Charging Year, any receipts or savings received, made or reasonably anticipated in the said Charging Year through prudent management action or otherwise.

14B.3.3 whether action constitutes "prudent management action" shall be assessed by the Authority and the Department having regard to, amongst other things, the circumstances which were known or which ought reasonably to have been known to the Appointee at the relevant time.

14B.4 The Department for Regional Development may from time to time refer to the Authority the questions set out in subparagraph [14B.6.3], for determination by the said Department and the Authority together (having considered the proposals of the said Department).

14B.5 The Authority may from time to time refer the questions set out in subparagraph [14B.6.3] for determination by the said Authority and the Department for Regional Development together (having considered the proposals of the said Authority).

14B.6 The questions that the Appointee, the Department for Regional Development or the Authority as the case may be may refer for determination are:

14B.6.1 Whether the event or events that the Appointee has used as the basis of its calculation of the PE Budget and Regulatory Price Control Period Materiality Amount are such as to merit a review under this paragraph;

14B.6.2 Whether the Appointee's calculation of the PE Budget and Regulatory Price Control Period Materiality Amount is accepted by the Authority and the Department for Regional Development and, if not, what alternative amount they would assess; and

14B.6.3 Whether, having regard to any factors which the Authority and the Department for Regional Development consider relevant, they consider it reasonable for the Appointee to receive additional revenue or to be allowed less revenue and, if so, the appropriate amount of and timing for any such increase or reduction in revenue.

14B.7 The Authority and the Department shall consult with such other persons as they consider appropriate as to what determination, if any, it would be reasonable for them to make on the questions set out in subparagraph [14B.6], may agree such processes, factors or guidelines as to their performance of any such consultation and determinations as they consider appropriate and shall notify the Appointee promptly of any such determinations once made.

14B.8 Where the Authority and the Department for Regional Development have determined, under subparagraph [14B.6.3] that it would be reasonable for the Appointee to receive additional revenue or

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**Deleted:** or such other amount as the Authority may notify to the Appointee from time to time for these purposes (following such consultation as the Authority considers appropriate)

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to be allowed less revenue, the Authority shall also determine whether, in light of such determination and having regard to any other factors the Authority considers relevant, it would be reasonable to change the Adjustment Factor already determined for any relevant Charging Year or Years and, if so, what change should be made to the Adjustment Factor for such relevant Charging Year or Years; and shall notify the Appointee promptly of any such determinations once made.

14B.9 In making a determination under subparagraph [14B.8] the Authority shall consult with such persons as it considers appropriate and shall have regard to any processes, factors or guidelines as to its determination of those questions as it considers appropriate including, without limitation, any such processes, factors or guidelines which it has agreed from time to time with the Department for Regional Development.

14B.10 The Appointee shall ensure that when any reference is made under this subparagraph [14B] it shall, by such date as the Authority may specify from time to time, submit to the Authority a statement specifying (i) its calculation of the PE Budget and Regulatory Price Control Period Materiality Amount; (ii) any other information the Authority may specify from time to time; and (iii) any representations it wishes to make in relation to the questions set out in subparagraphs [14B.6].

15. *References to the Authority relating to Notified Items and Relevant Changes of Circumstance and circumstances having a substantial effect on the Appointed Business*

15.1 The Appointee may from time to time refer to the Authority for determination by him (having considered the proposals of the Appointee) the questions set out in subparagraph 15.2 or, as the case may be, subparagraph 15.3. Such reference shall be made by notice given to the Authority, which, in the case of the questions set out in subparagraph 15.2 shall be given in accordance with subparagraph 15.4. For the purposes of subparagraph 15.2 a single reference may be made in respect of any number of Notified Items and Relevant Changes of Circumstance and subparagraph 15.2 shall be construed accordingly.

15.2 In the case of a Notified Item or where there has been or is to be a Relevant Change of Circumstance all of the following:

- (1) what are, or are likely to be, the costs, receipts and savings reasonably attributable to the Relevant Item and also, in the case of a Relevant Change of Circumstance falling within subparagraph (2) of the definition, the costs, receipts and savings reasonably connected with the Relevant Disposal of Land. For this purpose, and without prejudice to the generality of the foregoing:
  - (i) the costs reasonably attributable to a Relevant Change of Circumstance falling within subparagraph (1) of the definition by virtue of the revocation or non-renewal of an existing abstraction licence (or the failure to obtain, following due application by Water Service or the Appointee, an abstraction licence for an existing controlled activity (as defined in Schedule 4 to the Water Abstraction and Impoundment (Licensing) Regulations (Northern Ireland) 2006)) or the grant of a new abstraction licence shall, for the avoidance of doubt, include the costs reasonably incurred by the Appointee, in the light of such revocation, non-renewal or grant, for the purpose of or in connection with developing a new source or exercising the power under Article 215 of the Order to abstract water; and
  - (ii) the costs reasonably attributable to a Relevant Change of Circumstance falling within subparagraph (4) of the definition shall be taken to be equal to the Indexed Capital Costs Amount;
- (2) except in the case of a Relevant Change of Circumstance falling with subparagraph (2) of the definition, to what extent:

- (i) are the costs determined under (1) reasonably recoverable through charges for services provided, functions carried out by, and other activities of, the Appointee in its capacity as a water undertaker or sewerage undertaker which are not Standard Charges for Basket Items (not being Excluded Charges);
- (ii) in the case of receipts and savings (but specifically excluding any receipts from land or property sales), is the Relevant Item relevant to services provided, functions carried out by, and other activities of, the Appointee as a water undertaker or sewerage undertaker which are not Basket Items in respect of which the Appointee makes Standard Charges (not being Excluded Charges),

and where it is determined that such costs are reasonably recoverable as aforesaid or, as the case may be, that the Relevant Item is relevant as aforesaid, either in full or to an extent, then references hereafter to costs, receipts and savings reasonably attributable to a Relevant Item are to those costs, receipts and savings except to that extent;

(3) both of the following:

- (i) what costs reasonably attributable to, or connected with, the Relevant Item as determined under (1) and what timing of incurring of such costs are appropriate and reasonable for the Appointee in all the circumstances to incur and programme, or, as the case may be to have incurred and programmed, by reason of the Relevant Item; and
- (ii) what receipts and savings reasonably attributable to, or connected with, the Relevant Item as determined under (1) and what timing of such receipts and savings are appropriate and reasonable for the Appointee in all the circumstances to achieve and programme or, as the case may be, to have achieved and programmed, by reason of the Relevant Item,

and for the purpose of determining the separate amounts under (i) and (ii), but without prejudice to the generality of the foregoing:

