



# ANNUAL PERFORMANCE REPORT 2020



Havant Thicket Winter Storage Reservoir

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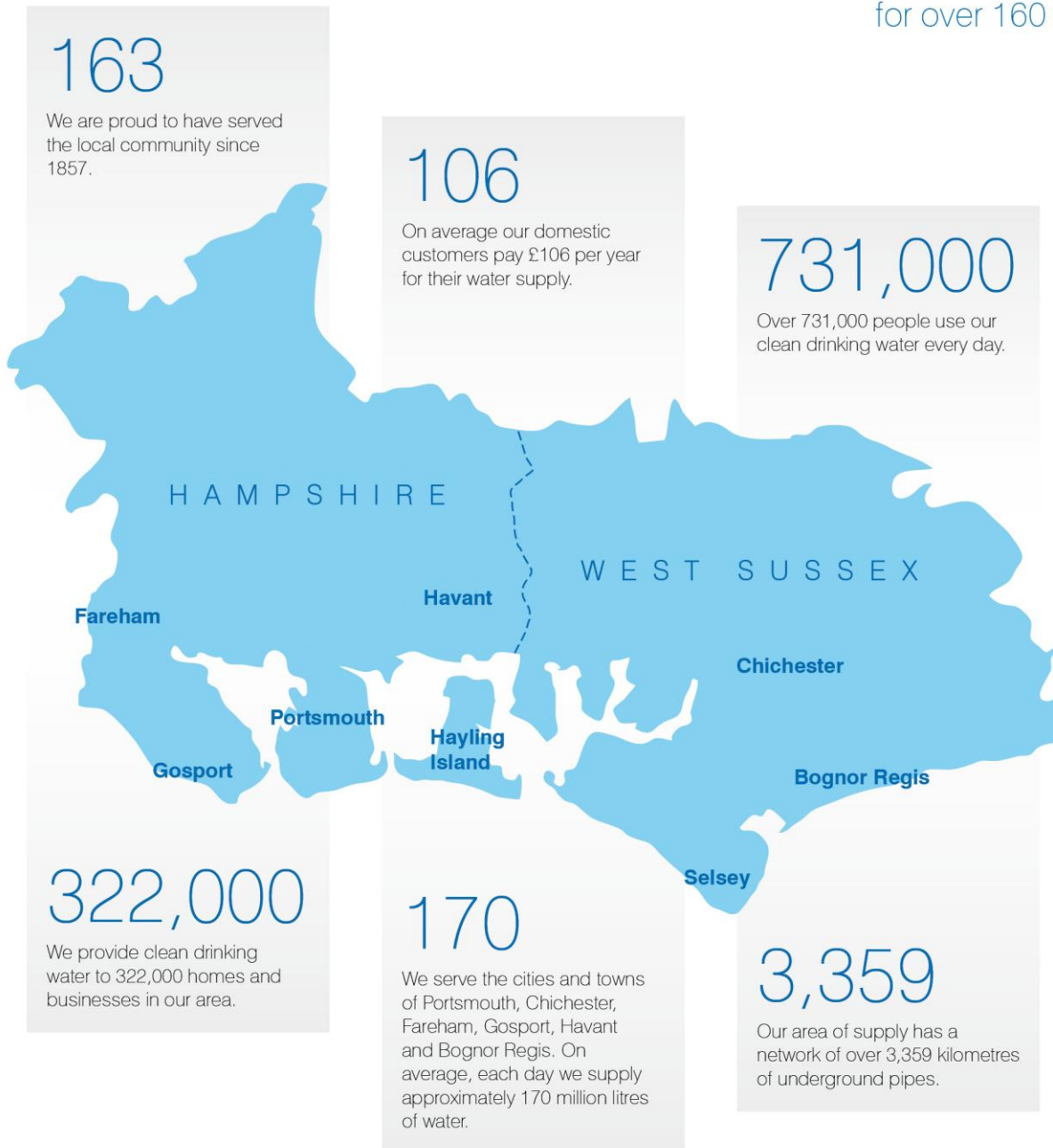
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## INTRODUCTION

### INTRODUCTION

Portsmouth Water Limited is a water supplier operating under an Instrument of Appointment granted by the Secretary of State for the Environment under the Water Industry Act 1991. In accordance with the requirements of the Company's licence conditions and Ofwat guidance the Company both operates and prepares its statutory Annual Report and Accounts ('ARA') having regard to the requirement of Disclosure and Transparency Rules and the relevant elements of the UK Corporate Governance Code. This Annual Performance Report ('APR') has been prepared in accordance with the requirements of Regulatory Accounting Guidelines published by Ofwat. The Company does not prepare a combined document covering both ARA and APR but, as permitted and where appropriate, cross references to the published ARA. Copies of the ARA can be obtained from the Company Secretary at PO Box 8, West Street, Havant, PO9 1LG and on the Company's website at [www.portsmouthwater.co.uk](http://www.portsmouthwater.co.uk).

A local company  
with a proud history of  
serving our customers  
for over 160 years



*We provide drinking water only. We do not provide sewerage services; these are normally provided by Southern Water*

### **“Delivering excellence for our customers, our people, the environment and the communities that we serve”**

Portsmouth Water’s Board takes overall responsibility for developing the Company Purpose - including the strategy, objectives, values and culture that the business needs to deliver this successfully.

The Company Purpose, together with the underlying strategy and objectives, is periodically re-assessed and revised by the Board to make sure that it continues to reflect the needs of our customers and stakeholders. This took place as part of the development of the regulatory Business Plan for 2020-2025 and the longer term vision beyond that.

In developing the Business Plan and Company Purpose the Company undertook significant engagement activities, with both customers and wider stakeholders. The Board was closely involved in understanding the approach to, and results of, this engagement. It took overall ownership for ensuring that the results of this engagement were appropriately reflected in the Business Plan and Company Purpose together with the strategy, objectives, values and culture needed to deliver for customers and stakeholders. As a result of this we updated the underlying business objectives for the next regulatory period 2020-2025 (known as 'outcomes') as set out below;

#### Company Outcomes:

**Safe, secure and reliable supply of drinking water**

**Long term resilience of supplies for our customers and to support the South East region**

**Low leakage**

**A service tailored to individual needs at an affordable price**

**An improved environment supporting biodiversity**

**Being recognised by the community as a good Corporate Citizen**

**Recognised by stakeholders as having a culture of Health & Safety through all of our activities**

The Board noted, in particular, the strong support across customers and stakeholders alike for our 'community driven' focus, particularly where we go beyond our statutory duties. Whilst Portsmouth Water has long been recognised as a business which cares about and supports our local communities we explicitly updated our Company Purpose to reflect this important aspect. In parallel our Young Persons Board was asked by the Board to develop the Portsmouth Water Community Partnership.

The Board puts great emphasis in ensuring our business has the right values and culture - which are aligned to the Company's Purpose. Indeed we recognise that our values driven approach empowers staff to 'do the right thing' and is a strong contributor to the consistently high levels of customer service we deliver. The Board also seeks the views of customers and stakeholders, with particular emphasis on independent assessments such as the Institute of Customer Service 'ServiceMark' accreditation and staff views through regular surveys. Where there is evidence of any misalignment of values and behaviours, the Board acts to correct this, through the executive team. More information in relation to the Company values, is included in the Annual Report & Accounts (ARA) under 'Our People'.

### **CORPORATE GOVERNANCE**

The Board of Portsmouth Water Limited, at 31 March 2020, comprised of two Executive Directors, two independent Non-Executive Directors and one Investor Director. The Executive Directors are Bob Taylor, who is the CEO, and Helen Orton who is the Finance and Regulation Director. The independent Non-Executive Directors are Mike Kirk (Chairman), Mike Coffin and Martin Johnson. In addition, there is one Investor Director, David Owens.

After 8 years as an Independent Director and Chairman, Mike Kirk has taken the decision to step down from the Board. Christopher Deacon was appointed as a Non-Executive Director on 1 May 2020 and was appointed to the Role of Chairman on 26<sup>th</sup> June following Mr Kirk's departure.

The Ofwat principles require that independent Non-Executives should constitute the largest single group of Directors. Portsmouth Water complies with this requirement.

Portsmouth Water are committed to high standards of Corporate Governance and take the lead from those principles set out in the UK Corporate Governance Code and guidance issued by Ofwat. That guidance highlighted Ofwat's principles by which they believe Water Companies should deal with Board Leadership, transparency and governance.

Detailed information in connection with the Company's Corporate Governance processes and compliance, including operation of the Board, Risk Management and Internal Control is set out on pages 36-53 of the Company's ARA.

### **Compliance**

In 2019 Ofwat published the updated principles by which water companies should deal with Board leadership, transparency and governance. These take full effect for the current reporting period. Accordingly the Company updated its own Governance Code to align to these principles. This can be found on the Portsmouth Water website. The Board complies with the Ofwat principles in all areas and has provided a summary of how the Company meets Ofwat's principles, on pages 7 and 8.

### **Auditors**

KPMG LLP were appointed as Auditors of the Portsmouth Water Group during 2017, in relation to the year ended 31 March 2018, and have continued in office since that time.

## CORPORATE GOVERNANCE

The Board has considered the revised Ofwat corporate governance requirements in relation to leadership, transparency and Governance. For ease of reference the key provisions have been summarised and referenced to the areas of the Annual Report & Accounts (ARA) where further information can be found, in the table below. This table refers to the relevant pages and sections of the Company's ARA.

<b>Purpose, values and culture</b> The Board of the Appointee establishes the company's purpose, strategy and values, and is satisfied that these and its culture reflect the needs of all those it serves.	
<b>Provisions</b>	
The board develops and promotes the company's purpose in consultation with a wide range of stakeholders and reflecting its role as a provider of an essential public service.	Following the extensive stakeholder engagement as part of PR19, we undertook work to update the Company Purpose, this is set out in more detail on page 8. In parallel to this we also formalized out commitments to the communities that we serve through our Community Partnership.
The board makes sure that the company's strategy, values and culture are consistent with its purpose.	The Company's Purpose is developed from and underpinned by the Company's "Vision" and "Values". We explain more about our values under "Our Customers and "Our People".
The board monitors and assesses values and culture to satisfy itself that behaviour throughout the business is aligned with the company's purpose. Where it finds misalignment it takes corrective action.	The Board assesses behaviors throughout the business in a number of ways including reviewing the results of Company-wide staff surveys and regular monthly management reporting. Where the Board finds misalignment this is addressed directly through the actions of the Executive directors and senior leadership team and through direct alignment to the company staff assessment and appraisal process. We explain more about this alignment under "Our People".
Companies' annual reporting explains the board's activities and any corrective action taken. It also includes an annual statement from the board focusing on how the company has set its aspirations and performed for all those it serves.	This is communicated throughout the annual Report and Accounts and in particular under, "Our Company Purpose", "Our Strategy" and "How we measure success".
<b>Standalone regulated company</b> The Appointee has an effective Board with full responsibility for all aspects of the Appointee's business for the long term.	
<b>Provisions</b>	
The regulated company sets out any matters that are reserved for shareholders or parent companies (where applicable); and explains how these are consistent with the board of the regulated company having full responsibility for all aspects of the regulated company's business, including the freedom to set, and accountability for, all aspects of the regulated company's strategy.	This is set out in the Corporate Governance section under "Board of Directors".
Board committees, including but not limited to audit, remuneration and nomination committees, report into the board of the regulated company, with final decisions made at the level of the regulated company.	This is set out in the Corporate Governance section under "Board of Directors".
The board of the regulated company is fully focused on the activities of the regulated company; takes action to identify and manage conflicts of interest, including those resulting from significant shareholdings; and ensures that the influence of third parties does not compromise or override independent judgement.	The Board is made up of a majority of independent Non-Executive Directors. This is set out in the Corporate Governance section under "Board of Directors".

## CORPORATE GOVERNANCE

### Board leadership and transparency

The Board of the Appointee's leadership and approach to transparency and governance engenders trust in the Appointee and ensures accountability for their actions.

#### Provisions

An explanation of group structure;	The Group structure is set out on page 47 of the Corporate Governance report.
An explanation of dividend policies and dividends paid, and how these take account of delivery for customers and other obligations (including to employees);	The dividend policy is explained on page 27 of the strategic report. This was updated as part of the PR19 Business Plan process.
An explanation of the principal risks to the future success of the business, and how these risks have been considered and addressed;	The Principle risks and uncertainties faced by the business are covered both under "the issues that affect us" and "Principal risks and uncertainties".
The annual report includes details of board and committee membership, number of times met, attendance at each meeting and where relevant, the outcome of votes cast;	This is set out in the table of meetings on page 50.
An explanation of the company's executive pay policy and how the criteria for awarding short and long-term performance related elements are substantially linked to stretching delivery for customers and are rigorously applied. Where directors' responsibilities are substantially focused on the regulated company and they receive remuneration for these responsibilities from elsewhere in the group, policies relating to this pay are fully disclosed at the regulated company level.	This is reflected under "Remuneration Committee" on pages 56 to 61, including the linkage of remuneration to stretching delivery targets.

### Board structure and effectiveness

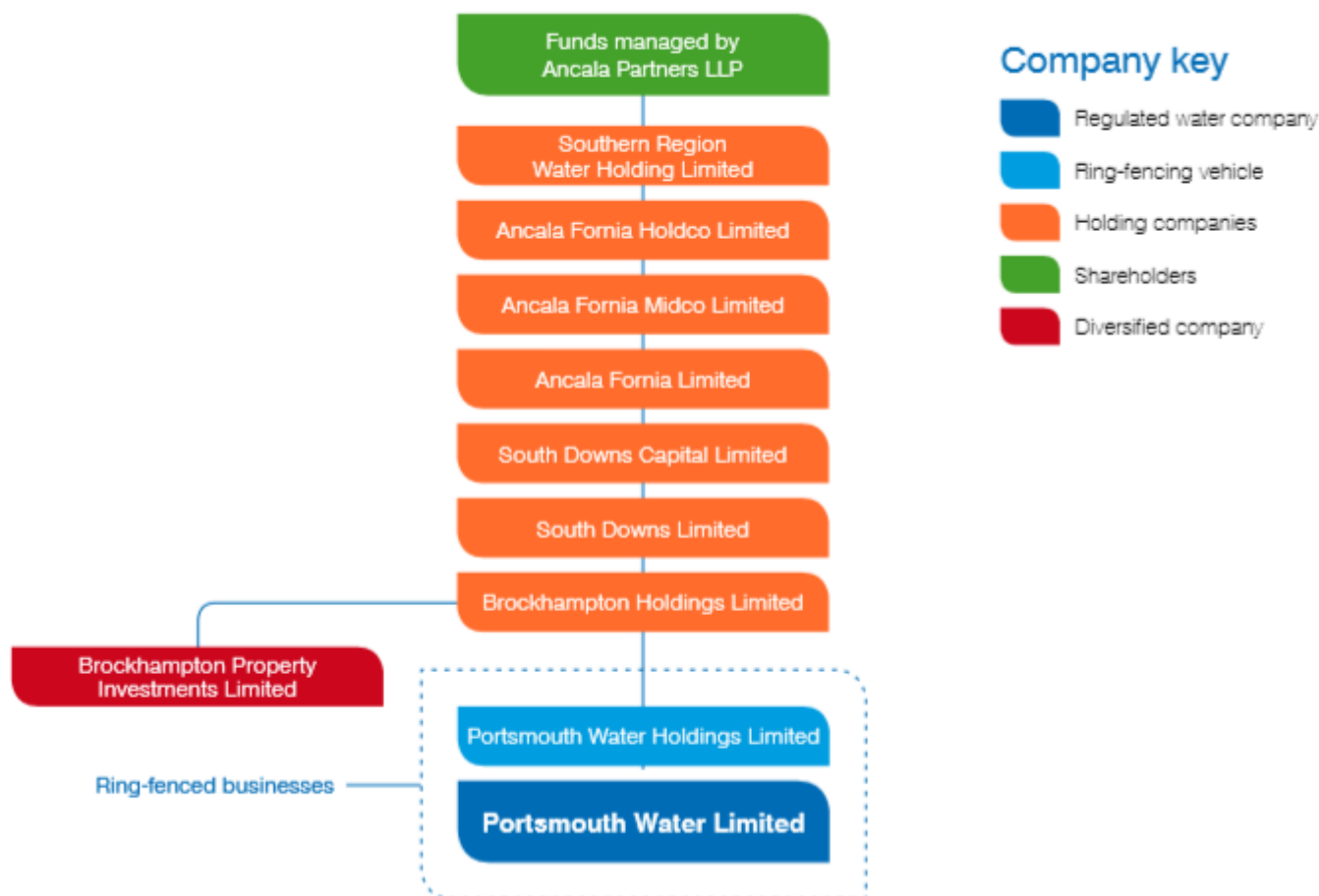
The Board of the Appointee and their committees are competent, well run, and have sufficient independent membership, ensuring they can make high quality decisions that address diverse customer and stakeholder needs.

#### Provisions

Boards and board committees have the appropriate balance of skills, experience, independence and knowledge of the company. Boards identify what customer and stakeholder expertise is needed in the boardroom and how this need is addressed.	This is set out in the Corporate Governance section including how we recruit NEDs to ensure the right balance of skills on page 55.  The Board have updated their assessment of the composition of Board.
Independent non-executive directors are the largest single group on the board.	This is set out in the Corporate Governance section under "Nomination Committee" on page 55.
The chair is independent of management and investors on appointment and demonstrates objective judgement throughout their tenure. There is an explicit division of responsibilities between running the board and executive responsibility for running the business.	This is set out in the Corporate Governance section under "Board of Directors" on page 51.
There is an annual evaluation of the performance of the board. This considers the balance of skills, experience, independence and knowledge, its diversity, how stakeholder needs are addressed and how the overarching objectives are met. The approach is reported in the annual report and any weaknesses are acted on and explained.	The board completes an annual performance evaluation and has set this out under "Board of Directors" on pages 50 and 51.
There is a formal, rigorous and transparent procedure for new appointments which is led by the nomination committee and supports the overarching objective.	This is set out in the section covering the "Nomination Committee" on page 55.
To ensure there is a clear understanding of the responsibilities attached to being a non-executive director in this sector, companies arrange for the proposed, final candidate for new non-executive appointments to the regulated company board to meet Ofwat ahead of a formal appointment being made.	This is set out in the section covering the "Nomination Committee" on page 55.
There is a majority of independent members on the audit, nomination and remuneration committees and the audit and remuneration committees are independently led.	This is set out under "Board Composition" on page 55 and in the sections covering the Audit, Nomination and Remuneration Committees.

## OWNERSHIP STRUCTURE

The following chart shows the ownership of the Company and the Group Structure. All companies are wholly owned by the parent company shown and all companies, with the exception of Southern Region Water Holding Limited (which is Hong Kong tax domiciled) are domiciled in the UK for tax purposes.



### Explanation of Ownership Structure

Portsmouth Water Limited is the primary trading company in the group and is included within the regulatory ring-fence as established by the Instrument of Appointment. The immediate parent of Portsmouth Water is Portsmouth Water Holdings, a company established in 2002 to protect the interest of Bond holders by exercising control over distributions.

Ancala Partners LLP ("Ancala") is a UK based infrastructure fund manager. Its investors are primarily UK corporate and local authority pension plans. The acquisition of South Downs Capital Limited in March 2018 was implemented by a new company, Ancala Fornia Limited, which is incorporated in the UK. The ultimate parent undertaking is Southern Region Water Holding Limited (SRWHL) which is incorporated in the Hong Kong and was set up in 2019. The investors in SRWHL comprise a number of investment vehicles, all focused primarily on UK long-term infrastructure investment and managed by Ancala Partners LLP. Ancala manages approximately £850 million of funds with investment from UK and European pension plans and institutional investors with a long term investment horizon.

We consider SRWHL to be the ultimate holding company and ultimate controlling entity. Consolidated group financial statement for the year ended 31 March 2020 will be prepared at the level of Ancala Fornia Holdco Limited and this will be the largest Group for which consolidated financial statements are prepared.

### Financing

Portsmouth Water Limited is financed primarily by way of an RPI indexed linked loan secured upon the assets of the Company. This thirty year £66.5m index-linked loan was issued in June 2002 and is repayable on 30 September 2032. The loan interest is calculated by adjusting the value of the loan by RPI and then charging interest on this amount at 3.635%. The current value of the loan is £109.7m (2019 - £106.7m).

### Setting Strategy and Objectives

As a monopoly supplier company the Board has constant regard to the moral and statutory responsibility to do the right thing for our customers, our people and our environment. The mission *“To supply high quality drinking water, whilst providing excellent levels of service for our customers, at the lowest price in the country”* is underpinned by relentless focus on customer service achieved through a motivated and committed work force. The Company’s strategic direction is informed by both a medium term, 5 year, view (driven by the regulatory planning cycle) and a longer term position. The regulatory planning cycle is clearly a key element in driving company strategy and performance objectives. In developing our Business Plan, as part of this process, we are closely informed by the view of our customers and our wider stakeholder groups.

As part of development of the PR14 Business Plan the Company established six “outcomes” which are aligned to our Outcome Delivery Incentives (“ODIs”) and many of which are established as Company Key Performance Indicators (KPIs). We also include metrics supporting our financial resilience. We have set out on pages 10 and 11 of our Annual Report and Accounts a summary of how our strategy aligns our Outcomes to KPIs and related risks, together with a summary of how these are delivered. Our measurement and trend of KPI performance is summarised on pages 12 and 13 of the ARA together with a clear indication of our performance.

The Company has completed the PR19 Business Plan, and during the year it received the Final Determination from Ofwat for the period 2020-2025. A significant part of this process related to activity at the Board level - setting the strategy and challenging the level of ambition. This was informed by detailed engagement with customers (including representatives of customer groups) across a wide range of topics and customer demographics. It was also informed by stakeholders such as employees, Ofwat, DEFRA, the EA, the DWI and local environmental groups. As a result of this the Business Outcomes for 2020-2025 were updated to reflect revisions and changes in emphasis within our overall business strategy.

The PR19 strategy leverages the Company’s strong water resources position with plans to deliver increasing volumes of bulk water supply to our neighbouring water company, Southern Water. This will be delivered through an ambitious combination of reduced leakage, lower demand and the development (over 10 years) of the new water resource: Havant Thicket Winter Storage Reservoir. We have committed to a range of stretching service levels to customers including a 20% reduction in leakage, increasing support for vulnerable customers and lower interruptions to water supplies. We will deliver this for lower bills at £106 in today’s prices. Customer acceptance levels of our Business Plan, at 84%, was extremely high.

The Board Governance processes and Board composition allows for a process of robust challenge both in terms of level of ambition and performance. In addition, Company objectives, driven by the strategy, for Executive Directors and Managers are set annually by the Board and linked to executive remuneration (both short and long term). This close linkage between delivering stretching performance for customers and executive remuneration will continue into the PR19 Business Plan.

### Company Performance

Company performance is tracked through a suite of KPIs which are reviewed and discussed monthly both at the Board and Senior Management level. These KPIs are closely aligned to the Business Plan Outcomes and ODIs, together with key financial outturn against the Final Determination. Where common performance metrics are available the Company also has regard to industry-wide performance. A key measure of whether the Company is delivering against its strategy is the position within the Service Incentive Mechanism (“SIM”) and the net promoter score for the Institute of Customer Services. We recognise that to be at the industry frontier in these measures requires constant adaptation and development of our services.

This drive to be an industry leader in customer service requires the Board to have a dynamic approach to managing the business and in setting ongoing strategy and making key business decisions. It also requires a close alignment between company objectives and executive remuneration. Company out-performance has generally been used to invest in service or asset improvement rather than payment to investors. The dividend policy is set out on page 45 of the APR.

As set out in the Annual Report and Accounts the Company has performed very well against its KPIs in the majority of areas during the five years of the AMP. We were also very pleased to be recognised, by Ofwat, as one of only three English water companies considered to be “delivering for customers”.

Totex performance is in line with the Final Determination. Outperformance has been driven by operational efficiencies and in particular, innovative contracting arrangements relating to infrastructure renewals. Over the regulatory period to date the Board has made the decision to reinvest efficiency savings in programmes such as leakage detection, a new ERP system, initial development work for the Havant Thicket Winter Storage reservoir and a number of schemes relating to water quality contact time. In the Board’s views this re-investment will support the Company in continuing to deliver high service levels for customers and in driving further business efficiencies.

Levels of customer satisfaction remain high. We were delighted to continue our sector leading customer service performance, being ranked first overall in the SIM for the 5 year period. The trial results for the new C-MEX measure supported this position with the Company ranked second.

## COMPANY DIRECTION AND PERFORMANCE

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As a member of the Institute of Customer Service we were also proud to hold the prestigious “Service Mark”. We strive to achieve the levels of net promoter scores seen for top performing UK business. Their annual Business Benchmarking survey gave Portsmouth Water a score of 82.7. When compared with their national survey results, where utilities average 72.1 and all sectors average 77.1, we perform strongly. This provides sound, independent evidence of our excellent customer service performance. We continue to develop further service offerings to enhance customer service experience.

For the ODIs that are consistent across water companies, the Company performs well and benchmarks in the upper quartile of the industry. This includes bursts, interruptions, leakage, SIM and water quality contacts. In Ofwat’s review of the industry’s performance, it named Portsmouth Water as one of only three Companies that it considered to be delivering for customers.

We achieved all but two of our Outcome Delivery Incentives (ODI’s) for the year. Unfortunately, we did not meet our ODI targets for Per capita consumption (PCC) or Mean Zonal Compliance (MZC)

PCC measures household water usage which, itself, is heavily influenced by the weather (and in particular summer usage). 2019/20 was generally a normal year in terms of rainfall and the Company fully met customer demand without imposing any restrictions such as hose-pipe bans. PCC was 153.6 l/h/d. Our target is set relative to a “normal” year and our actual performance is heavily influenced by weather.

Unfortunately the Company failed to meet the mean zonal compliance (MZC) measure of water quality. The overall results of this measure were disproportionately impacted by one nickel failure as a result of a new kitchen tap being sampled and a lead failure as a result of lead in the customer side supply pipes. Accordingly we do not feel that this is a fair representation of the Company’s overall performance. We support the development of the new measure of water quality compliance, the Compliance Risk Index, as we feel that the impact of the type of failures experienced will be more accurately reflect the quality of the water delivered to customers.

The company also notes the particularly strong performance in a number of areas and particularly with respect to significant reductions in leakage and strong performance in relation to interruptions to supply and water quality contacts.

We realise that leakage is an important priority for many customers and have invested significantly in leak detection and repair activities over recent years. As a result, we have reduced leakage to 23.6Ml per day in 2019/20 a reduction of 4Ml/d (15%) relative to 2018/19 and outperformed our regulatory target for 2019/20 by over 6 Ml/d. We have installed new technology in our network of over 3,550km mains to help us identify and locate leaks quickly. This has resulted in us now having an industry leading level of leakage at just under 75 litres per property per day. We are well placed to continue this improvement in the next five year period, where we plan to reduce leakage by a further 20%.

