Greensands Holdings Limited

Annual Report and Financial statements for the year ended 31 March 2021

Contents

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44 Esplanade
St Helier
Jersey
JE4 9WG

Registered no. JE98700

Introduction

Greensands Holdings Limited ('GSH' or 'the company') is the ultimate parent company of Southern Water Services Limited (Southern Water) and all other group companies disclosed in note 37, with no minority interests.

The only operating company in the Group is Southern Water and the information contained in this Strategic Report is therefore mainly based upon the activities of this company. This information is fully supported by GSH and has been adopted from the Southern Water Annual Report which is published on the Southern Water website. Sections 1 and 2 that follow contain reviews of GSH and Southern Water for the year to 31 March 2021, respectively.

1) Greensands Holdings Limited

Strategic Report:

The Business

GSH acts as a holding company, with the only trading subsidiary being Southern Water.

This section sets out the financial performance and structure of the Group as well as the corporate governance in place at GSH. A summary of the activities, performance and key risks relating to Southern Water is described in section 2 from page 18.

Group financial performance

Accounting policies

The accounting policies of the Group, including any changes in accounting policies in the year, are set out on pages 55 to 67.

Consolidated income statement

The group's income statement is summarised in Table 1 below.

Table 1	Years ended 31 March	
	2021	2020
	£m	£m
Revenue	**784.2**	878.0
Amortisation of regulatory settlement payments	**35.6**	-
Total revenue	**819.8**	878.0
Other operating income	**1.7**	1.4
Operating costs before regulatory settlement	**(369.4)**	(376.9)
Trade receivables impairment charge	**(34.8)**	(29.6)
Depreciation, net of amortisation	**(293.0)**	(271.3)
Operating profit before regulatory settlement	**124.3**	201.6
Profit on disposal of fixed assets	**0.8**	0.9
Profit before interest and tax	**125.1**	202.5
Net finance costs	**(290.8)**	(342.0)
Fair value (losses)/gains on derivative financial instruments	**(456.6)**	349.4
(Loss)/Profit before tax	**(622.3)**	209.9
Tax credit/charge	**67.6**	(106.5)
(Loss)/Profit for the financial year	**(554.7)**	103.4

Operating profit largely reflects the trading results of Southern Water for the year and additional depreciation from the revaluation of assets on acquisition.

Revenue

Revenue before the regulatory settlement decreased to £784.2 million (2020: £878.0 million). This decrease in revenue was expected and principally results from the changes to Southern Water's inflation-linked water and wastewater tariffs which were agreed as part of its Business Plan for 2020–25. Southern Water's revenues were also affected by COVID-19 which reduced the level of trade effluent and developer income it received. as well as reducing its main water and wastewater income.

As a result of COVID-19 , it experienced a significant change in the mix of that revenue between household and non-household customers.

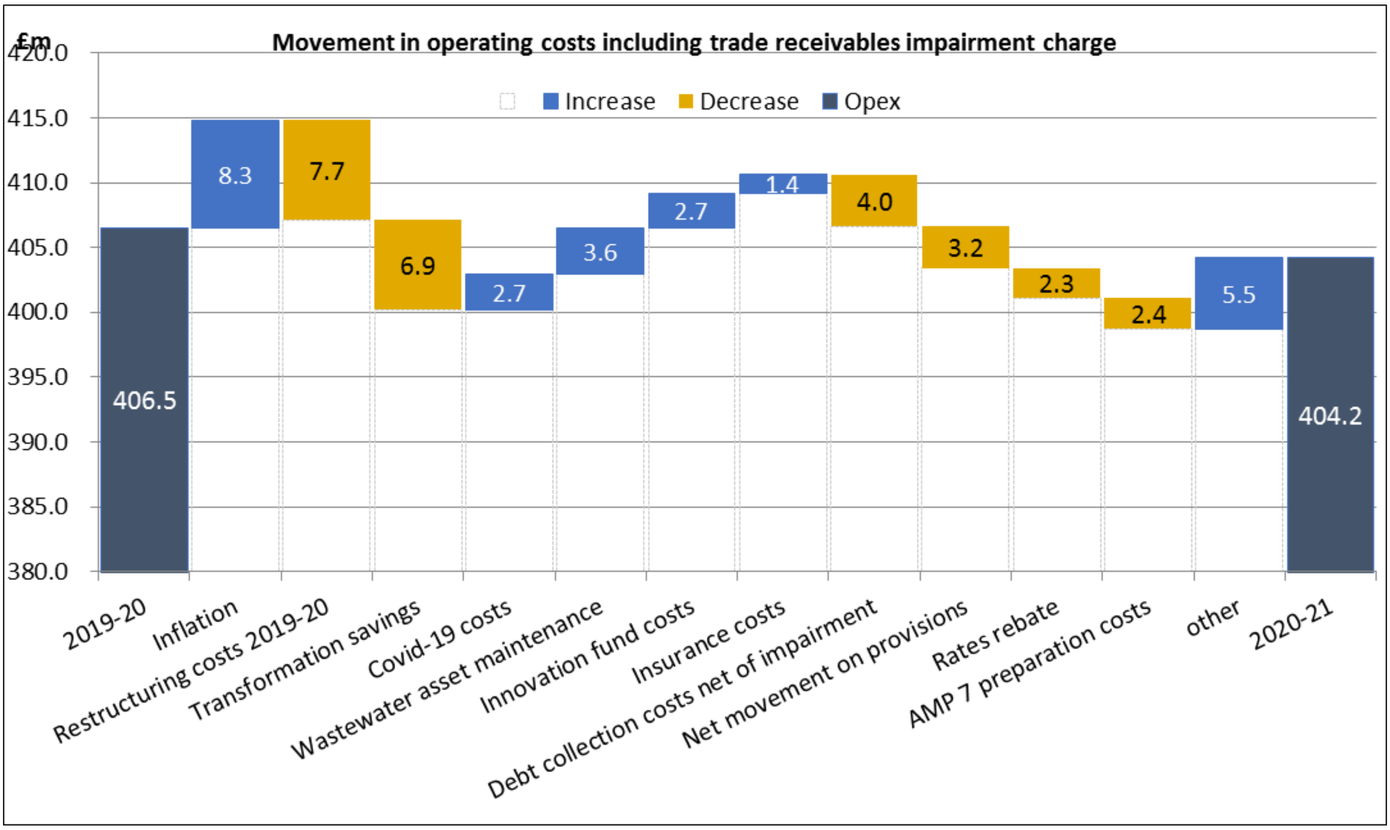
The national lockdown resulted in a large increase in household demand, with many customers spending more time at home. As a result, Southern Water's household revenues for 2020–21 were £22.2 million above expectations. The increased household revenue was offset by a similar reduction in non-household revenue, resulting from the restrictions on businesses, which was £30.8 million below expectations.

In 2018–19 Southern Water made provision for rebates, based on its regulatory settlement with Ofwat, to be provided to customers over the period from 2020–25. These rebates are now included within the company's tariffs and so part of the revenue reported in the income statement. The provision made in 2018–19 for these rebates is being released in line with the tariff adjustment over the same period.

An analysis of revenue is provided in note 5 to the financial statements.

Operating costs and trade receivables impairment charge

Operating costs including the impairment charge against trade receivables for the year decreased by £2.3 million from £406.5 million to £404.2 million. This decrease is explained in the chart below:



In order to prepare for the challenge of this five-year period, improve its services and reduce costs, Southern Water undertook a number of restructuring activities during 2019–20. These included transferring the majority of its customer services activities to Capita, closing the company's final salary pension scheme and reshaping a number of teams across the business. As a result, Southern Water incurred a number of one-off restructuring costs, totalling £7.7 million in the prior year.

These transformation activities resulted in a reduction of £6.9 million in its ongoing operating costs for 2020–21 as a result of lower employee and pension costs.

Over the course of the year Southern Water have experienced a number of cost increases the most notable of these being:

- The impact of COVID-19 – excluding the impact on debt collection, the net impact of COVID-19 was £2.7 million. This increase largely resulted from additional costs to ensure the health and safety of employees and contractors and facilitate remote working for its office-based staff, the treatment and water supply costs to meet the significant increase in customer demand for water, in particular during the first lockdown in May, and support for its supply chain to cover additional operating costs as well as extended vehicle hire costs. These increases were partly offset by some cost reductions most notably regarding travel and expenses as well as the deferment of some training activities.
- Wastewater asset maintenance – Southern Water increased maintenance expenditure on its wastewater assets by £3.6 million in order to improve its wastewater operational performance and reduce the risk of equipment failures.
- Innovation fund costs – for the current five year regulatory period, Ofwat introduced an Innovation Fund to drive innovation across the water industry through a series of competitions to select projects to progress. There is an allowance within the revenues Southern Water collect from customers for the cost of this fund and this income is ring-fenced for use on the schemes selected as part through the competition. Its operating costs for 2020–21 include a provision of £2.7 million for the liability for its contribution to the fund.
- Insurance costs – during 2020–21 Southern Water have experienced an increase in insurance premium costs of £0.6 million together with higher insurance losses, following a higher number of claims, of £0.8 million.
- Other costs – largely reflect those of the Group (£5 million) and are costs associated with external specialist advisors engaged to assess available options in order to financially restructure the Greensands Group.

The impact of these cost increases has been offset by a number of cost reductions:

- Debt collection costs – In response to COVID-19 and in order to support customers in financial hardship as a result of the pandemic Southern Water suspended its debt collection activities during the year which resulted in lower debt collection costs of £9.0 million. These savings were offset by an increase in its overall provision for impairment of £5.0 million, reflecting the fact that the likely recovery of debt that has reached the end of the recovery process has worsened and the impact of the pandemic on its outstanding debt.
- Provisions – As reported in its Annual Report last year, Southern Water made provisions in 2019–20 of £3.0 million for historic guaranteed standards of service (GSS) payments for missed appointments and £1.0 million in relation to the charges presented by the Environment Agency to the court regarding historic wastewater performance. No additional provisions were made for these matters during 2020–21 resulting in a reduction in operating costs of £4.0 million offset by an increase of £0.8 million to the environmental provision held in respect of work to improve the resilience of the Rivers Test and Itchen in Hampshire for periods of severe drought. Further details regarding the Environment Agency investigation can be found on page 21 and in note 27 to the accounts.
- Rates rebate – following a successful appeal Southern Water received a net reduction in its Business Rates charges of £2.3 million
- AMP7 preparation costs – during the prior year Southern Water incurred costs in relation to its business plan submission to Ofwat and its preparations for delivering its plans for this regulatory period. As a result its operating costs fell by £2.4 million for this year.

Depreciation and amortisation

Depreciation and amortisation increased to £293.0 million (2020: £271.3 million) as a result of the completion and commissioning of a large number of its capital investment schemes. The most significant of these were its new wastewater treatment works at Woolston which increased depreciation by £4.0 million and a number of short life IT and system related assets which added over £4.0 million.

Operating profit

As a result, operating profit decreased to £124.3 million (2020: £201.6 million), a 38% reduction, the majority of which relates to the reduction in Southern Water's revenues that were agreed as part of its Business Plan for 2020–25.

Financing costs and profit before tax

Net finance costs decreased by £51.2 million to £290.8 million (2020: £342.0 million). This reduction is largely driven by the refinancing activities undertaken in the prior year which have resulted in a reduction in net interest payable of £55.7 million offset by an increase in Eurobond interest in Greensands Europe of £17.7 million. There was also lower indexation on our index-linked debt of £8.8 million and a lower financing charge associated with Southern Water's pension deficit of £2.9 million.

The fair value loss on our derivative financial instruments amounted to £456.6 million (2020: gain £349.4 million). The primary driver for changes in the valuation is the fluctuation in UK Government bond yields which are used to discount the future cash flows. As Government gilt yields are constantly moving the valuation of derivative instruments can be volatile, this is particularly evident over the past year, largely as a result of the pandemic, and the gain experienced at March 2020 has reversed as markets have recovered. These changes do not represent immediate cash flows.

The loss before tax for the year amounted to £622.3 million (2020:£209.9 million profit).

Taxation

We have recognised a total tax credit to the income statement of £67.6 million (2020: £106.5 million tax charge). This differs from the credit that may be expected of £118.2 million, based on the loss before tax of £622.3 million and the current period tax rate of 19%, as described in note 11 and is due to differences between the accounting and taxation treatment of transactions.

Cash flow statement

Overall, cash and cash equivalents increased in 2020–21 by £134.7 million (2020: £232.3 million decrease). This movement of £367.0 million principally results from the refinancing activities that Southern Water undertook during the year. Further details of the year-on-year movements are provided below.

	Years ended 31 March			
	2021 £m	2020 £m	Movement £m	Explanation
Net interest related transactions	**(272.9)**	(295.3)	22.4	In total, the net cash outflow in relation to interest decreased by £22.4 million. The principal reasons were as follows. A payment of £194.5 million was made in the 2020–21 (2020: nil) in relation to accrued indexation on our index-linked loans. This payment was offset by lower net interest payable in the year, following the refinancing activities completed in 2019–20 of £109.7 million. In 2019–20 net interest payments also included interest of £107.2 million in relation to 2018–19 as the 31 March 2019 fell on a weekend.
Net movement on borrowings	**411.0**	(80.8)	491.8	During the year we made loan and credit facility repayments totalling £696.2 million (2020: £642.8 million); these were offset by proceeds from new bonds issued under our Sustainable Finance Framework in May 2020 and March 2021 totalling £1,107.2 million (2020: £562.0 million).
Payments on restructure of derivative instruments	**-**	140.0	(140.0)	During 2019 we restructured the cash flows associated with an existing financial instrument, which brought forward a cash receipt of £140.0 million at present value.
Other	**(3.4)**	3.8	(7.2)	The net cash movement from operating activities and our capital investment programme. A reduction in cash received from operations, resulting from the reduction in our revenues was offset by lower capital expenditure.
	134.7	(232.3)		

Consolidated statement of financial position

	31 March 2021 £m	31 March 2020 £m
Non-current assets	6,952.7	6,825.7
Current assets (excluding cash)	198.3	217.6
Cash and cash equivalents	417.2	282.5
Total assets	7,568.2	7,325.8
Current liabilities	(418.8)	(1,084.4)
Non-current liabilities	(8,810.3)	(7,290.9)
Total liabilities	(9,229.1)	(8,375.3)
Total net assets	(1,660.9)	(1,049.5)
Total equity	(1,660.9)	(1,049.5)

At the end of the year to 31 March 2021, we had non-current assets of £6,952.7 million (2020: £6,825.7 million), an increase of £127.0 million from March 2020. This increase results from Southern Water's ongoing capital investment programme which, after depreciation, increased the value of property plant and equipment and intangible assets by £137.2 million. In addition Southern Water recognised an intangible asset of £124.6 million for the future right to a bulk supply of water associated with a new reservoir at Havant Thicket which is being constructed by Portsmouth Water. These increases in asset values were offset by a decrease in the value of non-current financial derivative assets of £134.8 million.