- (i) no account shall be taken of:
  - (A) any trivial amounts;
  - (B) any costs, to the extent that they would have been, or would be, avoided by prudent management action taken since the transfer date (and for this purpose what constitutes "prudent management action" shall be assessed by reference to the circumstances which were known or which ought reasonably to have been known to the Appointee at the relevant time);
  - (C) any savings achieved by management action taken since the transfer date over and above those which would have been achieved by prudent management action (and for this purpose what constitutes "prudent management action" shall be assessed by reference to the circumstances at the relevant time); or
  - (D) any amounts attributable to matters allowed for in making a Relevant Determination, except to such an extent that such amounts otherwise fall to be taken into account as amounts reasonably attributable to, or connected with, the Relevant Item under this subparagraph (3) and subparagraph (1) by virtue of the definition of a Notified Item and a Relevant Change of Circumstance; and

- (ii) in the case of a Relevant Change of Circumstance falling within subparagraph (1) of the definition, regard shall be had to whether either:
- (a) the Department of the Environment or the Department for Regional Development has notified the Authority of any change of policy, concerning any environmental or water-quality standard, which has been made since the Adjustment Factor was last determined; or
  - (b) the Appointee has itself given notice to the Authority of the application to it of, or any change to, any legal requirement, before referring that legal requirement to the Authority under subparagraph 15.1;
- (4) having determined under (3) the separate amounts of costs and of receipts and savings in respect of each Relevant Item, what are the annual cash flows thereof (costs being netted off against the amount of receipts and savings for this purpose) over each Charging year included in the timing determined under (3) (those annual cash flows being hereinafter referred to as the **Base Cash Flows**);
- (5) what is the annual aggregate of:
- (i) one half of the Base Cash Flows in respect of Relevant Changes of Circumstance falling within subparagraph (2) of that definition; and
  - (ii) the Base Cash Flows in respect of all other Relevant Changes of Circumstance and Notified Items,
- in both cases the subject of the notice or notices under subparagraph 15.4 or paragraph 16;
- (6) (a) where any part of an annual aggregate derived under subparagraph (5) consists of items to which (b) below does not apply, what is the Net Present Value of that part of the annual aggregate, calculated up to the start of the first of the Charging Years for which the next Periodic Review falls to be carried out;
- (b) where any part of the annual aggregate derived under subparagraph (5) consists of revenue and/or Operating Expenditure, what is the Net Present Value of that part of the annual aggregate, calculated over 15 years; and
- (c) what is the aggregate of the Net Present Values calculated under (a) and (b) ("**the Materiality Amount**");
- (7) is the Materiality Amount equal to or does it exceed 10% of the turnover attributable to the Appointed Business in the latest financial year for which accounting statements have been prepared and delivered to the Authority under Condition F, as shown by those accounting statements, and for this purpose where the Materiality Amount is a negative figure it shall be treated as though it were a positive figure;
- (8) if so, for each year (the **relevant year**) until the first of the Charging Years for which the next Periodic Review falls to be carried out (having regard to any Review Notice or Reference Notice which has been given at the time when the reference is made),
- (i) what are the following amounts:
    - (i) all Base Cash Flows at Outturn Prices attributable to the creation or acquisition of depreciable assets (**Allowable Capital Expenditure**);

**Deleted:** (or, as the case may be, the Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue)



- (ii) all Base Cash Flows at Outturn Prices (save in respect of Relevant Changes of Circumstances falling within subparagraph (2) of that definition, where one half of the Base Cash Flow at Outturn Prices shall be used) attributable to the creation, acquisition or disposal of non-depreciable assets (**Allowable Infrastructure Asset Expenditure**);
- (iii) all other Base Cash Flows at Outturn Prices (**Other Allowable Expenditure**);
- (iv) the sum of the Current Value of all Allowable Capital Expenditure occurring up to and including the relevant year, divided by the weighted average expected life of the assets attributable to that Allowable Capital Expenditure at the time those assets were or are expected to be created or acquired (**Allowable Depreciation**);
- (v) the sum of the Current Value of all Allowable Capital Expenditure occurring up to and including the relevant year less the sum of the Current Value of all Allowable Depreciation occurring up to and including the relevant year (**Allowable Net Asset Value**);
- (vi) the sum of the Current Value of all Allowable Infrastructure Asset Expenditure occurring up to and including the relevant year (**Allowable Infrastructure Asset Value**);
- (vii) the Appropriate Discount Rate, adjusted so as to exclude any allowance for changes in the Retail Price Index, multiplied by the sum of:
  - A. the Allowable Net Asset Value for the relevant year; and
  - B. the Allowable Infrastructure Asset Value for the relevant year;
 (the **Allowable Return**); and
- (ii) what is the sum of:
  - (i) Other Allowable Expenditure;
  - (ii) Allowable Depreciation; and
  - (iii) the Allowable Return;
 (the **Annual Allowable Amount**);
- (9) what change to:
  - the Adjustment Factor,

over the period until the first of the Charging Years for which the next Periodic Review falls to be carried out (having regard to any Review Notice or Reference Notice which has been given at the time when the reference is made) (the **Relevant Period**) is most likely to allow, or, as the case may be, require, the Appointee to make such charges over the Relevant Period (**Adjusted Charges**), in such a manner as to secure that the increase, or, as the case may be, decrease, in revenue attributable to the making of Adjusted Charges would, in each year of the Relevant Period, be equal to:

**Deleted:** ; or

**Deleted:** where the first of the Charging Years referred to in subparagraph 15.4(1) (in any case where a Reference Notice has been given in respect of subparagraph 15.2) or referred to in subparagraph 16.1(1) (in any other case) is a Charging Year commencing prior to 1 April 2010, the Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue,

- (i) the Annual Allowable Amount for that year; and
- (ii) where Base Cash Flows at Outturn Prices have occurred prior to the first year of the Relevant Period, the amount, which, calculated as a constant annual amount over the Relevant Period, would result in the sum of the Net Present Values of these amounts equalling the sum of the Net Present Values of the Annual Allowable Amounts for each of the years prior to the Relevant Period.

Provided that:

- (a) where costs have been allowed for in determining the Annual Allowable Amount, it shall be assumed that those costs will be financed other than by the proceeds of an issue of equity share capital; and
- (b) the revenue attributable to the making of Adjusted Charges over the Relevant Period shall not result in interest cover which, measured both by its level in any one year and by trends in that level over time, is less than that appropriate to the financial position and performance which investors and creditors would reasonably expect of a properly managed company holding the Appointments, whose sole business consists of being a water and sewerage undertaker and having its equity share capital admitted to the Official List and to trading on the London Stock Exchange's market for listed securities,
- (c) the revenue attributable to the making of Adjusted Charges over the relevant period shall not result in cash flow interest cover which, measured both by its level in any one year and by trends in that level over time, is less than that appropriate to the financial position and performance which creditors would reasonably expect to be sufficient for a properly managed company holding the Appointments, whose sole business consists of being a water and sewerage undertaker, to secure an investment grade credit rating for the company.

In this Condition:

**cash flow interest cover** means the ratio of earnings (revenue less operating expenditure as defined in paragraph 14.3(3) of Condition B) to net interest payable (gross interest payable less interest receivable).

