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The Rt Hon Michael Gove MP
Secretary of State for Environment, Food and Rural Affairs
Department for Environment, Food and Rural Affairs
Nobel House
17 Smith Square
London
SW1P 3JR

31st January 2018

Dear Secretary of State,

Thank you for your letter earlier today and your support for our action to improve the financial resilience of the water sector. It's an immense privilege for a company to hold a monopoly public service licence, and this must not be taken lightly. Companies need resilient capital structures to maintain resilient operations and the trust of their customers and the public.

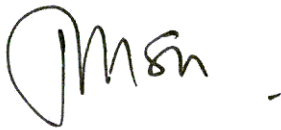
As you note, we have been working to ensure that all companies serve customers' long term interests. It is entirely reasonable, when companies adopt more aggressive structures than customers are paying for, that Ofwat and customers want companies to be transparent about their financing and returns and explain them clearly.

We are pushing companies on a number of fronts, including engaging intensively with the most highly leveraged companies. Starting with our public action in respect of Thames Water last year, I have called on companies which have taken on aggressive financial structures, to demonstrate that they are on a sustainable financial footing.

The forthcoming price review will also require companies to demonstrate that their plans are financially resilient now and over the long term. We are also increasing expectations on companies' corporate governance arrangements and increasing transparency on company returns, with companies to publish a comparison of their actual returns to investors and what those returns would be under the structure we use in setting customers' prices. Highly leveraged companies will have to explain to their customers how the higher returns from their regulated companies look fair.

But as we both recognise, there is more to do to ensure that we have a thriving water sector that can hold the trust and confidence of customers and wider society. I am grateful for your support for our ongoing efforts and help if it is needed. I would suggest that after further work on this, and responses we are expecting from all highly leveraged companies, I will revert to you by early April with an update on progress and our next steps.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Jonson Cox', with a small dash at the end.

Jonson Cox
Chair

Cc Thérèse Coffey, Parliamentary Under Secretary of State for the Environment and Rural Life Opportunities.

Cc Sonia Phippard Director General for Marine, Natural Environment and Rural.