SOUTH EAST WATER CORPORATE GOVERNANCE CODE

Code Objectives

This Code is designed to ensure that South East Water shows continuously high standards of governance and leadership and demonstrates transparently to customers, shareholders, investors, regulators and other stakeholders how this is achieved.

It is an essential part of South East Water's wider corporate governance framework that recognises that "*society is best served by corporations that have aligned their goals to the long-term goals of society*"[1] and the importance for a regulated water company to have an ethical and inclusive culture of public service guided by a strong sense of purpose.

The board wants to maintain South East Water's reputation for high standards of conduct as a dependable provider of an essential public service and this code within our corporate governance framework helps us, and the company as a whole, enhance our corporate governance and demonstrate a genuine concern for all environmental, social and governance matters and our impact on society and the environment.

Our purpose, to "provide today's public water service and create tomorrow's water supply solutions, fairly and responsibly, working with others to help society and the environment to thrive" is centred on our core functions as provider of the public water service and also expresses our ambition to contribute to society and the protection of our environment.

As a board we promote transparency, accountability, ethical conduct, inclusive engagement with customers and stakeholders, a fair balance between the various interests that we and our staff must consider every day and a commitment to high standards of performance in delivering services to customers and protecting the environment.

We have the support of our investors to improve our governance as they recognise that strong environmental, social and governance performance protects the long term value and sustainable success of the company and strengthens our licence to operate.

[1] The Compact for Responsive and Responsible Leadership 2017 - International Business Council of the World Economic Forum

South East Water's principal owners are signatories of the United Nations Principles of Responsible Investment (UN PRI) and are committed to good corporate governance as part of a broader desire to ensuring that South East Water:

- Incorporates Environmental, Social and Governance (ESG) matters into its investment analysis and decision-making processes
- Incorporates the consideration of ESG matters into its policies and practices
- Seeks appropriate disclosure on ESG matters
- Reports on its activities and progress towards implementing improved ESG consideration
- Promotes better ESG consideration, including corporate governance.

We continue to work with our investors and our Responsible Business Committee to improve our corporate governance and reporting to integrate external standards, frameworks and benchmarks.

We are already benchmarking our ESG performance against peers through the GRESB assessment for real estate and infrastructure investments which was adopted by our investors.

We will draw on and integrate into our corporate governance framework and reporting other standards and frameworks including the UN Sustainable Development Goals (SDGs), the principles of integrated reporting, the recommendations of the Task Force on Climate-Related Disclosure (TCFD) and the EU taxonomy.

Corporate Governance Principles

This Code sets out how the board ensures compliance with principles of corporate governance to achieve the Code Objectives. In the context of company law and its Articles of Association, South East Water follows the principles of governance set out in:

- the UK Corporate Governance Code 2018 which can reasonably be applied to a privately owned company;
- the Ofwat's principles of board leadership, transparency and governance; and
- the conditions of its Instrument of Appointment and in particular the obligation to meet the overarching objectives of Ofwat's board leadership, transparency and governance principles

(together the "Corporate Governance Principles")

We also have regard to guidance and other publications issued in relation to the Corporate Governance Principles and to other relevant guidance or best practice publications by regulators and stakeholders.

Compliance Commitments

Under this Corporate Governance Code South East Water will comply with the following provisions:

- In defining and implementing its corporate governance framework the board will seek to achieve optimum compliance with the Corporate Governance Principles.
- Where there is divergence between any of the Corporate Governance Principles the board will explain how it reconciles these differences.
- Where specific conditions of the Company justify following an alternative to a provision the board will seek to achieve an equivalent outcome and explain clearly and carefully how its actual practices are both consistent with the principle to which the particular provision relates and how they contribute to good governance.
- The board will develop and maintain an internal action plan pertaining to all corporate governance matters.
- The board will review the effectiveness of South East Water's corporate governance framework annually and following this review determines what steps are required to ensure that it is in line with developments in corporate governance and best practice. Resulting actions will be implemented and monitored by way of a corporate governance action plan.
- The board will publish South East Water's Corporate Governance Code on its Website.
- The board will regularly review South East Water's practices in relation to reporting and ESG matters to ensure that it complies with the Corporate Governance Principles and this Code Objectives and that it is fair, transparent and accessible.