### 15.3 All of the following:

- (1) whether any circumstance (other than a Relevant Change of Circumstance) has occurred which has or will have:
  - (i) a substantial adverse effect on the Appointed Business or on its assets, liabilities, financial position, or profits or losses, not being one which would have been avoided by prudent management action taken since the transfer date; or
  - (ii) a substantial favourable effect on the Appointed Business, or on its assets, liabilities, financial position, or profits or losses, being one which is fortuitous and (ii) not attributable to prudent management action; and
- (2) if so, what change should be made to the Adjustment factor. For this purpose:
  - (i) what constitutes "prudent management action" shall be assessed by reference to the circumstances which were known or which ought reasonably to have been known to the Appointee at the relevant time;

**Deleted:** (or Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue, as the case may be)

- (ii) an effect shall not be regarded as a substantial adverse effect or a substantial favourable effect in any case unless, if the questions set out in subparagraph 15.2 were to be asked in relation to the circumstance giving rise to it, the answer to that in 15.2(7) (taking the reference in it to 10% as a reference to 20%) would be in the affirmative.

15.4 A Reference Notice given to the Authority in respect of subparagraph 15.2 shall contain or be accompanied by reasonable details of the Relevant Item in respect of which the Reference Notice is given and, unless the Authority otherwise consents, shall be given not later than:

- (1) the fifteenth day of September immediately preceding the first of the Charging Years in respect of which the Appointee wishes the change to the Adjustment Factor to take effect; or
- (2) if later, where the Authority has given a notice to the Appointee under subparagraph 16.1 in respect of the same Charging Year, within 14 days from the receipt by the Appointee of that notice.

**Deleted:** or Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue (as to the case may be)

16. *Changes to the Adjustment Factor initiated by the Authority relating to Notified Items and Relevant Changes of Circumstance and circumstances within 15.3(1)(ii)*

**Deleted:** the Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue and/or

16.1 In the case of a Notified Item or where any Relevant Change of Circumstance has occurred or is to occur, the Authority may, having given notice to the Appointee specifying the Notified Item or, as the case may be, the Relevant Change of Circumstance, of its intention so to do not later than:

- (1) the fifteenth day of September immediately preceding the first of the Charging Years in respect of which it proposes the change to the Adjustment Factor to take effect; or
- (2) if later, where the Appointee has given a Reference Notice to the Authority in respect of subparagraph 15.2 and falling within subparagraph 15.4(1) in respect of the same Charging Year, within 14 days from the receipt by the Authority of that Reference Notice,

**Deleted:** Domestic Base Allowed Revenue and Non-Domestic Base Allowed Revenue and/or the

determine the questions set out in subparagraph 15.2 in respect of that Notified Item or, as the case may be, that Relevant Change of Circumstance. A single notice may be given under this subparagraph 16.1 in respect of any number of Notified Items and Relevant Changes of Circumstance and subparagraph 15.2 shall be construed accordingly.

16.2 Where subparagraph 15.4(2) or 16.1(2) applies, the questions set out in (5) to (9) inclusive of subparagraph 15.2 shall be determined in respect of all Notified Items and Relevant Changes of Circumstance in respect of which the Appointee and the Authority have given notice, taken as a whole.

16.3 In the case of subparagraph 15.3, the Authority shall give notice to the Appointee of its intention to determine the questions set out in subparagraph 15.3 (1)(ii) and (2).

#### Part V. *References to the Competition Commission and Modification of this Condition*

#### 17. *References to the Competition Commission*

Where:

- (1) pursuant to paragraph 10 or following a reference under paragraph 12, the Authority has not given notice to the Appointee of its determination within one year from the Review Notice Date or, in the case of a reference under paragraph 12, within one year from the date of the relevant Reference Notice;

- (2) following a reference under paragraph 15, the Authority has not given notice to the Appointee of its determinations (including any determinations under paragraph 16 which fall to be taken into account in determining the questions the subject of the reference under paragraph 15) within three months from the date of the relevant Reference Notice;
- (3) the Appointee disputes any determination made by the Authority under Part III or Part IV of this Condition.

The Appointee may, by notice given to the Authority within:

- (i) 13 months from the Review Notice Date or, in the case of a reference under paragraph 12, from the date of the relevant Reference Notice (in the cases referred to in subparagraph (1));
- (ii) four months from the date of the relevant Reference Notice (in the case referred to in subparagraph (2)); or
- (iii) two months from the date on which the Authority gives notice of its determination to the Appointee (in the cases referred to in subparagraph (3)),

require the Authority to refer to the Competition Commission for determination by it:

- (i) in any case referred to in subparagraph (1) or (2), the relevant question or questions (including, where relevant, the questions in respect of any Notified Item or Relevant Change of Circumstance the subject of a notice under paragraph 16); or
- (ii) in any case referred to in subparagraph (3), the disputed determination.

18. *Modification of this Condition following Periodic Reviews and references to the Authority or the Competition Commission*

18.1 Except in the case of a Periodic Review carried out under paragraph 12, this Condition shall be modified by the change (if any) to the Adjustment Factor (which may be a different number for any Charging Year and may be a positive or negative number, or zero) necessary to give effect to any determination made by the Authority or the Competition Commission under, or, as the case may be, following a reference under Part III, Part IV or Part V of this Condition.

**Deleted:** Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue or the

**Deleted:** in the case of the Adjustment Factor

18.2 Where the Appointee requires the Authority to make a reference to the Competition Commission under paragraph 17 in the case referred to in subparagraph (3) of that paragraph this Condition shall be modified by the change (if any) to the Adjustment Factor necessary to give effect to the Authority's determination but so that subparagraph 18.1 shall then apply to the determination made by the Competition Commission following such reference.

**Deleted:** Domestic Base Allowed Revenue or Non-Domestic Base Allowed Revenue, the

Part VI. *Provision of Information to the Authority*

19.

19.1 The Appointee shall furnish to the Authority:

- (1) [Removed]
- (2) not later than 30<sup>th</sup> September immediately following the date of the Reference Notice (in the case of a reference under paragraph 12);
- (3) at the time when it gives the relevant Reference Notice to the Authority (in the case of a reference under paragraph 15 falling within subparagraph 15.4(1));

- (4) as soon as reasonably practicable and in any event not later than the expiry of one month from the date of the Authority's notice to the Appointee under paragraph 16 (in case of such a notice, including the case of a reference under paragraph 15 falling within sub paragraph 15.4(2)),

such Information as the Appointee reasonably believes is necessary or, as the case may be, as the Authority may reasonably require in its said notice, to enable the Authority to make its determination. The Appointee shall also furnish to the Authority as soon as reasonably practicable such further Information as the Authority may from time to time by notice to the Appointee reasonably require to make its determination.

19.2 The Appointee shall also furnish to the Authority from time to time when so requested by the Authority such Information as the Authority may reasonably require to decide whether or not to make determinations under paragraph 16.

19.3 Any Information furnished to the Authority under this paragraph 19 or under paragraph 10 shall, if the Authority so requires to make its determination, be reported on by a person appointed by the Appointee and approved by the Authority (such approval not to be unreasonably withheld) (the **Reporter**).

