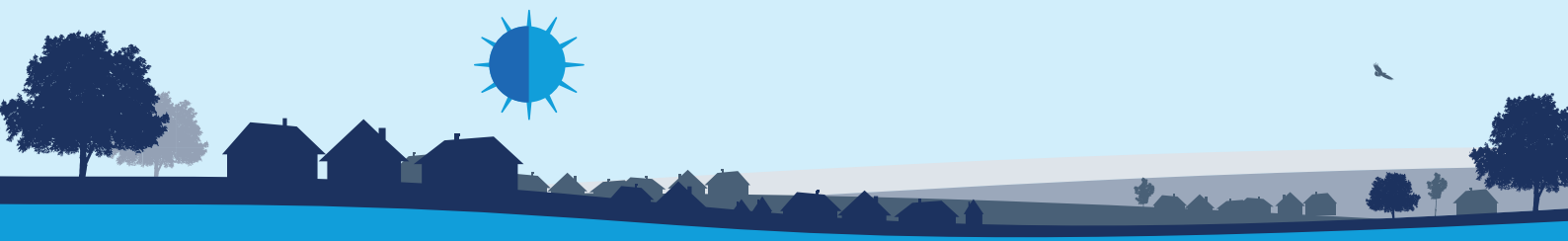




South Staffs Water



South Staffs Water

Annual Report and Accounts
together with the
Annual Performance Report

Year Ended 31 March 2018

Company Registration No: 2662742



Highlights



Strong response to the March Freeze/Thaw Incident

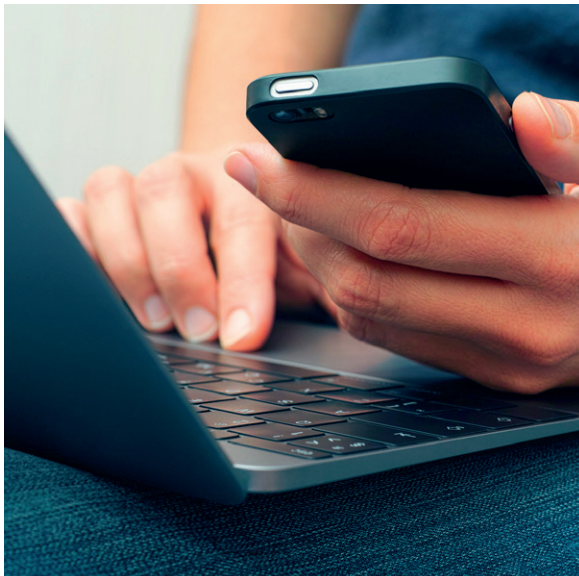
Successful completion of new Outwoods reservoir



A step change in customer engagement as part of our business plan

Highlights

Successful opening of our new Community Hub in Wednesbury



Improved complaints performance with a 37% fall across both regions

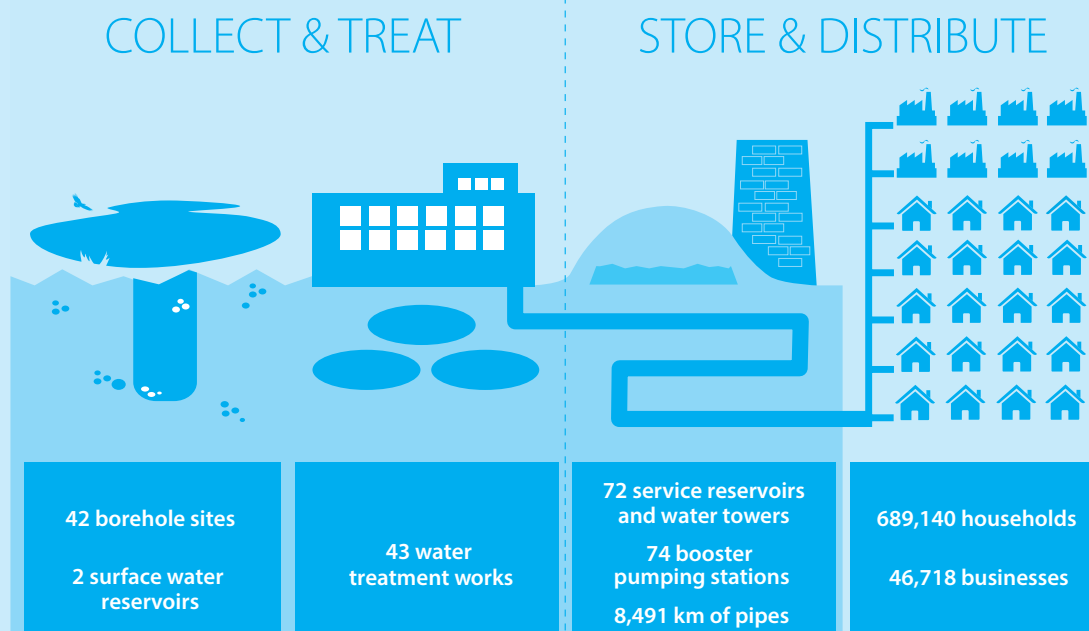
Disappointed with our mixed leakage performance through the year



At a Glance

South Staffs Water - making water count

Business Model



Our Vision

To consistently deliver high quality water at great value with excellent service to our customers, communities, employees and wider stakeholders.

Our Mission

At South Staffs Water we deliver:

Excellent water quality and secure and reliable water supplies supported by an excellent customer experience to all customers and their communities.

As water is a precious resource we're committed to operations that are environmentally sustainable.

We innovatively manage our business to deliver a first class service and value for money for our customers.

This is achieved through the commitment of our employees, making South Staffs Water a great place to work.

Turnover

2018	2017
£124.1m	£123.7m

Operating Profit

2018	2017
£30.4m	£32.6m

Corporation Tax

2018	2017
£3.3m	£1.6m

Appointed Dividends

2018	2017
£5.0m	£6.5m

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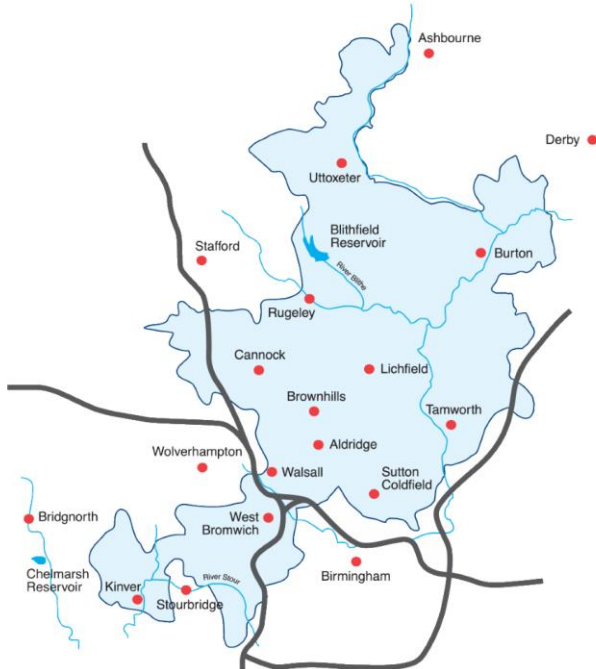
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Strategic Report – Company Overview

South Staffordshire Water PLC (“South Staffs” / “South Staffs Water” / “The Company”) is part of the South Staffordshire Plc group of companies, a privately owned integrated services group concentrating on regulated water supply and complementary specialist service businesses.

We operate across two regions under a single water supply licence.



South Staffordshire

- 1,490 square kilometres covered
- Approximately 1.3million population served
- Three main sources
 - Blithfield Reservoir
 - River Severn
 - Borehole sources across the region

Cambridge

- 1,173 square kilometres covered
- Approximately 0.3 million population served
- All water sourced from boreholes, all from chalk aquifers



South Staffs Water (incorporating the transferred business of Cambridge Water) is a water only company and as such does not supply sewerage services. However, it does bill customers for these services on behalf of Severn Trent Water and Anglian Water Services.

Strategic Report – A Message from Our Chairman

Sir James Perowne



The water industry has had an interesting journey through 2017/18 from the opening of a new competitive market for non-household customers through to discussion of nationalisation and reform. South Staffs has been fully engaged at an industry level in these important matters but has continued to maintain real focus on meeting the needs of customers in the here and now as well as planning for the delivery of our Business Plan for 2020 to 2025 and beyond.

With the other members of the Board, I have been closely involved in the Business Planning process with regular updates on progress and key decisions to make. Our focus as a Board has been to continually challenge the Executive Team to go further for our customers. I've been pleased to see the real step change we have made in the engagement with customers which has already delivered huge rewards in terms of understanding their needs and priorities. In effect we are shaping the future of the business with our customers and that is how it should be for a business that provides a vital public service.

During the year we have welcomed a number of our important stakeholders and regulators to the Board. These have included the Chief Executive of Ofwat, the Chief Inspector of Drinking Water, our Regional Consumer Council for Water Chair and the Independent Chair of our Customer Panel. We have enjoyed the opportunity to engage directly with them and they have provided fantastic insights and challenge as well as honest and generally positive feedback about South Staffs.

Performance in 2017/18 has seen some real highs in areas such as complaints reduction, the continued improvement in the number of customers contacting us about the quality of their water, and great steps towards helping our most vulnerable customers. However there have also been some areas where we have fallen short and must work harder. Most notably in the area of leakage, a matter which we know is hugely important to our customers.

I wish to extend my welcome to our new majority shareholder Arjun Infrastructure Partners and express my gratitude to KKR who have been excellent investors over the last five years. These are sensitive times for the industry and I am confident that Arjun will fully embrace the public service in private ownership approach that we hold dear.

Finally I want to express my gratitude to our staff. Their dedication was illustrated perfectly in our response to the 'Beast from the East' freeze thaw in March. Our office and field based teams worked tirelessly together through this challenging period to protect supplies to our customers and I am proud to see how well we performed overall.



Strategic Report – Managing Director’s Welcome

Phil Newland



Thank you for taking the time to read our latest accounts and annual performance report. I hope you find this document useful in helping to understand more about what South Staffs Water does and how well we are doing our job.

We believe it’s important to be transparent with our customers and stakeholders and are working hard to regularly share more information about our performance. This report is just one of the many ways we are making this happen. We remain the only company in the industry that reports operational performance to our customers each month via a customer friendly dashboard (see below). We are also making further disclosures around remuneration, governance, tax and our ownership structure as we know these are important matters for customers.

2017/18 has been a challenging year both in terms of our operation and the broader environment in which we work. South Staffs has largely reacted well to the challenges. We are particularly pleased to see a significant reduction in customer complaints in both our regions of operation. In the South Staffs region we have achieved our lowest ever level. We have also taken positive steps towards both understanding and addressing some of the needs of our most vulnerable customers. Of course, maintaining the reliable supply of the highest quality water is the most important thing we do for our customers and we have continued to reduce the number of customers contacting us about the quality of their water, this is now at an all-time low. We have also reduced the number of accidents resulting in an injury in our business to 10 in the year, all accidents should be avoided but this is still another big step in the right direction.

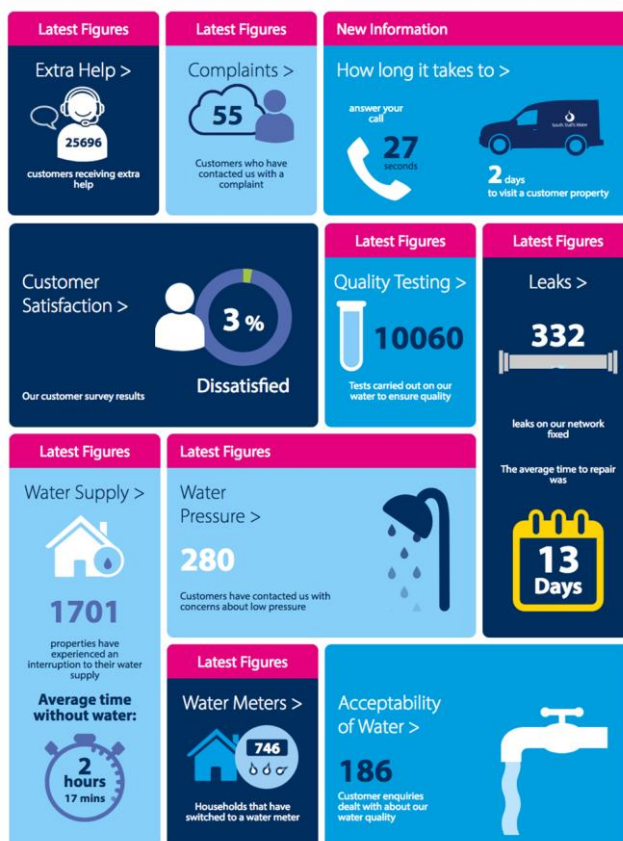
However there have also been some disappointments and areas where we must redouble efforts. We have seen improvements in our Service Incentive Mechanism (SIM) score – the water industry customer service measure but we have not yet reached our target of being amongst the very best. We have also had a tough year with regard to leakage, just missing the targets in both of our regions. Throughout the year we have been on track to achieve the targets in both regions having significantly increased our investment levels. In March we were frustrated by some unexpectedly challenging weather, the ‘Beast from the East’ with the resulting impact on leakage. Our teams worked tirelessly to minimise the impact on customers and we are pleased overall with how we managed the incident and the recent Ofwat report ‘Out in the Cold’ would appear to support this view. Nonetheless we will reflect, improve and learn from others in how we manage such events.

This year we have placed considerable effort into the production of our Water Resources Management Plan (WRMP) as we seek to achieve the right balance in providing reliable water to a growing population whilst encouraging customers to use less, reducing leakage and protecting the natural environment both in the near and longer terms. Engagement with our customers has been both essential and stimulating, resulting in new ideas and a far better understanding of their demands and aspirations. To date we have been encouraged by their feedback as well as the reactions of our regulators to the work.

We have also been preparing our Business Plan for 2020 to 2025, known as PR19 which has to be submitted in September. As one of the smaller companies in the sector we have found the impact

Every day we supply over half a million homes with clean, fresh water through a network of 6,000km of pipes

We think it’s important our customers know how well we’re doing this so will share how we’re performing every month. Take a look at our latest figures



[Above is an in year illustrative example for South Staffs Region]

Strategic Report – Managing Director’s Welcome

of preparing, what we intend to be a high quality, ambitious, well researched plan to be considerable but ultimately we believe worthwhile. We are proposing an ambitious level of investment to transform our two largest works, Seedy Mill and Hampton Loade into higher performing and more resilient treatment facilities in order to deliver better and more reliable water to the substantial number of customers they serve. In addition to our ongoing programme of customer engagement dialogue we have spoken to over 32,000 of our customers in formal research and it is their diverse views and priorities that we will aim to reflect in the final plan. They are challenging us to be more ambitious but also taking us into new areas. Customers in general are reminding us of our obligation to educate them about the value of water. Our younger customers in particular are encouraging us to place greater emphasis on the impact of our operations on the environment. Finally in our role as a public service provider, we are embracing a renewed challenge to listen, and to support some of the most vulnerable in society. Our aim through all this is to be an industry leader on cost and service but also increasingly to innovate and through this not only benefit our customers but the sector as a whole.

This year saw the launch of the non-household retail market for water, as reported last year South Staffordshire PLC entered into a joint venture to operate in the retailer space with Pennon Group. This joint venture operates at arms-length and is not covered by this report. We have however successfully operated as a wholesaler during the first year of the market with performance amongst the best in the industry against the market standards.

The water industry continues to see unprecedented transformation with complex challenges including deregulation, environmental pressures, changes in customer expectations and political challenge. At South Staffs we are building increased flexibility and resilience into our operations which means we can respond quickly and adapt as necessary to the changing landscape.

I’d also like to take this opportunity to say thank you to our teams in South Staffs and Cambridge, none of our progress or achievements in the year would be possible without their commitment and hard work.



Five-year targets

Our five outcomes and 15 performance commitments reflect what customers say is important to them. Some are financially incentivised over the five-year period, meaning we may incur an underperformance penalty or an outperformance payment. For the first three years of this period, we have earned a total outperformance payment of approximately £1.1 million. At the next price review in 2019, this payment will be factored into our overall business plan to determine the customer charges for 2020 to 2025.

Outcome	ODI name	Unit of measurement	Year						Target achieved	Performance against last year
			2015/16	2016/17	2017/18		2018/19	2019/20		
			Actual	Actual	Target	Actual	Target	Target		
1 Excellent water quality	Mean Zone Compliance	%	99.884	99.982	100.00	99.943	100.00	100.00	✘	Declining
	Acceptability of water to customers	Contacts per thousand population	1.96	1.66	1.23	1.42	1.23	1.23	✘	Improving
2 Secure and reliable supplies	Interruptions to supply	Minutes and seconds per property	04:14	05:11	10:00	08:32	10:00	10:00	✓	Declining
	Asset health infrastructure	Category	Stable	Stable	Stable	Stable	Stable	Stable	✓	Stable
	Asset health non-infrastructure	Category	Stable	Stable	Stable	Stable	Stable	Stable	✓	Stable
3 Excellent customer experience	Service Incentive Mechanism	Score	86.3	84.4	90.0	87.0	90.0	90.0	✘	Improving
	Customer satisfaction	%	98	99	98	97	98	98	✘	Declining
	Community engagement	Days	257	222	400	425	400	400	✓	Improving
4 Environment	Leakage South Staffs region	Megalitres per day	69.9	69.9	70.5	72.4	70.5	70.5	✘	Declining
	Leakage Cambridge region	Megalitres per day	13.2	14.3	13.5	14.4	13.5	13.5	✘	Declining
	Water efficiency	Litres per person per day	129.59	129.85	129.52	133.09	128.91	128.31	✘	Declining
	Biodiversity	Hectares of land	76	92	106	119	116	116	✓	Improving
	Carbon emissions	Tonnes of carbon saved	178	285	2428	550	3742	5210	✘	Improving
5 Fair customer bills	Value for money and affordability satisfaction	%	93	91	90	94	90	90	✓	Improving
	Support for customers in debt	Number of customers	19621	23895	24800	29036	27400	30000	✓	Improving

Excellent water quality



Outcome

99.94%
water quality
compliance

Contacts from
1.42 out of every
1,000 people
regarding Acceptability of Water

Water quality is one of the most important areas of our service and is a top priority for customers. That's why we have two performance targets covering overall compliance and the acceptability of water to our customers, measured by how often our customers contact us to report issues. We have been stretching regulatory targets for both of these measures.

We are disappointed to report that we have not met 100% water quality compliance, as 15 out of nearly 23,000 samples did not meet the strict regulatory compliance standards. Despite this, our water quality remains at a very high standard overall. The causes of the small number of failures were thoroughly investigated and all corrective actions have been put in place to resolve any issues. We also engaged with the Drinking Water Inspectorate (DWI) on any issues throughout the year.

For the second year in a row, we have delivered an improvement to the acceptability of water, measured by how often customers contact us to report issues. The actions we have taken and investments we have made to improve our water quality have delivered just over a 14% reduction in the number of customers who contact us. Since 2015, this means we have delivered nearly a 30% reduction in the number of customers contacting us to report water quality issues, and this puts us on track to achieve our stretching regulatory target by 2019.

Installing UV in our South Staffs region

Continuing with our programme of work to invest in the latest water treatment technology, we are installing state of the art UV treatment into our largest water treatment works at Hampton Loade near Bridgnorth and also two other borehole sites. This proven, regulated and environmentally-friendly technology ensures water is free from harmful organisms. Less chlorine is needed, reducing the risk of taste and smell issues for our customers.



“

Improving the quality of water is the number one priority for the business.

Secure and reliable supplies



Outcome

8 minutes 32 seconds

average supply interruption
per customer

stable

asset health for **pipes,**
pumping stations & reservoirs

One of our highest priorities is to maintain a continuous supply of wholesome water to our customers' taps. Despite a significant number of burst main events during the year and the impact of 'the Beast from the East' in March, we have achieved our performance commitments with a significant amount of hard work from all of our staff in some very challenging conditions.

The 'Beast from the East'

On Sunday 4 March we felt the full impact of the 'Beast from the East'. Following a sustained period of freezing weather, a rapid thaw led to a 25% increase in demand across our networks. We were prepared for the event and had increased the amount of water we had stored in our reservoirs, ensured additional resources were available to respond to the event and enacted our emergency response plans. Despite the significant impact this event had across the whole of the UK, the disruption caused to our customers was minimal. Our teams worked around the clock to ensure our treatment works operated at full capacity, bursts were repaired quickly, our customers were kept informed of the situation and support was given to those who needed our help.

We are pleased to have met our targets despite dealing with this event, although we did see a deterioration from last year's performance. We have put in place a number of initiatives such as targeting 'zero' interruptions from any planned works we undertake. We are already seeing the positive benefits of these initiatives and anticipate further enhancement to the level of service we deliver.



The 'Beast from the East' caused disruption across the UK, but we responded well and our customers largely went without any disruption to service.

An excellent customer experience to customers and the community



Outcome

SIM score of
87.0

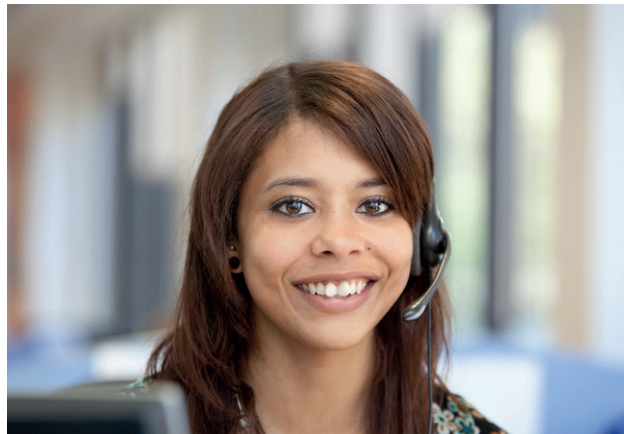
97%
customer
satisfaction

425 days
of community
engagement activity

We are continuing to focus on our customer service performance. Our SIM score, a regulatory measure of customer service performance, increased from last year due to the strong actions we put in place. We also had a very high level of customer satisfaction, although not quite meeting our exceptionally-high target of 98%.

In addition, we have worked hard to improve our customer service in cooperation with internal and external stakeholders, such as our Customer Panel and the Consumer Council for Water (CCWater), implementing solutions to address issues that customers told us they were dissatisfied with.

These changes included a new dedicated customer service team for the Cambridge region, improving our budget plans, more contact with customers to proactively inform and resolve billing issues, and improved response times throughout all our communication channels.



We are pleased to report that our changes have seen a reduction of 37% in the number of complaints and an 11% decrease in complaint response time. We've also seen an increased satisfaction level in our SIM surveys – the second highest increase in the industry.

Our efforts mean that the South Staffs region remains as one of the top complaint performers in the industry, while we will be continuing to work hard to improve Cambridge region's position in the coming year.

“

Ensuring excellent customer service remains at the heart of everything we do.

Community Hub

South Staffs Water aims to make a positive difference and develop strong and lasting partnerships with the communities in which we live and work through education about water usage and efficiency, enhancing biodiversity and charitable support.

We have made great progress this year with our community-based activity, which supports those customers, who may require additional support to access or use our services. We have made contact with over 600 organisations and maintain an active relationship with over 200 of them. We now have two Community Engagement Officers, who build relationships and work with community-based organisations to help customers access the best tariff, provide information about water meters and water efficiency, and ensure we have customers on our priority service register.

To support our community work, we recently opened our first Community Hub in Wednesbury, so that we can provide a place for customers to be in direct contact with us and support those who may not be able to or do not want to use either a contact centre or our website.

A change in how we approach engagement with schools has been introduced during the year. We believe that in switching from a location-based offering in the South Staffs region alone to an outreach service in both regions, we are better placed to meet the needs of educational institutions, be able to increase our work in this area and also start to build meaningful relationships with our future customers.

We are pleased to report that due to these efforts, we have met our regulatory target for community engagement this year, almost doubling last year's performance.



“

We want to make a positive difference within the communities where we live and work.

Operations that are environmentally sustainable



Outcome

133.09 litres of water per day used by each person we supply

119 hectares of land with a biodiversity initiative

550 tonnes of carbon reduction

72.4 MI/d leakage in South Staffs region

14.4 MI/d leakage in Cambridge region

Water is a precious and finite resource and we must ensure that adequate water supplies and the natural environment are maintained properly in order to support future generations. We also have wider environmental responsibilities and we take great care to ensure that our operations do not impact on the natural environment.

Despite making very good progress on leakage during the year, the late impact of the 'Beast from the East' prevented us from achieving our leakage targets, and we will incur a penalty as a result of this performance, which will be reflected in customer charges from 2020 onwards. A number of initiatives have been put in place during the year that have delivered a prompt recovery and a very positive start to 2018/19, when we are confident that these targets will be achieved.

We have continued to work closely with landowners and the Environment Agency to deliver innovative catchment management solutions to mitigate impacts on the environment and improve the quality of raw water that supplies our treatment works. We now have more than 80 participants within our innovative 'SPRING' and 'PEBBLE' schemes, which encourage sustainable farming practices and biodiversity.

We have a number of initiatives in place to further enhance water efficiency which includes direct engagement with customers and developers, who are encouraged to build properties that incorporate rainwater and grey water harvesting. We anticipate the full commissioning of the Eddington rainwater harvesting scheme later this year, which will eventually provide recycled supplies to more than 8,000 customers. This scheme has been delivered in collaboration with the University of Cambridge and is the largest in the UK.

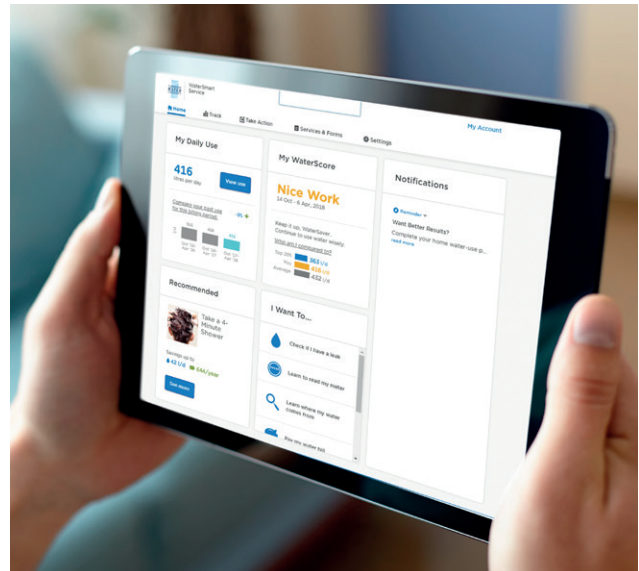
We are in the process of concluding the consultation process on our Water Resources Management Plan, which details how we will operate in the future and demonstrates how we will mitigate impact on the natural environment. The feedback received to date from a wide range of stakeholders has been largely positive. We anticipate that the final version of this document will be published later in the year once clearance is received from the Secretary of State.

“

We understand the impact of what we do and are committed to protecting our environment.

WaterSmart

Our continuing commitment to water efficiency has led us into an exciting and innovative pilot in our Cambridge region. This involves 15,000 randomly-selected customers and software from a California-based company, called WaterSmart. This leading tool is designed to produce personalised water consumption trends for customers. The project's aim is to educate the customer on the value of water, providing tips around reducing consumption and even indicating, if there may be a leakage problem. We see this approach as integral to improving and encouraging customer engagement in water efficiency. We hope the analysis will also help to address affordability and vulnerability and ultimately improve debt management.



SPRING environmental protection scheme

Our new SPRING (Slug Pesticide Rethink - Ideas for Nurturing Growth) environmental protection scheme has built on previous success to further support arable farmers in the Blithe catchment area. We have made grants available towards the costs of voluntary on-farm infrastructure improvements and agricultural management schemes designed to protect the environment and improve water quality. Grants have been awarded for activities such as contour cropping and pesticide sprayer washdown.



PEBBLE funds

We also work to deliver innovative projects that will enhance biodiversity across our region. The first round of funding from our PEBBLE fund (Projects that Explore Biodiversity Benefits in the Local Environment) has rewarded applications, ranging from creating a wildlife walk, and clearing scrubland to supporting a school keen to raise awareness of the environment and local wildlife among pupils. The photographs below show a PEBBLE-funded scheme that created a pond for wildlife at Leasowes.



Fair customer bill and fair investor returns



Outcome

94% satisfaction score
for value for money
and affordability

29,036 customers
helped with debt-support options

We believe it's important to keep our bills as low as possible for our customers, who continue to have low water bills when compared to the other water companies in England and Wales. We think very carefully about how we spend money, and what we invest in. We try to find the right balance, ensuring that our bills are affordable for all, while investing enough in our assets to maintain our service for future generations.

We are pleased that our annual tracker survey shows a 94% overall satisfaction with our value for money and the affordability of our service. This is an increase from last year and meets our regulatory commitment.

We are also committed to providing extra support for our most vulnerable customers when they need it most. We do this by providing a range of additional help schemes tailored to customers' individual circumstances. Through our range of debt support initiatives, we have helped over 29,000 customers, meeting our regulatory target.

Support for vulnerable customers

Our Assure tariff continues to grow. Introduced in April 2016, we have already accepted over 10,000 customers onto the tariff, which is designed to help our customers who struggle to pay their water bills by providing up to an 80% discount, depending on qualifying conditions.

We have undertaken extensive promotion of our new tariff to ensure that those who need it most know about it. This has included digital campaigns on our website and social media channels, as well as local advertising. We expect many of our existing Assure customers to renew for the next financial year, and our continued promotion will ensure an increase in customers being helped.

We have also invested in staff to allow us to visit customers in their own home where necessary. This helps us better understand their needs and support them in accessing extra help. We are visiting an average of 21 customers each month.

Mr and Mrs Walters are customers who have received extra help.

"We couldn't believe it! It just didn't seem real that you can get a bit of help like this when you need it most. The reduction has helped us with things we wouldn't have been able to afford, at a time that we really really needed it. It's definitely made a big difference, our bill is more affordable and its helped us more than we ever thought. Thank you!"
Mr & Mrs Walters, South Staffs Water customers.

Water & sewerage charges for 2017/18:	£369.05
New bill after extra help discount:	£62.82
Overall annual saving:	£306.23

“

Our Assure tariff and other types of financial help are making a difference to customers who need it most.

Strategic Report – Operational Review

The highest quality water, today and tomorrow

The single most important aspect of our operation continues to be ensuring that the water we supply to customers every day is of the highest quality; our customers have confirmed this is what they expect. Improving the quality of our water beyond simply meeting regulatory commitments is a key objective for the business, with an aim to achieve 100% water quality compliance and to further improve customer perception of water through appearance, taste and odour. We aspire to an unrestricted, uninterrupted supply of water of the highest possible quality.

We have continued to see year on year improvements, approximately 30% reduction per year, in terms of the number of customers contacting us about the quality of their water. This has been largely driven by continued investment in assets and processes. We had another challenging year for drinking water quality water in 2017, and incurred an ODI penalty based on our Mean Zonal Compliance (MZC) score. However this was primarily driven by single failures in very small water quality zones. These failures have a disproportionate impact on the overall calculation as the sample numbers are low. We have reviewed and further improved our root cause analysis process where failures occur to ensure that we capture and embed the learning across the business. Additionally we are in the process of analysing the impact of the Drinking Water Inspectorate's new metrics, Compliance Risk Index (CRI) and Events Risk Index (ERI). CRI will be tracked alongside MZC until the end of 2019 but will then replace it. Although we had a challenging year for CRI last year overall, our CRI performance in the Cambridge region was comparatively very good. The elevated CRI for the South Staffs region was primarily driven by a single failure at one of our largest works. We carried out a robust root cause investigation and have taken prompt remedial action to prevent a recurrence. Based on the nature of the failures and the remedial actions taken in response we are confident of an improved performance in 2018.

Leakage

During the year we have worked incredibly hard and improved our leakage performance, however the impact of the 'Beast from the East' in March effectively created a double winter which prevented us from achieving our leakage targets. The significant investment made in both human resource and technology has supported a positive recovery during the early part of 2018/19. Along with the utilisation of automated leak detection equipment including satellite and drone technology we have now initiated the implementation of a 'live network' allowing us to become increasingly proactive in the management of leakage from the network. We will continue to invest in our people and are very optimistic about the impact we expect to see from additional technology based developments during the coming year, we have made a very positive start to 2018/19 and are confident that we will achieve our leakage targets in both regions.

Hampton Loade ultra-violet installation

The installation of a new ultra-violet (UV) treatment stage at Hampton Loade, our largest treatment works, commenced in September 2017 and is due to complete in October 2018. The scale of the works makes this a major activity but the most significant challenge is that delivery of this complex capital project will be while the water treatment works is live and delivering hundreds of millions litres of water every day. This requires careful planning to ensure that the works are delivered safely and efficiently, and at the same time ensuring that water quality and supply resilience are maintained.

Outwoods reservoir

In August 2017 we successfully completed the build of a new 10 million litre service reservoir at Outwoods, near Burton on Trent. The reservoir was needed to complement an existing reservoir on the same site which is reaching the end of its operational life having been constructed in 1882. The scheme was completed on time and on budget ensuring the delivery of additional potable water storage to ensure supplies are maintained to the Burton upon Trent area.

Customers contacting us about the quality of water

Ensuring that our customers are happy with the water we supply to their tap is absolutely critical to us; and an area where we have expended a significant amount of effort to make improvements in recent years. These efforts have seen us deliver 15% year on year reductions in the number of customers contacting us about the quality of their water over each of the last 2 years, with 2018 currently on target to deliver a further improvement. This is being delivered through working smarter and embedding water quality risk management processes into everything we do across our supply system.

Strategic Report – Operational Review

The ‘Beast from the East’

The end of February and beginning of March 2018 saw the arrival of a cold spell which became commonly referred to as the ‘Beast from the East’ bringing sustained freezing temperatures, followed by a rapid thaw. We were aware that both the freezing weather, and the subsequent thaw, were coming and prepared by increasing the volumes of water we store in our reservoirs and also by enacting our emergency plans. Despite this, the scale of the rapid thaw on Sunday 4 March 2018 caused a significant increase in demand across our network due to both burst mains and significant leakage within customers’ premises. This resulted in a 25% increase in demand in a 24 hour period, which put the whole system under considerable strain. Unfortunately the result was a small number of customers experiencing low pressure and interrupted supplies. To manage this event, we had teams working around the clock for a period of a week repairing burst mains, ensuring treatment works were at full capacity and assisting customers with issues on their premises. Ofwat has carried out an investigation into the industry response during this period, whilst there are some areas to improve upon our performance was one of the best.



Secure and reliable supplies, now and in the future

One of our highest priorities is to maintain a continuous supply of wholesome water to our customers tap. Despite a significant number of burst mains during the year and the late impact of the ‘Beast from the East’ we have again beaten our performance commitment with a significant amount of hard work from all of our staff in some very challenging conditions, although we have performed less well than in previous years. Our focus will continue to be on ensuring that our pipes and networks are well maintained and that decisions regarding our infrastructure place us in the best possible position to provide secure and reliable supplies. Water efficiency is fundamental to safeguarding supplies and we remain committed to helping customers change the way they value and use water every day through an ongoing programme of educational engagement.



Successful collaboration with the University of Cambridge will see completion of phase 1 of the award winning £1 billion Eddington development in North West Cambridge supplying 3,000 homes, 2,000 student rooms and other community facilities from the UK’s largest rainwater recycling scheme this coming year. We see this as a living example of how future developments in a water scarce area, which is also seeing significant population growth, should be approached.

Our continuing commitment to water efficiency has led us into an exciting and innovative pilot in our Cambridge region. This involves 15,000 randomly selected customers and software from a California based company called WaterSmart. This leading tool is designed to produce customer level analysis around personalised water consumption trends. Available across multiple channels (e-mail, text / SMS, Mobile App) the reports aim to educate the customer on the value of water, providing tips around reducing consumption, positively influencing behaviour and even indicating if there may be a leakage problem. We see this approach as integral to improving and encouraging customer engagement in water efficiency. We also hope the analysis could help to address affordability and vulnerability within the customer base and ultimately improve debt management.

In addition to the WaterSmart trial mentioned above we have also deployed another innovative method to promote water efficient behavioural change. This technology has been developed by Suez and is also being rolled out in the Eddington North West Cambridge development. The Suez solution is similar to WaterSmart but uses real time data rather than manual readings. We continue to focus a lot of time and effort in promoting water efficiency to our customer base and have distributed all of the water saving devices that we intended to this year.

Strategic Report – Our Customers and Communities

Excellent customer service, every time

We continue to place our customers and community at the heart of everything we do and have worked to improve the service we provide whilst developing longer term customer service solutions. We are focused on ensuring that we deliver the right service through the right channel, as and when our customers chose to engage with us. We have been testing service solutions through a range of channels from the digitally innovative, such as the launch of our voice activated Alexa Skill, to the more tailored face to face experience that a home visit can bring.

A key area of focus throughout the year was to reduce the volumes of complaints we received, especially within our Cambridge region. A series of initiatives were completed including improving our debt recovery letters, process improvements to our customer journey, changes to our MyAccount system and setting up our Cambridge First contact centre team. These changes combined with investment in customer service training across the business for field teams and contact centre staff ensured we delivered a 37% reduction in complaints, with the levels in our South Staffs region at our lowest recorded level.

Although significant progress has been made in certain service delivery areas such as complaints we are still seeing industry average results within the Ofwat SIM survey. Towards the end of the year we have started to work on improving transactional interactions such as home moves and making payments, this has seen positive increases to our quarterly SIM scores. We will continue to work on this throughout the following year.

As well as launching the Alexa Skill we have also developed our digital contact channels and have added both Twitter and Facebook which are proving to be useful service channels and a great way of communicating quickly with some of our customers, especially if we have a supply issue.

We continue to find ways to better listen to our customers and respond to what we hear from them. More in-depth, regular research has been put in place to better understand customers' current and future needs as well as their views of our services. The research has been targeted with specific customer groups, including those in vulnerable circumstances and non-bill payers, to enable us to better understand how we can offer the right level of service and support. This additional research combined with our ongoing customer dialogue and information obtained from customer contacts and complaints is creating insights that are being used to inform business decisions to match with what customers have told us they value. We have also altered our approach to how we engage with customers to give them a greater say in shaping the future of their water services.

These research findings are being complemented by the contribution of the new independent Customer Panel which meets once a quarter. On the panel there are representatives from the Environment Agency and CC Water plus members with a variety of skills and expertise within the public and private sectors. The use of their insight and experience to actively challenge how we engage with our customers and perform as a business has been a significant achievement this year. In addition, our Independent Non-executive Directors attend the panel on a rotation basis to complement attendance by senior management and to ensure that the appropriate actions are being taken based on the meeting outcomes. We welcome the independent and challenging contribution the panel brings.



"The Customer Panel has been set up at the instigation of the regulator Ofwat and is separate and independent from the water company. Our role is to give assurance to the regulator when they receive the company's proposed five year Business Plan for 2020 to 2025 about whether customers' views have been adequately researched and how far the plan reflects customer preferences. As Chairman of the Panel I am grateful to the company for its openness, its respect for the Panel's independence, and its unfailing delivery of whatever information or practical support we need to carry out our role."

Simon Sperryn – Customer Panel Chairman (Pictured left)

Strategic Report – Our Customers and Communities

Fair and affordable bills for all of our customers

South Staffs Water's household customers continue to enjoy some of the lowest bills in England and Wales. We are committed to maintaining affordability of bills and supporting our most vulnerable customers with a range of help when they need it most. During the year, we exceeded our performance commitment in providing extra help to over 23,000 customers in debt by helping them manage their water accounts and take control of their consumption.

We offer a range of solutions to support our customers who are struggling to pay or who have debts which they find difficult to meet. We offer debt write off through our Charitable Trust which supports customers who are struggling to pay and our Assure social tariff, which we launched in 2016/17, has been really successful this year providing assistance to over 10,000 customers. We have achieved this through a combination of direct customer communication, community engagement activity working with charities and organisations to promote the tariff and by fast tracking customers directly onto the tariff through other organisations.

Connecting with our communities



Our first Community Hub opened in Wednesbury.

South Staffs Water aims to make a positive difference and develop strong and lasting partnerships with the communities in which we live and work through education about water usage and efficiency, enhancing biodiversity and charitable support.

We have made great progress this year with our community based activity which supports those customers who may require additional support to access or use our services. We have made contact with over 600 organisations and maintain an active relationship with over 200 of those. We now have two Community Engagement Officers who build relationships and work with community based organisations to help

customers access the best tariff, provide information about water meters and water efficiency and ensure we have customers on our priority service register.