Current assets decreased to £198.3 million (2020: £217.6 million). Following the reduction in Southern Water's tariff, which reduced revenues, there was a reduction in accrued income as well as a higher level of provision made against outstanding historic gross receivables. The combined impact of these was a reduction in the value of net receivables by £22.4 million.

Current liabilities decreased to £418.8 million (2020: £1,084.4 million). This is mainly caused by loans of £679.5 million which were repaid during the year.

At 31 March 2021, non-current liabilities totalled £8,810.3 million (2020: £7,290.9 million). This increase of £1,519.4 million was principally the result of the following:

- An increase in borrowings of £1,317.1 million largely as a result of new bonds issued under Southern Water's Sustainable Financing Framework of £1,107.7 million and an increase in the Eurobond debt of £168.2 million.
- An increase in the derivative financial instrument liability of £127.3 million.
- An decrease in the deferred tax liability of £80.9 million as a result of the loss recorded for the year and the increase in the retirement benefit obligation.
- An increase in retirement benefit obligations of £54.0 million. The final salary pension scheme was closed to future accrual on 31 March 2020 During the year a lump sum deficit payment of £17.5 million was made but this was offset by the movement in market conditions at 31 March 2021 which increased the deficit by £70.0 million together with past service and financing costs of £1.5 million.
- The transfer of £24.3 million of the regulatory settlement provision to short-term liabilities.
- The recognition of a liability totalling £124.6 million for future capacity charge payments, to be made to Portsmouth Water in relation to the Havant Thicket reservoir scheme, mentioned above, over the period to 2100.

Overall, net liabilities increased from £1,049.5.5 million to £1,660.9 million.

Dividend policy

The detail of the dividend policy for the group is determined by the dividend policy of Southern Water.

Any dividend paid by Southern Water is firstly used to pay interest on borrowings outside of Southern Water and surplus cash is then used to pay interest on the Eurobonds and/or a shareholder dividend.

Dividend policy of Southern Water:

Southern Water's dividend policy is formulated to ensure a fair balance of reward between customers and investors. To deliver on its vision for the successful delivery of its business plan for 2020–25, all stakeholders must share in success: customers benefiting through enhanced service and lower bills, and shareholders earning a fair return on the near £2 billion of equity invested.

When proposing payment of a dividend, the directors of Southern Water Services Limited, acting independently in accordance with their directors' duties and in accordance with the company's licence, will apply the following principles:

1. Determination of a base level of dividend, based on an equity return consistent with our most recent Final Determination and its actual level of gearing. This recognises Southern Water's management of economic risks and capital employed.
2. In assessing any adjustment to the base level of dividend, the company will take into account all aspects of its performance. This would reflect its overall financial performance as compared to the final business plan as agreed by Ofwat and would explicitly consider a qualitative assessment of customer service levels and how customers share in its successes.
3. Southern Water will consider its financial resilience ahead of any dividend decision and whether any financial outperformance should be reinvested to benefit customers. This consideration will include taking into account the interests of its employees, other stakeholders, and the company's pension schemes.

   Southern Water's dividend policy is intended to support the financial resilience and investment grade credit ratings of the business and ensure continued access to diversified sources of finance. As part of step three, Southern Water carry out an assessment of:

   a. headroom under debt covenants
   b. the impact on the company's credit rating
   c. the liquidity position and ability to fulfil licence conditions
   d. key areas of business risk.
4. It will be transparent in the payment of dividends and will clearly justify the payment in relation to the factors outlined above.
5. Southern Water will publish its dividend policy annually (as part of the Annual Report) and highlight any changes.

These tests have not been applied to the interim dividends of £4.0 million paid in 2020–21 to Southern Water Services Group (SWSG) as this dividend payment is instantly offset by a corresponding interest receipt from SWSG and is therefore immediately repaid to the company in a 'dividend loop' resulting in no net cash outflow for the company. The dividends to enable SWSG to pay the interest for the second half of 2020–21 have not yet been approved. This interest has been accrued in the Southern Water Services financial statements at March 2021.

The Southern Water Board has resolved that the company will not pay dividends, other than those associated with the 'dividend loop' mentioned above, until it is clear that to do so would not be detrimental to the company's financial position.

The Southern Water Board has not approved the payment of preference share dividends for 2020–21 (2020: £9.0 million dividends and £50.1 million redemption). Preference share dividends are disclosed as interest in the financial statements and an accrual for £4.9 million in relation to this liability is included within the Southern Water financial statements.

No dividend has been proposed or paid by GSH in the period or subsequently.

Group Tax Policy

The Group's Tax Policy is consistent with the overall values and corporate strategy of the Group and considers financial risk, reputational risk, and social responsibilities. The Group's approach to tax planning is to align to business decisions made in the best interests of customers and stakeholders, rather than use tax planning to drive or determine business decisions. Group focus is therefore on compliance and tax planning is always aligned with commercial and economic activity.

The Group's approach to tax management is to be fully compliant with tax laws, rules, regulations and reporting requirements in all operations. This extends to following both the letter of the law as well as the spirit of the law. A culture of doing the right thing is embedded in the Group's core values and the Group's approach to tax embodies this by ensuring it pays the right amount of tax, in the right place, at the right time. The Group also uses the expertise of professional tax advisers to ensure it maintains best practice in its approach to compliance and in circumstances when additional advice is deemed appropriate.

The Group is open and transparent and does not use tax avoidance schemes or take an aggressive stance on the Group's interpretation of tax legislation when tax planning.

All companies within the Greensands Group are UK tax resident, ensuring that each company is subject to UK tax. Tax planning is always aligned with the Group's commercial and economic activity. This practice continues to be recognised by HMRC, which assesses the Group as 'low-risk'.

Further information regarding the Southern Water tax position can be found in the Annual Report for Southern Water which is published on its website.

Financial KPIs

Under the Group financial structure there is a comprehensive set of covenanted financial ratios. Of these, two are key ratios, namely the ratio of consolidated net debt to Regulatory Capital Value (RCV) and the ratio of consolidated EBITDA to consolidated net cash interest cost.

The net debt used in the net debt to RCV ratio is calculated as consolidated secured short-term and long-term borrowings less cash and short-term deposits. The RCV of Southern Water is set by Ofwat at each five-year periodic review and reflects its initial market value plus subsequent capital investment and inflation. The RCV is adjusted at each periodic review for relevant changes to the level of expenditure or performance during the five-year period.

Please refer to the Directors' report, pages 42 to 46, for a detailed review of the Group's going concern position.

Net debt: RCV	Hold co %	Mid co %	SWS %
2018–19 performance	90	76	66
2019–20 performance	90	76	67
2020-21 performance	94	80	70
Covenanted lock-up level	93	85	75
Covenanted default level	95	95	95

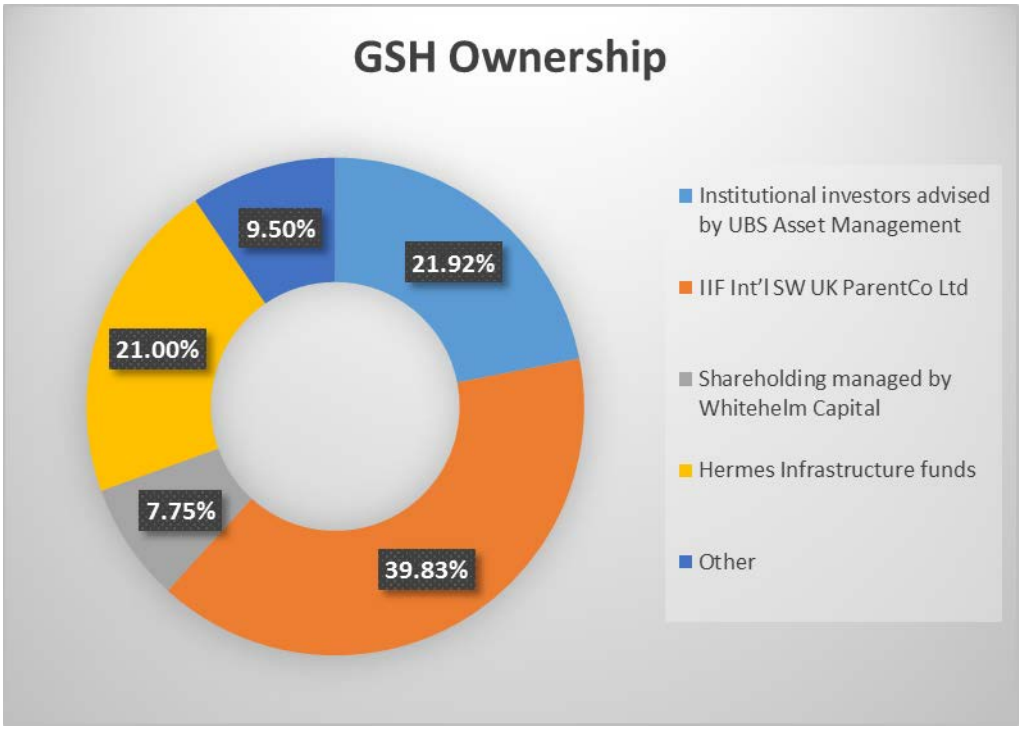
Consolidated EBITDA to cash interest cover	Hold co Times
2018–19 performance	2.9
2019–20 performance	2.8
2020-21 performance	2.7
Covenanted default level	2.0

Capital structure, liquidity and other financial matters

Capital structure, ownership and borrowing covenants

Ownership

GSH is owned by a consortium of long-term investors representing infrastructure investment funds, pension funds and private equity and no single shareholder has majority control.



UBS Asset Management – shareholding advised by UBS Asset Management, a large-scale global asset manager, offering investment capabilities across all major traditional and alternative asset classes.

IIF Int'l SW UK ParentCo Ltd - a constituent entity of the Infrastructure Investments Fund (IIF), a fund advised by J.P. Morgan Asset Management, a large-scale global asset manager advising institutional investors.

Whitehelm Capital – Shareholding managed by Whitehelm Capital on behalf of Motor Trades Association of Australia and Prime superannuation funds.

Hermes Infrastructure funds – Hermes Infrastructure is part of Federated Hermes International, formerly Hermes Investment Management and is a specialist infrastructure manager operating a diversified, well-established, UK-focused shared investment platform. With £4.1bn of assets under management, Hermes Infrastructure is one of the UK's largest direct investors.

Other – other minor shareholdings held by infrastructure investment companies.

Group structure

In September 2007, the Greensands group of companies was established for the purpose of the acquisition of 100% of the share capital of Southern Water Capital Limited, the then ultimate parent company of Southern Water, from the Royal Bank of Scotland (investing £1.9 billion of equity and debt to finance the acquisition).

During 2018–19 additional Greensands financing companies were added to the group structure as part of a financing plan to improve the financial resilience of Southern Water ahead of the five-year price review period starting April 2020. These new companies form the 'Midco' financing companies in the holding company structure diagram on page 12.

Financing in 2020–21

A Sustainable Financing Framework was put in place at Southern Water during 2019–20 which aligns its long-term strategy with its social and environmental commitments. An independent Second Party Opinion is also provided by DNV-GL to ensure alignment with the relevant bond/loan principles and guidelines.

The framework also sets out a robust process for project evaluation, project selection, the management of proceeds and reporting.

The majority of its assets and expenditure on projects, and programmes of work, fall within the eligible green categories and the eligible social categories taken from the Green Bond Principles and the Social Bond Principles.

Southern Water issued its inaugural financing under the Sustainable Financing Framework in May 2020 with a dual tranche public bond amounting to £825 million.

The company also issued a further public bond in March 2021, of £300 million, under the Sustainable Financing Framework.

The proceeds of these bond issuances was used to repay a £350m public bond which matured on 31 March 2021 and will be used to finance the capital investment programme until at least December 2022.

The Greensands financing companies also maintain liquidity facilities which can provide a short-term source of finance.

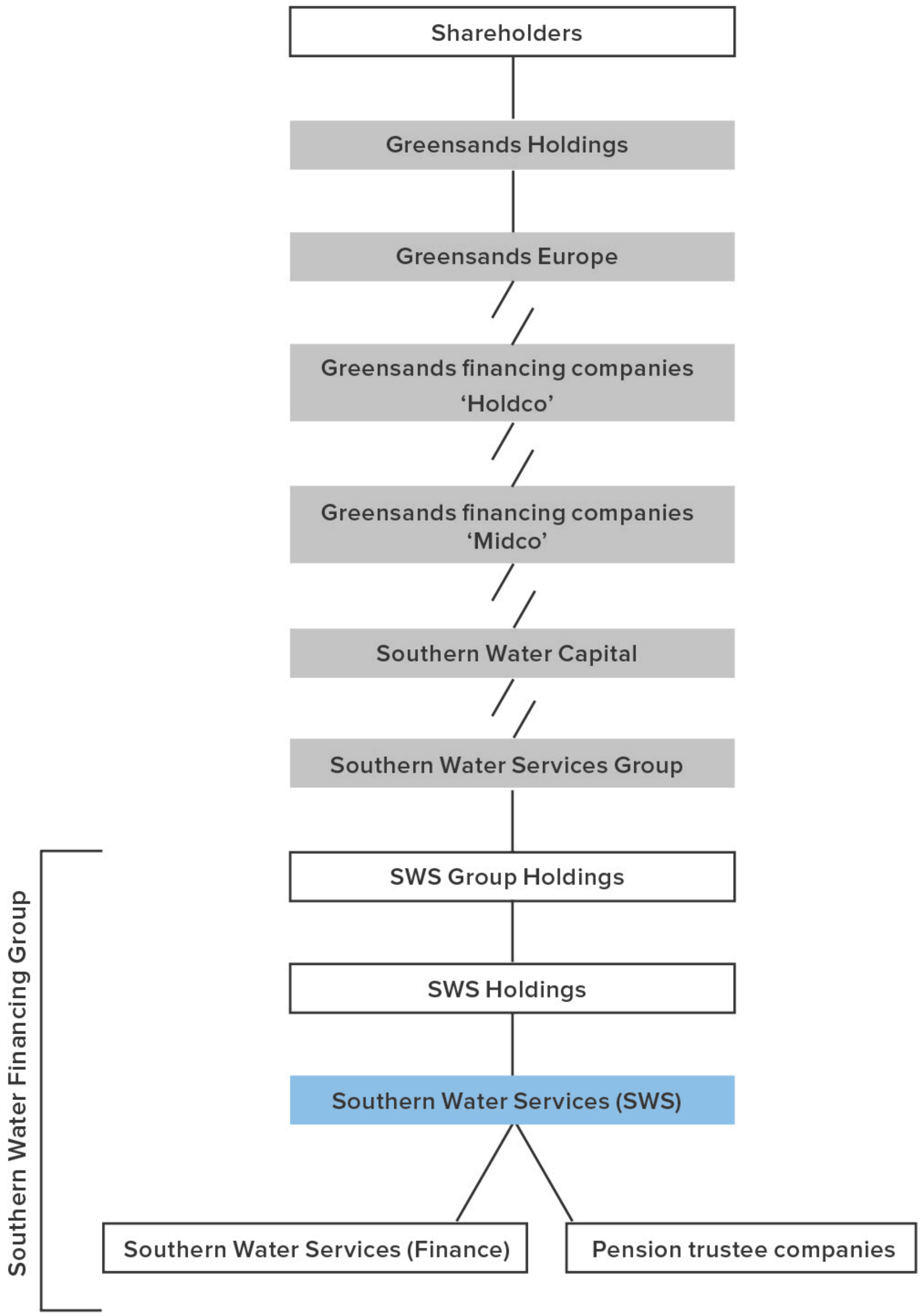
Southern Water is the only operating company in the group. As a result, all companies above Southern Water in the group structure are reliant on dividends being passed up from Southern Water to allow them to make interest payments due on external loans.