19.4 The Appointee shall enter into a written contract of engagement with the Reporter which shall:

- (1) where such a report is required by the Authority under subparagraph 19.3, require the Reporter to prepare and furnish to the Authority, and separately to the Appointee, a written report addressed jointly to the Authority and the Appointee in form and substance such as may be specified by, or consistent with any guidelines specified by, the Authority at the time when it requires the report to be furnished, the matters so specified being reasonably appropriate to enable the Authority to make its determination (to the extent that the Information in respect of which that report is required to be prepared and furnished is relevant to that determination); and
- (2) include a term that the Reporter will provide such further explanation or clarification of his report as the Authority may reasonably require and such further Information in respect of, or verification of, the matters which are the subject of his report as the Authority may reasonably require.

The contract of engagement may also include provisions requiring the Reporter, his employees and agents to keep confidential and not to disclose, except to the Authority or as required by law, any Information which the Reporter obtains in the course of preparing his report.

19.5 The Appointee shall co-operate fully with the Reporter to enable him to prepare his report, including without limitation, so far as is necessary for that purpose:

- (1) subject to reasonable prior notice to the Appointee, giving to the Reporter access at reasonable hours to any Relevant Plant and to any premises occupied by the Appointee in relation to the Appointed Business; and
- (2) subject to reasonable prior notice to the Appointee, allowing the Reporter at reasonable hours:
  - (i) to inspect and make photocopies of, and take extracts from, any books and records of the Appointee maintained in relation to the Appointed Business;
  - (ii) to carry out inspections, measurements and tests on or in relation to any such premises or Relevant Plant; and

- (iii) to take on to such premises or on to or in to any Relevant Plant such other persons and such equipment as may be necessary for the purposes of preparing and completing his report.

19.6 Nothing in subparagraph 19.5 shall require the Appointee:

- (1) to do anything which is outside its reasonable control; or
- (2) to do, or to allow the Reporter to do, anything which would materially disrupt the Appointee's business (unless it is essential that that thing be done to enable the Reporter to prepare his report).

19.7 In subparagraphs 19.4 and 19.5:

- (1) references to the Reporter include references to his employees and agents; and
- (2) **Relevant Plant** means any plant used by the Appointee for the purpose of carrying out the Regulated Activities including, without limitation, water mains, sewers and other pipes and their accessories.

Condition F     Accounts and accounting information

1.                *Introduction*

The purposes of this Condition are to ensure that:

- (1) the financial affairs of the Appointed Business can be assessed and reported on separately from other businesses and activities of the Appointee, as if its sole business consisted of being a water undertaker having its equity share capital admitted to the Official List and to trading on the London Stock Exchange's market for listed securities;
- (2) information on revenues, costs, assets and liabilities attributable to specified activities of the Appointed Business can be provided and reported on;
- (3) transactions between the Appointed Business and any other business or activity of the Appointee or any Associated Company can be assessed and reported on;
- (4) there is no cross-subsidy between the Appointed Business and any other business of the Appointee or between the Appointed Business and any Associated Company;
- (4A) The transfer of assets (including the provision of financial support) to Associated Companies does not adversely affect the Appointee's ability to carry out its functions as a water and sewerage undertaker or to finance those activities;
- (5) the Authority is furnished with regular accounting and other information to enable it to compare the financial position and performance (including, without limitation, costs) of the Appointed Business and of so much of the respective businesses and activities of undertakers holding appointments in England and Wales made under Chapter I of Part II of the Water Act 1989 or in Northern Ireland made under Chapter I of Part III of the Order as consists of the carrying out of the Regulated Activities; and
- (6) the Appointee has at its disposal sufficient financial and managerial resources to carry out the Regulated Activities (including any investment programme necessary to fulfil its obligation under the Appointment(s)).

2.                *Interpretation and Construction*

2.1              In this Condition and for the purposes of this Condition:

references to "**the Appointed Business**" shall be construed as if the Appointed Business included the management and holding by the Appointee of any protected land.

"**infrastructure assets**" means

- (1) Network Assets; and
- (2) all of the following:
  - (a) valves and hydrants forming part of the water and trunk main systems;
  - (b) impounding and pumped raw water storage reservoirs;
  - (c) dams;

- (d) sludge pipe lines; and
- (e) outfall pipes and other pipes for the conveyance of effluent from any sewage disposal works of the Appointee which discharge directly into the sea or coastal waters;

**"infrastructure renewals expenditure"** means expenditure on maintaining or restoring the original operating capability, qualitative performance and condition of infrastructure assets, other than expenditure which is capitalised and routine day to day maintenance expenditure which is charged as an operating cost to the profit and loss account;

**"Network Assets"** means

- (1) in respect of a water undertaker:
  - (a) water mains and trunk mains (other than any pumps, valves and hydrants);
  - (b) resource mains and discharge pipes; and
  - (c) so much of any service pipe as is vested in the water undertaker; and
- (2) in respect of a sewerage undertaker:
  - (a) public sewers (other than any pumps);
  - (b) any outfall pipe or other pipe for the conveyance of effluent from any sewage disposal works of the sewerage undertaker; and
  - (c) any pipe vested in the sewerage undertaker and used for the drainage of one building or of any buildings or yards appurtenant to buildings within the same artilage

but excluding any pipe which discharges directly into the sea or coastal waters

**"PPP contract"** means:

- (i) any long-term arrangements with the Appointee under HM Government's private finance initiative; or
- (ii) broadly equivalent long-term arrangements with the Appointee involving the significant transfer of risk from the Appointee to the counterparty and the provision to the Appointee of capital works, both in relation to the performance by the Appointee of the Regulated Activities,

pursuant to which, in each case, the counterparty provides works (or, as the case may be, such works) whether or not together with facilities or services, which relate to the performance by the Appointee of the Regulated Activities;

**"Principal Services"** means

- (1) water supply; and
- (2) sewerage services,

and references to a Principal Service are to either and each of water supply and sewerage services;

**Deleted:** (including the PPP Legacy Contracts)



"sewerage services" includes sewage treatment and disposal and reception, treatment and disposal of trade effluent.

2.2 Except where otherwise expressly provided, references in this Condition to costs or liabilities shall be construed as including taxation, and references to any profit and loss account shall be construed accordingly.

2.3 For the purposes of this Condition:

- (1) all forms of property shall be assets, whether situated in the United Kingdom or not, including:
  - (a) options, debts and incorporeal property generally; and
  - (b) any currency including sterling;
- (2) references to the supply of a service include references to anything (including the service of any employee) being made available; and
- (3) references to a transfer of an asset or liability include references to a part transfer of an asset or liability and, without limitation, there is a part transfer of an asset where an interest or right in or over the asset is created.