To support our community work we have recently opened our first Community Hub in Wednesbury so that we can provide somewhere for customers to access direct contact with us and support those who may not be able to, or do not want to use either a contact centre or our website.

We have an ambitious target to deliver at least 400 days of support in our communities through initiatives including an education programme, biodiversity projects and our employee volunteering scheme. This remains a challenge as we are a small team, but this year we have made a difference in supporting schools, charities and other organisations. We ended the year having delivered 425 days of support.

During the year, in light of customer feedback, we took the strategic decision to change the focus of our educational activities away from our school visit centre at Blithfield to an outreach approach. We have taken time to develop brand new educational materials concerning the water lifecycle and water efficiency and by the end of 2018 will have engaged with over 500 pupils. We believe that in switching from a location-based offering in the South Staffs region alone, to an outreach service in both regions, we are better placed to meet the needs of educational establishments, and to increase our work in this area by building meaningful relationships with our future customers.

In November 2017, we employed an Education and Community Outreach Co-ordinator, who has worked on developing our educational offer to schools within both our supply regions. Since the beginning of 2018, we have engaged with 249 pupils, educating them in water efficiency and where their water comes from. We have recently sent out a promotion to schools to encourage them to book an educational visit with us for the autumn term and have received a promising response, with bookings already coming in for September. To help in the delivery of our education programme, we are looking to recruit a team of education volunteers in both regions, so that we can meet the demand from schools.

Strategic Report – Our Approach to Business Planning

Our Business Plan for 2020 to 2025

We have been developing our Business Plan for 2020 to 2025 throughout the last 12 months, which we will submit to Ofwat in early September 2018.

We have focused our attention on engaging with customers, so that we can understand the things that are most important to them. Since April 2017, we have gained feedback on a number of areas from more than 30,000 customers using a wide range of engagement techniques, including surveys, interviews, focus groups and workshops. We have triangulated customers' responses where they vary to better understand different views.

We think our new approach has given us a clear and robust view of our customers' priorities, and the areas where they want to hold us to account. These are:

- having clean, high-quality and reliable water supplies
- having fair, accurate and affordable bills
- receiving great customer service
- reducing leakage
- protecting the natural environment
- helping customers who may need extra support

We are developing a Business Plan that focuses on the promises we have made to our customers based on the services they want us to deliver now and over the long term. We have considered these promises carefully and have developed a series of performance commitments and targets that sit beneath them so that our customers can see how we are doing.

A key part of our engagement has been to ask customers, in a number of innovative ways, to co-create these commitments. This means we can be sure that we are delivering the things that matter most to them. Our Board have challenged these along with the independent Customer Panel.

Having looked at length at our customers' priorities and their expectations for the services they want us to deliver, we then considered our operations alongside the resource issues facing us, now and in the future. This has meant adopting a different approach to that taken with previous Business Plan submissions. It has also meant taking a more holistic view of the long-term capabilities of our network and understanding what our customers want and what they can afford to pay.

So, we have reviewed and evaluated our existing operations across both our regions and worked with leading organisations to help us shape our plans. Looking at our operations in the round this way has enabled us to identify the best plan for our customers.

For example, we worked with Arup to develop a robust and flexible decision-making framework to help guide our long-term planning and investment strategy. This has meant combining our approach to how we manage our assets with our 25-year water resources management plans. This represents a move to considering all our assets in the round, taking into account things like customer preferences and resilience.

Our decision-making framework goes further than the cost-benefit analysis used with previous Business Plan submissions. It utilises a multi-criteria analysis model to come up with a range of solutions across all our operations – in total, we have appraised more than 1,000 investment operations over an 80-year timeframe.

This new approach has given us flexibility to adapt to a changing future. It has also enabled us to weight different criteria to reflect the importance to the business and to customers of the investment options we have considered. As well as being robust, it has encouraged greater engagement with stakeholders.

The work we have carried out to develop our Business Plan represents a step change in how we invest in services. It has also meant that we will be delivering a plan for 2020 to 2025 that our customers have said they want, and that they are willing to pay for. In short, it is about how we are making water count for our customers and the communities we serve, now and in the future.

Strategic Report – Our Approach to Business Planning

Case study - Engaging effectively with customers

Over the past 12 months we have talked and listened to more than 32,000 customers and community voices. We are continuing to speak to even more throughout the rest of this year and then beyond. We are using all this feedback to help us improve now and also to put together our Business Plan for 2020 to 2025 to ensure that it is right for all customers and wider stakeholders. We are also using a wide range of feedback tools to ensure we listen to as many customers as possible all the time, both through day-to-day contacts and also to talk to customers in depth about the matters they say are most important to them.

As part of this more rounded approach to customer engagement, we commissioned an independent specialist Community Research in 2017 to run a comprehensive programme of qualitative and quantitative engagement with a broad range of household and business customers and wider stakeholders to understand their views on areas specific to our Water Resource Management Plans (WRMP) and which long-term demand and supply options they wanted us to focus on.

Key findings from our WRMP engagement included:

- The top three priorities (among uninformed customers) were broadly consistent, both in this study across the range of customers who took part and also with the findings from our Foundation priorities research. These were: 1. ensuring water quality; 2. keeping bills affordable; and 3. reducing leakage.
- Stakeholders and larger business customers' spontaneous priorities mirrored these, but often came from a more informed position because of their job remit. They were also concerned about us planning for the future and ensuring the resilience of water supplies.
- The majority of customers believe that metering is the fairest way to charge – i.e. “pay for what you use”
- The message on leakage is very clear – all audiences (customers and stakeholders) want the company to do more, going beyond current targets
- Avoiding restrictions (Temporary Use Bans (previously known as hose pipe bans) for households and non-essential use bans for non-households) is not a priority for the vast majority customers in either region. Levels of service could potentially be reduced and few customers said they would worry if this were the case. However, as many customers cannot recall experiencing the most recent ban, there is no sure way to know how this would impact on their overall satisfaction levels if they were to experience one. Maintaining the current levels of service would therefore be the best option based on our customers' views.
- Customers did not immediately place significant priority on the environment as many had limited knowledge of the link between a water company's activities and the impact this can have on the natural environment. However, when customers were provided with further information on ten demand- and supply-side options, environmental considerations did come to the top of mind when they were discussing which ones we should prioritise in our plans. Future bill payers placed a high level of importance on environmental concerns.
- Over half of customers agree they could do more to reduce water usage. Both passive and pro-active education and support are welcomed in this space

At the workshops and in the on-line follow up survey we also used gamification techniques to allow customers to make informed choices about complex decisions around our strategic options. When taken through a selection of supply and demand side options (and given information on cost, volume of water supplied, environmental impact, deliverability, level of future proofing) the demand management options were consistently more appealing to customers.

We have used this in-depth engagement to place our customers' preferences at the heart of our WRMP plans and our multi-criteria analysis modelling to help us decide where best to invest customers' money to make sure we can always meet customer demand for water, now and in the future.



A short video showing our all day workshop event for households and small businesses can be seen on our website at:

<https://www.south-staffs-water.co.uk/about-us/making-water-count/customer-feedback/finding-out-when-and-where-customers-want-us-to-invest>

Strategic Report – Our People

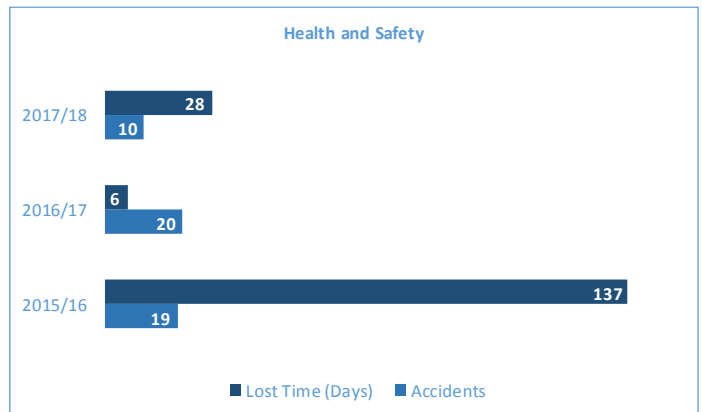
Valuing our people

Our people are crucial to our business and to delivering our service. Everything they do is about ensuring the best outcomes for customers in both our South Staffs and Cambridge regions. Our aspiration to be a leader in the sector also means that our health and safety performance must be outstanding. We are committed to making South Staffs Water a great place to work with a safe, positive and rewarding working environment.

Employee health & wellbeing

One of our key people measures relates to how safe our operations are and our aspiration to be a zero accident business. We are pleased with the progress we are making in educating our people, providing safe systems and the right tools to deliver, and our outcome this year of halving the number of accidents is a great success. We had one reportable accident which is reflected in the increase in number of days lost.

Our safety performance continues to be supported by staff health monitoring and support. This benefit supports risk management and also provides wellbeing assurance and appropriate interventions where health support need is identified.



Apprenticeships

We recruited three additional apprentices during this year, strengthening our future talent pool across the spectrum of our operations in both regions. Our apprentices are assigned a workplace mentor to support them as they gain experience from rotating across all functions of the business and gaining formal qualifications. We are pleased to have retained 13 apprentices out of an intake of 14 over the 3 years that we have been running the program, and we continue to help shape their career futures.

Celebrating success

We proudly take the opportunity to celebrate the work of our teams and supply chain partners through internal communications and by submissions of case studies for awards.



The North West Cambridge / Eddington project in partnership with Cambridge University was shortlisted at the Utility Week Awards in the Environment category. The innovative project was additionally shortlisted at the edie Sustainable Leaders Awards in the Water Management category.



With our customer partner Echo Managed Services, we were shortlisted at the Utility Week Awards in the Customer Care category for our success with Assure Home Visits.

Strategic Report – Our People

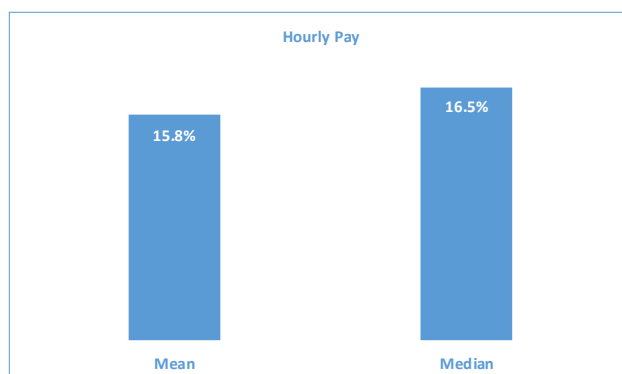


Through great teamwork, we were awarded the prestigious ‘Constellation Award for Collaborative Work with a Supplier’ at the Utility Week Star Awards in recognition of a successful partnership for the project to install a new ultra-violet (UV) water treatment facility at our Seedy Mill treatment works. In partnership with Integrated Water Services (IWS) and the UV technology supplier atg UV Technology (atg UV), the scheme was delivered as one of the largest UV water treatment plants in the UK. Judges commented on the ‘deep level of integration in a highly ambitious project’ that would ordinarily take around two and a half years but was completed in just ten months owing to the strong working relationships.

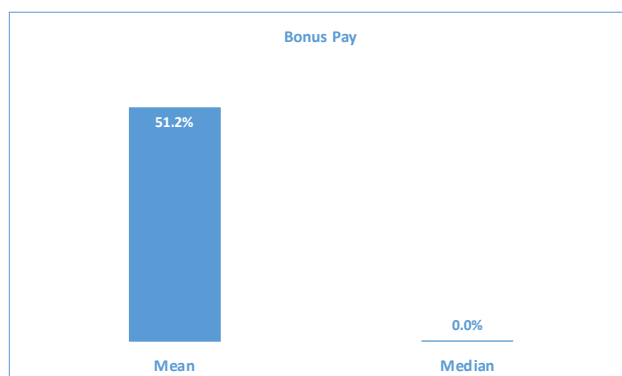
Gender pay gap and gender profile

We reported for the first time on our gender profile this year (April 2017 snapshot date). Our workforce gender split overall is 75% male, 25% female. We are confident that our gender pay gap does not stem from paying men and women differently for the same or equivalent work. Rather, it is the result of the roles which men and women undertake within the organisation and the pay that these roles attract. We fundamentally believe that everyone has an equal opportunity to develop.

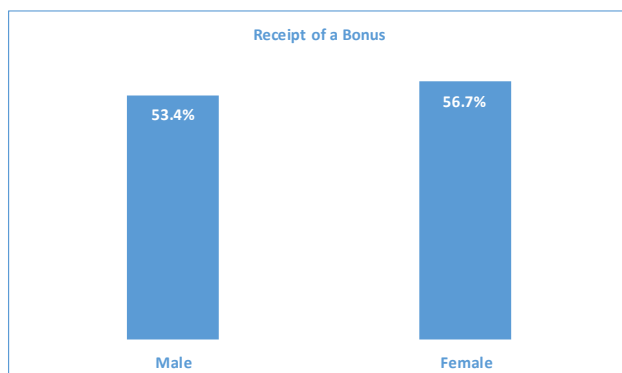
Our gap data reports the difference between the mean and median **hourly pay** of our male employees and our female employees (shown as men earning more than women)



And the difference in mean and median **bonus pay** (shown as men earning more than women)



The percentage of staff receiving a bonus (shown as more women receiving a bonus)



Strategic Report – Our People

As a business, we are committed to do all that we can to reduce the gender pay gap, but this will take time. Steps we are taking to promote gender diversity in all areas of our workforce include the following:

- Our career opportunities - We are re-thinking the way in which we attract new talent and how we present ourselves as a business in our communities. We will ensure job vacancies are written in a way that is gender neutral, focusing on skills, abilities and opportunities for development. We aim to attract more women applicants.
- Apprenticeships, schools, colleges and universities - We will take proactive action by working with schools, colleges and universities to communicate more on what we can offer as a business and in our Group. We can help to encourage more females into engineering and technical education and can offer support through apprenticeships and degree sponsorships. We will actively attend school careers fairs to continue educating on the opportunities we have to offer.
- Continue improving our flexible-working approach - Our flexible-working policy is available to employees in all business areas and at all levels of the organisation. Anyone can apply and be considered for flexible working regardless of their role. Flexible working need not be limited to part-time working and should not be viewed as something that is deemed impossible for senior roles, when typically more women than men take a more flexible approach to work.



Apprenticeship Careers Fair at Sheffield Academy, Walsall.

The split between male and female employees as at March 2018 is as follows (March 2017 figures in brackets):

	Directors and Executive Team	Senior Managers	Other Employees
Male	9 (10)	6 (7)	317 (302)
Female	1 (2)	6 (6)	84 (98)

Also shown in the table below is an age and length of service profile for male and female employees:

Years	Male	Female	Total
Average Age	44.8	40.9	43.9
Average Length of Service	12	9	12

Strategic Report – Environment

Environmentally sustainable operations

Water is a precious and finite resource and we must take care to ensure we do not adversely impact upon the natural environment as a result of our operations, we must ensure that adequate water supplies and the natural environment are maintained properly in order to support future generations.

We have a number of initiatives in place to further enhance water efficiency which includes direct engagement with customers and developers who we are encouraging to build properties that incorporate rainwater and grey water harvesting. We anticipate the full commissioning of the Eddington rainwater harvesting scheme later this year which will eventually provide recycled supplies to more than 8,000 customers. This scheme has been delivered in collaboration with the University of Cambridge and is the largest in the UK.

We are in the process of concluding the consultation process on our Water Resources Management Plan (WRMP) which details how we will operate in the future and demonstrates how we will mitigate impacts on the natural environment. The feedback received to date from a wide range of stakeholders has been largely positive, we anticipate that the final version of this document will be published later in the year once clearance is received from the Secretary of State.



We have again delivered very good progress with the management of catchments working closely with landowners and the Environment Agency developing partnerships to deliver innovative solutions to mitigate environmental impacts. This has positively impacted upon the quality of raw water whilst ensuring any deterioration of the natural environment is mitigated.

Our new SPRING Environmental Protection Scheme has built on previous success to further support arable farmers in the Blithe catchment area. We have made grants available towards the costs of voluntary on-farm infrastructural improvements and agricultural management schemes designed to protect the environment and improve water quality, such as contour cropping and pesticide sprayer wash-down.



We also work to deliver innovative projects that will enhance biodiversity across our region. The first round of funding from our PEBBLE fund (Projects that Explore Biodiversity Benefits in the Local Environment) has rewarded applications ranging from creating a wildlife walk, and clearing scrubland to supporting a school keen to raise awareness of the environment and local wildlife among pupils. The photographs to the left show a PEBBLE funded scheme that created a pond for wildlife at Leasowes.

Strategic Report – Financial Performance

Our Outcome Delivery Incentive (ODI) targets represent our commitment to deliver what our customers said was important to them in the last price review. The performance of our Directors' and Executive Team is measured against these, our budget for the year and the Final Determination as set by Ofwat. Key financial KPIs are used; these include but are not limited to:

- Turnover
- Operating costs
- EBITDA (excluding Infrastructure Renewals Expenditure)
- Operating profit
- Net debt
- Return on Capital Employed and Return on Equity
- Totex by price control (A regulatory financial KPI that combines operating and capital expenditure and is discussed in the Annual Performance Report Price Review and Segmental Reporting section on pages 118 to 126)

The budget is set as part of an annual process by combining the required regulatory and operational targets, and comparing to historical and predicted future performance. Performance against budget is monitored and actively managed on a monthly basis through reporting and presentation to the Directors and the Executive Team.

Financial performance

Turnover increased by £0.4m to £124.1m in 2017/18. Following our exit from the non-household retail market a reduction in the related retail income (2016/17: £2.9m) was offset by increased appointed turnover in existing markets in line with allowed regulatory uplifts from an RPI of 2.2% offset slightly by a negative K factor of -0.5%. We continue to see strong growth in the non-appointed side of our business with turnover of £5.2m (2016/17: £4.1m) driven by our Aqua Direct spring water business.

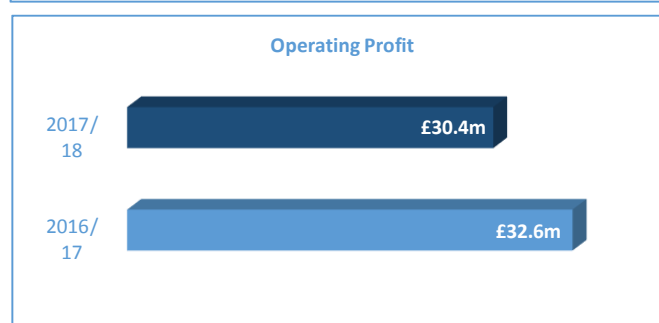
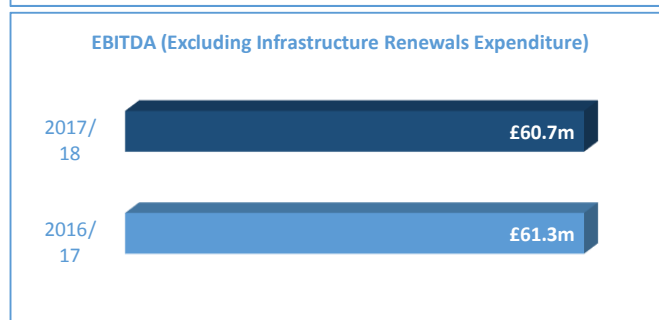
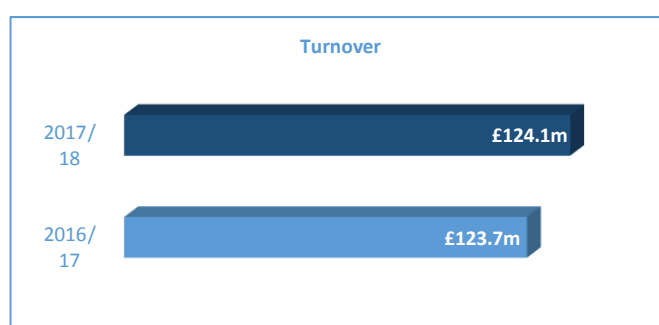
EBITDA (excluding Infrastructure Renewals Expenditure – see reconciliation below) was £60.7m (2016/17: £61.3m) a decrease of £0.6m. Operating profit was £30.4m (2016/17: £32.6m) a decrease of £2.2m. For both of these of profitability measures the exit from the non-household retail market contributed to the reduction (2016/17: EBITDA £1.8m, Operating Profit £1.7m). Higher power costs, leakage detection and repair, and the impact of costs relating to the 'Beast from the East' contributed to the EBITDA reduction with increases in infrastructure renewals and higher depreciation then adding to these to drive the reduction in Operating Profit. We are committed to the control of our cost base which increased by only 2.0% in the year in the face of upward inflationary pressure.

Finance charges of £11.7m in the year (2016/17: £12.2m) decreased by £0.5m due largely to a reduction in the indexation charges associated with our index linked debt.

The tax charge for the year was £3.3m (2016/17: £1.6m) an increase of £1.7m with the main reason being that the charge in 2016/17 was impacted by a reduction in the rate used to provide for deferred tax liabilities (from 18% to 17%) with no corresponding reduction in 2017/18.

On 1 April 2017 we exited the non-household retail market; as discussed above the comparable performance in the prior year was a turnover of £2.9m and operating profit of £1.7m.

Accounting policies are disclosed in note 1 to the financial statements on page 81.



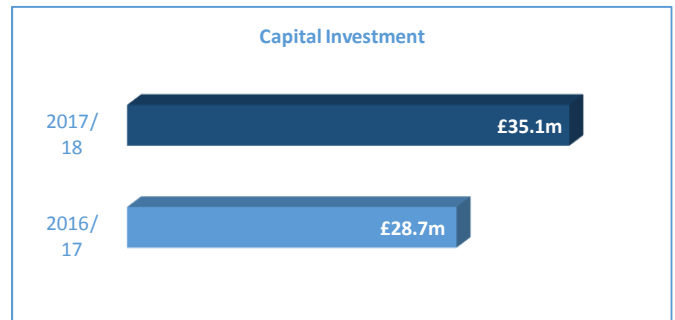
£m	2017/18	2016/17
Operating Profit	£30.4m	£32.6m
Depreciation : non-infrastructure assets	£19.1m	£18.8m
Depreciation : infrastructure assets	£3.6m	£3.5m
Infrastructure renewals expenditure	£10.1m	£8.7m
Amortisation of capital contributions	(2.4m)	(2.3m)
EBITDA (Excluding Infrastructure Renewals Expenditure)	£60.7m	£61.3m

Strategic Report – Financial Performance

Capital investment

We continued to make good progress in delivery of our capital programme, to ensure that our assets remain in good condition, and that we maintain stable asset serviceability and provide good quality, reliable water supplies to customers.

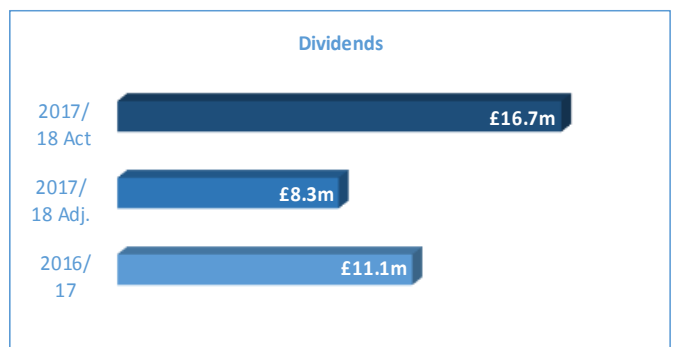
Wholesale appointed capital expenditure for the year was £35.1m (net of contributions and excluding infrastructure renewals expenditure), £5.7m above the Final Determination (FD) for the year. This reversed the under spend in the first two years of the AMP with expenditure expected in line with the FD in this 5 year AMP.



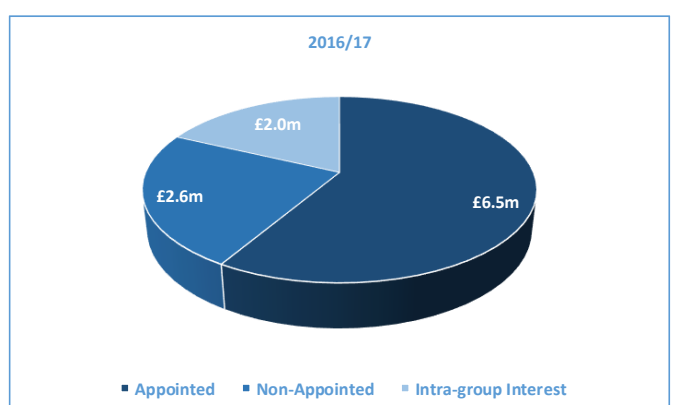
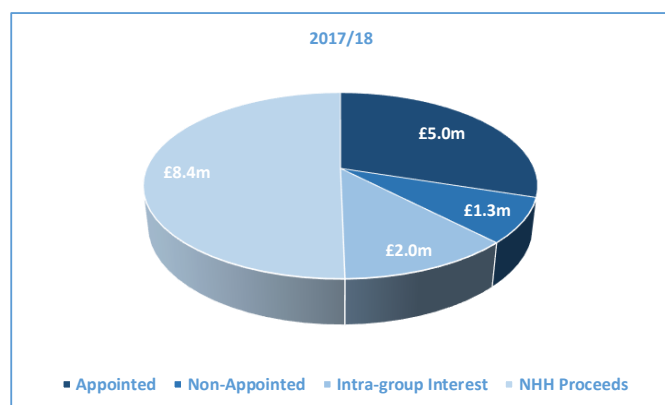
The level of expenditure reflected continued and increased focus on key treatment works to address water quality issues as agreed with the DWI, including the commencement of a UV installation at Hampton Loade Treatment works.

Dividend payment

Dividends paid during the year increased to £16.7m (2016/17: £11.1m). The dividend is made up of £5.0m paid from appointed profits (2016/17: £6.5m), £1.3m from non-appointed profits (2016/17: £2.6m), £2.0m to enable intra-group loan interest to be paid to the Company (2016/17: £2.0m) and a one off payment in the year of £8.4m in respect of the cash proceeds received from the sale of our non-household retail business.



The key driver of the total increase was the one off payment in relation to the disposal of our non-household retail business. Adjusting for this the underlying dividend was £8.3m (2017/18 Adj.), a decrease of £2.8m against the prior year driven by reductions of £1.5m in the appointed dividend and £1.3m in the non-appointed dividend. This is illustrated in the charts below.



The 2017/18 appointed dividend of £5.0m is less than that allowed in the FD and represents 4% of regulated equity.

Moving forward the Directors will continue to take a responsible approach in determining the levels of dividends to be paid.

Strategic Report – Financial Performance

Net debt and borrowing covenants

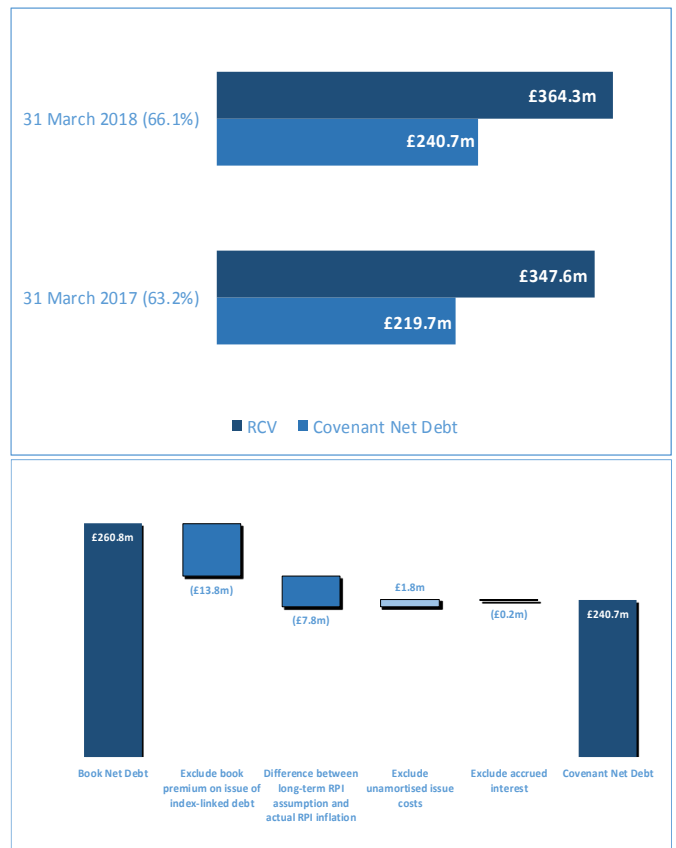
Net debt is inclusive of index linked debt, bank loans and debenture stock less cash.

For covenant reporting net debt was £240.7m at 31 March 2018 and represented a ratio of 66.1% of the Regulatory Capital Value (RCV) which was £364.3m at year end.

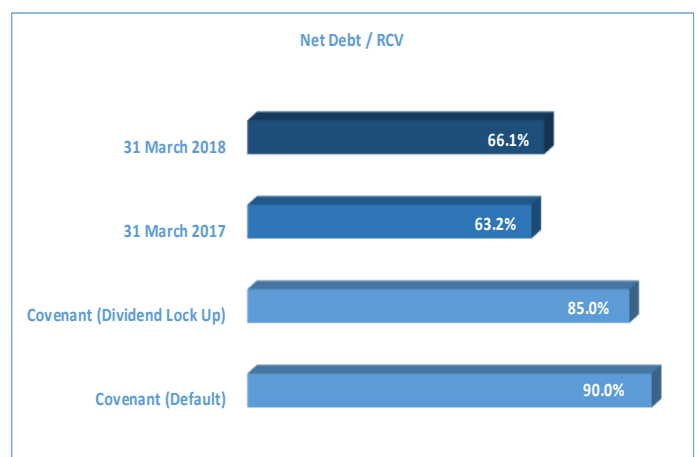
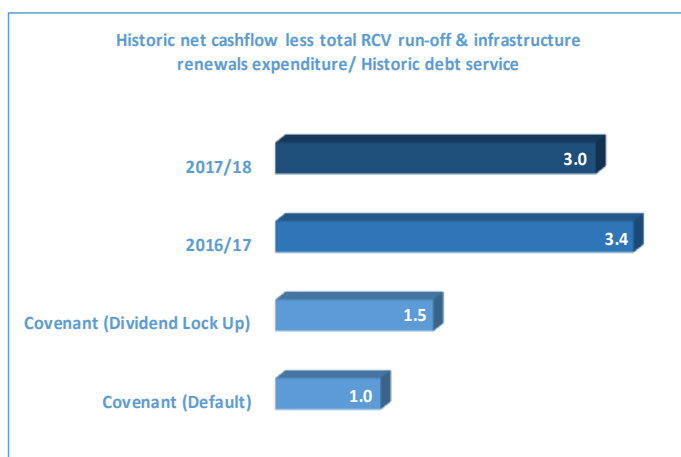
The RCV represents that from the PR14 Final Determination uplifted for inflation. The RPI value used this year at 31 March 2018 was 3.3% (March 2017: 3.1%).

The reconciliation between covenant net debt and book net debt is shown to the right and also in the notes to the accounts on page 80 along with a full analysis of our borrowings. The Directors target a net debt / RCV ratio of up to 66.0%.

We maintain significant headroom in respect of all of our borrowing covenants and liquidity with cash of £2,192,000 and undrawn facilities of £17,548,000 giving total liquidity headroom of £19,740,000.



There are two financial covenants relating to the Company’s borrowings in all borrowing agreements. These are set out below along with the actual ratios for 2017/18 and 2016/17 and show that there is significant headroom in both.



Standard and Poor’s continues to rate the Company as BBB+ with the Moody’s rating at Baa2. Both are well within investment grade.

Strategic Report – Financial Performance

Approach to tax

South Staffs Water takes the legal and social responsibilities for meeting its tax obligations seriously. We have no operations outside the United Kingdom, and therefore the following has specific reference to UK taxation only.

We are committed to complying with tax laws in a responsible manner, balancing obligations to the Government and the public with our duty to manage our affairs efficiently in order to deliver cost-effective services to customers while generating an economic return to investors. We make timely and accurate tax returns that reflect our fiscal obligations to the Government.

In particular we:

- Will not engage in aggressive tax planning and is not linked with commercial and economic activity
- Will not engage in artificial tax arrangements
- Will seek to maintain a transparent and collaborative relationship with HM Revenue & Customs, principally through our Customer Compliance Manager
- Will seek independent professional tax advice on material matters where the application of tax law is complex or uncertain

We will make use of applicable tax incentives provided by the Government within the terms outlined above. These may include, for example, preferential rates of capital allowances or enhanced tax relief for research and development costs and certain designated capital assets that add efficiency to our operations. Such incentives have been put in place to encourage appropriate business investment.

For our regulated water supply business, such incentives will generally have the effect of reducing customers' water bills under the funding model adopted by Ofwat, our economic regulator.

In addition to corporation tax, we contribute to the UK Exchequer by means of a number of other taxes and levies, including but not limited to:

- Employment taxes, National Insurance and the Apprenticeship Levy
- Carbon taxes and other energy-related taxes and levies
- Fuel duty and other vehicle-related taxes
- Business rates
- Regulatory charges and licences such as water abstraction charges

Our approach to risk management applies to tax as it does to other business areas, with escalation of key issues to the Board. Taxation compliance and advisory services are provided by our parent company, South Staffordshire Plc, which is responsible for identifying, assessing and managing tax risk across the entire Group. All material tax matters are discussed with our finance team and significant issues are escalated to the Board for consideration. The Group Internal Audit function will also review significant risk areas where considered appropriate.

We have identified economic uncertainty as a risk area. This includes risk in relation to the possibility of unexpected tax law and policy changes by the Government. South Staffordshire Plc carefully monitors published tax legislation, guidance and policy documents to ensure we can assess the compliance requirements and the economic implications for us. They also engage with HM Revenue & Customs on our behalf where our tax position is likely to be materially affected by policy changes.

Treasury policy

The main purpose of our financial instruments, including derivatives, is to finance operations and limit risk to fluctuations in external indices outside our control including, where considered appropriate, entering into floating to fixed interest rate swaps. Throughout this year and the previous year, our policy has been that no trading in financial instruments is undertaken. In respect of cash, loans receivable and borrowings our policy is to maintain flexibility with both fixed and floating rates of interest and long and short-term borrowings.

Strategic Report – Financial Performance

Transfer of non-household retail business

On 1 April 2017, we transferred our non-household retail operations and related assets to SSWB Ltd (SSWB), a fellow Group company for £8.4m and therefore exited the non-household retail water market on that date. There was no profit or loss on disposal.

On the same day our parent company, South Staffordshire Plc, transferred its 100% equity interest in SSWB to Pennon Water Services Ltd (PWS), in return for a 20% equity share in PWS. South West Water Ltd also transferred its non-household retail operations to PWS on the same day, forming a joint venture to operate in the non-household retail market.

In the year we operated as a wholesaler within the newly formed non-household market. We have acted in accordance with the required market rules and regulations to ensure that a competitive environment was created and maintained, and have ensured that all interactions with retailers were carried out at arm's length.

As the newly formed market has continued to develop throughout the year, we have contributed actively to market development and participated in consultations.

As reported on page 27 our non-household retail operations generated £2.9m turnover and £1.7m operating profit in 2016/17.

Strategic Report – Our Risk Review

We recognise that risks exist in all businesses and our approach to risk reflects our status as a regulated and licensed water undertaking providing essential public services. We accept that not all risks can be mitigated entirely but our aim is to ensure that risk management activities reduce the overall estimated impact of risks to a level that is considered to be acceptable and that does not impact on our long-term viability.

To facilitate the risk management process, every six months the Executive Team reviews our key business risks as identified and documented by senior managers. They consider the risks of the whole business and the proposed mitigating controls and procedures which are designed to reduce risks to an acceptable level. These risk are then presented to the Audit Committee for review, challenge and comment with any agreed actions passed on to the relevant senior manager, and any significant issues escalated to the Board.

The objective of this risk management process is to:

- Ensure that the Executive Team is able to identify and prioritise all key business risks
- Implement appropriate procedures and controls to mitigate risks to an acceptable level
- Enable senior managers to highlight, document, prioritise and execute any identified actions

Each risk identified is assessed and scored against two factors:

- The impact on the business
- The likelihood of this risk occurring

Risk Matrix

Probability ↑	Certain	5	10	15	20	25
		4	8	12	16	20
		3	6	9	12	15
		2	4	6	8	10
	Rare	1	2	3	4	5
		Negligible	→			Extreme
			Impact			

The impact assessment considers the estimated consequences of the risk on our net assets, but other factors such as loss of trust of customers, reputation and brand erosion are also taken into account. The overall risk rating is determined by taking the product of the impact and probability scores (impact x probability).

The score between 1 (lowest risk) to 25 (highest risk) allows us to focus on the most important risks.

Where the assessment of the risk score changes between six monthly assessments, this is highlighted to the Executive Team and Audit Committee with recommended actions.

Strategic Report – Our Risk Review

Key risks

The following section lists our key risks, as identified using the process described, and details what each risk means for us, the actions we are taking to mitigate the impacts and any change in risk.