Going concern

Reflecting the reduced distributions arising from Southern Water Services Limited due to the implementation of the 2019 Final determination, and the Group's financing potentially being subject to certain credit rating covenants outside of the Greensands Holdings Limited Directors' control, a financial review of the debt held above the Southern Water Services Limited ring fenced group has been required. The Board has engaged external specialist advisors to identify and assess the mitigation options and activities available, to the Board and shareholders, in order to financially restructure the Greensands Group above the regulated company Southern Water. The financial restructuring plans under consideration, amongst a range of options, include additional investment from third parties where negotiations are at an advanced stage. Other options should these not complete could include covenant amendments, liquidity being made available and/or debt restructuring to provide liquidity to meet the requirements of the Group's borrowing facilities. Whilst discussions regarding additional investment from third parties are at an advanced stage, final agreement on these plans and contractual completion has not yet happened. Further detail of this material uncertainty associated with going concern is set out in the Directors' Report below.

The holding company structure for the Greensands group is shown in the diagram below and this is followed by an explanation of the principal companies in the structure.

Southern Water ownership structure summary



Greensands Holdings (GSH) – The ultimate parent company within the group. GSH was established in 2007 for the acquisition of the Southern Water Capital group, from RBS, by the shareholders. The company is Jersey registered, but it is UK tax resident and, as such, is liable for tax in the UK. The company was incorporated in Jersey because Jersey law allows greater choice than the UK as to the way distributions can be made to shareholders. GSH holds 100% of the share capital of Greensands Europe and has no direct holdings in any other entities.

Greensands Europe (GSE) – A subsidiary of GSH incorporated in England and Wales and resident for tax in the UK. GSE was established to issue bonds as part of the financing for the acquisition of the Southern Water Capital group in 2007. GSE has issued debt, Eurobonds, which are held by our shareholders in proportion to their respective shareholdings. This bond debt meets the eligibility requirements of the 'quoted Eurobond exemption' for tax purposes. The Eurobonds are listed on the International Stock Exchange in the Channel Islands which is a recognised stock exchange for the purposes of the quoted Eurobond exemption by HMRC. The bonds were issued on this stock exchange for ease of administration, as they are issued to the shareholders of the group and are not traded. As detailed in note 38, since 31st March the Eurobonds have been purchased from the shareholders for equity.

Greensands financing companies 'Holdco'– A number of companies, all incorporated in England and Wales and resident for tax in the UK, were established to provide additional external financing for the acquisition of the Southern Water Capital group in 2007. A further £250 million of additional finance was secured during 2019, the proceeds of which were invested into SWS. The security granted to the lenders of this financing is limited to the share capital of Greensands Holdings Ltd. There are no debt guarantees in place between the Greensands financing companies and the Southern Water Financing Group, with the result that SWS is fully protected, and fully isolated, from a default at any Greensands company.

Greensands financing companies 'Midco'– The Greensands Midco group of financing companies was incorporated in 2018 as part of a financial restructuring exercise to improve the financial resilience of Southern Water. The objective of the restructure was to reduce the total leverage within the Southern Water Financing Group and to reduce interest payments at Southern Water to help manage financial covenants. The debt issued by Midco companies is senior to that issued by the Greensands Holdco group of financing companies.

Southern Water Capital (SWC) – The previous holding company for the Southern Water group established as part of the sale of Southern Water by ScottishPower in 2002. SWC is incorporated in England and Wales and resident in the UK for tax. It does not trade and holds preference shares in SWS from which it receives dividends.

Southern Water Services Group (SWSG) – The immediate parent company of the securitised group which acts as a holding company for this group following the financial restructuring in 2003. SWSG is incorporated in England and Wales and resident in the UK for tax.

Southern Water Financing Group – Southern Water established a financing structure, known as a Whole Business Securitisation (WBS), in 2003 following its sale by ScottishPower. The WBS sets strict rules which demonstrate to investors that Southern Water is a safe and reliable business in which to invest. This structure helps to reduce its financing costs and improves access to long-term and secure sources of finance. Reducing financing costs ultimately benefits customers in the form of lower bills.

In 2018-19, SWS repaid it £400 million of outstanding Class B debt and entered into a deed that no further Class B debt will be issued for so long as Midco debt is outstanding. The £400 million of outstanding Class B debt was repaid out of the £700 million of new finance invested into SWS (net of £12 million costs).

The WBS works by creating a ring-fence around the Southern Water business in the form of a financing group. The financing group, whose immediate parent is SWSG, provides security to finance providers in the form of a charge over the share capital of SWS Group Holdings (SWSGH). No security is provided over Southern Water's individual regulated operating assets. This structure ensures that, in the unlikely event that either Southern Water or SWSF were to default on their debt obligations, Southern Water would continue to operate as usual. Debt providers are not permitted to either break up or interrupt the business and can therefore only look to a new owner of the financing group to recover their debt in the unlikely event of serious default.

The WBS also sets out arrangements for the ongoing management of the debt issuance programme as well as a number of operating arrangements in order to minimise our financial risk and adhere to good industry practice.

One of the WBS arrangements is a limit on the indebtedness of Southern Water and SWSF. This includes precautionary 'early warning' limits which prevent the payment of dividends if a limit is breached. We seek to ensure that we operate with sufficient financial headroom against these limits and have not breached a limit at any time since the implementation of the financing framework in 2003.

SWS Group Holdings – An intermediate holding company forming part of the securitised group. The company is incorporated in England and Wales and resident for tax in the UK.

SWS Holdings – The immediate holding company for Southern Water, forming part of the securitised group. The company is incorporated in England and Wales and resident for tax in the UK.

Southern Water Services (SWS) – This is the only operating company within the group, providing water and wastewater services to customers across Kent, Sussex, Hampshire and the Isle of Wight. Southern Water is incorporated in England and Wales and resident for tax in the UK.

Southern Water Services (Finance) (SWSF) – Southern Water's financing subsidiary, SWSF, was established for the express purpose of raising debt finance under the securitisation in 2003.

Due to administrative reasons applicable at the time of the WBS it was necessary for SWSF to be registered in the Cayman Islands in order to raise debt listed on bond markets. This original requirement for it to be registered in the Cayman Islands is no longer necessary and we are in the process of closing this company.

SWSF is wholly and exclusively resident for tax in the UK and files tax returns only with HMRC. This means that any profit or loss made by this company is subject only to UK tax.

Rating

Credit ratings for Southern Water Services are as follows:

Credit rating	Southern Water Services
Standard & Poor's	Class A debt: BBB+
Fitch	Class A debt: BBB+
Moody's	Class A debt: Baa3

The credit ratings are shown in the table above and the outlook for Standard and Poor's is Negative Outlook, the outlook for Fitch is Ratings Watch Negative, and the outlook for Moody's is Stable.

A further credit rating downgrade by one or more Rating Agencies would result in a Trigger Event under Southern Water's Common Terms Agreement which would restrict the payment of dividends and require the preparation of a remedial plan for its lenders. Southern Water has obtained a waiver from its lenders to continue to access permitted financial indebtedness to refinance the business in the event of a downgrade Trigger Event.

A further credit rating downgrade, or the assignment of a negative outlook, by Moody's would lead to a restriction on the payment of dividends under the terms of our Licence.

Under our Common Terms Agreement, a Trigger Event would occur if any two of the credit ratings fall to BBB (Standard & Poor's), BBB (Fitch) or Baa2 (Moody's) or below; and a default would occur if any two of the credit ratings are less than the minimum rating required for the status of investment grade.

The Group is fully in compliance with all its debt covenants.

Corporate Governance Overview

Greensands Holdings Limited (GSH) acts as a single-purpose entity as the ultimate holding company for Southern Water and provides the financing structure for the Group. As a consequence, the GSH Board complements and supports the aims of Southern Water for its long-term success. While certain matters are reserved to the GSH Board and/or GSH's shareholders, these matters do not impact the day-to-day operations of Southern Water, nor do they materially affect Southern Water's ability to function as an independent company in providing an essential public service.

Details of the governance of GSH are listed below, and those of Southern Water can be found in its Annual Report which is published on the Southern Water website.

Board membership and Chairman

The GSH Board comprises five directors. Three of these directors are appointed by an infrastructure fund managed by JP Morgan Asset Management; one director is appointed by infrastructure funds managed by UBS Asset Management; and one is appointed by pension funds and infrastructure funds managed by Hermes. Another shareholder is entitled to appoint an observer to attend and take part, but not vote, at GSH Board meetings.

In October 2020, R Wall resigned as a director and was replaced by H De Run as the Hermes representative.

The Chairman of Southern Water is not a member of the GSH Board and so no members of Southern Water's Board sit on the Board of GSH.

Board operation

GSH is party to the shareholder agreement between the shareholders in the Greensands consortium. Under that agreement, the GSH Board members, apart from the Chair (if one has been appointed), also comprise the Boards of the six subsidiaries down to Greensands Investments Limited. Three of the GSH directors comprise the Board of Southern Water Capital Limited and three of the directors of GSH are also directors of the MidCo entities – Greensands Finance Holdings Limited, Greensands Finance Limited and Greensands Financing plc. Mike Nagle is also a director on the Boards of the MidCo entities. No director of GSH is also a director of Southern Water Services Limited.

The GSH Board normally meets at least four times a year on its own. The business at such meetings includes agreeing formally any changes in membership, noting any relevant shareholder activity and approving formally any transfers of shareholdings as well as to review and, if thought fit, approve any matters reserved to the GSH Board. Areas of particular focus during the year have included:

- Southern Water's updated execution plan to enable it to deliver the 2020-25 Business Plan
- The issuing of a 'Green Bond' in May 2020.
- The refinancing exercises undertaken in March 2021.

The GSH Board also receives regular operational and financial performance reports in respect of Southern Water with the Chairman, Chief Executive Officer and Chief Financial Officer as regular attendees at GSH Board meetings. The financial performance of Southern Water represents the principal financial performance of the Group.

The GSH Board members are very mindful of the independence of the directors of Southern Water. GSH Board members are not present when the Southern Water Board meets, unless specifically invited to attend. The GSH Board members can bring additional knowledge, skills and resources of their nominating shareholders and employers, as well as their own personal skills, experience and knowledge of businesses and business sectors similar to that of Southern Water.

For compliance with Condition P of Southern Water's Licence, the shareholders who are considered to be the Joint Ultimate Controllers of Southern Water have given undertakings to provide all necessary information to that company, not to cause Southern Water to breach any of its obligations and to ensure that there are not fewer than three independent non-executive directors on the Southern Water Board.

GSH does not have any executive directors nor any dedicated management employees.

The GSH directors are not remunerated by GSH for their appointments.

Role of the Company Secretary

Richard Manning, together with Intertrust Corporate Services (Jersey) Limited, act as joint company secretary. Richard Manning is also General Counsel & Company Secretary of Southern Water.

All directors have access to the advice and services of the Company Secretariat team. The Company Secretary is responsible for ensuring that the Board operates in accordance with its governance framework and that there are good information flows to the Board. The appointment and removal of the company secretary is reserved to the GSH Board.

Director induction, training and development

GSH directors take advantage of the induction and training opportunities available to Southern Water directors as appropriate. On appointment to the Board, a director will discuss and agree induction coverage and then an appropriate comprehensive and individualised induction pack is provided, which will include information on Southern Water and the holding group structure, the regulatory framework of Southern Water, customer service and the operation of assets, strategic plans, financial reports, business plans and the governance framework. This and further relevant information is summarised in a directors' handbook.

Board meetings

The Board held six scheduled meetings during the year. In addition to the scheduled Board meetings, the Board met a number of times to discuss and receive reports on the business' credit ratings and other financial matters. The Board also addressed a number of other matters through written resolutions. The agenda and papers are sent to the Board members in advance of each meeting.

The Board has no standing committees.

Table of attendance at Board meetings

Attendance at scheduled Board meetings in 2020-21	
S Howard	6/6
P Hedley	6/6
J Lynch	6/6
B Somes	6/6
R Wall (resigned 13 October 2020)	3/3
H De Run (appointed 13 October 2020)	3/3

Note: attendance includes attendance in person and by telephone, noting that a majority, including the Chair must be physically located in the United Kingdom pursuant to the Company's Articles of Association.

Annual General Meeting

As a result of changes in Jersey Company Law, to bring it in line with Company Law in England and Wales, GSH, as a private company, is no longer required to hold an AGM. As a result the Board has decided that it will no longer hold an Annual General Meeting.

Due to the impact that COVID-19 has had on normal working practices, regular meetings are continuing to be held but via approved telecommunication means.

2) Southern Water Services Limited

Southern Water Services Limited is the only operating company of the Group. The financial statements of Southern Water, containing a full Strategic Report and Corporate Governance report, are published alongside these financial statements on the Southern Water website. An overview of the performance of Southern Water is provided below.

As a supplier of essential public services, Southern Water's priorities throughout this year have been to keep water flowing and its wastewater services operating safely and smoothly for its customers,while also protecting and supporting its employees and supply chain and offering help and advice to customers who found themselves in vulnerable circumstances**.**

At the same time, Southern Water has needed to make rapid and complex decisions to ensure the financial stability of the business, making sure that delays to capital projects, increases in delayed payments(and bad debt) and workforce and supply chain constraints were managed and accounted for.

As Southern Water entered this financial year, the primary impacts of the COVID-19 crisis relating to people and logistics were already being felt. Ensuring safe working practices for colleagues and customers, and adequate supplies of chemicals and personal protective equipment were a priority. As Southern Water came to the height of the summer months, the company also experienced a significant shift in demand for water as domestic customers used more water at home while commercial customers used far less. Southern Water hasincreased its provision for bad debt to reflect the fact that customers have faced financial hardship as a result of the impact of the pandemic. Throughout these difficult times, we are extremely proud of all those involved in keeping those essential services running for customers, both direct employees of Southern Water and those working for the company throughout its supply chain,and we can only thank them for their continued dedication and for, on many occasions, putting themselves on the frontline.

