

## DEROGATION LETTER

### IN RESPECT OF INITIAL ENFORCEMENT ORDERS ISSUED PURSUANT TO SECTION 72(2) ENTERPRISE ACT 2002

**Consent under section 72(3C) of the Enterprise Act 2002 to certain actions for the purposes of the Initial Enforcement Order made by the Competition and Markets Authority ('CMA') on 8 January 2024**

### ACQUISITION BY PENNON GROUP PLC OF SUMISHO OSAKA GAS WATER UK LIMITED

We refer to your email of 1 February 2024 requesting that the CMA consents to derogations from the Initial Enforcement Order of 8 January 2024 (the '**Initial Order**'). The terms defined in the Initial Order and any directions issued under the Initial Order have the same meaning in this letter.

Under the Initial Order, save with the written consent of the CMA, Pennon and the Target are required to hold separate the Target business from the Pennon business and refrain from taking any action which might prejudice a reference under section 22 of the Act or impede the taking of any remedial action following such a reference.

After due consideration of your request for derogations from the Initial Order, based on the information received from you and in the particular circumstances of this case, Pennon and the Target may carry out the following actions, in respect of the specific paragraphs:

#### **1. Paragraphs 5(c) and 5(i) of the Initial Order**

On 9 January 2024, the CMA granted Pennon a derogation to allow certain individuals on the board of the Target subsidiaries to resign, and to appoint certain individuals at the Target to fill these positions on a temporary basis (the '**Target Subsidiary Temporary Appointees**'). Pursuant to the derogation, Pennon was required to submit a further derogation request to the CMA by 7 February 2024 to appoint new directors to the boards of the Target subsidiaries to serve in that position for as long as the Initial Order remains in force (the '**Target Subsidiary Confirmed Appointees**'). Following this, the Target Subsidiary Temporary Appointees would resign.

Pennon therefore requests a derogation from paragraphs 5(c) and 5(i) of the Initial Order to allow for: (i) the resignation of the Target Subsidiary Temporary Appointees; and (ii) the appointment of the Target Subsidiary Confirmed Appointees to the positions shown in column 3 of Table 1.

**Table 1: Target Subsidiary Temporary Appointees and Target Subsidiary Confirmed Appointees**

(1) Target Subsidiary	(2) Target Subsidiary Temporary Appointees	(3) Target Subsidiary Confirmed Appointees
Sutton and East Surrey Water Services Limited (02446416)	[REDACTED]	[REDACTED]
	[REDACTED]	[REDACTED]
SES Business Water Limited (10167930)	[REDACTED]	[REDACTED]
	[REDACTED]	[REDACTED]
SES Home Services Limited (10167931)	[REDACTED]	[REDACTED]
	[REDACTED]	[REDACTED]

The CMA consents to Pennon’s request for a derogation on the basis that:

- (a) this derogation will not result in any integration between the Target business and the Pennon business;
- (b) none of the Target Subsidiary Confirmed Appointees is an employee or officer of the Pennon business;
- (c) this derogation will not result in any disruption to, or impact the viability of the Pennon business or the Target business; and
- (d) no other organisational or key staff changes will be made to the Pennon business as a result of the proposed changes.

**2. Paragraphs 5(a), 5(e), 5(g) and 5(l) of the Initial Order**

Pennon submits that the Target has in place insurance coverage in respect of [REDACTED].

Pennon further submits that, under the terms of each of the Target’s insurance policies, the Target is required to notify each insurer of [REDACTED] the Target being acquired by Pennon) and that following such notification each insurer will amend the relevant insurance policy to include Pennon as an additional named insured.

Pennon therefore requests a derogation from paragraphs 5(a), 5(e), 5(g) and 5(l) to allow the Target to notify each insurer of the acquisition of the Target by Pennon and for Pennon to be named as an additional named insured on each of the Target’s

insurance policies which will ensure that Pennon's investment in the Target is protected.