Portsmouth water continues to have one of the best levels of performances in the industry for interruptions to supply for customers. At an average of 3 mins 22 per property, this is our best performance in the last five years and is one of the best performances in the industry. Our network has been designed so that water can be quickly fed to customers using different pipes in the event of a burst on their normal supply. This allows us to keep the impact to customers of any burst in our pipes to a minimum. We also consider carefully the impact on customers when we plan essential work. In many cases we provide temporary supplies to customers whilst we undertake work on our network. We continue to explore the use of new technology to make repairs to our network, so that customers are not impacted by any failure.

Water quality contacts is the measure of the number of times that customers contact us with queries connected to water taste, odour, discolouration or illness. This is calculated as the number of contacts per 1,000 population served and reported annually (for the calendar year) to the Drinking Water Inspectorate. We set ourselves an industry leading challenging target of less than 0.412/1,000 population served. We have shown significant improvements in this stretching performance target over the 5 year period. We achieved our target this year, having achieved 0.395/1,000. However, despite this performance we failed to meet the overall target for the average over 5 years. Although our average performance remains upper quartile for the industry.

Finally, performance in relation to key financial metrics is satisfactory and stable. In the Board’s view this supports a business which continues to be financially resilient. The impacts of the COVID-19 pandemic has just begun to be seen as we ended financial year and has increased levels of uncertainty. As a result the Company has undertaken extensive modelling in relation to COVID-19 impacts, taken a range of mitigating measures and made an additional £1.5m provision for potential bad debt at the year-end. More detail in relation to the Company’s response to COVID-19 is set out on pages 35-36 of the ARA. In addition the Viability Statement also reflects considerations of COVID-19 impacts and available mitigations.

On balance the Board’s view is that the Company’s overall performance is delivering for customers and stakeholders and that levels of executive remuneration and investor return are both appropriate and consistent with this level of company performance. Further detailed information on executive remuneration is set out on pages 15 and 16 of the APR and pages 46 to 51 of the ARA. The Company maintains a stable and transparent dividend policy in line with levels of expected notional equity returns.

### **Financial Viability**

The Company’s financial position is set out in the ARA on pages 67 to 87, including cash flows, liquidity position, borrowing facilities and loan maturities. The Strategic Report, on pages 8 to 39 of the ARA, also covers aspects such as the overall financial performance and financial risks. Finally the Viability Statement on pages 40 to 43 of the ARA (and repeated on pages 13-17 below) sets out the factors considered and the conclusions reached by the Board in assessing both the going concern of the business over the period of 12 months from the balance sheet date and the prospects over a longer period of just under 7 years to the end of the next PR19 Business Plan.

**Company's Assurance Process and Outcomes**

The Company set out its approach to data assurance, including assurance over the APR, in its Final Audit Plan which was published on 6 April 2020. We have completed our data assurance in accordance with that plan and will publish a summary of the relevant results in the Data Assurance Summary which will be published in July 2020. The Board and the Audit Committee have considered the results of data assurance processes, together with the Company's proposed response to relevant findings, and are satisfied with the overall outcome.

## VIABILITY STATEMENT

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### 1. Assessment of prospects

The Board has assessed the prospects of the Company over a period of 10 years.

#### Background information

The Company's business model and strategy are central to an understanding of its prospects. Further explanation of the business model and strategy can be found on pages 8 and 9 of the ARA. As a regulated, capital intensive, utility provider the nature of the Company's activities are long-term and, although subject to some regulatory changes, the business model is generally stable. The Company's current overall strategy, budget and cash flow projections are intrinsically linked to the Ofwat 5 year regulatory review cycle. Consequently, the 5 year regulatory Business Plan (which runs from 1 April 2020 to 31 March 2025 and for the Havant Thicket price control for 10 years to 2030) and the related Ofwat Final Determination are the primary drivers for the Company's future prospects. The Final Determination sets out the allowed revenue, operating expenditure, capital expenditure and agreed business Outcomes for the regulatory period. In addition we have extended our assumptions for the core business in order to reflect our estimate of the regulatory outcome (for the core business) for the period 2025-2030. More information in respect of the regulatory regime is set out in pages 30 to 33.

The Company has recently received the Final Determination for the 2020-2025 regulatory Business Plan cycle (for the Havant Thicket price control the period from 2020-2030) and together with an estimate of the regulatory outcome for the period 2025-2030 considers that this represents the best indication of future operating activity and financial results.

The Board continues to take a conservative approach to the Company's strategy. The business' focus is largely on delivering the agreed regulatory Outcomes and out-performing the operating costs set out in the Ofwat Final Determination. Decisions relating to major capital schemes, water quality, resilience of supply and changes to the business strategy are made with a low tolerance for risk. In particular, the Board has considered the changes in the risk profile of the Company in the Business Plan resulting from the lower allowed cost of capital, the development of Havant Thicket reservoir and a more challenging regime of rewards and penalties.

Given the current circumstances of the COVID-19 pandemic and its impact on business operations and the wider economy, the Board has modified its assessment process to consider the COVID-19 impacts in combination with a range of other down-side scenarios.

#### The assessment process of the Company prospects

The Board recognises that the assessment of viability is dependent upon forecasts which, by nature, involves an element of uncertainty.

#### Budget process

The Company's prospects are routinely assessed, primarily, through its budget process and performance against regulatory Outcomes. These are both closely linked to the financial position set out in the Ofwat Final Determination for the core business period to 2025 and Havant Thicket price control to 2030 which drives the key budget assumptions. This has been extended to cover a longer term, 10 year duration.

The budget prepared included;

- Detailed budget analysis by department for the forthcoming (2020/21) financial period.
- Five year analysis to 2025 in line with the Final Determination.
- Cash flow projections to 2025.
- Projection of key financial ratios including those required for banking covenants and to maintain an investment grade credit rating.

It also has regard to committed funding & liquidity positions and future funding requirements.

This assessment process involves an annual review of the budget (including financial projections through to the end of the 2025 regulatory period) and related objectives, led by the CEO and Finance Director, through the Budget Committee and Management Board. All Company departmental heads are involved in this review. A key part of this review is a comparison of the projected total operating and capital expenditure ("Totex") against that set out in the Company's submitted business plan and the Ofwat Final Determination for the 5 year period.

The Board participates fully in the annual process by means of the budget review and approval process, setting annual business objectives and strategy. The annual budget process was completed and approved by the Board during February and March 2020.

The key business assumptions in the budget related to;

- Increase in CPI(H) (which drives tariffs and costs)
- Levels of capital and renewals spend and related efficiency and cost savings
- Levels of capital spend relating to Havant Thicket reservoir and a capital injection to finance this growth in RCV
- Headcount and salary increases
- Interest rates and loan indexation rates
- Levels of operating expenditure out-performance against the final determination and targeted cost savings
- Levels of activity and cost related to delivering key ODI improvements – particularly leakage and PCC.

## VIABILITY STATEMENT

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### COVID-19 impact

We have modified our process of viability assessment in order to consider the impact of the COVID-19 pandemic – both in terms of the operational performance of the business and the wider economic conditions. As a business we have undertaken multiple iterations of scenario analysis considering 3, 6 and 12 months “severe business impact” of the pandemic and we have set out further information relating to our response to the COVID-19 pandemic on pages 35 and 36 of the ARA. The Board has been, and continues to be involved, in the process of assessing the potential impact of COVID-19 on the business. This includes the presentation of detailed board papers, weekly COVID-19 Board meetings and close tracking of the actual outcomes versus modelled scenarios. The Board will continue to carefully monitor the effects and to refine its assessment of the overall impact. However, it should be recognised that there remains an inherent level of uncertainty relating to the COVID-19 situation.

Accordingly, we have considered, as a first step of this viability assessment, a 6 month severe COVID-19 business impact. The Board has assessed that the 6 month severe COVID-19 impact represents the best estimate of the likely outcome at this time. This has been completed initially on an unmitigated basis and then mitigating actions applied. We have then considered a further 12 month severe but plausible COVID-19 scenario. All additional viability scenarios were performed in combination with the post mitigation 6 month COVID-19 scenario.

The material down-side assumptions used in the 6 month COVID-19 scenario include;

- Reduction in non-household revenue as a result of lower consumption and void properties
- Reduction in non-household cash collection as a result of the above together with extended credit terms
- Reduction in household cash collection and resultant bad debts due to economic conditions
- Additional operating costs including cover for illness

The significant mitigating actions applied include;

- Deferral and restriction of dividends
- Restriction of capital expenditure
- Restriction of infrastructure renewals expenditure
- Headcount freeze
- Deferral of management salaries and bonuses
- Regulatory mechanisms permitting the recovery of revenue in later periods
- Furloughing of some employees
- Utilisation of revolving credit facility up to the current level of £25m

### Risk assessment

The Company updates the analysis of significant risks that could prevent the budget and Outcomes from being delivered. The Board performs regular reviews of the principal risks and uncertainties and a formal annual review and a robust assessment was completed and updated in April 2020. As part of the Business Plan process the Company performed an assessment of “resilience in the round” building from an understanding of operational risks through financial resilience and with regard to overall company resilience including governance and management effectiveness.

The overall summary of the principal risks and uncertainties (set out on pages 30 to 31) reflects this consideration of “resilience in the round”. Details of the Board risk assessment process are set out on page 43. The purpose of the principal risks table is, primarily, to summarise those matters that could prevent the Company from delivering on its strategy. A number of other aspects of the principal risks;

- because of their nature or potential impact
- could also threaten the Company’s ability to continue in business in its current form if they were to occur. This was considered as part of the assessment of the Company’s viability, as explained further below.

In setting out specific scenarios for the Viability Statement we have reviewed the risk register together with resilience modelling prepared as part of the PR19 Business Plan and considered the impact of the current COVID-19 pandemic.

Using this information we have developed a range of relevant severe, plausible and reasonable business scenarios which have been linked to the relevant business risks. These were reviewed and approved by the Board and are summarized in section 2 below.

### The period of assessment

The Board conducted the assessment for a period of 10 years to 31 March 2030. The Board considers that this period of 10 years to be most appropriate given the current stage of the regulatory review cycle, the longer term nature of the business and the new 10 year Havant Thicket price control. This period covers; for the “core business” the 5 years of the next regulatory period and an assessment of the results for the successive regulatory period; and for the Havant Thicket price control the 10 years to the end of the price control. This is consistent with the timing of the regulatory review cycle and an expectation that, for the subsequent regulatory period, Ofwat’s methodology will not be significantly changed. This is also consistent with Ofwat’s guidance relating to the period of assessment.

The Board feels that this is an appropriate length of time to permit a reasonable assessment of likely business performance and to make reasonable estimates of key assumptions. As set out above, the Ofwat Final Determination, the Business Plan, the delivery of Havant Thicket reservoir and the related Outcomes are significant drivers of the business strategy & performance. In addition the Board has considered the impact of the COVID-19 pandemic. These are key drivers to the end of the next regulatory period and beyond to 2030.

## VIABILITY STATEMENT

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### 2. Assessment of viability

The Assessment of Viability therefore uses; for the “core business” a period of 5 years of regulatory business plan to 2025 and a further 5 years of projection to 2030; and for the Havant Thicket price control a period of 10 years of the regulatory business plan to 2030. Although these results reflect the Directors’ best estimate of the future prospects of the business, they have also stress tested the potential impact on the Company of a number of scenarios. This has been performed by quantifying their financial impact and overlaying this on the financial forecasts. The potential impact has been considered in relation to operating profit, cash flow, liquidity and the key financial ratios needed for banking covenants and the retention of an investment grade credit rating (such as gearing, net debt:RCV and interest cover). These scenarios (which are summarised on pages 42 and 43), have been driven from the Boards assessment of the impact of COVID-19 and of “resilience in the round” (and are reflected in the principal risks and uncertainties set out in pages 38 to 39). These scenarios represent ‘severe, plausible and reasonable’ circumstances that the Company could experience. As noted above we have undertaken a two-step process first assessing the impact of a severe 6 month COVID-19 scenario and then overlaying this with further severe but plausible downside scenarios.

In addition the Directors also tested a number of broad sensitivities including increase in interest rates and adverse movements in Retail Price Index/Consumer Price Index. In each case the availability and effectiveness of mitigating actions that could reasonably be taken to reduce the impact was taken into account. The primary mitigating actions relate to the use of available credit facilities, levels of insurance cover, the ability to defer capital and renewals spend and the discretion not to pay dividends.

It has also been assumed that adverse impacts, which may have an adverse but short lived (1 year) effect on financial ratios, could be managed by careful discussion with key stakeholders such as bond holders and the rating agencies.

The results of this stress testing showed that, due to the stability of the business, the Company would be able to withstand the impact of these scenarios occurring over the period of the financial forecasts by making adjustments to its operating plans within the normal course of business. This included both the restriction and elimination of dividend payments.

### 3. Viability statement

Based on their assessment of prospects and viability above, the Directors confirm that they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the ten years ending 31 March 2030.

### 4. Going concern

The Directors have carefully considered the going concern basis of the Annual Performance Report. Notwithstanding net current liabilities of £12,816,000 as at 31 March 2020 and a loss for the year then ended of £3,326,000, the regulatory accounting statements have been prepared on a going concern basis which the Directors consider to be appropriate for the following reasons.

The Directors have prepared cash flow forecasts for a period of 12 months from the date of approval of these regulatory accounting statements which indicate that, taking account of reasonably possible downsides, including the impact of COVID-19, the Company will have sufficient funds through cash balances, operating cash flow and its’ RCF facility to meet its liabilities as they fall due for that period.

Our base case forecast assumes that, in line with the Business Plan assumptions, we will receive an additional capital injection of up to £32m in March 2021 to fund growth in the Regulatory Capital Value due to HTWSR. Our investors, Ancala, have indicated that they have the intent (and the means) to provide this capital. Were this injection not to be received the HTWSR project would be paused and other funding options pursued. This would not impact the going concern of the Company and the base case and downsides have been modelled with and without the HTWSR project.

The full impact of the COVID-19 pandemic remains uncertain at this time and our key priorities are the continued supply of our essential services and the health of our employees, customers and other business partners. Accordingly, the Directors have reviewed the COVID-19 situation and have modelled a series of ‘downside’ scenarios of varying duration and severity. A 12 month COVID-19 downside scenario was considered to be “severe but plausible” and include assumptions relating to the estimates of the impact of: reduced revenue from non-household customers and reduced cash flow from both non-household and household customers together with the operational impacts on both operating costs and capital spend. Further information relating to our business response to COVID-19 is included on pages 35 to 36 of the ARA. Further longer term scenarios have also been set out in the Viability Statement. In the severe but plausible downside scenario the Company remains financially viable following mitigating actions which include; deferral of management bonuses and dividends, reduction in capital expenditure and infrastructure renewals activities and furlough of employees. The Directors consider that these mitigating actions are all within the control of the business.

In conclusion, the Directors, after reviewing the Company’s operating budgets, investment plans and financing arrangements, consider that the Company will have sufficient funds available, to allow the Company to continue to meet its liabilities as they fall due, for a period of at least 12 months from the date of approval of the regulatory accounting statements. Accordingly, the Directors are satisfied that it is appropriate to prepare the financial statements on a going concern basis.

## VIABILITY STATEMENT

Set out below are summaries of the results of the financial sensitivity analysis performed in support of the Viability Statement. The first table summarises the impact of "step one" of the COVID-19 6 month scenario upon the Company's original budget (both unmitigated and mitigated). The Directors consider that a 6 month impact represents a reasonable assessment of the most likely impact on the business. It should be noted that significant additional mitigating actions were included in our COVID-19 mitigation modelling. This is in order to provide sufficient headroom to withstand the high levels of uncertainty relating to the duration and severity of the pandemic.

COVID-19 INITIAL IMPACT				
	Gearing	Artesian Interest Cover Ratio	Moody's Interest Cover Ratio	S&P FFO/Net debt
<b>Targets</b>				
AMP 7 Average	60.00%	1.40	1.50	7.00%
AMP 8 Average	70.00%	1.40	1.50	7.00%
<b>Budget before the impacts of COVID</b>				
AMP 7 Average	49.85%	1.65	1.99	9.30%
AMP 8 Average	62.22%	1.97	2.21	7.39%
<b>Budget including the 6 month impacts of COVID (unmitigated)</b>				
AMP 7 Average	50.71%	1.87	1.94	9.20%
AMP 8 Average	62.22%	1.97	2.21	7.39%
<b>Budget including the 6 month impacts of COVID (mitigated)</b>				
AMP 7 Average	48.51%	1.97	1.99	9.89%
AMP 8 Average	62.22%	1.97	2.21	7.39%

## SUMMARY OF RESULTS

Individual Scenario	Impact (pre mitigation)	Mitigation	Opex	Capex	Loan	Capital	Other
<b>STEP ONE - COVID-19 SCENARIOS</b>							
COVID 6 month	FY21 EBITDA £2.5m lower & cash generated from operations £2.9m lower, due to lower non-household consumption and lower cash collections across household and non-household.  Unmitigated, Artesian ratio Moody's ICR and S&P FFO/Net Debt all fall below target in FY21.	Mitigating actions are made in FY21 - EBITDA saving, deferral of capital spend and deferral of dividends being the most significant. These are effective in mitigating the impact on ratios entirely. No further mitigation is needed for FY22 onwards as there is sufficient headroom in the financial ratios.	✓	✓	✓		✓
COVID 12 months	FY21 EBITDA £4m lower & cash generated from operations £5.5m lower, due to lower non-household consumption and lower cash collections across household and non-household.  Unmitigated, Artesian ratio Moody's ICR and S&P FFO/Net Debt all fall below target in FY21.	Mitigating actions are made in FY21 - EBITDA savings, reduction in Capex programme and reduction in dividends being the most significant. These are effective in mitigating the impact on ratios entirely. No further mitigation is needed for FY22 onwards as there is sufficient headroom in the financial ratios.	✓	✓	✓		✓

Following this assessment of the COVID-19 6 month impact and related mitigation we have, at step 2, overlaid further longer term "severe but plausible" scenarios (including combined scenarios) and summarise the results on the following page. It should be noted that in all scenarios the impact is considered to be mitigated in full by employing measures which are both reasonable and wholly within the control of management. These include additional borrowings, within the headroom of the current revolving credit facility, deferring the timing of capital expenditure and reducing operating expenditure, for example through a temporary reduction in infrastructure renewals.

## VIABILITY STATEMENT

### SUMMARY OF RESULTS

Individual Scenario	Impact (pre mitigation)	Mitigation			
<b>STEP TWO - Additional scenarios overlaid onto COVID-19 post mitigation scenario</b>					
Major NHH retailer defaults	<p>Following the change to extend additional credit to retailers the greatest potential exposure is in May 20. Assume retail default at this time resulting in gross exposure of £1.2m. Under-recovered revenue is assumed to be recovered in FY23. The initial impact is not reduced by the regulatory cap on exposure to NHH default.</p> <p>The impact of this is that the Moody's ICR ratio falls below target to 1.15x in FY21 and adverse cash flow requires additional borrowing in year. All other ratios remain above the target for all years.</p>	A £1.5m reduction in Opex would be required in FY21 together with additional in year borrowing to manage cash flow and mitigate impact on ratios.	✓	✓	
Household bad debt costs substantially increased due to socio economic factors relating to COVID-19	<p>Assumption that the bad debt cost projected in the COVID-19 scenario is insufficient and the impact of COVID on customer's paying bills extends beyond FY21. This scenario models a nominal increase of £950k over the AMP-phased £250k, £300k, £200k, £100k and £100k for FY21 - FY25 respectively.</p> <p>The impact of this is that the Moody's ICR falls below target in FY21 (1.43x). All other ratios remain above target for all periods.</p>	To mitigate, a £200k opex saving would be required in FY21.	✓		
Multiple ODI failures resulting in penalty - 3% of RoRE in Y3	<p>Assumed 3% RoRE ODI penalty based upon FY21 performance, amounting to £1.5m downward revenue penalty applied in FY23. EBITDA and cash both £1.5m lower in the year.</p> <p>The impact of this is that the Artesian ICR falls below target in FY23, to 1.16x. All other ratios remain above target for the duration.</p>	£1.5m additional drawdown on Revolving Credit Facility in FY23- repaid in FY25. This is within the authorized limit.			✓
RPI and CPI lower by 2%/1% respectively	With CPI at 1% EBITDA reduced by £0.7m over AMP7 and an additional £1.3m in AMP8. This is somewhat offset by lower indexation on the Artesian loan (reducing interest charges). This improvement in the interest charge (£1.7m over both AMPs) mitigates to some degree impact on interest cover ratios. By the end of AMP8 cash is £1.3m lower. None of the ratios fall below target.	No mitigation required.			
50bps reduction in WACC in AMP8	<p>Revenue decline of £5.1m in AMP8, ending the AMP with £4.7m less cash.</p> <p>The impact of this is that the S&amp;P FFO/Net Debt ratio falls below target from FY27 to FY30, falling by c0.6%.</p>	Over AMP8 would need to reduce Opex by £4m to meet target S&P FFO/Net Debt ratio. This equates to £1m per year from FY27. There may be some savings in interest costs where new debt is raised.	✓		
Loss of Company specific premium in AMP8	<p>Loss of the Company Specific Premium (0.30% on the cost of debt) in AMP8 would reduce revenue by £300k-£400k per annum (£1.8m over the whole AMP).</p> <p>The impact of this is that the S&amp;P FFO/Net Debt ratio falls below target from FY27 to FY30, falling c0.2% in each of these years, taking the ratio just below the 7% target.</p>	Opex savings of £1.1m would be required in AMP8.	✓		
Pension deficit of £2m through £250k increase in annual contribution	Deficit is recovered through an increase in contributions of £250k per annum. At the end of AMP7 cash is £1.4m lower rising to £2m lower by the end of AMP8. This scenario impacts both the Moody's ICR and the S&P FFO/Net Debt ratios. The Moody's ICR is falls to 1.42x and the S&P FFO/Net Debt falls marginally below target in FY27 & FY28.	Impact in AMP7 can be managed by reprofiling spend and borrowing an additional £0.5m on the RCF in FY23. A total of £400k opex saving required in AMP8.	✓	✓	
HTWSR delay in project increased costs	<p>Assumption of an initial 12 mth delay in the HTWSR project. Additional spend needed to meet commissioning date totaling £5.2m, incurred from mid-way through FY23. This represents a P90 scenario.</p> <p>This results in fall of the Artesian ICR in FY24, with coverage at 1.26x (a decline of 0.23x from Covid Base Case) resulting in a dividend lock up without mitigation (but not breached). The S&amp;P FFO/Net Debt ratio falls marginally below 7% FY27 to FY30.</p>	Fully mitigated through additional draw down on the RCF of £1m in FY24. £250k of opex saving required in FY28 to meet the S&P FFO/Net Debt target level.	✓	✓	
Cost of debt increases 50bps - impact to new debt raise in AMP8	<p>£99.5m of new debt is forecasted to be raised in AMP8. An increase of 50bps on the cost of debt raised in AMP8 increases interest costs by £205k in FY26, rising to £498k in FY30 (£2m over the whole of AMP8). Cash at the end of AMP8 is £1.9m lower.</p> <p>The S&amp;P FFO/Net Debt ratio falls below target in FY27 to FY30, having declined by c0.25%.</p>	Opex savings (in nominal terms) would need to be achieved in AMP8 to offset the increased cost of borrowing. This would need to amount to £1.1m over AMP8.	✓		
<b>COMBINED SCENARIOS</b>					
Pension deficit combined with ODI failure	<p>£1.5m ODI penalty applied to revenue in FY23 based upon FY21 failure, together with additional £250k (nominal) per annum cost to recover the pension deficit.</p> <p>Moody's ICR falls in FY21 and FY23 (declining 0.13x and 0.81x to 1.42x and 1.46x respectively). The Artesian ratio falls to 1.10x in FY23. S&amp;P FFO/Net debt target ratio is not met in FY27 to FY30.</p>	Total Opex savings of £0.8m over the two AMPs, additional £1.5m drawdown on the debt facility in FY23 and £0.5m in FY24 are required.	✓	✓	
Combination of NHH retailer default, increase in household bad debt costs and ODI failure as set out above.	The net impact of these scenarios are that the Moody's ICR is failed in FY21, falling to 1.09x, the Artesian ratio marginally fails in FY23 1.39x and the S&P FFO/Net Debt ratio fails in FY28 at 6.98%.	Opex saving of £1.8m are needed in FY21 to ensure compliance with the Moody's ICR. Headroom in FY23 ratio means that these costs can be deferred from FY21 to FY23. Additional £2m drawdown on the credit facility in FY23 (repaid in full in FY25). £100k (nominal) opex saving in FY28 required.	✓	✓	

### **Corporate Structure**

The Group structure in which the Company resides, has recently changed and is set out on page 9 of the APR. The Group is wholly owned by funds managed by Ancala Partners LLP ("Ancala") through a Hong Kong domiciled holding company Southern Region Water Holdings Limited. Ancala Partner LLP the ultimate owner of the group is a UK based and domiciled independent infrastructure fund manager.

Portsmouth Water is committed to full compliance with UK tax laws. As a Company we understand that collecting and paying tax is an important part of contributing to the economic environment that we operate in and in addition to paying corporation tax we also contribute as a result of indirect taxes, employee related taxes and environmental taxes. The Company's tax affairs are managed in a way which takes into account the wider corporate reputation. At all times the tax affairs are managed in line with the Company mission statement of Integrity, Excellence and Respect.

### **Governance in relation to UK taxation**

- The ultimate responsibility for the tax strategy of Portsmouth Water Limited sits with the Board.
- The Finance and Regulation Director is the Board member with executive responsibility for tax matters.
- The day-to-day management of the tax affairs is delegated to the Financial Controller who reports to the Finance and Regulation Director.
- Members of the Finance team are trained to a level that ensures tax compliance and a continuous cycle of training occurs to ensure all skills are relevant and up to date.
- For tax filing, specialist advice and support Portsmouth Water engage the services of specialist Finance and Accountancy professionals.

### **Risk Management**

#### **Attitude towards tax planning and level of risk**

Portsmouth Water Limited manages risks to ensure compliance with legal requirements in a manner which ensures payment of the correct amount of tax.

Portsmouth Water's attitude towards tax planning is one of prudence; seeking to comply fully with relevant tax legislation and to achieve a high degree of certainty in the company's tax affairs. The wider group of Companies applies the same approach to tax planning as a whole.

At all times Portsmouth Water seeks to act in a way which upholds its reputation as a good corporate citizen.

For any specific issue or transaction the Board is ultimately responsible for identifying the risks, including tax risks, which need to be addressed and for determining what actions should be taken to manage those risks. In doing so the Board has regard to the materiality of the amounts and where specific risks occur the Company will seek specialist professional advice.