Ensuring the resilience of the business

Despite redirecting its operational efforts to ensure the smooth running of its frontline services throughout the year, Southern Water has continuedthe transformation of its business. As Keith Lough, its Chairman, highlights in his statement in Southern Water's Annual Report, Southern Water needs to continue to deliver tangible improvements in historic areas of concern such ascustomer experience, pollutions and water quality, through better planning and, the introduction of more efficient processes.

Although Southern Water are in 16th place out of 17 water companies in terms of the customer overall satisfaction (C-MeX) score, its customer service improvement programme has delivered some positive progress. Billing calls have reduced by 21% year on year as a result of proactive work withhigh usage customers and a focus on collections activity. Digital transactions have increased 47% compared to the same period last year as a result of improvements made to its YourAccount' self-serve portal and new self-serve journeys. We know Southern Water has more to do to improve its satisfaction (C-MeX) ranking, but believe the work undertaken this year has improved the underlying trajectory and is focused on the right drivers to improve its performance over the remaining four years of this investment period.

The Southern Water Business Channels team, serving its commercial and developer customers, meanwhile, ended the year in 15th place, driven by its levels of service for water and wastewater design and improved communications. This year, Southern Water launched a new workflow solution, web pages and cleared project delays caused by the impact of COVID-19.

Although its pollution performance is still not where we would like it to be, the first few months of 2021 have delivered some significant improvements. For the last quarter incident numbers were 40% of their 2019 equivalent, and Southern Water was able to finish the year with under 400 category 3 incidents, four category 2 and no category 1 incidents on the Environment Agency's (EA) tracker. This improvement has been driven through its Pollution Incident Reduction Plan, published in September 2020 (**southernwater.co.uk/our-performance/reports/ pollution-reduction-programme**).

From a water quality point of view, Southern Water's provisional score for the end of the first regulatory year of the Drinking Water Inspectorate's new Compliance Risk Index (CRI) measure is 4.53 (2019: 7.7). Although this represents a significant improvement, it is still not as good as Southern Water would like to be.

Leakage for 2020–21 was 98.5 Ml/d (2020: 94Ml/d) largely due to extreme seasonal fluctuations in the weather, alongside the demand associated with increased customer usage due to COVID-19. Southern Water is continuing to invest in improvements in the teams and technology used to detect leaks and its plans are to reduce leakage by 15% by 2025, 40% by 2040 and 50% by 2050.

Southern Water's financial performance

Southern Water accepted Ofwat's funding settlement for our business plan of its price controls for 2020–25 in February 2020 despite the significant challenge it presents in delivering what its customers want within the financial envelope Ofwat has set. It led to a 13% reduction in average customer bills and that, in turn, is the principal reason for the reduction in its operating profit of £73.5 million to £138.8 million.

As already mentioned, COVID-19 had a significant impact on the demand for water from customers. Southern Water experienced a significant increase to its revenues from the additional household demand however, this was offset by the reduction in income from its non-household customers and new housing developments.

COVID-19 also increased its operating costs by £2.7 million, with additional expenditure to ensure the health and safety of staff, facilitate remote working, support suppliers and maintain services to meet the significant increase in water demand.

In order to support its customers in vulnerable circumstances, Southern Water introduced a number of support schemes to assist them in paying their bills. This included pausing its normal debt recovery activities and introducing payment breaks for those in financial difficulty. As a result Southern Water incurred lower debt recovery costs in the year although they were in part offset by an increase in its provision for bad debt, reflecting the impact of the pandemic on itslikelihood of recovering some of its charges. The net impact of these items was a reduction in its operating costs of £4.0 million.

Over the past two years Southern Water has undertaken a number of transformation and re-organisation activities, in order to improve its performance and deliver efficiencies. These resulted in an overall reduction in operating costs from the prior year of £14.6 million reflecting both the one-off costs incurred last year to make the transformation and the ongoing cost savings resulting from the changes made.

Its capital programme for the new investment period commenced with over £380 million spent onimprovements to its assets. This included initial payments towards the construction of a new reservoir at Havant Thicket with a number of schemes in the Hampshire area aimed at tackling the impact of climate change and population growth.

Southern Water's credit ratings are an indicator of financial health used by its lenders when it borrows money to finance its capital investment programme; its licence of appointment also contains minimum credit rating provisions. Southern Water's ratings have continued to be under pressure in 2020-21 as a result of operational performance challenges against key regulatory indicators such as pollutions, wastewater treatment works compliance and customer performance, plus a challenging financial position with reduced turnover and increased costs, and financial uncertainty regarding the outstanding prosecution by the Environment Agency relating to wastewater permit breaches from 2010 to 2015.

Action taken to support Southern Water's credit ratings include a commitment by the Board to not pay dividends, if to do so will undermine its financial resilience and its transformation programmes to improve both operational and financial performance. During the year, Southern Water have also mitigated a risk from credit rating downgrade by securing consent from its lenders to continue to be able to finance the business in the event either its credit ratings or financial ratios fall below prescribed levels set out in our borrowing covenants.

In order to support the delivery of its business plan, Southern Water has continued to benefit from the support of its lenders in the successful issuance of £825 million bonds in May 2020 plus a further issuance of £300 million of bonds in March 2021. These bonds were issued under its newly established sustainable financing framework which includes a set of environmental, social and governance (ESG) standards for our operations that socially-conscious investors use to screen potential investments.

Other areas of significant progress

A number of key strategic projects were approved by the Board in December 2020, which will see the company focus on improving digital, logistics and asset maintenance capability across its network, allowing it to take a more proactive approach to the management of risk, in turn protecting its environment and improving its performance and services for customers.

These projects, which will drive £150 million of efficiency improvements to 2025, represent the final phase of its transformation programme. Started in 2017, this has focused on improving people, processes and systems, in support of its Business Plan 2020–25 targets; providing Southern Water with a new baseline to start allowing for outperformance in the next asset management period to 2030.

A key pillar of Southern Water's purpose ,protecting and improving the environment is something that sits at the very heart of Southern Water's business, which is why Dr Toby Willison has been recruited to its Executive Leadership Team. Toby brings with him a wealth of experience from the Environment Agency, and over the past few months has helped Southern Water to redefine its environmental ambitions.

Over the next four years Southern Water will invest nearly £1 billion in programmes that will deliver environmental benefits as a result of improvements to its network, and Southern Water has committed an extra £5 million to an environmental improvement fund, which will be focused on initiatives that deliver nature-based solutions and environmental net-gain, in partnership with local Wildlife Trusts and the Rivers Trusts. One project already identified is focusing on the important natural habitats in Chichester and Langstone Harbours working in partnership with the Chichester Harbour Protection & Recovery of Nature (CHAPRoN) project.

We are excited about the year ahead, as Southern Water publishes its net zero plans, it will take further steps to embed natural capital approaches in its planning processes and refocus its efforts on helping customers reduce their water usage as part of its flagship Target 100 water efficiency programme.

As already mentioned, Southern Water saw an enormous increase in demand for water as a result of changes to peoples' lifestyle due to COVID-19, which has seen individual daily water usage increase significantly. With life slowly returning to something like normal, Southern Water expects demand to remain high over the summer as people continue to work from home and holiday closer to home. Southern Water are prepared for this, and has adjusted its plans. Southern Water continue to work with Ofwat and our peers to understand the longer-term effects on usage. The increase seen is not unique to Southern Water's region. However, as it operates in an area of water scarcity it recognises the need to work with its customers to try and drive down consumption in order to meet its target of a 118.8 litres per person, per day by 2025 (this is a three-year rolling average).

Water is a precious, and increasingly scarce, resource for people and wildlife. It is essential that Southern Water strike the right balance between protecting the environment and maintaining supplies for customers. In Hampshire, that means taking less water from the sensitive chalk stream habitats of the Rivers Test and Itchen and more from sustainable sources instead. As part of its Water for Life Hampshire plans, which launched its first consultation in February of this year, Southern Water is planning to create a new network of water mains across this region and investigating new treatment techniques such as desalination and water recycling. You can read more at **southernwater.co.uk/water-for-life-hampshire**.

Challenges Southern Water are still facing as a business

Climate change and population growth in the South East present very real challenges that initiatives like Water for Life Hampshire are looking to address. Plans like this, and bulk supply collaborations with neighbouring water companies, are needed to secure reliable water supplies for the future, alongside reducing the amount of water lost through leaks and encouraging people to use less water.

This will help the country tackle extremes in weather such as droughts, which are likely to happen more often and be more serious, as the climate changes. It will also help provide water supplies to more customers in the future and enable us to leave more water in the environment to support habitats and wildlife.

In February, Southern Water signed an 80-year bulk supply agreement with Portsmouth Water, under which it will supply us with 21 million litres of water a day. Together, Southern Water are developing Havant Thicket Reservoir in Portsmouth Water's supply area; the first new reservoir to be developed in the UK since the 1990s, which will play a key role in reducing the amount of water taken from the Rivers Test and Itchen. It will be the first time a large water supply asset has been developed in this collaborative way

Reflections on a difficult year for Southern Water and its future priorities

At the end of the first year of delivery of this new five-year period, we would like to reflect on how far Southern Water have come in what has been a year of unprecedented challenge for the company. Southern Water started in a tough place, with a challenging Final Determination from its regulator and increased regulatory scrutiny as a result of a number of legacy issues with its culture and performance. Southern Water also received the lowest score in the industry in its annual Environmental Performance Assessment from the Environment Agency.

We are pleased to report that as a result of its transformation programme, Southern Water has continued to drive the changes in people, processes and systems that its regulators that its Board and regulators have been asking for. A great example is the development of its People Strategy and focus on diversity and inclusion, its commitment to which earned a ranking in the Inclusive Companies list of Top 50 UK Employers.

The Consumer Council for Water (CCW) mentioned Southern Water in its annual 'Water for All' report, published in November, citing its partnership working approach to vulnerability and its proactive contact methods to build its Priority Services Register as best practice.

A great example of collaboration in action is the development of catchment-based Drainage and Wastewater Management Plans (DWMPs), engagement for which has been ongoing throughout the year via a series of online stakeholder workshops. These plans set out how Southern Water intends to extend, improve and maintain a robust and resilient drainage and wastewater system in the future, providing greater transparency, robustness and clarity towards investment decisions. Working with its regional stakeholders is vital if Southern Water is to manage future risks to the people, businesses and the environment of the South East.

As its Chairman mentioned in Southern Water's Annual Report, its new culture dashboard is allowing it to measure and track the development of its company culture. The development of such metrics to track its progress in this area has been highlighted by Ofwat in its Board governance review as good practice.

Southern Water's culture is underpinned by its values of succeeding together, doing the right thing and always improving and this year, more than ever, Southern Water has embedded these at the heart of the delivery of its services to stakeholders. A clear focus on its core priorities during the pandemic has ensured that customers have had priority services and financial support when they have needed it most, that employees and supply chain have been able to work safely, prioritising essential services and keeping customers in supply and avoiding significant spikes in flooding incidents despite the challenges of extreme demand and fluctuations in the weather.

As Southern Water moves into a new financial year, the company is focused on continuing to drive the changes needed in its business to improve performance and its services for its many stakeholders.

We would like to take this opportunity to say thank you again for the hard work, commitment and sacrifice demonstrated by all its employees – whether Southern Water or supply chain – during the year. All of whom have had to adjust to new ways of working, meeting significant challenges along the way and that is not easy when you are juggling huge changes in your personal circumstances and home lives at the same time. Southern Water has achieved a lot despite this and, although we know it has challenges going forward to build on the confidence and trust it has now established with its stakeholders, there is positive change happening and it needs to keep that momentum.

Environment Agency Investigations

Like other wastewater operators, in the normal course of operations Southern Water occasionally faces Environment Agency investigations. Southern Water has been subject to a detailed investigation regarding permit breaches at some of its wastewater treatment works in two locations during the period 2010–15. In February 2020 the agency presented 51 charges before the court and Southern Water have entered guilty pleas to these charges. We will be open and transparent and are committed to working with the agency to ensure a swift conclusion to the case. Since Chief Executive Ian McAulay joined in 2017, he has been driving thorough internal reviews of its wastewater business and is leading a major transformation programme, which has already delivered a number of improvements to processes, people and systems.

For the reasons also set out in note 27 to the financial statements, supported by legal advice, the Southern Water Board has concluded that it is not yet possible to make a reliable overall estimate of the financial obligation that will arise from this prosecution, notwithstanding the guilty pleas and the Sentencing Council's Guidelines for Environmental Offences. However, the Southern Water Board does recognise that there will be a minimum liability associated with these charges and having reviewed the latest information, has maintained the provision of £1 million, recognised in 2019–20, reflecting a minimum amount as indicated by the Sentencing Guidelines and an allowance for legal costs.

The court has a very broad discretion to assess the level of the fine and the provision is not intended to indicate or predict any particular level. When considering the above it is noted that there are disputed levels of culpability and environmental harm. The sentencing guidelines are very wide and there is a requirement for the court to examine the financial circumstances of the organisation in the round. The next court hearing may take place in July. The Board will continue to review the level of provision made as more information becomes available.

Southern Water are also committed to assisting the Environment Agency with its separate investigation into sampling compliance and reporting issues between 2010 and 2017 (inclusive). The Southern Water Board, supported by legal advice, has again, and for similar reasons, concluded that it is not yet possible to make a reliable estimate of the financial obligation that will arise from this separate investigation but will also keep this under review.

Principal risks and uncertainties

The group has one operating company, Southern Water. The risks relating to this company are covered in detail on the following pages. The Group faces additional financial risks which are detailed below:

Liquidity and refinancing risk

The Group comprises three separate debt financing structures of Southern Water, Greensands Financing (Midco), and Southern Water (Greensands) Financing (Holdco).

Debt covenant ratios for 2020-21 are all within Trigger and Default levels with the exception of the HoldCo. Holdco's debt/RCV is in distribution lock-up as at March 2021 (Net debt to RCV of 94% versus the covenanted lock-up level of 93%).

Southern Water is in a strong position of liquidity following a total £1,125 million of bonds issued during 2020-21 under the Southern Water sustainable financing framework. Southern Water has sufficient liquidity in place to finance the business for at least the next twelve months. Southern Water also obtained a waiver from its lenders in February 2021 which allows full use of available liquidity, plus the raising of new finance, even in a Trigger Event scenario of a credit rating downgrade or a breach of a trigger debt compliance ratio.

The going concern statement in the Director's report on pages 42 to 46 sets out the importance of the shareholder financial restructuring plans for the MidCo and HoldCo group companies to continue to meet the requirements of its borrowing facilities.

As detailed in note 38 since the 31st March 2021 the Eurobonds have been purchased from the shareholders for equity and no longer represents external group debt.