1.	What is the risk	Business Plan for 2020 to 2025
	What does it mean for us?	<p>There are a number of strategic and regulatory challenges in our Business Plan:</p> <ul style="list-style-type: none"> • Water resources, water quality and network resilience • The achievement of a 15% leakage reduction • Delivering against challenging performance commitments • Rewards and penalties creating possible volatility in customer bills • Cost of customer debt • Embedded debt • Improving customer service to developers • Achieving a successful determination • Financing large capex spend with a low weighted average cost of capital
	How are we managing the risk?	<p>The Business Plan is being led by a dedicated project team, business managers and a steering group with in depth Board engagement at every stage and an independent specialist assurance partner closely involved. As part of the process we are:</p> <ul style="list-style-type: none"> • Undertaking a high level of customer engagement, capturing all insights to shape the plan. The Customer Panel plays a key role in this process • Fully utilising customer ‘willingness to pay data’ along with other customer insight to develop our totex programme • Engaging specialist skilled resource in the fields of customer engagement and report presentation • Liaising with advisors in respect of mitigating the impact of the relatively high cost of embedded index-linked debt • Applying lessons learned from the 2015 to 2020 process ensuring that our submission is proactively developed and fully compliant • Stress testing financial metrics against severe plausible and realistic scenarios • Increasing the scope for external assurance partners
	Changes in risk score	↔
2.	What is the risk	Water Quality
	What does it mean for us?	<p>In delivering the highest quality water Seedy Mill and Hampton Loade have suffered historically from some water quality and compliance issues. Further failures could result in:</p> <ul style="list-style-type: none"> • Not delivering the highest quality water as demanded by our customers • Public health safeguarding measures such as boil orders or removing assets from supply resulting in customer service impact • Regulatory pressure • Adverse public relations affecting trust and confidence • Significant cost
	How are we managing the risk?	<p>Significant work has been undertaken at both treatment works to mitigate risks:</p> <ul style="list-style-type: none"> • Continued with extensive internal and external reviews • Since April 2016 all water leaving Seedy Mill has been subject to an additional treatment process (UV) • UV treatment is in the process of being installed at Hampton Loade, with investigations ongoing as to the most appropriate long term solution • The business is engaging with regulators in terms of our long term plans for both our major treatment works
	Changes in risk score	↔

Strategic Report – Our Risk Review

3.	What is the risk	Health and Safety
	What does it mean for us?	Risks associated with health and safety include: <ul style="list-style-type: none"> • Injury and fatality to employees and others • Non-compliance prosecutions • External investigations • Employer brand and reputational damage
	How are we managing the risk?	In a continued drive to improve accident rates and reduce risk we are: <ul style="list-style-type: none"> • Continuing to drive a culture that puts health and safety first • Fully utilising the Group Incident and Accident Database • Demanding prompt hazard identification and reporting • Conducting health and safety strategic working groups • Undertaking Senior Management and Director site and work audits We have an aspirational goal of achieving a zero injury workplace.
	Changes in risk score	↔
4.	What is the risk	Systems Availability and Cyber Security
	What does it mean for us?	The loss of critical IT infrastructure could have a major business impact with risk around: <ul style="list-style-type: none"> • Cyber-attack resulting in any or all of the following • External failures (loss of communication links, power, or internet) • System failures (failure of hardware or software and reduced performance) • Data integrity (including loss or corruption) • Lack of access to technical skills
	How are we managing the risk?	Group and Company Information Security Steering Groups work in tandem to focus on protecting the business and drive improvements through: <ul style="list-style-type: none"> • The creation of an Information Security Control team • Delivering a strategy to improve resilience, security and agility • Our IT services provider has received ISO 27001 certification • Updates of all server software to current levels • Continued engagement in national and international industry forums • Provision of information security awareness training • Involvement in an Network Information Security (NIS) pilot programme
	Changes in risk score	↔
5.	What is the risk	Data Security and Privacy
	What does it mean for us?	The security of our customers' and employees' data has always been a key area of focus with risk around: <ul style="list-style-type: none"> • Loss of or restricted access to data leading to loss of trust from our customers and employees, and reputational damage • Compliance with the required GDPR regulations around the increased data protection for individuals, and avoidance of penalties or reputational damage • Continued Ofwat emphasis on the need for confidence and assurance in data provided
	How are we managing the risk?	In order to understand and drive compliance in this area we: <ul style="list-style-type: none"> • Enacted a GDPR project that has delivered phase one and we will closely monitor compliance going forward • We have rolled out training on GDPR and data security for all employees alongside a Companywide communication campaign
	Changes in risk score	↔

Strategic Report – Our Risk Review

6.	What is the risk	Asset Reliability and Resilience
	What does it mean for us?	The reliability and resilience of our assets could cause risks around: <ul style="list-style-type: none"> • Delivery capacity for investments • Additional expenditure required but not included in the Business Plan • Not achieving the required Outcome Delivery Incentives (ODIs) for secure and reliable supplies
	How are we managing the risk?	Long term plans are being considered in the wider context of managing and maintaining our assets and supply capabilities. From these we have: <ul style="list-style-type: none"> • Undertaken significant investment expenditure on a UV plant at Seedy Mill with further similar activity underway at Hampton Loade • Accommodated significant expenditure on non-infrastructure assets, specifically our water treatment works, by reducing planned expenditure on underground assets and in other areas with limited risk deterioration in the service these assets provide • Established preferred portfolios for the 2020 to 2025 Business Plan with preparatory activity to be undertaken before 2020
	Changes in risk score	↔

7.	What is the risk	Leakage
	What does it mean for us?	Leakage plays a significant part in our supply / demand position and has been defined as high priority by our customers and Ofwat with these specific risks being: <ul style="list-style-type: none"> • Poor performance would have a negative impact on our reputation with both regulators and our customers • A need to deliver at least a 15% leakage reduction commitment by 2025 • Failure to deliver on ODI commitments leading to penalty scenarios and fines from Ofwat
	How are we managing the risk?	Due to the significance of leakage performance we: <ul style="list-style-type: none"> • Report our current performance monthly and forecast positions going forward to the Board on a monthly basis • Continue to invest in additional leakage resource across both regions • Strive to be innovative in our detection methods • Detailed water resources management plan (WRMP) • Have approved further investment in network monitoring sensors and other technology
	Changes in risk score	↑

8.	What is the risk	Regulatory Environment
	What does it mean for us?	Risks within the regulatory environment include but are not limited to: <ul style="list-style-type: none"> • Not meeting our Outcome Delivery Incentives (ODIs) or the required disclosures and assurance within the Company Monitoring Framework • Increased developer activity and costs affecting contributions • Our gearing position relative to Ofwat expectations • Meeting changing regulatory expectations particularly regarding governance • Ensuring annual charges comply with legal obligations
	How are we managing the risk?	To mitigate and manage the risk in the regulatory environment we have: <ul style="list-style-type: none"> • Established an ODI monitoring system that is reported monthly to the Board • Published an assessment of our risks, strengths and weaknesses for consultation • Engaged with Ofwat regarding developer contributions • Engaging with Ofwat regarding gearing expectations and governance • Followed the charging rules set out in our 'Instrument of Appointment'
	Changes in risk score	↔

Strategic Report – Our Risk Review

9.	What is the risk	Customer
	What does it mean for us?	The impact of changing customer requirements may lead to: <ul style="list-style-type: none"> • Failure to meet customer expectations • Failure to comply with non-household market rules • A reduction in SIM scores and poor performance regarding complaints • Increased levels of customer debt
	How are we managing the risk?	In mitigating the customer risk we have: <ul style="list-style-type: none"> • Operated in a compliant manner within the non-household market • Made further investment in order to improve customer service following a year of significant change • SIM insight addressed at weekly meetings and monthly at an Executive Steering group • Revised our governance and reporting structure in debt management and proposed investment in new systems in this area • Significantly increased customer engagement with oversight through the Customer Panel
	Changes in risk score	↔
10.	What is the risk	Business Processes
	What does it mean for us?	The direction of the industry in the future has necessitated changes in processes and operational structures that could give rise to risks around: <ul style="list-style-type: none"> • Non-compliance with market rules and requirements • Changes to our wholesale operation to remain efficient • Changes to our household retail operation to remain efficient
	How are we managing the risk?	Business processes have been changed to fit with market requirements and we have: <ul style="list-style-type: none"> • Introduced a Wholesale Portal and Wholesale Service Desk. • Delivered training to all key staff on the required processes and delivery timeframes • Put service measures in place which are monitored weekly • Identified that similar approaches need to be taken as new business process changes are identified, delivered and put into day to day operation across wholesale and retail
	Changes in risk score	↔
11.	What is the risk	Water Resources
	What does it mean for us?	Including reforms being proposed to the upstream market and to abstraction licences key risks are: <ul style="list-style-type: none"> • Abstraction licences being capped at recent actual usage levels • Reductions in abstraction volumes • Pressure on groundwater body status • Population growth • Revised Environment Agency policy for renewal of 'Time-limited' licences • Requirements from our drought plans
	How are we managing the risk?	In order to mitigate the risk and feed into Business Planning for 2020 to 2025 we are: <ul style="list-style-type: none"> • Keeping abreast of consultation documents on upstream market and abstraction reform attending all relevant industry workshops and seminars • Engaging and working with the Environment Agency around sustainable abstractions • Completing a full range of demand management, resources and trading options as part of our long term planning (WRMP) • Maintaining robust plans for water resources and drought management
	Changes in risk score	↓

Strategic Report – Our Risk Review

12.	What is the risk	Financial
	What does it mean for us?	<p>We currently face a number of financial risks based around:</p> <ul style="list-style-type: none"> • Wholesale revenue restrictions • The ODI risk and reward mechanism • Increasing power costs • A required reduction to household retail costs • Operating within the requirements of the market • A high level of fixed cost embedded debt
	How are we managing the risk?	<p>In order to mitigate financial risk we have:</p> <ul style="list-style-type: none"> • A strong focus on, and a culture of, cost control • Ensured that ODIs are used as operational decision making tools and are monitored monthly at Board level • Generated a longer term strategic view on power costs with a project around use of gas powered generation approved by the Board • Reduced retail costs in line with expectations • Acquired key knowledge on level playing field expectations, maintaining good relationships with external retailers and the market representatives • Committed to the submission of a strong Business Plan with full customer support • Engaged with external advisors on options for reducing our cost of embedded debt
	Changes in risk score	↔

13.	What is the risk	Skills
	What does it mean for us?	<p>Our Business Planning focus introduces a changing priority for our people and our skills requirements which will encompass:</p> <ul style="list-style-type: none"> • Different skills being needed to meet our longer term requirements • Innovation, efficiency and resilience driving a need for changing skill sets and increased flexibility in our workforce • Increased resilience in our operations
	How are we managing the risk?	<p>The Executive Team is planning the future shape of the business and has:</p> <ul style="list-style-type: none"> • A strategic succession plan in place • Created a Senior and Middle Manager Development Programme and an Apprenticeship Framework • Developed new organisational structures across the business • Started to change the Customer Service and Retail structures to drive efficiency • Strengthened employee skills through the Energy and Utility Skills Register (EUSR) and exploring opportunities funded through the apprenticeship levy
	Changes in risk score	↔

Strategic Report – Our Risk Review

14.	What is the risk	Environmental
	What does it mean for us?	<p>The business has a number of environmental obligations and reputational outcomes to comply with including:</p> <ul style="list-style-type: none"> • Customer expectations • Water Industry National Environment Programme (WINEP) • 2015 to 2020 catchment management obligations • Adherence to and renewal of abstraction licences • Minimising pollution incidents from mains flushing and burst main events • Maintaining efficient levels of per capita consumption • An obligation to look after our environment
	How are we managing the risk?	<p>In order to deliver on our environmental obligations we are:</p> <ul style="list-style-type: none"> • Engaging with customers and other stakeholders and responding to their expectations • Continuing to work on delivering WINEP • Through our catchment management team: <ul style="list-style-type: none"> • Engaging with farmers around pesticide use • Working jointly with Severn Trent in the Severn catchment • Working to align catchment management for ground water to DWI expectations and developing our proposals for the 2020 to 2025 Business Plan. • Monitoring abstraction licence usage regularly • Taking sample discharges to give early warning of potential pollution failure • Monitoring water efficiency and biodiversity through monthly ODI reporting • Measuring against ODIs on biodiversity and carbon
	Changes in risk score	↔

Brexit

Following the vote by the UK in June 2016 to leave the European Union (EU) the country is expecting to exit the EU in March 2019. Whilst the business has limited trading with the EU and therefore limited risk, the impact on the Company is most likely to arise from changes in macroeconomic conditions, in particular but not limited to, inflation and interest rates changes and availability and the terms of capital funding.

Strategic Report – Long Term Viability

As part of the PR19 process we have prepared a detailed Business Plan which identifies our strategic objectives, operational plans and the key business issues that we face up to 2025 and beyond. This has been created with the support and engagement of our customers and other stakeholders and is now in the final stages of approval prior to submission. We also of course have a detailed awareness of the factors that will affect us up to 2020, and of our associated plans and activities.

The Company's detailed planning process extends to March 2025 which is the end of the regulatory price control period covered by PR19 (plus the remaining years of PR14). The period to March 2025 has been selected as it includes the remainder of the current price control which is relatively predictable plus the full five years of the next price control. This combined period is considered to be appropriate for a long-term regulated business that provides an essential public service and invests for the long-term.

We have also modelled scenarios for the five years to March 2030. This modelling relies on some very broad assumptions, however as stated in our Long Term Viability Statement on pages 39 to 40, we also have confidence that the regulatory system under which South Staffs is licensed will ensure that we remain financeable in future periods provided we operate our business efficiently and Ofwat continues to make proportionate decisions regarding WACC and other key factors.

Based on detailed planning, we have prepared financial forecasts up to March 2025, which reflect our stated and anticipated strategic objectives and operational plans. These include trading forecasts comprising turnover, operating and capital maintenance costs, cash flow projections including operating cash flows, the planned investment programme, tax and finance related cash flows. The level of net debt is also projected through the period and is compared to the level of gearing as permitted in the Company's borrowing covenants as is interest cover and the return to investors.

In order to assess the long-term viability and financial resilience of the Company to possible changing circumstances, stresses have been applied to these financial forecasts to assess the impact on profitability, cash flows, liquidity, borrowing capacity, credit ratings and compliance with borrowing covenants of a number of severe but plausible and reasonable adverse changes to the most important assumptions made within the base projections. Tests on key exposures around capital investment, operational costs, and inflation and interest rate fluctuations were performed as in previous years as they are important in our risk management processes.

We have also specifically considered the following scenarios set out by Ofwat in its "Putting the sector back in balance" consultation:

- Totex underperformance (15% of totex)
- ODI penalty (3% of RORE) in one year
- Inflation set above/below the independent forecasts for the UK economy as published by Treasury (3% above/below)
- Increase in level of bad debt (20%)
- Debt refinanced as it matures, and new debt financed as required at 2% above the forward projections
- Financial penalty – equivalent to 3% on one year Appointee turnover
- Any relevant intercompany financing scenarios

A combined scenario has also been modelled considering underperformance of totex and retail expenditure of 10% in each year of the price control, an ODI penalty equivalent to 1.5% of RORE in each year and a financial penalty equivalent to 1% of revenue in one year.

We recognise that in its July decision Ofwat has amended a number of the above scenarios; we have decided not to change our stress testing as none of the amendments make the scenarios any more severe.

These scenarios have been modelled taking account of the key risks we face as a business; these are set out in detail on pages 32 to 38. The financial impact of the majority of the key risks identified would effectively create a totex underperformance, some plausible examples by risk category are:

- A Final Determination which does not fully address the requirements highlighted and supported by our customers
- Redirecting capital and operating expenditure to address water quality issues
- Cyber-attack leading to loss of operational capability or data
- Breach of GDPR rules leading to financial penalty
- Expenditure required beyond expectations to ensure asset resilience

Strategic Report – Long Term Viability

- Further expenditure required to secure reduced leakage levels
- An Ofwat decision to adjust the level of developer contributions received
- Performance below customer expectations (ODI impact)

The Board has considered the impact of these stress tests on our ability to maintain key financial metrics including our credit ratings with Moody's and Standard & Poor's and our ability to service debt. Clearly where extra expenditure is required, these metrics are placed under pressure therefore, where appropriate, mitigating actions have also been modelled and considered as part of this process. The key mitigations considered were:

- Re-prioritisation of totex
- Reduction in dividend
- Equity injection
- Use of financial levers
- Outperformance of either cost or service performance in AMP7

Based on the financial projections, the stress tests performed and the mitigations available, the Board has made a declaration on page 145 that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to March 2025 and that this is expected to be the case beyond that point (not tested). This expectation is based on the realistic assumption that the Company continues to have its existing access to capital markets to fund its required investment programme and provide sufficient liquidity.

The majority of the specialist work required to form this Board level expectation has been performed in-house with review and oversight from the Audit Committee and Board. Independent (Group) Internal Audit has cross checked calculations and in addition, following a reassessment of the risk (compared to last year) under our Assurance Framework a third party, Jacobs U.K. Limited (Jacobs) has been used to validate both the calculations and the basis of our testing.

Strategic Report – Company Direction and Performance Statement

This short statement sets out how we are delivering for our customers and how our customers are central to everything we do, including the setting of our targets and aspirations.

Our primary operational targets are broadly those proposed to Ofwat (our economic regulator) in the Business Planning process for 2015 to 2020, and approved as part of our Final Determination for this period. These targets are known as Outcome Delivery Incentives (ODIs) and are grouped under a series of five “Outcomes” designed to benefit our customers and stakeholders. We report specifically on these on pages 9 to 16, some carry a financial reward or penalty and all were developed following significant customer engagement. Our ODIs are underpinned by many other operating targets which are set annually as part of our financial and operating budget setting process. All targets are set to ensure we maintain our ability to meet customer needs today and in the future. They are based on the Ofwat Final Determination, and are fine-tuned through constant customer engagement. As would be expected, in addition to the customer focus we are required to outperform our ODI targets whilst also delivering shareholder returns, ensuring capital investment takes place and operating as an efficient business across all price controls (currently Wholesale and Retail Household). We also have some non-regulated aspects to our business which are managed under a similar framework.

Each year our Executive Team proposes targets based on detailed knowledge of our customer needs and our operational requirements; our Board, led by the independent non-executive members uses its expertise and insight to challenge the targets we propose. Detailed discussion follows based on customer views, forecasts, outcomes to date and future expectations in order to agree the way forward. The subjects covered by the Board this year are set out on page 142. This process is constant, but reaches an annual conclusion in April each year. Variances from customer expectations, annual targets and the Ofwat Final Determination are strongly challenged throughout the year, with plans required to get back on track if there are shortfalls.

To ensure that customer and stakeholder expectations are met within both annual performance and target setting, the Executive Team are held to account by the independent non-executive Board members who have specific relevant expertise. Sir James Perowne has extensive strategic and customer service experience, Keith Harris has a strong financial and regulatory background and Stephen Kay is an engineer who has led a water company.

To ensure that our customers have visibility of the decisions we make and our performance through the year, we report monthly via our customer dashboard. This allows our customers to hold us to account constantly, and see where we are improving or failing, and makes us all the more aware of their views. A snapshot of the dashboard is shown on page 7.

We believe that our targets are stretching, as evidenced by the challenges that we have faced in delivering against all of them. The year overall has seen progress in some areas and setbacks in others, we have not managed to achieve all targets this year, however that has not reduced either our determination to do so next year or the increasing level of challenge in each target set. How we are performing against our targets is set out in detail on pages 9 to 16 and summarised below. Our proposed targets for 2020 to 2025 are still to be submitted to and reviewed by Ofwat; they are in the final stages of challenge by our Board and our customers, a process that will ensure our required performance is stretching.

Leakage – despite additional resources being deployed for the majority of the year, we entered the freeze-thaw event in March without margin for error in either region. The resultant bursts on the network both in terms of our assets and those of our customers resulted in a full year leakage ODI penalty in our Cambridge region whilst we were in the penalty dead band for South Staffs. However, we start the New Year with more leakage resources and an agreed investment in increased smart network monitoring. We anticipate that we will continue to deploy additional resources until it is proven that the investment in ‘working smarter’ is reaping its anticipated benefits.

Supply Interruptions – following two very strong years of performance we have experienced four notable incidents over the course of the year and in doing so demonstrated that this measure can be vulnerable to sudden change. In light of this we have adopted a ‘zero planned interruption’ approach to our own works in order to create a greater buffer against unforeseen events. We still achieved a performance reward by delivering 8:32 against a target of ten minutes.

Water Quality – we are pleased to have delivered a further reduction in customer contacts from 1.66 to 1.42 contacts per 1,000 of population. Unfortunately this resulted in a penalty due to the tightening of the target to 1.23. Our performance under MZC has been reasonable again.

SIM – we have made some progress towards recovering our historically upper quartile SIM position. In the latest Ofwat published full year qualitative SIM rankings we were 9 with a score of 4.44 against an industry average of 4.40 (highest 4.52, lowest 4.16). Due to the bunching of scores we were 0.04 points away from a top 4 position. We have improved our qualitative

Strategic Report – Company Direction and Performance Statement

ranking from 13 in 2016/17 and await the quantitative element (25%) and would expect a small improvement based on past experience. The final results are not confirmed until August.

Complaints – this year has seen extremely positive progress on reducing customer complaint levels. In our Cambridge region complaints have reduced from 460 to 288 and in the Midlands they have reduced from 924 to 591, a position that should see us close to top in the industry.

Health and Safety – we are delighted to see measurable progress on health and safety performance. Our underlying ‘all accident’ measure has reached its lowest level for many years with 10 accidents in the business through the year (18 in 2016/17). We continue to strive for zero.

The ‘Beast from the East’ – March brought about the most significant freeze thaw weather event since 2010. It is pleasing to report that through the hard work of our people, often in very challenging conditions, we delivered strong performance in the way we managed and recovered from the event. For those customers affected, we paid compensation directly to them swiftly. Following an industry wide investigation, Ofwat noted that we performed well and largely met our customers’ expectations, but that there was still room for improvement.

The performance of our business is directly reflected in the level of remuneration received by our Executive Team including Phil Newland, our Managing Director. Details are provided on page 63 but in principle, the maximum bonus payable is based on a percentage of salary, the percentage paid is lower if targets are not met. This year, the average percentage paid was 36% reflecting a year where some targets were achieved and some missed.

The industry as a whole has operated under significant political pressure throughout the year and while South Staffs is generally seen as a well-run, responsible business we are impacted by the wider sentiment towards the sector and must be continually mindful of it. Our particular areas of focus have been around governance (details on pages 43 to 64), transparency where we believe that our engagement with our customers and our reporting particularly through our dashboard is amongst those leading the industry, dividend policy (details on page 144) and the link between executive pay and performance which is detailed above. How we address these concerns combined of course with how we deliver our services is key to making sure our customers are central to everything we do.

The Strategic Report on pages 5 to 42 is approved on behalf of the Board of Directors.

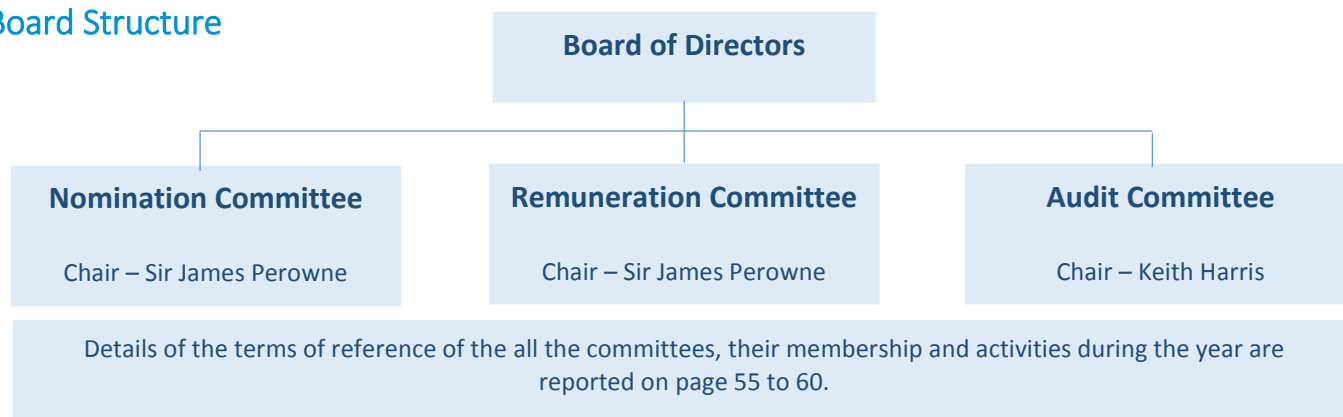
The Directors, in preparing this Strategic Report, have complied with s414C of the Companies Act 2006.



Phil Newland
Managing Director
13 July 2018

Our Governance – Board, Directors and Executive Team

Board Structure



Board of Directors

During the year the Board comprised the Independent Chair, one Executive Director (the Managing Director), the Group Chief Executive and four other Non-Executive Directors. Two of the other Non-Executive Directors were considered to be independent in addition to the Independent Chair. The largest single group of Directors on the Board during the year was that of Independent Non-Executive Directors, including the Independent Chair.



Sir James Perowne – Independent Non-Executive Chair

Appointed Independent Chairman in April 2017, and an Independent Non-Executive Director since January 2011. Sir James spent 37 years in the Royal Navy where he was appointed Flag Officer Submarines in 1996 and also served as Deputy Supreme Allied Commander Atlantic in NATO. He was Chairman of the Central Region of the Consumer Council for Water serving for 8 years prior to joining South Staffordshire Water and brings strong customer and strategic insight experience to the Board.

External Appointments

Constable and Governor of Windsor Castle; President of Submariners Association; Trustee of British Forces Foundation; President of ARNO/RNBSO.



Phil Newland – Managing Director

Appointed as Managing Director in April 2014. From 2006 Phil worked within the South Staffordshire Plc Group as Managing Director of Echo Managed Services Ltd supplying technology and retail services to the water industry. Previously Phil was a Management Consultant with Automatic Data Processing (ADP) and Terence Chapman Associates.

External Appointments

Director Pennon Water Services Ltd



Adrian Page – Group Chief Executive South Staffordshire Plc

Appointed as a Director in July 1998. Adrian was appointed as Group Chief Executive for South Staffordshire Plc in January 2013 having been Group Finance Director since April 2004. Previously he was Group Finance Director of South Staffordshire Group Plc from 1998 to 2002 and with ACT Group and KPMG.

External Appointments

Director Pennon Water Services Ltd; Director of the Water Companies Pension Scheme Trustee Company

Our Governance – Board, Directors and Executive Team



Keith Harris – Independent Non-Executive Director

Appointed as an Independent Non-Executive Director in April 2015. Keith is the owner of the advisory business LorraineHouse and spent 20 years at Wessex Water, including a period of time at ENRON / AZURIX where he was global Head of Regulation. At Wessex Water he held various senior executive and Board positions, including CFO and deputy CEO, and brings strong financial and regulatory experience to the Board.

External Appointments

Independent Non-Executive Director of Ervia the parent company of Irish Water; Advisory Board member of private equity firm Buckthorn Partners.



Stephen Kay – Independent Non-Executive Director

Appointed as an Independent Non-Executive Director in April 2013. Stephen is a Chartered Engineer who has spent his career in the water industry both in the UK and internationally. He was the Managing Director of Cambridge Water PLC until March 2013 and brings strong water industry, engineering and compliance experience to the Board.

External Appointments

Independent Non-Executive Director of Jersey New Waterworks Company; Chairman of the Water Regulations Advisory Service; Chairman of the Water UK Technical Standards Board; Director of the Water Companies Pension Scheme Trustee Company; Trustee of the Arthur Rank Hospice Charity.



Ram Kumar – Non-Executive Director and KKR Representative (Resigned 3 July 2018)

Appointed as a Director in July 2013. Ram is an Engineer who joined KKR in 2009 and is a Director in the European Infrastructure team. He is also a Non-Executive Director of South Staffordshire Plc. Prior to joining KKR, he worked at Goldman Sachs for nearly seven years across mergers and acquisitions, leveraged and structured finance and infrastructure investments.



Ryan Miller – Non-Executive Director and KKR Representative (Resigned 3 July 2018)

Appointed as a Director in November 2017. Ryan joined KKR in 2016 and is a member of the Energy & Infrastructure team. He is also a Director of South Staffordshire Plc. Prior to joining KKR, he was the commercial manager at Genel Energy, and a London listed oil and Gas Company with assets in the Kurdistan Region of Iraq and Africa.

As part of the sale of their 75% interest in the Group by the Global infrastructure fund of KKR and its co-investors, Ram Kumar and Ryan Miller stepped down from their Board positions on 3 July 2018. Further appointments to the Board are expected to be made in due course.

Our Governance – Board, Directors and Executive Team

Executive Team



Tim Orange – Finance, Regulation and Business Services Director

Tim joined Cambridge Water in March 2009 and South Staffs Water in April 2013. Tim has responsibility for the financial performance of the business. He graduated in geography from Downing College, Cambridge and went on to train as a chartered accountant with Grant Thornton. After four years in the British Virgin Islands with Deloitte, he returned to work for Scottish & Newcastle, ntl and more recently Enviros, an environmental consultancy.



Pete Aspley – Wholesale Director

Pete has a well-established background within the water industry having previously worked in South Staffs Water and then within the South Staffordshire Plc Group for 27 years. In 2004 he set up and became Managing Director of Integrated Water Services Ltd (IWS), a Group company providing a wide range of specialist support services to water and related industries. Pete re-joined South Staffs Water in 2015.



Marcella Nash – Director of Human Resources

Marcella was appointed in January 2014 previously having worked within South Staffordshire Plc Group as Head of Human Resources for Echo Managed Services Ltd. Prior to this she was a Senior HR Manager in Severn Trent Group and Severn Trent Water.

Our Governance – Directors’ Report

The Directors are pleased to present their report and accounts for the year ended 31 March 2018. The Directors confirm that they consider the report and accounts to be fairly presented and understandable. It provides the shareholders and other stakeholders with the necessary information to assess the Company’s performance for the year ended 31 March 2018, the Company’s business model and its strategy.

Directors

The Directors who held office during the year and subsequently, along with the number of Board meetings attended by each Director, while holding office during the year, are as follows:

Director	Director Type	Date Appointed	Date Resigned	Meeting Attendance
Sir James Perowne	Independent Non-Executive Chairman	01/01/2011		9/9
Phil Newland	Managing Director	01/04/2014		9/9
Adrian Page	Group Chief Executive – South Staffordshire Plc.	01/07/1998		9/9
Ram Kumar	Non-Executive Director	30/07/2013	03/07/2018	9/9
Oleg Shamovsky	Non-Executive Director	31/07/2015	30/11/2017	3/5
Ryan Miller	Non-Executive Director	30/11/2017	03/07/2018	4/4
Keith Harris	Independent Non-Executive Director	30/04/2015		9/9
Stephen Kay	Independent Non-Executive Director	01/04/2013		9/9

No Director had any material interest in any contract of significance with the Company.

As part of the sale of their 75% interest in the Group by the Global infrastructure fund of KKR and its co-investors, Ram Kumar and Ryan Miller stepped down from their Board positions on 3 July 2018. Further appointments to the Board are expected to be made in due course.

The details of the sale noted above are contained in note 24 of the financial statements on page 103.

Financial results

The Company’s financial results are shown in the accounts on pages 74 to 103 and in pages 27 and 31 of the Strategic Report.

Dividends of £16.7m were paid during the year (2016/17: £11.1m), including appointed dividends of £5.0m (2017: £6.5m). A breakdown of the dividend payment for the year along with a comparison to the prior period is contained in the Financial Performance section of the Strategic Report on page 28.

Details of future developments can be found within the Strategic Report on pages 5 and 42

Payment of creditors and commercial arrangements

The Company’s policy is to pay suppliers in line with the terms of payment agreed with each of them, when contracting for their products or services. Trade creditors at 31 March 2018 represent 51 days (31 March 2017: 56 days) of purchases. The Company is not reliant on any single commercial arrangement.

No political donations were made during the financial year (2017: Nil).

Our Governance – Directors' Report

Corporate social responsibility

South Staffordshire Water PLC regards the implementation of responsible social and ethical standards and the health, safety, wellbeing and fair treatment of its employees, including disabled persons, as fundamental to the Company. Compliance with relevant environmental laws is also integral.

The Company has an equal opportunities and non-discrimination policy. Every reasonable effort is made to provide disabled people with equal opportunities for employment, training and promotion.

The Company places considerable value on the engagement of its employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the performance of the Company. This is achieved through formal and informal meetings and a regular Conduit emailed to colleagues. Employee representatives are consulted regularly on a wide range of matters affecting their current and future interests through our Information Consultation and Communication (ICC) forum. Further details regarding our people can be found on pages 23 to 25 of the Strategic Report.

We consider human rights issues not to be a material risk for the business, due to existing regulatory requirements in the UK and the nature of our supply chain.

Further information on the Company's corporate social responsibility activities is provided in the Strategic Report on pages 6 to 42.

Corporate governance

A detailed report on Corporate Governance is set out on pages 48 to 60. The Group structure is shown in charts on pages 48 to 50 and accompanying paragraphs on page 49, including changes to the structure since 31 March 2018 but before approval of this report.

Risk management

The Company's practices in respect of risk management are provided on pages 32 and 38 of the Strategic Report.

Going concern

The Company's statement on Going Concern and the basis for the Going Concern Assumption are provided on page 54.

Independent Auditor

In accordance with the provisions of s418 of the Companies Act 2006, the Directors confirm that, as far as they are aware, there is no relevant audit information of which the Company's auditor is unaware. The Board has taken all reasonable steps to make itself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

A resolution proposing the reappointment of Deloitte LLP as independent auditor will be put to the Board.

Approved by the Board and signed on its behalf by:



J.R. Goodwin

Company Secretary

13 July 2018

Registered Office: Green Lane, Walsall, West Midlands, WS2 7PD

Registered in England and Wales, number 2662742

Our Governance – Corporate Governance Report

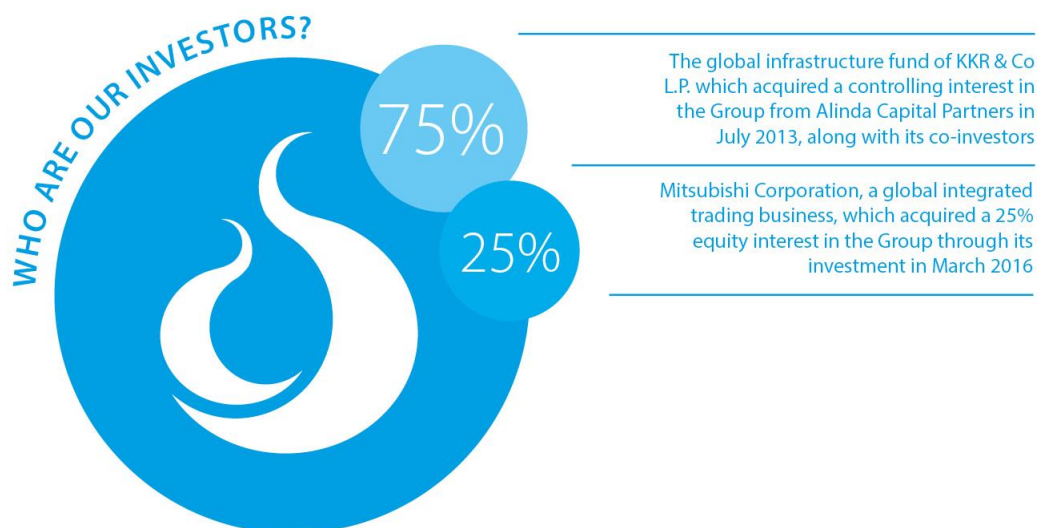
The Directors of South Staffordshire Water PLC have always placed good governance at the core of the business. They are aware of their obligations to ensure effective leadership, and appropriate governance arrangements are in place within the Company. Following the publication of Ofwat’s principles on Board leadership, transparency and governance in January 2014 the Company developed its own Corporate Governance Code (“the SSW Code”) which seeks to not only meet but exceed these principles. A copy of the SSW Code can be found on the Company’s website (www.south-staffs-water.co.uk).

Although the Company is not a public listed company, its Board of Directors recognises that due to public interest in how the Company performs and the regulated environment in which it operates it should act as if it were. The SSW Code has specifically drawn on Ofwat’s principles and certain principles of the UK Corporate Governance Code (“the UK Code”), those considered applicable and appropriate to a privately owned but regulated Company providing essential services. They believe that this approach enforces effective leadership and appropriate governance arrangements. Details of how the Company follows these principles are provided below. The Company also applies the Walker Guidelines on transparency and disclosure. The Company frequently monitors corporate governance best practice and the appropriateness of developments to the Company. Any changes to the Company’s governance arrangements are implemented within agreed timescales.

Details of how the Company preserves value over the long term, its business model and how it delivers this and its strategy are provided in the Strategic Report.

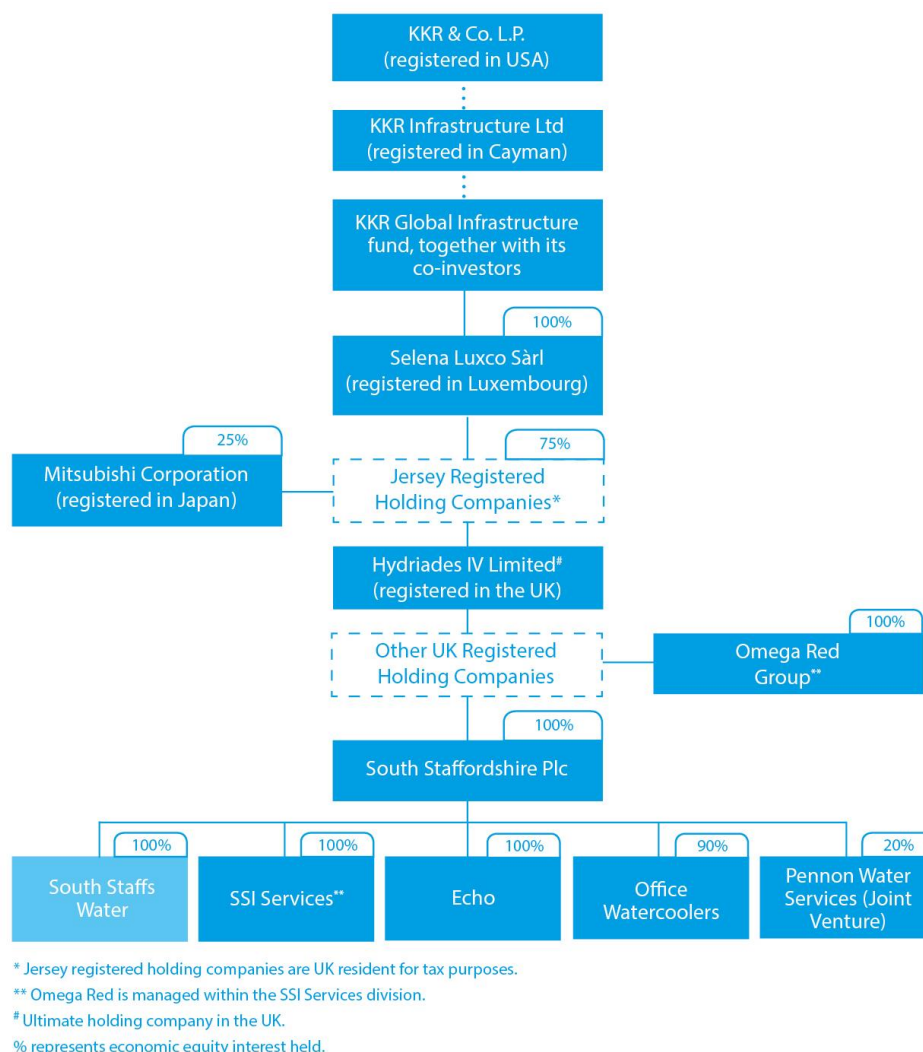
Group structure

Who were our investors during the year ended 31 March 2018?



Our Governance – Corporate Governance Report

Our Group structure during the year ended 31 March 2018



During the year, and until 3 July 2018, the Company was controlled by the Global Infrastructure Fund of the investment business KKR & Co. L.P. (KKR), which is quoted on the New York Stock Exchange and which held a majority controlling interest in the Group, together with certain co-investors. The KKR Infrastructure Fund is controlled and managed by its General Partner KKR Infrastructure Limited, a company registered in the Cayman Islands (the “Holding Company”).

South Staffordshire Plc, as the immediate parent company of South Staffordshire Water PLC, ensures through its comprehensive knowledge of its subsidiaries and the water industry that it understands the duties and obligations of a regulated company. This includes Condition P of its licence and, although some Directors sit on both Boards, South Staffordshire Water PLC acts, with the support of the Group, as if it were a separate listed company. South Staffordshire Plc provides management, professional and administrative support services to South Staffordshire Water PLC and its other subsidiaries at cost. There was no direct interaction between South Staffordshire Water PLC and the Holding Company during the year.

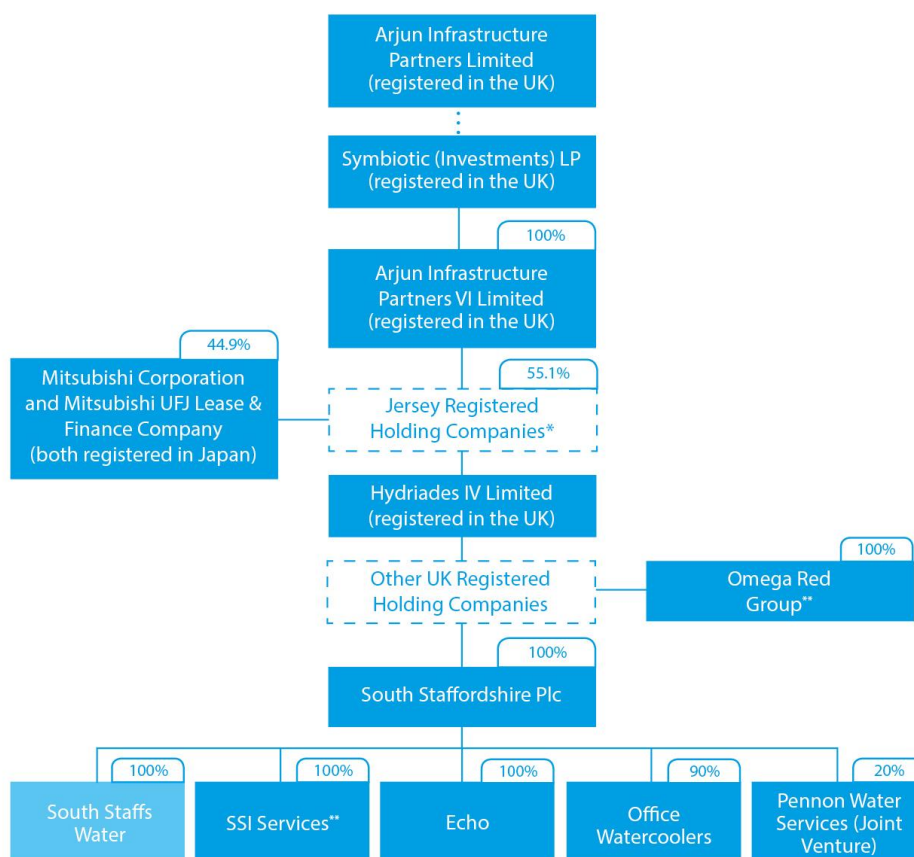
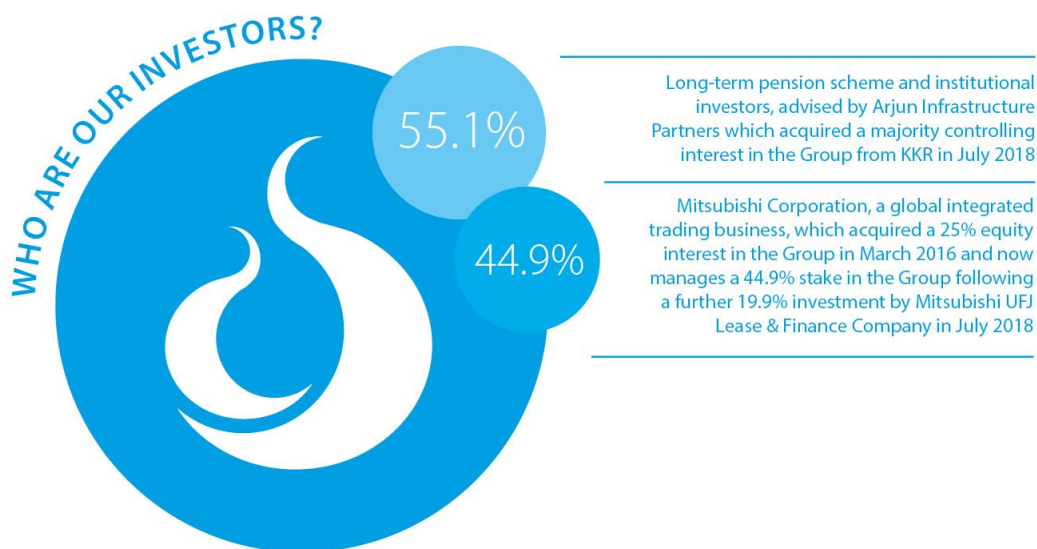
Details of the borrowings of South Staffordshire Water PLC are provided in the accompanying reported accounts and the finance section of the Strategic Report. Similarly, details of the borrowings of South Staffordshire Plc are provided in its own Annual Report and Accounts.