1 BOARD LEADERSHIP AND COMPANY PURPOSE

1.1 Leadership of the standalone regulated company

A **The company has an effective board with full responsibility for all aspects of the company's business as a regulated company for the long term**. 2.2

1.1.1 There are no matters reserved for shareholders or parent companies. 2.2(i)

1.1.2 Board committees, including but not limited to audit and risk, remuneration and nomination committees, report into the board of the company, with final decisions made at the level of the company. 2.2(ii)

1.1.3 The board of the company is fully focused on the activities of the company; takes action to identify and manage conflicts of interest, including those resulting from significant shareholdings; and ensures that the influence of third parties does not compromise or override independent judgement. 2.2(iii)

1.2 Long term sustainable success

B **A successful company is led by an effective and entrepreneurial board, whose role is to promote the long-term sustainable success of the company, generating value for shareholders and having a positive impact on wider society and the environment.** A

C **The board should ensure that the necessary resources are in place for the company to meet its objectives and measure performance against them. The board should also establish a framework of prudent and effective controls, which enable risk to be assessed and managed.** C

1.2.1 The board should assess the basis on which the company generates and preserves value over the long-term. It should describe in the annual report how opportunities and risks to the future success of the business have been considered and addressed, the sustainability of the company's business model and how its governance contributes to the delivery of its strategy 1

1.2.2 Where directors have concerns about the operation of the board or the management of the company that cannot be resolved, their concerns should be recorded in the board minutes. On resignation, a non-executive director should provide a written statement to the chair, for circulation to the board, if they have any such concerns. 8

1.3 Purpose, values and culture

D **The board establishes the company's purpose, strategy and values, and is satisfied that these and its culture reflect the needs of all those it serves.** 2.1 B

E **All directors must act with integrity, lead by example and promote the desired culture.** B

F **In order for the company to meet its responsibilities to shareholders and stakeholders, the board should ensure effective engagement with, and encourage participation from, these parties.** D

G **The board should ensure that workforce policies and practices are consistent with the company's values and support its long-term sustainable success. The workforce should be able to raise any matters of concern.** E

1.3.1 The board develops and promotes the company's purpose in consultation with a wide range of stakeholders and reflecting its role as a provider of an essential public service. 2.1(i)

1.3.2 The board makes sure that the company's strategy, values and culture are consistent with its purpose. 2.1(ii)

1.3.3 The board monitors and assesses values and culture to satisfy itself that behaviour throughout the business is aligned with the company's purpose. 2.1(iii)

1.3.4 Where it is not satisfied that policy, practices or behaviour throughout the business are aligned with the company's purpose, values and strategy, it takes corrective action. 2 2.1(iii)

1.3.5 The company's annual reporting explains the board's activities and any corrective action taken. It also includes an annual statement from the board focusing on how the company has set its aspirations and performed 2.1(iv) 2 for all those it serves. In addition, it should include an explanation of the company's approach to investing in and rewarding its workforce.

1.3.6 The chair should seek regular engagement with shareholders in order to understand their views on governance and performance against the strategy. Committee chairs should seek engagement with shareholders on significant matters related to their areas of responsibility. The chair should ensure that the board as a whole has a clear understanding of the views of shareholders. 3

1.3.7 The board should understand the views of the company's other key stakeholders and describe in the annual report how their interests and the matters set out in section 172 of the Companies Act 2006 have been considered in board discussions and decision-making. The board should keep engagement mechanisms under review so that they remain effective. For engagement with the workforce, one or a combination of the following methods should be used: 5

- a director appointed from the workforce;
- a formal workforce advisory panel;
- a designated non-executive director.

If the board has not chosen one or more of these methods, it should explain what alternative arrangements are in place and why it considers that they are effective.