Southern Water risks

Managing risk

Southern Water's approach to risk management is designed to provide a clear and consistent framework for managing and reporting risks associated with our operations, to executive management and to the Southern Water Board. The framework seeks to promote better decision-making, avoid incidents and encourage the best outcome for the company and our customers by allowing us to:

- understand the risk environment, identify the specific risks and assess the potential exposure for Southern Water;
- determine how best to manage identified risks to balance overall potential exposure;
- take action to manage the risks we do not want to be exposed to, ensuring our resources are effectively and efficiently prioritised and used;
- define its appetite for the range of risks and monitor and report risks against its desired risk appetite;
- and report up the management chain and to the board on a periodic basis on how significant risks are being managed, monitored, assured and the improvements that are being made

Risk management embedded in business processes

Southern Water want to provide a risk management process that provides a consistent basis for measuring risk to:

- establish a common understanding of risks on a like-for-like basis, taking into account potential impact and likelihood;
- report risks and their management to the appropriate levels of the company; and
- inform prioritisation of specific risk management activities and resource allocation.

All areas of the company review significant risks and business processes to help inform and enable risk based decision-making. As part of Southern Water's annual planning process, the Executive Leadership Team and Board review the business's principal risks. These may be updated during the year in response to changes in internal and external circumstances.

Risk appetite

The Southern Water Board defines its risk appetite, enabling Southern Water, in both quantitative and qualitative terms, to judge the level of risk it is prepared to take in achieving its overall objectives.

Southern Water have aligned its risk appetite to its principal risks, and they have streamlined and simplified the process. This has included a review of its risk categories and its risk assessment criteria and is linked to wider improvements to its risk management framework.

The risk appetite for each of its principal risks, underpins its governance and reporting framework and is reviewed regularly by the Southern Water Board.The alignment of principal risk with risk appetite allows for an informed analysis and discussion of its risk position and has provided the Board risk insight to key decisions.

As a company Southern Water are tolerating a level of risk which is outside its current risk appetite, and isreflected in the review of its principal risks as described in the following pages. This can result in more focus driven to short-term issues than longer-term resilience. The Southern Water Board and the Risk Committee are actively engaged in looking at longer-term strategic risks, as well as reviewing its risk appetite

COVID-19

The COVID-19 pandemic has brought a great amount of uncertainty. However, Southern Waters role as a provider of vital water and wastewater serviceshas not changed. What has become apparent is its need to be responsive and agile in its plans to protect public health as the pandemic continues to develop.

At the start of the pandemic, Southern Water moved in just oneweek from business as usual to a well-rehearsed Business Continuity Plan running against four simple priorities which have underpinned its COVID-19 response:

- Maintaining provision of essential services at alltimes
- Protecting the health, safety and wellbeing of its employees, including its supply chain, and its customers
- Providing the maximum practicable level ofassistance to its vulnerable customers
- Protecting the financial stability of its business.

The pandemic continues to impact Southern Water's domestic customers, many of whom are facing uncertain futures and are struggling to pay their water bills. Southern Water have supported them in the short term,offering payment breaks and increased access to its support tariffs while making sure that Southern Water monitor and prepare for the potential of increasing bad debt in the long term. In addition to keep customers informed, Southern Water created a dedicated COVID-19 area on its website, which included a letter from its CEO, Ian McAulay, and answers to common questions about the impact of pandemic on its services, changes to its ways of working, and the support available to them.

Its frontline employees were identified by the Government as key workers, so Southern Water also published details of essential work that would carry on during the lockdown.

COVID-19 continues to challenge all parts of the business. The second lockdown in November 2020 and the third lockdown in January 2021 have stressed the importance of managing this element of risk to the business. All areas continueto monitor, review, and update their risks with reference to the pandemic as appropriate to reflect the latest view of COVID-19 impacts.

COVID-19 risks continue to be reviewed at a monthly risk session. As the pandemic evolves, and in light of government announcements of the 22nd February, and the 5th April 2021, Southern Water are in preparation for the transition out of the national lockdown. The company continue with COVID-19 adaptations where appropriate to mitigate continued risks, with regular monitoring and the ability to revert to business continuity mode as required. As the situation could change at any time, regular monitoring and risk assessment willremain in place.

There can be no assurance that the COVID-19 pandemic will not have a material adverse impacton the future of the company, should the situationchange with future variants or waves of infection in the UK or other countries.

Brexit

As Southern Water moved towards the UK leaving the EU at the end of December 2020 Southern Water undertook significant planning and preparations to ensure that the company was able to maintain its operations. Specific focus was given to its preparations for the supplies of chemicals, asset parts, and logistics. Additional work included preparations to confirm its operations in and around some of its coastal ports (Dover and Southampton) were not disrupted by any transportdelays related to border crossings.

As Southern Water moved into January 2021 the risks the company identified did not materialise, and were relatively minor when compared to the scenarios for which Southern Water had planned and prepared.

Emerging risk

To reflect the requirements of the UK Corporate Governance Code Southern Water have identified emerging risks it is facing:

Drinking Water Inspectorate (DWI) enforcement regime – during February and March 2021, the DWI has been consulting on a change to its method of regulatory enforcement. The DWI is considering a new approach to include a punitive financial penalty regime within its regulatory framework. Southern Water is currently subject to a number of DWI notices; this could lead to a risk of additional financial penalties.

The potential introduction of a UK version of the Sarbanes Oxley Act will require close monitoring, reporting and understanding, to appropriately determine the impact on Southern Water's business. These changes, which will impact the UK Corporate Governance Code, are not likely to impact until 2025. Southern Water are making preparations in this area by reviewing and making improvements to its system of internal control across both financial and non-financial aspects of Southern Water.

Further mutation and establishment of new variants of COVID-19 significantly impact the recovery of the UK economy or supply chain links in other countries. Additional and prolonged national lockdowns may also be required, this could give rise to increased customer and employee health and wellbeing issues that would need careful management.

As COVID-19 continues to impact the economy, the potential for long-term solvency issues could see tighter bank lending standards that could impact on both Southern Water's ability to raise funds, but also its supply chain.

As Southern Water begins to direct efforts to meet its net zero carbon obligations, there may be legislation and significant costs involved with market-based mechanisms designed to support the process. For example, carbon offsetting may be cost prohibitive and limit Southern Water's ability to meet targets.

Environmental stakeholders are increasing pressure on water companies to limit their impact on the environment. This has emerged as a national debate on the future use of Combined Sewer Overflows and their impact on the environment.

Risk Oversight and Governance

To successfully embed risk management across Southern Water, the risk management process is supported by a governance structure that defines roles and responsibilities at each level of Southern Water.

The Southern Water Board has overall responsibility for risk management but discharges this role through the Southern Water Board Risk Committee. The committee meets three times a year and allows a detailed focus on risk factors to be discussed.

The Southern Water Risk Committee advise the Southern Water Board on its overall risk appetite, tolerance and strategy, taking into account the current and prospective regulatory, legal, political, macroeconomic and financial environment.

The Southern Water Board retain ownership and approval of its overall risk appetite, tolerance and strategy. The Southern Water Board still has ultimate accountability for risk management in Southern Water.

The Southern Water Risk Committee oversee and advise the Southern Water Board on the current risk exposure of Southern Water and its future risk strategy. The Southern Water Risk Committee have a key role in risk assessment:

Reviewing Southern Water's overall risk assessment processes that inform Southern Water's board decision making, ensuring both qualitative and quantitative metrics are used;

Reviewing regularly and approving the parameters used in these measures and the methodology adopted;

Setting a standard for the accurate and timely monitoring of large exposures and certain risk types of critical importance.

In addition the Southern Water Risk Committee review its capability to identify and manage new risk types and review reports on any material breaches of risk limits and the adequacy of proposed action.

The Executive Leadership Team (ELT) is responsible for ensuring the corporate risk management system is effective and embedded in Southern Water, and operates in accordance with the Southern Water's risk management approach.

Key responsibilities include:

SWS Board	**The Board retains overall accountability for risk management in the company** Attendees: SW Board members (including Executive, Non-Executive Directors)
SWS Board Risk Committee	**Responsible for oversight and challenge of the effectiveness of the risk management environment – meets three times a year** Attendees: SW Board members (including Executive, Non-Executive Directors)
Executive Risk Committee	**Reviews enterprise risks, risk improvements, strategic risk review – meets quarterly** Attendees: Executive committee (ExCom) of the Executive Leadership Team
Executive Leadership Team	**Receives monthly updates on operational risk dashboard** Attendees: Executive Leadership Team
Enterprise Risk Management and Resilience Team (ERMR)	**Provides support, guidance, training and management reporting** Development, maintenance and embedding of the risk framework
Directorate Risk Forum	**Responsible for ensuring that effective risk management is in place and operating across all activities within their remit – meets at least quarterly** Attendees: Senior Management team and Delegates

Our transformation

The Board continues to recognise the importance of effective risk and resilience management, champions its use within decision-making forums and is deeply committed to embedding risk management at every level of the organisation. As part of our transformation, we have recognised the need to improve our approach to risk and resilience management. Additional resource and expertise has been brought into the company to support the further development of risk management. A key aspect of this development is the implementation of a new business partnering model developed to ensure teams across the company are supported, facilitating risk-informed insight into day-to-day business activities Our Risk Management team has proactively engaged and collaborated with key stakeholders from across the business to identify improvements and enhancement to the existing risk management framework. Through extensive engagement with the Executive Leadership Team, Executive Risk Committee and wider company, a number of areas of improvement were identified.

Transforming its approach to risk management…

Framework:

- Collaborating across the company to better understand the needs of the key stakeholders and identify any gaps and inconsistencies in the existing framework.
- Redefining the Enterprise Risk Management & Resilience framework, aligning it to industry best practice in the form of ISO 31000 – Risk Management

Risk Criteria:

- Through engagement with the Board and other key stakeholders, revised criteria for assessing material impact has been re-focused to be more reflective of its business operations.
- The downside areas of impact for each risk assessed have been refreshed and broadened to reflect its priorities and values.
- The impact descriptions are now more detailed and prescriptive to help teams across the business better understand the downside consequence of risk events.
- Risk Taxonomy:
- Southern Water have refreshed its taxonomy and aligned the structure to its Principal Risks.
- The new taxonomy allows for clear, enhanced identification and allocation of risk from both a top-down and bottom-up perspective.
- Risk tolerances have been added to each risk component within the risk taxonomy, allowing each element to be confirmed against the Board approved risk appetite.

Risk Appetite:

- The Board have refreshed their view of risk appetite, and is underpinned by the updatedrisk taxonomy.
- A new simplified three-band approach to risk appetite has been implemented.
- The refreshed framework now supports the company in understanding where as a company Southern Water should be reducing the impact of downside risk, versus those risks where Southern Water should or could be seeking risk if there is a possibility of upside opportunities.
- The new approach is being actively used to support decision making, not least at Board level, where risk appetite is considered on key decisions, including the approval of the latest Execution plan (EP-21).

Roles & Responsibilities:

- The Board have championed an approach to managing and owning risk in Southern Water.
- Each Directorate senior management team reviews and monitors their risks and has an established risk forum that meets at least quarterly.
- These fora are actively supported by the enterprise risk team who support as part of their business partnering approach, and provide a forum for focused discussion on risk management, supporting and promoting a dialogue on risk and supporting decision making.

Data Cleanse:

- As part of the wider changes detailed above a full review of the risk profile was initiated
- Working with the risk communities, a revised priority risk profile has been identified and supports all stakeholders ensuring effective risk-based decision making.

Enhancements in reporting have been achieved through the revised risk profile, with company-wide risk insight provided to senior management and the executive leadership team and the Board

The next 12 months…

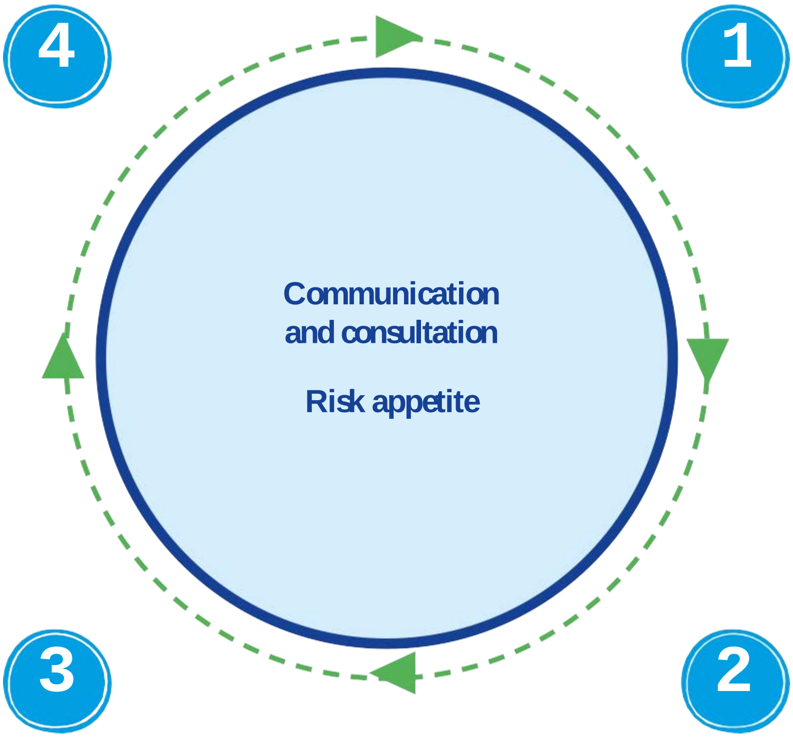
The coming year will see continued embedding of Southern Water's risk management approach; it is recognised that its journey is not complete and additional improvements have already been identified to further support risk-based decision making across the company. This will see effort focused on maturing in a number of areas:

- Continued training across the risk communities, through the use of virtual and workshop sessions. This will focus on embedding its approach to risk management.
- To support its approach to risk management, and to deliver on commitments to Ofwat, Southern Water are implementing a Governance, Risk and Control (GRC) system. The project solution will provide a robust system solution to strengthen its risk management improvements and will also support assurance and control work across its risk and compliance teams.
- Enhancing its ability to report its risk positon is a key focus and priority and will be achieved through the integration of enhanced reporting tools. The ability to extract and tailor assurance data will support the business in fully understanding the risk landscape and its relationship to its risk appetite, helping the company make better, risk-informed decisions.

The improvements Southern Water are making to its risk management approach are setting the company up for future success. As Southern Water further embed these improvements Southern Water will be able to demonstrate to its customers and external stakeholders that the decisions Southern Water make are considered, well thought through, and demonstrate continued commitment to its values.

The purpose of its approach to risk management is to support better decisions through an improved understanding of risk

The objectives of its risk management strategy relating to principal risks are to:



1. identify and understand all the principal risks that we face;
2. select and proactively adopt strategies and plans to address, including seeking opportunities from, those risks that deliver the right returns, and understand their potential impact on the company;
3. take action to mitigate its exposure to the principal risks, ensuring its resources are effectively and efficiently prioritised and used: and
4. use the analysis of its principal risks to inform its strategy and to monitor and report the risks we are taking against its desired strategic objectives.