### 3. *Accounting Records*

The Appointee shall keep proper accounting records in a form which enables the revenues, costs, assets and liabilities of, or reasonably attributable to, the respective businesses and activities of the Appointee described in this Condition and the other matters mentioned in this Condition to be separately identified, having regard to the terms of any guidelines notified from time to time by the Authority to the Appointee under paragraph 5, 6, 7, or 8.

### 4. *Accounting Statements*

4.1 The Appointee shall prepare on a consistent basis in respect of each financial year ending after the transfer date accounting statements which shall comprise, and show separately in respect of each of:

- (1) the Appointed Business;
- (2) on an aggregated basis, all businesses and activities of the Appointee other than the Appointed Business; and
- (3) on an aggregated basis, all businesses and activities of the Appointee including the Appointed Business

a profit and loss account, a statement of assets and liabilities and a statement of source and application of funds, together with notes thereto, setting out the revenues, costs (including depreciation, where charged), assets and liabilities thereof, or reasonably attributable thereto.

4.2 Accounting statements prepared under subparagraph 4.1 shall:

- (1) so far as reasonably practicable having regard to the purposes of this Condition, have the same content as the annual accounts of the Appointee prepared under the 1986 Order and be prepared in accordance with the formats and the accounting policies and principles which apply to those accounts; and
- (2) state the principal accounting policies applied.

5. *Segmental Information*

5.1 Accounting statements prepared under paragraph 4 shall show or disclose separately:

- (1) an analysis of total operating costs (excluding interest and taxation) of the Appointed Business showing separately for each Principal Service:
  - (a) manpower costs
  - (b) other costs of employment
  - (c) power
  - (d) local authority rates
  - (e) water charges (including abstraction charges and amounts payable for taking supplies of water in bulk)
  - (f) local authority sewerage agencies
  - (g) materials and consumables
  - (h) hired and contracted services
  - (i) PPP contract costs;
  - (j) charges for bad and doubtful debts
  - (k) depreciation and amortisation (where charged)
  - (l) intangible assets written off
  - (m) infrastructure renewals expenditure
  - (n) exceptional items, and
  - (o) on an aggregated basis, all other operating costs.

The analysis shall include the details reasonably necessary to reconcile the operating costs shown in it with the total operating costs (excluding interest and taxation) of the Appointee shown in the accounting statements prepared under paragraph 4 in respect of the same period;

- (2) an analysis of total turnover of the Appointed Business showing separately turnover attributable to:
  - (a) water supply and, separately on an aggregated basis, sewerage and sewage treatment and disposal (excluding reception, treatment and disposal of trade effluent), distinguishing in each case between the provision of those services on a measured and unmeasured basis respectively;
  - (b) on an aggregated basis, reception, treatment and disposal of trade effluent;
  - (c) grants; and
  - (d) on an aggregated basis, all other sources;

- (3) an analysis of total tangible fixed assets attributable to the Appointed Business showing separately:
- (a) for each of the items included in the annual accounts of the Appointee prepared under the 1986 Order required to be disclosed under section B of Part I of Schedule 4 to the 1986 Order; or
  - (b) for each of the items included in such other analysis of tangible fixed assets by asset type as is disclosed in those annual accounts; and
  - (c) if not separately disclosed in those annual accounts, for infrastructure assets

amounts attributable to each Principal Service, and as a separate category, on an aggregated basis tangible fixed assets which are not attributable to either Principal Service.

The analysis shall include:

- (i) the details reasonably necessary to reconcile the tangible fixed assets shown in it with the tangible fixed assets shown in the analysis prepared under this subparagraph in respect of the immediately preceding financial year (including details of grants);
  - (ii) a statement of any assets which have been re-classified as current assets during the relevant financial year; and
  - (iii) to the extent that information is required to be given in respect of any of the items included in the annual accounts of the Appointee prepared under the 1986 Order referred to in this subparagraph 5.1(3) by virtue of Part III of Schedule 4 to the 1986 Order, the same information in respect of those items. In the case of the first analysis prepared under this subparagraph the reconciliation required to be included under (i) above shall be with the analysis prepared by the Water Service in respect of the financial year ended last before the transfer date; and
- (4) details necessary to reconcile expenditure made or incurred in relation to infrastructure assets with the expenditure made or incurred in relation to Network Assets during the same financial year as shown (in relation to a financial year commencing on or after 1 April 2010) in the statement required to be delivered to the Authority under subparagraph 5.3 of Condition L.

5.2 Accounting statements prepared under paragraph 4 shall show separately for each item relating to sewerage services included in the analyses under subparagraphs 5.1(1) (operating costs) and 5.1(3) (tangible fixed assets) an analysis between amounts which are attributable to sewerage (including reception of trade effluent) and sewage treatment and disposal (including treatment and disposal of trade effluent).

5.3 The Authority may, after consulting with such bodies as are reasonably representative of undertakers holding appointments under Chapter I of Part III of the Order, or if none, the Appointee, from time to time by reasonable notice to the Appointee specify in such guidelines as are reasonable and appropriate for the purpose set out in subparagraph 1(5), variations of:

- (1) the matters required to be shown or disclosed under subparagraph 5.1(1) (but not so as to require separate analyses of matters comprised within any of the items listed in that subparagraph); and
- (2) the items in respect of which the analysis of total fixed assets is to be prepared under subparagraph 5.1(3),

and thereafter the Appointee shall show or disclose information under subparagraph 5.1(1) in respect of those matters or, as the case may be, shall prepare the analysis under subparagraph 5.1(3) in respect of those items, in each case as so varied from time to time.

6. *Transactions entered into by the Appointee or the Appointed Business with or for the benefit of Associated Companies or other businesses or activities of the Appointee*

6.1 The Appointee shall ensure that every transaction between the Appointed Business and any Associated Company (or between the Appointed Business and any other business or activity of the Appointee) is at arm's length, so that neither gives to or receives from the other any cross-subsidy.

6.2 Subject to subparagraphs 6.3 to 6.7, accounting statements prepared under paragraph 4 shall disclose in relation to each transaction of a description specified in the first column of the Appendix to this Condition which took place during the financial year to which those statements relate, the company or, as the case may be, the business or activity which was party to the transaction with the Appointee or, as the case may be, the Appointed Business or which otherwise benefited from the transaction and the information in relation to that transaction specified in the second column of that Appendix.

6.3 Subject to subparagraph 6.4, any amount required to be disclosed in relation to a transaction specified in paragraph 3, 4, 5, or 6 of the Appendix may be aggregated with any amount relating to any other transaction falling within the same paragraph with the same company or other business or activity of the Appointee.

6.4 Subject to subparagraph 6.7, if the amount to be disclosed under subparagraph 6.2 in respect of any single transaction between the Appointee and any Associated Company (or between the Appointed Business and any other business or activity of the Appointee) exceeds 0.5% of the turnover of the Appointed Business, or £100,000, whichever is the greater, then that transaction shall not be aggregated under subparagraph 6.3 and the Appointee shall include in any accounting statement prepared under paragraph 4 the information about that transaction which is specified in the Appendix in relation to a transaction of that kind and which complies with any guidelines issued by the Authority for this purpose.