The CMA consents to Pennon's request for a derogation on the basis that:

- (a) this derogation will not result in Pennon having any influence over the commercial or strategic direction of the Target;
- (b) this derogation will not affect any of the insurance premiums that the Target currently has in place;
- (c) Pennon being named as an additional named insured on each of the Target's insurance policies will not be difficult or costly to reverse;
- (d) any information provided to Pennon by the Target business in connection with Pennon being named as an additional named insured on each of the Target's insurance policies is limited to that which is strictly necessary to secure the benefit of each of the Target's insurance policies for Pennon as an additional named insured;
- (e) such information would be shared only with [X] (Pennon's Group Director Risk and Assurance) and [X] (Pennon's Group Insurance Manager) (together the **Insurance Authorised Individuals**) who are representatives of Pennon and are not directly engaged in, nor responsible for making commercial or strategic decisions with regards to the Pennon business. The identity of the Insurance Authorised Individuals cannot be changed except through written consent by the CMA (which can be given via email);
- (f) the Insurance Authorised Individuals must enter into non-disclosure agreements in a form agreed with the CMA, with a view to preventing any information received from the Target business in connection with the insurance process from being shared with any part of Pennon's wider business;
- (g) should remedial action be required by the CMA in relation to the Target business, any records or copies (electronic or otherwise) of business secrets, know-how, commercially-sensitive information, intellectual property or any other information of a confidential or proprietary nature, wherever they may be held, that were received from the Target business for the purposes of this derogation will be returned to the Target business and any copies destroyed, except to the extent that record retention is required by law or regulation;
- (h) all electronic files and emails exchanged in this context will be password protected, adequately ring-fenced, and only accessible to the Insurance Authorised Individuals;

- (i) this derogation will not result in any disruption to, or impact the viability of the Pennon business or the Target business; and
- (j) this derogation will not result in any pre-emptive action which might prejudice the outcome of a reference or impede the taking of any action which may be justified by the CMA's decision on a reference.

### 3. Paragraphs 5(a), 5(c), 5(j) and 5(l) of the Initial Order

Pennon submits that [X] has been re-appointed as auditor of Pennon to hold office until the conclusion of the next annual general meeting at which accounts are laid before Pennon, which is currently scheduled to be held on [X]. Pennon submits that [X] is also currently engaged by the Target to provide tax advisory services.

Pennon further submits that it is a public interest entity (as defined in section 494A of the Companies Act 2006) and that section 5.40 of the Financial Reporting Council's Revised Ethical Standard 2019 requires that an audit firm carrying out statutory audits of public interest entities shall not provide (either directly or indirectly) other services to an audited entity or any of its controlled undertakings. Accordingly, Pennon submits that [X] will be prohibited from providing tax advisory services to the Target. Pennon also submits that appointing a replacement tax advisor would require a tender process that would likely take several months to complete.

Pennon therefore requests a derogation from paragraphs 5(a), 5(c), 5(j) and 5(l) to allow [X] (Pennon's Group Head of Tax), [X] (Pennon's Group VAT Manager), [X] (Pennon's Group Senior Tax Accountant) and [X] (Pennon's Group Tax Trainee) (together the **Tax Services Authorised Individuals**) to provide tax advisory services to the Target.

The CMA consents to Pennon's request for a derogation on the basis that:

- (a) This derogation will not result in Pennon having any influence over the commercial or strategic direction of the Target;
- (b) [X] will be prohibited from providing tax advisory services to the Target and appointing a replacement tax advisor for the Target would require a tender process that would likely take several months to complete;
- (c) any information provided to Pennon by the Target business in connection with the provisions of tax advisory services by the Tax Services Authorised Individuals is limited to that which is strictly necessary to enable the Tax Services Authorised Individuals to effectively provide such services;

- (d) such information would be shared only with the Tax Services Authorised Individuals who are representatives of Pennon and are not directly engaged in, nor responsible for making commercial or strategic decisions with regards to the Pennon business. The identity of the Tax Services Authorised Individuals cannot be changed except through written consent by the CMA (which can be given via email);
- (e) the Tax Services Authorised Individuals must enter into non-disclosure agreements in a form agreed with the CMA, with a view to preventing any information received from the Target business in connection with the provision of tax advisory services from being shared with any part of Pennon's wider business;
- (f) should remedial action be required by the CMA in relation to the Target business, any records or copies (electronic or otherwise) of business secrets, know-how, commercially-sensitive information, intellectual property or any other information of a confidential or proprietary nature, wherever they may be held, that were received from the Target business for the purposes of this derogation will be returned to the Target business and any copies destroyed, except to the extent that record retention is required by law or regulation;
- (g) all electronic files and emails exchanged in this context will be password protected, adequately ring-fenced, and only accessible to the Tax Services Authorised Individuals;
- (h) this derogation will not result in any disruption to, or impact the viability of the Pennon business or the Target business; and
- (i) this derogation will not result in any pre-emptive action which might prejudice the outcome of a reference or impede the taking of any action which may be justified by the CMA's decision on a reference.

Yours sincerely,

Matteo Alchini

Assistant Director, Remedies Business and Financial Analysis

9 February 2024