Operational risk- 1 Water

Risk Climate Key: Deteriorating Stable Improving

Description:

We must ensure we can supply enough good quality drinking water to cater for a growing population of more than 2.6 million people across Kent, Sussex, Hampshire and the Isle of Wight.

Should operational water treatment processes fail, the water supply become contaminated, or its water distribution network fail:

- there is a risk that water could be supplied to customers that is unfit for consumption,
- large numbers of customers could find their water supply becomes cut off,
- harmful chemicals could be released to the environment.

Southern Water executive accountability:

Director of Wholesale Water Services

Link to Southern Water's values:

Doing the right thing / Succeeding together /Always improving

Forecasted business impact:

Long term

Areas impacted:

Customer experience, business disruption, brand and reputation, legal and regulatory, financial

Risk climate:

Southern Water's risk profile has deteriorated following the introduction of challenging regulatory targets in the 2020–25 business plan; in particular, the amendment of regulatory limits on the amount of water that can be abstracted for water supply in its Western region is proving challenging.Furthermore, increased demand from customers, particularly within the Sussex North region, during the ongoing COVID-19 pandemic has placed additional stress on its asset infrastructure. In addition Southern Water is now working to challenging performance targets, with respect to leakage, interruptions to Supply and Compliance Risk Index (CRI) and Event Risk Index (ERI) and Security of Supply Index (SoSi).

Risk drivers:

- Levels of investment in maintenance and growth schemes to support asset capability and capacity.
- Ageing infrastructure increasing the frequency and severity of asset failure.
- Non adherence to established processes and procedures when under pressure of operational incidents.
- Challenging regulatory targets from source to tap.
- Management of contracts for operational and maintenance services.
- Fluctuation and severity of weather events.

Mitigating strategy

- New bulk supply arrangement with SES Water and improvements to key assets to support water resilience in the Sussex North area.
- Portsmouth and Havant Thicket reservoir to provide additional long-term resilience.
- Water for Life Hampshire – programme of significant capital and asset improvements to provide long-term resilience in its Western area.
- Introduction of a rolling 12-month strategy plan that identifies the needs of the business to meet its commitments.
- Water First, its improvement programme strengthening internal processes and asset performance.
- Water quality hazard review programme complete at its water production sites, with similar programmes being undertaken at network booster stations and treated water storage assets.
- Maintained ISO 9001 accreditation for continuous improvement.
- Robust and extensive regulatory monitoring programme of samples from source to tap.
- Incident and emergency planning system, process and procedures in place.
- Proactive leakage detection monitoring and reporting.
- Customer education programme supporting an improved understanding of the value of water – Target 100 waterefficiency programme.

Operational risk- 2 Wastewater

Risk Climate Key: Deteriorating Stable Improving

Description:

Southern Water's region benefits from a high-quality environment, both inland and coastal. It is fortunate to have some extremely rare habitats, as well as some of the best quality river fishing and coastline in the UK. Reliable wastewater services are essential to maintain public health and protect the environment.

Should operational wastewater treatment processes fail,or sewers and pumping stations become blocked or fail, Southern Water's assets may discharge sewage, which is not of the required standard, to the environment. This may cause risks to the environment or public health from pollution and/or sewer flooding. There is also the potential to cause damage to the environment or distress to customers. This could lead to prosecution and fines by the Environment Agency and a reduction in stakeholder and customer confidence.

Southern Water executive accountability:

Director of Wastewater and Asset Management

Link to Southern Water's values:

Doing the right thing / Always improving

Forecasted business impact:

Long term

Areas impacted:

Customer experience, business disruption, brand and reputation, legal and regulatory, financial

Risk climate:

The environment for which this risk relates to has deteriorated over the past 12 months, this is largely due to increased challenges, specifically in light of increased capacity demand, fluctuations in extreme weather events and challenging regulatory targets that are expected to be more onerous should newly planned restrictive regulation be implemented. A national debate on the water companies' impact on the environment, and particular the use of Combined Sewer Overflows (CSOs) has intensified over the last year. This could lead to additional regulatory scrutiny or intervention. Southern Water is working to increasingly challenging targets in the business plan period 2020–25, a number of which were not funded in the price review, with respect to Wastewater Treatment Compliance and Pollution.

Risk drivers:

- Asset capability performance due to ageing infrastructure
- Increase in regional power outages.
- Investment requirements to support growth schemes for new housing developments.
- Levels of investment in maintenance and development schemes to support asset capability.
- Meeting the required standards of wastewater treatment and asset management to protect the environment and/ or public health from pollution and/or sewer flooding.
- Non adherence to established processes and procedures when under pressure of operational incidents.
- Management of contracts for operational and maintenance services.

Mitigating strategy

- Pollution Incident Reduction Plan (PIRP) delivery is ongoing, and leading to improvements in underlying performance.
- Introduction of a rolling 12-month strategy plan that identifies the needs of the business to meet its commitments.
- Dedicated growth planning team established tasked with developing plans and strategies that consider long-term resilience over the next 25 years.
- Generator maintenance programme in place with new contract maintenance process being embedded throughout 2021.
- Regular testing of power management systems and its back-up generator capacity to ensure continuity of services.
- High voltage equipment maintenance programme in place with external suppliers.
- Public Interest Commitment (PIC) to become a carbon neutral (net zero) company by 2030.
- Customer awareness/education programmes on avoiding blocked drains, targeted at catchments with blockage hotspots.
- A culture transformation programme to develop a behavioural competency framework for its employees'

Operational risk- 3 Customer

Risk Climate Key: Deteriorating Stable Improving

Description:

Providing an excellent customer experience is a key objective for us. Southern Water recognise the importance of prioritising its customers, and that accomplishing its strategic goals is contingent on providing the level of service expected by its customers and its regulators. Southern Water may not be able to provide the desired standard of service to its customers if there is inadequate capability in its people, process or systems.

Southern Water executive accountability:

Director of Customer Service

Link to Southern Water's values:

Doing the right thing /Always improving

Forecasted business impact:

Medium term

Areas impacted:

Customer experience, brand and reputation,legal and regulatory, financial

Risk climate:

The scale of the challenge is significant if the business plan period 2020–25 execution plan is to be delivered; the spend on Customer Service in 2015–20 is £95m more than the allocation in the Final Determination (FD) for 2020–25, the scale of improvement required to deliver the FD is therefore significant. Its performance on key performance metrics is improving although Southern Water remain in the bottom third of companies for both key performance metrics (C-MeX and D-MeX).

There has been no significant change in its risk profile during 2020–21. Southern Water continue to deliver improvements through its customer transformation plan (Velocity), and supported many of its customers impacted by the effects of the COVID-19 Pandemic. Improvements to how Southern Water run its developer services channels have also been implemented strengthening performance in this area.

Risk drivers:

- Customer and wholesale business impact on its C-MeX and D-MeX performance.
- New property builds requiring additional odour mitigation measures.
- Manual processes, which may lead to errors that require automating.
- Lack of key third-party customer service providers contract management.
- Transformation project (Velocity) does not deliver in improvement of cost to serve.

Mitigating strategy

- The customer transformation project (Velocity) continues to develop the processes and technology that underpin itscustomer service.
- Contractual targets in place with key customer service providing third-party suppliers.
- Leadership team led Operations Committee held monthly tasked with monitoring C-MeX and D-MeX performance.
- Cross functional C-MeX working group established to ensure appropriate accountability and management focus across all relevant parts of the business.
- Dedicated team in place to proactively engage with local authorities and new-build developers, to ensure the appropriateness of supply planning and connection.
- Specific incident management process and procedures for customers in the event of service impacts.
- Process in place to support vulnerable customers affected by an incident such as COVID-19 or water emergencies

  Customer insight work to better understand customer requirements.

Financial risk- 4 Financial

Risk Climate Key: Deteriorating Stable Improving

Description:

Exposure to financial markets and other macro-economicfactors, impacting the ability to accurately forecast and ensure the continued ability to meet Southern Water's short-term and long-term financial obligations. A failure to maintain certain credit ratings could lead to an increase in interest cost and reduced availability of finance. This could put pressure on its ability to finance the capital investment programme, or refinance existing debt maturities, at risk in the future. Southern Water only enter into treasury transactionsto manage inherent risk and support prudent funding, not to speculate.

Southern Water executive accountability:

Chief Financial Officer

Link to Southern Water's values:

Doing the right thing / Succeeding together

Forecasted business impact:

Medium term

Areas impacted:

Brand and reputation, legal and regulatory, financial

Risk climate:

Southern Water's risk profile has deteriorated due to significant adverse financial impacts as a result of a challenging final determination, and managing the effects of the COVID-19 Pandemic with revenue loss through an increase in bad debt and additional COVID-19 related costs.

During the year one of the rating agencies has forecast that Southern Water will be downgraded in the credit ratings as a result of concern regarding perceived challenges facing the company in delivery of the business plan 2020–25, difficulties in meeting Ofwat Outcome Delivery Incentives (ODIs), and potential fines from the outstanding prosecution from the Environment Agency.

Southern Water's current credit ratings are provided on page 15.

Risk drivers:

- Accuracy of forecasts to meet long term financial liabilities and obligations.
- Ability to access cost effective capital through maintaining an appropriate credit rating.
- Revenue impacts caused by counterparty defaults due to delayed Brexit or ongoing COVID-19 influences.

Mitigating strategy

Southern Water's plans include:

- Liquidity testing and reporting is carried out on a regular basis, forming part of the going concern assessment.
- Sufficient cash and facilities are maintained to mitigate such risks as bond market closures.
- Southern Water ensure the aggregate nominal value of debt maturities does not exceed 40% of RCV in any single regulatory period (and 20% of RCV in any 24 months).
- Flexible dividend policy supports management of financial risk.
- Regular discussion with ratings agencies to evaluate financial health.
- Southern Water take each of the main credit agency ratios, relevant for its ratings, into account when setting the plan (one-year,five-year).
- Regular discussion with bank groups and lenders.
- Southern Water established a Sustainable ESG Framework during the year and in May 2020 issued its first dual tranche sustainable bond.
- Current borrowings are 'fixed rates' or 'index-linked' and Southern Water have no exposure to interest rate rises on its current borrowings.
- Southern Water ensure sufficient funds are available for its operational and capital investment programme.

The liquidity and refinancing risk faced by the Group is set out on page 22. The Director's report on pages 42 to 46 contains detailed information on going concern and the strategies being undertaken to manage the uncertain position.

Corporate risk- 5 Compliance

Risk Climate Key: Deteriorating Stable Improving

Description:

Southern Water is a highly regulated business with three main regulators: Ofwat, the Drinking Water Inspectorate (DWI)and the Environment Agency (EA) and high standards of compliance are expected.

Inadequate culture, structure, capability, governance and assurance could result in failure to meet these high standards consistently. The consequences can be regulatory enforcement, fines, legal action and, in the worst case, the loss of its appointment as a water and wastewater company. As with all companies, Southern Water are also required to comply with corporate legislation (for example Competition Law and the Bribery Act).

Existing and changing legal and regulatory requirements encourage the business to operate in an agile way to ensure continued compliance with its obligations.

Southern Water executive accountability:

Director of Risk and Compliance

Link to Southern Water's values:

Doing the right thing /Always improving

Forecasted business impact:

Short term

Areas impacted:

Brand and reputation, legal and regulatory

Risk climate:

This risk remains high as a result of regulatory compliance issues, which have been raised by its regulators. Southern Water continue to be the subject of intense regulatory scrutiny. Southern Water is being prosecuted by the Environment Agency (EA) for wastewater permit breaches, Southern Water has pleaded guilty to charges in court and Southern Water are assisting the EA with its investigations into legacy issues relating to wastewater sampling compliance. Further detail on these and the recent Ofwat investigation can be found on pages 30 and 31 and in Southern Water's Annual Performance Report.

The Drinking Water Inspectorate (DWI) and the EA continue to monitor its delivery of regulatory schemes (outputs) and this is likely to continue in the future. Challenging performance on the Compliance Risk Index (CRI) from the DWI, and one-star performance on the EA's Environment Performance Assessment (EPA) is reflected in continued scrutiny from both quality regulators. Ofwat continue to focus on its ODI performance and compliance with its Section 19 Undertakings

Risk drivers:

- Failure to comply with the requirements of its Licence of Appointment with Ofwat (including its Section 19 undertakings).
- Failure to meet its obligations with the EA, as reflected in the Environmental Performance Assessment (EPA).
- Meeting its Water Quality obligations as reflected in key performance metrics (CRI and ERI) and DWI notices and enforcement.
- Failure in the ability to embed core controls over key processes, either financial or non-financial.
- Threat of a breach in its business ethics or Code of Conduct by an employee or contractor.
- Protection of data – GDPR.

Mitigating strategy

- Embedding of a robust three lines of defence compliance model and a dedicated Risk and Compliance function.
- Improved training, investment, internal business processes and controls via our transformation programmes.
- Company values linked to culture and performance management.
- Subject matter experts and mandatory compliance related training.
- Annual reporting is externally verified by financial and technical auditors to provide assurance on our compliance.
- Technical assurance of front line operations is supported by ISO9000, ISO17025 and ISO14001 accreditation.
- A compliance framework with internal monitoring and assurance and an ethical business framework.
- Compliance with company procedures is reviewed through self-assessment every six months.
- Mandatory training courses are identified and communicated to all employees for completion.
- Contracted suppliers are required to sign up to our Code of Conduct and evidence operating within expectations of the legal and regulatory environment.
- Enhancements delivered across the system of internal control, specifically within the assurance functions

Corporate risk- 6 Climate change

Risk Climate Key: Deteriorating Stable Improving

Description:

The impacts of climate change will continue to increase Southern Water's related risks of water resources, drought, flooding, and extreme weather events. Southern Water supply drinking water to a growing population in areas already classified as under 'severe water stress'.

If Southern Water is unable to improve its resilience to the extreme weather events predicted by the physical impacts of climate change:

- Southern Water will find it increasingly difficult to supply sufficient water to meet the growing demands of its customersthough scarcity of water resources, or contamination by saline intrusion of existing water reserves;
- the assets on its sites, or its sewer system network, could more easily be overwhelmed by storm events, leading to flooding or pollution in its region; and
- its coastal sites may become inundated from risingsea levels or at risk of coastal erosion.

Southern Water executive accountability:

Director of Environment & Corporate Affairs

Link to Southern Water's values:

Doing the right thing / Succeeding together /Always improving

Forecasted business Impact:

Long term

Areas impacted:

Customer experience, business disruption, brand and reputation, legal and regulatory, financial

Risk climate:

Southern Water's risk profile has deteriorated due to continued worsening external climate change factors impacting the ability to supply sufficient water to meet the growing demands of its customers. Ongoing challenges with more stringent revised abstraction licences in Hampshire, which limits its ability to access water in Hampshire and makes Southern Water more vulnerable to weather events. In addition Southern Water has seen the emergence of supply issues in its Sussex North area.