6.5 The Appointee shall, when submitting accounting statements prepared under paragraph 4 to the Authority, report to it the turnover of any Associated Company with which the Appointed Business has undertaken any transaction of any kind specified in the Appendix.

6.6 Nothing in subparagraph 6.2 shall require the disclosure of any information if the aggregate of any amounts required to be disclosed under paragraphs 3, 4, 5, and 6 of the Appendix relating to transactions with the same company or other business or activity of the Appointee is not material to the Appointed Business as a whole. For the avoidance of doubt, if the aggregate of such amounts is material to the Appointed Business as a whole then information shall be disclosed in accordance with this paragraph and the Appendix in relation to each such transaction (subject always to subparagraph 6.3). For the purpose of this subparagraph the question whether an amount is material to the Appointed Business as a whole shall be determined by the Auditors by reference to whichever is the greater of:

- (1) The book value of the asset or liability the subject of, or affected by, the transaction; and
- (2) The consideration or other charge given, paid or waived.

6.7 Nothing in this paragraph 6 or the Appendix shall require the disclosure of information which relates solely to a transaction wholly unconnected with the Appointed Business.

6.8 The Appointee shall not, in respect of any Charging Year make any payments to any Associated Company in respect of the services rendered to the Appointee by that company, which exceeds:

- (i) such prices in respect of the service in question which the Appointee has ascertained by market testing in accordance with such arrangements as the Authority may have approved for the purpose of this paragraph and as set out in any part of Ofwat's Regulatory Accounting Guideline 5 (Transfer Pricing in the Water and Sewerage Industry) or any substitute which the Authority may from time to time specify for the purposes of this Condition and which is notified to undertakers holding appointments under Chapter I of Part III of the Order, provided that those arrangements have no prejudicial effect upon the proper carrying out of the Appointee's functions or any of them; or
  - (ii) if, in the opinion of the Authority, the Appointee has demonstrated that market testing as described in (i) above is inappropriate, such proportion as the Authority may agree of the Associated Company's costs in providing to the Appointee the service in question (including a reasonable return to the Associated Company).
- 6.9 Without prejudice to paragraphs 6.1 to 6.7 above, the Appointee shall obtain from any Associated Company referred to in paragraph 6.8, such information about the latter's costs as the Authority may reasonably require.
- 6.10 The Appointee shall not, without the consent of the Authority and otherwise than in compliance with its directions concerning the valuation of the asset and the treatment of the consideration in the Appointee's accounts, transfer to any Associated Company to which paragraph 6.8 applies any right or asset to which paragraph 3 of Condition K applies.
- 6.11 (1) The Appointee shall not, without the consent of the Authority:
  - (i) give any guarantee of any liability of any Associated Company; or
  - (ii) make to any such company any loan.
- (1A) The Appointee shall not, without the consent of the Authority, enter into an agreement or incur a commitment incorporating a cross-default obligation.
- (B)(2) For the purposes of this paragraph 6.11:
  - (a) "**liability**" includes the creation of any mortgage, charge, pledge, lien or other form of security or encumbrance, the making of any loan and the undertaking of any other indebtedness;
  - (b) "**loan**" includes the transfer or lending, by any means, of any sum of money or of any rights in respect of that sum; and
  - (c) "**cross-default obligation**" means a term of any agreement or arrangement whereby the Appointee's liability to pay or repay any debt or other sum arises or is increased or accelerated by reason of a default of any person other than the Appointee.
- 6.12 Without prejudice to the application of paragraph 6.2, the Appointee shall declare or pay dividends only in accordance with a dividend policy which has been approved by the board of directors of the Appointee and which complies with the following principles:
  - (i) the dividends declared or paid will not impair the ability of the Appointee to finance the Appointed Business; and
  - (ii) under a system of incentive regulation, dividends would be expected to reward efficiency and the management of economic risk.

### *Ring-Fencing*

- 6A.1 (1) The Appointee shall at all times act in the manner best calculated to ensure that it has adequate:
- (i) financial resources and facilities;
  - (ii) management resources; and
  - (iii) 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 Appointments. The above 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, or carry out works for, the Appointee in its capacity as a Relevant Undertaker.
- (1A) For the purposes of subparagraph (1)(iii) above, the Appointee shall ensure that its systems of planning and internal control comply with such guidance as the Authority may, from time to time, specify in writing for the purposes of this Condition.
- (1B) Paragraph 10 in this Condition F (Reference of disputed matters to the Competition Commission) shall apply to the guidance referred to in subparagraph (1A) above, as it applies to the guidelines mentioned in subparagraph 10.1.
- 6A.2A The Appointee shall, at the same time as it complies with subparagraph 9.3 (submission of Accounting Statements) submit to the Authority a Certificate in the following terms:
- (1) that in the opinion of the directors the Appointee will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the Regulated Activities (including the investment programme necessary to fulfil the Appointee's obligations under the Appointments);
  - (2) that in the opinion of the directors the Appointee will, for at least the next 12 months, have available to it:
    - (i) management resources; and
    - (ii) methods of planning and internal control which are sufficient to enable it to carry out those functions as required by subparagraph (1) in 6A.1 above; and
  - (3) that in the opinion of the directors, all contracts entered into with any Associated Company include all necessary provisions and requirements concerning the standard of service to be supplied to the Appointee, to ensure that it is able to meet all its obligations as a water and a sewerage undertaker.
- 6A.2B (1) The Appointee shall, when it complies with paragraph 6A.2A, submit with each certificate a statement of the main factors which the directors have taken into account in giving that certificate.
- 6A.2B (2) Without prejudice to paragraph 6A.3 below, the directors shall inform the Authority in writing as soon as they become aware of any circumstances which causes them to believe that the most recent certificate under paragraph 6A.2A could not be repeated in the light of that circumstance.