Our Governance – Corporate Governance Report

Group structure from 3 July 2018

Since the end of the financial year ended 31 March 2018, the Global Infrastructure Fund of KKR together with its co-investors, sold their 75% equity stake in the Group to pension funds and other institutional investors advised and managed by Arjun Infrastructure Partners Limited, with the sale completing on 3 July 2018. These investors then sold a 19.9% stake to Mitsubishi UFJ Lease and Finance Company with Mitsubishi Corporation retaining its 25% interest.

Details of the Group structure since 3 July 2018 are provided below.



* Jersey registered holding companies are UK resident for tax purposes.

** Omega Red is managed within the SSI Services division.

% represents economic equity interest held.

Our Governance – Corporate Governance Report

Relations with shareholders and the immediate Holding Company

During the year there were a number of UK registered intermediate holding companies above the immediate parent South Staffordshire Plc in the Group structure, headed by Hydriades IV Limited, the ultimate holding company registered in the UK as at 31 March 2018. There are also intermediate holding companies above Hydriades IV Limited, which are registered in Jersey but are resident in the UK for tax purposes. In March 2016, Mitsubishi Corporation acquired a 25% equity interest in one of these companies, Selena Bidco Limited, and therefore during the year held a 25% equity interest in the South Staffordshire Plc Group and the Company. In line with other KKR investments in Europe, during the year, the parent of the Jersey resident companies was a company registered in Luxembourg (Selena Luxco S.à.r.l.). The KKR fund that invested in this company is controlled and managed by KKR Infrastructure Limited. Two of the UK registered holding companies have loans payable to South Staffordshire Water PLC, both of which bear interest which is paid in full each year. Any UK tax losses surrendered to South Staffordshire Water PLC from other companies in the structure are paid for at their net tax value.

From 3 July 2018, and with the change in the Group structure as set out on page 50, the ultimate controlling party is now Arjun Infrastructure Partners Limited, a company registered in the UK. Both Arjun Infrastructure Partners Limited and Mitsubishi Corporation have signed Condition P undertakings in accordance with the Company's Instrument of Appointment.

There is a regular and detailed dialogue between the Board and shareholders to ensure that their objectives and priorities are carefully considered. This dialogue is achieved through Board meetings that shareholders attend, with major shareholders having representation on the Board of Directors or attending Board meetings, and through other less formal communication.

The Board of Directors

The Directors are collectively responsible for the long term success of the Company. They may be appointed by the Company by Ordinary Resolution or by the Board. As set out in the Company's Articles of Association, a Director appointed by the Board will hold office until the next Annual General Meeting (AGM). At each AGM one third of the Directors will retire by rotation and will submit themselves for re-election at least once every three years.

All Directors are aware of the procedure to seek independent legal and other professional advice. The Board also has access to the advice and services of the Company Secretary, who is also responsible for monitoring corporate governance matters. Indemnities have been given to all of the Directors to the extent permitted by the Companies Act 2006. All Directors and Senior Management are covered by a Directors' & Officers' insurance policy, against any actions taken against them as Officers of the Company.

Board membership

Sir James Perowne was appointed Independent Non-Executive Chairman on 1 April 2017. Senior Executives of KKR who held positions on the Board of the Company at 31 March 2018 were Ram Kumar and Ryan Miller, both of whom were also Directors of all holding companies above South Staffordshire Plc in the Group structure at 31 March 2018. Ram Kumar and Ryan Miller were also a Non-Executive Directors of the Company's immediate parent, South Staffordshire Plc. On 3 July 2018 both of these Directors resigned from all of the Group companies that they were Directors of as part of the KKR Global Infrastructure Fund's and its co-investors' sale of their 75% equity interest in the Group. At 31 March 2018, Adrian Page was also an Executive Director of the immediate parent and all of its UK subsidiaries and holding companies.

Stephen Kay is considered by the Board to be independent in both character and judgement. While Stephen is a former Managing Director of Cambridge Water PLC, he has never served as an Executive Director of South Staffordshire Water PLC. It is considered that he brings to the Board valuable industry knowledge, engineering skills and experience and extensive links and knowledge of the Cambridge supply region, all of which are important attributes to the balance of the Board's composition. In addition, the appointment of Stephen Kay is consistent with the commitment given to the Competition Commission and in the licence unification process to have a Non-Executive Director on the Board with links to the Cambridge region.

Our Governance – Corporate Governance Report

Functions of the Board

Under the SSW Code, the Company should have an effective Board. The Board's primary focus being to develop, implement and fulfil the strategy to deliver the service and performance to meet the needs of customers, the environment, the business, employees, shareholders and other stakeholders. The Board should also be in a position to make well-informed and high quality sustainable decisions, and to make decisions that are in the best interests of the Company, and are consistent with its statutory and regulatory duties.

The Board sets standards of conduct to promote the success of the Company, provide leadership, and review the Company's internal controls and governance structure. It approves major financial and investment decisions above senior management thresholds, evaluates the performance of the Company as a whole by monitoring reports received directly from Senior Management and also from Directors. The Non-Executive Directors led by the Independent Chair, are responsible for overseeing this work, and scrutinising management performance. They constructively challenge and help develop proposals on strategy.

In conjunction with the Audit Committee, the Board is also responsible for the Company's systems of internal control and for evaluating and managing significant risks to the Company.

On joining the Board, Directors receive induction material appropriate to their needs and responsibilities. This may include, but is not limited to, information on the regulatory framework of the Company, operational activities, financing structure, strategic and financial plans and the wider Group structure. The Directors and Executive Team carry out site visits to maintain familiarity with the Company's operations and to refresh their skills and knowledge. The Directors also keep up to date with legal and regulatory changes and developments by receiving written and verbal updates from both internal and external advisers and regulators.

The Directors are supported by an Executive Team and by other senior managers, who have responsibility for assisting them in the development and achievement of the Company's strategy and reviewing the financial and operational performance of the Company. The Executive Team is responsible, along with the Directors, for monitoring policies and procedures and other matters that are not reserved for the Board. There are procedures providing a regime of authorisation levels for key decision-making. Details of the skills and experience of the Executive Team are contained in their biographies on pages 43 to 45.

In accordance with the SSW code, a formal evaluation of Board and individual member's performance is carried out by reviewing the effectiveness of the Board as a whole and of the individual members of the Board.

Matters reserved for the Board

A schedule of matters specifically reserved for the Board's decision has been adopted based on the Institute of Chartered Secretaries and Administrators (ICSA) best practice. The terms include, but are not limited to:

- Ensuring observance of all matters required by the Company's Instrument of Appointment
- Approval of Directors' assurance statements to Ofwat, including but not limited to; the Annual Performance Report, Annual Viability of the Business; the setting of water tariffs and other regulatory assurance as required
- Material submissions to Ofwat, the Competition and Markets Authority and similar regulators, agencies or bodies
- Reviewing and approving of capital and operating budgets
- Reviewing and approving the Company's strategy and performance
- Reviewing and approving any significant changes to the Company's capital structure and borrowings
- Reviewing and approving financial reports
- Contracts that are material, either strategically or by reason of size, according to specified limits
- Appointment and removal of any Director
- Prosecution, defence or settlement of litigation above £1 million or being otherwise material;
- Material changes to the Company's pension arrangements
- Ensuring maintenance of a sound system of internal control and risk management
- Considering the balance of interests between shareholders, employees, customers and the community
- Powers to delegate authority

Our Governance – Corporate Governance Report

The Directors maintain a flexible approach to Board matters with the delegation of power to a Committee, with precise terms of reference, being used for specific routine purposes. Both the terms of reference and composition of the Committees are regularly reviewed to ensure their ongoing effectiveness.

Whilst South Staffordshire Water PLC acts as though it were a separate public listed company, a limited number of matters in respect of this subsidiary company also need the approval of the Board of South Staffordshire Plc its immediate parent, Company. These include:

- Material submissions to Ofwat, particularly in respect of Price Reviews and major structural reform;
- Contracts that are material either strategically or by reason of size, according to specified limits;
- Appointment and removal of any Director, in its role as shareholder;
- Prosecution, defence or settlement of litigation above £1 million or being otherwise material;
- Material changes to pension arrangements where operated on a Group basis

Board meetings

The Board holds regular scheduled meetings throughout the year. During the year ended 31 March 2018 there were nine scheduled meetings of the Board.

In compliance with the SSW Code, all Directors are provided with sufficient information prior to any Board meeting to allow appropriate preparation to ensure that they can properly discharge their duties.

The attendance by individual Directors at scheduled meetings of the Board during the year ended 31 March 2018, is shown in the table with in the Directors' Report on page 46.

Organisational structure

A defined organisational structure for the Company exists with clear lines of responsibility, accountability and appropriate division of duties.

The Directors set an overall strategy and have delegated the necessary authority to the Executive Team and business departments in order to deliver that strategy. This is communicated to employees by way of published policies and procedures and regular management and staff briefings.

The Company's extensive financial regulations specify authorisation limits for individual managers, with all material transactions being approved by a member of the Executive Team, a Director or by the Board collectively. In addition, formal treasury policies are in place. Where appropriate, commercial and financial responsibility is clearly delegated to the Executive Team and supported by the Directors.

Risk management

The Company's approach to risk reflects its status as a regulated and licensed water undertaking providing essential public services. It balances the need to effectively manage exposure to risk, whilst aiming to deliver high standards of operational and financial performance. A strong risk management and control framework is therefore in place to understand and manage identified risks. The effectiveness of the Company's risk management and internal control systems is discussed and reviewed by the Board and Audit Committee on a regular basis. The Company's Executive Team is required to monitor risk and its management, with any significant changes in business risk and any subsequent procedures or controls to mitigate the risk being reported to the Board and the Audit Committee. Further details of risk management and principal risks are provided in the Strategic Report on pages 32 to 38.

Our Governance – Corporate Governance Report

Regulatory reporting

South Staffordshire Water PLC makes significant efforts to produce regulatory documentation and information that is reliable, robust and accurate and is supported by suitable systems and procedures. The Board, including Independent Non-Executive Directors, are involved in the approval process for key regulatory information. This process supports the governance in place, the review of information by an independent technical auditor (Jacobs), the audit work and certain agreed upon procedures in respect of the extraction of specific information performed by the external independent auditor (Deloitte LLP). Where identified as necessary by the Company Assurance Framework, the Group's internal audit function will review processes and data in to provide appropriate assurance.

The Company places great emphasis on regulatory reporting to ensure that it continues to have sufficient processes and internal systems of control to fully meet its obligation for the provision of information to Ofwat, other regulators and stakeholders. It is important to the Company that this information is robust, not just for its external credibility, but to also allow it to manage the performance of the business and make appropriate decisions with reference to this data.

The Company's Regulatory Accounts are contained within the Annual Performance Report set out on pages 104 to 165.

Going concern and basis for assumption

The Directors consider that it is appropriate to prepare the accounts on a going concern basis. This is based upon a review of the Company's budget for the year ending 31 March 2019 and the longer term plan and financial forecasts to 31 March 2025 and the related stress testing performed on this plan as detailed in the Long Term Viability section on pages 39 to 40 of the Strategic Report. This assertion is also based on the Company's investment programme, the Final Determination for 2015-20 and the Company's plan in relation to it, the committed borrowing facilities available to the Company together with cash balances, actual and forecast compliance with borrowing covenants and other important financial metrics and ratios, and its access to capital markets to fund operations in the future. The Company is confident it has sufficient access to capital markets and relationships with banks and other lenders to refinance borrowing facilities that mature within 12 months of approval of the annual report and accounts. In addition, the Directors are required to certify to Ofwat under Condition F of its Instrument of Appointment that sufficient financial resources are available for at least the next 12 months.

The Company's business activities, its business model and strategy together with the factors likely to affect its future development, are set out in the Strategic Report on pages 5 to 42. The financial position of the Company, its liquidity position and available borrowing facilities are set out on the balance sheet on page 75 and in note 23 to the accounts, which includes the Company's objectives for managing its financial risks, details of its financial instruments and hedging activities and its exposure to interest, credit and liquidity risk. The Company has a large number of both domestic and commercial customers, none of which make up a significant proportion of turnover. The Company has significant undrawn borrowing facilities in addition to its cash balances and has significant headroom in respect of all of its borrowing covenants, both on a historic and forward looking basis.

Our Governance – Corporate Governance Report

The Audit Committee for the year ended 31 March 2018

Chair -
Keith Harris



Sir James
Perowne



Stephen
Kay



Director	Role	Meeting Attendance
Keith Harris	Chair	2/2
Sir James Perowne	Member	2/2
Stephen Kay	Member	2/2

Meetings also regularly attended by:

- Observers from shareholders
- Deloitte LLP, our external independent auditor
- Finance, Regulation and Business Services Director
- Director of Regulation
- Financial Controller
- Company Secretary
- Group Financial Controller
- Group Internal Audit Manager

Role and responsibilities

The Audit Committee is responsible for reviewing and monitoring the Company's financial statements, internal controls and systems for mitigating the risk of financial and non-financial loss. This includes assessing the integrity of financial statements, considering changes to accounting policies, reviewing financial reporting procedures and risk management processes and monitoring systems.

The Committee is responsible for recommending to the Board the appointment, reappointment and if necessary the removal of the external auditor and monitoring the auditor's independence, performance and effectiveness. Responsibilities extend to approving the nature and scope of external audits and the auditor's remuneration.

Key terms of reference:

- Review and appraise the work of the external auditor by meeting with the auditor twice a year, reviewing the results of its work, discussing the quality of the audit with senior management, reviewing the level of non-audit fees and the nature of non-audit services provided and reviewing the auditor's own assessment of its independence

Our Governance – Corporate Governance Report

- Monitor, review and challenge when necessary the integrity of the financial statements of the Company, including its Statutory Accounts, Annual Performance Report, Interim Accounts and any other formal announcement relating to its financial performance, and reviewing significant financial reporting issues and judgements which they contain
- Keep under review the effectiveness of the Company's internal audit arrangements, internal controls and risk management policies and practices
- Report to the Board of Directors on how it has discharged its responsibilities

Audit Committee activities

The Committee focused on the key business risks on our risk register as detailed in the strategic report on pages 32 to 38; it also focused on the areas of significant judgement and estimate as identified by the external auditor. These are primarily revenue recognition, recoverability of receivables, capitalisation and useful economic lives of fixed assets, hedge accounting and amortised cost of index linked borrowings.

Key emphasis this year was placed on the primary business risks which are identified as Business Planning for 2020 to 2025 and Water Quality. The Committee also recognised, in line with our external auditor's opinion that the most significant financial risks are around revenue recognition (accrued income), the recoverability of receivables and capitalisation of fixed assets.

With regards to Business Planning for 2020 to 2025, the Committee tasked management to provide an accurate forward looking forecast for the rest of AMP6 by price control. This gives the Board the necessary insight to make decisions on how the plan for 2020 to 2025 should be shaped. Management completed this task and provided required information to the Board as part of the 2018/19 budgeting process; this was shared with the Chair of the Committee. Management was also required to provide comfort to the Committee that the required assurance was in place around the Business Plan.

The Committee required management to provide details of how Water Quality risks will be mitigated and proactively managed in the future. It has been confirmed that Water Quality is a high priority in the Business Plan for 2020 to 2025 and future plans have been incorporated. The Committee also directly requested information regarding the technical audit process and received feedback from management with regards to the internal operational audit programme which will now be reported specifically to the Committee annually moving forward.

In reviewing the significant financial reporting risks surrounding revenue recognition, recoverability of receivables and capitalisation of fixed assets the Committee worked with management to ensure that these risks were mitigated and that the Company's practices are in line with applicable accounting regulations and satisfied the requirements of our external auditors.

In the year the Committee reviewed revenue recognition practices to ensure that they were in line with both statutory and regulatory reporting guidelines. The budget for revenue for the rest of AMP6 was also subject to review as part of the planning process.

Alongside the above the Committee reviews and challenges papers and feedback from management, external auditors' reports, reports from Group Internal Audit and the Company risk register. It also discusses areas of judgement and estimation and where appropriate makes comment; recommendations; and seeks further management clarification where required.

Financial reporting and forecasting

The Board supported by the Audit Committee recognises the need to present a balanced, understandable and clearly defined assessment of the Company's operational and financial performance and position including its future prospects. This is provided by a review of the Company's operations and performance as set out in the Strategic Report.

Business plans, annual profit and loss budgets, cash flow budgets and forecasts, longer term financial forecasts and investment proposals for the Company are formally prepared, reviewed and approved by the Board supported by the Audit Committee. Actual financial results and cash flows, including a comparison with budgets and forecasts, are regularly reported to the Board with variances being identified and used to initiate any action deemed appropriate.

Our Governance – Corporate Governance Report

Details of the Company's actual and forecast future compliance with its borrowing covenants are also prepared on a regular basis, and forecasts of the Company's level of undrawn and available borrowing facilities for liquidity purposes are also prepared and reported to the Board.

As detailed in the Strategic Report, stress testing has been carried out on the Company's longer term financial forecasts to ensure the long term viability of the Company. This makes sure that the Company has the ability to withstand a series of severe, plausible and reasonable events. The Audit Committee is integral in assessing the tests carried out and the conclusions formed in order that the Board is assured of the long term viability and financial resilience of the Company.

Internal control

The Board supported by the Audit Committee attaches considerable importance to the Company's system of internal control and reviews its effectiveness. This includes ensuring reasonable steps are taken to safeguard the assets of the Company and to prevent and detect fraud and other irregularities. The control systems are designed to manage rather than eliminate risks, and can provide only reasonable assurance against misstatement or loss. South Staffs has an established internal control framework that is continually reviewed and updated taking into account the nature of the Company's operations.

The Audit Committee is closely involved in challenging the Company's processes for the identification, evaluation and management of significant risks; a detailed review of the current assessment of these is on pages 32 to 38 of the Strategic Report.

The Audit Committee has also challenged the Company to identify and mitigate against upcoming risks, this has ensured close attention to current issues such as Brexit and nationalisation and has also encompassed current challenges such as GDPR and cyber security.

Internal audit

South Staffs benefits from independent reviews of performed by an Internal Audit function operated by the Company's parent. This service is dedicated to ensuring that internal control activities remain a priority within the Group and provides valuable support to South Staffs in maintaining good systems of internal control, providing assurance over the quality of information (depending on the Assurance Framework categorisation) and helps ensure appropriate Corporate Governance.

An Internal Audit Plan is presented to the Audit Committee each year; this is subject to challenge and approval. The plan combines the need for regulatory and financial reporting assurance, risk management and control evaluation with the provision of independent resource to enhance the Company's operations. Progress against the plan is monitored by the Audit Committee via the reporting of findings and recommendations at each meeting.

Internal Audit was heavily involved in the assurance processes around exiting the non-household retail market at the start of 2017/18 but as the year has progressed the emphasis has shifted to providing one of the layers of assurance around the PR19 process.

The internal audit arrangements in operation are considered to be appropriate to the size and complexity of the Company, an assessment which the Board will continue to review via the Audit Committee.

External independent auditor

The Board supported by the Audit Committee reviews the external independent auditor's performance each year considering effectiveness, independence and fees including the level of non-audit services and related non-audit fees.

In evaluating the external auditor, the Audit Committee assesses the calibre of the audit firm, the audit scope and plan (which is agreed in advance with the Audit Committee via discussions with the Chair) and the level and nature of audit communications, including the reporting to the Audit Committee of any significant issues.

Our Governance – Corporate Governance Report

The responsibilities of the external independent auditor in the area of financial reporting are set out in their report relating to each year's financial statements.

The current external audit provider, Deloitte LLP, has been the Company's auditor since the year ended 2003, with a change in the audit Partner occurring every 5 years. Based on current legislation, Deloitte LLP can be re-appointed for all financial years up to and including the year to 31 March 2023. Thereafter, auditor rotation is required once every 10 years extendable to 20 years if a tender is conducted after 10 years.

Our Governance – Corporate Governance Report

The Nomination Committee for the year ended 31 March 2018

Chair - Sir James
Perowne



Keith
Harris



Stephen
Kay



Adrian
Page



Ram
Kumar



Director	Role	Meeting Attendance
Sir James Perowne	Chair	1/1
Keith Harris	Member	1/1
Stephen Kay	Member	1/1
Adrian Page	Member	1/1
Ram Kumar (Resigned 03/07/2018)	Member	1/1

Membership of the Committee

The Nomination Committee is mainly comprised of Independent Non-Executive Directors and is chaired by the Company's Independent Chair. Meetings are convened as required to discuss changes or appointments to the Board of Directors, one meeting was held in 2017/18 as there was a change to the Board in the year.

Role of the Committee

Considerable attention is given by the Committee to the composition of the Board including reviewing the balance of skills, knowledge, experience, diversity including gender and the level of non-executive and independent challenge.

External search advisors are engaged to assist the Nomination Committee where considered appropriate but are not considered necessary for all appointments.

Key terms of reference:

- Preparing an appropriate specification for open Board positions
- Ensuring any appointment to the Board carefully considers the balance of the Board composition
- Ensuring successful candidates have the necessary skills, experience, information and knowledge to fulfil their duties

Diversity

Gender diversity details for the Company can be found in the Strategic Report on page 24.

Our Governance – Corporate Governance Report

The Remuneration Committee for the year ended 31 March 2018

Chair - Sir James
Perowne



Keith
Harris



Stephen
Kay



Adrian
Page



Ram
Kumar



Director	Role	Meeting Attendance
Sir James Perowne	Chair	1/1
Keith Harris	Member	1/1
Stephen Kay	Member	1/1
Adrian Page	Member	1/1
Ram Kumar (Resigned 03/07/2018)	Member	1/1

Membership of the Committee

The Committee is mainly comprised of Independent Non-Executive Directors and is chaired by the Company's Independent Chair.

Role of the Committee

The Committee is responsible for the remuneration policy and setting the remuneration packages of the Board, the Executive Team and other senior management. The Committee meets at least once a year.

Key terms of reference:

- Agree remuneration that will ensure that Executive Directors and the Executive Team are provided with appropriate incentives to achieve high standards of performance and reward them for their individual contributions to the success of the Company
- Ensure that the performance related elements of remuneration for the executive directors of the company relate to standards of performance for customers and wider society
- Determine remuneration packages and arrangements with regard to any relevant legal requirements and associated guidance and to obtain reliable, up-to-date information about remuneration in other companies
- Ensure that contractual terms on termination are fair and that failure is not rewarded
- Oversee any material changes in employee benefits structures throughout the Company

A detailed remuneration report is set out on pages 61 to 64.

Our Governance – Remuneration Report

Remuneration policy

Remuneration packages and fees are designed to attract, retain and motivate high-calibre Directors and Executive Team members. The Remuneration Committee has overall responsibility for determining Board Directors' remuneration packages and considering those of the Executive Team.

The total remuneration packages of Board Directors and the Executive Team include basic salary, benefits and annual and deferred bonuses which are linked to business targets and personal performance related objectives. Performance related objectives are designed to encourage and reward continuing improvement in the Company's performance over the longer term. Annual salary, benefits and annual bonus awards are normally pensionable whereas deferred bonuses are not normally pensionable.

The Committee recognises that transparency on the relationship between pay policy and outperformance will help customers see how performance pay is earned in providing an essential service. The company has an obligation under Section 35A of the Water Industry Act 1991 to make a statement in relation to remuneration that is linked to standards of performance. This has been enhanced further this year.

Board and Executive terms of engagement

As Group Chief Executive, Adrian Page is appointed to the Board of the Company in accordance with the requirements of his Group wide role. Ram Kumar and Ryan Miller were appointed to the Board as representatives of KKR the majority shareholder; their appointments have no fixed term.

Sir James Perowne, Keith Harris and Stephen Kay as Independent Non-Executive Directors are appointed to Board for three year fixed terms. They can be re-appointed for a further two periods before being required to stand down after a maximum of nine years of service. In accordance with their appointment the Independent Non-executive Directors are required to commit the appropriate time needed to sufficiently fulfil their duties within a regulated utility business.

The Managing Director and Executive Team are employed on service contracts of no fixed term, with a notice periods of either 6 or 3 months. They are entitled to basic pay, private medical insurance, company car or car allowance, fuel allowance and payments made to a Group money purchase pension scheme. In addition there is participation in the bonus scheme. Bonus awards are linked to personal objectives as well as being aligned to the Company's standards of performance in the areas of:

- Customer Service (based upon the SIM Performance, and complaints performance as reported to Ofwat)
- Achievement of ODI performance targets (as reported in Table 3A of the APR)
- Financial performance based upon profitability, operating costs and cash generation

The standards of performance to which bonuses are linked are reviewed annually by the Remuneration Committee to ensure consistency is maintained.

Bonus awards are linked to the above standards of performance as the Remuneration Committee considers such arrangements will maintain consistency between the objectives of the Directors and principal stakeholders including customers and shareholders. The standards of performance to which bonuses are linked are reviewed annually by the Remuneration Committee to ensure this consistency continues to be maintained.

Adrian Page is Group Chief Executive and an Executive Director of the parent company, South Staffordshire Plc. As part of his remuneration package an element of his bonus is set aside specifically linked to the performance of the Water Company.

Further details in respect of the Managing Director's and Executive Team's remuneration are provided in this report on page 63, along with a more detailed breakdown of bonus awards on page 64, including the detail in respect of Adrian Page.

Our Governance – Remuneration Report

Board and Executive Team

The Board of Directors and Executive Team were made up as follows during the year; more detailed biographies are on pages 43 to 45.

Name	Role
Sir James Perowne	Independent Non-Executive Chair
Phil Newland	Managing Director
Adrian Page	Group Chief Executive - South Staffordshire Plc
Ram Kumar	Non-Executive Director (Resigned 03/07/2018)
Oleg Shamovsky	Non-Executive Director (Resigned 30/11/2017)
Ryan Miller	Non-Executive Director (Appointed 30/11/2017; Resigned 03/07/2018)
Keith Harris	Independent Non-Executive Director
Stephen Kay	Independent Non-Executive Director

The Executive Team

Name	Role
Tim Orange	Finance, Regulation and Business Services Director
Pete Aspley	Wholesale Director
Marcella Nash	Director of Human Resources
Rachel Barber	Customer Service Director (Resigned 31/10/2017)
Colin Wayper	Operations Director (Retired 30/04/2017)

The tables on the next page detail remuneration for the year for the Board of Directors and the Executive Team. The Executive Team table shows the total pay for all members and an average per member calculation.

Ram Kumar, Oleg Shamovsky and Ryan Miller were not remunerated by the Company or South Staffordshire Plc during the year.

Our Governance – Remuneration Report

Remuneration table

The Board £'000							
Name	Basic Salary	Bonus*	Other Benefits and Pay**	Fees	Total Emoluments	Pension Contributions ***	Total Remuneration
Sir James Perowne	-	-	-	40	40	-	40
Phil Newland	168	61	15	-	244	21	265
Adrian Page	-	-	-	-	-	-	-
Ram Kumar	-	-	-	-	-	-	-
Oleg Shamovsky	-	-	-	-	-	-	-
Ryan Miller	-	-	-	-	-	-	-
Keith Harris	-	-	-	30	30	-	30
Stephen Kay	-	-	-	30	30	-	30
Total	168	61	15	100	344	21	365
The Executive Team £'000							
Name	Basic Salary	Bonus*	Other Benefits and Pay**	Fees	Total Emoluments	Pension Contributions ***	Total Remuneration
Total	363	85	54		501	48	549
Average	73	17	11		101	10	111

* Bonus figures include any deferred amounts paid in the year and approved figures in respect of the year ended 31 March 2018

** Other Benefits and Pay combine company car benefit in kind, car cash and benefit allowances, fuel allowances, the taxable value of private medical insurance provision

*** Pension contributions are payments by the company in respect of money purchase pension schemes

Compensatory payments made on cessation of employment of £142,000 have been made in respect of the Executive Team members that are not included in the table above.

Our Governance – Remuneration Report

Bonus awards

The maximum levels of bonus available to the Managing Director and Executive Team are 60% and 40% (average), for the year ended March 2018 the Remuneration Committee awarded bonus payments of 36% and 23% (average) reflecting the level of performance of individuals and the Company in the year

Phil Newland, as an Executive Director of the Company is due a bonus in respect of the above performance and individual targets in respect of the year ended 31 March 2018 approved at £61,700 reflecting the performance of the business in the year. This bonus is payable following the year end. This bonus is less than that paid in respect of the previous year reflecting that operational performance in a number of areas was less than expected.

The bonus awarded to Phil as an Executive Director is based on a “sliding scale” with the bonus award in each category increasing with performance up to a specified maximum award for excellent performance. In addition, Phil has a number of personal targets to achieve for the year, primarily focused on the development of a high quality Business Plan for PR19 and the required customer engagement. Progress has largely been as expected and a bonus of 10% has been proposed to be paid.

The following performance against target was achieved during the year:

Standard of Performance	Target	Actual	Average % of Salary Awarded
Customer Service	Improve SIM and reduce customer complaints	Target partially achieved	10%
Outcome Delivery Incentives	Achieve Target for key operational performance	Target partially achieved	10%
Financial Performance	Achieve profitability, cost and cash generation	Target not fully achieved	6%

As discussed earlier in this report an element of the bonus in the year for Adrian Page of £35,000 is specifically linked to the performance of the Company including delivery of ODI targets, and the development of a high quality Business Plan for PR19, of which only half is proposed to be paid reflecting operational performance in the year.

Executive pay ratio

There is increased scrutiny being placed upon the pay for Board members in the water industry (and other public service organisations), particularly when set against that of the lowest paid employees within an organisation.

A 20:1 ratio has been discussed within political and social forums as an acceptable maximum multiplier with regards to the gap between the lowest paid employees and highest paid Board member.

The Company is committed to paying the foundation living wage to employees; based on a 37 hour a week contract at £8.45 (2017 rate for outside London) this would give an annual salary of £16,258. All our staff (excluding modern apprentices) are paid at or higher than the foundation rate.

In comparison to Phil Newland, the highest paid directly employed Board member, this gives a ratio of 10:1 against basic salary and 16:1 against total remuneration both of which sit within the bounds of a 20:1 ratio.

Directors' Responsibilities Statement

The following statement, which should be read in conjunction with the auditor's statement of its responsibilities, set out on pages 66 to 73, is made with a view to distinguishing for shareholders the respective responsibilities of the Directors and of the auditor in relation to the accounts.

The Directors are required by Company Law, and under Condition F of the Instrument of Appointment by the Secretary of State for the Environment, as a water undertaker under the Water Industry Act 1991, to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company at the end of the financial year and of the profit or loss for the financial year. Under Company Law, the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland".

In preparing the accounts the Directors are required to:

- Select suitable accounting policies (see pages 116 to 117) and then apply them consistently
- Make judgements and estimates that are reasonable and prudent
- State whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements
- Prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business, in which case there should be supporting assumptions or qualifications as necessary

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors have the responsibility for the maintenance and integrity of the Company's website. Information published on the Internet is accessible in many countries with different legal requirements. Legislation in the United Kingdom governing the preparation and dissemination of the financial statements may differ from legislation in other jurisdictions.

Independent Auditor's Report

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SOUTH STAFFORDSHIRE WATER PLC

Report on the audit of the financial statements

Opinion

In our opinion the financial statements:

- **give a true and fair view of the state of the Company's affairs as at 31 March 2018 and of its profit for the year then ended;**
- **have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including Financial Reporting Standard 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland"; and**
- **have been prepared in accordance with the requirements of the Companies Act 2006.**

We have audited the financial statements of South Staffordshire Water PLC (the 'Company') which comprise:

- the profit and loss account;
- the balance sheet;
- the statement of comprehensive income;
- the statement of changes in equity;
- the cash flow statement;
- the notes to the cash flow statement; and
- the related notes 1 to 26.

The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the Company.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independent Auditor's Report

Summary of our audit approach

Key audit matters	The key audit matters that we identified in the current year were: <ul style="list-style-type: none">• Revenue recognition in relation to unbilled revenue• Valuation of trade receivables• Classification of costs between operating and capital expenditure, in particular focusing on appropriateness of capitalised costs.
Materiality	The materiality that we used in the current year was £1.8m which was determined on the basis of EBITDA.
Scoping	We have considered which account balances, classes of transactions and disclosures are at greatest risk of misstatement and we designed our audit procedures to specifically address these areas.
Significant changes in our approach	There have been no significant changes to our audit approach for the year ended 31 March 2018.

Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where:

- the directors' use of the going concern basis of accounting in preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of these matters.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements for the year ended 31 March 2018 and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters

Independent Auditor's Report

Revenue Recognition in relation to unbilled revenue

Key audit matter description



Revenue is made up of the supply of water in the year, together with an estimation of amounts supplied but not yet billed at year end. As at 31 March 2018, the accrued income recognised is £11.1m (31 March 2017: £14.2m). The total balance has decreased due to the transfer of the non-household (NHH) retail business on 1 April 2017 to SSWB Limited.

We have identified a key audit matter in relation to the valuation of accrued income for household measured water customers. For these customers, revenue is recognised based on the value of water supplied with estimates made at an individual customer level and based on historical meter reading data. This is used to estimate consumption since the date of the last invoice (which itself could be estimated), and to determine the unbilled income to be accrued at the year-end date.

Significant judgement is required by management in forming these estimates and we have determined that there is a risk of inappropriate bias in the accounting of the balance.

The accounting policy related to metered water consumption is disclosed in note 1.

How the scope of our audit responded to the key audit matter

- We have tested the design, implementation and operating effectiveness of controls over the recognition of accrued income and general IT controls over the billing system;
- Our data specialists have performed a re-calculation of the accrued income balance and assessed the difference to the amount recognised in the accounts;
- We have tested the accuracy and completeness of the source data from which the historic billed consumption data is derived;
- We have assessed the methodology used by management which forms the estimated consumption data; and
- We have reviewed the accounting practices in place in relation to revenue in accordance with FRS 102.

Key observations

Overall, the accrued income calculations and revenue recognition policies are reasonable and consistent with the prior year.

Independent Auditor's Report

Valuation of trade receivables

Key audit matter description



As disclosed in note 15, the Company holds £12.6m (31 March 2017: £16.3m) of receivables from customers at 31 March 2018, which is stated net of a provision for bad and doubtful debts. The total amount of the provision included within the above, as at 31 March 2018 was £34.1m (31 March 2017: £33.6m). The key estimate is the level of bad debt provision which is recorded against the Company's debtors. The bad debt provision is calculated by management with reference to the anticipated amount of cash that they expect will be collected as a percentage of the amount billed per annum.

Management monitor the debt collection profile for each billing year and review the calculation of the bad debt provision to ensure the provision continues to be reasonable relative to recent actual collection experience.

Significant judgement is required by management in forming these estimates and we considered the risk of inappropriate bias in the accounting for this balance.

How the scope of our audit responded to the key audit matter

- We have tested the design, implementation and operating effectiveness of controls over the calculation of the bad debt provision.
- We have reviewed and challenged the method used to calculate the bad debt provision to assess whether it is reasonable by considering the most recent collection experience, plans for future collections, consistency of the method with prior years and any changes in our understanding of the business;
- We have obtained the year end bad debt provision calculation and reviewed the accuracy of management's calculation in the context of historical trends and plans for future collection and to test whether it is calculated in line with the Company's policy;
- Our IT specialists have performed procedures to gain assurance over the historical cash collection rates information derived from the billing system; and
- We tested the control environment including the IT controls within the accounting system and billing system to ensure that these systems have an effective control environment

Key observations

Overall, the valuation of trade receivables is reasonable and consistent with the prior year.

Independent Auditor's Report

Classification of costs between operating and capital expenditure

Key audit matter description



Water companies make a significant investment each year in the infrastructure network and above ground assets, which includes repairs, infrastructure renewals, upgrades on tangible fixed assets and new capital expenditure. Identifying which expenditure represents capital expenditure rather than renewal expenditure may include significant judgement.

Property, plant and equipment ("PPE") additions in the year were £45.4m disclosed in Note 11 (31 March 2017: £36m).

Expenditure in relation to increasing the capacity or enhancing the tangible asset base is treated as capital expenditure. Capital projects may contain a combination of enhancement and maintenance activity which are not distinct and therefore there is a key audit matter that PPE is valued incorrectly as a result of items of operating expenditure being misclassified. Due to the level of judgement involved, we have determined that there is a risk of inappropriate bias in the accounting of the balance.

How the scope of our audit responded to the key audit matter

- We have tested the design, implementation and operating effectiveness of controls over the capitalisation of expenditure;
- We selected a sample of capital additions to test that they went through the documented approval process and we agreed amounts capitalised to supporting invoices;
- We have reviewed and audited a sample of the assets in the course of construction including a consideration of whether the assets were in use at year end and if they meet the classification criteria;
- We have performed a critical assessment and challenge of the process for the capitalisation of internal labour costs and overheads and the assessment of which costs are suitable to be capitalised. A sample of those costs have been selected to test whether they have been appropriately capitalised in accordance with the requirements of FRS 102; and
- We have obtained a detailed understanding of a sample of infrastructure renewals to assess whether these have been appropriately allocated as expenses.

Key observations

Overall, we are satisfied that the classification of costs between capital assets and operating expenditure is appropriate.

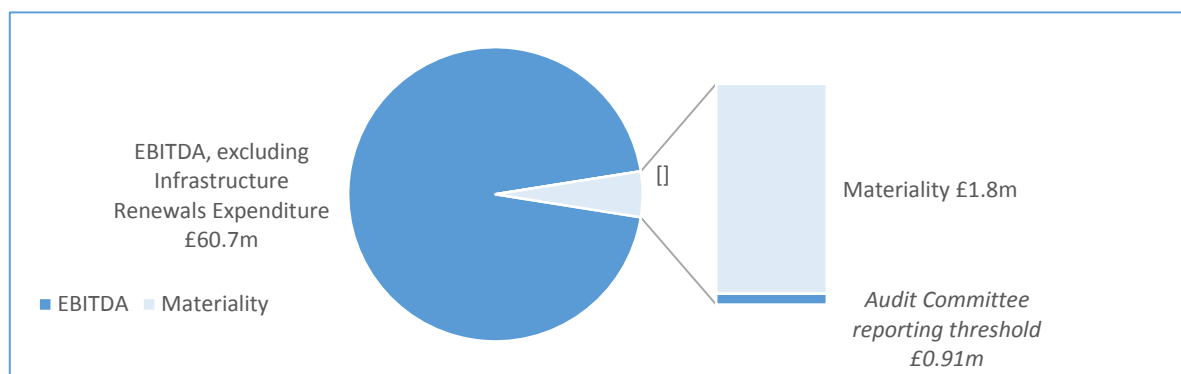
Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Materiality	£1.8m (2017: £1.5m)
Basis for determining materiality	3% of earnings before interest, tax, depreciation and amortisation ('EBITDA').
Rationale for the benchmark applied	We have used EBITDA, excluding Infrastructure Renewals Expenditure as the benchmark for determining materiality as this benchmark is deemed to be a key driver of business value, is a critical component of the financial statements and is a focus for users of those financial statements.