Combating climate change is also about mitigating the causes of climate change. In terms of Southern Water's efforts to join in with the global response to climate change, Southern Water has made a Public Interest Commitment (PIC) to becoming a Carbon neutral (net zero) company by 2030 (as part of the English water companies).

Risk drivers:

- Failure to adapt to the long-term effects of climate change.
- Challenging regulatory targets.
- Unless unprecedented investment there is an inability to meet the demands of a significantly increased customer base.
- Onerous and challenging targets to mitigate the effects of its carbon footprint.
- Fluctuation and severity of weather events.

Mitigating strategy

- Public Interest Commitment to become a carbon neutral (net zero) company by 2030.
- Board approved net zero plan.
- 50-year Water Resources Management Plan, to provide resilience against drought and climate change.
- Drought Plan containing measures to conserve water, operate our sources and secure additional resources.
- In excess of £400 million was invested in the existing water and wastewater infrastructure through 2015–20.
- Established climate change working group.
- Customer education programme supporting an improved understanding of the value of water – Target 100 water efficiency programme.
- Investment in new infrastructure including the Havant Thicket Reservoir.
- RAPID process will lead to new investment in the Western Area as part of Water For Life – Hampshire.

Corporate risk- 7 Delivery

Risk Climate Key: Deteriorating Stable Improving

Description:

Southern Water has a planned investment programme of £2.1 billion between 2020 and 2025. Southern Water have plans in place to ensure it will deliver this and is working hard to ensure its focus is maintained to complete all works on time.

If Southern Water is unable to deliver significant parts of the programme on schedule, its ability to provide an excellent service to its customers could be compromised. Any failure to deliver would also prevent it from fulfilling the promises that it has made in its business plan with regard to performance measured by its outcome delivery incentive measures, along with commitments to its regulators.

Southern Water executive accountability:

Director of Engineering and Construction

Link to Southern Water's values:

Succeeding together / Doing the right thing / Always improving

Forecasted business impact:

Medium term

Areas impacted:

Customer experience, brand and reputation, financial, people

Risk climate:

The scale of the requirements of the capital investment delivery programme combined with a tight financial settlement in the period 2020–25 has increased risk in this area.

Southern Water's risk profile has deteriorated due to the size and scale of the requirements of the capital investment delivery programme, during the unprecedented time of managing the effects of the ongoing COVID-19 Pandemic. The financial pressure on the capital programme, plus stringent requirements from regulators to deliver extensive programmes of work has seen an increase in risk in this area. Key recent focus has been on delivery of its WINEP obligations and on key notices from the Drinking Water Inspectorate (DWI).

Risk drivers:

- A tight Financial Determination from Ofwat has put pressure on capital delivery budgets.
- Challenging delivery efficiencies that are required to deliver value for the wider business.

Mitigating strategy

- Southern Water has brought significant investment capability in house including:
  - an embedded in-house engineering and capital delivery function
  - an established long-term delivery partner supply chain.
- Enhanced management information procedures ensure the delivery of the business plan is given the greatest level of focus.
- Risk and value are considered at each step of the investment cycle to provide best value for money to its customers.
- Enhancing and continuously developing its asset planning systems, processes and capabilities.
- Monitoring the delivery of its final determination obligations, continually assessing its financing status.

Corporate risk- 8 Information technology

Risk Climate Key: Deteriorating Stable Improving

Description:

If Southern Water does not maintain the resilience of its operational and enterprise IT systems, their failure could have a significant impact on its business reputation, ability to operate, and the resilience of its operational assets.

Additionally, Southern Water hold and process personal and payment data about its customers and employees so it is important that Southern Water treat this information with respect and in accordance with the requirements of information governance.

Failure to properly protect the data Southern Water hold could lead to reputational damage and loss of confidence from its customers, as well as significant fines under Data Protection (GDPR) and the Network and Information Systems (NIS) Directive.

Southern Water's executive accountability:

Managing Director

Link to Southern Water's values:

Doing the right thing / Always improving /Driving results

Forecasted business impact:

Long term

Areas impacted:

Customer experience, business disruption, brand and reputation, legal and regulatory, financial

Risk climate:

There has been no significant change in the risk climate, notwithstanding managing the effects of the COVID-19 Pandemic providing additional IT infrastructure, hardware, and other key equipment to support remote working.

Southern Water continues to rebuild its IT capability. This transformation has been ongoing for the past four years and has featured in-sourcing of its IT capability, and has seen an improvement in its IT estate.

Risk drivers:

- Lack of cyber security controls and monitoring in place for business systems.
- Technology failure through the use of and dependency on legacy systems.
- Appropriate business continuity processes to reduce any impact on its IT systems.
- Mishandling or deliberate sabotage of employee or customer data.
- Non-compliance with NIS directive requirements.
- Inability to monitor and manage operational functions (telemetry & control) or to provide IT supported customer services, including billing or new service provision.
- Weakness in the security of SW's telemetry network, where physical access to the network can be obtained.
- Non-compliance with PCI-DSS.
- Malicious attacks leading to significant customer or environmental incidents from sabotaged plant activity or the loss of control of major site systems.

Mitigating strategy

- Southern Water has implemented two new Datacentres – these are focused on resilience, protecting its core services and preventing issues before they occur.
- Active programme for migration of services off heritage infrastructure and onto new fully-managed infrastructure.
- Migration of existing critical and core service solutions to the new data centres which are focused on resilience,protecting core services and preventing issues before they occur.
- Enhanced suite of IT general controls identified following alignment to the Network and Information System – Cyber Assessment Framework.
- Mandatory business-wide Cyber Security and Data Protection Training provided to all employees.
- Information Governance Council in place with the responsibility of oversight and governance of its GDPR and NIS compliance.
- Continued investment in cyber threat mitigation strategies in response to the ever-changing risk landscape.

Corporate risk- 9 Resources

Risk Climate Key: Deteriorating Stable Improving

Description:

Southern Water's business model includes the use of long-term contracts for the provision of critical goods, services and works, as well as some outsourced activities. Some of its most critical resources include the supply of chemicals, fuel and spare parts to ensure continuity of service, as well as the energy required to power its operational equipmenton a continuous basis, at a commercially viable price.

There is a risk that a failure to have the required external market capability and capacity, would lead to Southern Water being unable to deliver its committed obligations, required efficiencies in its business plan, and a return for its shareholders. There is a risk that a failure to have an effective resilient energy model in place will lead to power interruption at its sites and subsequent operational interruption, and cost inefficiencies.

Southern Water executive accountability:

Managing Director

Link to Southern Water's values:

Doing the right thing / Always improving

Forecasted business impact:

Short term

Areas impacted:

Business disruption, brand and reputation, financial

Risk climate:

In light of the COVID-19 pandemic and conclusion of BREXIT, there has been no significant change in the risk climate.

Risk drivers:

- Failure to effectively manage third-party suppliers and contracts to ensure availability of critical chemicals and services.
- Ineffective assessment of supplier criticality and resulting vendor management plan thereafter.
- Lack of central monitoring of supplier base and related performance versus contractual terms and service levels. Failures in due diligence process when tendering or on- boarding new suppliers.
- Cost inefficiencies through the use of multiple suppliers contracted to deliver similar or the same products and services.
- Failures through non-compliance with internal policy procuring goods and services from suppliers.
- Lack of a swift reconciliation of projects following closure leading to financial claims by suppliers.
- There is a risk that a failure to have an effective resilient energy model in place will lead to power interruption at its sites and subsequent operational interruption, and cost inefficiencies.

Mitigating strategy

- Supplier procurement framework in place that mandates the processes required to be completed, including management approval and sign-off in line with authority levels.
- Processes in place to identify key suppliers with additional alerts and monitoring processes in operation.
- A reconciliation hub for completed projects has been implemented to ensure accounts are completed.
- Working group established to review alternative key sourcing options.
- Key working groups established and operational to manage the effects of BREXIT and COVID-19.
- Each business function has a continuity plan in place in the event that the supply of critical resources from its suppliers is interrupted. The plans will include identification of of alternative suppliers or stockpiling of necessary resources (e.g. chemicals) supported by its dedicated Contract and Supplier Managers.
- Southern Water created a new centralised Contract and Supplier Management capability.
- The Supplier Relationship Management framework is in place which covers principles to drive the right collaborative relationships with its key supply chain partners.

Operational risk- 10 Health, Safety, Security and Wellbeing

Risk Climate Key: Deteriorating🔴 Stable🟡 Improving🟢

Description:

The health, safety, security and wellbeing of its employees and the public while Southern Water provide its services is of the highest priority. The nature of its work requires that its employees and contractors undertake activities or use equipment which, if uncontrolled, have the potential to cause significant harm.

Failure to comply with its Health and Safety Management System and associated procedures could result in death, serious injury or adverse health effects. Southern Water could be liable for prosecution under the Health and Safety at Work and Corporate Manslaughter Acts, civil claims and employers' liability and professional liability.

Southern Water executive accountability:

Chief Executive Officer

Link to Southern Water's values:

Doing the right thing / Always improving

Forecasted business impact:

Short term

Areas impacted:

Business disruption, brand and reputation,legal and regulatory, financial

Risk climate: 🟡

There has been no significant change in its risk profile during 2020–21.

Southern Water have seen an increase in reported instances this year, however, this reflects improvements in its reporting of incidents which is giving us a much more accurate view of its level of risk.

Risk drivers:

- Incidents as a result of deteriorating assets, trips and hazards.
- Lack of training and controls to prevent incidents through poor behaviours and the handling of hazardous materials.
- Environmental from damage, disturbance and nuisance as a result of business activities.
- Integrity of dams and reservoirs.
- Threats to asset security and personal safety due to unexpected incidents.

Mitigating strategy

- Clearly defined strategy, safety protocols and standards are set to help prevent injury and occupational ill health to its employees and contractors, and are continuously reviewed and changed in line with legislation and industry bestpractice.
- Site safety inspections and audits to assess working practises and equipment.
- Suppliers and delivery partner performance is monitored to ensure they meet its standards and expectations forhealth safety and wellbeing.
- Mechanism for reporting near misses and lost time incidents, with follow-up investigation process established.
- Health safety and wellbeing performance and compliance is monitored and reported monthly to the Executive Leadership Team and the Board.
- Mandatory health, safety and wellbeing training for all employees, including mental health awareness training.
- Employees have access to a digital mental health platform 'Unmind' and Mental Health First Aiders.

Corporate risk- 11 Corporate affairs

Risk Climate Key: Deteriorating🔴 Stable🟡 Improving🟢

Description:

During recent years, there has been a significant focus on the water industry at a political and regulatory level. Failure to effectively monitor and adapt to any changes in its regulatory frameworks, or a failure to influence change to the political or regulatory landscape, may lead to potential increases in administrative costs, reduced revenue, and ultimately non-compliance. Its current business plan and approved pricing structure runs until 2025. The Final Determination imposes stringent financial constraints, performance incentives and targets, making longer term resilience more challenging.

There is a risk that changes in the political landscape (e.g. Brexit) may cause costly consequential impacts on the water sector to which Southern Water will have to adapt.

Southern Water's executive accountability:

Director of Regulation

Link to Southern Water's values:

Doing the right thing / Always improving

Forecasted business impact:

Long term

Areas impacted:

Customer experience, brand and reputation,legal and regulatory

Risk climate: 🟡

Risk maintained following Ofwat's Final Determination and potential changes in future regulatory environment and future price reviews. There has been no significant change in its risk profile during 2020–21.

Risk drivers:

- Inability to meet assumed performance as reflected in ODI performance.
- Ineffective regulatory change horizon scanning.
- Lack of influence in shaping the outcomes of change.
- Ability to adapt and transform the business to meet the changing environments in which Southern Water operate.
- Inability to influence the perception of the business following past events.

Mitigating strategy

- Closely monitor developments in the requirements from all of its regulators on key issues.
- Maintain close dialogue with Government, Ofwat and other regulators on key issues.
- Work with its customers to understand their perception of its delivery, and future ambitions.
- Continue to engage constructively with all of its regulators in regards to the water scarcity challenges Southern Water face in the South East of England.
- Input the outputs of the appeals to the Competition and Markets Authority by four companies in the sector against their final determinations, and their implications for the next Price Review.
- Work with its regulators on how Southern Water better understand and address its customers' needs to enable successful outcomes in the next price review period 2025–30.

Corporate risk- 12 Transformation

Risk Climate Key: Deteriorating🔴 Stable🟡 Improving🟢

Description:

Through a comprehensive and ongoing transformation programme, the business is completely committed to delivering the level of service its customers, and all of its stakeholders, expect and deserve. The degree of transformation in itself brings with it both risks and significant opportunities, which Southern Water will closely monitor.

The business has identified a significant volume of change required to transform the business over the 2020–25 period. There is a risk that these business changes will not lead to delivery of efficiencies, improve its general performance, and support its incentive performance.

Due to financial constraints, and the impacts caused by the COVID-19 pandemic, its ability to conclude and sustain the volume of change could be impacted due tofurther restraints in capacity or capability. As a result Southern Water may not be able to effectively coordinate the required changes, which might result in the possible failure to deliver some customer promises, including financial targets and incentives.

Southern Water's executive accountability:

Managing Director

Link to Southern Water's values:

Doing the right thing / Always improving

Forecasted business impact:

Medium term

Areas impacted:

Customer experience, business disruption,legal and regulatory, people, financial

Risk climate: 🔴

There has been a deterioration in its risk profile during 2020–21 – its execution plans are comprehensive but also challenging, and the financial pressure on the company as a whole will be substantial. This is notwithstanding managing the effects of the COVID-19 pandemic ensuring that its employees and contractors are able to carry out their work safely.

Risk drivers:

- Failure to deliver transformation and realise strategic benefits.
- A lack of governance in the management and delivery of business-wide transformation programmes.
- Negative impact on employee morale and fatigue through continued change.
- Ability to attract and retain the right skills to get optimum value from its people.
- Failure to appropriately train and develop employees to retain key capability.

Mitigating strategy

- Several strategic projects have been initiated to support the delivery of efficiencies.
- Comprehensive approach to the development of its execution plan that includes a range of activity to support the realisation of strategic benefits.
- A high level strategic talent review has been completed across the organisation.
- Workforce planning analysis that has captured external market trends and labour statistics has been completed across the business.
- Control Transformation Project underway which includes people plan.
- Annual Workforce planning process to be implemented which will review existing workforce, obtain market insight on industry needs and identify critical data feeds.
- Talent review board to be put in place to provide insight to senior management of the future business capability and capacity needs.
- Plan to develop People Plans for each directorate and functions to identify skills for the future that will feed into the overarching HR People Strategy.
- Transformation portfolio, office, and governance forums established.
- All business initiatives are developed with standard processes, ranked in order of priority, resources and wider business impacts.
- Annual engagement surveys are used to assess its employee satisfaction, with action plans developed to identify and improve any areas of concern in the business.

Corporate risk- 13 Covid 19

Risk Climate Key: Deteriorating🔴 Stable🟡 Improving🟢

Description:

The COVID-19 pandemic has put unprecedented pressure on the overall operation of the organisation.This has impacted all areas.

