

Details of proposed VWUK/First Aqua transaction structure

[*Details omitted. See note on page iv.*]

1. The preference shares, which carry no voting rights, [*Details omitted. See note on page iv.*]. FIB, the two [✂] investors, will own approximately [*Details omitted. See note on page iv.*]. VWUK through an SPV (VWUK SPV) will own approximately [✂] per cent of the voting equity, have legal control and hence be able to consolidate the results of Southern. [✂], VWUK will have provided [✂] of the total purchase consideration of £2,081 million (or [✂] per cent). Appendix 3.15 shows the financial structure of JVCo.

Structure of the boards of JVCo and Southern

2. VWUK SPV will have the right to nominate [✂] of the directors on the board of JVCo (including the [*Details omitted. See note on page iv.*]). FIB will have the right to nominate between them [✂] directors (including the [*Details omitted. See note on page iv.*]). The remaining directors will be independent directors to be nominated [*Details omitted. See note on page iv.*]. The board will appoint the directors. [*Details omitted.*
See note on page iv.]

3. The Southern board will be nominated by the parties in the same proportions as the JVCo board, also taking into account Ofwat's new ring-fencing conditions, which First Aqua has agreed to, which require that there be three non-executive directors independent of the controlling shareholder. It is a requirement of Southern's instrument of appointment that the board of Southern act independently from JVCo and exclusively in the interests of Southern.

Preference shareholder rights

4. As indicated in paragraph 3.93, the structure of this deal is predicated on the security of cash flows to FIB, [*Details omitted. See note on page iv.*], to meet interest payments on debt funding. In relation to certain limited issues ('reserved matters') unanimous shareholder consent is required. Article 18 of the JVCo articles of association provides the preference shareholders with a number of rights necessary to protect their financial investment. These include control over any proposal by JVCo to:

- (a) (
- (b) *Details omitted. See note on page iv.*
- (c))
- (d))

Consent of [✂] of the preference shareholders is required in relation to any of these matters.

Agreed Financing Plan

5. Completion of SPA2 is conditional, among other things, on the availability of the AFP, which is intended to be implemented at completion of SPA2. Citicorp and RBS have both been engaged by VWUK to arrange the structured financing. The AFP is intended to refinance debt incurred by JVCo in relation to SPA1. FIB would be funded [*Details omitted*
See note on page iv.]. It is a

highly structured transaction intended to minimize credit risk. [*Details omitted. See note on page iv.*], resulting in a strong credit rating and hence a lower cost of debt. SBIL and its legal advisers are currently formulating an offering memorandum for these securities.

6. Table 1 summarizes the capital structure envisaged by the AFP.

TABLE 1 **Proposed capital structure of JVCo following completion of SPA2**

	Ordinary equity (voting)		Preference equity (non-voting)	Shareholder loan	Total
	£m	%	£m	£m	£m
VWUK Fair Isle Bute	[<i>Figures omitted. See note on page iv.</i>]				

Source: VWUK.

7. SPA2 allows for the possibility that, if the AFP does not come to fruition, SPA2 may be completed by VWUK with different financing or without any external financing. However, the parties to the transaction are required by the cooperation agreement to work together in good faith and use all reasonable means to implement the AFP. VWUK told us that, even if the AFP were not implemented in the form currently envisaged, any alternative structure was also likely to involve a high level of debt and the securitization of Southern's cash flow.

Trigger events

8. There are certain 'trigger events' which provide FIB with certain rights to restrict the financial rights of VWUK. In extreme circumstances of financial underperformance or failure to remedy a trigger event (termed 'material failure of the business plan'), FIB will have the right to appoint additional directors to the board and so gain majority control of the board of JVCo.

Implications of the termination of SPA2

9. [


Details omitted. See note on page iv.

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10. [

Details omitted. See note on page iv.

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11. More likely, in circumstances where SPA2 does not complete, the articles of association of JVCo and the cooperation agreement set out provisions which effectively require First Aqua to put Southern up for sale or conduct a refinancing. JVCo would be required to appoint independent financial advisers ([]) to advise and implement either a refinancing of the group's non-trading debt or a sale of (a) JVCo's ordinary shares (and preference shareholders would be offered the opportunity to sell their preference shares), or (b) equity shares of other members of the group (ie JVCo and its subsidiaries), or (c) all or a material part of the assets of the group. [

Details omitted. See note on page iv.

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