In line with the Company's ethos to strive for continuous improvement through innovation we are able to utilise government tax initiatives such as the R&D Tax Credits scheme to reduce our corporation tax charge and therefore continue to maintain one of the lowest costs to serve in the industry.

### **Working with HMRC**

Portsmouth Water seeks to have a transparent, respectful and proactive relationship with HMRC at all times, be that directly or through intermediaries acting on our behalf.

Any inadvertent errors that may occur in any submission made to HMRC are fully disclosed as soon as reasonably practicable after they are identified and independent specialist advisors are commissioned to validate the value of any error. Following this, an internal review will then identify any required process changes of internal controls, to ensure full and ongoing compliance.

Future tax changes are considered through Water UK's Tax Forum, of which Portsmouth Water is a member. This group allows us the opportunity to discuss how future tax legislation should be interpreted and applied to the Water Industry.

### **Corporate Criminal Offences Code of Conduct**

Tax evasion, tax fraud and attempts to facilitate such actions are unethical and inconsistent with the ethos of Portsmouth Water. Portsmouth Water is committed to complying in full with the UK tax laws, and we expect everyone working with the Company to fully comply with their tax obligations. We believe in paying our fair share, and that everyone working with us should too. This extends to recent but now delayed changes in IR35 legislation within the private sector.

### **Accountability & Governance**

The board of our Company has approved a code of conduct policy and supports our commitment to a zero tolerance of tax evasion or its facilitation. The Finance and Regulation director is responsible for monitoring compliance with the policy and is supported by the Board and the management team in doing so.

### **Employee responsibilities**

Our code of conduct sets the standards of behaviour we expect all employees to adhere to and if employees are ever asked to act in any way that could facilitate tax evasion, this must be reported without delay. This is formalised through our whistleblowing policy.

### **Risk assessment and mitigating factors**

Our business risk assessment covers those areas of business operation where there is a risk of tax evasion. In relation to these risks we have considered relevant mitigating factors (including internal controls). Where necessary we have developed further activities and controls to mitigate areas of exposure.

### **Our commitment**

Portsmouth Water is committed to the following principles:

- Our business is carried out fairly, honestly, and openly in every part of our work.
- Our values inform everything we do.
- We will never transact with any supplier where it is known or suspected that any aspect of the transaction is being misused, abused or otherwise corrupted for the purposes of tax evasion.
- We will immediately terminate any agreement or business relationship if we learn of or suspect tax evasion may be taking place.
- We will not do business with others who do not also hold to at least the same standard of preventing tax evasion.
- Any employee found in breach of our policy will be subject to disciplinary action.
- No employee will suffer demotion, penalty, or any other adverse action for reporting or from refusing to carry out an action which may lead to tax evasion.

## REPORT ON REMUNERATION

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### Remuneration Committee

#### Role of Committee

The primary objective of the Committee is to set a policy to ensure that competitive reward packages are offered that will attract, retain and motivate talented senior executives to run the business effectively and to promote the success of the Company for the benefit of customers, the environment and stakeholders.

We align executive pay to stretching delivery targets ensuring we deliver real value through high quality customer service and operational performance, whilst ensuring we provide the cheapest water in the country through incentivising financial efficiencies.

Within these arrangements, a proportion of reward is based on performance against demanding targets. These targets are set by the Committee based on key strategic priorities benefiting customers, investors and other stakeholders and consistent with a Board approved level of risk.

At the beginning of the year the Committee assessed previous bonus targets with the rest of the industry and with the intention of ensuring the targets were structured to align motivational rewards with structuring targets that will drive forward the business for the benefit of both customers and stakeholders. As a result of this review the annual targets were increased to offer a maximum reward of 51% of base salary.

The Committee will shortly be completing work on setting the LTIP to cover the next five year AMP period. This will continue to incentivise the delivery of long term sustainable performance for customers and stakeholders. This new LTIP will be fully detailed in this 2021 Annual Report.

#### Activities during the Year

During the year the Committee dealt with the following matters:

- Annual executive salary review and achievement of performance targets
- Determining performance targets in respect of 2019/20 annual incentive bonus plan, and increasing the potential rewards to reflect the industry norm.
- Preparing the Executive Bonus Framework for AMP7, aligning Remuneration to the key strategic objectives and stakeholder priorities
- Taking ongoing responsibility for the approval and changes in Managers' salaries as well as assessing ongoing staff bonus payments

### Remuneration Report

#### Remuneration Policy

The objective is to attract, retain and motivate high calibre Senior Executives through pay arrangements which are competitive and fair and reasonable for the responsibilities involved. In addition to individual performance, reference is made to pay levels in companies of similar size, within the same or relevant other industries.

The remuneration packages of the Executive Directors, as reported in the accounts, includes a performance related element. The performance related element is based upon the achievement of agreed financial, customer service and personal targets for the whole of the previous year.

#### Service Contracts

All Executive Directors appointed to the Board are employed on service contracts of no fixed term with a notice period of one year, both by the Company and the Director. Both Executive Directors are entitled to pension provision and certain contractual benefits, details of which are summarised in the ARA. Each Executive Director also participates in bonus or incentive arrangements at the sole discretion of the Remuneration Committee which are also described later in this Report. All Executive Directors are subject to retirement by re-election at the AGM.

Mr. C. R. Taylor serves as a Director for the Institute of Water, an organisation that supports the development of professionals in the water industry. He is also a Director of Water UK, the industry trade association.

Mrs. H. M. G. Orton serves as a Non-Executive Director for UKWIR, an organisation set up by the 20 water and sewerage undertakers in England, Wales, Scotland, Northern Ireland and the Republic of Ireland to identify and provide research requirements to meet the industry's business needs.

The Chairman and other Non-Executive Directors have service contracts but these can be terminated without compensation. All Non-Executive Directors are subject to re-election at the AGM.

For full details of the Remuneration Report, including details of actual performance and amounts paid, see pages 56-61 of the ARA.

### Link between Directors' Remuneration and Standards of Performance

The Company, through the oversight of the Remuneration Committee, seeks to demonstrate a transparent linkage between the discretionary elements of remuneration and standards of business performance. In particular this has a clear linkage to those areas of company performance which customers value, through close alignment with the targets set for Company Outcomes and Business Plan objectives.

## REPORT ON REMUNERATION

The bonus package for Executive Directors is based on an annual and a long term element (the latter of which is aligned to Company performance over the AMP). Annual Company-wide objectives are set by the Board aligning to the strategic and operational priorities of the business. These have regard to a range of priorities relevant to different stakeholders with particular emphasis on all elements of Customer Service performance.

The long term element of the bonus scheme is linked directly to the Company's performance in relation to key strategic outcomes for each of the 5 years of the AMP, together with other strategic business objectives. Whilst this is accrued annually it is awarded at the end of the AMP, determined by overall levels of performance throughout the regulatory period.

By implementing the short and long-term elements of discretionary Executive remuneration the Board and the Remuneration Committee believes that there is appropriate balance between delivering the Outcomes for the AMP together with the flexibility to deliver any particular areas of business strategic focus. This permits a dynamic element of the approach to discretionary remuneration. The executive incentive plan has been in operation in the business since 2010 and the overall objectives are reviewed on a quinquennial basis in line with the business planning cycle. The elements of the bonus structure are summarised below.

### Annual Incentive Scheme – maximum 51% of base salary award

Maximum Percentage Award	Measure	Finance & regulation Director	CEO
Up to 17%	Business Outcomes	Corporate control environment, budgetary process, customer service, TOTEX level	Water Quality, Leakage, Customer service, TOTEX levels.
Up to 34%	Programme delivery	Capital programme, HTWSR programme, Business Plan conclusion, banking covenants, customer debt level, social contract, financing strategy, customer engagement strategy	Capital programme, HTWSR programme, Business Plan conclusion, banking covenants, customer debt level, social contract, long term efficiency improvements, financing strategy, customer engagement strategy

The annual incentive award is further modified if any RIDDOR health and safety events arise during the year as follows:

Number of RIDDOR events	Retained bonus
0	100%
1	80%
2	60%
3	25%
4+	0%

### Long term Incentive Scheme (5 years aligned to AMP)

Maximum 10% award based on a range of strategic objectives including; consistent SIM performance, staff engagement and culture, leakage, PCC and financial resilience.

### Analysis of incentive award by nature

The following summarises the maximum incentive award by nature. This demonstrates both alignment to the overall business strategy and a balance of the award across a range of relevant measures.

	Annual	Long term
Customer service related	16%	3.5%
Corporate strategy & control	7%	
Totex performance & efficiency	9%	
Financial resilience & control	12%	2%
Capital programme including HTWSR	7%	
Combined ODI performance		4.5%
<b>Total</b>	<b>51%</b>	<b>10%</b>

## REPORT ON REMUNERATION

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### **Determination of performance**

The majority of the executive bonus scheme is linked to clearly defined performance metrics, the majority of which are ODIs. These are subject to external audit as part of the APR and other regulatory reporting processes. The assurance processes are also set out in detail in the “Company Monitoring Framework”, which is subject to annual review and consultation and published annually on the Company’s website. Other performance metrics, such as credit rating, are unambiguous measures.

When personal objectives are set these follow the SMART approach for objective setting (Specific, Measureable, Achievable, Realistic and Time limited). As part of the Remuneration Committee’s review these are challenged and agreed at the start of the objective setting process and supporting evidence is sought at the end of the assessment period before an award is made. In this way the Board has confidence that the performance can be objectively assessed.

### **Summary of Directors’ remuneration**

A detailed report on Director’s remuneration, including the operation of the incentive bonus scheme is set out in detail on pages 58 to 61 of the ARA.

## DIRECTORS STATEMENTS AND RESPONSIBILITIES

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### Statement of Directors' Responsibilities

The Directors are responsible for preparing the Annual Performance Report and the financial statements in accordance with applicable law and regulations.

The Directors responsibilities are in accordance with the requirements;

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 by the Secretary of State for the Environment, Food and Rural Affairs (Defra) and as a water undertaker under the Water Industry Act 1991; Regulatory Accounting Guidelines issued by Ofwat.

In preparing these accounting statements, the Directors are required to:

- select suitable accounting policies 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; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business

The Directors are also responsible for:

- keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 2006 and Condition F.
- safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities; and
- the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

We confirm that to the best of our knowledge that the accounts are prepared in accordance with the applicable set of accounting standards and give a true and fair view of the assets, liabilities, financial position and profit of the Company.

### Confirmation of disclosure of information to auditors

In so far as the Directors are aware:

- there is no relevant audit information of which the Company's auditors are unaware; and
- the Directors have taken all steps that they ought to have taken as directors to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

### Statement of Compliance with Licence Condition P – ring-fencing

In accordance with the provisions of Condition P of the Licence we hereby present a Ring-fencing Certificate. This certificate confirms that, in the opinion of the Board of Portsmouth Water Limited:

- (a) Portsmouth Water Limited will have available to it sufficient financial resources and facilities to enable it to carry out the Regulated Activities, for at least the next twelve months
- (b) Portsmouth Water Limited will have available to it sufficient management resources and systems of planning and internal control to enable it to carry out the Regulated Activities, for at least the next twelve months; and
- (c) all contracts entered into between Portsmouth Water and any Associated Company include the necessary provisions and requirements in respect of the standard of service to be supplied to the Appointee, to ensure that it is able to carry out the Regulated Activities.

In providing this Ring-fencing Certificate, the Board of Portsmouth Water has taken into account the factors set out in the following table. In the opinion of the Board of Directors they have carried out a robust assessment of these factors and have summarised the matters that they have considered below.

## DIRECTORS STATEMENTS AND RESPONSIBILITIES

Factors	Summary of Board considerations
<b>Financial resources and facilities</b>	
Financial Position	A detailed review and consideration of the year-end financial statements with particular attention to available cash and short term facilities. Consideration of the Company's investor report including forecast headroom in relation to key financial ratios. A process of robust challenge and review of budgets prior to Board approval. With further approval of budget modifications made to reflect the impact of COVID-19 impacts are explained further below. Plans to support the business with additional capital are explained further below.
Performance against PR14 Final Determination	Routine Board reporting of key PR14 delivery metrics, including TOTEX outturn and Outcome Delivery Incentives. Board attendance at CCG meetings considers external challenge. Overall the Board concluded that the Company has delivered key PR14 promises to customers.
Credit related factors	The Board approved the company's "Investor Report" including headroom against financial covenants and key financial ratios at both 31 March 2020 and as forecast for the next 5 years. The company has maintained investment grade credit rating. The Board approved the extension of the Revolving Credit Facility to £25m in May 2020 and further considered liquidity headroom as part of the COVID-19 assessment (set out further below).
Business plans & long-term viability statements.	Board approval of PR19 Business Plan, acceptance of the Final Determination and approval of management plans & budgets to deliver the Plan. The significant Havant Thicket Winter Storage Reservoir project (HTWSR) is consider further below. Extensive analysis of, and evidence supporting, Going Concern and the Viability Statement was presented to the Board, reviewed and approved. This included detailed assessment of the impact of COVID-19 as set out further below.
Any relevant reports – internal or third-party.	All relevant internal and external reports are reviewed by the Board. Of particular interest was the report by the Company's financial auditors (KPMG) and the report on key non-financial information by the Reporter (Jacobs). The Board challenges management as to the outcome of those reports and tracks performance against any recommendations. The non-executive Directors also met privately with the financial auditors. Reports by credit rating agencies are reviewed by the Board.
<b>Management Resources</b>	
Management skills, experience and relevant qualifications. Recruitment process, staff engagement	The Board undertakes an annual assessment of the mix of skills across its members and takes action to respond to any significant gaps identified. The Board, through the Executive Directors and senior leadership team, assess the skill, experience and performance of employees. The Board receives periodic reports and updates on employee training & development and reviews the results of employee engagement surveys – challenging findings and reviewing any plans to address concerns. The Board formally reviews the minutes of the Executive Directors' meetings with trade unions (the joint information and communication committee & the joint negotiation committee).
Succession planning for key management/staff;	The Board has reviewed management papers and plans in relation to succession planning. It has also considered the Board's assessment of its own skills mix and taken actions to ensure that the appropriate balance of skills is retained.
Quality of management/staff induction and other training and development;	The Board, through the Executive Directors and senior leadership team, has oversight of employee induction and training activities. The Executive Directors are represented on all staff induction sessions.
Process for ensuring diversity of perspectives;	The Board challenges the Executive Directors and senior leadership team to ensure appropriate breadth of thinking and perspective. This includes engagement with wider stakeholder groups and supporting initiatives, such as the Young Person's Board (YPB), which support and encourage a diversity of thinking. The Board met with the YBP during the year and regularly has direct contact with other stakeholder groups such as Regulators and the CCG. The Board, through the Nomination Committee, is responsible for ensuring that the Company policies an Equal Opportunities, including diversity and inclusion are adhered to across the business.
Board or management activities, reports or statements;	There is a transparent process of both routine management reporting and reporting on specific matters to the Board. The Board meets monthly and actively considers and challenges management reports and related information. The Board is content that it has access to and has considered all relevant management reports.
Independence of Board.	As part of the Annual Report and Accounts and Annual Performance Report the Board has considered independence and confirmed that the Board remains independent.
<b>Systems of planning and internal control</b>	

## DIRECTORS STATEMENTS AND RESPONSIBILITIES

Governance procedures; risk management frameworks, oversight procedures. Internal and/or external audit policies, processes, activities and/or reports.	The Board has considered the Company's robust framework of governance, risk management and control. They consider the Company's risk register and discuss emerging & retiring risks. The Board also reviews and tracks the outcomes of external assurance (financial and non-financial) and considers, annually, the need for an internal audit function. Following the implementation of the revised Ofwat leadership, transparency and governance guidelines the Board considered papers covering the Company's approach and prepared a summary of enhanced reporting included in the Annual Report & Accounts.
Systems for maintaining supply/business continuity, stated action plans.	The Board periodically considers the Company's business continuity/disaster recovery framework. It also receives reports of any significant operational issues arising and considers the effectiveness of Company response and lessons learned. During the year the Board has particularly considered the impact of a large burst main on Hayling Island and the COVID-19 response. The Board undertook reviews of the Company's approach to IT and Operational Technology cyber security risks, including assessment of the results of third party reviews.
Policies to prevent fraud and other unethical behaviour; whistleblowing policy;	The Company has clear policies on behaviour, values and fraud - these are revised periodically by the Board. The Company also operates key systems of internal control designed to prevent and detect fraud and the Board carefully reviews any internal control recommendations made by the external auditors or failings identified through operational reports. The Whistleblowing Policy was reviewed and updated by the board during the year and a refresher campaign run with employees to reinforce the operation of the policy and lines of reporting. The Board considers that it leads from the top in terms of reinforcing the Business' ethics and values.
Risk, compliance other assurance statements	The Board reviews and approves the Company's risk compliance statement as part of the approval of the Annual Performance Report. As noted above the Board leads the process of assessing and managing risk. The Board, through the Audit Committee, assesses the requirements, appropriateness and outcome of formal assurance processes particularly the approval of the Annual report & Accounts and the Annual Performance Report.
<b>Rights and resources other than financial resources</b>	
Corporate missions and/or values.	The Board performs an annual review of the Company's vision, mission and values. During the year the Board formally review and updated the Company Purpose and as a result made revisions to formally reflect the importance of "communities" in the Company Purpose. The Board and the senior leadership team place great emphasis on operating at all times in line with the Company's values and promotes this throughout the business, monitoring performance and addressing behaviours not felt to be in line with these values. The Board has confirmed that both the Board evaluation and employee survey strongly support the view that the Company, at all times, operates within its values.
Technology and other systems for ensuring checks and balances. Policies to encourage an integrated approached and 'systems thinking'. Planning systems.	The Company has a comprehensive range of technology and systems used to ensure effective monitoring and control of key operating activities. The Board encourages a process of continuous improvement. This includes systems used for planning and delivering all of the Company's key activities such as production, supply, capital investment, billing and account management and finance. The Head of IT is a member of the senior leadership team meetings in order to ensure that an integrated approach is taken across the business to systems and processes.
Assets maintenance/insurance factors.	As part of the Business Plan process the Company prepared assessment s of asset health, risk and resilience and this informed the asset maintenance programme for future periods. The Board undertook a detailed review of the asset maintenance programme as part of the approval of the PR19 Business Plan and obtains regular reports in relation to asset health metrics and progress in the capital maintenance programme. Appropriate insurance is maintained by the Company and the Board reviewed the annual insurance renewal, including an assessment of any areas where insurance cover is not taken/available and the related risk.
<b>Contracting</b>	
Position/status of key contracts in place.	As part of governance processes the Board considers and approves all material contracts entered into by the Company. For example the Board reviewed the renewal of the contract with the key partner Cappagh and has taken oversight of key contracting activities in relation to HTWSR through the steering committee. The company is currently undertaking a review of its procurement strategy and the Board is represented in this process by an appropriately experienced Non-Executive Director.

## DIRECTORS STATEMENTS AND RESPONSIBILITIES

<p>All contracts between the Appointee and all Associated Companies were checked for compliance with license requirements on standards.          Note on transactions between the Appointee and any Associated Company. Compliance with license provision on cross-subsidies between the Appointee and any Associated Company (Condition I).          No Guarantees or Cross-Default Obligations given without Ofwat's written consent.</p>	<p>The Company has limited contracting activities with related parties. The Board reviews and approves the disclosure of transactions between the Company and "Associated Companies" as part of the approval of this Annual Performance Report. The Board has not identified any breaches of compliance with license conditions in relation to Associated Companies, including cross subsidiaries, nor has it approved any new guarantees or cross-default obligations.</p>
<p><b>Other material issues or circumstances</b></p>	
<p>COVID-19 impact</p>	<p>The Board has considered the impact of the current COVID-19 pandemic upon the Company's sufficiency of financial resources. This has included a detailed Board review of financial scenarios with three different durations of severe impact (3, 6 and 12 months) together with mitigating actions which were considered to be reasonable. The Board has been involved in the decision making process around the Company's response to COVID-19 and the mitigating actions which have been taken. This has included the extension of the Company's Revolving Credit Facility in May 2020 by a further £5m to £25m in order to allow additional financial headroom. The Board has reviewed the impact upon liquidity. Key financial ratios and covenants under a range of COVID-19 scenarios and has concluded that, following the application of reasonable mitigating measures, the Company retains sufficient financial resources. Further detail in relation to the COVID-19 response is set out in the Annual Report and Accounts and the Annual Performance Report.</p>
<p>Havant Thicket Winter Storage Reservoir</p>	<p>The HTWSR projects represents a significant programme for the business due to its size relative to the Company's Regulatory Capital Value. The Board has been closely involved in the oversight of this programme and has representation on the HTWSR Steering Committee. Regular reports are brought to the Board in relation to the project, including risk assessment and financial modelling. The Board has also considered the need to obtain additional capital to support the development of HTWSR and has concluded on this in light of both the indications of the Group's investor – Ancala – and the Company's wider financing strategy. Further detail in relation to the HTWSR project is set out in the Annual Report and Accounts.</p>

A formal certificate together with supporting appendices, in compliance with the licence condition, will be separately provided to Ofwat.

### Statement of Compliance of Licence Requirement Condition K

In accordance with its Instrument of Appointment under the Water Industry Act 1991, the Directors are of the opinion that the Company is in compliance with paragraph 4.3 (1) (g) of Condition 'K' of that Instrument as there have been no such transactions during the year.

### Statement of Compliance with Regulatory Accounting Guideline 5

The Directors hereby certify that, in their opinion, Portsmouth Water Limited complies with the objectives and principals of the above Regulatory Accounting Guideline, in so far as they apply to the Company, transactions with associated companies are at arm's length and that cross subsidy is not occurring.

### Statement on Risk & Compliance

The Directors confirm that the Company, in their opinion:

- has a full understanding of, and is meeting, its statutory licence and regulatory obligations and the expectations of its customers;
- has satisfied itself that it has sufficient processes and internal systems of control to fully meet its obligations; and
- has appropriate systems and processes in place to allow it to appropriately identify, manage, mitigate and review its risks.

## DIRECTORS STATEMENTS AND RESPONSIBILITIES

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In preparing this statement, the Directors confirm that the Company is aware of the obligations in legislation and in its licence with which it must comply. In particular, the Directors confirm that the Company:

- has sufficient rights and assets available to enable a special administrator to run the business;
- trade with associates is at arm's length;
- publishes a statement explaining the links between directors' pay and standards of performance; and
- maintains an investment grade credit rating.

The risk management, monitoring and control systems and processes upon which the Directors rely in making this statement are described in the Company's Annual Report and Accounts within the Strategic Report on pages 36 and 37 and the Corporate Governance Report on page 46.

**Signed by:**

C Deacon 

C R Taylor 

H M G Orton 

M P Johnson 

M R Coffin 

D W Owens 

**SECTION 1 REGULATORY FINANCIAL REPORTING**

**1A INCOME STATEMENT**

For the 12 months ended 31 March 2020

	Note	Current year				Total appointed activities £'000
		Statutory £'000	Adjustments		Total adjustments £'000	
			Differences between statutory and RAG definitions £'000	Non-appointed £'000		
<b>Revenue</b>	2	43,147	(1,525)	222	(1,747)	41,400
Operating costs	3	(35,068)	0	(76)	76	(34,992)
Other operating income	4	103	0	0	0	103
<u>Exceptional items:</u>						
COVID related bad debt provision	13	(1,489)	0	0	0	(1,489)
National Insurance cost relating to exercise of share options	24	(2,433)	0	0	0	(2,433)
<b>Operating profit/(loss)</b>		4,260	(1,525)	146	(1,671)	2,589
Other income	5	0	1,525	0	1,525	1,525
Interest income	6	1,062	0	0	0	1,062
Interest expense	7	(7,296)	0	0	0	(7,296)
Other interest income	6	672	0	0	0	672
<b>(Loss)/Profit before tax and fair value movements</b>		(1,302)	0	146	(146)	(1,448)
Fair value gains/(losses) on financial instruments		0	0	0	0	0
<b>(Loss)/Profit before tax</b>		(1,302)	0	146	(146)	(1,448)
UK Corporation tax	8	(313)	0	0	0	(313)
Deferred tax	8	(1,711)	0	0	0	(1,711)
<b>(Loss)/Profit for the year</b>		(3,326)	0	146	(146)	(3,472)
Dividends	9	3,685		146	(146)	3,539
<b>Tax Analysis</b>						
Current Year	8	0	0	0	0	0
Adjustments in respect of prior years	8	(313)	0	0	0	(313)
<b>UK Corporation Tax</b>		(313)	0	0	0	(313)

## 1B STATEMENT OF COMPREHENSIVE INCOME

For the 12 months ended 31 March 2020

	Note	Current year			Total appointed activities £'000	
		Statutory £'000	Adjustments			
			Differences between statutory and RAG definitions £'000	Non-appointed £'000		Total adjustments £'000
<b>Loss for the year</b>		(3,326)	0	146	(146)	(3,472)
Remeasurement of net defined benefit asset	22	(9,269)	0	0	0	(9,269)
Movement on deferred tax relating to pension asset	20	1,760	0	0	0	1,760
<b>Total Comprehensive (loss)/income for the year</b>		(10,835)	0	146	(146)	(10,981)

1C STATEMENT OF FINANCIAL POSITION

As at 31 March 2020

	Note	Current year				Total appointed activities £'000
		Statutory £'000	Adjustments		Total adjustments £'000	
			Differences between statutory and RAG definitions £'000	Non-appointed £'000		
<b>Non-current assets</b>						
Fixed assets	10	150,185	0	0	0	150,185
Intangible assets	11	936	0	0	0	936
Investments - loans to group companies	12	55,484	0	0	0	55,484
Investment Properties	12	325	0	0	0	325
Retirement benefit assets	22	15,546	0	0	0	15,546
<b>Total non-current assets</b>		<b>222,476</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>222,476</b>
<b>Current assets</b>						
Inventories		537	0	0	0	537
Trade & other receivables	13	7,552	0	311	(311)	7,241
Investments - other	14	2	0	0	0	2
Cash & cash equivalents	15	29,337	0	0	0	29,337
<b>Total current assets</b>		<b>37,428</b>	<b>0</b>	<b>311</b>	<b>(311)</b>	<b>37,117</b>
<b>Current liabilities</b>						
*Trade & other payables	17	(14,258)	0	(311)	311	(13,947)
Capex creditor	17	(4,689)	0	0	0	(4,689)
Borrowings	16	(20,784)	0	0	0	(20,784)
Current tax liabilities	17	(9,101)	0	0	0	(9,101)
Provisions	17	(1,412)	0	0	0	(1,412)
<b>Total current liabilities</b>		<b>(50,244)</b>	<b>0</b>	<b>(311)</b>	<b>311</b>	<b>(49,933)</b>
<b>Net Current liabilities</b>		<b>(12,816)</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>(12,816)</b>
<b>Non-current liabilities</b>						
Borrowings	18	(109,742)	0	0	0	(109,742)
Deferred income - G&C's	19	(28,043)	0	0	0	(28,043)
Deferred tax	20	(8,094)	0	0	0	(8,094)
<b>Total non-current liabilities</b>		<b>(145,879)</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>(145,879)</b>
<b>Net assets/(liabilities)</b>		<b>63,781</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>63,781</b>
<b>Equity</b>						
Called up share capital	21	1,078	0	0	0	1,078
Retained earnings & other reserves	21	62,703	0	0	0	62,703
<b>Total Equity</b>		<b>63,781</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>63,781</b>

\* The non-appointed amount is meter reading deferred income relating to the sale of the Non-household retail business. The original amount on the Balance Sheet was £1.2m, and this was to cover 5 years of meter reading income.