1.3.8 There should be a means for the workforce to raise concerns in confidence and – if they wish – anonymously. The board should routinely review this and the reports arising from its operation. It should ensure that arrangements are in place for the proportionate and independent investigation of such matters and for follow-up action. 6

2 DIVISION OF RESPONSIBILITIES AND BOARD COMPOSITION

2.1 Chair

H **The chair leads the board and is responsible for its overall effectiveness in directing the company. They should demonstrate objective judgement throughout their tenure and promote a culture of openness and debate. In addition, the chair facilitates constructive board relations and the effective contribution of all non-executive directors, and ensures that directors receive accurate, timely and clear information.** F

2.1.1 The chair is independent of management and investors on appointment. 2.4(iii)

2.1.2 The chair independence is assessed against the circumstances set out in provision 2.2.4. The roles of chair and chief executive should not be exercised by the same individual. A chief executive should not become chair of the same company. If, exceptionally, this is proposed by the board, shareholders should be consulted ahead of appointment. The board should set out its reasons to all shareholders at the time of the appointment and also publish these on the company website. 9

2.2 Board composition and effectiveness

I **The board of the company and their committees are competent, well run, and have sufficient independent membership, ensuring they can make high quality decisions that address diverse customer and stakeholder needs.** 2.4

J **The board should include an appropriate combination of executive and non-executive (and, in particular, independent non-executive) directors, such that no one individual or small group of individuals dominates the board's decision-making. There should be a clear division of responsibilities between the leadership of the board and the executive leadership of the company's business.** G

K **Non-executive directors should have sufficient time to meet their board responsibilities. They should provide constructive challenge, strategic guidance, offer specialist advice and hold management to account.** H

L **The board, supported by the company secretary, should ensure that it has the policies, processes, information, time and resources it needs in order to function effectively and efficiently** I

2.2.1 Independent non-executive directors are the largest single group on the board. 2.4(ii)

2.2.2 There is a majority of independent non-executive directors on the audit and risk, nomination and remuneration committees and the audit and risk and the remuneration committees are independently led. 2.4(vii)

2.2.3 There is an explicit division of responsibilities between running the board and executive responsibility for running the business. 2.4(iii)

2.2.4 The board should identify in the annual report each non-executive director it considers to be independent. Circumstances which are likely to impair, or could appear to impair, a non-executive director's independence include, but are not limited to, whether a director: 10

• is or has been an employee of the company or group within the last five years;

• has, or has had within the last three years, a material business relationship with the company, either directly or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company;

• has received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option or a performance-related pay scheme, or is a member of the company's pension scheme;

• has close family ties with any of the company's advisers, directors or senior employees;

• holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;

• represents a significant shareholder; or

• has served on the board for more than nine years from the date of their first appointment.

Where any of these or other relevant circumstances apply, and the board nonetheless considers that the non-executive director is independent, a clear explanation should be provided.

2.2.5 Non-executive directors have a prime role in appointing and removing executive directors. Non-executive directors should scrutinise and hold to account the performance of management and individual executive directors against agreed performance objectives. The chair should hold meetings with the non-executive directors without the executive directors present. **13**

2.2.6 The responsibilities of the chair, chief executive, board and committees should be clear, set out in writing, agreed by the board and made publicly available. **14**

2.2.7 The annual report includes details of board and committee membership, number of times met, attendance at each meeting and where relevant, the outcome of votes cast. **2.3(iv)**

2.2.8 All directors should have access to the advice of the company secretary, who is responsible for advising the board on all governance matters. Both the appointment and removal of the company secretary should be a matter for the whole board. **16**

3 APPOINTMENT, SUCCESSION AND EVALUATION

3.1 Appointment and succession

M **Appointments to the board should be subject to a formal, rigorous and transparent procedure, and an effective succession plan should be maintained for board and senior management. Both appointments and succession plans should be based on merit and objective criteria and, within this context, should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths.** J

N **The board and its committees have the appropriate balance of skills, experience, independence and knowledge of the company. Consideration should be given to the length of service of the board as a whole and membership regularly refreshed.** K 2.4(i)

3.1.1 There is a formal, rigorous and transparent procedure for new appointments which is led by the nomination committee and supports the overarching objective that the board of the company and their committees are competent, well run, and have sufficient independent membership, ensuring they can make high quality decisions that address diverse customer and stakeholder needs. 2.4(v)