Independent Auditor's Report



We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £91,000 (2017: £81,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our audit was scoped by obtaining an understanding of the entity and its environment, including internal control, and assessing the risks of material misstatement. Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon.

We have nothing to report in respect of these matters.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

Independent Auditor's Report

Responsibilities of directors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

Independent Auditor's Report

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made.

We have nothing to report in respect of this matter.

Other matters

Auditor tenure

We were appointed by the Board on 31 July 2002 to audit the financial statements for the year ending 31 March 2003 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is 16 years, covering the years ending 31 March 2003 to 31 March 2018.

Consistency of the audit report with the additional report to the audit committee

Our audit opinion is consistent with the additional report to the audit committee we are required to provide in accordance with ISAs (UK).

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.



Jacqueline Holden, FCA (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
London
United Kingdom
13 July 2018

Profit and Loss Account

For the year ended 31 March 2018

		2018	2017
	Note	£'000	£'000
Turnover	2	124,082	123,686
Operating costs (net)	3	(93,712)	(91,069)
Operating Profit		30,370	32,617
Finance charges (net)	7	(11,697)	(12,197)
Profit on ordinary before taxation		18,673	20,420
Taxation on profit ordinary activities	8	(3,317)	(1,575)
Profit on ordinary activities after taxation		15,356	18,845
Earnings per share			
Basic	10	723.2p	887.6p
Diluted	10	723.2p	887.6p

The results above are derived from continuing operations.

The accompanying notes are an integral part of these financial statements.

Balance Sheet

As at 31 March 2018

	Note	2018 £'000	2017 £'000
Fixed Assets			
Tangible assets	11	511,021	488,985
Current Assets			
Stocks	14	1,714	1,747
Debtors - amounts recoverable within one year	15	30,407	32,320
Debtors - amounts recoverable in more than one year	15	43,547	43,667
Investments	16	2	2
Cash at bank and in hand		2,192	8,723
		77,862	86,459
Borrowings - amounts falling due within one year	17	(2,041)	(218)
Other Creditors - amounts falling due within one year	17	(59,183)	(60,315)
Net current assets		16,638	25,926
Total assets less current liabilities		527,659	514,911
Borrowings - amounts falling due after more than one year	18	(260,902)	(249,834)
Other Creditors - amounts falling due after more than one year	18	(12,727)	(23,226)
Accruals and deferred income - falling due after more than one year	13	(146,496)	(138,862)
Provisions for liabilities - falling due after more than one year	20	(39,336)	(34,534)
Net Assets		68,198	68,455
Capital and Reserves			
Called up share capital	21	2,123	2,123
Share premium account		495	495
Hedging reserve		(6,153)	(7,280)
Revaluation Reserve		34,441	34,894
Capital Redemption Reserve		4,450	4,450
Profit and loss account		32,842	33,773
Shareholders' Funds		68,198	68,455

The accompanying notes are an integral part of these financial statements.

The financial statements of South Staffordshire Water PLC (Company number 2662742) were approved by the Board of Directors and authorised for issue on 13 July 2018



Phil Newland

Statement of Comprehensive Income

For the year ended 31 March 2018

	2018	2017
	£'000	£'000
Profit on ordinary activities after taxation	15,356	18,845
Movement in hedging reserve	1,358	(320)
Deferred tax impact of movement in hedging reserve	(231)	54
Deferred tax rate move impact in year	-	(84)
Total comprehensive income	16,483	18,495

Statement of Changes in Equity

As at 31 March 2018

	Called up Share Capital	Share Premium Account	Capital Redemption Reserve	Revaluation Reserve	Profit and Loss Account	Hedging Reserve	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Balance at 1 April 2016	2,123	495	4,450	35,347	25,595	(6,930)	61,080
Profit for the Financial period	-	-	-	-	18,845	-	18,845
Change in value of hedging instruments - cash flow hedges (Gross of deferred tax)	-	-	-	-	-	(501)	(501)
Deferred tax impact of change in value of hedging instruments	-	-	-	-	-	85	85
Amounts recycled to profit and loss (Gross of deferred tax)	-	-	-	-	-	181	181
Deferred tax impact of amounts recycled to profit and loss	-	-	-	-	-	(31)	(31)
Deferred tax rate move	-	-	-	-	-	(84)	(84)
Amounts transferred to profit and loss	-	-	-	(453)	453	-	-
Total comprehensive income	2,123	495	4,450	34,894	44,893	(7,280)	79,575
Dividends (Note 9)	-	-	-	-	(11,120)	-	(11,120)
Balance at 31 March 2017	2,123	495	4,450	34,894	33,773	(7,280)	68,455
Profit for financial period	-	-	-	-	15,356	-	15,356
Change in value of hedging instruments - cash flow hedges (Gross of deferred tax)	-	-	-	-	-	1,177	1,177
Deferred tax impact of change in value of hedging instruments	-	-	-	-	-	(200)	(200)
Amounts recycled to profit and loss (Gross of deferred tax)	-	-	-	-	-	181	181
Deferred tax impact of amounts recycled to profit and loss	-	-	-	-	-	(31)	(31)
Amounts transferred to profit and loss	-	-	-	(453)	453	-	-
Total comprehensive income	2,123	495	4,450	34,441	49,582	(6,153)	84,938
Dividends (Note 9)	-	-	-	-	(16,740)	-	(16,740)
Balance at 31 March 2018	2,123	495	4,450	34,441	32,842	(6,153)	68,198

Cash Flow Statement

As at 31 March 2018

	Note	2018		2017	
		£'000	£'000	£'000	£'000
Cash inflow from operating activities			47,591		52,953
Corporation tax paid			(1,933)		(2,786)
Net cash inflow from operating activities	(a)		45,658		50,167
Cash flows from investing activities					
Purchase of tangible fixed assets		(46,547)		(32,624)	
Proceeds from sale of tangible fixed assets		527		679	
Proceeds from disposal of non-household retail assets to fellow group undertaking		8,400		-	
Capital contributions received		10,047		6,827	
Part repayment of long-term balance with group undertaking		(8,992)		(10,200)	
Interest received		2,545		2,545	
Net cash outflow from investing activities			(34,020)		(32,773)
Cash flows from financing activities					
Interest paid		(8,881)		(8,756)	
Equity dividends paid		(16,740)		(11,120)	
Draw down of short term bank loans		2,050		-	
Draw down of long term bank term loans		5,402		-	
Capital element of finance lease and hire-purchase rental payments		-		(174)	
Net cash outflow from financing activities			(18,169)		(20,050)
Decrease in cash			(6,531)		(2,656)
Cash or Cash Equivalents at the beginning of the year			8,723		11,379
Cash or Cash Equivalents at the end of the year			2,192		8,723

Purchase of tangible fixed assets relates to the cash paid out in the year in relation to fixed asset additions. The difference in that paid £46,547,000 and additions in the fixed asset note 11 of £45,434,000 is due to a decrease in year of creditors due relating to capital purchases of £1,113,000.

Notes to Cash Flow Statement

(a) Reconciliation of Operating Profit to Net Cash Inflow from Operating Activities

	2018		2017	
	£'000	£'000	£'000	£'000
Total operating profit		30,370		32,617
Depreciation	22,660		22,275	
Amortisation of capital contributions	(2,413)		(2,318)	
Profit on disposal of tangible fixed assets	(499)		(590)	
		19,748		19,367
Decrease / (Increase) in stocks	34		(193)	
Increase in debtors	(6,538)		(3,083)	
Increase in creditors	3,977		4,245	
Cash inflow from operating activities		(2,527)		969
Corporation tax paid		(1,933)		(2,786)
Net cash inflow from operating activities		45,658		50,167

(b) Reconciliation in Movement in Net Debt

	2018		2017	
	£'000	£'000	£'000	£'000
Decrease in cash		(6,531)		(2,656)
Movements in finance lease (cash)		-		174
Movements in finance lease (non-cash)		218		-
Draw down of bank loans (cash)		(7,452)		-
Bank term issue cost amortisation (non-cash)		(38)		(85)
Movement on index-linked debt (non-cash)		(5,618)		(6,269)
Increase in net debt in year		(19,421)		(8,836)
Net debt brought forward		(241,330)		(232,494)
Net debt carried forward		(260,751)		(241,330)

Notes to Cash Flow Statement

	Balance 1 April 2017	Cash Flow	Non-Cash Movements	Balance at 31 March 2018
	£'000	£'000	£'000	£'000
Cash at bank and in hand	8,723	(6,531)	-	2,192
Short-term bank loans	-	(2,050)	9	(2,041)
	8,723	(8,581)	9	151
Irredeemable debenture stock	(1,652)	-	-	(1,652)
Movements on finance leases and hire purchase contracts	(218)	-	218	-
Bank loans (net of issue costs)	(29,868)	(5,402)	(47)	(35,318)
Index-linked debt (net of issue costs and including premium)	(218,315)	-	(5,618)	(223,933)
Net debt	(241,330)	(13,983)	(5,438)	(260,751)

	31 March 2018	31 March 2017
	£'000	£'000
Book net debt (as reported above)	(260,751)	(241,330)
Exclude book premium on issue of index linked debt	13,768	14,079
Difference between long-term RPI assumption and actual RPI inflation	7,840	9,199
Exclude unamortised issue costs	(1,814)	(1,890)
Exclude accrued interest	209	202
Net debt reported for borrowing covenants	(240,748)	(219,740)
Regulated Asset Value	364,318	347,600
Covenant Net Debt / Regulated Asset Value	66.1%	63.2%

It is noted that the covenant net debt value as opposed to the book net debt value is used by stakeholders, including investors, lenders and rating agencies, to monitor key financial metrics such as the Net Debt / Regulated Asset Value as shown above.

Notes to the Financial Statements

Notes

1. Statement of accounting policies

The principal accounting policies are summarised below. They have all been applied consistently throughout the year and to the preceding year.

The Company meets the definition of a qualifying entity under FRS 102 and has therefore taken advantage of the disclosure exemptions available to it in respect of its related parties. South Staffordshire Water PLC is consolidated in the financial statements of its ultimate holding company in the United Kingdom Company, Hydriades IV Limited which may be obtained from Companies House in the UK. The holding company's registered address is Green Lane, Walsall, West Midlands, WS2 7PD.

a) General information and basis of accounting

South Staffordshire Water PLC is a public listed company limited by shares incorporated in the United Kingdom under the Companies Act 2006 and is registered in England and Wales. The address of the registered office is Green Lane, Walsall, West Midlands, WS2 7PD. The nature of the Company's operations and its principal activities are set out in the strategic report on pages 5 to 42. The financial statements have been prepared under the historical cost convention, modified to include certain items at fair value, and in accordance with Financial Reporting Standard 102 (FRS 102) issued by the Financial Reporting Council. The functional currency of the Company is considered to be pounds sterling because that is the currency of the primary economic environment in which the Company operates.

b) Turnover

Turnover comprises the value of sales (excluding VAT and similar taxes) of goods and services in the normal course of business. For water supplied turnover includes amounts billed for water supplied in the year together with an estimation of amounts supplied but unbilled at the year end. Further information on the Company's revenue recognition policy is shown on page 116 of the APR.

c) Tangible fixed assets and depreciation

Tangible fixed assets comprise infrastructure assets (water mains, impounding and pumped raw water storage reservoirs and dams), operational structures (pumping stations, treatment stations, boreholes and service reservoirs) and other assets.

Infrastructure assets

Infrastructure assets comprise a network of systems include two regional network assets that, as a whole, are intended to be maintained in perpetuity at a specified level of serviceability by the continuing replacement and refurbishment of their components. Expenditure on infrastructure assets relating to increases in capacity or enhancements of the networks is treated as additions which are capitalised at cost.

Infrastructure renewals expenditure which is the annual expenditure required to maintain the operating capability of the network is not capitalised within tangible fixed assets but is expensed within operating costs for the year. In accordance with FRS 102, new infrastructure assets are depreciated over their useful economic life of 100 years.

The deemed cost of existing infrastructure assets determined as part of the transition to FRS 102 in the prior year is being depreciated over the estimated remaining economic life of 80 years.

Notes to the Financial Statements

Operational structures and other fixed assets

Operational structures and other fixed assets are stated at cost less accumulated depreciation and provisions for impairment. Depreciation is provided on a straight-line basis to write off the cost, less estimated residual value, over the estimated useful lives of the assets, with the exception of land, which is not depreciated. The estimated useful lives of the assets are as follows:

Buildings and Service Reservoirs	50-80 years
Boreholes	100 years
Fixed Plant	20-30 years
Meters	15 years
Mobile Plant	5 years
Motor Vehicles	3-7 years
Office Equipment	5-7 years

d) Capital contributions

Capital contributions, including those in respect of infrastructure assets, are treated as deferred income and released to operating costs over the useful lives of the assets concerned.

e) Leased assets

Assets financed by leasing agreements, which transfer substantially all of the risks and rewards of ownership to the Company, are included within fixed assets, and the net obligation to pay future rentals is included in creditors. Rentals are apportioned between finance charges and a reduction of the outstanding liability for future rentals so as to produce a constant charge to the profit and loss account based upon the capital outstanding.

f) Stocks

Stocks and work in progress are valued at the lower of cost and net realisable value. Cost includes materials and an appropriate element of overheads. Provision is made for obsolete, slow-moving or defective items where appropriate.

g) Pensions

For the defined contribution schemes the amount charged to the profit and loss account is the contributions payable in the year. Both sections (South Staffs and Cambridge) of the defined benefit scheme are closed to new entrants and have ceased future accruals. In accordance with the agreed policy in the Company and the Group, as the scheme is a multi-employer scheme with deferred members of the scheme also being employees of other Group companies the Company is not able to identify its share of the scheme's assets and liabilities on a reasonable and consistent basis. Therefore, in accordance with the stated policy the amount charged to the profit and loss account of the Company is equivalent to the deficit contributions payable in the year by the Company with the profit and loss items, actuarial gains and losses and assets and liabilities relating to the scheme being accounted for in the accounts of South Staffordshire Plc, the immediate holding company.

h) Research and development

Research and development is charged to the profit and loss account in the year in which it is incurred.

i) Taxation

Current tax is charged on estimated taxable profits at the current rate.

Deferred taxation is provided in respect of capital allowances in excess of depreciation and all other timing differences that have originated but not reversed at the balance sheet date using the future rate of tax anticipated at the time of reversal based on legislation changing rates enacted or substantively enacted at the balance sheet date.

Notes to the Financial Statements

j) Financial instruments

Financial assets

All financial assets, being cash and cash equivalents, trade debtors and loans receivable are measured at amortised cost. Cash and cash equivalents comprise cash at bank and in hand and short-term deposits.

Financial liabilities

Financial liabilities are initially measured at fair value and subsequently measured at amortised cost. The premium/discount and costs of issue are amortised over the life of the instrument, with the amortisation being included in the effective interest rate of the instrument which is included in finance charges (net) in the profit and loss account.

k) Hedge accounting

The Company has entered into derivative financial instruments to hedge exposure to floating interest rates. These derivative financial instruments are recorded on the balance sheet at fair value on inception and at each balance sheet date. Movements in fair value are recorded in the profit and loss account except where hedge accounting has been adopted by the Company.

The Company designates certain hedging instruments as cash flow hedges. At inception of the hedge relationships, the Company documents the relationships between the hedging instruments and the hedged items along with the Company's risk management strategy and objectives in relation to each hedge. At the inception of the hedges, and on an ongoing basis, the Company documents whether the hedging instruments are highly effective in offsetting changes in cash flows of hedged items.

The effective proportion of changes in fair value of hedging instruments that are designated and qualify as cash flow hedges are deferred in equity in a hedging reserve net of deferred tax. The gain or loss relating to the ineffective proportion is recognised immediately in the profit and loss account. Hedge accounting is discontinued when the Company de-designates the hedging relationships, the hedging instruments expire, are terminated or are sold or they no longer qualify for hedge accounting. Amounts deferred in the hedging reserve are recycled to the profit and loss account in the periods when the hedged items are recognised in the profit and loss account. When forecast transactions are no longer expected to occur, the cumulative gains or losses are recognised immediately in the profit and loss account.

l) Dividends

Dividends are recognised in the profit and loss account if they have been paid or if they have been approved by the Company's Board and shareholders before the period end.

m) Exceptional items

The Company separately presents certain items on the face of the profit and loss account as exceptional. Exceptional items are material items of income or expense that, because of their size or incidence, are presented separately to allow an understanding of the Company's financial performance and comparison to the prior year. They are not expected to be incurred on a recurring basis.

Principal accounting judgements, estimates and assumptions

In the application of the accounting policies, which are described above, the Directors are required to make judgements, estimates and assumptions in respect of the carrying amounts of assets and liabilities recognised in the financial statements. These are based on historical experience, future forecasts and other factors that are considered to be relevant. It is recognised that historical experience and forecasts change over time and these judgements, estimates and assumptions are therefore reviewed and amended where necessary on a regular basis. However, it is also recognised that the actual outcomes may still differ to the judgements, estimates and assumptions made. Provided below are details of the principal accounting judgements, estimates and assumptions that the Directors have made when applying the Company's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

Notes to the Financial Statements

The more significant judgements were:

Hedge accounting

In applying the Company's interest rate hedging strategy and the corresponding hedge accounting applied in the financial statements a judgement has been made that there will be highly probable floating interest rate payments over the term of the interest rate derivatives. Underlying this judgement is the assessment that the future refinancing of bank facilities is highly probable. The basis for this judgement includes the Company's long-term 25-year water supply licence, its related long-term business model and regulated asset base, its ability to access capital markets including the bank debt market, its strong investment grade credit rating and also the stability and predictability of the regulated UK water sector as a whole.

Tangible fixed assets – Determining costs which are capital in nature

Judgment is required to determine whether costs incurred when work is carried out on Company assets are capital or revenue in nature. This work includes repairs, like-for-like replacement, new assets or replacement of assets with an element of asset enhancement or increased capacity. Identifying which element of expenditure represents capital expenditure rather than revenue expenditure may include judgement that the Company's two regional infrastructure networks each represent single infrastructure assets. In order to apply the appropriate accounting, a judgement is made as to whether it is probable that the expenditure will generate future economic benefits and also if the costs can be measured reliably.

The key accounting estimates were:

Accrued income

An estimate of water consumption by metered customers since the date of the last water bill and an estimate of the corresponding income that remains unbilled at the end of the year (accrued income) is required to be made each year. This estimate uses a historical water consumption rate for each customer from the Company's billing system and applies this consumption rate to the unbilled period and the related tariff to estimate unbilled income for that period. The accrued income for metered customers as at 31 March 2018 was £11,132,000 (2017: £14,190,000), with the reduction due to the Company's exit from the non-household retail market.

Amortised cost of index-linked borrowings

In order to record the Company's index-linked borrowings at amortised cost an estimate of the long-term average inflation rate (Retail Price Index - RPI) per annum is required to be made. In forming this estimate, financial market data such as the long-term yields for fixed rate and index-linked (RPI) gilts is obtained and considered with the difference between these yields being the market implied long-term inflation assumption. The net book value of index-linked borrowings as at 31 March 2018 was £223,933,000 (2017: £218,315,000).

Bad and doubtful debt provision

The recoverability of trade debtors, and therefore the amount of bad and doubtful debt provision held against trade debtors in the balance sheet at each year-end, requires judgement. This judgement requires consideration of the historical and forecast debt collection rates in respect of different categories of customers and trade debt, usually calculated as a percentage of the total amount billed in each year. This information is used in order to estimate the level of debt outstanding at the end of the year which is expected to be irrecoverable after following the processes of collection that the Company adopts. This estimate represents the appointed year-end bad and doubtful debt provision which was £34,055,000 as at 31 March 2018 (2017: £33,558,000).

Tangible fixed assets – Assessment of useful economic lives

There is a requirement to estimate the useful economic lives of the Company's tangible fixed assets in order to depreciate the cost or deemed cost of these assets and make an appropriate charge to the profit and loss account over that period for each asset. This estimate is based on a combination of engineering data, experience of similar assets and on the businesses forecast replacement or rehabilitation cycle and its investment plan. Industry practice is also considered as part of the overall estimate of assets lives.

The total net book value of tangible fixed assets as at 31 March 2018 is £511,021,000 (2017: £488,985,000)

Notes to the Financial Statements

2. Segmental information

The Directors consider that the Company operates substantially in the UK in one class of business, that being water supply. No analysis of turnover, profit before tax or net assets, by geographical area or class of business, is considered necessary. Revenue from UK operations in the year was £124,082,000 (2017: £123,686,000).

On 1 April 2017 the OpenWater market commenced allowing competition in the non-household retail market for water supply and the non-household retail operations of the Company were transferred to SSWB Limited. As a consequence of this the retail element of non-household water no longer forms part of the turnover of South Staffordshire Water PLC. The value of this in 2017 was £2.9m.

Notes to the Financial Statements

3. Operating costs (net)

	2018	2017
	£'000	£'000
Operating costs (net) were as follows:		
Other operating income (see note 6)	(1,250)	(985)
Raw materials and consumables	4,656	4,219
Staff costs (see note 4)	20,233	20,058
Own work capitalised	(8,399)	(8,014)
Depreciation : non-infrastructure assets	19,105	18,803
Depreciation : infrastructure assets	3,555	3,472
Infrastructure renewals expenditure	10,078	8,736
Amortisation of capital contributions	(2,413)	(2,318)
Other operating costs	48,147	47,098
	<hr/> 93,712	<hr/> 91,069

Auditor remuneration is analysed as follows:

	2018	2017
	£'000	£'000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	73	67
Other services pursuant to legislation	49	47
	<hr/> 122	<hr/> 114

There were no non-audit services payable in the period (2017: Nil).

4. Staff costs

	2018	2017
	£'000	£'000
Wages and salaries	15,528	15,416
Social security costs	1,572	1,506
Pension costs (see note 22)	3,133	3,136
	<hr/> 20,233	<hr/> 20,058

	2018	2017
	Number	Number
Monthly average number of employees	410	407

Notes to the Financial Statements

5. Directors' remuneration

	2018	2017
	£'000	£'000
Emoluments	344	324

Contributions made by the Company in respect of money purchase pension schemes for directly employed Directors was £21,000 (2017:£21,000).

The highest paid directly employed Director received emoluments of £244,000 (2017: £244,000) and he was not a member of a defined benefit pension scheme and had contributions of £21,000 (2017:£21,000) paid by the Company in respect of defined contribution pension schemes during the year.

During the year and the prior year, certain Directors received no emoluments as Directors of this Company. These directors were remunerated by the immediate parent company, South Staffordshire Plc, (or received no remuneration for their services) and the total of their emoluments received during the year was £352,000 (2017: £383,000). Contributions in respect of money purchase pension schemes for these Directors was £58,000 (2017: £61,000).

No Directors (2017: Nil) who held office at the end of the year were accruing benefits due in the year under a defined benefit pension scheme and 2 Directors (2017: 2) were contributing members under a money purchase scheme.

The remuneration report on pages 61 to 64 gives further detail around the remuneration of the Directors and Executive Team.

6. Other operating income

	2018	2017
	£'000	£'000
Profit on disposal of fixed assets	499	590
Rental income	751	395
	1,250	985

Notes to the Financial Statements

7. Finance charges (net)

	2018	2017
	£'000	£'000
Interest payable and similar charges:		
Index-linked debt (Cash)	7,385	7,131
Index-linked debt (Non-cash)	5,618	6,269
Bank loan and other interest	991	1,092
Finance charges in respect of finance leases	-	1
Debenture interest	67	68
	<hr/> 14,061	<hr/> 14,561
Interest receivable:		
Loans to parent undertakings	(2,545)	(2,545)
	<hr/> 11,516	<hr/> 12,016
Other finance charges:		
Amounts recycled from hedging reserve	181	181
	<hr/> 11,697	<hr/> 12,197

Notes to the Financial Statements

8. Taxation on profit on ordinary activities

	2018	2017
	£'000	£'000
Current tax:		
UK corporation tax at 19% (2017: 20%)	3,533	4,243
Adjustments in respect of prior periods	(4,787)	(2,641)
Total current tax (credit) / charge	(1,254)	1,602
Deferred tax:		
Origination and reversal of timing differences	254	(30)
Impact of changes in future tax rates	-	(2,349)
Adjustments in respect of prior periods	4,317	2,352
Total deferred tax charge / (credit)	4,571	(27)
Total tax charge	3,317	1,575
Tax included in statement of comprehensive income		
Deferred tax:		
Movement in hedging reserve	231	(54)
Effect of change in deferred tax rate	-	84
Total tax charge	231	30

The adjustments to prior year current and deferred tax arise primarily as a result of the transition to FRS 102 in the year ended 31 March 2016. The change of basis of accounting for certain historical items gave rise to deferred tax temporary differences and the Company has, in the years ended 31 March 2017 and 31 March 2018, revised its estimate of the impact of this transitional adjustment on current and deferred tax.

Notes to the Financial Statements

Factors affecting the total tax charge

The tax assessed on the profit on ordinary activities for the year is lower than the standard rate of corporation tax in the UK of 19% (2017 - 20%). The differences are reconciled below.

	2018	2017
	£'000	£'000
Profit on ordinary activities before tax	18,673	20,420
Profit on ordinary activities multiplied by standard		
UK corporation tax rate of 19% (2017: 20%)	3,548	4,084
Expenses not deductible for tax purposes (net)	269	123
Deferred tax provided at lower rate	(30)	6
Effect of changes in deferred tax rate	-	(2,349)
Adjustments in respect of prior years	(470)	(289)
Total tax charge	3,317	1,575

Factors that may affect the future tax charge

A reduction in the future UK corporation tax rate from 18% to 17% was substantively enacted in October 2016 and will take effect in April 2020. Deferred tax has been recognised at 17% (2017: 17%) on the basis of the expected reversal period.

No deferred tax has been recognised on capital gains rolled over against the cost of acquisition of certain property and structures owned by South Staffordshire Water PLC. The gains will come into charge if the assets are sold and not replaced by suitable qualifying assets. As the properties are essential assets of the water supply business it is regarded as unlikely that the gains will come into charge. The potential deferred tax amounts to £1,858,000 (2017: £1,847,000).

Notes to the Financial Statements

9 Dividends paid

	2018	2017
	£'000	£'000
Equity Interests		
Ordinary Dividends paid of 788.4p (2017: 523.7p) per share	16,740	11,120

In 2018 the dividend was made up of £5,000,000 from the Appointed Business (2017: £6,500,000); £1,340,000 from the Non-Appointed Business (2017: £2,600,000); £2,000,000 from intra-group interest to be paid back to the Company (2017: £2,000,000); and £8,400,000 from the one off proceeds of the sale of the Non Household Retail Business (2017: Nil).

Further details of the dividends paid in the year are provided on page 28 of the Strategic Report

10 Earnings per share

The calculation of earnings per share is based on the profit on ordinary activities after taxation divided by the weighted average number of shares in issue during the year.

The calculations of earnings per share are based on the following profits and number of shares:

	2018	2017
	£'000	£'000
Profit on ordinary activities after taxation and profit for earnings per share	15,356	18,845

	2018	2017
	Number of Shares	Number of Shares
Weighted average number of shares for basic and diluted earnings per share	2,123,210	2,123,210

Notes to the Financial Statements

11 Tangible fixed assets

	Specialised Operational Assets £'000	Non Specialised Operational Assets £'000	Infrastructure Assets £'000	Other Tangible Assets £'000	Total £'000
Cost					
At 1 April 2017	202,929	23,260	458,410	192,377	876,976
Additions	19,767	103	11,538	14,026	45,434
Disposals	-	(125)	-	(1,233)	(1,358)
At 31 March 2018	222,696	23,238	469,948	205,170	921,052
Depreciation					
At 1 April 2017	93,638	7,248	177,938	109,167	387,991
Charge for the year	6,903	385	3,555	11,817	22,660
Disposals	-	(49)	-	(571)	(620)
At 31 March 2018	100,541	7,584	181,494	120,412	410,031
Net Book Value					
At 31 March 2018					
Owned	121,802	15,654	288,454	84,476	510,385
Leased	353	-	-	283	636
	122,155	15,654	288,454	84,759	511,021
Net Book Value					
At 31 March 2017					
Owned	108,743	16,012	280,472	82,729	487,956
Leased*	548	-	-	481	1,029
	109,291	16,012	280,472	83,210	488,985

*Restated to present leased assets appropriately.

Tangible fixed assets financed by leasing and hire-purchase contracts amounted to £7,375,000 (2017: £7,886,000) less accumulated depreciation of £6,739,000 (2017: £6,857,000). Depreciation charged to the profit and loss account for the year in respect of leased assets amounted to £143,000 (2017: £221,000). Tangible fixed assets include freehold land of £2,337,000 (2017: £2,465,000) which is not subject to depreciation.

Tangible fixed assets in the course of construction or commissioning included in the above table had a cost of £36,537,000 at 31 March 2018 (2017: £16,928,000).

Notes to the Financial Statements

12 Commitments

Capital commitments outstanding at 31 March 2018 were £10,572,000 (2017: £6,700,000).

13 Capital contributions – Accruals and deferred income

	Infrastructure Assets	Other Assets	Total
	£'000	£'000	£'000
Balance at 1 April 2017	130,401	8,461	138,862
Capital contributions received	7,180	2,867	10,047
Transfers	446	(446)	-
Amortised in year	(1,639)	(774)	(2,413)
Balance at 31 March 2018	136,388	10,108	146,496

An amount included in the above balance is expected to be amortised in the next year. However due to the varied timing of receipts, the movement of associated projects from work in progress to completion, and general changes in the work undertaken as part of the capital programme this balance has not been segregated.

Notes to the Financial Statements

14 Stocks

	2018	2017
	£'000	£'000
Raw materials and consumables	1,714	1,747

There is no material difference between the balance sheet value of stocks and their replacement cost.

15 Debtors

	2018	2017
	£'000	£'000
Amounts recoverable within one year:		
Trade debtors	12,554	16,262
Other debtors	80	9
Amounts due from other group undertakings	1,916	1,916
Amounts due from parent undertakings	364	364
Prepayments and accrued income	15,493	13,769
	30,407	32,320
Amounts recoverable in more than one year:		
Loans receivable from parent undertakings	40,000	40,000
Other amounts owed by parent undertakings	3,547	3,667
	43,547	43,667
	73,954	75,987

Detail of provisions against bad debt are shown in note 23 on page 102.

16 Investments

	2018	2017
	£'000	£'000
Investments	2	2

The balance represents the cost of investment of £1,596 related to 798 "A" ordinary shares and 8% of unsecured loan stock of WRc PLC, a research-based group, providing consultancy in the water, waste and environment sectors, incorporated in England and Wales.

Notes to the Financial Statements

17 Creditors – amount falling due within one year

	2018	2017
	£'000	£'000
Bank loans (unsecured and net of issue costs)	2,041	-
Obligations under finance leases	-	218
Borrowings	2,041	218
Payments received in advance	22,014	22,114
Trade creditors	18,767	19,637
Other creditors	7,812	7,719
Amounts owed to other Group undertakings	8,554	6,205
Corporation tax payable	916	4,103
Other taxation and social security	1,120	537
Other creditors	59,183	60,315
	61,224	60,533

The gross bank loans (unsecured) of £2,050,000 (2017: nil) included in amounts falling due within one year is used for covenant reporting purposes but, in accordance with FRS 102, is stated above net of unamortised issue costs. This consists of a facility of £15,000,000 of which £2,050 was drawn at 31 March 2018 which matures in March 2019.

18 Creditors – amount falling due after more than one year

	2018	2017
	£'000	£'000
Irredeemable debenture stock (unsecured) (note 19)	1,633	1,633
Perpetual debenture stock (unsecured)	19	19
Bank loans (unsecured and net of issue costs):		
payable between two and five years	35,318	29,868
Retail Price Index-linked debt (unsecured)	223,933	218,315
Borrowings	260,902	249,834
Other creditors	9,754	10,083
Amounts owed to other Group undertakings	1,304	10,296
Derivative financial liabilities	1,669	2,846
Creditors	12,727	23,226
	273,629	273,060

The gross bank loans (unsecured) of £35,402,000 (2017: £30,000,000) included in amounts falling due after more than one year is used for covenant reporting purposes but, in accordance with FRS 102, is stated above net of unamortised issue costs. These consist of two loans at a total of £30,000,000 which mature in December 2020 and another facility of £10,000,000 of which £5,402,000 was drawn at 31 March 2018 which matures in March 2023.

Derivative financial liabilities represent the market value of floating to fixed rate interest rate swaps designated as cash flow hedges.

The book value index-linked debt of £223,933,000 (2017: £218,315,000) is stated above at amortised cost in accordance with FRS 102. The indexed principal of £203,835,000 (2017: £196,594,000) is used for borrowing covenant reporting purposes. Details of the terms of our index-linked debt is shown on page 101 in note 23.

In the year the Company repaid the remaining balance payable to Cambridge Water PLC of £8,992,000. This had previously been categorised as a long term creditor, as there was no legal requirement to make a payment within the year.

Notes to the Financial Statements

19 Irredeemable debenture stock

	2018	2017
	£'000	£'000
3.5%	476	476
4.0%	627	627
5.0%	500	500
	1,603	1,603
Net premium on irredeemable debenture stock	30	30
	1,633	1,633

20 Provisions for liabilities

	Deferred Taxation	
	£'000	
At 1 April 2017	34,534	
Charged to profit and loss account	4,571	
Charged to other comprehensive income	231	
At 31 March 2018	39,336	
	2018	2017
	£'000	£'000
Analysis of deferred tax		
Accelerated Capital Allowances	40,592	36,315
Timing differences in respect of hedging reserves	(1,260)	(1,491)
Timing differences in respect of finance charges	(174)	(179)
Other timing differences	179	(111)
Provision for deferred tax	39,336	34,534

Deferred tax assets and liabilities are offset only where the Company has a legally enforceable right to do so and where the assets and liabilities relate to taxes levied by the same taxation authority.

21 Share capital

	2018	2017
	£'000	£'000
Authorised:		
8,800,000 Ordinary shares of £1 each	8,800	8,800
Allotted, called-up and fully-paid:		
2,123,210 Ordinary shares of £1 each	2,123	2,123

Notes to the Financial Statements

22 Pension retirement benefits

The Company operates a number of funded pension schemes for the benefit of its employees. The Company participates in the Water Companies Pension Scheme, by way of a separate section (the South Staffordshire Section of the Scheme) which provides benefits based on pensionable pay. The scheme was closed to all future benefit accrual with effect from 1 April 2015 and as such only funding deficit contributions are now being paid by the Company into the Scheme (with these being £1,814,000 in the year ended 31 March 2018 and £1,778,000 in the year ended 31 March 2017) with an equivalent amount charged to the profit and loss account in the year. No current service contributions are now paid. There was also £442,000 (2017: £433,000) charged to the profit and loss account in relation to the Cambridge section of the Water Companies Pension Scheme. The assets and liabilities of the South Staffordshire section of the Scheme are accounted for in the accounts of the immediate parent undertaking, South Staffordshire Plc. The assets and liabilities for the Cambridge section of the scheme are accounted for within Cambridge Water Plc. In addition, the Company participates in a defined contribution Money Purchase Pension Scheme. The assets of all schemes are held separate from those of the Company, and are invested by fund managers.

The contributions to the defined contribution scheme is charged against profits as incurred with the amount for the year ended 31 March 2018 being £877,000 (2017: £925,000).

Additional disclosures regarding the defined benefit pension scheme are required by FRS 102. The latest actuarial valuation of the South Staffordshire section of the scheme as at 31 March 2018, prepared for the purposes of the consolidated financial statements of the parent company under FRS 102 rather than on the actuarial basis used for funding purposes, shows a surplus before deferred tax of £52,974,000 (2017: surplus of £32,174,000). The market value of the assets in this section of the scheme and the present value of the liabilities in the scheme that were accounted for in the parent company at the balance sheet date were:

	2018	2017	2016
	Valuation	Valuation	Valuation
	£'000	£'000	£'000
Growth assets including equities and diversified growth funds	25,066	91,736	87,807
High yield bonds / gilts and liability driven investments	187,406	136,390	112,115
Emerging markets multi-asset funds	19,941	16,937	14,762
Cash / (Overdraft)	1,599	769	(230)
Market value of assets	234,012	245,832	214,454
Present value of scheme liabilities	(181,038)	(213,658)	(186,361)
Surplus in the scheme before deferred tax	52,974	32,174	28,093
Related deferred tax liability	(9,006)	(5,470)	(5,057)
Surplus after deferred tax	43,968	26,704	23,036

Notes to the Financial Statements

23 Financial assets and liabilities

The analysis of the Company's financial assets and liabilities included below includes cash, loans receivable, borrowings, trade creditors and trade debtors. Borrowings represent bank loans, finance lease obligations, index-linked borrowings and irredeemable and perpetual debenture stock. The main purpose of these financial instruments is to finance the Company's operations. It is, and has been throughout the period under review, the Company's policy that no trading in financial instruments shall be undertaken. The Company's policy in respect of cash, loans receivable and borrowings is to maintain flexibility with both long and short term debt while not exposing the Company to significant risk of market movements (see below). The Company is not exposed to any material foreign exchange risk.

Bank loans bear interest that is linked to LIBOR plus a bank margin which is applied to the drawn down element of each loan some of which are hedged through interest rate swaps.

Interest rate risk profile

Borrowings

The interest rate profile of the borrowings (stated at book value) of the Company as at 31 March 2018 was as follows:

	Fixed rate financial liabilities	Floating rate financial liabilities	Retail Price Index- Linked debt
	£'000	£'000	£'000
31 March 2018	31,600	7,410	223,933
31 March 2017	31,738	-	218,315

Floating rate loans that are hedged by the floating to fixed interest rate swaps are shown above as fixed rate. The Company's cash balances earn interest at floating rates linked to LIBOR or the Bank of England base rate. The Company's trade debtors and trade creditors are not subject to interest unless considered to be overdue.

For all financial assets and liabilities, the book values and fair values are not materially different, except for the Retail Price Index-linked Loan and the Retail Price Index-linked Bond shown in the table below:

	2018	2017
	£'000	£'000
Retail Price Index-Linked Loan		
Un-indexed Loan Value	111,400	111,400
Indexed / Covenant Loan Value	158,669	153,146
Book Value	176,447	172,134
Fair Value	328,808	328,909
Retail Price Index-Linked Bond		
Un-indexed Bond Value	35,000	35,000
Indexed / Covenant Bond Value	45,166	43,448
Book Value	47,486	46,181
Fair Value	59,686	61,793

Notes to the Financial Statements

Fixed rate borrowings

	Weighted average interest rate	Weighted average period for which rate is fixed
	%	Years
31 March 2018	2.8	2.8
31 March 2017	2.8	3.7

Borrowing facilities

The Company has various borrowing facilities available to it. The undrawn committed facilities available at 31 March 2018 in respect of which all conditions precedent have been met were as follows:

	2018	2017
	£'000	£'000
Expiring in one year or less	12,950	-
Expiring in more than one year but not more than two years	-	15,000
Expiring in more than two years but not more than five years	4,598	10,000
	<hr/> 17,548	<hr/> 25,000

In addition to the above at 31 March 2018 the Company had cash balances of £2,192,000 increasing liquidity headroom, to £19,740,000.

The Company is confident it has sufficient access to capital markets and relationships with banks and other lenders to refinance borrowing facilities that mature within 12 months of approval of the annual report and accounts.

Financial risks

The Company's activities result in it being subject to a limited number of financial risks, principally credit risk as the Company has financial assets receivable from third parties. Management of financial risks focuses on reducing the likely impact of these risks to a level that is considered acceptable. The Company has formal principles for overall risk management as well as specific policies to manage individual risks.

1) Interest rate risk

Interest rate risk arises from borrowings issued at floating rates including those linked to LIBOR and the Retail Price Index (RPI) that expose the Company's earnings and cash flows to changes in LIBOR and RPI. Risks of increases in LIBOR are managed by limiting the value and proportion of the Company's borrowings that are linked to this variable and by entering into floating to fixed rate swap contracts. Risks associated with increases in RPI are effectively hedged against the revenues and the Regulatory Asset Value of the regulated water business, both of which are also linked to RPI.

2) Credit risk

As is market practice, the Company grants customers credit on amounts due for the services it supplies, leading to limited risk over the recovery of the amounts receivable from these customers. Full details of the way this risk is managed are provided below. Credit risk also includes the risk of over recovery of loans receivable. This risk is managed by ensuring that loans are only made to entities with sufficient financial resources to both service and repay the loans.