## 1D STATEMENT OF CASHFLOWS

For the 12 months ended 31 March 2020

	Note	Current year			Total appointed activities £'000	
		Statutory	Adjustments			
			Differences between statutory and RAG definitions	Non-appointed		Total adjustments
£'000	£'000	£'000	£'000	£'000		
<b>Operating profit</b>		4,260	(1,525)	146	(1,671)	2,589
Other income		0	1,525	0	1,525	1,525
Depreciation		6,121	0	0	0	6,121
Amortisation - G&C's		(709)	0	0	0	(709)
Changes in working capital		489	0	0	0	489
Notional Pension Costs		864	0	0	0	864
Movement in provisions		(147)	0	0	0	(147)
Loss on sale of fixed assets		(103)	0	0	0	-103
<b>Cash generated from operations</b>		10,775	0	146	(146)	10,629
Net interest paid		(3,128)	0	0	0	(3,128)
Tax paid		271	0	0	0	271
<b>Net cash generated from operating activities</b>		7,918	0	146	(146)	7,772
<b>Investing activities</b>						
Capital expenditure		(16,823)	0	0	0	(16,823)
Grants & Contributions		1,612	0	0	0	1,612
Disposal of fixed assets		172	0	0	0	172
Other		0	0	0	0	0
<b>Net cash used in investing activities</b>		(15,039)	0	0	0	(15,039)
<b>Net cash generated before financing activities</b>		(7,121)	0	146	(146)	(7,267)
<b>Cashflows from financing activities</b>						
Equity dividends paid		(3,685)	0	(146)	146	(3,539)
Equity payment received		2,433	0	0	0	2,433
Net loans received		10,500	0	0	0	10,500
<b>Net cash generated from financing activities</b>		9,248	0	(146)	146	9,394
<b>Increase in net cash</b>		2,127	0	0	0	2,127

## 1E NET DEBT ANALYSIS (Appointed activities)

As at 31 March 2020

	<b>Interest rate risk profile</b>			
	*Fixed rate	**Floating rate	Index linked	Total
	£'000	£'000	£'000	£'000
Borrowings (excluding preference shares)	784	20,000	110,452	131,236
Preference share capital				0
<b>Total borrowings</b>	<b>784</b>	<b>20,000</b>	<b>110,452</b>	<b>131,236</b>
***Cash				<b>(20,588)</b>
Short term deposits				0
<b>Net Debt</b>	<b>784</b>	<b>20,000</b>	<b>110,452</b>	<b>110,648</b>
Gearing				71.47%
Adjusted Gearing				n/a
Full year equivalent nominal interest cost (£m)	0.018	0.352	7.025	7.395
Full year equivalent cash interest payment (£m)	0.018	0.352	4.015	4.385
<b>Indicative interest rates</b>				
Indicative weighted average nominal interest rate	2.30%	1.76%	6.36%	5.67%
Indicative weighted average cash interest rate	2.30%	1.76%	3.64%	3.36%
Weighted average years to maturity	10	< 1	12	10

\* Perpetual Debt of £0.284m

\*\* Interest charged at 1% over LIBOR. Average LIBOR in the year 0.76%. Floating rate debt relates to the Company's revolving credit facility. On 29 May 2020 the Company extended this facility by £5m to a total of £25m.

\*\*\* Included within the cash at bank and in hand value, on the Balance Sheet, is an amount of £9.020m due to be paid to HMRC and relating to social security taxes. Funds to cover this payment were received from Ancala Partners in advance of the required settlement date. An adjusted Gearing has been calculated to remove the effect of this atypical cash balance. Further details are set out in note 24 of the APR.

Total Borrowings difference between 1C and 1E is the deferred arrangement costs of £0.710m on the index linked debt.

## 1F FINANCIAL FLOWS

**For the 12 months ended 31 March 2020  
(2012/13 financial year average RPI)**

	Units	%			£		
		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	%	5.70%	4.69%	5.70%	2,759,974	2,271,631	2,271,631
Actual performance adjust. 2010/15	%	1.79%	1.47%	1.79%	866,951	713,555	713,555
Adjusted return on regulatory equity	%	7.49%	6.16%	7.49%	3,626,925	2,985,185	2,985,185
Regulatory Equity Base	£	48,433,000	48,433,000	39,863,382			
<b>Financing</b>							
Gearing	%	0.00%	0.58%	0.58%	0	232,313	232,313
Variance in corporation tax	%	0.00%	0.25%	0.30%	0	120,000	120,000
Group relief	%	0.00%	0.00%	0.00%	0	0	0
Cost of debt	%	0.00%	-1.78%	-2.39%	0	(862,602)	(951,503)
Hedging instruments	%	0.00%	0.00%	0.00%	0	0	0
<b>Sub total</b>	%	7.49%	5.21%	5.99%	3,626,925	2,474,896	2,385,995
<b>Operational Performance</b>							
Totex out / (under) performance	%	0.00%	-5.32%	-6.47%	0	(2,578,000)	(2,578,000)
ODI out / (under) performance	%	0.00%	-4.97%	-6.04%	0	(2,407,000)	(2,407,000)
Retail out / (under) performance	%	0.00%	-0.30%	-0.37%	0	(147,000)	(147,000)
Other exceptional items	%	0.00%	-2.59%	-3.15%	0	(1,254,000)	(1,254,000)
<b>Sub Total</b>	%	0.00%	-13.19%	-16.02%	0	(6,386,000)	(6,386,000)
Total earnings	%	7.49%	-7.97%	-10.03%	3,626,925	3,911,104	4,000,005
RCV growth from RPI inflation	%	2.59%	2.59%	2.59%	1,253,785	1,253,785	1,031,943
Total shareholder return	%	10.08%	-5.38%	-7.45%	4,880,710	2,657,319	2,968,061
Net dividend	%	4.00%	4.32%	5.25%	1,937,320	2,091,890	2,091,890
Retained Value	%	6.08%	-9.70%	-12.69%	2,943,390	4,749,208	5,059,951
<b>Dividends reconciliation</b>							
Gross Dividend	%	4.00%	6.15%	7.47%	1,937,320	2,979,283	2,979,283
Interest Receivable on Intercompany loans	%	0.00%	1.83%	2.23%	0	887,393	887,393
Net dividend	%	4.00%	4.32%	5.25%	1,937,320	2,091,890	2,091,890

\*The Notional return in regulatory equity has been adjusted for the sale of the non-household business. This amounts to -0.15%.

1F FINANCIAL FLOWS continued

For the Price Review to date  
(2012/13 financial year average RPI)

		%			£		
	Units	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	%	5.77%	5.01%	5.77%	2,699,128	2,342,791	2,342,791
Actual performance adjust. 2010/15	%	1.16%	1.01%	1.16%	541,536	470,043	470,043
Adjusted return on regulatory equity	%	6.93%	6.01%	6.93%	3,240,664	2,812,834	2,812,834
Regulatory Equity Base	£	46,764,800	46,764,800	40,590,945			
<b>Financing</b>							
Gearing	%	0.00%	0.43%	0.43%	0	176,115	176,115
Variance in corporation tax	%	0.00%	0.18%	0.20%	0	82,200	82,200
Group relief	%	0.00%	0.10%	0.11%	0	45,656	45,656
Cost of debt	%	0.00%	-2.00%	-2.48%	0	(933,620)	(1,005,130)
Hedging instruments	%	0.00%	0.00%	0.00%	0	0	0
<b>Sub total</b>	%	6.93%	4.73%	5.20%	3,240,664	2,183,185	2,111,675
<b>Operational Performance</b>							
Totex out / (under) performance	%	0.00%	-0.90%	-1.04%	0	(420,800)	(420,800)
ODI out / (under) performance	%	0.00%	-0.76%	-0.88%	0	(355,600)	(355,600)
Retail out / (under) performance	%	0.00%	-0.86%	-0.99%	0	(400,800)	(400,800)
Other exceptional items	%	0.00%	0.41%	0.48%	0	193,500	193,500
<b>Sub Total</b>	%	0.00%	-2.10%	-2.42%	0	(983,700)	(983,700)
Total earnings	%	6.93%	2.62%	2.78%	3,240,664	1,199,485	1,127,975
RCV growth from RPI inflation	%	2.52%	2.52%	2.52%	1,177,912	1,177,912	1,022,405
Total shareholder return	%	9.45%	5.14%	5.30%	4,418,576	2,377,397	2,150,380
Net dividend	%	4.00%	2.99%	3.44%	1,870,592	1,396,351	1,396,351
Retained Value	%	5.45%	2.16%	1.86%	2,547,984	981,046	754,029
<b>Dividends reconciliation</b>							
Gross Dividend	%	4.00%	4.79%	5.51%	1,870,592	2,237,812	2,237,812
Interest Receivable on Intercompany loans	%	0.00%	1.80%	2.07%	0	841,461	841,461
Net dividend	%	4.00%	2.99%	3.44%	1,870,592	1,396,351	1,396,351

## COMMENTARY

**Basis of preparation**

In preparing the table 1F Financial Flows the following should be noted:

- The notional returns on Regulatory Equity are taken from the Ofwat FD Risk Assessment Tool, adjusted from 2017/18 to exclude the return for the Non-Household Retail business.
- The notional regulatory equity values are taken from Ofwat's documents "Appointee Regulatory Equity", for each year. These documents include the historic regulatory equity values from 2015/16.
- The gearing and cost of debt calculations use the year end RCV numbers published by Ofwat in 'Regulatory Capital Values', in each year. The gearing calculation adjusts the actual return on net debt by the July RPI movement, in line with the actual loan arrangements.
- Actual returns include exceptional items relating to the sale of the non-household business operations (note 25) and the COVID-19 provision for bad debt (note 13). Exceptional costs relating to the sale of the Company are excluded.

**Variations between the Final Determination and the results for 2019/20**

We have considered the significant variations arising between the return assumed in the Final Determination and the actual return for 2019/20. In overall terms the **actual** total shareholder return is -£2.8m and the dividend paid is £2.1m, compared to the notional total shareholder return of £5.1m and notional net dividend paid of £1.9m, based upon the Final Determination.

The material differences are driven by:

- higher gearing than the notional company
- lower corporation tax charges than assumed in the Final Determination
- higher cost of debt than allowed in the Final Determination
- operational under performance
- inclusion of an exceptional COVID-19 bad debt provision -£1.3m
- ODI penalties relating to the AMP, partially offset by the SIM reward
- lower net dividend levels than assumed in the Final Determination

**Gearing**

Actual average gearing of 68.9% is above the notional gearing of 62.5% by 6.4 percentage points. This has two implications. Firstly it results in a lower regulatory Equity Base as regulatory equity % (the reciprocal of gearing) is lower in the actual structure (actual equity 31.1% versus notional equity of 37.5%). Secondly it results in a benefit of £0.232m due to a higher allowed cost of debt.

**Corporation Tax**

(Amounts in 2012/13 prices)	£'000
Allowed corporation tax charge in FD	151
Actual Corporation tax credit on appointed activities	<u>(232)</u>
Variance	(383)
Minus variance arising from prior year adjustment	263
Total variance (favourable)	<u>(120)</u>

There is a favourable tax difference to the FD in the year as a result of an actual loss before tax in 2019/20 and claims for R&D tax credits together with a tax adjustment relating to prior years. Further analysis of tax is set out in note 8.

**Cost of debt**

The Company's actual cost of debt of 3.64% (index linked) exceeds the allowed cost of debt, together with the slightly higher gearing levels (noted above) this results in a £1.0m reduction in financial returns.

**Totex under performance**

See commentary relating to Table 4B on page 63.

The 2019/20 variance on capital expenditure is -£5,164k, including a small adjustment for timing differences. This variance relates to the reinvestment of savings made earlier in the AMP, with the completion of schemes not included in the Business Plan. The remaining adverse variance relates largely to leakage recovery operating costs in the year.

**Retail out/under performance**

The 2019/20 Household Retail expenditure is broadly in line (but slightly above) the FD.

**ODI penalty and SIM reward**

The ODI penalty for the AMP is included in the March 2019/20 schedule, -£2.4m, as this is an end of AMP calculation, except the MZC penalty which was incurred in 3 of the 5 years. The SIM reward of £1.4m is allocated evenly over the first 4 years of the AMP.

**Cumulative variances for the price review to date**

The material elements of the cumulative variances are also consistent with the significant factors explained above.

In relation to Totex, in the AMP to date, the favourable variance due to the efficiency in renewals expenditure has been eliminated in the final year of the AMP as the Company reinvested this saving in additional schemes.

The retail variance for the AMP to date is adverse by £392k. This is partly due to an increase in the provision for doubtful debts overall of around £200k. Also, there is an adverse impact from the change in the allocation method for General Rates, which is partially offset by a decrease in other shared services costs.

## RECONCILIATION BETWEEN STATUTORY ACCOUNTS AND REGULATORY ACCOUNTS

For the year ended 31 March 2020

	Statutory £'000	Regulatory £'000	Commentaries
<b>INCOME STATEMENT</b>			
Revenue	43,147	41,400	See a) below
Operating profit	<u>4,260</u>	<u>2,589</u>	See b) below
<b>STATEMENT OF FINANCIAL POSITION</b>			
Tangible fixed assets (net book value)	<u>150,185</u>	<u>150,185</u>	See c) below

- a) The difference relates to the way these figures have been presented in both sets of accounts. In the ARA, this figure includes amortisation of Developer Contributions and income from Connection Charges. In addition, there is non-appointed revenue of £0.075m, which relates to Commercial Services, and £0.147m, which is income from the sale of the Non-Household business, and relates to meter reading services. All of these amounts are excluded from the Regulatory revenue.

	£'000
Statutory revenue	43,147
Amortisation of Developer Contributions	(709)
Income from Connection Charges	(816)
Non-appointed revenue	(75)
Non-appointed meter reading revenue	(147)
Regulatory revenue	<u>41,400</u>

- b) The difference relates to the way these figures have been presented in both sets of accounts, as well as the inclusion of non-appointed business in the ARA. In the ARA, this figure includes other income of £1.525m, but this is reported after operating profit in the APR. The breakdown of this income is shown below.

There is a non-appointed operating profit of £0.074m, which relates to Commercial Services, as well as a number of other non-appointed items relating to rental properties and the sold Non-Household Retail Business. These are excluded from Regulatory operating profit.

	£'000
Statutory operating profit	4,260
Amortisation of Developer Contributions	(709)
Income from Connection Charges	(816)
Non-appointed operating profit	(74)
Non-appointed meter reading revenue	(147)
Non-appointed Rental Income	(109)
Non-appointed Home Assistance	(1)
Non-Household meter reading costs	24
Non-appointed Commercial department	161
Regulatory operating profit	<u>2,589</u>

- c) N/A

### 1 ACCOUNTING POLICIES

The statutory financial statements of Portsmouth Water Limited have been prepared in compliance with UK Accounting Standards, including Financial Reporting Standard 102 “The Financial Reporting Standard applicable in the United Kingdom and Republic of Ireland” (“FRS 102”) and the Companies Act 2006. This Annual Performance Report has been prepared on the basis of these statutory financial statements and have been presented and, where applicable, modified in accordance with the requirements of the Regulatory Accounting Guidelines (‘RAGs’) published by Ofwat and in force at the date of these accounts. The principal accounting changes in respect of the application of RAGs relate to the treatment of non-appointed business.

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied, unless otherwise stated. The financial statements are presented in pounds sterling.

In view of the licence conditions under which the Company operates as a water supplier, it is required to publish information about its annual results as if it were a company covered by the listing Rules of the Financial Conduct Authority, except where it is considered inappropriate to do so. Earnings per share disclosures are not presented as the Company is a wholly owned subsidiary. Segmental reporting has not been presented as, in the opinion of the Directors, the Company undertakes a single activity.

The principal accounting policies, which have been applied consistently, are as follows:

#### (a) Revenue

Revenue, which excludes value added tax, represents the income receivable for goods and services provided to external customers in the ordinary course of business.

Revenue from the regulated water business includes amounts billed for the year, together with an estimation of amounts used but unbilled at the year-end, for measured water customers. Where an invoice has been raised or payment received but the service has not been provided in the year this will be treated as a payment in advance. This will not be recognised within the current year’s turnover but will instead be included within creditors as deferred income.

Unmeasured income bills are generally based on the rateable value of properties. Unmeasured customers are billed annually in advance of 1 July and amounts invoiced in advance are not recognised in turnover until earned.

Measured income arises from customers who have meters fitted at their premises therefore amounts billed are based on actual water consumption. In addition a ‘measured income accrual’ is calculated in order to estimate of the value of water used but unbilled at the year-end. The estimation of the amounts unbilled at the year-end uses a defined methodology based upon valuing an estimate of unbilled water consumed. This is calculated using known factors such as the date of the customers’ last bill and the customer tariff rate together with an estimate of the water consumed. The estimated water consumed is calculated from various factors including; the number of days elapsed since the last meter read, historical consumption levels for each premises (which is calculated from historical customer billing data) or estimated average consumption per property type (where a historic actual is not available). The assumptions reflect historic experience and current data. Management review both the data sets used, the outcome of the calculation and quarterly trends in determining the year end position. There has been no change in the methodology for calculating the measured income accrual during the year.

Charges on income arising from court, solicitors and debt recovery agency fees are credited to operating costs and any out of pocket court costs are added to the relevant customer account. They are not recognised within turnover.

#### Differences between Statutory and Regulatory accounts

Non-appointed income is included within turnover in the statutory accounts but is excluded from turnover in the APR.

#### Void Properties

Empty household properties are classed as “voids” and no bill is raised. There is a defined process for determining if a property is unoccupied. The first stage is that an Occupation Form is posted to the property, requesting details of the occupier. If there is no reply a reminder is sent. The meter continues to be read and monitored and, if consumption is present, further steps are taken. The next stage involves a Visit Notice being raised and given to an Inspector. The Inspector will then go to the property and confirm if the property is void or not, and will turn off the water supply if appropriate. Accordingly revenue is only recognised if the property can be shown not to be void.

#### Empty Property Charging Policy

Charges are payable if premises are furnished unless the Company is asked to turn off the supply. No retrospective allowances are given. If the premises do not have a separate supply pipe it may not be possible for the Company to turn off the supply.

Where turn-off is required pending the sale of a property, or for a planned period of more than six months, no charge will be made to turn the water back on, provided this is undertaken within normal working hours and sufficient notice has been given.

## NOTES TO THE ACCOUNTS

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No charges are payable in respect of unoccupied unfurnished premises, where no water is being used. No retrospective allowances are given.

Where a property is unoccupied following the death of the owner/occupier, the Executors/Administrators can decide whether a supply is maintained to furnished premises, with charges accruing, or the supply is turned off. In either case, the bill outstanding will only become payable upon Probate or Letters of Administration having been obtained.

All new properties are metered. Charges accrue from the date at which the meter is installed. The developer is billed between the date of connection and first occupancy and this is recognised as turnover.

If the developer is no longer responsible for the property and no new occupier has been identified the process referred to above, for void properties, is followed to identify the new occupier. Until the new occupier has been identified the property is treated as unoccupied and is not billed.

### (b) Fixed assets

#### Tangible fixed assets

The Company holds both above ground assets and a below ground infrastructure network of mains. This classification, together with the value and nature of items, drives both the approval process and the accounting treatment of tangible fixed assets.

As part of the annual budgeting process a detailed capital programme is drawn up for the forthcoming financial year. This categorises capital schemes between mains infrastructure and above ground assets. This is approved by the Company's Board. Following Board approval individual schemes are programmed for the coming year by Project Managers responsible for delivering the schemes. The Project Managers are responsible for the control of expenditure on the schemes and authorise each individual item of expenditure incurred. The Financial Controller reviews the scheme expenditure in order to ensure that the correct accounting treatment has been applied. For small plant, equipment and vehicles a list is drawn up and also approved by the Company's Board. Purchases made are reviewed for correctness of treatment and to ensure that these are all capital items. The policy adopted by the Company is that only items above £500 are capitalised.

#### Mains infrastructure (below ground assets)

Infrastructure assets comprise a network of mains and communications pipes. The company undertakes expenditure on this network in order to maintain it in an ongoing serviceable condition. Where this expenditure meets certain criteria (set out below) it is capitalised. All other expenditure is expensed as incurred.

Expenditure on infrastructure assets relating to increases in capacity or other economic enhancement is capitalised. Other economic enhancements relate primarily to schemes addressing specific water quality issues or areas where mains have been diverted to avoid damage. Such items are treated as additions and included in property, plant and equipment at cost.

The cost of infrastructure assets is their purchase cost, together with incidental expenses of acquisition and directly attributable labour costs which are incremental to the Company. The assets are depreciated over their useful lives of between 40 and 100 years on a straight line basis. There are no expected residual values.

#### Other fixed assets (above ground assets)

Other assets comprise buildings and reservoirs, pumping plant, vehicles, mobile plant and office equipment. The cost of other assets is the purchase cost, together with incidental expenses of acquisition and directly attributable labour costs which are incremental to the Company. Depreciation is provided on all tangible fixed assets, with the exception of freehold land. It is calculated to write off the cost of assets over their estimated useful economic lives using the straight line method. There are no expected residual values. Those lives are estimated as follows:

Building and reservoirs	100 years
Pumping and other plant (including solar panels)	15-25 years
Office equipment	5-10 years
Vehicles and mobile Plant	5-7 years
Computer and network hardware	5 years
Meters	7-12 years

#### Assets in the course of construction

Assets in the course of construction are included in tangible fixed assets at cost but are not depreciated until they come into use.

#### Impairment

The values of fixed assets are reviewed regularly to determine whether their carrying amounts exceed their fair values in use. Where such an excess is believed to exist, it is treated as an impairment loss and charged to the income statement.

## NOTES TO THE ACCOUNTS

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### **Intangible fixed assets other than goodwill**

Intangible assets acquired separately from a business are recognised at cost and are subsequently measured at cost less accumulated amortisation and accumulated impairment losses. Amortisation is recognised so as to write off the cost or valuation of assets over their useful lives on the following basis:

Software (acquired before 31<sup>st</sup> March 2016) 5 years  
Software (acquired after 31<sup>st</sup> March 2016) 3 years  
Consultancy and internal staff costs (acquired before 31<sup>st</sup> March 2016) 5 years  
Consultancy and internal staff costs (acquired after 31<sup>st</sup> March 2016) 3 years

Intangible assets in the course of construction are included in intangible fixed assets at cost but are not amortised until they come into use. The purchase date may therefore place them in one category but the commencement of their economic life places them in another. Where this occurs the post March 2016 policy shall apply.

### **(c) Investment properties**

The Directors consider certain holdings of freehold land and buildings to be investment properties. In accordance with FRS 102, they are included in the statement of financial position at their open market value. The surplus or deficit on revaluation is recognised in the profit or loss for the year, along with the related deferred tax charge or credit. Depreciation is not provided in respect of these holdings. It is the Company's policy to obtain an external third party valuation of 1/5<sup>th</sup> of the property portfolio on a rolling basis with the remainder being valued based on a management review and using relevant indices.

### **(d) Capital contributions**

#### *Mains contributions*

In certain circumstances third parties make non-returnable contributions towards the cost of specific infrastructure assets. In accordance with the Companies Act 2006 and FRS 102 requirements to include fixed assets at cost, such contributions are treated as deferred income and released to the income statement over the useful economic life of the corresponding assets.

#### *Infrastructure charges*

Infrastructure charges are made in respect of new connections in accordance with Condition 'C' of the Instrument of Appointment. These charges are treated as mains contributions as explained above.

### **(e) Stocks**

Stocks of raw materials are valued on a weighted average cost basis at the lower of cost or net realisable value. In accordance with established practice in the water industry, no value is placed upon the water in reservoirs, mains or in the course of treatment.

### **(f) Taxation**

Current tax, including UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the statement of financial position date.

Deferred tax is recognised on all timing differences where the transactions or events that give the company an obligation to pay more tax in the future, or the right to pay less tax in the future, have occurred by the statement of financial position date. Deferred tax assets are recognised when it is probable that they will be recovered. Deferred tax is measured using rates of tax that have been enacted or substantively enacted by the statement of financial position date.

Deferred tax is recognised when assets are revalued and the gain or loss expected to arise on sale has been recognised in the financial statements.

### **(g) Leases**

All leases are regarded as operating leases. Operating lease payments are charged to the income statement on a straight line basis over the lease term. Lease income is recognised on a straight line basis over the lease term.

### **(h) Pension costs and other post-retirement benefits**

Portsmouth Water Limited is the principal employer and its parent company, Brockhampton Holdings Limited, is the participating employer in the Brockhampton Pension Scheme. This scheme is a defined benefit scheme. The assets of the scheme are held in a separate trustee administered fund. As principal employer Portsmouth Water includes the pension asset in its financial statements.

## NOTES TO THE ACCOUNTS

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The current service costs are charged to the income statement and included as staff employment costs. The interest cost and interest income are shown as a net amount within other interest income. Re-measurements of the net defined benefit asset are recognised immediately in other comprehensive income.

Pension scheme liabilities are measured on an actuarial basis using the projected unit method and are discounted to their present value using the AA corporate bond rate.

Pension scheme assets are valued at fair value at the statement of financial position date. The pension scheme surplus is recognised in full on the statement of financial position.

The deferred tax relating to a defined benefit asset is offset against the defined benefit asset and not included with other deferred tax liabilities.

Detailed information regarding the surplus and actuarial position of the scheme is given in note 22 of the APR.

The Company also operates a defined contribution pension scheme. The charge to the income statement amounts to the contributions payable to the scheme in respect of the accounting period.

### **(i) Financial instruments**

Financial assets and financial liabilities are recognised when the company becomes party to the contractual provisions of the instrument.

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the company after deducting all of its liabilities.

All financial assets and liabilities are initially measured at transaction price (including transaction costs), except for financial assets classified as fair value through profit and loss, which are initially measured at fair value (normally transaction price excluding transaction cost).

If an arrangement constitutes a financing transaction, the financial asset or financial liability is measured at the present value of the future payments discounted at a market rate of interest for a similar debt instrument.