- 6A.3 (1) Whenever the directors become aware that the Appointee or any Group Company is proposing to embark upon any activity which is not one of those described in subparagraph 6A.1 and which may be material in relation to the Appointee's ability to finance the carrying out of the functions mentioned in that subparagraph, they shall as soon as is practicable, having regard to the purposes of this Condition, notify the Authority about that proposal.
- 6A.3 (2) Not later than 14 days after the directors become aware that the Appointee or any Group Company has embarked upon any activity to which subparagraph 6A.3 (1) applies, they shall submit to the Authority a Certificate in the terms specified in subparagraph 6A.2A.
- 6A.4 Each certificate under subparagraph 6A.2A, 6A.2B or 6A.3 shall be either:
- (1) signed by the directors of the Appointee for the time being; or
  - (2) approved by a duly-convened meeting of the board of directors of the Appointee for the time being, signed (in confirmation of that approval) by a director or the secretary of the Appointee and have attached to it a certified copy of an extract of the minutes of the relevant meeting containing the resolution to approve it.
- (3) (a) Each certificate under paragraph 6A.2A, shall be accompanied by a report prepared by the Appointee's Auditors and addressed to the Authority, stating whether they are aware of any inconsistencies between that certificate and either the statements referred to in paragraph 9.3 or any information which the Auditors obtained in the course of their work as the Appointee's Auditors and, if so, what they are.
- (b) Each certificate under paragraph 6A.2A(2) shall be accompanied by a report prepared by the Appointee's Reporter and addressed to the Authority, setting out the Reporter's opinion about the extent to which the Appointee has, during the preceding 12 months complied with its obligation in subparagraph (1)(iii) and paragraph (1A) in 6A.1 of this condition.
- 6A.5A The Appointee shall, at all times, conduct the Appointed Business as if it were substantially the Appointee's sole business and the Appointee were a separate listed public limited company. The Appointee should have particular regard to the following in the application of this Condition:
- (a) the composition of the board of directors of the Appointee should be such that the directors, acting as such, are able to act independently of the parent company or controlling shareholder and exclusively in the interests of the Appointee;
  - (b) the Appointee must ensure that each of its directors must disclose, to the Appointee and the Authority, conflicts between duties of the directors as directors of the Appointee and other duties;
  - (c) where potential conflicts exist between the interests of the Appointee as a water and a sewerage undertaker and those of other Group Companies, the Appointee and its directors must ensure that, in acting as directors of the Appointee, they should have regard exclusively to the interests of the Appointee as a water and a sewerage undertaker;
  - (d) no director of the Appointee should vote on any contract or arrangement in which he has an interest by virtue of other directorships although nothing in this subparagraph shall prevent any director of the Appointee from voting on the declaration, recommendation, payment or making of a dividend or other form of distribution. This arrangement should be reflected in the Articles of Association of the Appointee;
  - (e) the Appointee should inform the Authority without delay when:

- (i) a new director is appointed;
- (ii) the resignation or removal of a director takes effect; or
- (iii) any important change in the functions or executive responsibilities of a director occurs.

The Appointee should notify the Authority of the effective date of the change and, in the case of an appointment, whether the position is executive or non-executive and the nature of any specific function or responsibility;

- (f) the dividend policy adopted by the Appointee and the implications of paragraph 6.12 of this Condition F; and
- (g) the Principles of Good Governance and Code of Best Practice (or any successor document having a similar purposes and content) as may from time to time be incorporated into or approved for the purposes of the Listing Rules of the Financial Services Authority.

6A.5B The Appointee shall, at such times and in such ways as may from time to time be required by the Listing Rules of the Financial Services Authority, publish such information about its annual interim and final results as is by those rules required to be announced by a company whose shares are for the time being admitted to the Official List and to trading on the London Stock Exchange's market for listed securities.

6A.6(1) The Appointee shall ensure that it, or any Associated Company as issuer of corporate debt on its behalf, obtains by 31<sup>st</sup> March 2008 a shadow rating and obtains by 30 June 2009, and thereafter maintains at all times, an issuer credit rating. The Appointee shall have as its objective the obtaining, and maintaining thereafter, of an investment grade rating by 30 June 2009.

6A.6(2) Once an issuer credit rating has been obtained in accordance with paragraph 6A.6(1), the Appointee shall not transfer, lease, license or lend any sum or sums, asset, right or benefit to any Associated Company save in accordance with paragraph 6A.6(3), if:

- (a) the Appointee does not hold an investment grade rating;
- (b) where the Appointee holds more than one issuer credit rating, one or more of the ratings so held is not investment grade; or
- (c) any issuer credit rating held by the licensee is BBB- by Standard & Poor's Ratings Group (or any of its subsidiaries) or Fitch Ratings Ltd or Baa3 by Moody's Investors Service, Inc. (or such higher issuer credit rating as may be specified by any of these credit rating agencies from time to time as the lowest investment grade credit rating), or is an equivalent rating from another reputable credit rating agency which has comparable standing in the United Kingdom and the United States of America and:
  - (i) is on review for possible downgrade; or
  - (ii) is on Credit Watch or Rating Watch with a negative designation;

or, where neither (i) nor (ii) applies:

- (iii) the rating outlook of the Appointee as specified by any credit rating agency referred to in subparagraph (c) which at the relevant time has assigned the lower or lowest investment grade issuer credit rating held by the licensee has been changed from stable or positive to negative.



6A.6(3) Where subparagraph 6A.6(2) applies, the Appointee may not without the prior written consent of the Authority (following disclosure of all material facts) transfer, lease, license or lend any sum or sums, asset, right or benefit to any Associated Company otherwise than by way of:

- (a) payment properly due for any goods, services or assets in relation to commitments entered into prior to the date on which the circumstances described in paragraph 6A.6(2) arise, and which are provided on an arm's length basis and on normal commercial terms;
- (b) a transfer, lease, licence or loan of any sum or sums, asset, right or benefit on an arm's length basis, on normal commercial terms and where the value of the consideration due in respect of the transaction in question is payable wholly in cash and is paid in full when the transaction is entered into;
- (c) repayment of, or payment of interest on, a loan not prohibited by Condition F and which was contracted prior to the date on which the circumstances in paragraph 6A.6(2) arise, provided that such payment is not made earlier than the original due date for payment in accordance with its terms; and
- (d) payments for group corporation tax relief or for the surrender of Advance Corporation Tax calculated on a basis not exceeding the value of the benefit received, provided that the payments are not made before the date on which the amounts of tax thereby relieved would otherwise have been due.

6A.6(4) In this condition:

**"Investment grade rating"** means a stand alone rating not being a shadow rating recognised as investment grade by Standard and Poor's Rating Group (or any of its subsidiaries), by Moody's Investors Services Incorporated (or any of its subsidiaries) or by Fitch Ratings Limited, or any other reputable credit rating agency which has comparable standing in the United Kingdom and the United States of America.

**"Issuer credit rating"** means a credit rating assigned to an issuer of corporate debt by Standard and Poor's Rating Group (or any of its subsidiaries), by Moody's Investors Services Incorporated (or any of its subsidiaries) or by Fitch Ratings Limited, or any other reputable credit rating agency which has comparable standing in the United Kingdom and the United States of America.

**"Shadow rating"** means a credit rating (not being an issuer credit rating) assigned to the Appointee by any reputable financial institution or firm of accountants applying principles, methodology and standards that are analogous to and consistent with those adopted by reputable credit rating agencies.

**"Stand alone rating"** means, in relation to the Appointee, a rating that has been assigned to the Appointee on a basis that disregards the effect of any ownership or guarantee provided by the Department for Regional Development or any other government entity.

## 7. *Basis of allocations and apportionments*

7.1 The analyses of operating costs and tangible fixed assets prepared under subparagraphs 5.1(1) and 5.1(3) and 5.2 shall give a description of the bases of any apportionments or allocations of costs and assets and shall be prepared in accordance with any guidelines which may be issued from time to time by the Authority under subparagraph 7.3.