3.1.2 To ensure there is a clear understanding of the responsibilities attached to being a non-executive director in this sector, companies arrange for the proposed, final candidate for new non-executive appointments to the company board to meet Ofwat ahead of a formal appointment being made. 2.4(vi)

3.1.3 When making new appointments, the board should take into account other demands on directors' time. Prior to appointment, significant commitments should be disclosed with an indication of the time involved. Additional external appointments should not be undertaken without prior approval of the board, with the reasons for permitting significant appointments explained in the annual report. Full-time executive directors should not take on more than one non-executive directorship or other significant appointment. 15

3.1.4 The board should establish a nomination committee to lead the process for appointments and to ensure plans are in place for orderly succession to the board. The chair of the board should not chair the committee when it is dealing with the appointment of their successor. 17

3.1.5 The chair should not remain in post beyond nine years from the date of their first appointment to the board. To facilitate effective succession planning and the development of a diverse board, this period can be extended for a limited time, particularly in those cases where the chair was an existing non-executive director on appointment. A clear explanation should be provided. 19

3.1.6 Open advertising and/or an external search consultancy should generally be used for the appointment of the chair and non-executive directors. If an external search consultancy is engaged it should be identified in the annual report alongside a statement about any other connection it has with the company or individual directors. 20

3.1.7 The board identifies what customer and stakeholder expertise is needed in the boardroom and how this need is addressed. 2.4(i)

3.1.8 The board leads the process to ensure plans are in place for orderly succession to senior management positions, and to oversee the development of a diverse pipeline for succession.

3.1.9 The annual report should describe the work of the board, including:

• the policy on diversity and inclusion, its objectives and linkage to company strategy, how it has been implemented and progress on achieving the objectives; and

• the gender balance of those in the senior management and their direct reports.

3.2 Board evaluation and nomination committee reporting

O **Annual evaluation of the board should consider its composition, diversity and how effectively members work together to achieve objectives. Individual evaluation should demonstrate whether each director continues to contribute effectively.** L

3.2.1 There is an annual evaluation of the performance of the board, its committees, the chair and individual directors. This considers the balance of skills, experience, independence and knowledge, its diversity, how effectively members work together to achieve objectives, how stakeholder needs are addressed and how the overarching objectives set out in Ofwat's 2.4(iv) 21 board leadership, transparency and governance principles and the principles set out in the SEW Code are met.

3.2.2 The evaluation of the performance of the board and its committees is usually conducted via a non-attributable questionnaire with the results collated by the Company Secretary and discussed by the board. The chair should have an individual discussion with each director to discuss their performance and any development needs. The non-executive directors will be responsible for performance evaluation of the chair, taking into account the views of executive directors.

3.2.3 The chair should act on the results of the evaluation by recognising the strengths and addressing any weaknesses of the board. Each director should engage with the process and take appropriate action when development needs have been identified. **22** **2.4(iv)**

The approach is reported in the annual report and any weaknesses are acted on and explained.

3.2.4 The annual report should describe the work of the nomination committee, including: **23**

• the process used in relation to appointments and its approach to succession planning; and

• how the board evaluation has been conducted, the outcomes and actions taken, and how it has or will influence board composition.

4 AUDIT, RISK AND INTERNAL CONTROL

4.1 Audit and risk committee

P **The board should establish formal and transparent policies and procedures to ensure the independence and effectiveness of internal and external audit functions and satisfy itself on the integrity of financial and narrative statements.** M

4.1.1 The board should establish an audit and risk committee. The chair of the board should not be a member. The board should satisfy itself that at least one member has recent and relevant financial experience. The committee as a whole shall have competence relevant to the sector in which the company operates. 24