Debt instruments which meet the applicable conditions are recognised as basic financial instruments and subsequently measured at amortised costs using the effective interest rate method. Instruments that are payable or receivable within one year of initial recognition and meet the applicable conditions are measured at the undiscounted amount of consideration expected to be paid or received, net of impairment.

Financial assets are derecognised when and only when the contractual rights to the cash flows from the financial assets expire or are settled, or the company transfers substantially all of the risks and rewards of ownership of the financial asset.

Financial liabilities are derecognised only when the obligation specified in the contract is discharged, cancelled or expires.

The Company subsequently categorises financial instruments as follows:

- Fixed asset investments consist of loans to Group undertakings, which earn interest based on London Interbank rates and are classified as loans and receivables.
- Other financial assets consist of short term bank deposits and debtors and are classified as loans and receivables.

The Company's financial liabilities consist of fixed rate borrowings in the form of perpetual debentures, an index linked loan and an intercompany loan.

### **Investments**

Investments consist of non-current and current investments.

Non-current investments are in respect of loans to group companies. They are measured at amortised cost using the effective interest rate method.

Current asset investments are held at cost less impairment since fair value cannot be measured reliably.

### **(j) Provisions**

A provision is recognised when the Company has a legal or constructive obligation as a result of past events and it is probable that an outflow of economic benefits will be required to settle the obligation. The effect of the time value of money is not material and therefore the provisions are not discounted.

## NOTES TO THE ACCOUNTS

### (k) Cost allocation policies

#### Accounting Separation

The tables which relate to the PR14 price controls have been completed in accordance with RAG 2 - Guideline for classification of costs across the price controls. The details of this classification are included in the separately published Accounting Separation Methodology Statement, which can be located on the Company website at [www.portsmouthwater.co.uk](http://www.portsmouthwater.co.uk).

The Methodology Statement details the systems in place and the sources of information used to populate the relevant tables in the Annual Performance Report. The detailed nominal ledger management information reports allow costs to be identified for each cost centre of the Company, and the direct costs of Business Units, for example Retail, can be readily identified.

The Company has used the guidance issued by Ofwat in the separating of costs and assets between the Wholesale and Retail business units. It has followed the prescribed hierarchy of cost drivers when deciding upon the most appropriate basis for allocation of both costs and assets. Where the Company has opted to base the allocation of a number of costs and assets on a management estimate, it is satisfied that this was the only valid option given the time and costs involved in other methods.

A summary of the bases of allocation for the operating costs, excluding depreciation, is included below:

#### **ANNUAL PERFORMANCE REPORT - BUSINESS UNIT TABLES**

**2019/20**

#### **BASIS OF ALLOCATION**

##### **DIRECT COSTS**

Employment Costs	Direct and management estimate
Power	Pumping Head
Hired & Contracted Services	Direct
Materials & Consumables	Direct
Service Charges	Direct
Other Direct Costs	Direct

##### **GENERAL & SUPPORT ACTIVITIES**

Land & Property	Direct and prorata on direct
Production Technical	Direct and prorata on direct
Production Engineer	Production Technical basis
Network General & Admin	Direct
Personnel Services	FTE's
Legal & Property	FTE's
Financial Services	FTE's
Directors	Time on activities and Board Agenda
IT	No. of computers & mobile devices
Operational / Technical Support	GMEAV of asset additions
Vehicles & Plant	No of vehicles
Stores	Direct material costs

##### **GENERAL ADMIN**

Directly identifiable items	Direct
Other General Admin	Direct/Floor space/FTE's

Other Business Activities	Direct/1/5 per Business Unit
Scientific Services	Quality samples
Doubtful Debts	Direct
General Rates	Floor space
Bulk Supply	Direct
Third Party Costs (RCW)	Direct
Renewals Expensed	Direct

The allocation of shared assets and the associated depreciation is based on the same methodology. These assets are grouped into categories, such as IT or Scientific Services, and allocated on the same basis as the corresponding operating costs.

### (l) Critical accounting judgements and key sources of estimation uncertainty

Information on critical accounting judgements and key sources of estimation uncertainty can be found on page 74 of the Annual Report and Accounts.

## NOTES TO THE ACCOUNTS

	Appointed	Non	Total	Appointed	Non	Total
	2020	Appointed	2020	2019	Appointed	2019
	£000	2020	£000	£000	2019	£000
<b>2. REVENUE</b>						
Unmeasured household supplies	21,396	-	21,396	21,148	-	21,148
Measured household supplies	10,227	-	10,227	9,678	-	9,678
Non-household supplies	9,116	-	9,116	8,757	-	8,757
Third party services	612	222	834	556	175	731
Other sources	49	-	49	51	-	51
	<u>41,400</u>	<u>222</u>	<u>41,622</u>	<u>40,190</u>	<u>175</u>	<u>40,365</u>

### Measured Income Accrual

For the year 2018/19 the measured income accrual was £2,387,384, and the corresponding actual billed revenue was £2,436,636. This is a difference of £49,252.

### 3. ANALYSIS OF OPERATING COSTS

This note has been prepared in accordance with Condition 'F' of the Company's Instrument of Appointment.

	Appointed	Non	Total	Appointed	Non	Total
	2020	Appointed	2020	2019	Appointed	2019
	£000	2020	£000	£000	2019	£000
Manpower costs	10,433	180	10,613	10,272	29	10,301
Other costs of employment	303	-	303	438	-	438
Power	2,720	-	2,720	2,659	-	2,659
Rates	2,499	-	2,499	2,487	-	2,487
Hired and contracted services	6,731	3	6,734	5,669	-	5,669
Materials and consumables	1,673	1	1,674	2,220	-	2,220
Service charges	1,322	-	1,322	1,319	-	1,319
Renewals expensed	2,358	-	2,358	2,580	-	2,580
Provision for bad and doubtful debts	536	-	536	544	-	544
Other operating costs	296	(108)	188	299	(146)	153
Depreciation and Amortisation	6,121	-	6,121	5,865	-	5,865
	<u>34,992</u>	<u>76</u>	<u>35,068</u>	<u>34,352</u>	<u>(117)</u>	<u>34,235</u>

Manpower costs include a notional pension charge which should not be included for efficiency purposes, as the notional pension charge is excluded from the price determination. A comparison of these costs are shown below:

	2020	2019
	£000	£000
Manpower as reported	10,433	10,272
Notional Pension Cost	(864)	(811)
	<u>9,569</u>	<u>9,461</u>
Manpower Cost for Efficiency and Price Determination purposes		

	Appointed	Non	Total	Appointed	Non	Total
	2020	Appointed	2020	2019	Appointed	2019
	£000	2020	£000	£000	2019	£000
<b>4. OTHER OPERATING INCOME</b>						
Profit/ (Loss) arising on disposal of fixed assets	103	-	103	(494)	-	(494)

**NOTES TO THE ACCOUNTS**

		Appointed	Non	Total	Appointed	Non	Total
		2020	Appointed	2020	2019	Appointed	2019
		£000	2020	£000	£000	2019	£000
<b>5.</b>	<b>OTHER INCOME</b>						
	Amortisation of Developer Contributions	709	-	709	646	-	646
	S45 Connection Charges	816	-	816	1,150	-	1,150
		<u>1,525</u>	<u>-</u>	<u>1,525</u>	<u>1,796</u>	<u>-</u>	<u>1,796</u>
<b>6.</b>	<b>INTEREST INCOME</b>				<b>2020</b>		<b>2019</b>
					<b>£000</b>		<b>£000</b>
	Loan to Group Company				1,054		953
	Interest on short term deposits				8		4
					<u>1,062</u>		<u>957</u>
	Other Interest Income (see note 22)				<u>672</u>		<u>762</u>
<b>7.</b>	<b>INTEREST EXPENSE</b>				<b>2020</b>		<b>2019</b>
					<b>£000</b>		<b>£000</b>
	£66.5m loan - interest				3,970		3,867
	- indexation				2,976		3,357
	- amortisation of fees				57		57
	- administration expenses				212		131
					<u>7,215</u>		<u>7,412</u>
	Other bank loans and overdraft				65		10
	Debenture stocks				14		10
	Other interest payable				2		12
					<u>7,296</u>		<u>7,444</u>
<b>8.</b>	<b>TAXATION (APPOINTED BUSINESS ONLY)</b>				<b>2020</b>		<b>2019</b>
					<b>£000</b>		<b>£000</b>
	<b>Current tax</b>						
	United Kingdom corporation tax at 19% (2019 - 19%)				-		-
	Group relief				-		-
	Adjustment in respect of prior periods				313		(140)
					<u>313</u>		<u>(140)</u>
	<b>Deferred tax</b>						
	Origination and reversal of timing differences				346		302
	Effect of tax rate change on opening balance				1,385		-
	Adjustment in respect of prior periods				(20)		(155)
					<u>1,711</u>		<u>147</u>
	<b>Tax on loss on ordinary activities</b>				<u>2,024</u>		<u>7</u>

## NOTES TO THE ACCOUNTS

### 8. TAXATION (APPOINTED BUSINESS ONLY) (continued)

	2020 £000	2019 £000
The tax charge for the year is lower (2019 - lower) than the standard rate of Corporation tax in the UK of 19% (2019 - 19%), explained as follows:		
Loss on ordinary activities before tax and fair value movements	(1,448)	(1,007)
Loss before tax (taxable)	<u>(1,448)</u>	<u>(1,007)</u>
Loss on ordinary activities multiplied by standard rate of corporation tax in the UK of 19% (2019 - 19%)	(275)	(191)
Effect of:		
Depreciation on assets not qualifying for capital allowances	236	64
Other tax adjustments (including effect of change in tax rate)	39	20
Prior year adjustments	313	(140)
Expenses not deductible for tax purposes	-	107
<b>Current tax charge/(credit) for the year</b>	<u>313</u>	<u>(140)</u>

### RECONCILIATION BETWEEN CURRENT TAX CHARGE AND CURRENT TAX IN PRICE LIMITS

		Statutory Accounts	Non- Appointed	Appointed	Final Determination	Tax Difference @19%
	Note	£'000	£'000	£'000	£'000	£'000
Loss before tax	1	(1,302)	146	(1,448)	3,547	949
Owat adjustments gearing	1	0	0	0	(1,175)	(223)
PBT adjusted for gearing	1	(1,302)	146	(1,448)	2,372	726
Add depreciation	2	6,121		6,121	4,190	(367)
Less Capital allowances	2	(6,853)		(6,853)	(5,891)	183
Pensions difference		192		192	189	(1)
Other adjustments	3	753		753	300	(86)
Tax losses utilised in the period	4		(146)	146		(28)
Corporate interest rate restriction	5	1,089		1,089		(207)
Adjusted profit chargeable to CT		<u>0</u>	<u>0</u>	<u>0</u>	<u>1,160</u>	<u>220</u>
@ tax rate 19%		0	0	0		
Current Tax charge		<u>0</u>	<u>0</u>	<u>0</u>	<u>220</u>	
Prior year adjustment	6	(313)	0	(313)		
		<u>(313)</u>	<u>0</u>	<u>(313)</u>		

We have analysed the differences between the current tax credit of £0.313m for the appointed business against the tax charge calculated in the Final Determination of £0.220m. The significant movements are as follows:

1. Loss before tax of £1.4m, FD profit of £3.5m. However, this should be further adjusted for by a charge of £1.2m which reflects the Owat net tax adjustment for gearing. This reflects the higher actual finance cost when compared to the notional finance cost included in the FD.
2. Actual depreciation and capital allowances outturn is higher than estimated in the Business Plan submission.
3. Impact of chargeable gains and other disallowable items.
4. Losses utilised against non-regulated profits.
5. Corporate interest rate restriction.
6. Prior year current tax adjustment.

## NOTES TO THE ACCOUNTS

### 9. DIVIDENDS

#### Equity: Ordinary/'A' Ordinary

	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
Interim paid	1,710	3,076
Final paid	1,975	-
<b>Total Dividends</b>	<b>3,685</b>	<b>3,076</b>

Given the current COVID-19 related financial concerns and mitigants employed around cash flow protection, the Directors are not proposing payment of a final dividend for the year ended 31 March 2020. This position will be kept under review for the current time.

#### Dividend Policy

For the appointed business a base level of dividend will be calculated using a 5% dividend yield on average regulatory equity value. The Company will adjust this base dividend in the period 2020-25 to reflect and recognise company performance and delivery to customers, in particular performance above or below that assumed in the Final Determination.

The Board's decision on the dividend will reflect a mixture of financial and non-financial incentives, with account being taken of known and forecast performance and relative importance to customers and stakeholders.

Specifically it will recognise:-

- Our regulatory obligations
- The commitments we have made to customers and other stakeholders
- Any adjustments for out / underperformance against regulatory metrics and benefit sharing
- Employee interests and pension obligations
- Our actual capital structure and the need to finance future investment (RCV growth) beyond committed equity injections.
- The short / medium term financial resilience of the Business.

In determining the level of the dividend the Company will apply a 4 step process:-

1. Understanding the Financial Performance of the appointed and non-appointed business and its ability to provide a dividend
2. Reflect Commitments to Customers and Stakeholders including customer service & ODI commitments.
3. Undertake Financeability Tests.
4. Recognising Regulatory Tests including licence conditions

The Board is committed to considering these factors in declaring a dividend and in setting out clearly, in each Annual Performance Report, the dividend policy, the factors that have been considered in determining the dividend and how these relate to the dividend declared. The Board will also explain how the decision in relation to dividends reflects how the Company has delivered for customers.

For the Non-Appointed business the Company will consider business performance including available Non-Appointed profits and the extent to which further future investment may be required to support or develop the Non-Appointed business.

In light of the impact of the current COVID-19 pandemic, the Board has taken the decision to defer any dividend payments at this time. It will keep this situation under review and any future distributions will continue to be considered in line with this policy.

	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
Dividend ultimately for group shareholders	2,550	2,626
Servicing of intercompany debt net of tax	1,135	450
<b>Total Dividends</b>	<b>3,685</b>	<b>3,076</b>

NOTES TO THE ACCOUNTS

10. TANGIBLE FIXED ASSETS

	Freehold land, buildings & reservoirs Restated £'000	Mains Restated £'000	Pumping Plant £'000	Vehicles, mobile plant & office equipment £'000	Total Restated £'000
<b>COST</b>					
At 1st April 2019	58,311	64,173	56,221	23,467	202,172
Additions	5,786	3,784	7,685	2,479	19,734
Disposals	-	(93)	-	(217)	(310)
At 31st March 2020	<b>64,097</b>	<b>67,864</b>	<b>63,906</b>	<b>25,729</b>	<b>221,596</b>
<b>DEPRECIATION</b>					
At 1st April 2019	14,061	5,895	30,155	15,925	66,036
Charge for year	527	1,130	2,094	1,864	5,615
Disposals during year	-	(25)	-	(215)	(240)
At 31st March 2020	<b>14,588</b>	<b>7,000</b>	<b>32,249</b>	<b>17,574</b>	<b>71,411</b>
<b>NET BOOK VALUE</b>					
At 31st March 2020	<b>49,509</b>	<b>60,864</b>	<b>31,657</b>	<b>8,155</b>	<b>150,185</b>
At 1st April 2019	44,250	58,278	26,066	7,542	136,136

ASSETS IN THE COURSE OF CONSTRUCTION

Included in the above table are assets in the course of construction as follows:

	Freehold land, buildings & reservoirs £'000	Mains £'000	Pumping Plant £'000	Vehicles, mobile plant & office equipment £'000	Total £'000
<b>COST</b>					
At 1st April 2019	3,882	2,941	(822)	31	6,032
Additions	5,786	4,211	7,685	1,175	18,857
Transferred into fixed assets	(820)	(3,749)	(3,858)	(922)	(9,349)
At 31st March 2020	<b>8,848</b>	<b>3,403</b>	<b>3,005</b>	<b>284</b>	<b>15,540</b>
<b>DEPRECIATION</b>					
At 1st April 2019	-	-	-	-	-
Charge for year	-	-	-	-	-
At 31st March 2020	-	-	-	-	-
<b>NET BOOK VALUE</b>					
At 31st March 2020	<b>8,848</b>	<b>3,403</b>	<b>3,005</b>	<b>284</b>	<b>15,540</b>
At 1st April 2019	3,882	2,941	(822)	31	6,032

No depreciation has so far been provided on the above cost.

## NOTES TO THE ACCOUNTS

### 11. INTANGIBLE FIXED ASSETS

	<b>Software, Consultancy and Internal costs £'000</b>
<b>COST</b>	
At 1st April 2019	3,030
Additions (WIP completed assets)	326
Disposals	(16)
At 31st March 2020	<b>3,340</b>
<b>AMORTISATION</b>	
At 1st April 2019	1,914
Disposals	(16)
Charge for year	506
At 31st March 2020	<b>2,404</b>
<b>NET BOOK VALUE</b>	
At 31st March 2020	<b>936</b>
At 1st April 2019	1,116

Intangible fixed assets primarily comprise software costs and the in house development of bespoke software and related IT solutions. Included in the numbers above is £0.290m of assets in the course of construction, which relates to the development of the AMP7 Commercial and procurement Strategies for the future capital spend.

### 12. FIXED ASSET INVESTMENT

	<b>Loan to Group Undertakings £000</b>
At 1 April 2019	55,484
At 31 March 2020	55,484

Non-current asset investments represent a loan to the parent entity South Downs Ltd. These loans are repayable other than by instalments and are held at amortised cost. Interest is charged 6 monthly at a rate of LIBOR + 1%. The Company has confirmed that it does not intend to request payment of this loan within 12 months from the date of approval of the PWL financial statements.

### INVESTMENT PROPERTIES

	<b>Investment Properties £000</b>
At 1 April 2019	325
At 31 March 2020	325

The historic cost of the investment properties at 31 March 2020 was £0.195m (2019 - £0.195m)

There are no restrictions on the realisability of investment property. There are no contractual obligations to purchase, construct or develop investment property or to make any repairs or enhancements.

## NOTES TO THE ACCOUNTS

13. DEBTORS	<b>2020</b> <b>£000</b>	<b>2019</b> <b>£000</b>
Trade debtors	2,111	3,070
*Amounts owed by Group companies	975	960
Prepayments and accrued income	3,461	3,714
Other debtors	694	731
	7,241	8,475

\* Amounts owed by Group companies excludes the notional intercompany payable of £0.311m (2019 - £0.458m), relating to the deferred income for Non-household meter reading, which is non-appointed.

All of the above amounts fall due within one year. Included within other debtors is corporation tax recoverable of nil (2019 - £0.271m)

As at 31 March 2020, trade debtors had a carrying value of £6.934m (2019 - £7.706m) before provision for bad debt. Trade debtors in arrears are provided for on a sliding scale depending on age of debt and include an additional exceptional COVID-19 bad debt provision of £1.089m. The total amount of the provision was £4.823m as at 31 March 2019 (2019 - £4.636m).

The ageing of these debtors was as follows:

	<b>2020</b> <b>£000</b>	<b>2019</b> <b>£000</b>
Up to 12 months	4,497	3,690
Over 12 months	2,437	4,016
	6,934	7,706

The debtors provided for are mainly in respect of water charges for household customers where experience in the water industry has shown over time that it is likely that there will be difficulties in recovering the water charges for the periods concerned.

An additional provision related to future debt attributable to the COVID-19 situation has been recognised for £1.489m, of which £1.089m relates to provision for bad debts and a further £0.4m reflects a reduction of accrued income. This has been classified as exceptional by virtue of its' size and atypical nature

	<b>2020</b> <b>£000</b>	<b>2019</b> <b>£000</b>
As at 1 April 2019	4,636	4,580
Provision for bad debt required in the year	428	544
Additional COVID-19 related provision	1,089	-
Debt written off in the year as uncollectable	(1,330)	(488)
	4,823	4,636

The other classes within debtors do not contain balances that may be irrecoverable. The maximum exposure to credit risk at the reporting date is the fair value of each class of debtor mentioned above. The Company does not hold any collateral as security for routine trading debt, however, according to the Open Water Terms of Business collateral is now held in the form of cash and guarantees to cover any non-household risk.

	<b>2020</b> <b>£000</b>	<b>2019</b> <b>£000</b>
<b>Total Debtors Outstanding &gt; 30 days</b>		
- Household	5,741	5,564

## NOTES TO THE ACCOUNTS

### Write Off Policy

Our bad debt write off policy has been reviewed and updated during the year. In addition the policies set out below, all debt over 6 years old is written off in full.

*Customers who remain within our area of supply;*

Domestic – written off upon Bankruptcy or the granting of a Debt Relief Order.

*Customers who have moved outside of our area of supply;*

Debt less than £50 – limited automated credit control and then periodic automatic write off.

Debt greater than £50 – credit control process then passed to a Debt Collection Agency (DCA) for recovery on a no success, no fee basis. Periodic write off exercise for accounts returned by DCA, following internal review.

Differences in amounts written off from year to year are generally the result of differences in the timing of write off exercises rather than as a result of any particular trends.

### Provisioning policy

Based upon extensive data analysis the bad debt provisioning policy has been updated during the year:-

The Company makes an estimate of the recoverable value of trade receivables. When assessing impairment of trade receivables, management considers factors including aging profile of the receivables, stage of credit control and historical experience. After an exercise to develop our understanding about the relationship between bad debt and certain customer segmentation information, we made a decision to revise the accounting estimate for the bad debt provision. We believe that this provides a more accurate reflection of the bad debt risk based upon customer characteristics. As part of this analysis we also considered the linkage between collection history and debt ageing. Accordingly we revised the levels of provision based on debtor age in line with updated experienced collection rates.

The bad debt provision remains largely consistent year and the application of this revised methodology resulted in a charge of £0.4m compared to the previous methodology that would have resulted in a charge of £0.8m. This revised methodology will be consistently applied from now onwards.

The Bad Debt Provision applies the following recovery rates;

Provision rate	Overdue up to 1 year	1-2 years	2-3 years	3-4 years	4-5 years	5-6 years
Measured	23%	65%	72%	77%	83%	90%
Unmeasured	27%	63%	68%	72%	78%	87%

### COVID-19 related specific bad debt provision

The Company has made an estimate on the level of customer debt, (both for invoiced and accrued amounts), as at 31 March 2020 that may now be subject to additional risk due to the impact of COVID-19. Of this total provision of £1.489m, £1.089 has been allocated against trade debtors, as a bad debt provision and a further £0.400m against accrued, but unbilled income. Significant analysis and modelling has been undertaken which has considered customer segmentation and socio economic factors which might impact the ability to recover debts under the COVID-19 circumstances, such as unemployment levels. The current level of provision of £1.489m has been presented as an exceptional item by virtue of its size and atypical nature. This is classified by nature, as an operating expense.

## 14. INVESTMENTS

	2020 £000	2019 £000
Unlisted investments	2	2

## 15. CASH AT BANK AND IN HAND

Of the total amount shown of £29.337m (2019 - £27.210m), £2.021m (2019 - £1.968m) is held specifically for the payment of the next half yearly loan interest charges.

£8.749m (2019 - £9.020m) of the increase in cash is due to proceeds of sale and share options being transferred from Ancala. This is to settle future incremental employment related social security liabilities brought about by the transaction (See note 31 of the APR)

**NOTES TO THE ACCOUNTS**

<b>16. BORROWINGS: DUE WITHIN ONE YEAR</b>	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
3% Perpetual debenture stock	60	60
3½% Perpetual debenture stock	185	185
4% Perpetual debenture stock	39	39
Balance outstanding on revolving credit facility	20,000	10,000
*Short term intercompany loan	500	-
	<u>20,784</u>	<u>10,284</u>

The Revolver Credit Facility is part of a three year £20m working capital facility, which is secured upon the assets of the Company and bears interest at London Interbank rates. Following the year end this facility was extended to £25m.

\*An intercompany short term loan carrying interest charged at 3 months LIBOR + 1%

<b>17. OTHER CURRENT LIABILITIES</b>	<b>Appointed</b>	<b>Non</b>	<b>Total</b>	<b>Appointed</b>	<b>Non</b>	<b>Total</b>
	<b>2020</b>	<b>Appointed</b>	<b>2020</b>	<b>2019</b>	<b>Appointed</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>
Payments received on account	1,399	-	1,399	1,845	-	1,845
Trade creditors	2,868	-	2,868	3,118	-	3,118
Amounts owed to Group companies	433	-	433	119	-	119
Other creditors	420	-	420	425	-	425
Accruals	997	-	997	818	-	818
Water rates in advance	7,830	311	8,141	6,657	458	7,115
	<u>13,947</u>	<u>311</u>	<u>14,258</u>	<u>12,982</u>	<u>458</u>	<u>13,440</u>
Trade and other payables						
Provisions	1,412	-	1,412	1,412	-	1,412
Capex creditor	4,689	-	4,689	2,356	-	2,356
Other taxation and social security	9,101	-	9,101	9,281	-	9,281
	<u>29,149</u>	<u>311</u>	<u>29,460</u>	<u>26,031</u>	<u>458</u>	<u>26,489</u>

<b>18. NON-CURRENT LIABILITIES</b>	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
In five years or more:		
Bank loan	110,452	107,476
Less: deferred arrangement costs	(710)	(767)
	<u>109,742</u>	<u>106,709</u>

The thirty year £66.5m index-linked loan was issued on 26 June 2002, is repayable on 30 September 2032, and is secured upon the assets of the Company. The capital value of the loan is adjusted by the change in the Retail Prices Index from year to year. The fees associated with the loan issue of £1.722m are amortised over the life of the loan. The amount owing on the loan is stated net of the unamortised issue fees.

The loan interest is calculated by adjusting the value of the loan by the Retail Prices Index and then charging interest on this inflated amount at 3.635% per annum.

**NOTES TO THE ACCOUNTS**

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**19. DEFERRED INCOME: CAPITAL CONTRIBUTIONS**

	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
Capital Contributions	28,752	27,783
Release of Capital Contribution to Turnover	(709)	(645)
	28,043	27,138

**20. PROVISIONS FOR LIABILITIES**

	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
<b>DEFERRED TAXATION:</b>		
At 1 April 2019	6,919	6,764
Charged during the year in profit and loss account	1,175	155
	8,094	6,919
At 31 March 2020	8,094	6,919

The amount provided for deferred taxation represents timing differences caused by the excess of tax allowances over depreciation.