3) Liquidity risk

Liquidity risk represents the risk of the Company having insufficient liquid resources to meet its obligations as they fall due. The Company manages this risk by regularly monitoring actual and forecast cash flows and ensuring that the payment of its obligations are at least matched with cash inflows and availability of adequate banking facilities including sufficient headroom. The table above details the undrawn committed borrowing facilities available to the Company to manage this risk.

Notes to the Financial Statements

Sensitivity analysis

The following analysis illustrates the sensitivity to reasonably possible movements during the year, in variables affecting financial liabilities, being LIBOR and the long term forecast for the UK Retail Price Index (RPI) on the pre-tax profit and loss account of the Company for the year ended 31 March 2018. There is no impact on reserves other than the impact on the profit and loss account after tax.

	2018	2017
	£'000	£'000
RPI +0.25%	(527)	(508)
RPI -0.25%	527	508
LIBOR +1.00%	(206)	(137)
LIBOR -1.00%	206	137

We have chosen a long term RPI forecast change of +/- 0.25% as “reasonably possible movements” in the year as a good estimate for possible variations in the long term forecast RPI over the period based on market data. LIBOR has remained at particularly low and stable levels over recent years, and + / - 1.0% is reasonable.

The impact on the pre-tax profit and loss account for 2018 detailed above has been calculated by assuming that the illustrated changes to the variables occurred on 1 April 2017 and remained different to the actual variables recorded by the stated amount during the year and with all other variables remaining at the actual amounts. The comparative figures have been calculated using the same methodology assuming the change to the variables occurred on 1 April 2016.

Notes to the Financial Statements

Maturity of financial assets and liabilities

The maturity profile of the Company's financial liabilities at current repayment value, not the book value, at 31 March 2018 was as follows:

	2018	2017
	£'000	£'000
Borrowings		
In one year or less or on demand	2,050	218
In more than one year, but not more than two years	-	-
In more than two years, but not more than five years	35,402	30,000
In more than five years	-	-
In more than twenty years	205,487	198,246
	<hr/> 242,939	<hr/> 228,464
Other Financial Liabilities		
In one year or less or on demand	59,183	60,315
In more than one year, but not more than two years	479	454
In more than two years, but not more than five years	3,497	11,812
In more than five years, but not more than twenty years	8,751	10,959
In more than twenty years	-	-
	<hr/> 314,849	<hr/> 312,004

The table above excludes future interest payments and future indexation on financial liabilities. Index-linked borrowings of £203,835,000 (2017: £196,594,000) included in the table above are stated at the principal amount indexed by RPI to the balance sheet date. The estimated redemption value of index-linked borrowings at redemption in 2045 is £358,265,000 (2017: £399,467,000) and at redemption in 2051 is £118,379,000 (2017: £139,996,000).

Debtors recoverable in more than one year of £43,547,000 (2017: £43,666,000) principally represent loans receivable from the Company's parent companies of £40,000,000 (2017: £40,000,000) with £15,000,000 (2017: £15,000,000) due to be repaid by 31 March 2020 and £25,000,000 having no fixed repayment date (2017: £25,000,000).

Notes to the Financial Statements

Trade debtors

Provision is made within the trade debtor values detailed below, based on judgement by senior management for amounts considered to be unrecoverable due either to their nature or age. The total amount charged to the profit and loss account in the year to March 2018 in respect of such provisions was £3,205,000 (2017: £3,525,000). Total trade debtors as at 31 March 2018 were £12,554,000 (2017: £16,262,000). The total amount of the provision included in the above, as at 31 March 2018 was £34,123,000 (2017: £33,604,000).

In accordance with the market conditions prescribed by MOSL, the wholesale market operator, we hold collateral where required and in line with market rules from Retailers which purchase water from the Company. This collateral is held in the form of four parent company guarantees; one bank guarantee and six cash collateral balances totalling £104,458 at year end.

The Directors consider that debtors that are neither past due nor impaired are of a high quality and were considered, at the balance sheet date to be fully recoverable at their net book value. The largest balance outstanding from any single customer at 31 March 2018 was £1,774,000 (2017: £147,000), representing 13.8% of the Company total (2017: 0.9%). This increase was expected and the customer is our largest Retailer in the Non-household market; this debt is supported by a parent company guarantee.

An ageing analysis of trade debtors that are invoiced but not impaired is provided below:

Regulated	< 1 year	1 - 2 years	2 - 3 years	3 - 4 years	4 - 5 years	5 years +	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
2018	7,540	2,189	1,441	957	418	347	12,892
2017	9,913	2,355	1,337	642	366	-	14,613

Non-Regulated	<1 month	1-2 months	>2 months	>3 months	Total
	2018	504	379	14	40
2017	474	58	20	60	612

Non-regulated debtors that are considered to be impaired and so netted out of the figure above are to the value of £68,000 (2017: £46,000) and were all more than two months past due. An ageing analysis of appointed debtors that are considered to be impaired is provided below:

Regulated	< 1 year	1 - 2 years	2 - 3 years	3 - 4 years	4 - 5 years	5 years +	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
2018	3,872	3,383	3,384	3,298	3,226	16,892	34,055
2017	3,973	3,566	3,553	3,437	3,352	15,677	33,558

The Directors consider that the carrying value of trade and other debtors including loans receivable, net of provisions, detailed in note 15 approximates to their fair value.

Notes to the Financial Statements

24 Post balance sheet event

On 3 July 2018 the ultimate controlling party of the Company changed to Arjun Infrastructure Partners Limited as described in detail in note 26 below.

25 Related party transactions

Historical agreements were put in place with a holding company in the Group structure to offset the impact on South Staffordshire Water PLC of certain hedging relationships entered into with a third party bank, on both cash flow and the profit and loss account. The balance due from Selena Bidco Limited in respect of these transactions at 31 March 2018 was £3,911,000 (2017: £4,030,000). In accordance with applicable accounting standards, the impact of both arrangements on the profit and loss account has been netted off with no overall impact.

On 1 April 2017, the Company transferred its non-household retail operations and related assets to SSWB Ltd (SSWB), a fellow Group company for £8,400,000, and therefore exited the non-household retail water market. There was no profit or loss on disposal.

On the same day our parent company, South Staffordshire Plc, transferred SSWB to Pennon Water Services Ltd (PWS), in return for a 20% equity share in PWS. South West Water also transferred its non-household retail operations to PWS on the same day, therefore forming a Joint Venture between South Staffordshire Plc and Pennon Group Plc to operate in the non-household retail market.

The £8,400,000 transferred consisted of the following balances:

Fixed Assets	£477,000
Trade Debtors	£3,851,000
Measured Income Accrual	£4,072,000
	<u>£8,400,000</u>

During the year the Company provided Wholesale water services to the retailer PWS and its subsidiary SSWB and turnover of £22,299,000 in relation these transactions was recognised and there was a trade debt outstanding of £1,774,000 at the year end.

Remuneration for key personnel is reported on page 63.

26 Ultimate controlling party

The immediate parent company is South Staffordshire Plc which is registered in England and Wales and is the smallest group preparing consolidated accounts that include South Staffordshire Water PLC. During the year the ultimate parent company in the United Kingdom was Hydrades IV Limited, also registered in England and Wales which was the largest UK group preparing consolidated accounts that include South Staffordshire Water PLC at 31 March 2018. The consolidated accounts for both these companies can be obtained from the Company's registered office, Green Lane, Walsall, West Midlands, WS2 7PD. The ultimate controlling party during the year ended 31 March 2018 was KKR Infrastructure Limited, which during that year controlled and managed, and was the General Partner of the Global Infrastructure Fund of the investment business KKR & Co L.P., which is quoted on the New York Stock Exchange.

Since the end of the year on 3 July 2018 the ultimate controlling party became Arjun Infrastructure Partners Limited a Company registered in England and Wales, which controls and manages and is the General Partner of a UK registered investment entity that acquired a majority equity interest of a holding company of South Staffordshire Water PLC and therefore of the Group, on that date.



South Staffs Water



Annual Performance Report



Introduction

Our Annual Performance Report (APR) is published each year and provides information for the Company's appointed business. It is split into four sections:

1. Regulatory Accounts Primary Statements
2. Price Review and Segmental Reporting
3. Performance Summary
4. Additional Regulatory Information

Our statutory accounts on their own are considered insufficient to assess the performance of a vertically integrated, price-controlled monopoly such as South Staffordshire Water PLC. This is particularly relevant in a water sector with long-life assets and where there is still an absence of competitive markets for different parts of the value chain. These regulatory accounting statements use audited information and comply with Ofwat's published Regulatory Accounting Guidelines (RAGs) that can be found on their website at www.Ofwat.gov.uk

Performance Commitments

At the heart of our performance reporting is a set of five Outcomes and 15 performance commitments that reflect the priorities of customers and benchmarking of water companies in England and Wales carried out in 2014. These outcomes and performance commitments provide broad coverage of our service provision, from water quality and reliability, through to environmental commitments, customer service and customer bills.

The 2014 price review set challenging targets for performance commitments based on industry benchmarking. Tough glide paths were imposed necessitating a review of how the business delivers the core aspects of our service.

We have not reached the challenging targets we set and that our customers expect in some areas this year. As anticipated we have seen improvements in our Service Incentive Mechanism (SIM) score, but not yet reached our upper quartile target although we are getting closer. We have also had a tough year with regards to leakage missing the targets in both of our regions. We have put considerable resource in to addressing leakage and understand the need to reduce leakage and are working to achieve and beat future targets as quickly as possible.

The Company has also published a separate performance report on our website and this can be found at the following link:

<https://www.south-staffs-water.co.uk/publications/annual-reports>

In the summary below and table 3A our performance against our commitments is shown with an in depth review included in our Strategic Report on pages 9 to 16.

Outcome	ODI name	Unit of measurement	Year						Target achieved	Performance against last year
			2015/16	2016/17	2017/18		2018/19	2019/20		
			Actual	Actual	Target	Actual	Target	Target		
1 Excellent water quality	Mean Zone Compliance	%	99.884	99.982	100.00	99.943	100.00	100.00	✘	Declining
	Acceptability of water to customers	Contacts per thousand population	1.96	1.66	1.23	1.42	1.23	1.23	✘	Improving
2 Secure and reliable supplies	Interruptions to supply	Minutes and seconds per property	04:14	05:11	10:00	08:32	10:00	10:00	✓	Declining
	Asset health infrastructure	Category	Stable	Stable	Stable	Stable	Stable	Stable	✓	Stable
	Asset health non-infrastructure	Category	Stable	Stable	Stable	Stable	Stable	Stable	✓	Stable
3 Excellent customer experience	Service Incentive Mechanism	Score	86.3	84.4	90.0	87.0	90.0	90.0	✘	Improving
	Customer satisfaction	%	98	99	98	97	98	98	✘	Declining
	Community engagement	Days	257	222	400	425	400	400	✓	Improving
4 Environment	Leakage South Staffs region	Megalitres per day	69.9	69.9	70.5	72.4	70.5	70.5	✘	Declining
	Leakage Cambridge region	Megalitres per day	13.2	14.3	13.5	14.4	13.5	13.5	✘	Declining
	Water efficiency	Litres per person per day	129.59	129.85	129.52	133.09	128.91	128.31	✘	Declining
	Biodiversity	Hectares of land	76	92	106	119	116	116	✓	Improving
	Carbon emissions	Tonnes of carbon saved	178	285	2428	550	3742	5210	✘	Improving
5 Fair customer bills	Value for money and affordability satisfaction	%	93	91	90	94	90	90	✓	Improving
	Support for customers in debt	Number of customers	19621	23895	24800	29036	27400	30000	✓	Improving

Regulatory Performance Summary

The following summary aims to give a high level view of performance with more detail provided in the following sections:

- Section 1 – Regulatory Accounts Primary Statements
- Section 2 – Price Review and Segmental Reporting
- Section 3 – Performance Summary
- Section 4 – Additional Regulatory Information

Appointed financial performance

- Revenue of £118.9m; operating profit of £19.2m; tax charged in the year of £2.8m
- Dividend paid of £15.4m
 - This can be broken into a one off payment of £8.4m relating to the sale of our retail non-household business, £2.0m in respect of intra-group interest and £5.0m dividend on in year profits (£6.5m for last year)
- Regulatory book net debt of £260.5m which provides a gearing ratio of 71.51% against an RCV of £364.4m
 - The more appropriate measure is Covenant net debt of £240.7m with gearing of 66.1% which is in line with a desire to maintain a gearing ratio of up to 66%
- Across the AMP to date an actual shareholder return of 16.7% has been achieved which is 6.0% higher than the notional return in the Final Determination (FD). A more appropriate calculation using Covenant net debt and interest paid on debt is 12.7%
- Retained value for the AMP to date was an average of 9.0% at 2.3% higher than the notional retained value in the FD
- Return on Regulated Equity for the AMP was an average of 8.01% (7.41% using Covenant net debt) which is higher than that allowed in the FD of 5.98%, with our out performance on ODIs and Retail costs helping to drive this.

Wholesale and Retail performance

- Wholesale operating profit was £16.6m with Retail operating profit of £2.6m
- Wholesale revenue was £4.4m higher than that assumed in the price control
 - Revenue from water customers was £0.2m higher (+0.22%) and will be adjusted through the Wholesale Revenue Forecasting Incentive Mechanism (WRFIM) in wholesale charges for 2019/20
 - Contributions were £4.2m higher and predominantly driven by developer charges reflecting a high number of new property connections and high costs incurred from non-standard brownfield connections
 - The Company has had no net benefit from higher capital contributions which were a result of higher costs; following dialogue with Ofwat these will be addressed as part of the next price review process
- Wholesale Totex in the year was £81.9m and was £4.1m higher than the FD; AMP to date totex at £230.5m is £1.6m lower than allowed in the FD
 - In the year capital expenditure was £5.7m above the FD which reversed the lower spend from the first two years of the AMP; expenditure across the AMP is being managed in line with FD expectations
 - Operating expenditure in the year was £0.8m lower than the FD driven by benefits from laboratory service costs and business rates
- Household retail revenue for the year was £15.2m which was £0.4m below that assumed in the FD
- Retail costs were £11.6m; £2.5m lower than that allowed in the price limit for the year
 - Savings have continued due to efficiencies made in contact centre services and structural changes made in the year

ODI performance

- Our performance in the year saw us incur a net penalty as discussed below. We were disappointed with our leakage performance overall and are working hard to remedy; the impact of the severe March weather was a significant contributory factor. Our SIM score, whilst improving in the year, is still not up with the best which is our desired outcome
- In the year penalties were incurred totalling £0.24m with the impact driven by:
 - £40k from missing MZC as results decline from 99.98 to 99.94 in the year
 - £300k from Acceptability of Water to Customers despite a really strong downward trend in contacts per 1,000 customers from 1.66 to 1.42; the target is also getting tougher
 - £120k from our leakage performance in Cambridge which despite considerable efforts continued at similar levels to last year
 - These were offset by a £212k reward from Interruptions to Supply which whilst not as good as in previous years continues to outperform
- AMP to date our net reward position is £1.1m

Regulatory Accounts Primary Statements

1A – Income statement

For the 12 months ended 31 March 2018

	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
	£m	£m	£m	£m	£m
Revenue	124.082	-	5.188	(5.188)	118.894
Operating costs	(94.962)	(8.001)	(3.128)	(4.872)	(99.834)
Other operating income	1.250	(0.751)	0.343	(1.094)	0.156
Operating profit	30.370	(8.752)	2.402	(11.154)	19.216
Other income	-	8.752	0.424	8.327	8.327
Interest income	2.545	-	0.014	(0.014)	2.531
Interest expense	(14.061)	-	-	-	(14.061)
Other interest expense	(0.181)	-	-	-	(0.181)
Profit before tax and fair value movements	18.673	-	2.841	(2.841)	15.832
Fair value gains/(losses) on financial instruments	-	-	-	-	-
Profit before tax	18.673	-	2.841	(2.841)	15.832
UK Corporation tax	1.254	-	(0.512)	0.512	1.766
Deferred tax	(4.571)	-	-	-	(4.571)
Profit for the year	15.356	-	2.329	(2.329)	13.027
Dividends	(16.740)	-	(1.340)	1.340	(15.400)
Tax analysis					
Current year	3.533	-	0.512	(0.512)	3.021
Adjustments in respect of prior years	(4.787)	-	-	-	(4.787)
UK Corporation tax	(1.254)	-	0.512	(0.512)	(1.766)
Analysis of non-appointed revenue			Non- appointed		
Imported sludge			-		
Tankered waste			-		
Other non-appointed revenue			5.188		
Revenue			5.188		

Differences between statutory and RAG definitions

In the statutory accounts the Company classifies certain income in particular rental income as operating income (£0.8m). RAG definitions state that this should be classified as other income which is below the operating profit line. Profit before tax and fair value movements are unaffected by this reclassification.

In the statutory accounts the amortisation of capital contributions income (£2.4m) and contributions in relation to infrastructure renewal expenditure (£5.6m) are included within operating costs. RAG definitions state that this should be classified as other income which is below the operating profit line. Profit before tax and fair value movements are unaffected by this reclassification.

Regulatory Accounts Primary Statements

Reconciliation of appointed current taxation to standard tax rate

This reconciliation of the appointed current tax charge results from applying the standard tax rate to the profit before tax as shown in table 1A.

	2018 £m	Current Tax £m
PBT		
Appointed	15.832	(1.766)
Non appointed	2.841	0.512
Total	18.673	(1.254)
Appointed Profit on ordinary activities	15.832	
Appointed profit before tax at standard UK corporation tax rate of 19%	3.008	
Expenses not deductible for tax purposes		0.133
Capital allowances less than depreciation		(0.142)
Other timing differences		0.022
Adjustments in respect of prior years		(4.787)
	(4.774)	
Appointed current tax charge	(1.766)	
Appointed total current tax charge allowed in price limits	2.509	
Variance		
Impact of difference between tax rate used in price limits (20%) and actual tax rate (19%)		(0.125)
Differences in profit before tax		(0.319)
Taxable interest income for which no tax allowance given in price limit		0.484
Expenses not deductible for tax purposes for which no tax allowance given in price limit		0.491
Capital allowances in advance of depreciation		(0.083)
Other timing differences		0.064
	0.512	
Current year	3.021	
Adjustments in respect of prior years	(4.787)	
Appointed current tax charge	(1.766)	

The current tax charge in respect of the year at £3.0m was higher than that allowed in price limits by £0.5m and was offset by adjustments from prior years of £4.8m. These arise primarily as a result of the Company revising its estimate of the tax impact of the transition to FRS 102. The change of basis of accounting for certain historical items, on transition, and the related revision to estimates, have given rise to a current tax credit and an equivalent offsetting deferred tax charge during the year.

Regulatory Accounts Primary Statements

1B – Statement of comprehensive income For the 12 months ended 31 March 2018

	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
	£m	£m	£m	£m	£m
Profit for the year	15.356	-	2.329	(2.329)	13.027
Actuarial gains/(losses) on post employment plans	-	-	-	-	-
Other comprehensive income	1.127	-	-	-	1.127
Total Comprehensive income for the year	16.483	-	2.329	(2.329)	14.154

Other comprehensive income relates to the movement in the hedging reserve net of deferred tax.

Regulatory Accounts Primary Statements

1C – Statement of financial position

As at 31 March 2018

	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
	£m	£m	£m	£m	£m
Non-current assets					
Fixed assets	511.021	-	1.410	(1.410)	509.611
Intangible assets	-	-	-	-	-
Investments - loans to group companies	-	40.000	-	40.000	40.000
Investments - other	-	-	-	-	-
Financial instruments	-	-	-	-	-
Retirement benefit assets	-	-	-	-	-
Total non-current assets	511.021	40.000	1.410	38.590	549.611
Current assets					
Inventories	1.714	-	0.046	(0.046)	1.667
Trade & other receivables	73.958	(40.656)	0.108	(40.764)	33.194
Financial instruments	-	-	-	-	-
Cash & cash equivalents	2.192	-	(0.001)	0.001	2.192
Total current assets	77.864	(40.656)	0.154	(40.810)	37.054
Current liabilities					
Trade & other payables	(53.278)	-	7.075	(7.075)	(60.353)
Capex creditor	(4.990)	-	-	-	(4.990)
Borrowings	(2.041)	-	-	-	(2.041)
Financial instruments	-	-	-	-	-
Current tax liabilities	(0.916)	-	(0.512)	0.512	(0.404)
Provisions	-	-	-	-	-
Total current liabilities	(61.225)	-	6.563	(6.563)	(67.788)
Net current assets / (liabilities)	16.639	(40.656)	6.716	(47.372)	(30.734)
Non-Current liabilities					
Trade & other payables	(11.059)	-	(0.379)	0.379	(10.679)
Borrowings	(260.902)	-	-	-	(260.902)
Financial instruments	(1.669)	-	-	-	(1.669)
Retirement benefit obligations	-	-	-	-	-
Provisions	-	-	-	-	-
Deferred income - G&C's	(146.496)	-	(0.008)	0.008	(146.488)
Deferred income - adopted assets	-	-	-	-	-
Preference share capital	-	-	-	-	-
Deferred tax	(39.336)	-	-	-	(39.336)
Total non-current liabilities	(459.462)	-	(0.387)	0.387	(459.075)
Net assets	68.198	(0.656)	7.739	(8.395)	59.803
Equity					
Called up share capital	2.123	-	-	-	2.123
Retained earnings & other reserves	66.075	(0.656)	7.739	(8.395)	57.680
Total Equity	68.198	(0.656)	7.739	(8.395)	59.803

Differences between statutory and RAG definitions

In the statutory accounts a long term group debtor of £40.000m is disclosed within debtors due after more than one year. The RAGs state that this should be classified as an investment.

The difference in the statutory accounts trade and other receivables that impacts retained earnings is based on a difference in the regulatory recognition of income and the statutory policy detailed on page 81.

Regulatory Accounts Primary Statements

1D – Statement of cash flows

For the 12 months ended 31 March 2018

	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
	£m	£m	£m	£m	£m
Statement of cashflows					
Operating profit	30.370	(8.752)	2.402	(11.154)	19.216
Other income	-	8.752	0.424	8.327	8.327
Depreciation	22.660	-	0.166	(0.166)	22.495
Amortisation - G&C's	(2.413)	-	-	-	(2.413)
Changes in working capital	(2.527)	-	(2.773)	2.773	0.246
Pension contributions	-	-	-	-	-
Movement in provisions	-	-	-	-	-
Profit on sale of fixed assets	(0.499)	-	(0.343)	0.343	(0.156)
Cash generated from operations	47.591	-	(0.124)	0.124	47.715
Net interest paid	(6.336)	-	0.014	(0.014)	(6.351)
Tax paid	(1.933)	-	(0.543)	0.543	(1.390)
Net cash generated from operating activities	39.322	-	(0.652)	0.652	39.975
Investing activities					
Capital expenditure	(46.547)	-	(0.065)	0.065	(46.481)
Grants & Contributions	10.047	-	-	-	10.047
Disposal of fixed assets	0.527	-	0.414	(0.414)	0.113
Other	(0.592)	-	-	-	(0.592)
Net cash used in investing activities	(36.565)	-	0.348	(0.348)	(36.913)
Net cash generated before financing activities	2.757	-	(0.304)	0.304	3.061
Cashflows from financing activities					
Equity dividends paid	(16.740)	-	(1.340)	1.340	(15.400)
Net loans received	7.452	-	-	-	7.452
Cash inflow from equity financing	-	-	-	-	-
Net cash generated from financing activities	(9.288)	-	(1.340)	1.340	(7.948)
Increase / (decrease) in net cash	(6.531)	-	(1.644)	1.644	(4.887)

Differences between statutory and RAG definitions

In the statutory accounts we classify certain income in particular rental income as operating income. RAG definitions state that this should be classified as other income which is below the operating profit line.

In the statutory accounts the amortisation of capital contributions income and contributions in relation to infrastructure renewal expenditure is included within operating costs. RAG definition state that this should be classified as other income which is below the operating profit line.

Capital expenditure relates to the cash paid out in the year in relation to fixed asset additions. The difference in that paid for appointed assets of £46.481m and additions in the fixed asset table in 2D of £45.374m is due to an decrease in year of creditors due relating to capital purchases of £1.113m.

Pension contributions (including pension deficit contributions) of £3.133m are included as a cash cost within operating profit.

Regulatory Accounts Primary Statements

1E – Net debt analysis As at 31 March 2018

	Interest rate risk profile			Total £m
	Fixed rate £m	Floating rate £m	Index linked £m	
Borrowings (excluding preference shares)	31.601	7.410	223.723	262.733
Preference share capital				0.000
Total borrowings				262.733
Cash				(2.192)
Short term deposits				0.000
Net Debt				260.541
Gearing				71.51%
Adjusted gearing				66.08%
Full year equivalent nominal interest cost	0.897	0.081	13.294	14.273
Full year equivalent cash interest payment	0.897	0.081	7.285	8.264
Indicative interest rates				
Indicative weighted average nominal interest rate	2.84%	1.10%	6.52%	5.88%
Indicative weighted average cash interest rate	2.84%	1.10%	3.57%	3.40%
Weighted average years to maturity	3.20	3.90	28.33	24.28

Net debt comprises the book value of debt excluding accrued interest defined by the Regulatory Accounting Guidelines. In addition to the coupons payable, interest costs include the impact of hedging.

The adjusted gearing of 66.1% is based on the Company's covenant net debt of £240.7m which differs to the book net debt of £260.8m. Covenant debt is the key metric used by the Board, investors, lenders and rating agencies in assessing gearing.

The difference between covenant and book net debt includes £12.0m which relates to the unamortised premium and costs on issuance of the Company's debt. The remaining £7.8m mainly relates to the difference in the long-term inflation assumption to maturity used for the book value of index-linked debt compared to the lower actual inflation rate used for covenant reporting. A full reconciliation between book net debt and covenant net debt is provided below.

The difference between book net debt in table 1E £260.5m and that stated in the table below at £260.7m is in relation to accrued interest of £0.2m which is not recognised as part of net debt in accordance with Regulatory Accounting Guidelines. The Regulatory Gearing ratio is at 71.51% (71.57% using statutory book debt below).

	31 March 2018	
	£'000	Gearing %
Book net debt	(260.751)	71.57%
Exclude accrued interest	0.209	(0.06%)
Book net debt (as reported above)	(260.542)	71.51%
Exclude book premium on issue of index linked debt	13.768	(3.78%)
Difference between long-term RPI assumption and actual RPI inflation	7.840	(2.15%)
Exclude unamortised issue costs	(1.814)	0.50%
Net debt reported for borrowing covenants	(240.748)	66.08%

Regulatory Accounts Primary Statements

1F – Financial flows

Average for AMP6

			%			£		
	Units	DP	Notional returns and notional regulatory equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity	Notional returns and notional regulatory equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity
Return on regulatory equity	%	2	5.98%	4.70%	5.98%	7.06	5.55	5.55
Actual performance adjustment 2010-2015	%	2	2.38%	1.88%	2.38%	2.82	2.22	2.22
Adjusted return on regulatory equity	%	2	8.35%	6.57%	8.35%	9.88	7.76	7.76
Regulatory equity base	£	0	118	118	93			
Financing								
Gearing	%	2	0.00%	0.72%	0.91%	-	0.84	0.84
Variance in corporation tax	%	2	0.00%	1.55%	1.97%	-	1.82	1.82
Group relief	%	2	0.00%	0.00%	0.00%	-	-	-
Cost of debt	%	2	0.00%	0.40%	0.53%	-	0.48	0.49
Hedging instruments	%	2	0.00%	(0.32%)	(0.41%)	-	(0.38)	(0.38)
Sub total	%	2	8.35%	8.92%	11.35%	9.88	10.53	10.54
Operational Performance								
Totex out / (under) performance	%	2	0.00%	(0.15%)	(0.20%)	-	(0.18)	(0.18)
ODI out / (under) performance	%	2	0.00%	0.31%	0.40%	-	0.37	0.37
Retail out / (under) performance	%	2	0.00%	2.23%	2.84%	-	2.64	2.64
Sub Total	%	2	0.00%	2.39%	3.04%	-	2.82	2.82
Total earnings	%	2	8.35%	11.31%	14.39%	9.88	13.35	13.37
RCV growth	%	2	2.32%	2.32%	2.32%	2.73	2.73	2.15
Total shareholder return	%	2	10.67%	13.62%	16.71%	12.61	16.09	15.52
Net dividend	%	2	4.00%	6.08%	7.73%	4.72	7.18	7.18
Retained value	%	2	6.67%	7.54%	8.97%	7.89	8.91	8.34
Dividends reconciliation								
Gross dividend	%	2	4.00%	7.70%	9.80%	4.72	9.10	9.10
Interest receivable on intercompany loans	%	2	0.00%	1.62%	2.07%	-	1.92	1.92
Net dividend	%	2	4.00%	6.08%	7.73%	4.72	7.18	7.18

Regulatory Accounts Primary Statements

1F – Financial flows

Average for AMP6

Commentary to financial flows

The financial flows table above is based on book debt rather than covenant debt to be consistent with Ofwat guidance and is the average of the three years from 2015/16 to 2017/18.

- Actual shareholder returns of 16.71% is 6.04% above the notional return in the Final Determination and is driven by:
- Returns from higher gearing using book debt of 70.5% compared to the notional gearing of 62.5%, this is 0.91%.
- Higher returns from a lower tax charge of 1.97%. This is predominantly as a result of the Company revising its estimate of the tax impact of the transition to FRS102.
- The change of basis of accounting for certain historical items gave rise to a current tax credit and a deferred tax charge during the year.
- Operational outperformance resulting in a benefit of 3.04% driven by significant cost reductions in the residential retail business compared to that allowed in the Final Determination.

Dividend yield is 3.74% above the Final Determination with 2.69% of this outperformance as a result of the sale of the non-household retail business which generated a dividend of £8.4m. Excluding this one-off dividend results in an outperformance of 1.05%

The remaining 2.30% of outperformance on shareholder returns has been retained within the business.

The table shows an outperformance on the cost of debt of 0.5%. As per Ofwat guidance this is calculated net of interest received on intercompany loans which are not part of net debt. If this is correctly excluded, there is an underperformance on the cost of debt of 1.5%.

Calculating the financial flows using the more appropriate measure for gearing of covenant debt and excluding interest received on intercompany loans that are not part of net debt this gives an actual shareholder return of 12.7% instead of 16.7%, which is 2.0% above the notional return, as set out below.

Shareholder return using Ofwat guidance	16.7%
Impact of using covenant debt rather than book debt	-2.0%
Exclusion of interest received on intercompany loans	-2.0%
Shareholder return using company alternative calculation	12.7%

The dividend yield on this basis is 2.4% higher than the Final Determination, all of which is due to the sale of the non-household retail business.

Accounting Policies

1. Accounting policy for price control segments

The regulatory accounts have been prepared in accordance with RAG 2 (Guideline for the classification of costs across price controls) and follow the Company's accounting separation methodology statement. This statement is available on the Company's website at the link below:

<https://www.south-staffs-water.co.uk/publications/annual-reports>

Data for accounting separation is predominately taken from the Company's financial system, through downloads into spreadsheets. The financial information is captured at a location and activity level. Account codes are used to classify the expenditure to the correct cost lines within the relevant tables in section 2 and section 4 of the APR. Costs and assets are then attributed directly to business units in line with RAGs.

For general and support expenditure, a number of cost drivers have been identified for allocation of costs into the relevant business units. These include headcount, number of vehicles, floor space and asset values.

2. Revenue recognition

In the regulatory accounts, income is based on the value of bills and accrued income for measured customers raised in the year in line with RAGs. This is different to the statutory accounting policy on page 81.

For metered consumption not yet billed, an accrual is estimated. Where a property is unoccupied and fully furnished, charges are still applicable. Charges are also applicable where a property is renovated.

Charges may be waived in special circumstances, for example hospitalisation, probate and incarceration. Where a property is believed to be occupied, but the occupier details are not known, the income is not recognised until the occupant details are obtained. The Company uses Land Registry searches and void inspector visits to ascertain the identity of any occupier.

The Company does not bill unmetered void properties speculatively to 'the occupier'. Properties are visited by void inspectors to confirm that a property is unoccupied. For void metered properties, where consumption has been measured and the identity of the customer is not known following a void inspection, the property will be billed for the full charges in the name of 'the occupier'. Charges raised are realised as revenue in the same way as other metered income.

The first bill for a new connection is based on an actual meter reading. Where a customer has been connected during the year but has not had a meter reading, an estimate of the income is accrued based on the average household consumption.

Charges on income include charging orders and attachment of earnings. Cash received is applied against the outstanding debt with income being recognised from the billing date.

The Company operates an 'income maximisation' project that is used to identify properties not held on the Company's billing system. Any properties billed under this approach are not recognised as turnover until the running costs of the project have been covered.

Income recognised during the year is based on the value of bills raised. For metered consumption not yet billed, an accrual is estimated based on historical average daily consumption for each customer. The measured income accrual at March 2018 was £11.1m compared to £14.2m in the previous year.

The measured income accrual at March 2017 was £14.2m. Following comparison to the income actually billed for these customers in the year, there are no significant differences to report.

Accounting Policies

3. Capitalisation policy

Capital expenditure which results in the acquisition of an asset for continuing use within the business with a view to earning income or making profits from its use, either directly or indirectly.

Operating expenditure is incurred either for the purpose of the day to day running of the business or to maintain the existing capacity of fixed assets.

Costs are allocated between operating and capital expenditure in accordance with the Company's accounting policies and applicable accounting standards. The deminimis level for capitalisation is £1,000 for minor assets and £5,000 for buildings.

4. Bad debt policy

Before passing an account for write-off, all debts will be pursued through every available recovery method and will usually include attempts by the Sheriff Officers or Debt Collection Agencies. Only where it is impossible, impractical or inefficient to collect debt, will a recommendation for a write-off be made.

There will be a variety of circumstances when it will be necessary to write off irrecoverable debts; these can be summarised below:

Absconded

- Where returned mail is received on accounts, no forwarding details are available and a final account is created, and where all recovery options have been exhausted.
- Where a debt has been passed to a "Trace and Collect Agency" and the agency is unable to trace the customer and therefore is unable to collect the debt outstanding.
- Where the total debt is less than £50, it is uneconomic to pass for trace and collection and therefore the debt outstanding is unable to be collected.
- Where a customer has debt greater than 6 years old and no billing activity or correspondence has been received in this period, (statute barred).

Bankruptcy

- A domestic customer where official and final notification has been received from the courts or a check has been made with the online insolvency website service.

Deceased

- Where the balance outstanding is less than £25 the amount is written off immediately.
- Where the balance outstanding is greater than £25, the estate is approached. Where written confirmation has been received in writing that the estate has insufficient funds, the balance is written off.
- In circumstances where a joint tenancy liability exists, the remaining party is pursued for the whole amount of the arrears.
- Where attempts to contact the executors (or next of kin) have failed to produce a response, balances under £100 are written off after a period of 6 months.

Liquidation

- A commercial customer where final notification has been received from an Official Receiver, Insolvency Practitioner or Liquidator that the company has been liquidated.
- Debts where a company has ceased to trade leaving no assets.

Uneconomic to collect

- Final debt over 4 years old will be written off where evidence exists that it has become non-collectable. A minimum of three attempts to contact a customer by telephone and / or letter in the prior 12 months has proved to be ineffective and there has been no payment or contact in the preceding 12 months.
- The debtor's age, health or other social factors make it inappropriate to pursue the debt.
- Sums of less than £25 will be written-off as they are deemed to be uneconomic to collect.

Price Review and Segmental Reporting

2A – Segmental income statement For the 12 months ended 31 March 2018

	Retail		Wholesale			Total
	Household	Non-household	Water Resources	Water Network +	Water Total	
	£m	£m	£m	£m	£m	
Revenue - price control	15,218	-	-	101,874	101,874	117,092
Revenue - non price control	-	-	-	1,802	1,802	1,802
Operating expenditure	(11,583)	-	(6,423)	(59,322)	(65,745)	(77,328)
Depreciation - tangible fixed assets	(1,091)	-	(0,264)	(21,151)	(21,415)	(22,506)
Amortisation - intangible fixed assets	-	-	-	-	-	-
Other operating income	-	-	-	0,156	0,156	0,156
Operating profit before recharges	2,544	-	-	-	16,672	19,216
Recharges in respect of 'principal use' assets						
Recharges from other segments	0,036	-	-	-	-	0,036
Recharges to other segments	-	-	-	(0,036)	(0,036)	(0,036)
Operating profit	2,580	-	-	-	16,637	19,216

Price Review and Segmental Reporting

2B – Totex analysis – Wholesale For the 12 months ended 31 March 2018

	Water Resources	Water Network +	Total
	£m	£m	£m
Operating expenditure			
Power	2.023	10.479	12.502
Income treated as negative expenditure	-	-	-
Abstraction charges/ discharge consents	2.854	0.217	3.071
Bulk supply/ Bulk discharge	0.012	0.025	0.037
Other operating expenditure - renewals expensed in year (Infrastructure)	-	14.571	14.571
Other operating expenditure - renewals expensed in year (Non-Infrastructure)	(0.000)	1.084	1.084
Other operating expenditure - excluding renewals	1.367	26.233	27.600
Local authority and Cumulo rates	0.162	5.307	5.469
Total operating expenditure excluding third party services	6.417	57.916	64.333
Third party services	0.006	1.405	1.411
Total operating expenditure	6.423	59.322	65.745
Capital Expenditure			
Maintaining the long term capability of the assets - infra	-	-	-
Maintaining the long term capability of the assets - non- infra	2.414	16.731	19.145
Other capital expenditure - infra	0.377	10.465	10.842
Other capital expenditure - non-infra	1.044	13.154	14.198
Infrastructure network reinforcement	-	0.970	0.970
Total gross capital expenditure excluding third party services	3.835	41.320	45.155
Third party services	-	-	-
Total gross capital expenditure	3.835	41.320	45.155
Grants and contributions			
Grants and contributions	-	15.629	15.629
Totex	10.258	85.013	95.271
Cash Expenditure			
Pension deficit recovery payments	-	-	-
Other cash items	-	-	-
Total	10.258	85.013	95.271
Totex including cash items	10.258	85.013	95.271

Pension deficit recovery payments of £1.805m are included in the totex lines within operating and capital expenditure.

Third party operating expenditure includes the costs of providing bulk supplies and other rechargeable works.

Price Review and Segmental Reporting

2C – Operating cost analysis – Retail For the 12 months ended 31 March 2018

	Household	Non-household	Total
	£m	£m	£m
Operating expenditure			
Customer services	4.804	-	4.804
Debt management	0.590	-	0.590
Doubtful debts	3.221	-	3.221
Meter reading	0.796	-	0.796
Services to developers	-	-	-
Other operating expenditure	2.171	-	2.171
Total operating expenditure excluding third party services	11.583	-	11.583
Third party services operating expenditure	-	-	-
Total operating expenditure	11.583	-	11.583
Depreciation - tangible fixed assets	1.091	-	1.091
Amortisation - intangible fixed assets	-	-	-
Total operating costs	12.674	-	12.674
Debt written off	0.118	-	0.118

Total retail operating costs (before depreciation charges) of £11.6m were £2.5m lower than that allowed in price limits for the year.

Savings continue to be driven by historic changes in metering operations, the transfer of non-voice back office functions off shore and the merging of the Cambridge customer contact centre operations with those in the South Staffs region.

We have continued to drive further efficiency through changes in retail operational structures and ongoing offshoring and digitalisation projects.