7.2 Accounting statements prepared under paragraph 4 and, where relevant, the description of transactions prepared under paragraph 6 shall:

- (1) describe the basis of any apportionment or allocation of revenues, costs, assets and liabilities between the Appointed Business and any other business or activity of the Appointee or between the Appointee and any Associated Company;

- (2) specify the nature of the revenues, costs, assets or liabilities which have been so apportioned or allocated; and
- (3) specify between which business, activity or Associated Company the revenues, costs, assets or liabilities have been so apportioned or allocated.

7.3 The Authority may, after consulting such bodies as are reasonably representative of undertakers holding appointments made under Chapter I of Part III of the Order, or if none, the Appointee, from time to time by reasonable notice to the Appointee issue such guidelines as are reasonable and appropriate for the purpose set out in subparagraph 1(5) as to the bases of allocations and apportionments to be adopted in preparing the analyses required under subparagraphs 5.1(1) and 5.1(3) and 5.2 and in making the allocations and apportionments referred to in subparagraph 7.2(1) and thereafter the Appointee shall prepare the analyses and make the allocations and apportionments in accordance with such guidelines as may apply from time to time.

#### 8. *Current Cost Accounting Statements*

8.1 In addition to preparing accounting statements under paragraph 4, the Appointee shall prepare accounting statements, on the current cost basis in respect of the same period in accordance with such guidelines as are reasonable and appropriate for the purposes of this Condition as the Authority may from time to time, after consulting with such bodies as are reasonably representative of undertakers holding appointments made under Chapter I of Part III of the Act, or if none the Appointee, notify to the Appointee for the purposes of this paragraph.

8.2 Guidelines notified by the Authority to the Appointee under subparagraph 8.1 may:

- (1) specify the form and content of current cost accounting statements, including information on specified types of revenue, cost, asset or liability and information on the revenues, costs, assets and liabilities attributable to specified activities, provided that the guidelines may not require the Appointee to disclose information in such current cost accounting statements in respect of items in respect of which the Appointee is not required to give information in accounting statements prepared under paragraph 4 from time to time;
- (2) require any reconciliation that may be required with the annual accounts of the Appointee prepared under the 1986 Order;
- (3) specify the accounting principles and the bases of valuation to be used in preparing current cost accounting statements; and
- (4) specify the nature of the report by the Auditors required to be given in respect of accounting statements.

#### 9. *Audit and publication of Accounting Statements*

9.1 The Appointee shall procure the following reports by the Auditors addressed to the Authority:

- (1) in respect of each set of accounting statements prepared under this Condition, a report stating whether in their opinion:
  - (a) proper accounting records have been kept by the Appointee as required by paragraph 3; and
  - (b) that set of accounting statements (including the information required to be shown or disclosed under paragraphs 5, 6 and 7) is in agreement with the Appointee's accounting records and complies with the relevant paragraphs (including any

relevant guidelines) or, in the case of accounting statements prepared under paragraph 8, complies with the relevant guidelines;

- (2) in respect of each set of accounting statements prepared under paragraph 4, a report stating whether in their opinion that set of accounting statements represents a true and fair view of the revenues, costs, assets and liabilities of, or reasonably attributable to, the business and activities mentioned in paragraph 4; and
- (3) in respect of each set of accounting statements prepared under paragraph 8, a statement of opinion as to such other matters as may be specified in the guidelines applying to those accounting statements.

9.2 The Appointee shall enter into a contract of appointment with the Auditors which shall include a term that the Auditors will provide such further explanation or clarification of their reports, and such further Information in respect of the matters which are the subject of their reports, as the Authority may reasonably require.

9.3 The Appointee shall deliver to the Authority a copy of each set of accounting statements prepared under this Condition and of each report referred to in subparagraph 9.1 as soon as reasonably practicable and in any event not later than 15 July following the end of the financial year to which they relate.

9.4 Accounting statements prepared under this Condition (excluding the information required to be disclosed under subparagraphs 5.1(4) and 5.2, paragraph 6 and subparagraphs 7.1 and 7.2 and any information exempted from this subparagraph from time to time by the Authority by notice to the Appointee), together with the Auditors' reports delivered to the Authority under subparagraph 9.3 in respect of those accounting statements (but excluding any part of any such report to the extent that it relates specifically to any information excluded or exempted from this subparagraph as aforesaid), shall be published with the annual accounts of the Appointee prepared under the 1986 Order or, at the Appointee's option, with the annual accounts of its holding company prepared under the 1986 Order and copies thereof made available upon request to customers.

#### *10. Guidelines and references to the Competition Commission*

10.1 The Appointee may, by notice given to the Authority within one month of the date of any such notice or notification as is referred to in paragraphs 5, 6, 7 and 8, require the Authority to refer to the Competition Commission for determination by it the question whether the guidelines the subject of the relevant notice or notification are appropriate and reasonable for the purposes specified in the relevant paragraph.

10.2 Where the Appointee requires the Authority to make a reference to the Competition Commission under subparagraph 10.1 any guidelines issued by the Authority which are the subject of that reference shall not apply unless and until the Commission determines that they shall apply.

# APPENDIX

COLUMN 1		COLUMN 2	
1.	Any borrowings or sums lent:	1.	The principal of the amount borrowed or lent, the date on which or the dates between which repayment is to be made and the rate of interest payable.
	by or to the Appointed Business to or by any other business or activity of the Appointee; or		
	by or to the Appointee to or by any Associated Company.		
1A	Any dividend paid to any Associated Company.	1A	The basis on which the dividend has been established.
2.	The giving of any guarantee or any other form of security by the Appointee for or in respect of any obligations of any Associated Company.	2.	The form of the guarantee or other security given, the assets, the subject of the security, the amount of the obligation (including where relevant the rate of interest payable) and the date of maturity of the obligation.
3.	The transfer of any asset or liability:	3.	The asset or liability the subject of the transfer, the amount of the consideration for the transfer and the value attributed to the asset or liability in the accounting records kept by the Appointee.
(a)	to or by the Appointee by or to an Associated Company; or		
(b)	to or by the Appointed Business by or to any other business or activity of the Appointee.		
4.	The supply of any service by or to the Appointee to or by an Associated Company or by or to the Appointed Business to or by any other business or activity of the Appointee.	4.	The nature of the service supplied, the terms on which it was supplied and the total charge made for the service.
5.	The omission by the Appointee or any Associated Company to exercise a right as a result of which the value* of the aggregate assets less the aggregate liabilities ( <b>net assets</b> ) of the Appointee is decreased.	5.	The company omitting to exercise the right and the amount by which the value* of the net assets of the Appointee is decreased.
6.	The waiver by the Appointee or the Appointed Business of any consideration,	6.	The amount or the consideration, remuneration of payment waived.

	<i>remuneration or other payment owed to it by any Associated Company or other business or activity of the Appointee.</i>		
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\*For this purpose the value shall be taken to be the value attributed to the relevant items in the accounting records kept by the Appointee or, in case of an interest in land or buildings which is affected by the omission, the open market value of that interest.