	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
<b>Deferred tax including that relating to pension asset:</b>		
Accelerated capital allowances	9,265	8,088
Other timing differences	(1,171)	(1,169)
Pension asset (note 22)	3,647	4,871
	11,741	11,790
Total provision for deferred tax	11,741	11,790
At 1 April 2019	11,790	11,842
Deferred tax charge in profit and loss account (note 8)	1,711	147
Deferred tax credited to the statement of comprehensive income	(1,760)	(199)
	11,741	11,790
At 31 March 2020	11,741	11,790

## NOTES TO THE ACCOUNTS

### 21. RESERVES

	Called up Share Capital £'000	Share Premium Account £'000	Capital Redemption Reserve £'000	Retained Earnings £'000	Total £'000
Balance at 1st April 2019	1,078	6,949	3,250	64,591	75,868
Loss for Financial Year	-	-	-	(3,326)	(3,326)
Remeasurement of net defined benefit asset	-	-	-	(9,269)	(9,269)
Movement on deferred tax relating to pension scheme	-	-	-	1,760	1,760
Total comprehensive profit for the year	-	-	-	(10,835)	(10,835)
New share capital/share premium issued	-	2,433	-	-	2,433
Dividends	-	-	-	(3,685)	(3,685)
Balance at 31st March 2020	<b>1,078</b>	<b>9,382</b>	<b>3,250</b>	<b>50,071</b>	<b>63,781</b>

The retained earnings balance represents accumulated profits and losses, including unrealised profits on the re-measurement of investment properties, net of dividends paid and other adjustments. As at 31 March 2020 £49.941m (2019 - £64.461m) was distributable in accordance with company law and £0.130m (2019 - £0.130m) was not distributable.

The share premium reserve contains the premium arising on the issue of equity shares, net of issue costs.

The accompanying notes form an integral part of these accounts.

### 22. PENSIONS

Portsmouth Water Limited, a subsidiary undertaking, is the principal employer and its parent company, Brockhampton Holdings Limited, is the participating employer in the Brockhampton Pension Scheme. This scheme provides defined benefits based primarily on pensionable earnings. The assets of the scheme are held in a separate trustee administered fund.

The formal actuarial valuation as at 31 March 2018 was updated to the 31 March 2020 accounting date by an independent qualified actuary in accordance with FRS 102. As required by FRS 102, the value of the defined benefit liabilities has been measured using the projected unit method.

The estimated Company contributions expected to be paid to the Scheme by Portsmouth Water Ltd for the year commencing 1 April 2020 is £1.7m (2019 actual: £1.1m). Of this amount, £1.5m is contributed directly by the Company and £0.2m is contributed by employees by salary sacrifice under the SMART arrangement. The key FRS 102 assumptions used for the scheme were as follows:

	2020 % per annum	2019 % per annum	2018 % per annum
RPI inflation	2.5	3.3	3.2
CPI inflation	1.9	2.4	2.3
Discount rate	2.4	2.3	2.5
Pension increases	2.0	2.4	2.3
Salary growth	2.0	4.4	4.3

Life expectancy of a male aged 65 at the accounting date is 22.0 years and for a female is 24.4 years. Allowances for future improvements in life expectancy mean that life expectancy of a male aged 65 at the accounting date plus 20 years is 23.6 years and for a female is 26.1 years.

The fair value of assets in the scheme, a breakdown of the assets into the main asset classes, the present value of the FRS 102 defined benefit obligation and the surplus of assets over the FRS 102 defined benefit obligation (which equals the gross pension asset) are set out below:

## NOTES TO THE ACCOUNTS

		<b>2020 Fair Value £000</b>		<b>2019 Fair Value £000</b>		<b>2018 Fair Value £000</b>
Equities	17	23,783	34	56,452	32	52,727
Absolute Return Fund	13	18,158	24	40,922	25	41,111
LDI	10	13,957	22	37,610	23	38,205
Property	12	17,404	10	17,312	11	17,525
Cash	3	4,565	10	15,851	9	15,480
Buy-in policy	45	64,162	-	-	-	-
		<hr/>		<hr/>		<hr/>
	100	142,029	100	168,147	100	165,048
		<hr/>		<hr/>		<hr/>

	<b>2020 £000</b>	<b>2019 £000</b>
Total fair value of scheme assets	142,029	168,147
FRS 17 value of scheme liabilities	(113,826)	(133,273)
Impact of asset ceiling	(9,010)	(6,221)
	<hr/>	<hr/>
Gross pension asset	19,193	28,653
Related deferred tax liability	(3,647)	(4,871)
	<hr/>	<hr/>
Net pension asset	15,546	23,782
	<hr/>	<hr/>

Under FRS 102, the scheme is represented on the statement of financial position at 31 March 2020 by an asset of £19.193m (2019 - £28.653m), which amounts to £15.546m net of deferred tax (2019 - £23.782m).

The Company paid contributions at a rate of 20.6% of earnings. Members pay contributions at a rate of 5% of earnings via salary sacrifice. The Company also operates a defined contribution pension scheme. The contributions payable by the Company for the year in respect of the defined contribution scheme amounted to £334,876 (2019 - £240,016).

### **Movement in the net balance sheet position**

The FRS 102 value of scheme assets moved over the period as follows:

	<b>2020 £000</b>	<b>2019 £000</b>
Opening asset	28,653	29,872
Expense charged to profit and loss	(1,271)	(1,231)
Loss recognised outside of income statement	(9,269)	(1,170)
Employer contributions	1,080	1,182
	<hr/>	<hr/>
Closing asset	19,193	28,653
	<hr/>	<hr/>

### **Movement in present value of defined benefit obligation**

The FRS 102 value of scheme defined benefit obligation moved over the period as follows:

	<b>2020 £000</b>	<b>2019 £000</b>
Opening scheme liabilities	133,273	135,176
Employer's part of current service cost	1,944	1,993
Interest on scheme liabilities	2,996	3,312
Benefits paid	(6,071)	(5,452)
Actuarial (gain)/loss	(18,318)	(1,756)
	<hr/>	<hr/>
Closing scheme defined benefit obligation	113,826	133,273
	<hr/>	<hr/>

## NOTES TO THE ACCOUNTS

### **Movement in fair value of scheme assets**

The FRS 102 value of scheme assets moved over the period as follows:

Opening fair value of scheme assets	168,147	165,048
Interest on scheme assets	3,811	4,074
Contributions by the Company, including employee contributions under the SMART arrangement	1,080	1,182
Benefits paid	(6,071)	(5,452)
Actuarial (loss)/gain	(24,938)	3,295
	<hr/>	<hr/>
Closing fair value of scheme assets	142,029	168,147
	<hr/>	<hr/>

### **Expense recognised in Income Statement**

The following amounts have been included within operating profit:

Current service cost (employer's part only)	(1,944)	(1,993)
Total operating charge	(1,944)	(1,993)

The following amounts have been included as other finance income under FRS 102:

Interest on pension scheme assets	3,811	4,074
Interest on pension scheme defined benefit obligation	2,996	(3,312)
	<hr/>	<hr/>
Net return	672	762
	<hr/>	<hr/>
Total return recognised in the Income Statement	1,272	(1,231)
	<hr/>	<hr/>

### **Amounts recognised outside Income Statement**

The following amounts have been recognised within the Statement of Changes in Equity:

	<b>2020</b>	<b>2019</b>
	<b>£000</b>	<b>£000</b>
Actual return less interest	24,938	(3,295)
Experience gains arising on scheme defined benefit obligation	(603)	(3,083)
Loss/(gain) due to changes in assumptions	(17,713)	1,327
Change in asset limit other than interest	2,647	6,221
	<hr/>	<hr/>
Remeasurement loss/(gain) of net defined benefit asset	9,269	1,170
	<hr/>	<hr/>

The actual loss on plan assets was £21.127m in the year to 31 March 2020 (2019 - £7.369m gain).

**23. ULTIMATE CONTROLLING PARTY**

During the year, the Company's shareholders incorporated Southern Region Water Holding Limited in Hong Kong on 13 September 2019 and transferred 100% of the investment held in Anacala Fonia Holdco Limited to Southern Region Water Holding Limited.

We consider SRWHL to be the ultimate holding company and ultimate controlling entity. Consolidated group financial statement for the year ended 31 March 2020 will be prepared at the level of Anacala Fonia Holdco Limited and this will be the largest Group for which consolidated financial statements are prepared.

**24. DISPOSAL OF THE SOUTH DOWNS CAPITAL GROUP**

On 16 March 2018 the South Downs Capital Group (of which Portsmouth Water Limited is the primary trading company) was sold to funds managed by Ancala Partners LLP ("Ancala"), an infrastructure investment fund. The Group was previously owned 73% by an Employee Benefit Trust (EBT) and 27% by external shareholders (comprising former senior management and one current director).

As a result of this transaction, share options relating to the 73% EBT shareholding were issued to the trust beneficiaries at market value (the majority of current employees and certain former employees). These options were exercised immediately and the shares disposed of as part of the transaction.

External tax advice and HMRC clearance indicated that the sales proceeds, due to employees, were deemed to have arisen "by virtue of their employment" by the Group. As such these distributions were subject to PAYE and NI contributions. In order to tax effect these sale proceeds due to employees the gross consideration was paid to the Company and processed through payroll with payments being made net to employees. As such, additional employee PAYE and NIC contributions were settled out of the gross proceeds and were payable during April 2018 and 2019. These payments were structured to be made in three annual tranches in March 2018, 2019 and 2020. This resulted in a beneficial cash flow position of £8.749m (2019 - £9.020m) as at 31 March 2020 due to the timing of the receipt of proceeds for distribution and the settlement of PAYE and NIC liabilities.

It should be noted that the Company's role was merely one to distribute the proceeds and, therefore (with the exception of employer NIC and apprenticeship levy – discussed further below) no income statement charges arose on this transaction.

A further impact of the transaction and its manner of distribution was the liability arising in respect of employers NIC and apprenticeship levy. As these are payable on payroll costs, a total additional charge of £2,433,039 (2019 - £2,422,000) arose in relation to the sale proceeds paid to employees. As this could not be deducted from the employees' distribution it results in a charge to the income statement which has been treated as an exceptional cost. However, this has been compensated for by the injection of additional share capital and share premium of £2,433,039 (2019 - £2,422,000) (note 23 in ARA). This reflects part of the total purchase consideration.

**25. DISPOSAL OF THE NON-HOUSEHOLD BUSINESS**

As previously disclosed, the non-household retail business was disposed of to Castle Water Limited on 1 April 2017, the date that the non-household market opened to competition. Proceeds of £2.9m, including deferred meter reading income, was received in the previous financial year. After taking into account transaction costs a profit of £1.8m was realised. Meter reading revenue has been deferred and amortised over a period of 5 years. This is non-appointed revenue in these accounts.

**26. POST BALANCE SHEET EVENT**

On 29 May 2020 the Company extended the revolving credit facility by £5m to a total of £25m.

## SECTION 2 PRICE REVIEW AND OTHER SEGMENTAL REPORTING

### 2A SEGMENTAL INCOME STATEMENT

For the 12 months ended 31 March 2020

	Current year					Total
	Retail		Wholesale			
	Household	Non-Household	Water Resources	Water Network+	Water Total	
	£'000	£'000	£'000	£'000	£'000	£'000
Revenue - price control	4,800	0		35,939	35,939	40,739
Revenue - non-price control	0	0		661	661	661
Operating expenditure	(4,568)	0	(4,680)	(19,623)	(24,303)	(28,871)
Depreciation - tangible fixed assets	(86)	0	(293)	(5,236)	(5,529)	(5,615)
Amortisation - intangible fixed assets	(4)	0	(9)	(493)	(502)	(506)
Other operating income	(1,489)	0	0	(2,330)	(2,330)	(3,819)
Operating profit before recharges	(1,347)	0			3,936	2,589
Recharges from other segments	(218)	0	(21)	0	(21)	(239)
Recharges to other segments	0	0	0	239	239	239
<b>Operating (loss)/profit</b>	<b>(1,565)</b>	<b>0</b>			<b>4,154</b>	<b>2,589</b>

Recharges from Water Network+ to Retail and Water Resources, include a charge for the use of the Head Office Building. The market value of the rental is £332k per annum, of which 47.1% relates to Retail and 6.3% to Water Resources.

Amount of £1.489m in Other operating income, relates to COVID-19 bad debt provisions, as previously disclosed.

**2B TOTEX ANALYSIS – WHOLESALE WATER**

**For the 12 months ended 31 March 2020**

<b>£'000</b>	Water Resources	Water Network+	Water Total
<b>Operating expenditure</b>			
Power	1,010	1,551	2,561
Abstraction charges/ discharge consents	1,322	0	1,322
Bulk supply/ Bulk discharge	0	0	0
Other operating expenditure			
- Renewals expensed in year (Infrastructure)	0	2,358	2,358
- Renewals expensed in year (Non-infrastructure)	0	0	0
- Other operating expenditure excluding renewals	1,861	12,961	14,822
Local authority and Cumulo rates	487	1,775	2,262
<b>Total operating expenditure excluding third party services</b>	<b>4,680</b>	<b>18,645</b>	<b>23,325</b>
Third party services	0	978	978
<b>Total operating expenditure</b>	<b>4,680</b>	<b>19,623</b>	<b>24,303</b>
<b>Capital expenditure</b>			
Maintaining the long term capability of the assets - infra	0	2,043	2,043
Maintaining the long term capability of the assets - non-infra	984	5,477	6,461
Other capital expenditure - infra	0	1,385	1,385
Other capital expenditure - non-infra	6,664	2,976	9,640
Infrastructure network reinforcement	0	356	356
<b>Total gross capital expenditure (excluding third party)</b>	<b>7,648</b>	<b>12,237</b>	<b>19,885</b>
Third party services	0	27	27
<b>Total gross capital expenditure</b>	<b>7,648</b>	<b>12,264</b>	<b>19,912</b>
Grants and contributions	0	1,612	1,612
<b>Totex</b>	<b>12,328</b>	<b>30,275</b>	<b>42,603</b>

## 2C OPERATING COST ANALYSIS – RETAIL

For the 12 months ended 31 March 2020

£'000	Household	Non- Household	Total
<b>Operating expenditure</b>			
Customer services	1,967	0	1,967
Debt management	362	0	362
Doubtful debts	536	0	536
Meter reading	178	0	178
Services to developers	0	0	0
Other operating expenditure	1,525	0	1,525
Total operating expenditure excluding third party services	4,568	0	4,568
Third party services operating expenditure	0	0	0
Total operating expenditure	4,568	0	4,568
Depreciation - tangible fixed assets	86	0	86
Amortisation - intangible fixed assets	4	0	4
Total operating costs	4,658	0	4,658
Debt written off	1,330	0	1330

**2D HISTORIC COST ANALYSIS OF TANGIBLE FIXED ASSETS - WHOLESALE & RETAIL**

£'000	Wholesale		Retail		Total
	Water Resources	Water Network+	Household	Non-Household	
<b>Cost</b>					
At 1 April 2019	16,695	184,236	1,241	0	202,172
Impairment	0	0	0	0	0
Disposals	0	(310)	0	0	(310)
Additions	7,607	12,022	105	0	19,734
At 31 March 2020	24,302	195,948	1,346	0	221,596
<b>Depreciation</b>					
At 1 April 2019	3,874	61,234	928	0	66,036
Adjustments	0	0	0	0	0
Disposals	0	(240)	0	0	(240)
Charge for year	293	5,236	86	0	5,615
At 31 March 2020	4,167	66,230	1,014	0	71,411
Net book amount at 31 March 2020	20,135	129,718	332	0	150,185
Net book amount at 1 April 2019	12,821	123,002	313	-	136,136
<b>Depreciation charge for year</b>					
Principal Services	293	5,236	86	0	5,615
Third Party Services	0	0	0	0	0
Total	293	5,236	86	0	5,615

The net book value includes £6.0m in respect of assets in the course of construction.

2E ANALYSIS OF 'GRANTS AND CONTRIBUTIONS' AND LAND SALES - WHOLESALE

For the 12 months ended 31 March 2020

£'000	Current year			
	Fully recognised in income statement	Capitalised and amortised against depreciation	Fully netted off capex	Total
<b>Grants and contributions - water</b>				
Connection charges <sup>1</sup>	816	0	0	816
Infrastructure charge receipts	0	949	0	949
Requisitioned mains	0	663	0	663
Other Contributions (price control)	0	0	0	0
Diversions	0	0	0	0
Other Contributions (non-price control)	0	0	0	0
<b>Total</b>	<b>816</b>	<b>1,612</b>	<b>0</b>	<b>2,428</b>

Movements in capitalised grants and contributions	Current year	
	Water	Total
<b>Balance sheet</b>		
Brought forward	27,140	27,140
Capitalised in year	1,612	1,612
Amortisation (in income statement)	(709)	(709)
Carried forward	28,043	28,043

Land sales	Current year	
	Water	Total
Proceeds from disposals of protected land	0	0

<sup>1</sup> Connection Charges (s45) were included in Third Party Revenue in the Business Plan, and not Grants and Contributions.

## 2F REVENUES BY CUSTOMER TYPE

For the 12 months ended 31 March 2020

### HOUSEHOLD

	Wholesale charges revenue	Retail revenue	Total revenue	Number of customers	Average household retail revenue per customer
	£m	£m	£m	000s	£
Unmeasured water only customer	18.486	2.910	21.396	200.250	15
Measured water only customer	8.337	1.890	10.227	96.362	20
<b>Total</b>	<b>26.823</b>	<b>4.800</b>	<b>31.623</b>	<b>296.612</b>	<b>16</b>

### NON-HOUSEHOLD

Portsmouth Water has exited the non-household retail business, so Table 2G has been excluded, as per the Ofwat guidance. The Wholesale revenue for the non-household business in 2019/20 is £9,116k.

## 2I REVENUE ANALYSIS

For the 12 months ended 31 March 2020

£'000	Current year		Total
	Household	Non-Household	
<b>Wholesale charge - water</b>			
Unmeasured	18,486	266	18,752
Measured	8,337	8,850	17,187
Third party revenue	0	0	0
<b>Water Total</b>	<b>26,823</b>	<b>9,116</b>	<b>35,939</b>
<b>Wholesale Total</b>	<b>26,823</b>	<b>9,116</b>	<b>35,939</b>
<b>Retail revenue</b>			
Unmeasured	2,910	0	2,910
Measured	1,890	0	1,890
Other third party revenue	0	0	0
<b>Retail Total</b>	<b>4,800</b>	<b>0</b>	<b>4,800</b>
<b>Third party revenue - non-price control</b>			
Bulk supplies			401
Other third party revenue			211
<b>Principal Services - non-price control</b>			
Other appointed revenue			49
<b>Total appointee revenue</b>	<b>31,623</b>	<b>9,116</b>	<b>41,400</b>

	Current year	
	Water	Total
Wholesale revenue governed by price control	35,939	35,939
Grants and Contributions <sup>1</sup>	1,612	1,612
<b>Total revenue governed by wholesale price control</b>	<b>37,551</b>	<b>37,551</b>
Amount assumed in wholesale determination	37,832	37,832
Adjustment for WRFIM	(489)	(489)
<b>Total assumed revenue</b>	<b>37,343</b>	<b>37,343</b>
<b>Difference<sup>2</sup></b>	<b>208</b>	<b>208</b>

<sup>1</sup> Relevant capital contributions as defined in FD

<sup>2</sup> Narrative explanation on page 65

## 2J INFRASTRUCTURE NETWORK REINFORCEMENT COSTS

For the 12 months ended 31 March 2020

£'000	Current year	
	Network reinforcement capex	On site/site specific capex (memo only)
<b>Wholesale water network+ (treated water distribution)</b>		
Distribution and trunk mains	356	0
Pumping and storage facilities	0	0
Other	0	0
<b>Water Total</b>	356	0
<b>Wholesale Total</b>	356	0

## 2K INFRASTRUCTURE CHARGES RECONCILIATION

For the 12 months ended 31 March 2020

£'000	Current year	
	Water	Total
<b>Impact of infrastructure charge discounts</b>		
Infrastructure charges	949	949
Discounts applied to infrastructure charges	0	0
Gross Infrastructure charges	949	949
<b>Comparison of revenue and costs</b>		
Variance brought forward	1,069	1,069
Revenue	949	949
Costs	(356)	(356)
Variance carried forward	1,662	1,662

The cost of £356k for water mains network reinforcement works in 2019/20 was associated with two schemes at Haslar, Gosport and at Pook Lane, Chichester.

The variance between revenue and cost is due to the infrastructure charges being related to network reinforcement on a 5 year rolling programme. The cost of network reinforcement is not linear from year to year and is associated with the timing of specific developments. We have significant cost forecast in the next 3 years for network reinforcement works in the Barnham, Yapton and Farlington areas.

## NOTES ON THE PRICE REVIEW AND OTHER SEGMENTAL REPORTING

### RETAIL PRICE CONTROL ANALYSIS

#### Household Retail

Operating expenditure within the Household Retail price control was higher than the Business Plan assumptions by £113k, with operating costs £4,721k (including depreciation recharges), against a final determination of £4,546k.

This variance was spread over a number of different cost lines, with no significant individual cost variants.

### WHOLESALE CONTROL RECONCILIATION

REVENUE £'000	Actual	FD	Difference
Wholesale Charge:			
Household – Unmeasured	18,486	18,485	1
Household - Measured	8,337	8,193	144
Non-Household - Unmeasured	266	284	(18)
Non-Household - Measured	8,850	8,920	(70)
Total revenue from charges	35,939	35,882	57
Grants and Contributions	1,612	1,461	151
<b>TOTAL REVENUE</b>	<b>37,551</b>	<b>37,343</b>	<b>208</b>

We have compared actual revenue with that implicit in tariff setting for 2019/20, and this complied with the Final Determination.

The Wholesale revenue variance is £0.208m reflecting additional revenue from standard charges of £0.057m and more capital contributions from developers for mains of £0.151m.

The household measured wholesale revenue reflects slightly higher per property consumption than assumed. The household unmeasured wholesale revenue is in line with the FD.

The level of capital contribution is difficult to establish in advance, as it will be scheme specific. Our assumption was based on the historic five year average, and we will monitor this position going forward.

The variance of wholesale charges relative to the Final Determination is 0.2%.

The total variance of wholesale revenue relative to the Final Determination is 0.6%.

## SECTION 3 PERFORMANCE SUMMARY

### OUTCOME PERFORMANCE TABLE 3A

Row	Unique ID	Performance commitment	Unit	Unit description	Decimal places	2018-19 performance level - actual (for information)	2019-20 performance level - actual	2019-20 PCL met?	2019-20 outperformance payment or underperformance payment - in-period ODIs (indicator)	2019-20 outperformance payment or underperformance payment - ODIs payable at the end of AMP6 (indicator)	2019-20 outperformance payment or underperformance payment - ODIs payable at the end of AMP6 (indicator)	2019-20 outperformance payment or underperformance payment - ODIs payable at the end of AMP6 (indicator)
1	PR14PR TWSW_A1	A1: Bursts	nr	No. of burst mains per year	0	347	255	Yes	Outperformance payment deadband	Outperformance payment deadband		
2	PR14PR TWSW_A2	A2: Water quality standards	%	Mean zonal compliance (%)	2	99.96	99.93	No	Underperformance payment	Underperformance payment		-0.3190
3	PR14PR TWSW_A3	A3: Water quality contacts	nr	No. contacts per 1,000 population served	3	0.437	0.395	No	Underperformance payment	Underperformance payment		-0.3810
4	PR14PR TWSW_A4	A4: Temporary usage bans	nr	No. of temporary usage bans per year	0	0	0	Yes				
5	PR14PR TWSW_B1	B1: Leakage	nr	Megalitres per day (M/d)	2	28.12	23.58	Yes	Outperformance payment	Outperformance payment		0.0760
6	PR14PR TWSW_C1	C1: Interruptions to supply	time	Mins.secs per property per year	m:ins:secs	3 mins 54 secs	3 mins 22 secs	Yes	Outperformance payment	Outperformance payment		0.0730
7	PR14PR TWSW_D1	D1: Biodiversity	%	% (completion of agreed actions)	0	80	98	Yes	Underperformance payment deadband	Underperformance payment deadband		
8	PR14PR TWSW_D2	D2: Water Framework Directive (WFD)	text	Program me completion	na	n/a	n/a	Yes				
9	PR14PR TWSW_D3	D3: Carbon	%	Energy sourced from renewables (% increase)	0	> 95%	> 95%	Yes				
10	PR14PR TWSW_E1	E1: RoSPA Health and Safety accreditation	text	RoSPA Gold award	na	Awarded	Awarded	Yes				
11	PR14PR THHR_A1	A1: Service incentive mechanism (SIM)	text	Service incentive mechanism (SIM) score ranking	na	89.1	n/a	-				
12	PR14PR THHR_B1	B1: Reducing per capita consumption (PCC)	nr	Litres per head per day (l/h/d)	2	152.39	153.6	No	Underperformance payment	Underperformance payment		-0.3330
13	PR14PR THHR_C1	C1: Survey of developers	%	Satisfaction rate (%)	0	95	93	Yes				

## OUTCOME PERFORMANCE TABLE

### Introduction

Table 3A shows the performance of the Company against its 13 PR14 Outcome Delivery Incentives. The performance data has been assured by the Board of Portsmouth Water, who have engaged Jacobs to undertake an independent third party review of the data reported. This data has also been shared with our Customer Challenge Group and was discussed with the CCG on 12 May 2020.

### Background

The Company has 13 ODIs which apply for the five year period starting 1 April 2015. These were agreed as part the last Price Review, PR14. The table below classifies each ODI by division within the business, wholesale or retail and whether the ODI financial and attracts an outperformance / underperformance or is reputational in nature.

	Wholesale	Retail	Total
Financial (Table 3A)	7 (A1, A2, A3, B1, C1, D1 and D2)	2 (A1 and B1)	9
Reputational (Table 3A)	3 (A4, D3 and E1)	1 (C1)	4
<b>Total</b>	<b>10</b>	<b>3</b>	<b>13</b>

Of our 9 financial ODIs, 5 reflect performance over the 5 year period from 1 April 2015. Therefore, we have now in a position to fully quantify any outperformance or underperformance payments which will apply in the period 2020 - 25.

### 2019/20 performance

Table 3A shows the performance for each ODI in 2019/20 and quantifies any outperformance / underperformance payments which apply in the five year 2020 - 25. Looking at each of the 13 in turn:-

Bursts – at 255, the number of bursts in 2019/20 was below the annual target of 342. This ODI is judged over a five year period, with the average for the five years being 292. This means the performance lies in the deadband, with neither out or under-performance applying.

Water quality standards, as measured by Mean Zonal Compliance – at 99.93% MZC was below our annual target of 100.00% and below the 99.95% threshold for an under performance payment to be made. This is the third time we have incurred such a penalty in the AMP6 period. The annual penalty is £0.319m resulting in a total payment of £0.957m over the 5 years.

Water quality contacts – at 0.395 we have outperformed our annual target of 0.412 contacts per 1,000 population. However, this ODI is judged over the five year period ending March 2020, with the average of the five years being 0.523. The 5 year penalty is £1.903m.

Temporary Usage Bans – the Company did not need to introduce restrictions on customer usage. This is a reputational ODI.