Price Review and Segmental Reporting

2D – Historic costs analysis of fixed assets – Wholesale and Retail For the 12 months ended 31 March 2018

	Wholesale		Retail		Total
	Water Resources	Water Network +	Household	Non-household	
	£m	£m	£m	£m	
Cost					
At 1 April 2017	10.538	853.130	10.329	0.564	874.561
Disposals	-	(1.233)	-	-	(1.233)
Additions	3.835	41.318	0.221	-	45.374
Adjustments	-	(0.014)	0.553	(0.564)	(0.026)
Assets adopted at nil cost	-	-	-	-	-
At 31 March 2018	14.373	893.200	11.103	-	918.676
Depreciation					
At 1 April 2017	(2.554)	(376.742)	(7.410)	(0.422)	(387.128)
Disposals	-	0.571	-	-	0.571
Adjustments	-	-	(0.422)	0.422	-
Charge for the year	(0.264)	(21.151)	(1.091)	-	(22.506)
At 31 March 2018	(2.818)	(397.323)	(8.922)	-	(409.064)
Net book amount at 31 March 2018	11.554	495.877	2.181	-	509.612
Net book amount at 1 April 2017	7.983	476.388	2.919	0.143	487.433
Depreciation charge for year					
Principal services	(0.264)	(21.151)	(1.091)	-	(22.506)
Third party services	-	-	-	-	-
Total	(0.264)	(21.151)	(1.091)	-	(22.506)

Price Review and Segmental Reporting

2E – Analysis of capital contributions and land sales – Wholesale

	Fully recognised in income statement	Capitalised and amortised (in income statement)	Fully netted off capex	Total
	£m	£m	£m	£m
Grants and contributions - water				
Connection charges (s45)	-	3.175	-	3.175
Infrastructure charge receipts (s146)	-	2.454	-	2.454
Requisitioned mains (s43, s55 & s56)	-	0.668	-	0.668
Other contributions (price control)	-	-	-	-
Diversions (s185)	5.582	-	-	5.582
Other contributions (non-price control)	-	3.749	-	3.749
Total	5.582	10.047	-	15.629
Value of adopted assets	-	-	-	-
		Water		
		£m		
Movements in capitalised grants and contributions				
Brought forward	138.863			
Capitalised in year	10.047			
Amortisation (in income statement)	(2.413)			
Carried forward	146.496			
Land sales				
Proceeds from disposals of protected land	-			

Contributions for main diversions are now shown as other income within table 1A with the cost shown in table 2B at the gross position before contributions in line with the Regulatory Accounting Guidelines.

Price Review and Segmental Reporting

2F – Household – Revenues by customer type

	Wholesale charges revenue	Retail revenue	Total revenue	Number of customers	Average household retail revenue per customer
	£m	£m	£m	(000s)	£
Unmeasured water only customer	45.914	8.478	54.392	381	£22.26
Unmeasured wastewater only customer	-	-	-	-	£0.00
Unmeasured water and wastewater customer	-	-	-	-	£0.00
Measured water only customer	32.251	6.740	38.990	290	£23.26
Measured wastewater only customer	-	-	-	-	£0.00
Measured water and wastewater customer	-	-	-	-	£0.00
Total	78.164	15.218	93.382	671	£22.69

Household retail revenues are £0.4m lower than that assumed in the Final Determination. This is due to lower demand from metered customers during the year and fewer meter optants than anticipated in the Final Determination.

Price Review and Segmental Reporting

2G – Non-household water – Revenue by customer type

As at the 1 April 2017 we exited the non-household retail market and in accordance with reporting requirements can confirm that our Wholesale revenue relating to non-household was £23.710m for the year.

Non-household revenue was £0.4m higher than that assumed in the Final Determination, due to higher consumption in the metered customer base.

Price Review and Segmental Reporting

2I – Revenue analysis and Wholesale control reconciliation

	Household	Non-household	Total
	£m	£m	£m
Wholesale charge - water			
Unmeasured	45.914	0.994	46.908
Measured	32.251	22.716	54.966
Third party revenue	-	-	-
Total	78.164	23.710	101.874
Retail revenue			
Unmeasured	8.478	-	8.478
Measured	6.740	-	6.740
Other third party revenue	-	-	-
Retail total	15.218	-	15.218
Third party revenue - non-price control			
Bulk Supplies - water			0.268
Bulk Supplies - wastewater			-
Other third party revenue			0.723
Principal services - non-price control			
Other appointed revenue	-	-	0.811
Total appointed revenue	-	-	118.894

	Water
	£m
Wholesale revenue governed by price control	101.874
Grants & contributions	6.298
Total revenue governed by wholesale price control	108.172
Amount assumed in wholesale determination	103.968
Adjustment for in-period ODI revenue	-
Adjustment for WRFIM	(0.200)
Total assumed revenue	103.768
Difference	4.404

Wholesale revenues were £4.4m higher than that assumed in the wholesale price control. After adjusting for the WRFIM over-recovery from 2015/16 of £0.2m, revenue from water customers was only £0.2m higher (0.22%), with a household wholesale under recovery of £0.4m offset by a non-household over recovery of £0.6m.

Contributions predominantly from developer charges were £4.2m higher reflecting a higher number of new property connections in the year and higher costs incurred by the Company for a significant number of non-standard connections on brownfield sites and infill of smaller developments. The wholesale control assumed that all connections were large housing developments in greenfield sites.

The £0.2m over recovery of wholesale revenue from customers will be adjusted through the Wholesale Revenue Forecasting Incentive Mechanism (WRFIM) when setting wholesale charges for 2019/20.

The Company has had no net benefit from higher capital contributions from developers, which were as a result of higher costs incurred, and following dialogue with Ofwat will be addressed as part of the next Price Review process.

Price Review and Segmental Reporting

2J – Infrastructure network reinforcement costs

	Network reinforcement capex £m
Wholesale water network+ (treated water distribution)	
Distribution and trunk mains	0.690
Pumping and storage facilities	0.280
Other	-
Total	0.970

Performance Summary

3A – Outcome performance table

Performance commitment	Unit	Unit description	Decimal places	2016-17 performance level - actual (for information)	2017-18 performance level - actual	2017-18 CPL met?	2017-18 outperformance payment or underperformance penalty - in-period ODIs (indicator)	2017-18 outperformance payment or underperformance penalty - in-period ODIs (£m, to 4 dp)	2017-18 outperformance payment or underperformance penalty - ODIs payable at the end of AMP6 (indicator)	2017-18 outperformance payment or underperformance penalty - ODIs payable at the end of AMP6 (£m, to 4 dp)	31 March 2020 forecast - total AMP6 outperformance payment or underperformance penalty (indicator)	31 March 2020 forecast - total AMP6 outperformance payment or underperformance penalty (£m, to 4 dp)
								£m		£m		£m
1.1: Mean zonal compliance (MZC, combined company)	%	Mean zonal compliance (%)	3	99.982	99.943	No	-	0.0000	Underperformance penalty	(0.0383)	Underperformance penalty	(0.2003)
1.2: Acceptability of water to customers (combined company)	nr	No. of contacts per 1,000 population	2	1.66	1.42	No	-	0.0000	Underperformance penalty	(0.2957)	Underperformance penalty	(0.4986)
2.1: Interruptions to supply (combined company)	time	Minutes / property / year	1	5.2	8.5	Yes	-	0.0000	Outperformance payment	0.2120	Outperformance payment	3.8360
2.2: Serviceability infrastructure (combined company)	category	Asset health indicator	na	Stable	Stable	Yes	-	0.0000	-	0.0000	-	0.0000
2.3: Serviceability non-infrastructure (combined company)	category	Asset health indicator	na	Stable	Stable	Yes	-	0.0000	-	0.0000	-	0.0000
4.1: Leakage (South Staffordshire operating region)	nr	Megalitres per day (M/d)	1	69.9	72.4	No	-	0.0000	Underperformance penalty deadband	0.0000	-	0.0000
4.2: Leakage (Cambridge operating region)	nr	Megalitres per day (M/d)	1	14.3	14.4	No	-	0.0000	Underperformance penalty	(0.1190)	Underperformance penalty	(0.2166)
4.3: Water efficiency (household per capita consumption (PCC) reported annually, combined company)	nr	Litres per head per day (l/h/d)	2	129.85	133.09	No	-	0.0000	-	0.0000	-	0.0000
4.4: Biodiversity (cumulative total hectares of land under management per year, combined company)	nr	Cumulative total hectares of land	0	92	119	Yes	-	0.0000	-	0.0000	-	0.0000
4.5: Carbon emissions from power consumption (tonnes, combined company)	nr	tCO2e (tonnes CO2e) in real savings	0	285	550	No	-	0.0000	-	0.0000	-	0.0000
5.1: Independent customer surveys of value for money and affordability (combined company)	%	% customers satisfied with vfm & affordability	0	91	94	Yes	-	0.0000	-	0.0000	-	0.0000
5.2: Support for customers in debt (combined company)	nr	No. of customers engaged with on debt	0	23,895	29,036	Yes	-	0.0000	-	0.0000	-	0.0000
3.1: Service incentive mechanism (SIM, combined company)	score	Service incentive mechanism (SIM) score	1	84.4	87.0	No	-	0.0000	-	0.0000	-	0.0000
3.2: Customer satisfaction surveys (combined company)	%	% customer satisfaction	0	99	97	No	-	0.0000	-	0.0000	-	0.0000
3.3: Community engagement (combined company)	nr	No. of employee days per year	0	222	425	Yes	-	0.0000	-	0.0000	-	0.0000

Outcomes, ODIs, performance commitments and financial incentives are discussed in more detail in the section on Performance Commitments starting on page 9 in the Strategic Report.

We have also published a summary version of this APR, intended for customers and non-technical stakeholders, which can be found on our website at the following link:

<https://www.south-staffs-water.co.uk/publications/annual-reports>

The forecast AMP6 reward of £2.9205m is based upon the net rewards and penalties accrued in respect of 2015/16, 2016/17 and 2017/18 added to by a continued reward expectation in interruptions to supply.

Performance Summary

3B – Sub measure performance table

PC / sub-measure	Unit	Decimal places	2016-17 performance level - actual	2017-18 performance level - actual	2017-18 CPL met?
2.2: Serviceability infrastructure (combined company)	category	na	Stable	Stable	Yes
Mains bursts	nr	0	1,013	1,300	Yes
Supply interruptions > 12 hours	nr	0	102	637	No
Properties with persistent low pressure	nr	0	1	1	No
Discolouration contacts per 1,000 customers	nr	2	0.84	0.70	Yes
TIM index non-compliance	score	2	0.00	0.13	No
2.3: Serviceability non-infrastructure (combined company)	category	na	Stable	Stable	Yes
WTW coliform non-compliance	%	2	0.00	0.05	No
Service reservoir coliform non-compliance	%	2	0.00	0.00	Yes
WTW turbidity non-compliance	nr	0	0	0	Yes
DWI enforcement actions	nr	0	0	0	Yes
Unplanned maintenance work orders	nr	0	3,058	2,662	Yes

Our assessment of stable serviceability for both infrastructure and non-infrastructure has followed the detailed methodology we set out in our publication 'Asset Health ODI Methodology November 2015' located on our website here:

<https://www.south-staffs-water.co.uk/about-us/our-strategies-and-plans/our-assurance-framework>

Our calculation, and our resultant categorisation, has been externally assured by our external technical auditor Jacobs.

For infrastructure, our headline indicator is bursts and our performance has been better than the reference level of performance for the past three years although we did experience an increased number of bursts due to the 'Beast from the East' in March 2018. We have also seen an increase in the number of properties exposed to a supply interruption of greater than 12 hours due to a number of unplanned events. This indicator is therefore above the reference level of performance for 2017/18 but not sufficient in its own right to trigger a worsened serviceability rating overall when calculated as per our methodology. The remaining three indicators of properties with persistent low pressure, discolouration contacts per 1,000 customers and TIM index non-compliance, are all relatively stable over time.

For non-infrastructure, we have experienced a small number of coliform failures at water treatment works which is slightly above the reference level of performance but well within the control limit. We had zero failures at reservoirs, zero turbidity failures and no enforcement actions for microbiological parameters. Our final indicator, unplanned maintenance, is within the reference level of performance.

Performance Summary

3C – AIM table

For the 12 months ended 31 March 2018

Abstraction site	Decimal places	2017-18 AIM performance [MI]	2017-18 normalised AIM performance [nr]	Cumulative AIM performance 2016-17 onwards [MI]	Cumulative normalised AIM performance 2016-17 onwards [nr]	Contextual information relating to AIM performance
RIVEY B	1	(47.6)	(0.8)	(57.4)	(1.0)	-
LINTON	1	5.6	0.1	(14.4)	(0.5)	-
HAGLEY	1	-	-	-	-	-

The Abstraction Incentive Mechanism (AIM) was introduced from April 2016 and encourages water companies to reduce the environmental impact of abstracting water at environmentally sensitive sites during certain periods of low surface water flows.

We have three sites under AIM and during the year one site, Linton, slightly exceeded the baseline for the periods when flows are below the relevant threshold, however as a cumulative position all sites are below the required baselines. Hagley has not been in use during the year and therefore had no performance against the baseline to record.

Performance Summary

3D – SIM table

For the 12 months ended 31 March 2018

	Units	Decimal places	Score
Qualitative performance			
1st survey score	nr	2	4.47
2nd survey score	nr	2	4.37
3rd survey score	nr	2	4.44
4th survey score	nr	2	4.46
<hr/>			
Qualitative SIM score (out of 75)	nr	2	64.50
Quantitative performance			
Total contact score	nr	2	49.33
Quantitative SIM score (out of 25)	nr	2	22.53
SIM score			
Total annual SIM score (out of 100)	nr	2	87.03

The Service Incentive Mechanism (SIM) measures the levels of service that customers experience, by measuring performance across a number of contact channels, including telephone and written contacts, and also through a quarterly customer survey. SIM performance is financially incentivised, however the level of financial incentive each company receives is determined relative to other water companies at the next price review in 2019.

Additional Regulatory Information

4A – Non financial information

	Unmeasured	Measured
Retail household		
Number of void households	15.371	6.337
Per capita consumption (excluding supply pipe leakage) l/h/d	137.79	126.33
	Water	
Volume (Ml/d)		
Bulk supply export	32.160	
Bulk supply import	0.150	
Distribution input	385.050	

Additional Regulatory Information

4B – Wholesale totex analysis

	Current year	Cumulative 2015-20
	£m	£m
Actual totex		
Actual totex	95.271	261.051
Items excluded from the menu		
Third party costs	1.411	4.732
Pension deficit recovery payments	1.805	4.977
Other 'Rule book' adjustments	0.000	0.000
Total items excluded from the menu	3.216	9.709
Transition expenditure		
Transition expenditure	0.000	0.000
Adjusted Actual totex		
Adjusted Actual totex	92.055	251.342
Adjusted Actual totex base year prices	81.931	230.529
Allowed totex		
Allowed totex based on final menu choice – base year prices	77.804	232.098

The Company's totex of £81.9m (2012/13 prices) was £4.1m (5.3%) higher than allowed in price limits for 2017-18.

Actual wholesale operating costs per the regulatory accounts in 2017/18 are £1.9m lower than the fast money from the Final Determination (FD). IRE (which is included in both operating expenditure in the regulatory accounts and fast money in the FD) was £1.1m lower than the FD in 2017/18 following a decision to move some expenditure from infrastructure renewals to capital expenditure over the AMP period while maintaining the total level of expenditure across these two areas. As a result, wholesale capital expenditure was £5.7m above the FD reversing the underspend in prior periods of the AMP, with the cumulative overspend to be managed to a flat position in line with the Final Determination by the end of the AMP. The remaining £0.8m underspend in operating costs was as a result of cost efficiencies being achieved in our laboratory contract and cumulo rates charges.

The cumulative position for the three years to 2017/18 shows totex of £1.6m (0.7%) below the FD with operating costs being £11.4m lower than the FD.

Ofwat adjusted the Pay As You Go (PAYG) rate in our FD to smooth bills in the period to 2020. The impact was to have an FD PAYG rate of 73.9% in 2015/16 compared to the average in the FD of 68.2%, which was in line with the expected allocation between capital and operating expenditure. This smoothing accelerated £4.6m of fast money into the FD for 2015/16 year from slow money and adjusted subsequent years as an offset. The cumulative position for the three years to 2017/18 is an acceleration of £4.4m. IRE was £8.1m lower than the FD, offset by an overspend on capital expenditure of £9.8m. The remaining £1.1m overspend in operating costs was predominantly related to the ongoing upward pressure on power costs driven by higher pass through charge rates which have continued albeit offset in this year by the laboratory and cumulo rates benefits discussed above.

Overall for the 3 years, ignoring the PAYG adjustment outlined above, there was an overspend of £1.7m of capital investment and infrastructure renewals expenditure which is expected to reverse in future years and there was a £1.1m overspend on operating costs.

Additional Regulatory Information

4C – Forecast impact of performance on RCV

	£m
Cumulative totex over/underspend so far in the price control period	(1.817)
Customer share of cumulative totex over/underspend	(1.323)
RCV element of customer share of cumulative totex over/underspend	(0.674)
Adjustment for ODI rewards or penalties	0.000
RCV determined at FD at 31 March	364.351
Projected 'shadow' RCV	363.677

The cumulative totex underspend is as per that set out in table 4B uplifted to March 2018 prices.

The customer share of cumulative totex underspend and RCV have been calculated in the with the PR14 reconciliation rulebook calculations.

Additional Regulatory Information

4D – Wholesale totex analysis – Water

	Water Resources			Water Network +			Total
	Abstraction licences	Raw water abstraction	Raw water transport	Raw water storage	Water treatment	Treated water distribution	
	£m	£m	£m	£m	£m	£m	
Operating expenditure							
Power	-	2,023	0,985	-	0,842	8,653	12,502
Income treated as negative expenditure	-	-	-	-	-	-	-
Abstraction charges/ discharge consents	2,854	-	-	-	0,217	-	3,071
Bulk supply/ Bulk discharge	-	0,012	-	-	0,025	-	0,037
Other operating expenditure - renewals expensed in year (Infrastructure)	-	-	-	-	-	14,571	14,571
Other operating expenditure - renewals expensed in year (Non-Infrastructure)	-	(0,000)	-	-	(0,000)	1,085	1,084
Other operating expenditure - excluding renewals	-	1,367	0,288	0,012	4,798	21,135	27,600
Local authority and Cumulo rates	-	0,162	0,183	-	0,396	4,727	5,469
Total operating expenditure excluding third party services	2,854	3,564	1,456	0,012	6,277	50,170	64,333
Third party services	-	0,006	0,002	-	0,545	0,859	1,411
Total operating expenditure	2,854	3,569	1,458	0,012	6,822	51,029	65,745
Capital Expenditure							
Maintaining the long term capability of the assets - infra	-	-	-	-	-	-	-
Maintaining the long term capability of the assets - non-infra	-	2,414	-	-	3,300	13,431	19,144
Other capital expenditure - infra	-	0,377	-	-	-	10,465	10,842
Other capital expenditure - non-infra	-	1,044	-	-	9,156	3,998	14,198
Infrastructure network reinforcement	-	-	-	-	-	0,970	0,970
Total gross capital expenditure excluding third party services	-	3,835	-	-	12,456	28,864	45,155
Third party services	-	-	-	-	-	-	-
Total gross capital expenditure	-	3,835	-	-	12,456	28,864	45,155
Grants and contributions							
Grants and contributions	-	-	-	-	3,570	12,059	15,629
Totex	2,854	7,404	1,458	0,012	15,708	67,834	95,271
Cash Expenditure							
Pension deficit recovery payments	-	-	-	-	-	-	-
Other cash items	-	-	-	-	-	-	-
Totex including cash items	2,854	7,404	1,458	0,012	15,708	67,834	95,271
Unit cost information (operating expenditure)							
Licenced volume available (MI)	229,409,800						
Volume abstracted (MI)		158,350,525					
Volume transported (MI)			22,586,413				
Average volume stored (MI)				2,837,387			
Distribution input volume (MI)					140,543,250		
Distribution input volume (MI)						140,543,250	
Unit cost (£/MI)	12.439	22.541	64.568	4.312	48.540	363.084	
Population (000s)	1,669,329	1,669,329	1,669,329	1,669,329	1,669,329	1,669,329	
Unit cost (£/pop)	1.709	2.138	0.874	0.007	4.087	30.569	

Additional Regulatory Information

4F – Operating cost analysis – Household Retail

	Household unmeasured	Household measured	Total
	£m	£m	£m
Operating expenditure			
Customer services	2.327	2.477	4.804
Debt management	0.408	0.182	0.590
Doubtful debts	2.428	0.793	3.221
Meter reading	-	0.796	0.796
Other operating expenditure	1.197	0.974	2.171
Total operating expenditure excluding third party services	6.361	5.222	11.583
Third party services operating expenditure	-	-	-
Total operating expenditure	6.361	5.222	11.583
Depreciation - tangible fixed assets (on assets existing at 31 March 2015)	0.413	0.313	0.726
Depreciation - tangible fixed assets (on assets acquired since 1 April 2015)	0.207	0.158	0.365
Amortisation - intangible fixed assets (on assets existing at 31 March 2015)	-	-	-
Amortisation - intangible fixed assets (on assets acquired since 1 April 2015)	-	-	-
Total operating costs	6.981	5.693	12.674
Capital expenditure	0.126	0.095	0.221
Demand-side efficiency and customer-side leaks analysis - Household			
Demand-side water efficiency - gross expenditure			0.022
Demand-side water efficiency - expenditure funded by wholesale			0.021
Demand-side water efficiency - net retail expenditure			0.001
Customer-side leak repairs - gross expenditure			0.627
Customer-side leak repairs - expenditure funded by wholesale			0.627

Additional Regulatory Information

4G – Wholesale current financial performance

	£m
Revenue	103.676
Operating expenditure	(65.745)
Capital maintenance charges	(23.527)
Other operating income	0.156
<hr/>	
Current cost operating profit	14.561
Other income	8.327
Interest income	2.531
Interest expense	(14.061)
Other interest expense	(0.181)
<hr/>	
Current cost profit before tax and fair value movements	11.177
Fair value gains/(losses) on financial instruments	-
<hr/>	
Current cost profit before tax	11.177
<hr/>	

Additional Regulatory Information

4H – Financial metrics

	Units	Metric Using Covenant Net Debt	Metric Using Book Net Debt
Financial indicators			
Net debt	£m	240.748	260.541
Regulated equity	£m	123.582	103.809
Regulated gearing	%	66.08%	71.51%
Post tax return on regulated equity	%	14.00%	16.89%
RORE (return on regulated equity)	%	7.41%	8.01%
Dividend yield	%	10.79%	12.85%
Retail profit margin - Household	%		2.72%
Retail profit margin - Non household	%		0.00%
Credit rating	Text		Baa2
Return on RCV	%		8.20%
Dividend cover	dec		0.977
Funds from operations (FFO)	£m		39.729
Interest cover (cash)	dec		5.4661
Adjusted interest cover (cash)	dec		2.7746
FFO/Debt	dec		0.152
Effective tax rate	%		19.08%
RCF	£m		24.329
RCF/capex	dec		0.523
Revenue and earnings			
Revenue (actual)	£m		117.092
EBITDA (actual)	£m		39.764
Borrowings			
Proportion of borrowings which are fixed rate	%	13.01%	12.03%
Proportion of borrowings which are floating rate	%	3.05%	2.82%
Proportion of borrowings which are index linked	%	83.94%	85.15%
Proportion of borrowings due within 1 year or less	%	0.84%	0.78%
Proportion of borrowings due in more than 1 year but no more than 2 years	%	0.00%	0.00%
Proportion of borrowings due in more than 2 years but but no more than 5 years	%	14.57%	13.47%
Proportion of borrowings due in more than 5 years but no more than 20 years	%	0.00%	0.00%
Proportion of borrowings due in more than 20 years	%	84.58%	85.75%

Additional Regulatory Information

4H – Financial metrics

Ofwat reporting requires the dividend yield and dividend cover metrics to be calculated after deducting £2.0m (net of tax) of dividends paid to the Company's holding company to enable payment of intra group loan interest to the Company.

The table also shows the following metrics calculated using our covenant debt which is the key metric for the Company's borrowing; regulated gearing; post tax return on regulated equity; RORE and dividend yield.

Calculating RORE using the more appropriate measure for gearing of covenant debt and excluding interest received on intercompany loans that are not part of net debt this gives a return of 5.87% instead of 8.01%, which is 0.1% below the notional return.

The effective tax rate of 19.08% is before prior year adjustments of £4.787m.

Calculation of the Return on Regulated Equity (RORE) on book debt

The calculation of RORE follows the guidance issued by Ofwat in its letter of the 12 April 2017 and subsequent clarifications. We have engaged Jacobs UK Limited to review and audit our RORE calculation methodology; conclusion is that our approach is consistent with Ofwat's guidance.

The reported figure of 8.01% is the simple arithmetic mean of RORE figures in 2015/16 (5.76%), 2016/17 (7.97%) and 2017/18 (10.30%). This is higher than that allowed in the FD of 5.98%. The main driver for this is outperformance on retail costs and ODIs offset by the difference between the interest rate assumed by Ofwat and the actual higher interest rate on the Company's borrowings (which is predominantly made up of long term RPI index-linked debt).

	12-13 prices						Actual
	15-16 Final Determination	Totex (Note 1)	Retail (Note 2)	RCV run off (Note 3)	ODI (Note 4)	Interest (Note 5)	
	£m	£m	£m	£m	£m	£m	£m
Out / (under) performance		(0.825)	2.450	0.026	0.541	(2.508)	
Less tax (20%)		0.165	(0.490)	(0.005)	(0.108)	0.502	
Appointed business: profit	6.923	(0.660)	1.960	0.021	0.433	(2.007)	6.671
Appointed business: regulated equity	115.775						115.775
Appointed business: RORE (actual)	5.98%						5.76%

	12-13 prices						Actual
	16-17 Final Determination	Totex (Note 1)	Retail (Note 2)	RCV run off (Note 3)	ODI (Note 4)	Interest (Note 5)	
	£m	£m	£m	£m	£m	£m	£m
Out / (under) performance		(0.141)	2.767	0.006	0.808	(0.491)	
Less tax (20%)		0.028	(0.553)	(0.001)	(0.162)	0.098	
Appointed business: profit	7.065	(0.113)	2.214	0.004	0.647	(0.393)	9.423
Appointed business: regulated equity	118.205						118.205
Appointed business: RORE (actual)	5.98%						7.97%

	12-13 prices						Actual
	17-18 Final Determination	Totex (Note 1)	Retail (Note 2)	RCV run off (Note 3)	ODI (Note 4)	Interest (Note 5)	
	£m	£m	£m	£m	£m	£m	£m
Out / (under) performance		0.419	2.688	(0.016)	(0.241)	3.574	
Less tax (19%)		(0.080)	(0.511)	0.003	0.046	(0.679)	
Appointed business: profit	7.183	0.339	2.177	(0.013)	(0.195)	2.895	12.387
Appointed business: regulated equity	120.316						120.316
Appointed business: RORE (actual)	5.97%						10.30%

Additional Regulatory Information

4H – Financial metrics

Notes to the book debt RORE calculation

	2015-16	2016-17	2017-18
	£m	£m	£m
1. Totex out performance			
Totex out / (under) performance (12/13 price)	(1.671)	(0.287)	0.848
Cost sharing rate	49.35%	49.35%	49.35%
Out / (under) performance	(0.825)	(0.141)	0.419
Totex underperformance relates to operating costs excluding IRE as outlined in Table 4B			
2. Retail outperformance			
Per FD (allowed retail service expenditure including depreciation on assets post April 2015)	15.894	16.123	14.681
Actual retail costs (including depreciation on assets post April 2015)	13.443	13.356	11.993
Out / (under) performance	2.450	2.767	2.688
Retail out performance is outlined in table 2C			
3. Impact on RCV run off of totex out performance			
Totex out / (under) performance (12/13 price)	(1.671)	(0.287)	0.848
PAYG rate per FD	73.94%	68.33%	67.80%
RCV out / (under) performance	(0.436)	(0.091)	0.273
Run off rate (per FD)	6.00%	6.10%	6.00%
Impact on RCV run off	0.026	0.006	(0.016)
4. ODI reward			
Reward as set out in Table 3A	0.541	0.808	(0.241)
5. Interest (calculation as set out in Ofwat RD letter 12 April 2017)			
Net nominal interest paid	11.695	12.019	11.531
March opening net debt (book value)	233.179	233.708	242.976
March closing net debt (book value)	233.708	242.976	260.541
Average net debt (book value)	233.444	238.342	251.759
Nominal interest rate paid	5.01%	5.04%	4.58%
Year average RPI	1.08%	2.14%	3.74%
Deflate to real interest rate	3.89%	2.84%	0.81%
Cost of debt at PR14	2.59%	2.59%	2.59%
Difference	(1.30%)	(0.25%)	1.78%
Notional level of debt	192.959	197.008	200.527
Financial out / (under) performance	(2.508)	(0.491)	3.574

Additional Regulatory Information

4H – Financial metrics

Notes to the book debt RORE calculation

The performance on interest is as a result of a single industry cost of debt at PR14 of 2.60% compared to the average real interest rate on the Company's borrowings of 3.89% (2015-16), 2.84% (2016-17) and 0.81% (2017-18).

Most of the Company's debt is long-term RPI index-linked debt, the majority of which was issued in 2005. Since then, interest rates have fallen significantly. Therefore, the Company has not been able to benefit from these lower interest rates in comparison to larger water companies in the industry which, due to their size, issue new debt on a more regular basis.

Additional Regulatory Information

4I – Financial derivatives

Derivative type	Nominal value by maturity (net)			Total value			Interest rate (weighted average)			
	1 to 2 years	2 to 5 years	Over 5 years	Nominal value (net)	Mark to Market	Total accretion at 31 March 2018	Units	DPs	Payable	Receivable
	£m	£m	£m	£m	£m	£m				
Interest rate swap (sterling)										
Floating to fixed rate	-	-	30.000	30.000	(1.669)	(1.669)	%	2	2.14%	0.41%
Floating from fixed rate	-	-	-	-	-	-	%	2	0.00%	0.00%
Floating to index linked	-	-	-	-	-	-	%	2	0.00%	0.00%
Floating from index linked	-	-	-	-	-	-	%	2	0.00%	0.00%
Fixed to index-linked	-	-	-	-	-	-	%	2	0.00%	0.00%
Fixed from index-linked	-	-	-	-	-	-	%	2	0.00%	0.00%
Total	-	-	30.000	30.000	(1.669)	(1.669)	0	0		
Foreign Exchange										
Cross currency swap USD	-	-	-	-	-	-	%	2	0.00%	0.00%
Cross currency swap EUR	-	-	-	-	-	-	%	2	0.00%	0.00%
Cross currency swap YEN	-	-	-	-	-	-	%	2	0.00%	0.00%
Cross currency swap Other	-	-	-	-	-	-	%	2	0.00%	0.00%
Total	-	-	-	-	-	-	0	0		
Currency interest rate										
Currency interest rate swaps USD	-	-	-	-	-	-	%	2	0.00%	0.00%
Currency interest rate swaps EUR	-	-	-	-	-	-	%	2	0.00%	0.00%
Currency interest rate swaps YEN	-	-	-	-	-	-	%	2	0.00%	0.00%
Currency interest rate swaps Other	-	-	-	-	-	-	%	2	0.00%	0.00%
Total	-	-	-	-	-	-	0	0		
Forward currency contracts										
Forward currency contracts USD	-	-	-	-	-	-	%	2	0.00%	0.00%
Forward currency contracts EUR	-	-	-	-	-	-	%	2	0.00%	0.00%
Forward currency contracts YEN	-	-	-	-	-	-	%	2	0.00%	0.00%
Forward currency contracts Other	-	-	-	-	-	-	%	2	0.00%	0.00%
Total	-	-	-	-	-	-	0	0		
Other financial derivatives										
Other financial derivatives	-	-	-	-	-	-	%	2	0.00%	0.00%
Total	-	-	30.000	30.000	(1.669)	(1.669)				

Nominal values (net) above represent the nominal value of the interest rate swap of £30.0m which hedges the interest rate payments on £30.0m of bank loans. This does not equal the value reflected in total financial instruments in table 1C of £1.669m as the balance sheet value of the swap is recorded at mark to market value as described above.

The fixed payable element of the interest rate swap is 2.135% and the receivable floating rate element is 3-month LIBOR, shown above as the average for the 12 months to 31 March 2018 of 0.410%.

The receivable floating rate element of the swap exactly offsets the payable floating rate element (3-month LIBOR interest payment) of the related £30.000m bank loan. The effect of this is that the interest payable on the loan, when combined with the cash flows on the swap, is fixed to 2.135% per annum plus the agreed fixed bank margin percentage per annum.

Accounting Disclosures

Board agenda for the year

During the year the Board met nine times, the key areas discussed were:

- The Business Plan for 2020 to 2025 focusing on
 - Customer engagement and views
 - Setting ODIs and performance commitments
 - Long term planning and resilience
 - Balance between stretch and deliverability
 - Approach and assurance
- Leakage and water resource management
- Operational performance and issues
- Customer issues including vulnerability/affordability and tariff setting
- Financial performance, financeability, risk and cash management
- The views of key stakeholders and regulators, including visits from Ofwat, DWI, CC Water and the Customer Panel
- Approvals of capital activities, budgets, proposals and reports
- Assurance levels required and delivered
- Health and safety
- Legitimacy and other challenges facing the industry

Relationship between Director's remuneration and standards of performance

A detailed remuneration report covering the Board of Directors and the Executive Team can be found on pages 61 to 64.

The remuneration policy of the Company continues to provide remuneration packages designed to attract, retain and motivate good quality senior executives. Remuneration comprises salary, benefits and performance related bonus. Each Director receives a base salary which does not vary in relation to business or individual performance.

During the year ended 31 March 2018, Executive Directors had bonus arrangements in place which are payable upon achievement of certain performance objectives, with the intention of rewarding excellent performance. As part of the Company's policy on Corporate Governance, Independent Non-Executive Directors do not have bonus arrangements in place.

The annual bonuses awarded to Executive Directors are linked to the following standards of performance of the Company:

- Customer Service (based upon the SIM Performance, and complaints performance as reported to Ofwat)
- Achievement of ODI performance targets (as reported in Table 3A of the APR)
- Financial performance based upon profitability, operating costs and cash generation

The standards of performance to which bonuses are linked are reviewed annually by the Remuneration Committee to ensure consistency is maintained.

Bonus awards are linked to the above standards of performance as the Remuneration Committee considers such arrangements will maintain consistency between the objectives of the Directors and principal stakeholders including customers and shareholders. The standards of performance to which bonuses are linked are reviewed annually by the Remuneration Committee to ensure this consistency continues to be maintained.

Phil Newland, as an Executive Director of the Company is due a bonus in respect of the above performance and individual targets in respect of the year ended 31 March 2018 approved at £61,700 reflecting the performance of the business in the year. This bonus is payable following the year end. This bonus is less than that paid in respect of the previous year reflecting that operational performance in a number of areas was less than expected.

The bonus awarded to Phil as an Executive Director is based on a "sliding scale" with the bonus award in each category increasing with performance up to a specified maximum award for excellent performance. In addition, Phil has a number of personal targets to achieve for the year, primarily focused on the development of a high quality Business Plan for PR19 and the required customer engagement. Progress has largely been as expected and a bonus of 10% has been proposed to be paid.

Accounting Disclosures

The following performance against target was achieved during the year:

Standard of Performance	Target	Actual	Average % of Salary Awarded
Customer Service	Improve SIM and reduce customer complaints	Target partially achieved	10%
Outcome Delivery Incentives	Achieve Target for key operational performance	Target partially achieved	10%
Financial Performance	Achieve profitability, cost and cash generation	Target not fully achieved	6%

As discussed earlier in this report an element of the bonus in the year for Adrian Page of £35,000 is specifically linked to the performance of the Company including delivery of ODI targets, and the development of a high quality Business Plan for PR19, of which only half is proposed to be paid reflecting operational performance in the year.

Disclosure of information to auditors

The Directors confirm that as far as they are aware, there is no relevant audit information of which the Company's auditor is unaware and that the Board has taken all reasonable steps to make itself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Approach to taxation

South Staffs Water takes the legal and social responsibilities for meeting its tax obligations seriously. We have no operations outside the United Kingdom, and therefore the following has specific reference to UK taxation only.

We are committed to complying with tax laws in a responsible manner, balancing obligations to the Government and the public with our duty to manage our affairs efficiently in order to deliver cost-effective services to customers while generating an economic return to investors. We make timely and accurate tax returns that reflect our fiscal obligations to the Government.

In particular we:

- Will not engage in aggressive tax planning and is not linked with commercial and economic activity
- Will not engage in artificial tax arrangements
- Will seek to maintain a transparent and collaborative relationship with HM Revenue & Customs, principally through our Customer Compliance Manager
- Will seek independent professional tax advice on material matters where the application of tax law is complex or uncertain

We will make use of applicable tax incentives provided by the Government within the terms outlined above. These may include, for example, preferential rates of capital allowances or enhanced tax relief for research and development costs and certain designated capital assets that add efficiency to our operations. Such incentives have been put in place to encourage appropriate business investment.

For our regulated water supply business, such incentives will generally have the effect of reducing customers' water bills under the funding model adopted by Ofwat, our economic regulator.

In addition to corporation tax, we contribute to the UK Exchequer by means of a number of other taxes and levies, including but not limited to:

Accounting Disclosures

- Employment taxes, National Insurance and the Apprenticeship Levy
- Carbon taxes and other energy-related taxes and levies
- Fuel duty and other vehicle-related taxes
- Business rates
- Regulatory charges and licences such as water abstraction charges

Our approach to risk management applies to tax as it does to other business areas, with escalation of key issues to the Board. Taxation compliance and advisory services are provided by our parent company, South Staffordshire Plc, which is responsible for identifying, assessing and managing tax risk across the entire Group. All material tax matters are discussed with our finance team and significant issues are escalated to the Board for consideration. The Group Internal Audit function will also review significant risk areas where considered appropriate.

We have identified economic uncertainty as a risk area. This includes risk in relation to the possibility of unexpected tax law and policy changes by the Government. South Staffordshire Plc carefully monitors published tax legislation, guidance and policy documents to ensure we can assess the compliance requirements and the economic implications for us. They also engage with HM Revenue & Customs on our behalf where our tax position is likely to be materially affected by policy changes.

Dividend policy

Dividends of £15.4m were paid during the year for the appointed business (2016/17: £8.5m). This included £2.0m (net of tax) (2016/17: £2.0m) paid to the Company's holding company to enable it to pay intra group loan interest to the Company and a one off element £8.4m paid in relation to the proceeds from the sale of our non-household retail business.

Adjusting for the one off payment and intra company interest the appointed dividend was £5.0m (2016/17: £6.5m).

The 2017/18 dividend is less than allowed in the Final Determination and represents 4% of regulated equity. Moving forward the Directors will continue to take a responsible approach in determining the levels of dividends to be paid

At 31 March 2018 the Company's ratio of net debt/RCV was 66.1% (2016/17: 63.2%) of its Regulated Capital Value (RCV) of £364.3m (2016/17: £347.6.0m) being the PR14 FD RCV uplifted for inflation.

The (RPI) at March 2017 of 3.3% (March 2017: 3.1%), which is used to inflate RCV, whereas the majority of index-linked debt was inflated using RPI at July 2016 which was lower at 3.6% (July 2015: 1.0%), this would have had an adverse impact on the gearing ratio as index linked debt was uplifted by a higher RPI value. Going forward the Directors target a net debt / RCV rate of up to 66%.

Condition K

In the opinion of the Directors, the Company was in compliance with paragraph 3.1 of its Instrument of Appointment as at 31 March 2018.

Accounting Disclosures

Long term viability statement

The Board of South Staffordshire Water PLC (the Company) is responsible for the efficient running of the Company and for ensuring that it is resilient. In making the declarations below the Board has been guided by the Ofwat Information Notice IN 18/04.

The Directors declare that, in their opinion, the Company is financially viable for at least the next seven years, and that there is no reason to believe that this situation will change beyond that period. The seven year period has been selected because:

- The next two years financial plans are relatively certain due to the determination at PR14 and have been stress tested
- The five years from April 2020 are covered by the PR19 process; the Company will submit a financeable plan which has been stress tested
- We also have confidence that the regulatory system under which South Staffs Water is licensed will ensure that the Company will remain financeable in future periods provided the business operates efficiently and Ofwat continues to make proportionate decisions regarding WACC and other key factors; specific stress testing has been performed until March 2030 however this does rely on some very broad assumptions

The Directors also declare that the Company has carried out appropriate stress testing of its proposed performance over the next seven years, and that the results of these tests show the business to be financially resilient.

- Details of the tests carried out are described and shown in the Strategic Report on pages 39 to 40 of this document
- These tests are considered to cover, severe, plausible and reasonable scenarios for key variables
- The tests are based on, but not limited to, scenarios detailed by Ofwat in its “Putting the sector back in balance” consultation
- Where appropriate multiple scenarios have been considered
- The stress testing considers the impact on the South Staffordshire Group of which the Company is a part
- The stress testing considers the need for and availability of new funding
- The stress testing considers the implications on key metrics utilised by ratings agencies

The Directors also declare that they have received appropriate assurance that the testing carried out is both appropriate and accurately performed:

- Testing has been performed internally by expert staff within the Company
- The calculations used in this testing have been externally verified by Jacobs
- The basis and logic for the scenarios tested has also been verified by Jacobs
- A summary report by Jacobs is included in this report at pages 161 to 162 with a link to their detailed findings which are published on the Company websites
- This assurance is in line with the South Staffs Water Assurance Framework



Phil Newland
13 July 2018

Statement of Directors' Responsibilities for Regulatory Information

Further to the requirements of company law, the Directors are required to prepare accounting statements which comply with the requirements of Condition F of the Instrument of Appointment of the Company as a water and sewerage undertaker under the Water Industry Act 1991 and Regulatory Accounting Guidelines issued by Ofwat.