4.1.2 The main roles and responsibilities of the audit and risk committee should include: 25

- monitoring the integrity of the financial statements of the company and any formal announcements relating to the company's financial performance, and reviewing significant financial reporting judgements contained in them;
- providing advice (where requested by the board) on whether the annual report and accounts, taken as a whole, is fair, balanced and understandable, and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy;
- reviewing the company's internal financial controls and internal control and risk management systems;
- monitoring and reviewing the effectiveness of the company's internal audit function or, where there is not one, considering annually whether there is a need for one and making a recommendation to the board;
- conducting the tender process and making recommendations to the board, about the appointment, reappointment and removal of the external auditor, and approving the remuneration and terms of engagement of the external auditor;
- reviewing and monitoring the external auditor's independence and objectivity;
- reviewing the effectiveness of the external audit process, taking into consideration relevant UK professional and regulatory requirements;

• developing and implementing policy on the engagement of the external auditor to supply non-audit services, ensuring there is prior approval of non-audit services, considering the impact this may have on independence, taking into account the relevant regulations and ethical guidance in this regard, and reporting to the board on any improvement or action required; and

• reporting to the board on how it has discharged its responsibilities.

4.1.3 The annual report should describe the work of the audit and risk committee, including: 26

• the significant issues that the audit and risk committee considered relating to the financial statements, and how these issues were addressed;

• an explanation of how it has assessed the independence and effectiveness of the external audit process and the approach taken to the appointment or reappointment of the external auditor, information on the length of tenure of the current audit firm, when a tender was last conducted and advance notice of any retendering plans;

• in the case of a board not accepting the audit and risk committee's recommendation on the external auditor appointment, reappointment or removal, a statement from the audit and risk committee explaining its recommendation and the reasons why the board has taken a different position (this should also be supplied in any papers recommending appointment or reappointment);

• where there is no internal audit function, an explanation for the absence, how internal assurance is achieved, and how this affects the work of external audit; and

• an explanation of how auditor independence and objectivity are safeguarded, if the external auditor provides non-audit services.

4.2 Transparency and reporting

Q **The board of the company's leadership and approach to transparency and governance engenders trust in the company and ensures accountability for their actions.** 2.3

R **The board should present a fair, balanced and understandable assessment of the company's position and prospects.** N

4.2.1 The directors should explain in the annual report their responsibility for preparing the annual report and accounts, and state that they consider the annual report and accounts, taken as a whole, is fair, balanced and understandable, and provides the information necessary for shareholders 27 to assess the company's position, performance, business model and strategy.

4.2.2 The company publishes the following information in a form and level of detail that is accessible and clear for customers and stakeholders: 2.3(i)(ii)

i. An explanation of its group structure;

ii. An explanation of dividend policies and dividends paid, and how these take account of delivery for customers and other obligations (including to employees)

4.3 Risk Management and internal controls

S **The board should establish procedures to manage risk, oversee the internal control framework, and determine the nature and extent of the principal risks the company is willing to take in order to achieve its long-term strategic objectives.** O

4.3.1 The board should carry out a robust assessment of the company's emerging and principal risks. The board should confirm in the annual report that it has completed this assessment, including a description of its principal risks, what procedures are in place to identify emerging risks, and an explanation of how these are being managed or mitigated. The board also includes an explanation of the principal risks to the future success of the business, and how these risks have been considered and addressed in a form and level of detail that is accessible and clear for customers and stakeholders. 28 2.3(iii)

4.3.2 The board should monitor the company's risk management and internal control systems and, at least annually, carry out a review of their effectiveness and report on that review in the annual report. The monitoring and review should cover all material controls, including financial, operational and compliance controls. 29

4.3.3 In annual and half-yearly financial statements, the board should state whether it considers it appropriate to adopt the going concern basis of accounting in preparing them, and identify any material uncertainties to the company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements. 30

4.3.4 Taking account of the company's current position and principal risks, the board should explain in the annual report how it has assessed the prospects of the company, over what period it has done so and why it considers that period to be appropriate. The board should state whether it has a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary. 31

5 REMUNERATION

5.1 Remuneration policy

T **Remuneration policies and practices should be designed to support strategy and promote long-term sustainable success. Executive remuneration should be aligned to company purpose and values, and be clearly linked to the successful delivery of the company's long-term strategy.** P

U **Directors should exercise independent judgement and discretion when authorising remuneration outcomes, taking account of company and individual performance, and wider circumstances.** R