Leakage – at 23.6 MI/d we have significantly outperformed our 2019/20 target of 29.8MI/d. This ODI is judged over a five year period, with the average for the five years being 28.6MI/d. This means that an outperformance payment of £0.076m applies.

Interruptions to Supply – at 3 mins 22 secs per property we have significantly outperformed our 2019/20 target of 6 mins. This ODI is judged over a five year period, with the average for the five years being 3 mins 48 secs. This means that an outperformance payment of £0.073m applies.

Biodiversity – at 98% of agreed plans completed in the AMP period we have exceeded our target of 90%. No underperformance payment therefore applies.

Water Framework Directive – our agreed water resources NEP programme was completed and signed off by the EA in March 2018. No under or out performance payments apply as this was the agreed date for the programme.

Carbon – almost all of the energy we purchase is from a renewable source. This reputational ODI has been delivered relative to our target of 10% by the end of March 2020.

Health & Safety – we have been awarded the RoSPA accreditation for the 15 year in a row. This is a reputational ODI which has been achieved.

Service Incentive Mechanism – there is not a formal SIM score for 2019/20. It will be replaced by C-Mex from April 2020. However, at Ofwat's instruction we have used trial year values from the C-Mex survey to establish a proxy-SIM score, which is reported in Table 3D.

Reducing per capita consumption – at 153.6 l/h/d we have failed this ODI. An underperformance payment of £0.333m applies.

Survey of Developers – our result of 93% exceeds our target of 70%. This is a reputational ODI which has been achieved.

Our full ODI report will be published on our website by 15 July 2020.

### 3C AIM (Abstraction Incentive Mechanism)

For the 12 months ended 31 March 2020

Abstraction Site	AIM Performance MI	Normalised AIM Performance MI	Cumulative AIM Performance 2018/19 onwards	Cumulative Normalised AIM Performance 2018/19	Contextual information relating to AIM Performance
Northbrook	0	0	0	0	-

The abstraction incentive mechanism (AIM) has the objective of encouraging water companies to reduce the environmental impact of abstracting water at environmentally sensitive sites during defined periods of low surface water flows. The AIM aims to help to improve the resilience of water supply and ensure that it is provided in a more sustainable way (Guidelines on the abstraction incentive mechanism, Ofwat, 2016).

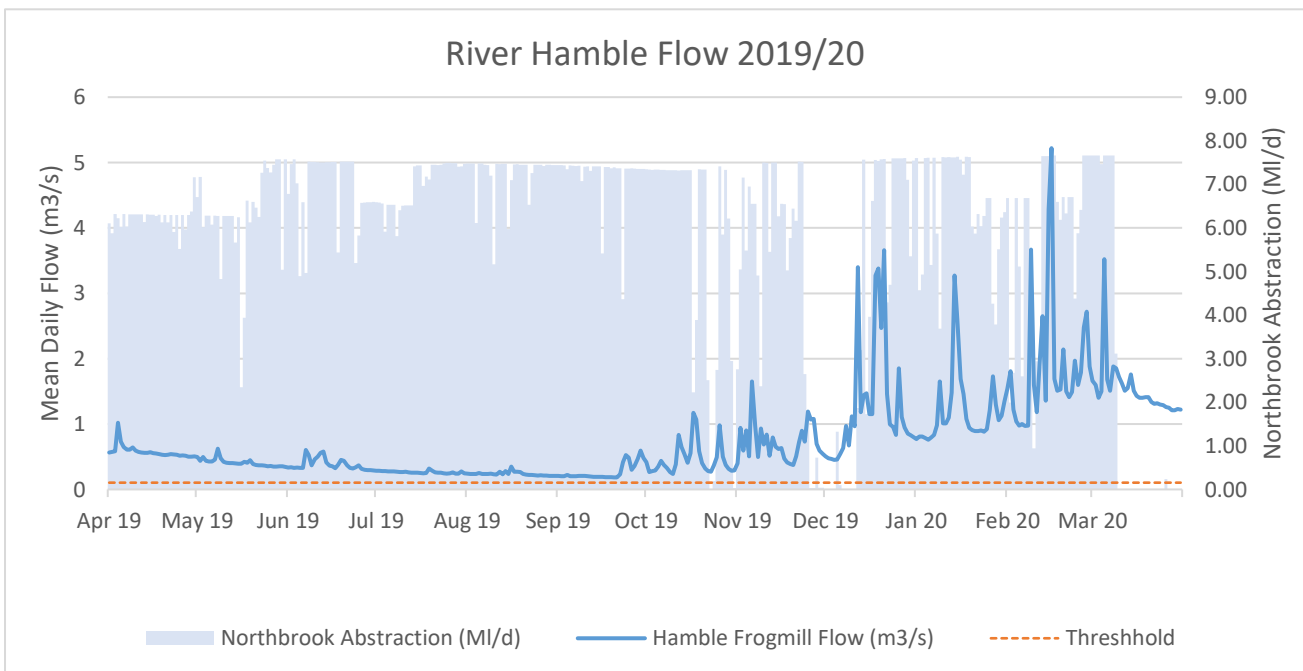
Northbrook is the only Portsmouth Water site remaining in the Abstraction Incentive Mechanism (AIM) as it is deemed to impact on flows on the River Hamble.

In 2017/18 Portsmouth Water completed an NEP (Natural Environment Program) scheme designed to improve water quality on the River Hamble. It is possible that future enhancement schemes may still take place for the River Hamble, although this is still subject to review.

The AIM minimum flow target for the River Hamble is 0.104 m<sup>3</sup>/second and is represented by the orange line in the figure below. This target is based on Q95 flows and recent actual abstraction from the period 2007 to 2014.

During 2019/20 the low flow trigger was not passed in any day, as measured at Frogmill, and therefore annual reporting is zero. The lowest recorded flow was 0.184 m<sup>3</sup> / second on 20 September 2019.

The graph below also shows, on the right hand axis, the abstraction rate from Northbrook over the year. Although we have an annual licence of 20.5MI/d we took no more than 8 MI/d, as there is a long term issue with a pump at this site. Had the river level fallen below the trigger level AIM would have required us to reduce abstraction at Northbrook to the target value of 18.8 MI/d.



**3D SIM (Service Incentive Mechanism) SCORE TABLE**

**For the 12 months ended 31 March 2020**

	Units	Decimal places	Score
<b>Qualitative Performance</b>			
1st Survey Score	nr	2	4.35
2nd Survey Score	nr	2	4.36
3rd Survey Score	nr	2	4.55
4th Survey Score	nr	2	4.48
Qualitative SIM Score (out of 75)	nr	2	64.31
Total Contact Score	nr	2	12.93
<b>Quantitative Performance</b>			
Quantitative SIM Score (out of 25)	nr	2	20.69
Total Annual SIM score (out of 100)	nr	2	85.00

**Performance commitment: Service incentive mechanism**

At PR14 Ofwat used a methodology for measuring customer service known as the Service Incentive Mechanism (SIM). In the PR19 Final Determination published by Ofwat, we received the highest SIM reward in the industry for our performance in the four years up to and including 2018/19.

For the period 2020-25 this measure has been replaced by a new measure called C-Mex and 2019/20 is a trial year for C-Mex. However, Ofwat have asked companies to report a SIM value for 2019/20, based on the C-Mex survey results and revisions to the quantitative components. This is called the proxy SIM. SIM seeks to measure the quality of service provided by companies to household customers only and is measured by two elements:

**Quantitative** - measured by:

- The total number of written complaints
- The number of escalated written complaints
- The number of CCWater investigations where a complaint was not resolved by a company

The number of unwanted telephone contacts is not required for this proxy SIM.

**Qualitative** - measures how satisfied customers are with the quality of service they receive based on a survey of customers who have had direct contact with their water company.

The table below compares performance for 2019/20 with 2018/19.

SIM Scores	Multiplier	2018/19		2019/20	
		Number	Score	Number	Score
Unwanted Phone Contacts	1	12,988	12,988	n/a	n/a
Written Complaints	5	294	1,470	309	1,545
Escalated Written Complaints	100	18	1,800	24	2,400
CCWater Investigated	1,000	0	0	0	0
			<b>16,258</b>		<b>3,945</b>
Connected Properties year end			303,208		305,957
<b>Quantitative SIM Score</b>			<b>22.3</b>		<b>20.7</b>
<b>Qualitative Measure</b>		<b>4.56</b>	<b>66.8</b>	<b>4.43</b>	<b>64.3</b>
<b>Total SIM Score</b>			<b>89.1</b>		<b>85.0</b>

The exclusion in unwanted calls from this new proxy SIM resulted in a change in the weightings of the Quantitative SIM score, and thus the two are not directly comparable. The importance is our relative position in the industry, which we will not know until July 2020.

## C-MEX AND D-MEX SCORE TABLES

**For the 12 months ended 31 March 2020**

### **C-MeX**

The customer measure of experience (C-MeX) is a mechanism to incentivise water companies to provide an excellent customer experience for residential customers, across both the retail and wholesale parts of the value chain.

C-MeX will run in 2019-20, the shadow year, prior to the 2020-2025 period when financial performance payments apply. C-MeX is comprised of two survey elements:-

- Customer Experience survey – a customer satisfaction survey amongst a random sample of the water company’s customers; and
- Customer Service survey – a customer satisfaction survey amongst a random sample of those who have contacted their water company.

The two surveys are weighted equally.

The table below shows the details of our quarterly performance on C-Mex for 2019/20. With the annual assessment being 84.35%.

%	Q1	Q2	Q3	Q4	2019/20
Customer Experience	83.43	86.51	83.04	82.25	83.81
Customer Service	83.04	83.96	86.74	85.85	84.90
<b>Total</b>	<b>83.24</b>	<b>85.24</b>	<b>84.89</b>	<b>84.05</b>	<b>84.35</b>

We await the publication of all companies’ performance to determine where we rank within the industry for C-Mex for 2019/20.

### **D-MeX**

The developer services measure of experience (D-MeX) is a mechanism to incentivise water companies to provide an excellent customer experience for developer services (new connections) customers.

These customers include small and large property developers, self-lay providers (SLPs), and those with new appointments and variations (NAVs).

D-MeX will run in 2019-20, the shadow year, prior to the 2020-2025 period when financial performance payments apply.

The D-MeX score for any water company is a weighted sum of the quantitative Water UK metrics and qualitative customer satisfaction survey results. The two elements are weighted equally.

The table below shows the details of our quarterly performance on D-Mex for 2019/20, with the annual assessment being 87.81%.

%	Q1	Q2	Q3	Q4	2019/20
Customer satisfaction	75.00	79.81	76.81	80.59	78.05
Level of Service	94.58	99.33	96.44	99.91	97.57
<b>Total</b>	<b>84.79</b>	<b>89.57</b>	<b>86.63</b>	<b>90.25</b>	<b>87.81</b>

We await the publication of all companies’ performance to determine where we rank within the industry for D-Mex for 2019/20.

## 3S SHADOW REPORTING OF NEW DEFINITION LEAKAGE AND SUPPLY INTERRUPTION DATA

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For the 12 months ended 31 March 2020

This schedule has been published alongside the Annual Performance Report.

## SECTION 4 ADDITIONAL REGULATORY INFORMATION

### 4A NON-FINANCIAL INFORMATION

For the 12 months ended 31 March 2020

<b>Retail - Household</b>	Current year	
	Unmeasured	Measured
Number of void households ('000s)	5.789	2.002
Per capita consumption (excluding supply pipe leakage) l/h/d	163.3	127.9

<b>Wholesale</b>	Current year Water
<b>Wholesale Volume (MI/d)</b>	
Bulk supply export	5.16
Bulk supply import	0.00
Distribution input	169.7

#### 4B WHOLESALE TOTEX ANALYSIS

	Current year	Cumulative 2015-2020
£m	Water	Water
<b>Actual Totex</b>	42.603	167.234
<b>Less: Items excluded from the menu</b>		
Third party costs	1.005	4.976
Pension deficit recovery payments	0.000	0.000
*Other 'Rule Book' adjustments	0.684	2.440
<b>Total costs excluded from the menu</b>	<b>1.689</b>	<b>7.416</b>
**Transition expenditure	(5.028)	(5.028)
<b>Adjusted Actual totex</b>	<b>35.886</b>	<b>154.790</b>
<b>Adjusted Actual totex - base year prices</b>	<b>30.210</b>	<b>137.520</b>
<b>Allowed totex based on final menu choice - base year prices</b>	<b>26.083</b>	<b>137.697</b>
<b>Variance - base year prices</b>	<b>(4.127)</b>	<b>0.177</b>

\* Wholesale share of FRS102 pension charges

\*\* Transition expenditure was capped at £5.4m in the Final Determination, in outturn prices.

#### TOTEX MENU VARIANCE ANALYSIS

In the Final Determination, the allowed expenditure from the totex menu is £30.976m, in 2019/20 prices. This menu position gives a variance to actual totex in the year of -£4.910m (-£4.127m in 2012/13 prices). The following table shows this variance for each element of totex.

2019/20 Prices	Allowed Menu Totex 2019/20	Actual 2019/20	Variance 2019/20
Operating Expenditure	18,698	20,283	(1,585)
Renewals	6,206	4,372	1,834
Capital Expenditure	7,528	12,843	(5,315)
Grants and Contributions	(1,456)	(1,612)	156
<b>WHOLESALE TOTEX</b>	<b>30,976</b>	<b>35,886</b>	<b>(4,910)</b>

## WHOLESALE TOTEX ANALYSIS

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### Operating Expenditure

Actual performance is adverse to the Final Determination by £1.585m. In the year, there were a number of one-off items of expenditure including the following:

- Additional costs in relation to leakage recover activity of £1.2m. This is for external contract staff to deliver additional leak detection and to increase the quantity of free repairs for customers. In addition, new connections are being carried out by contract labour and not PWL labour, as they are doing additional leak repairs.
- Higher shared services costs of £0.3m, mainly due to an increase in insurance, audit fees and other professional fees.
- Higher electricity costs than expected of £0.4m.

### Renewals

The renewals expenditure for the year was less than the Business Plan by £1.834m. This was due to the following:

- Activity in the year was less than expected, with 15km of pipe being renewed, compared to 22km in the Business Plan.
- Lower prices from the contractor and new installation technology. We have achieved 73% no-dig installations, which has the impact of reducing the amount of material required to reinstate roads after the work is completed.
- Increased amount capitalised in the year, amounting to 55% of the programme, due to the nature of the programmes undertaken.

### Capital Expenditure

Capital expenditure is higher than the Business Plan by £5.315m. There have been significant savings in the AMP, largely due to efficiencies in the renewals programme. These efficiencies have now been reinvested in additional capital schemes that were not included in the Business Plan. The significant variances are as follows:

- A number of capital schemes were completed earlier than expected and consequently a number of schemes were delayed until the final 2 years of the AMP. In particular, a large programme of work relating to Water Quality Contact Time was started in 2018/19, and completed in 2019/20. This amounted to an additional £0.795m in 2019/20. The scope of the Water Quality Contact Time work was also extended, resulting in additional spend of £1.166m.
- Eels screens were purchased in 2019/20, but were not included in the Business Plan. This amounted to £1.555m in the year.
- New mains expenditure was £1.741m, compared to £0.800m in the Business Plan. This is additional expenditure of £0.941m.
- Small Plant and vehicles expenditure was £400k higher than the Business Plan.
- Optional metering expenditure was lower than the Business plan by £629k
- There were a number of schemes not included in the Final Determination but completed in 2019/20, including ones relating to Treatment Works, Pump Stations and Boreholes.

Havant Thicket Winter Storage project work, although not in the Final Determination, continued in 2019/20 and amounted to £5.028m. This is classed as transition expenditure in 2019/20 and is excluded from the Totex menu reconciliation.

**4C IMPACT OF AMP PERFORMANCE TO DATE ON RCV**

<b>£m</b>	<b>Year to Date</b>
Cumulative totex over/underspend so far in the price control period (average 2012/13 prices)	0.177
Customer share of cumulative totex over/underspend	0.087
RCV element of cumulative totex over/underspend (in March 2020 prices)	0.051
Adjustment for ODI outperformance payment or underperformance payment	0.000
*RCV determined at FD at 31 March 2020	154.826
<b>Projected 'shadow' RCV</b>	<b>154.877</b>

The Final Determination average PAYG% is 75.7%.  
Therefore, the % of Totex underspend that adjusts the RCV is 24.3%.

The Ofwat template for Table 4C includes a line for the customer share of the totex over/underspend. However, in the Business Plan legacy Totex Menu Model for PR14, the cost sharing rate is not applied to the RCV. This line is for additional information only and does not impact the Projected 'shadow' RCV.

None of the ODI payments will impact the RCV, all of these will be made to the future allowed revenue.

\*RCV published by Ofwat, in March 2020 prices.

**4D WHOLESALE TOTEX ANALYSIS - WATER**

**For the 12 months ended 31 March 2020**

£'000	Water resources		Network +				Total
	Abstraction licences	Raw water abstraction	Raw water transport	<sup>1</sup> Raw water storage	Water treatment	Treated water distribution	
<b>Operating expenditure</b>							
Power	0	1,010	0	0	83	1,468	2,561
Abstraction charges/ discharge consents	1,322	0	0	0	0	0	1,322
Bulk supply	0	0	0	0	0	0	0
Other operating expenditure							
- Renewals expensed in year (infrastructure)	0	0	0	0	0	2,358	2,358
- Renewals expensed in year (Non-infra)	0	0	0	0	0	0	0
- Other operating expenditure excluding renewals	0	1,861	0	50	3,099	9,812	14,822
Local authority and Cumulo rates	0	487	0	12	1,192	571	2,262
<b>Total operating expenditure excluding third party services</b>	<b>1,322</b>	<b>3,358</b>	<b>0</b>	<b>62</b>	<b>4,374</b>	<b>14,209</b>	<b>23,325</b>
Third party services	0	0	0	0	0	978	978
<b>Total operating expenditure</b>	<b>1,322</b>	<b>3,358</b>	<b>0</b>	<b>62</b>	<b>4,374</b>	<b>15,187</b>	<b>24,303</b>
<b>Capital expenditure</b>							
Maintaining the long term capability of the assets - infra	0	0	0	0	0	2,043	2,043
Maintaining the long term capability of the assets - non-infra	0	984	0	1	3,228	2,248	6,461
Other capital expenditure - infra	0	0	0	0	0	1,385	1,385
Other capital expenditure - non-infra	0	6,664	0	0	1,838	1,138	9,640
Infrastructure network reinforcement	0	0	0	0	0	356	356
<b>Total gross capital expenditure (excluding third party)</b>	<b>0</b>	<b>7,648</b>	<b>0</b>	<b>1</b>	<b>5,066</b>	<b>7,170</b>	<b>19,885</b>
Third party services	0	0	0	0	0	27	27
<b>Total gross capital expenditure</b>	<b>0</b>	<b>7,648</b>	<b>0</b>	<b>1</b>	<b>5,066</b>	<b>7,197</b>	<b>19,912</b>
Grants and contributions						(1,612)	(1,612)
<b>Totex</b>	<b>1,322</b>	<b>11,006</b>	<b>0</b>	<b>63</b>	<b>9,440</b>	<b>20,772</b>	<b>42,603</b>
<b>Cash expenditure</b>							
Pension deficit recovery payments	0	0	0	0	0	0	0
Other cash items	0	0	0	0	0	0	0
<b>Totex including cash items</b>	<b>1,322</b>	<b>11,006</b>	<b>0</b>	<b>63</b>	<b>9,440</b>	<b>20,772</b>	<b>42,603</b>
<b>Unit cost information (operating expenditure)</b>							
	Licensed volume available	Volume abstracted	Volume transported	<sup>1</sup> Average volume stored	Distribution input volume	Distribution input volume	
Volume (Ml)	119,807	66,228	62,116	49,410	62,116	62,116	
Unit cost (£/Ml)	11.03	50.70	-	1.25	70.42	244.49	
Population	731,061	731,061	731,061	731,061	731,061	731,061	
Unit cost (£/pop)	1.81	4.59	-	0.08	5.98	20.77	

<sup>1</sup> The Company does not have any raw water storage reservoirs, with the exception of one facility at the River Itchen, which allows for 3 days of maximum abstraction from the river.

**4F COST ANALYSIS – HOUSEHOLD RETAIL**

**For the 12 months ended 31 March 2020**

£'000	Household Unmeasured	Household Measured	Total
	Water only	Water only	
<b>Operating expenditure</b>			
Customer services	1,151	816	1,967
Debt management	303	59	362
Doubtful debts	368	168	536
Meter reading	0	178	178
Other operating expenditure	1,029	496	1,525
<b>Total operating expenditure</b>	2,851	1,717	4,568
Depreciation - tangible fixed assets			
- on assets existing at 31 March 2015	28	14	42
- on assets acquired since 1 April 2015	30	14	44
Amortisation - intangible fixed assets			
- on assets existing at 31 March 2015	0	0	0
- on assets acquired since 1 April 2015	3	1	4
<b>Total operating costs</b>	2,912	1,746	4,658
<b>Capital Expenditure</b>	100	48	148

**Other operating expenditure includes the net retail expenditure for the following retail activities which are part funded by wholesale**

**Household**

Demand-side water efficiency - gross expenditure	
Demand-side water efficiency - expenditure funded by wholesale	0
Demand-side water efficiency - net retail expenditure	0
Customer-side leak repairs - gross expenditure	
Customer-side leak repairs - expenditure funded by wholesale	0
Customer-side leak repairs - net retail expenditure	0

**4G WHOLESALE CURRENT COST FINANCIAL PERFORMANCE  
INCOME STATEMENT**

For the 12 months ended 31 March 2020

£'000	Note	Water	Total
<b>Revenue</b>		36,600	36,600
Operating expenditure		(24,303)	(24,303)
Capital maintenance charges	1	(9,201)	(9,201)
Other operating income		(2,330)	(2,330)
<b>Current cost operating profit</b>		766	766
Other income		1,525	1,525
Interest income		1,062	1,062
Interest expense		(7,296)	(7,296)
Other Interest expense		672	672
<b>Current Cost Profit before tax and fair value movements</b>		(3,271)	(3,271)
Fair value gains/(losses) on financial instruments		0	0
<b>Current Cost Profit before tax</b>		(3,271)	(3,271)

## NOTES ON THE WHOLESALE CURRENT COST FINANCIAL PERFORMANCE

### 1. CAPITAL MAINTENANCE CHARGES

The Capital Maintenance charges of £9,201 include the Wholesale amount of the Current Cost Depreciation £7.436m and the Infrastructure Renewals Charge of £1.765m.

#### Current Cost Depreciation

	Operational Assets	Infrastructure Assets	Other Tangible Assets	Total
<b>GROSS REPLACEMENT COSTS</b>				
At 1st April 2019	276,243	1,126,532	28,294	1,431,068
RPI Adjustment	7,267	29,637	737	37,642
Disposals		(93)	(217)	(310)
Additions	13,470	3,784	2,806	20,060
At 31st March 2020	<b>296,980</b>	<b>1,159,860</b>	<b>31,620</b>	<b>1,488,460</b>
<b>DEPRECIATION</b>				
At 1st April 2019	136,899	-	19,755	156,654
RPI Adjustment	3,601		514	4,115
Disposals during year			(215)	(215)
Charge for year	4,551		3,012	7,563
At 31st March 2020	<b>145,051</b>	-	<b>23,066</b>	<b>168,117</b>
<b>NET BOOK VALUE</b>				
At 31st March 2020	<b>151,929</b>	<b>1,159,860</b>	<b>8,554</b>	<b>1,320,343</b>
At 1st April 2019	139,344	1,126,532	8,539	1,274,415
<b>DEPRECIATION</b>				
WHOLESALE	4,551	-	2,885	<b>7,436</b>
RETAIL	-	-	127	<b>127</b>
	<b>4,551</b>	-	<b>3,012</b>	<b>7,563</b>

#### Infrastructure Renewals Charge

##### Estimation of Infrastructure Renewals Charge at 2019/20 prices

	<b>£'000</b>
Actual expenditure 2019/20	2,014
Budget 2020/21	1,773
Business Plan 2021/22 - 2033/34	1,745
Average Cost over 15 years	<u><u>1,765</u></u>

The infrastructure renewals charge represents the average non-expensed infrastructure spend over 15 years.

## 4H FINANCIAL METRICS

For the 12 months ended 31 March 2020

Financial Indicators	Units	Current	AMP to
		year	date
		Metric	Metric
Net debt	£m	110.648	
Regulated equity	£m	44.178	
*Regulated gearing	%	71.47	
Post tax return on regulated equity	%	-3.72	
RORE (return on regulated equity)	%	-2.04	3.45
Dividend yield	%	5.44	
Retail profit margin - Household	%	0.45	
Retail profit margin - Non-Household	%	0.00	
**Credit rating	n/a	BBB	
Return on RCV	%	2.48	
Dividend cover	dec	-1.44	
Funds from operations (FFO)	£m	7.283	
Interest cover (cash)	dec	2.69	
Adjusted interest cover (cash)	dec	1.23	
FFO/Debt	dec	0.07	
Effective tax rate	%	0.00	
Free cash flow (RCF)	£m	3.744	
RCF/capex	dec	0.22	

Revenue and earnings		
Revenue (actual)	£m	40.739
EBITDA (actual)	£m	11.868

Movement in RORE			
Base Return	%	5.70	5.77
Totex out/(under) performance	%	-4.34	-0.73
Retail cost out/(under) performance	%	-0.25	-0.70
ODI out/(under) performance	%	0	0.00
Financing out/(under) performance	%	-1.03	-1.02
Other factors (exceptional item)	%	-2.12	0.13
Regulatory return for the year	%	-2.04	3.45

Borrowings		
Proportion of borrowings which are fixed rate	%	0.60
Proportion of borrowings which are floating rate	%	15.24
Proportion of borrowings which are index linked	%	84.16
Proportion of borrowings due within 1 year or less	%	15.64
Proportion of borrowings due in more than 1 year but no more than 2 years	%	0
Proportion of borrowings due in more than 2 years but no more than 5 years	%	0
Proportion of borrowings due in more than 5 years but no more than 20 years	%	84.16
Proportion of borrowings due in more than 20 years	%	0.20

\* As explained in note 24 and Table 1E, year-end cash balances include atypical cash of £9.020m. This has been excluded for the purpose of calculating gearing and this adjusted gearing figure has been used in other calculations to ensure consistency.

\*\* S&P rating of BBB has a negative watch status

## COMMENTARY ON THE RORE FINANCIAL METRIC

### RORE MOVEMENTS COMPARED TO BASE RORE SET AT PR14

RORE metrics were set at the last price review, for each of the 5 years of the AMP.

2015/16	FD RORE 5.88%	
2016/17	FD RORE 5.87%	
2017/18	FD RORE 5.70%	(Adjusted from 5.86%, to remove non-household business)
2018/19	FD RORE 5.70%	(Adjusted from 5.85%, to remove non-household business)
2019/20	FD RORE 5.70%	(Adjusted from 5.85%, to remove non-household business)

Adjustments have been made to these metrics, to reflect the actual results in each year.