This additionally requires the Directors to:

- Confirm that, in their opinion, the Company has sufficient financial resources and facilities, management resources and methods of planning and internal control for the next 12 months.
- Confirm that, in their opinion, the Company has sufficient rights and assets, which would enable a special administrator to manage the affairs, business and property of the company.
- Confirm that, in their opinion, the Company has contracts with any associated company with the necessary provisions and requirements concerning the standard of service to be supplied to ensure compliance with the Company's obligations as a water and sewerage undertaker.
- Report to Ofwat changes in the Company's activities, which may be material in relation to the Company's ability to finance its regulated activities.
- Undertake transactions entered into by the appointed business, with or for the benefit of associated companies or other businesses or activities of the appointed business, at arm's length.
- Keep proper accounting records, which comply with Condition F.

These responsibilities are additional to those already set out in the statutory financial statements.

Diversification and Protection of the Core Business (F6a Certificate)

The Directors declare that in their opinion:

- a) The Company 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 Company's obligations under its Instrument of Appointment.
- b) The Company will, for at least the next 12 months, have available to it management resources which are sufficient to enable it to carry out its activities and fulfil its obligations.
- c) 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 undertaker.
- d) The Company will, for at least the next 12 months, have available for it systems of internal control which are sufficient to enable it to carry out its functions.

In making this declaration, the Directors have taken into account:-

- a) The Company's budget for 2018/19 and the investment programme;
- b) The Final Determination for 2015-20 and the Company's plan in relation to it;
- c) The investment grade credit rating in the 'BBB+' band;
- d) The committed borrowing facilities available to the Company;
- e) The depth of the management team and the succession planning in place;
- f) The contracts in place with associated companies;
- g) The Company's internal control process which identifies evaluates and manages risks faced by the Company.



Phil Newland
13 July 2018

Risk and Compliance Statement

Background and requirements of the statement

South Staffs Water has a number of statutory and regulatory obligations as a Water Undertaker. These obligations are predominantly set down in the Water Industry Act 1991 and our Instrument of Appointment (the 'Licence'). The purpose of the Risk and Compliance Statement is to demonstrate that we fully comply with these obligations.

Ofwat guidance requires companies to confirm that it has:

- A full understanding of, and is meeting, all its relevant statutory, licence and regulatory obligations
- Taken steps to understand and meet customer expectations
- Satisfied itself that it has sufficient processes and internal systems of control to fully meet its obligations
- Appropriate systems and processes in place to allow it to identify, manage, mitigate and review its risks

Each of these is considered in the statement below along with how the Company has satisfied itself that it can confirm that the obligations have been met.

1. The Company confirms that it has a full understanding of, and is meeting, all its relevant statutory, licence and regulatory obligations

Each year, the Company considers its obligations as a water undertaker and that it understands and complies with them. This is done in a number of different ways:

- Assessing the impact of any licence changes or changes to the Water Industry Act made during the year and ensuring any new obligations are adopted;
- Reviewing and publishing relevant documents as required under its licence, for example Condition R compliance¹;
- The use of appropriate assurance where required, either through internal audit or external technical audit;
- Requiring Board sign-off of all significant obligations, for example customer charges and the Annual Performance Report;
- An annual review of compliance undertaken by the Audit Committee.

In particular, at a meeting of Directors held on 28 June 2018 the Board confirmed, under license condition F6a, that South Staffordshire Water:

- Has adequate financial resources and facilities, management resources and systems of internal control (including those needed to manage risk) to enable it to carry out its Regulated Activities (including the investment programme necessary to fulfil its obligations under the Appointment);
- Has maintained an investment grade rating from both Moody's and Standard and Poor's.
- Can confirm that there are sufficient rights and assets available to enable a special administrator to run the business;
- Has ensured that Executive Directors' remuneration packages are linked to the performance of the business, taking account of both financial and service performance;
- Has ensured that each Director has confirmed that, in accordance with the Companies Act 2006, as far as they are aware, there is no relevant audit information of which South Staffs Water's auditors are unaware. The Board has taken all reasonable steps to make itself aware of any relevant audit information and to establish that South Staffs Water's auditors are aware of that information.
- Complies with Condition F of its license. The Board can also confirm South Staffordshire Water's compliance with the objectives and principles of RAG 5.07, namely that transactions with associate companies are at arm's length and that cross subsidy is not occurring.

Based on the work undertaken during the year, the Company has not identified any exceptions and can confirm that it has a full understanding of and is meeting all its relevant statutory, licence and regulatory obligations.

1 <https://www.south-staffs-water.co.uk/media/1813/ssc-compliance-code-v3-0-final.pdf>

Risk and Compliance Statement

2. The Company confirms that it has taken steps to understand and meet customer expectations

The Company has a number of outcomes that reflect what our customers have expressed as what matters to them. These outcomes have performance commitments attached that customers can expect us to achieve. Each year we publish our performance in a customer specific report available on our website². We also work with our Customer Panel and share detailed information on our performance on a quarterly basis.

During the year, we have continued to find ways to better listen to our customers and respond to what we hear from them. More in-depth, regular research has been put in place to better understand customers' current and future needs as well as their views of our services. The results are being used to inform business decisions which match with what customers have told us they value.

These research findings are being complemented by the contributions of the Customer Panel which meet once a quarter. On the panel there are representatives from the Environment Agency, CCWater and other members with a variety of skills and expertise from within public and private sectors. The use of their skills and expertise to actively challenge how we as a Company, engage with our customers and perform as a business has been a significant achievement.

We recognise the importance of responding to lifestyle changes and offering greater choice and flexibility in how customers can access information and make contact with us. We already have an online account management service, MyAccount, and we are exploring ways in which we can expand of our digital offering further.

There has also been significant investment in the training of staff and during the year a review of processes and systems have been made to ensure that we are consistently delivering the quality of service our customers expect.

The Company can therefore confirm that it has taken steps to understand and meet customer expectations.

3. The Company confirms that it has satisfied itself that it has sufficient processes and internal systems of control to fully meet its obligations

The Company has a number of processes and controls in place to ensure that it delivers its statutory, licence and regulatory obligations.

There is an established internal control framework that is continually reviewed and updated. This process includes the identification, evaluation and management of the significant risks faced by the Company as set out in the Strategic Report.

Alongside this, the Company also has robust and transparent assurance processes in place as set out in its company monitoring framework³ and assurance plan⁴

There is an internal audit function operated by the Company's parent which provides support in maintaining good systems of internal control and assurance over the quality of information. In addition and as part of its terms of reference, the Audit Committee keep under review the effectiveness of the internal audit arrangements, internal controls and risk management policies and practices. This includes consideration of the statutory and regulatory obligations to ensure compliance.

Based on this, the Company is satisfied that it has sufficient processes and internal systems of control to fully meet its obligations.

² <https://www.south-staffs-water.co.uk/publications/annual-reports>

³ <https://www.south-staffs-water.co.uk/media/1935/risks-strengths-and-weaknesses-publication-november-2017.pdf>

⁴ <https://www.south-staffs-water.co.uk/media/2172/ssc-assurance-plan-april-18.pdf>

Risk and Compliance Statement

4. The Company confirms that it has appropriate systems and processes in place to allow it to identify, manage, mitigate and review its risks.

There is ongoing monitoring of the Company's risk management and internal control systems to review their continuing relevance to the business and their effectiveness and to ensure that appropriate risk management activities are in place or are planned to mitigate the risks identified.

It is accepted that risks can emerge and change quickly and therefore that risk identification and mitigation activities will need to be able to respond to this and that at any given point in time enhancements to mitigating actions may be required in response to changes. Risks are assessed both on a gross basis (likelihood and consequence before mitigating controls) and a net basis (likelihood and consequence after mitigating controls) so that the Directors can properly assess the overall significance of the risk and the estimated effectiveness of mitigating actions and therefore if further actions are required.

The Directors accept that not all risks can be mitigated entirely but aim to ensure that risk management activities reduce the overall impact of risks, on a net basis, to a level that is considered to be acceptable and that do not impact on the long-term viability of the Company.

Overall, the Company is satisfied that it has appropriate systems and processes in place to allow it to identify, manage, mitigate and review its risks.

This statement was approved at a meeting of Directors held on 28 June 2018 and duly signed on their behalf:



.....
Phil Newland
Director
South Staffordshire Water PLC



.....
Sir James Perowne
Independent Chairman
South Staffordshire Water PLC

Transactions Between The Appointee and Associated Companies

The Company is under a duty to trade at arm's length and to ensure that there is no cross-subsidy with respect to transactions with associated companies or between price control units. The Company's licence conditions require that all such transactions must be disclosed. In line with RAG 3.09, no single transaction exceeding £100,000 has been aggregated. Full details are set out on page 153.

Loans by or to the appointee

The Company has two loans to its parent undertaking, South Staffordshire Plc. In accordance with the Company's licence these loans were approved by Ofwat. The first loan is for £15.0m with interest payable at 5.3% and in the year the Company received £0.795m in interest. The second loan is for £25.0m with interest payable at 7% and in the year the Company received £1.750m in interest.

Dividends paid to associated companies

As a wholly owned subsidiary, the Company paid dividends of £16.7m in the year to its holding company, South Staffordshire Plc. This included £2.0m (net of tax) to enable it to pay intra group loan interest to the Company.

Guarantees or other forms of security by the appointee

The Company confirms that there are no guarantees or other forms of security with any associated companies.

Transfers of any asset or liability by or to the appointee

On 1 April 2017 the Company transferred its non-household retail operations and related assets to SSWB Limited, a fellow group company and subsidiary of South Staffordshire Plc (the Company's parent) and therefore exited the non-household retail water market.

On the same day, South Staffordshire Plc subsequently transferred the entire share capital of SSWB Limited to Pennon Water Services Limited (PWS), a subsidiary of Pennon Group Plc (the parent of South West Water Limited), in return for a 20% equity share in PWS for South Staffordshire Plc. Also on 1 April 2017, South West Water Limited transferred its non-household retail operations and related assets to PWS thereby forming a joint venture (PWS) to operate in the non-household retail market.

The Company transferred assets based on an agreed book value comprising; trade debtors; bad debt provisions, accrued income and some fixed assets to complete the transaction. As these were transferred at book value no profit or loss has been recorded in respect of the transaction.

During the year, the Company transferred no other assets or liabilities to an associated company.

Transfer of any corporation tax group losses by or to the appointee

The Company anticipates that it will not claim group loss relief for the year ended 31 March 2018. In the prior year group loss relief of £8.4m was claimed from group holding companies. The Company is paying £1.7m for the losses at the prevailing Corporation Tax rate of 20%, which is considered by both parties to be an arm's length rate.

Transactions Between The Appointee and Associated Companies

Other transactions

The Company can confirm that there has been no omission to exercise a right as a result of which the value of the net assets of the appointee is decreased and that there has been no waiver of any consideration, remuneration or other payment by the appointee.

Supply of services by or to the appointee

All supplies of services by associated companies comply with the objectives and principles of RAG 5.06. Transactions with associated companies are at arm's length, either through competitive tender or at cost, and cross-subsidy is not occurring.

Competitive tender

Whenever a tender process is undertaken and could potentially involve an associated business, the following procedures are followed:

- The procurement team must be involved from an early stage to ensure that a proper tender process is carried out. Where required, this must follow EU procurement rules.
- The tender process must be fully documented. This is to ensure that it is auditable and that the details can be reported in the Annual Performance Report.
- Appropriate approval of the award of contract must be given, usually through a meeting of the Executive Team or the Board of Directors. Any director of the Water Company who is also a director of an associated company tendering must declare an interest, take no part in the discussions and have no vote in the matters discussed.
- Once the award of contract to an associated business is approved, all transactions must be in line with the contract. Any variations to the contract must be approved separately.
- All transactions under a contract with an associated company must be signed off by the appropriate manager to confirm that it is in line with the contract terms.

'At cost' contracts

If work is undertaken by an associated company where no competitive tender has been undertaken, then those transactions must be at cost as per RAG 5.04. The following guidelines are followed:

- All 'at cost' contracts are approved by the Executive Team or the Board of Directors every 12 months. The approval should outline why the contract should continue at cost (for example, performance of the associate during the year, strategic reasons).
- All transactions under the 'at cost' contract must be signed off by the appropriate project manager.
- The cost allocation of the associated company must be fully auditable to show that it is 'at cost'. Sample audits are undertaken by the Group Internal Audit function.

Transactions between price controls

Since the 2014 Price Review, there are now separate binding price controls in place for wholesale, retail household and retail non-household services. Companies need to ensure that there is no cross subsidy between price control units.

The Company has followed the RAGs to ensure that costs are allocated between price controls correctly. The tables in section 2 of this APR and the accompanying cost allocation methodology statement have been reviewed externally by Jacobs to ensure that the Company is compliant with the RAGs.

In addition, there are additional requirements set out in Condition R of the Company's licence in relation to arm's length trading with related licensees operating in the retail business market. This information has to be updated and published each year on its website. The latest version can be found at the following link:

<https://www.south-staffs-water.co.uk/media/1813/ssc-compliance-code-v3-0-final.pdf>

Transactions Between The Appointee and Associated Companies

The following transactions occurred during the 12 months to March 2018:

Associate	Turnover of Associate	Service	Value	Terms of Supply
	£m		£m	
Onsite	66.548	Mainlaying and repair of water mains	16.407	Competitive tendering
		Mains Rehabilitation	3.641	Competitive tendering
		Minor Civils	1.134	Competitive tendering
		Metering	1.327	Competitive tendering
		Reservoir Refurbishment	0.313	Competitive tendering
		Drainage Surveys	0.055	Cost
Integrated Water Services Limited	31.660	Water Treatment	0.006	Cost
		Pump Refurbishment	0.392	Cost
		Capital Works	13.363	Competitive tendering
SSI services UK Limited	2.849	Motor vehicle repair and maintenance	0.595	Cost
Hydrosave	19.579	Leakage detection	0.317	Competitive tendering
Echo Managed Services Limited	30.550	Customer Services	6.354	Cost
		Billing Software	0.399	Cost
South Staffordshire Plc		Management services	3.700	Cost
		HR and Health & Safety	0.019	Cost
		Payroll Services	0.086	Cost
		IT Networks, Operations, Development and Telephony	0.917	Cost
		Finance, Treasury, Internal Audit and AP	0.563	Cost

Services supplied by the appointee to associated companies

Associate	Turnover of Associate	Service	Value	Terms of Supply
	£m		£m	
Echo Managed Services Limited	30.550	Sewerage collections support	0.215	Cost
Echo Managed Services Limited	30.550	Site Services	0.157	Cost
Echo Managed Services Limited	30.550	Recharges for the use of appointed assets	0.102	Cost
SSI Services UK Limited	2.849	Recharges for the use of appointed assets	0.009	Cost
South Staffs Water Non appointed	5.463	Recharges for the use of appointed assets	0.002	Cost
South Staffordshire Plc		Communications and media support	0.040	Cost
South Staffs Water Non appointed	5.463	Management fees	0.076	Cost
South Staffs Water Non appointed	5.463	Operational training	0.003	Cost
Echo Managed Services Limited	30.550	Operational training	0.002	Cost
Hydrosave	19.579	Operational training	0.004	Cost
Integrated Water Services Limited	31.660	Operational training	0.017	Cost
Onsite	66.548	Operational training	0.005	Cost
South Staffordshire Plc		Operational training	0.000	Cost
		Total above (net)	48.957	

Recharges for the use of appointed assets (buildings and vehicles) is based on the equivalent depreciation charge.

Data Assurance Summary

As a monopoly provider of a vital service, we recognise the importance of high quality assurance and governance to ensure that our customers and other stakeholders can have trust and confidence in the information that we publish and the services we provide to the people in our areas of supply on a daily basis.

In 2015 Ofwat published its Company Monitoring Framework, setting out its expectations for how water companies should demonstrate strong assurance and governance, and how Ofwat, as the industry regulator, would monitor this.

We have since worked with our major stakeholders to understand any areas of risk within our assurance processes, and to develop a holistic assurance framework that we use to assess our assurance requirements. Since 2015 we have consulted with our stakeholders each year to identify those risks and to put in place a plan to address them. Our latest assurance plan, covering this annual performance report and also other important submissions to take place this financial year, can be found on our website at:

<https://www.south-staffs-water.co.uk/about-us/our-strategies-and-plans/our-assurance-framework>

Our auditors

We have two primary audit requirements for the annual performance reporting information:

- financial data relating to our accounting reporting and financial performance
- technical data relating to our water service performance

We utilise a financial auditor, Deloitte LLP, for the statutory and regulatory financial accounting audits. They have an extensive understanding of the statutory and regulatory accounting requirements.

We utilise a technical auditor, Jacobs UK Limited, for the water service performance which includes performance commitments and other technical data related to water supply reporting. We appointed Jacobs in 2017 after a process of competitive tender, as we recognised that their broad experience of technical audit and their extensive knowledge of the current regulatory environment would work well with our continued data quality improvements.

The logo for Deloitte, featuring the word "Deloitte" in a bold, black, sans-serif font. A small green dot is positioned at the end of the word.The logo for Jacobs, featuring the word "JACOBS" in a bold, blue, sans-serif font. A registered trademark symbol (®) is located at the top right of the word.

Data Assurance Summary

Assurance of this Annual Performance Report (APR)

The APR is split into four sections. We summarise below our overall principles of assurance for each of those sections.

Sections 1 and 2 – Regulatory financial reporting, price review and other segmental reporting

Data reported in sections 1 and 2 is produced consistent with the RAGs published in November 2017. Deloitte LLP, our statutory auditor, audits this section of the APR and their audit opinion is contained within this APR document. The one exception is table 1F, financial flows, which is being piloted this year. We have decided to include it within our APR to ensure transparency and have used Jacobs to undertake assurance.

Section 3 – Performance summary

This section of the APR sets out our performance against our outcomes and ODIs.

We have used Jacobs, our external technical auditors, to audit our financially incentivised ODIs, reward and penalty calculations, asset health sub measures and SIM performance. A statement from Jacobs is provided on pages 161 to 162.

Our ODIs which are non-financial, and our AIM table, have been audited by the independent internal audit function of our parent company.

Section 4 – Additional regulatory information

There is a mix of tables and data within section 4 of the APR. Where data in these tables is the same as used in other areas of the APR then these data items are covered by the audits in sections 1, 2 and 3. We have also used Jacobs to review our Return on Regulated Equity (RORE) calculation as this is a key metric used by Ofwat and other key stakeholders.

Data Assurance Summary

Improvements we have made to our Annual Performance Report

In our Assurance Plan, published in April 2018, we defined a number of targeted areas that required extra focus this year. The table on the following page identifies those targeted areas that are relevant to this APR and explains how we have addressed them.

Targeted area	How we have improved
Cost allocation	<p>As committed to in our assurance plan, we subjected our cost allocation methodology to external assurance for this reporting year, using our assurance partner, Jacobs. Their work checked that our methodology complies with Ofwat's Regulatory Accounting Guidelines (RAGs).</p> <p>We also continued to use our statutory financial auditor, Deloitte LLP, to audit the cost allocation data back to source for the annual accounts.</p>
Annual performance report	<p>In November 2017, Ofwat indicated minor concerns with this area of our reporting for 2016-17 through our company monitoring framework assessment. This was in relation to how some financial metrics are calculated, which did not fully meet Ofwat's expectations. We reissued our 2016-17 APR with recalculated figures and have ensured that these metrics have been calculated in line with guidance for this year.</p> <p>We have used Jacobs to review some key data to this year's APR including:</p> <ul style="list-style-type: none"> • Table 1F – Financial flows (a new table for this year) • Table 4C – Forecast impact of performance on RCV (An existing table but with new guidance on how to complete) • Table 4H - Return on Regulated Equity (A key measure used by Ofwat across the industry)
Reporting of key metrics in a consistent way	<p>For the past year the water industry has collectively been working to understand any issues of reporting consistency between companies on core service measures. This data is not published as part of this report but is reported to Ofwat. Some of our data and systems are not fully compliant with the latest methodologies and need further development, which is the case for all companies. We are actively working towards full compliance by April 2020. We have separately provided Ofwat with a 'red amber green' assessment of our compliance against all of these metrics.</p>

Data Assurance Summary

We have also identified a number of additional improvements to our APR.

Theme of improvement	How we have improved
Data assurance summary	We have expanded the data assurance summary to cover all significant publications in the reporting year, as it is timely to provide this information to all stakeholders via this report.
Cost assessment tables	There are a number of new data tables to be completed this year, which although not part of the APR itself have been published separately on our website. These tables will be used by Ofwat as part of the PR19 price review process, and it is therefore important that they are accurate. We have therefore used Jacobs to assure these tables this year.
Financial monitoring framework	<p>We have enhanced the wording on our long term viability statement to meet Ofwat's expectations. This includes more details around:</p> <ul style="list-style-type: none"> • Explaining the stress tests we have used on our future financial plans; • Explaining the impact on our credit metrics • Setting out mitigating actions we can take to offset key risks • Explaining the choice of time period which the stress tests covers <p>We have also had our statement assured by Jacobs UK Limited and signed by our Managing Director on behalf of our Board.</p>
Transparency with stakeholders	<p>We recognise that the financial statements and full APR document are not easy to read at over 160 pages. Since 2015/16 we have also published a summary performance report alongside our full APR which is aimed at customers and non-technical stakeholders. We continue to engage with customers to improve this document, and we have also looked at the full APR document to improve readability where we can, for example by including more commentary and an upfront summary.</p> <p>We also want to maximise areas of voluntary disclosure – these are areas that are not explicitly required to be provided for in any guidance but which provide useful information and context about how we operate.</p>

Customer Panel

Throughout the year we have provided quarterly updates to our Customer Panel on our performance and year end forecasts. We have also sought the views of the panel on our summary version of our APR, which is significantly shortened version containing key information for customers and other stakeholders who do not need to read the full version of this document.

Data Assurance Summary

Other significant publications

The following table highlights other significant publications we have made in the reporting year.

Summary performance report	<p>As well as this full version of the APR, containing the full narrative and statutory and regulatory accounts, we have also implemented again this year a summary version of the APR targeted at customers, called the Summary Performance Report. We feel this is important as this full document is not easily absorbed by customers or non-technical stakeholders. We asked customers about our summary document in 2017 and we have improved our document again this year with a more succinct summary table detailing what performance commitments we have passed and failed. We'll continue to engage our customers to ensure they are getting what they want from our reporting.</p>
Draft water resources plan	<p>On 1st December 2017 we submitted a draft of our next Water Resource Management Plans (WRMP19) to Defra – we submitted a separate WRMP for each region. We ran a public consultation on these from March 2018 to May 2018.</p> <p>We received consultation responses from the EA, Defra, Ofwat, CCWater and other organisations and will publish our Statement of Response (SoR) by the end of August 2018.</p>
EA annual return 2017/18	<p>Each year we report our progress against our Water Resource Management Plan (WRMP) to Defra and the EA as an annual review. This annual review includes commentary on progress as well as data such as our actual 2017-18 water consumption.</p> <p>We followed the EA reporting guidance to produce our 2017-18 WRMP annual review. We produced separate submissions for each of our regions. As most of the data in our annual review is from the APR it has been through that level of assurance.</p> <p>We submitted our WRMP annual reviews on 29 June 2018 which met the deadline associated with these reviews.</p> <p>The final reports have also been placed on our website for general access (https://www.south-staffs-water.co.uk/publications/environment).</p>
DWI annual return 2017	<p>Over the reporting year we have extensive ongoing engagement with the DWI across a range of day to day processes, regular data submissions and end of year data submissions.</p> <p>The data submission in February 2018 covered the calendar year 2017 and provided data on customer contact rates to the DWI which is used, alongside regulatory sample data provided throughout the year, to monitor and report on our compliance. The DWI's Drinking Water 2017 report is due to be published in July 2018.</p> <p>The DWI have recently begun trialling a new water quality composite measure, the Compliance Risk Index (CRI). We will support DWI as appropriate by ensuring that data we supply and our interactions are high quality.</p>

Data Assurance Summary

<p>Carbon Reduction Commitment scheme 2017/18</p>	<p>The CRC Energy Efficiency Scheme is a UK government scheme designed to improve energy efficiency and cut carbon dioxide emissions in private and public sector organisations that are high energy users. The Environment Agency administers the scheme for the UK and regulates the scheme in England.</p> <p>In each compliance year, we collate and report information about our energy supplies in order to buy and surrender the appropriate carbon emission allowances. We inform the EA about changes to the organisation that could affect our registration and we also keep the appropriate records about our energy supplies and organisation in an evidence pack. To ensure accuracy and consistency we engaged independent internal audit to check through the data sources and calculation methodologies.</p> <p>Each autumn, the Environment Agency publishes a table showing the emissions data submitted by CRC participants in its Annual Report Publication (https://www.gov.uk/guidance/crc-energy-efficiency-scheme-annual-report-publication).</p>
<p>CCWater annual update 2017/18</p>	<p>We supply CCWater with final, audited, year-end data at the same time as we publish our APR. The data we submit being the final year end update to the quarterly reporting information that we send throughout the year but which does not get audited until June each year. The data we submit to CCWater at the year-end is robust as it is the same data that we publish in the APR.</p>
<p>Developer charges 2017/18</p>	<p>In February 2018 we published our new developer charges document which follows Ofwat’s new charging rules. These new rules are to ensure that companies have clear and transparent charging structures and are fair to both developers, self-lay providers and New Appointments and Variations (NAVs).</p> <p>We held two developer forums to understand stakeholder views and this helped us to design our charges in way that was clear and easy to understand, in particular moving to a cost per plot basis for any on-site mains required.</p> <p>We also adopted Ofwat’s thinking on how NAVs should be charged for a bulk supply from us and set this out in detail.</p> <p>Our charging document can be found here: https://www.south-staffs-water.co.uk/media/2207/developer-services-1st-april-charging-approach.pdf</p> <p>We also set out how we had complied with the new charging rules and this was approved by our Board. This can be found on our website: https://www.south-staffs-water.co.uk/media/2127/ssc-developer-charges-board-assurance-statement.pdf</p>

Data Assurance Summary

Board governance

Our Board has had extensive involvement in the production, audit and publication of our APR including the summary version intended for customers and non-technical stakeholders.

The Audit Committee has overseen the external and internal assurance that has been undertaken on the APR, and all audit reports produced internally and externally have been made available to the Committee and to the full Board for review and challenge.

The Board has also satisfied itself that we have implemented the improvements to the APR that we committed to in our assurance plan, shown in the table above.

With sight of all of the above audit information, the Board has signed off the APR submission as being an accurate set of information on our 2017/18 regulatory accounts and performance.

External Assurance of Financial ODIs

For the attention of the Audit Committee 12 July 2018

2017-18 APR assurance

For the period 2015-20 Ofwat requires companies to complete an Annual Performance Report (APR). For 2017/18 Ofwat expanded the scope of the APR to incorporate additional information, including on an expanded set of shadow Performance commitments (PCs) and additional cost and non-cost data in section 4 of the APR. These additional items were previously reported outside the APR and are designed to inform its PR19 determinations. As your technical assurance partner, you asked us to take a risk-based approach to the following APR areas.

- **PCs** – We reviewed the proposed performance figures for the PCs in your final determination (FD) that have financial rewards and penalties associated with them.
- **APR section 4 cost assessment tables (CAT)** – We sample checked data across a selection of lines in the APR section 4 tables, focusing mainly on tables and 4P, 4Q and 4C.
- **Shadow PCs** – Our assurance focused on the compliance assessments you are required to make for the six shadow PCs that you are required to report against in the APR.
- **Cost allocation** – We reviewed your overarching approach to cost allocation within the appointed business for allocations between price controls and business units, which supports your reporting of some financial information in section 4 of the APR.
- **Return on regulated equity (RoRE)** – We reviewed your notional return on regulated equity (RoRE) and your Financial Flows table for the period 2015-16 to 2017-18.
- **Long term viability statement (LTV)** - reviewed your statement and assessed its consistency with Ofwat guidance

Our assurance work is focused on assessing the level of reporting risk associated with data items. For the areas noted above we observed the following.

Across the PC and APR section 4 CAT data we reviewed we generally observed no material issues with the data being reported and that your teams understood the reporting requirements and their processes. At the time of writing there are only two areas we consider might present a material reporting risk (see table below).

Area	Potential outstanding material reporting risk
Serviceability (noninfra) PC - unplanned maintenance	The team has a good understanding of the process and data. However, we consider the quality and completeness of the source data presents a material risk to the CAM unplanned maintenance figure. The team is reliant on paper documentation and cannot reliably determine if it is capturing all unplanned maintenance paper records. We note that whilst material for the CAM region, the company's overall performance for this serviceability component is significantly below the reference level and the impact on the overall serviceability assessment of stable is unlikely to be material.
APR CAT data – CAM operational data	The team had worked hard to produce multiple datasets but we identified a number of issues with the data for these lines (e.g. current risk of double counting of a works in terms of volumes). We note the team is aware of the risks and is aiming to verify and finalise the outstanding figures for reporting ahead of publication.

We note that for leakage PC, we observed that your proposed performance figure reflected an undefined mix of real and methodology/data improvements. We recommended that you are clear how your leakage performance is being calculated and reported on and advised you to reflect on Ofwat's PR19 expectations for PC reporting in relation to real/methodological/data changes when reporting on 2015-20 performance and associated rewards and penalties. We understand your performance means you expect to incur financial penalties for your leakage performance in your Cambridge region. We also noted that within your water balance assessment, there was scope for you to explain more fully your levels of meter under registration, which we consider high compared to your peers. For the shadow PCs, we consider your reporting against each of the six measures currently carries a material level of reporting risk. Our assessment is driven by a mix of your teams' own assessment of compliance with Ofwat's guidance; the completeness of those assessments (including aggregation of assessment components); the clarity of Ofwat's guidance; and the fact that for most areas of non-compliance there is scope to develop more detailed, and more integrated, plans on how you expect to move to compliance. We note Ofwat expects companies to move towards full compliance as quickly as possible (to help inform its PR19 determinations) and by no later than the 2020-21 reporting year. For the per capita consumption shadow PC, we consider there is a risk your current plan to move to full compliance will not result in full compliance by 2020-21.

External Assurance of Financial ODIs

As part of our assurance on your cost allocation we observed that you have satisfactory processes in place to report financial data for tables 4D and 4F that are compliant with the principles and rules of Regulatory Accounting Guidelines 1-4. We observed that data is generally captured in your financial systems at a sufficiently granular level to allow reporting at business unit level. Although we note that currently the production of the APR tables is reliant on adjustments and data manipulation in Excel, and recommend that some of this process could be integrated into the system to reduce reporting risk.

During our review of your RoRE and financial flows reporting, we observed that the calculations, assumptions and inputs to the Headline RORE model are consistent with the methodology provided by Ofwat. Where appropriate you have sought consistency between your headline RORE calculations and Financial Flows calculations. With this principle in mind we note that you have calculated the cost of debt adjustment by reference to the net debt figure used in your headline RORE calculation. We also note that you identified a number of errors in the formulae contained within the updated Financial Flows Table that was provided by Ofwat 23 May 2018. You have amended them in the table you intend to submit and informed Ofwat of your approach.

As part of the year end reporting and in line with the "Corporate Code" and published Ofwat reporting requirements, you are required to publish a long term viability statement (LTV). As part of our review we noted some minor amendments that might enhance the statement, (for example, being explicit that the company recognises that any remedial action would need to be considered in the context of its quality obligations and customer commitments). Overall we considered that your LTV represents a fair, balanced and understandable assessment of the Company's position and prospects. Your statement appears to provide an appropriately detailed explanation of how the prospects of the Company have been assessed and over an appropriate period of seven years

This letter summarises the results of our APR assurance to date. We have provided you with a separate report that sets out our scope, findings and general observations in more detail.

Andrew McGeoghan

Head of Economic Regulation and Assurance

Management Response to Jacobs' Letter of Assurance

Jacobs has carried out a detailed and extensive review across six key areas of our APR as requested; we would like to thank Jacobs for the thoroughness of their work. We have engaged closely with this review and made a number of changes as a result of the insight provided, and continue to address some of the longer term recommendations and observations. The key purpose of this review has been to provide assurance to our Board (and to other stakeholders) as to the quality and accuracy of the reporting and the related data within our APR. We believe that the intended assurance has been successfully delivered. Jacobs raise a number of points that we feel are worthy of management comment:

Serviceability (non-infra) performance commitment – unplanned maintenance

We recognise the need to improve source data within our Cambridge region and the move away from paper records is now taking place. We agree that this matter will not materially affect the overall stable serviceability assessment.

APR cost assessment tables – operational data

We have carried out further validation of the Cambridge data and where necessary have made amendments where these can be agreed with Jacobs. We consider all changes to be minor.

Leakage performance commitment

We note the Jacobs' recommendation to clarify and explain some areas of leakage reporting.

Shadow performance commitments

We have a detailed plan for achieving compliance with all shadow performance commitments; our position is constantly improving as we deliver this plan and more detail is disclosed in our separate commentary to table 3S.

Reliance on Excel

We recognise that a more integrated approach would add value, and will work towards improving the process.

Internal Independent Assurance of Reputational ODIs

South Staffs and Cambridge Water 2017/18

As the South Staffordshire Group Internal Audit Manager (with over twenty-five years' experience of working within the Water Industry), Internal Audit was requested to perform an independent review of the reporting of reputational ODIs below:

- Biodiversity
- Carbon Emission savings
- Support for Customers in Debt
- Community Engagement
- Customer Satisfaction
- Value for Money and Affordability
- Abstraction Incentive Mechanism

The audit work carried out sought to review the methodology supporting the calculations to ensure accuracy, consistency and validity of the numbers provided.

Internal Audit has confirmed that that the figures reported have been validated and checked to supporting information.

Glyn Palmer BA (Hons) FCA
Group Internal Audit Manager
July 2018

Independent Auditors Report

Independent Auditors' report to the Water Services Regulation Authority (the WSRA) and the Directors of South Staffordshire Water Plc

Report on the audit of the Regulatory Accounting Statements

Opinion

We have audited the tables within South Staffordshire Water Plc's ("the Company") Annual Performance Report for the year ended 31 March 2018 ("the Regulatory Accounting Statements") which comprise:

- the regulatory financial reporting tables comprising the income statement (table 1A), the statement of comprehensive income (table 1B), the statement of financial position (table 1C), the statement of cash flows (table 1D) and the net debt analysis (table 1E) and the related notes; and
- the regulatory price review and other segmental reporting tables comprising the segmental income statement (table 2A), the totex analysis for wholesale water (table 2B), the operating cost analysis for retail (table 2C), the historical cost analysis of fixed assets for wholesale and retail (table 2D), the analysis of capital contributions and land sales for wholesale (table 2E), the household water revenues by customer type (table 2F), the non-household water revenues by customer type (table 2G), the revenue analysis & wholesale control reconciliation (table 2I), the infrastructure network reinforcement costs (table 2J) and the related notes.

We have not audited the financial flows table (table 1F), the outcome performance tables (tables 3A to 3d) and the additional regulatory information (tables 4A to 4I).

In our opinion, South Staffordshire Water Plc Regulatory Accounting Statements have been properly prepared in accordance with financial reporting provisions of Condition F, the Regulatory Accounting Guidelines issued by the WSRA (RAG 1.08, RAG 2.07, RAG 3.10, RAG 4.07 and RAG 5.07) and the accounting policies (including the Company's published accounting methodology statement, as defined in RAG 3.10, appendix 2), set out on pages 116 to 117.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)"), including ISA (UK) 800, and applicable law, and having regard to the guidance contained in ICAEW Technical Release Tech 02/16 AAF 'Reporting to Regulators on Regulatory Accounts' issued by the Institute of Chartered Accountants in England & Wales.

Our responsibilities under ISAs (UK) are further described in the Auditor's responsibilities for the audit of the Regulatory Accounting Statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the Regulatory Accounting Statements in the UK, including the Financial Reporting Council's Ethical Standard, and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of matter – special purpose basis of preparation

We draw attention to the fact that the Regulatory Accounting Statements have been prepared in accordance with Condition F, the Regulatory Accounting Guidelines, the accounting policies (including the Company's published accounting methodology statement, as defined in RAG 3.10, appendix 2) set out in the statement of accounting policies and under the historical cost convention. The nature, form and content of the Regulatory Accounting statements are determined by the WSRA. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the WSRA's purposes. Accordingly we make no such assessment.

The Regulatory Accounting Statements are separate from the statutory financial statements of the Company and have not been prepared under the basis of United Kingdom Generally Accepted Accounting Practice ("UK GAAP"). Financial information other than that prepared on the basis of UK GAAP does not necessarily represent a true and fair view of the financial performance or financial position of a Company as shown in statutory financial statements prepared in accordance with the Companies Act 2006.

Independent Auditors Report

The Regulatory Accounting Statements on pages 108 to 126 have been drawn up in accordance with Regulatory Accounting Guidelines with a number of departures from UK GAAP. A summary of the effect of these departures from Generally Accepted Accounting Practice in the Company's statutory financial statements is included in the tables within section 1.

The Regulatory Accounting Statements are prepared in accordance with a special purpose framework for the specific purpose as described in the respective directors' and auditor's responsibilities sections below. As a result, the Regulatory Accounting Statements may not be suitable for another purpose.

Our opinion is not modified in this respect.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which ISAs (UK) require us to report to you when:

- the directors' use of the going concern basis of accounting in the preparation of the Regulatory Accounting Statements is not appropriate; or
- the directors have not disclosed in the Regulatory Accounting Statements any identified material uncertainties that may cast significant doubt about the Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the Regulatory Accounting Statements are authorised for issue.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Company's ability to continue as a going concern.

Other information

The other information comprises all of the information in the Annual Performance Report other than the Regulatory Accounting Statements and our auditor's report thereon. The directors are responsible for the other information. Our opinion on the Regulatory Accounting Statements does not cover the other information and, accordingly, we do not express an audit opinion or any form of assurance thereon.

In connection with our audit of the Regulatory Accounting Statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Regulatory Accounting Statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the Regulatory Accounting Statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement or inconsistency of this other information, we are required to report that fact.

We have nothing to report based on these responsibilities.

Responsibilities of the Directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 146, the directors are responsible for the preparation of the Regulatory Accounting Statements in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the Company's accounting policies (including the Company's published accounting methodology statement, as defined in RAG 3.10, appendix 2).

The directors are also responsible for such internal control as they determine is necessary to enable the preparation of the Regulatory Accounting Statements that are free from material misstatement, whether due to fraud or error.

In preparing the Regulatory Accounting Statements, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Independent Auditors Report

Auditors' responsibilities for the Audit of the Regulatory Accounting Statements

Our objectives are to obtain reasonable assurance about whether the Regulatory Accounting Statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these Regulatory Accounting Statements.

A further description of our responsibilities for the audit of the Regulatory Accounting Statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Report on other legal and regulatory requirements

Opinion on other matters prescribed by Condition F

Under the terms of our contract we have assumed responsibility to provide those additional opinions required by Condition F in relation to the accounting records. In our opinion:

- proper accounting records have been kept by the appointee as required by paragraph 3 of Condition F; and
- the Regulatory Accounting Statements are in agreement with the accounting records and returns retained for the purpose of preparing the Annual Performance Report.

Use of this report

This report is made, on terms that have been agreed, solely to the Company and the WSRA in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewage undertaker under the Water Industry Act 1991 ("Condition F"). Our audit work has been undertaken so that we might state to the Company and the WSRA those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under Condition F to procure such a report and (b) to facilitate the carrying out by the WSRA of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the WSRA, for our audit work, for this report or for the opinions we have formed.

Our opinion on the Regulatory Accounting Statements within the Annual Performance Report is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2018 on which we reported on 13 July 2018, which are prepared for a different purpose. Our audit report in relation to the statutory financial statements of the Company (our "Statutory audit") was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our Statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a statutory audit report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our Statutory audit report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.



Deloitte LLP
Chartered Accountants and Statutory Auditors
London, United Kingdom
13 July 2018