5.1.1 Remuneration schemes and policies should enable the use of discretion to override formulaic outcomes. They should also include provisions that would enable the company to recover and/or withhold sums and specify the circumstances in which it would be appropriate to do so. 37

5.1.2 Only basic salary should be pensionable. The pension contribution rates for executive directors, or payments in lieu, should be aligned with those available to the workforce. The pension consequences and associated costs of basic salary increases and any other changes in pensionable remuneration, or contribution rates, particularly for directors close to retirement, should be carefully considered when compared with workforce arrangements. 38

5.1.3 Notice or contract periods should be one year or less. If it is necessary to offer longer periods to new directors recruited from outside the company, such periods should reduce to one year or less after the initial period. The remuneration committee should ensure compensation commitments in directors' terms of appointment do not reward poor performance. They should be robust in reducing compensation to reflect departing directors' obligations to mitigate loss. 39

5.1.4 When determining executive director remuneration policy and practices, the remuneration committee should address the following: 40

• clarity – remuneration arrangements should be transparent and promote effective engagement with shareholders and the workforce;

• simplicity – remuneration structures should avoid complexity and their rationale and operation should be easy to understand;

• risk – remuneration arrangements should ensure reputational and other risks from excessive rewards, and behavioural risks that can arise from target-based incentive plans, are identified and mitigated;

• predictability – the range of possible values of rewards to individual directors and any other limits or discretions should be identified and explained at the time of approving the policy;

• proportionality – the link between individual awards, the delivery of strategy and the long-term performance of the company should be clear. Outcomes should not reward poor performance; and

• alignment to culture – incentive schemes should drive behaviours consistent with company purpose, values and strategy.

5.1.5 The remuneration of non-executive directors should be determined in accordance with the Articles of Association or, alternatively, by the board. Levels of remuneration for the chair and all non-executive directors should reflect the time commitment and responsibilities of the role. Remuneration for all non-executive directors should not include share options or other performance-related elements. 34

5.2 Remuneration committee

V **A formal and transparent procedure for developing policy on executive remuneration and determining director and senior management remuneration should be established. No director should be involved in deciding their own remuneration outcome.** Q

5.2.1 The board should establish a remuneration committee. In addition, the chair of the board can only be a member if they were independent on appointment and cannot chair the committee. Before appointment as chair of the remuneration committee, the appointee should have served on a remuneration committee for at least 12 months. 32

5.2.2 The remuneration committee should have delegated responsibility for determining the policy for executive director remuneration and setting remuneration for the chair, executive directors and senior management. It should review workforce remuneration and related policies and the alignment of incentives and rewards with culture, taking these into account when setting the policy for executive director remuneration. 33

5.2.3 Where a remuneration consultant is appointed, this should be the responsibility of the remuneration committee. The consultant should be identified in the annual report alongside a statement about any other connection it has with the company or individual directors. Independent judgement should be exercised when evaluating the advice of external third parties and when receiving views from executive directors and senior management. 35

5.2.4 There should be a description of the work of the remuneration committee in the annual report, including: 41

- an explanation of the strategic rationale for executive directors' remuneration policies, structures and any performance metrics;
- reasons why the remuneration is appropriate using internal and external measures, including pay ratios and pay gaps;
- a description, with examples, of how the remuneration committee has addressed the factors in 5.1.4;
- whether the remuneration policy operated as intended in terms of company performance and quantum, and, if not, what changes are necessary;
- what engagement has taken place with shareholders and the impact this has had on remuneration policy and outcomes;
- what engagement with the workforce has taken place to explain how executive remuneration aligns with wider company pay policy; and
- to what extent discretion has been applied to remuneration outcomes and the reasons why.

5.2.5 The company publishes the following information in a form and level of detail that is accessible and clear for customers and stakeholders: 2.3(v)

- An explanation of the company's executive pay policy and how the criteria for awarding short and long-term performance related elements are substantially linked to stretching delivery for customers and are rigorously applied. Where directors' responsibilities are substantially focused on the regulated company and they receive remuneration for these responsibilities from elsewhere in the group, policies relating to this pay are fully disclosed at the regulated company level.