2015/16	Adjusted RORE 4.01%	
2016/17	Adjusted RORE 3.97%	
2017/18	Adjusted RORE 5.30%	(8.14% including exceptional gain on disposal of NHH)
2018/19	Adjusted RORE 3.37%	
2019/20	Adjusted RORE 0.07%	(-2.04% including exceptional COVID bad debt provision)

The average RORE for the 5 years of the AMP is 3.45% (including exceptional items)

2012/13 PRICES	2015/16	2016/17	2017/18	2018/19	2019/20	AMP	
NET INCOME – Final Determination	2.644	2.680	2.667	2.713	2.734	13.438	Used to calculate FD RORE %'s
TOTEX PAYG adjustments	0.419	0.189	0.532	(0.674)	(2.516)	(2.050)	75.7% of TOTEX in each year
Retail cost adjustments	(0.613)	(0.701)	(0.466)	(0.076)	(0.147)	(2.003)	
ODI adjustment	(0.298)		0.281			(0.017)	Provision for ODI reversed in 2017/18
Exceptional items			1.641		(1.254)	0.387	NHH business and COVID bad debt
Depreciation adjustment	0.005	0.005	0.013	(0.016)	(0.061)	(0.055)	Based on run-off rate of 3.8%
Interest adjustment	(0.569)	(0.578)	(0.592)	(0.603)	(0.608)	(2.950)	Based on real cost of debt of 3.6%
Tax on adjustments	0.211	0.217	(0.268)	0.260	0.871	1.292	Tax rate of 19%
<b>NET INCOME - Adjusted</b>	<b>1.799</b>	<b>1.812</b>	<b>3.808</b>	<b>1.604</b>	<b>(0.981)</b>	<b>8.042</b>	Used to calculate adjusted RORE %'s
<b>REGULATED EQUITY</b>	<b>44.930</b>	<b>45.623</b>	<b>46.757</b>	<b>47.631</b>	<b>47.976</b>	<b>232.917</b>	
<b>Adjusted RORE</b>	<b>4.01%</b>	<b>3.97%</b>	<b>8.14%</b>	<b>3.37%</b>	<b>(2.04%)</b>	<b>3.45%</b>	

#### Revenue Adjustment and Gain on Disposal

Due to the sale of the Non-Household Retail business, there is no longer any associated Retail profit. These amounts have been deducted from the Final Determination net income each year, from 2017/18. In addition, there is an exceptional gain on disposal in 2017/18 of £1.641m. The overall impact of this transaction is £1.569m, and this equates to +2.68% on the 2017/18 RORE.

#### Totex PAYG Adjustments

These reflect favourable Wholesale totex variances, adjusted for timing differences. The PAYG amounts are calculated using the average PAYG in the Final Determination.

Of these amounts, 75.7% is PAYG opex and 24.3% is added to the RCV and depreciated at a run-off rate of 3.8%. There is also a cost-sharing arrangement for the Totex over-performance of 50.7%. The favourable variances relate mainly to savings in the renewals programme as a result of the appointment of a new contractor and improved technology. The adverse variances in the final 2 years reflect the additional expenditure on leakage recovery.

An exceptional bad debt provision for COVID-19 has been included in the 2019/20 calculations.

#### Retail Operating Cost Adjustments

Retail costs are broadly in line with the FD, with no material variances to report.

#### ODI Adjustments

A penalty was accrued for in 2015/16 of £0.281m, relating to water quality failures. This amount was reversed in 2017/18 following accounting advice from our auditors.

#### Interest Cost Adjustments

These reflect the higher actual cost of debt as compared to the Final Determination of 2.84%. The actual cost of debt is 3.6% and this is applied to the notional level of net debt. The difference between this and the interest allowed in the FD is used to adjust the RORE metric. These adjustments are shown in the table above.

4J ATYPICAL AND NON-ATYPICAL EXPENDITURE BY BUSINESS UNIT – WHOLESALE WATER

For the 12 months ended 31 March 2020

£'000	Water resources		Network +				Total
	Abstraction licences	Raw water abstraction	Raw water transport	<sup>1</sup> Raw water storage	Water treatment	Treated water distribution	
<b>Operating expenditure (exclu. atypicals)</b>							
Power	0	1,010	0	0	83	1,468	2,561
Abstraction charges/ discharge consents	1,322	0	0	0	0	0	1,322
Bulk supply	0	0	0	0	0	0	0
Other operating expenditure							
- Renewals expensed in year (infrastructure)	0	0	0	0	0	2,358	2,358
- Renewals expensed in year (Non-infrastructure)	0	0	0	0	0	0	0
- Other operating expenditure excluding renewals	0	1,861	0	50	3,099	9,812	14,822
Local authority and Cumulative rates	0	487	0	12	1,192	571	2,262
<b>Total operating expenditure excluding third party services</b>	<b>1,322</b>	<b>3,358</b>	<b>0</b>	<b>62</b>	<b>4,374</b>	<b>14,209</b>	<b>23,325</b>
Third party services	0	0	0	0	0	978	978
<b>Total operating expenditure</b>	<b>1,322</b>	<b>3,358</b>	<b>0</b>	<b>62</b>	<b>4,374</b>	<b>15,187</b>	<b>24,303</b>
<b>Capital expenditure (excl. atypicals)</b>							
Maintaining the long term capability of the assets - infra	0	0	0	0	0	2,043	2,043
Maintaining the long term capability of the assets - non-infra	0	984	0	1	3,228	2,248	6,461
Other capital expenditure - infra	0	0	0	0	0	1,385	1,385
Other capital expenditure - non-infra	0	6,664	0	0	1,838	1,138	9,640
Infrastructure network reinforcement	0	0	0	0	0	356	356
<b>Total gross capital expenditure (excluding third party)</b>	<b>0</b>	<b>7,648</b>	<b>0</b>	<b>1</b>	<b>5,066</b>	<b>7,170</b>	<b>19,885</b>
Third party services	0	0	0	0	0	27	27
<b>Total gross capital expenditure</b>	<b>0</b>	<b>7,648</b>	<b>0</b>	<b>1</b>	<b>5,066</b>	<b>7,197</b>	<b>19,912</b>
Grants and contributions						(1,612)	(1,612)
<b>Totex</b>	<b>1,322</b>	<b>11,006</b>	<b>0</b>	<b>63</b>	<b>9,440</b>	<b>20,772</b>	<b>42,603</b>
<b>Cash expenditure (exclu. atypicals)</b>							
Pension deficit recovery payments	0	0	0	0	0	0	0
Other cash items	0	0	0	0	0	0	0
<b>Totex including cash items</b>	<b>1,322</b>	<b>11,006</b>	<b>0</b>	<b>63</b>	<b>9,440</b>	<b>20,772</b>	<b>42,603</b>
<b>Atypical expenditure</b>							
							0
							0
							0
<b>Total atypical expenditure</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total expenditure</b>	<b>1,322</b>	<b>11,006</b>	<b>0</b>	<b>63</b>	<b>9,440</b>	<b>20,772</b>	<b>42,603</b>

**4L ENHANCEMENT CAPITAL EXPENDITURE BY PURPOSE – WHOLESALE WATER**

**For the 12 months ended 31 March 2020**

£'000	Expenditure in report year						Total
	Water resources		Network +			Total	
	Abstraction licences	Raw water abstraction	Raw water transport	<sup>1</sup> Raw water storage	Water treatment		
<b>Enhancement capital expenditure by purpose</b>							
NEP - Making ecological improvements at abstractions (Habitats Directive, SSSI, NERC, BAPs)							0
NEP - Eels Regulations (measures at intakes)							0
NEP - Invasive Non-Native Species							0
Addressing low pressure							0
Improving taste/ odour/ colour							0
Meeting lead standards							0
Supply side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Supply side enhancements to the supply/demand balance (dry year annual average conditions)		5,028					5,028
Demand side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Demand side enhancements to the supply/demand balance (dry year annual average conditions)							0
New developments						1,741	1,741
New connections element of new development (CPs, meters)							0
Investment to address raw water deterioration (THM, nitrates, Crypto, pesticides, others)					1,622		1,622
Resilience							0
SEMD		47			189		236
NEP - Drinking Water Protected Areas (schemes)							0
NEP - Water Framework Directive measure		1,555					1,555
NEP - Investigations		28					28
Improvements to river flows		33					33
Metering (excluding cost of providing metering to new service connections) - meters requested by optants						685	685
Metering (excluding cost of providing metering to new service connections) - meters introduced by companies							0
Metering (excluding cost of providing metering to new service connections) - other							0
Boundary Boxes						453	453
							0
							0
<b>Total enhancement capital expenditure</b>	0	6,691	0	0	1,811	2,879	11,381

4L ENHANCEMENT CAPITAL EXPENDITURE BY PURPOSE – WHOLESALE WATER (continued)

For the 12 months ended 31 March 2020

£'000	Cumulative expenditure on schemes completed in report year						Total
	Water resources		Network +			Total	
	Abstraction licences	Raw water abstraction	Raw water transport	<sup>1</sup> Raw water storage	Water treatment		
<b>Enhancement capital expenditure by purpose</b>							
NEP - Making ecological improvements at abstractions (Habitats Directive, SSSI, NERC, BAPs)							0
NEP - Eels Regulations (measures at intakes)							0
NEP - Invasive Non-Native Species							0
Addressing low pressure							0
Improving taste/ odour/ colour							0
Meeting lead standards							0
Supply side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Supply side enhancements to the supply/demand balance (dry year annual average conditions)							0
Demand side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Demand side enhancements to the supply/demand balance (dry year annual average conditions)							0
New developments						1,741	1,741
New connections element of new development (CPs, meters)							0
Investment to address raw water deterioration (THM, nitrates, Crypto, pesticides, others)					1,622		1,622
Resilience							0
SEVID	47				189		236
NEP - Drinking Water Protected Areas (schemes)							0
NEP - Water Framework Directive measure	1,555						1,555
NEP - Investigations	28						28
Improvements to river flows	33						33
Metering (excluding cost of providing metering to new service connections) - meters requested by optants						685	685
Metering (excluding cost of providing metering to new service connections) - meters introduced by companies							0
Metering (excluding cost of providing metering to new service connections) - other							0
Boundary Boxes						453	453
							0
							0
<b>Total enhancement capital expenditure</b>	1,663	0	0	0	1,811	2,879	6,353

**4P NON-FINANCIAL DATA FOR WR, WT AND WD – WHOLESALE WATER**

**For the 12 months ended 31 March 2020**

<b>Water Resources</b>	<b>Units</b>	<b>Input</b>
Proportion of distribution input derived from impounding reservoirs	Propn 0 to 1	0
Proportion of distribution input derived from pumped storage reservoirs	Propn 0 to 1	0
Proportion of distribution input derived from river abstractions	Propn 0 to 1	0.161
Proportion of distribution input derived from groundwater works, excluding managed aquifer recharge (MAR) water supply schemes	Propn 0 to 1	0.839
Proportion of distribution input derived from artificial recharge (AR) water supply schemes	Propn 0 to 1	0
Proportion of distribution input derived from aquifer storage and recovery (ASR) water supply	Propn 0 to 1	0
Number of impounding reservoirs	nr	0
Number of pumped storage reservoirs	nr	0
Number of river abstractions	nr	1
Number of groundwater works excluding managed aquifer recharge (MAR) water supply schemes	nr	20
Number of artificial recharge (AR) water supply schemes	nr	0
Number of aquifer storage and recovery (ASR) water supply schemes	nr	0
Total number of sources	nr	21
Total number of water reservoirs	nr	1
Total capacity of water reservoirs	MI	135
Total number of intake and source pumping stations	nr	21
Total number of raw water transfer stations	nr	0
Total capacity of intake and source pumping stations	kW	6459
Total capacity of raw water transfer pumping stations	kW	0
Total length of raw water mains and conveyors	km	25.39
Average pumping head – resources	m.hd	27.38
Average pumping head – raw water transport	m.hd	0
Total length of raw and pre-treated (non-potable) water transport mains	km	0
Water resources capacity (measured using water resources yield)	MI/d	226.5
<b>Water Treatment</b>		
Total water treated at all SW simple disinfection works	MI/d	0
Total water treated at all SW1 works	MI/d	0
Total water treated at all SW2 works	MI/d	0
Total water treated at all SW3 works	MI/d	0
Total water treated at all SW4 works	MI/d	0
Total water treated at all SW5 works	MI/d	28.54
Total water treated at all SW6 works	MI/d	0
Total water treated at all GW simple disinfection works	MI/d	53.71
Total water treated at all GW1 works	MI/d	0
Total water treated at all GW2 works	MI/d	10.37
Total water treated at all GW3 works	MI/d	0
Total water treated at all GW4 works	MI/d	85.00
Total water treated at all GW5 works	MI/d	0
Total water treated at all GW6 works	MI/d	0
Total water treated at more than one type of works	MI/d	0
Total number of SW simple disinfection works	nr	0
Total number of SW1 works	nr	0
Total number of SW2 works	nr	0
Total number of SW3 works	nr	0
Total number of SW4 works	nr	0
Total number of SW5 works	nr	1
Total number of SW6 works	nr	0
Total number of GW simple disinfection works	nr	13
Total number of GW1 works	nr	0
Total number of GW2 works	nr	1
Total number of GW3 works	nr	0
Total number of GW4 works	nr	6
Total number of GW5 works	nr	0
Total number of GW6 works	nr	0
Number of treatment works requiring remedial action because of raw water deterioration	nr	0
Zonal population receiving water treated with orthophosphate	000's	643.408
Average pumping head – treatment	m.hd	2.14

4P NON-FINANCIAL DATA FOR WR, WT AND WD – WHOLESale WATER (continued)

For the 12 months ended 31 March 2020

<b>Water Distribution</b>	<b>Units</b>	<b>Input</b>
Total length of potable mains as at 31 March	km	3358.6
Total length of mains relined	km	0
Total length of mains renewed	km	14.99
Total length of new mains	km	19.4
Potable water mains (<320mm)	km	2999.3
Potable water mains 320mm - 450mm	km	150.2
Potable water mains 450mm - 610mm	km	149.8
Potable water mains > 610mm	km	59.3
Capacity of booster pumping stations	kW	3482
Capacity of service reservoirs	MI	484
Capacity of water towers	MI	0
Distribution input	MI/d	169.72
Water delivered (non-potable)	MI/d	0
Water delivered (potable)	MI/d	151.56
Water delivered (billed measured residential)	MI/d	27.15
Water delivered (billed measured business)	MI/d	32.32
Total Leakage	MI/d	23.58
Distribution losses	MI/d	15.04
Water taken unbilled	MI/d	2.62
Number of lead communication pipes	nr	80704
Number of galvanised iron communication pipes	nr	17983
Number of other communication pipes	nr	211324
Number of booster pumping stations	nr	26
Total number of service reservoirs	nr	30
Number of water towers	nr	0
Total length of mains laid or structurally refurbished pre-1880	km	77.6
Total length of mains laid or structurally refurbished between 1881 and 1900	km	88.1
Total length of mains laid or structurally refurbished between 1901 and 1920	km	161.1
Total length of mains laid or structurally refurbished between 1921 and 1940	km	364.9
Total length of mains laid or structurally refurbished between 1941 and 1960	km	419.2
Total length of mains laid or structurally refurbished between 1961 and 1980	km	866.1
Total length of mains laid or structurally refurbished between 1981 and 2000	km	793.7
Total length of mains laid or structurally refurbished post 2001	km	587.9
Average pumping head – distribution	m.hd	36.84
<b>Band Disclosure (nr)</b>		
WTW's in size band 1	nr	6
WTW's in size band 2	nr	4
WTW's in size band 3	nr	4
WTW's in size band 4	nr	4
WTW's in size band 5	nr	2
WTW's in size band 6	nr	1
<b>Band Disclosure (%)</b>		
Proportion of Total DI band 1	%	0.6
Proportion of Total DI band 2	%	7
Proportion of Total DI band 3	%	13.5
Proportion of Total DI band 4	%	22.2
Proportion of Total DI band 5	%	25.6
Proportion of Total DI band 6	%	31.1

**4Q NON-FINANCIAL DATA – PROPERTIES, POPULATION AND OTHER – WHOLESALE WATER**

**For the 12 months ended 31 March 2020**

<b>Properties and Population</b>	<b>Units</b>	<b>Input</b>
Residential properties billed for measured w ater (external meter)	000s	73.675
Residential properties billed for measured w ater (not external meter)	000s	22.687
Business properties billed measured w ater	000s	14.128
Residential properties billed for unmeasured w ater	000s	200.25
Business properties billed unmeasured w ater	000s	1.946
Total business connected properties at year end	000s	16.077
Total residential connected properties at year end	000s	305.597
Total connected properties at year end	000s	321.674
Number of residential meters renew ed	000s	4.461
Number of business meters renew ed	000s	0.352
Number of meters installed at request of optants	000s	2.322
Number of selective meters installed	000s	0
Total number of new business connections	000s	0.146
Total number of new residential connections	000s	2.199
Total population served	000s	735.029
Number of business meters (billed properties)	000s	17.041
Number of residential meters (billed properties)	000s	100.186
Company area	km <sup>2</sup>	686
<b>Other</b>		
Number of lead communication pipes replaced for w ater quality	nr	6
Total supply side enhancements to the supply demand balance (dry year critical/ peak conditions)	M/d	0
Total supply side enhancements to the supply demand balance (dry year annual average conditio	M/d	0
Total demand side enhancements to the supply demand balance (dry year critical/ peak condition	M/d	0
Total demand side enhancements to the supply demand balance (dry year annual average conditio	M/d	0
Energy consumption - netw ork plus	MWh	14
Energy consumption - w ater resources	MWh	11
Energy consumption - w holesale	MWh	25
Mean zonal compliance	%	99.93%
Compliance Risk Index (published by DWI by mid-July)	nr	
Event Risk Index	nr	157.80
*Volume of leakage above or below the sustainable economic level	M/d	-7.820

\*SELL=31.4 M/d

#### 4V OPERATING COST ANALYSIS – WATER RESOURCES

For the 12 months ended 31 March 2020

£'000	Impounding Reservoir	Pumped Storage	River Abstractions	Groundwater, exclu. MAR water supply schemes	Artificial Recharge (AR) water supply schemes	Aquifer Storage and Recovery (ASR) water	Other	Total
<b>Operating expenditure</b>								
Power	0	0	114	896	0	0	0	1,010
Abstraction charges/discharge consents	0	0	237	1,085	0	0	0	1,322
Bulk supply	0	0	0	0	0	0	0	0
Other operating expenditure	0	0	0	0	0	0	0	0
Renewals expensed in year (Infrastructure)	0	0	0	0	0	0	0	0
Renewals expensed in year (Non-Infrastructure)	0	0	0	0	0	0	0	0
Other direct operating expenditure	0	0	11	243	0	0	0	254
Other indirect operating expenditure	0	0	0	1,607	0	0	0	1,607
Total functional expenditure	0	0	362	3,831	.	0	0	4,193
Local authority and Cumulo rates	0	0	0	487	0	0	0	487
Total operating expenditure (excluding 3rd party)	0	0	362	4,318	0	0	0	4,680
Depreciation	0	0	0	302	0	0	0	302
Total operating costs (excluding 3rd party)	0	0	362	4,620	0	0	0	4,982

#### OTHER EXPENDITURE – WHOLESALE WATER

For the 12 months ended 31 March 2020

£'000	Water Resources	Raw Water Distribution	Water Treatment	Treated Water Distribution	Total
<b>Other Expenditure</b>					
Employment costs - directly allocated	22	7	558	2,937	3,524
Employment costs - indirectly allocated	937	0	1,377	2,203	4,517
Number FTEs - directly allocated	1	0	14	66	81
Number FTEs - indirectly allocated	17	0	25	40	82
*Costs associated with Traffic Management Act	0	0	0	192	192
<b>Service Charges</b>					
Canal & River Trust abstraction charges/ discharge consents	0	0	0	0	0
Environment Agency abstraction charges/ discharge consents	1,322	0	0	0	1,322
Other abstraction charges/ discharge consents	0	0	0	0	0
Statutory water softening	0	0	0	0	0

\*These costs include the cost of permits as well as staff time for administration.

## DISCLOSURE OF TRANSACTIONS WITH ASSOCIATES

The transactions required to be disclosed under Condition F of the Company's Instrument of Appointment are set out below:

### Borrowings or Sums Lent

There is a loan outstanding made to a Group Company, South Downs Limited, in June 2002. The balance of the loan, consisting of the principal amount and accrued interest to date, amounts to £55.484m. No repayment was made by South Downs Limited in the year, or in the previous year. This loan was made as a part of the refinancing package which was carried out in the financial year 2002/03. The interest rate for the loan is based on LIBOR plus a margin.

An amount of £0.500m was lent to Portsmouth Water Ltd from Ancala Bidco Ltd. This loan has subsequently been repaid. Interest was charged at 3 month LIBOR plus a margin of 1%.

### Interest Received

A receipt of interest amounting to £1,134,735 in respect of the inter-company loan made to South Downs Limited in 2002 (as covered above) was received from South Downs Limited.

### Dividends paid to Associated Undertakings

The dividends paid to the holding company, Portsmouth Water Holdings Limited, are shown in note 9 on page 36 of this Annual Performance Report. The dividend policy is also covered within this note. However, in response to the current COVID-19 pandemic and related financial uncertainty, no final dividend is proposed for the year ended 31 March 2020. This will be reviewed again carefully at a later date.

### Payments for Tax Losses

During the year Portsmouth Water made no payments to group companies relating to the surrender of tax losses to Portsmouth Water.

### Supply of Services

Details of services supplied to the Appointee by associates during the year are disclosed below.

Service	Associate Company	Turnover of Associate (£000's)	Terms of Supply	Value (£000's)
Rent of operational sites	Brockhampton Holdings Limited	289*	Market Tested	0
Solar power income			Market Tested	16

\*Brockhampton Holdings Limited accounts do not include any amounts classified as turnover. Amounts relating to rent and solar power income are included within other operating income which totals £289k of which £157k relates to total rental income and £132k relates to total income from solar power.

### Directors Remuneration

There is a recharge of Directors salaries amounting to £26,862 paid to Portsmouth Water Limited by Brockhampton Holdings Limited, which represents the time spent by Portsmouth Water Executive Directors on Group matters. There is also a recharge into the following entities relating to administrative time spent on Group matters:

Brockhampton Pension Scheme	£26,496
Brockhampton Holdings Ltd	£25,432
Brockhampton Property	£25,432
South Downs Ltd	£5,717
South Downs Capital Ltd	£2,973
Ancala Mid Co	£3,201
Ancala Bid Co	£3,201
Ancala Hold Co	£3,201

### Statement by Board of Directors

To the best of their knowledge, the Directors of the Company declare that all appropriate transactions with associated companies have been disclosed.

### Price Control Units

Portsmouth Water has closely followed the Ofwat guidance for the allocation of costs and assets between price control units. It believes that the only cross subsidy between them is the cost associated with the Head Office building. The market for rental in the local area has been studied in the past year, as part of a project to establish the options for the future leasing/purchase of a new Head Office building. An estimate of the annual leasing cost is £332k, and this has been allocated to the Retail and Water Resources business units on the basis of actual floor space.

## REPORT OF THE INDEPENDENT AUDITOR

### Independent Auditor's report to the Water Services Regulation Authority (the WSRA) and the Directors of Portsmouth Water Limited

#### Opinion

We have audited the sections of/tables within Portsmouth Water's Annual Performance Report for the year ended 31 March 2020 ("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), the net debt analysis (table 1E), the financial flows (table 1F) 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 and wastewater (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 grants and 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), the infrastructure charges reconciliation (table 2K) and the related notes.

We have not audited the Outcome performance table (tables 3A to 3S) and the additional regulatory information in tables 4A to 4W.

In our opinion, Portsmouth Water's Regulatory Accounting Statements have been prepared, in all material aspects, in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA (RAG 1.08, RAG 2.07, RAG 3.11, RAG 4.08 and RAG 5.07) and the accounting policies (including the Company's published accounting methodology statement(s), as defined in RAG 3.11, appendix 2]), set out on page 41.

#### 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 Auditors' responsibilities for the audit of the Regulatory Accounting Statements within the Annual Performance Report section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit, including the Financial Reporting Council's (FRC'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 a special purpose framework, Condition F, the Regulatory Accounting Guidelines, the accounting policies (including the Company's published accounting methodology statement, as defined in RAG 3.11, 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. In addition, we are not required to assess whether the methods of cost allocation set out in the accounting methodology statement are appropriate to the circumstances of the Company or whether they meet the requirements of the WSRA.

The Regulatory Accounting Statements are separate from the statutory financial statements of the Company and has 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.

The Regulatory Accounting Statements on pages 28 to 31 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 Responsibilities for the audit of the Regulatory Accounting Statements section below. As a result, the Regulatory Accounting Statements may not be suitable for another purpose.

## REPORT OF THE INDEPENDENT AUDITOR

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Our opinion is not modified in respect of this matter.

### 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 where:

- the directors' use of the going concern basis of accounting in the preparation of 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.

### Other information

The other information comprises all of the information in the Annual Performance Report other than the Regulatory Accounting Statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the Regulatory Accounting 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 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 of the other information, we are required to report that fact.

We have nothing to report based on these responsibilities.

### Responsibilities of the Directors for the Annual Performance Report

As explained more fully in the Statement of Directors' Responsibilities set out on pages 23-27, the directors are responsible for the preparation of the Annual Performance Report 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(s), as defined in RAG 3.11, appendix 2).

The directors are also responsible for such internal control as they determine is necessary to enable the preparation of the Annual Performance Report that is free from material misstatement, whether due to fraud or error.

In preparing the Annual Performance Report, 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.

### Auditors' responsibilities for the Audit of the Regulatory Accounting Statements within the Annual Performance Report

Our objectives are to obtain reasonable assurance about whether the Regulatory Accounting Statements are free from material misstatement, whether due to fraud or error, and to issue an auditors' 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 Financial Reporting Council's website at <https://www.frc.org.uk/auditors/audit-assurance/auditor-s-responsibilities-for-theaudit-of-the-fi/description-of-the-auditor%E2%80%99s-responsibilities-for>. This description forms part of our auditor's report, except for the following:

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. In addition, we are not required to assess whether the methods of cost allocation set out in the accounting methodology statement are appropriate to the circumstances of the Company or whether they meet the requirements of the WSRA.

## REPORT OF THE INDEPENDENT AUDITOR

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We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

### 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 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 is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2020 on which we reported on 11 June 2020, 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.

### James Ledward

For and on behalf of KPMG LLP

*Chartered Accountants*

Gateway House

Tollgate

Chandlers Ford

SO53 3TG

25<sup>th</sup> June 2020