However, Southern Water has moved quickly to ensure it maintains service levels to its customers and are ensuring that its employees and contractors are able to carry out their work safely. Southern Water provided payment breaks to support customers during challenging financial circumstances. The move to home working for a large proportion of its employees has impacted the way Southern Water work. If uncontrolled, COVID-19 would have potential to cause significant harm to ability to carry out its essential services and put its colleagues at risk of COVID-19.

Southern Water executive accountability:

Chief Executive Officer

Link to Southern Water's values:

Doing the right thing / Always improving / Succeedingtogether

Forecasted business impact:

Short term

Areas impacted:

Customer experience, business disruption,legal and regulatory, people, financial

Risk climate: 🟡

Coming on top of a very tight Final Determination, the COVID-19 pandemic has impacted the way Southern Water carry out its business and has presented significant challenges to its finances, its ability to provide its essential services to customers and meet regulatory targets and expectations. In addition, the risk has led to us transforming the way Southern Water do its business with increased remote working and additional processes to enable safe working for field-team working.

Risk drivers:

Failure to manage this risk could lead to the realisation of a number of issues including:

- Colleagues could be at risk of COVID-19, anxiety or other health and wellbeing issues.
- Its supply chain could not meet its needs, with the consequential impact upon its services.
- Operational failures due to resource gaps, chemical supplies/parts restrictions and customer demand increases /behaviour change could impact its essential services to customers of water supply, wastewater collection and customer contact.
- Managing concurrent events (e.g. asset failure, heat wave, property flooding) during COVID-19 will be more challenging due to additional social distancing and/or the increased number of vulnerable customers that will need additional support.
- Operational performance or regulatory duty issues linked to COVID-19 could result in challenges associated with regulatory penalties (ODIs) or other regulatory action such as enforcement or prosecution.
- Adverse financial impact due to revenue loss, increased bad debt and additional COVID-19 costs.

Mitigating strategy

Southern Water has developed a COVID-19 continuity plan, which is reviewed and adjusted as appropriate. All decisions and changes implemented as a result of COVID-19 are managed through existing governance processes.

At the start of the pandemic, Southern Water moved in just one week from business as usual to a well-rehearsed Business Continuity Plan running against four simple priorities which have informed our COVID-19 response:

- Maintaining provision of essential services at all times
- Protecting the health, safety and wellbeing of our employees, including our supply chain, and our customers
- Providing the maximum practicable level of assistance to our vulnerable customers
- Protecting the financial stability of our business.

In terms of its domestic customers, many are facing uncertain futures and are struggling to pay their water bills. This means we supported them in the short term, offering payment breaks and increased access to our support tariffs, while making sure that we monitor and prepare for the potential of increasing bad debt in the long term.

Directors' report for the year ended 31 March 2021

The directors of Greensands Holdings Limited (Registered Number: Jersey 98700) present their report and the audited financial statements for the year to 31 March 2021.

Group

Greensands Holdings Limited (the company) was incorporated on 28 September 2007 as the parent company of Greensands Europe Limited, whose subsidiaries include Greensands Investments Limited.

On 15 October 2007, the company became the ultimate parent company of the Southern Water group of companies, via the acquisition of Southern Water Capital by Greensands Investments Limited.

Principal activities of the company

The company's principal activity is that of a holding company for Greensands Europe Limited and its subsidiaries. The directors expect the company to continue to carry out these activities in the future.

In carrying out these activities the company is reliant on distributions from companies lower down in the group structure as its sole source of capital.

Principal activities of the Group

The principal activities of the Group are the provision of water supply and wastewater services in the south-east of England.

The trading results reflect the performance of the major trading subsidiary Southern Water Services Limited (Southern Water).

Strategic report

The information that fulfils the requirement of the Strategic Report can be found in the Strategic Report sections on pages 2 to 17 and pages 18 to 41.

Future developments

The information regarding future developments of the company can be found in the Strategic Report sections on pages 2 to 17 and pages 18 to 41.

Results and dividends

The consolidated statement of other comprehensive income on page 48 shows the Group's results and profit for the year. Further details are also available in the Strategic Report section from page 2.

No ordinary dividends were declared during the year ended 31 March 2021 (2020: £nil).

The company generated a profit for the financial year of £44.0 million (2020: loss £236.8 million). The profit this year has been caused by recognising an impairment reversal of £44.7 million in relation to amounts owed by group undertakings. Please see note 7 for further details.

Directors and their interests

The directors who held office during the year ended 31 March 2021 and up to the date of signing the financial statements, unless otherwise stated, were as follows:

None of the directors who held office during the financial year had any disclosable interests in the shares of the company or the Group.

B Somes
R Wall (Resigned 13 October 2020)
P Hedley
S Howard

J Lynch
H De Run (Appointed13 October 2020)

Research and development

The improvement of existing services and processes, together with the identification and development of new technology and solutions, are important aspects of the Group's strategy to enhance the quality of service to customers and improve methods of working. Research and development charged to the income statement amounted to £0.6 million (2020: £0.5 million).

Employees

Employee involvement: The Group recognises the importance of its employees and is committed to effective two-way communication and consultation.

The Group has re-established an Employee Voice Group to facilitate meaningful consultation between management and employees through elected employee representatives. The group meets regularly at both a functional and company-wide level.

In 2017, the Group introduced the Gallup employee survey which has been continued to be undertaken every six months to help develop management action plans, and provide insight into the views of employees. The Group also conducts further surveys throughout the year on specific matters, the results of which are reported to management or the board as appropriate.

The Group recognises the rights of every employee to join a trade union and participate in its activities. The Group via Southern Water has a single union agreement with Unison.

General information is posted on the Group intranet and regular team briefing sessions are also held. The information in these publications and briefings covers a wide range of subjects that affect the business, including progress on business and capital projects, the impact of regulatory issues and wider financial and economic issues that may affect the Group.

Equal opportunity: The Group's policy is to promote equality of opportunity in recruitment, employment continuity, training and career development. The Group takes full account of the needs of people with disabilities and follows set policies and procedures to support reasonable adjustments in the workplace.

Health and safety: The Group recognises its duties to make proper provision for the health, safety and welfare at work of its employees.

Every employee receives a copy of the corporate policy statement on health and safety. There are regular meetings of employee representatives and managers to consider all aspects of health and safety. In addition there is a health and safety management review group which ensures that there is an adequate system for meeting the Group's responsibilities for health and safety to its staff, customers and members of the public.

The Group holds an annual Health and Safety Conference, which this year focused on wellbeing. It attracted people from across the Group and its partners to share the latest developments within the health and safety industry. The Group is committed to the 'Time for change' programme to raise awareness and understanding of mental health issues.

The Group provides an internal occupational health service for employees, including the provision of physiotherapy. These services have been developed and are continuously reviewed to ensure they meet the needs of the business and its employees at work.

Disabled employees: Applications for employment by disabled persons are always fully considered, bearing in mind the abilities of the applicant concerned. In the event of members of staff becoming disabled every effort is made to ensure that their employment with the Group continues and that appropriate training is arranged. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

Speak Up: Employees are actively encouraged to Speak Up if they see things that are not quite right. This helps us work better as a Group and fosters a culture to ensure that the Group is always doing the right thing for each other, its customers, the environment and other stakeholders.

Environmental issues

The Group is committed to meeting or improving upon legislative and regulatory environmental requirements and codes of practice, and aims to contain the environmental impact of its activities to a practicable minimum.
The Group recognises its responsibility to operate within a framework that supports sustainable development and has established, where possible, indicator targets which are measurable. Performance against these targets is monitored and reported regularly.

Political donations

No political donations were made in either year.

Land and buildings

In the opinion of the directors, the market value of land is significantly more than its book value. However, it would not be practicable to quantify the difference precisely.

Financial risk management objectives and policies

Details of the financial risk management are covered in the risk section on page 22 of the Strategic Report and note 23 to the consolidated financial statements.

Going concern

The directors have undertaken a detailed review of the company's liquidity requirements compared with the cash and facilities available, the financial covenant position including projections based on future forecasts, the current credit ratings of entities within the Group and financial risk.

During this process it was identified that the implementation of the 2019 Final Determination for Southern Water Services Limited and reduced dividends arising was leading to increasing difficulties in complying with the financial covenants applicable to the debt held in the group structure above Southern Water Services Limited. The Group's financing may also be subject to certain credit rating covenants outside of the Greensands Holdings Limited Directors' control. At 31 March 2021 the Group was in compliance with its financial covenants, however ratios were close to trigger levels and the parent company gearing was at a 'lock up' level, restricting the flow of dividends out of the Group. The liquidity available to pay interest on debt at the Greensands holding companies level would be exhausted by October 2021 if refinancing steps are not successful.

The Directors have performed a strategic review and engaged external specialist advisors to identify and assess the options available, to the Board and shareholders, to financially restructure the Greensands Group above the regulated company Southern Water. The financial restructuring plans under consideration, amongst a range of options, include additional investment from third parties where negotiations are at an advanced stage. Other options should these not complete could include covenant amendments, liquidity being made available and/or debt restructuring to provide liquidity to meet the requirements of the Group's borrowing facilities. Whilst discussions regarding additional investment from third parties are at an advanced stage, final agreement on these plans and contractual completion has not yet happened. This represents a material uncertainty associated with the going concern assumption. Having considered the status of the discussions with third parties the directors have a reasonable expectation that the company will maintain adequate resources to continue in operational existence for the foreseeable future, being a period of at least 12 months from the approval of these financial statements.

In forming this assessment the directors have considered the following information:

- The group's business activities, together with the factors likely to affect its future development, performance and position, which are set out in the Strategic Report on pages 2 to 17.

- The potential impact of COVID-19 on company and group operations and financial performance.

- The financial position of the company, its cash flows, liquidity position, covenants and borrowing facilities, which are described in the Financial Performance review on pages 2 to 7.

- New financing totalling £1,125 million (net £1,101.1 million) was raised in 2020–21 by one of the company's subsidiaries, Southern Water Services (Finance) Limited. As at 31 March 2021, Southern Water Services Limited has available a combination of cash and committed undrawn bank facilities totalling £714.5 million (2020: £874.3 million). These funds are sufficient to fund the operating and capital investment activities of Southern Water Services Limited for the 12 months from the date of signing the financial statements.

- Southern Water Services Limited obtained a waiver from its lenders in February 2021 which allows full use of available liquidity, plus the raising of new finance, even in a Trigger Event scenario of a credit rating downgrade or a breach of a trigger debt compliance ratio.

- Southern Water operates in an industry that is currently subject to economic regulation rather than market competition. Ofwat, the economic regulator, has a statutory obligation to set price limits that it believes will enable the water companies to finance their activities.
- The engagement, by the Greensands Holdings Board, of external specialist advisors to identify and assess the options available, to the Greensands Holdings Board and shareholders, in order to financially restructure the Group. The financial restructuring plans under consideration, amongst a range of options, include additional investment from third parties, where negotiations are at an advanced stage. Other options should these not complete could include covenant amendments, liquidity being made available and/or debt restructuring to provide liquidity to meet the requirements of the Group's borrowing facilities.

- The Eurobonds issued by Greensands Europe Limited continue to accrue interest but hold no requirement for payment in the foreseeable future. As detailed in note 38 since the 31st March 2021 the Eurobonds have been purchased from the shareholders for equity and no longer represents external group debt.

As a result of the factors listed above, the directors have a reasonable expectation that the Group will maintain adequate resources to continue in operational existence for the next 12 months and they continue to adopt the going concern basis of accounting in preparing the annual financial statements. However, there is a material uncertainty related to a financial restructuring which has not been completed at the time of issuing the financial statements as identified above, which raise significant doubt about the ability of the Group and the Company to continue as a going concern and therefore the Group and Company may be unable to realise their assets and discharge their liabilities in the normal course of business.

Qualifying third party indemnity

Following shareholder approval, the Group has provided an indemnity for its directors and the Company Secretary, which is a qualifying third party indemnity provision for the purposes of the Companies Act 2006.

Directors' responsibilities statement

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the International Accounting Standards Board and as adopted by the European Union. The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the preparation and presentation of financial statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable IFRSs. However, directors are also required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the company's ability to continue as a going concern.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies (Jersey) Law 1991. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Responsibility statement

Greensands Holdings Limited confirm that to the best of its knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group; and
- the management report, which is incorporated into the directors' report, includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that they face.

Statement of disclosure of information to auditor

Each of the persons who is a director at the date of approval of this report confirms that:

(1) so far as the director is aware, there is no relevant audit information of which the Group’s auditor is unaware; and

(2) he/she has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the Group’s auditor is aware of that information.

Auditor

Deloitte LLP has indicated its willingness to continue in office.

Approved by the Board of Directors and signed on its behalf by:

R Manning
Company Secretary
6th July 2021

Financial statements

Consolidated income statement

For the year ended 31 March 2021

	Note	**2021**	2020
		£m	£m
Continuing operations			
Revenue	5	**784.2**	878.0
Amortisation of regulatory settlement	5	**35.6**	-
Total revenue		**819.8**	878.0
Other operating income	5	**1.7**	1.4
Operating costs before trade receivables impairment charge, depreciation and amortisation		**(369.4)**	(376.9)
Trade receivables impairment charge		**(34.8)**	(29.6)
Operating costs before depreciation, amortisation and regulatory settlement		**(404.2)**	(406.5)
Depreciation and amortisation		**(293.0)**	(271.3)
Total operating costs		**(697.2)**	(677.8)
Operating profit	6	**124.3**	201.6
Operating profit before regulatory settlement		**88.7**	201.6
Regulatory settlement		**35.6**	-
Operating profit		**124.3**	201.6
Other income	6	**-**	-
Profit on disposal of property, plant and equipment	6	**0.8**	0.9
Finance income	10	**100.7**	32.9
Finance costs	10	**(391.5)**	(374.9)
Fair value (losses)/gains on derivative financial instruments	10	**(456.6)**	349.4
Net finance (costs)/income	10	**(747.4)**	7.4
(Loss)/profit before taxation		**(622.3)**	209.9
Taxation credit/(charge)	11	**67.6**	(106.5)
(Loss)/profit for the financial year		**(554.7)**	103.4

The notes on pages 54 to 109 form part of these financial statements.

Consolidated statement of other comprehensive income

For the year ended 31 March 2021

	Note	**2021**	2020
		£m	£m
(Loss)/profit for the financial year		**(554.7)**	103.4
Other comprehensive (expense)/income:			
Items that cannot be reclassified to profit or loss:			
Actuarial (loss)/gain on pension scheme	25	**(70.0)**	111.7
Movement on deferred tax relating to retirement benefit obligations	24	**13.3**	(17.5)
Total other comprehensive (expense)/income for the year, net of tax		**(56.7)**	94.2
Total comprehensive (expense)/income for the year attributable to the owners of the company		**(611.4)**	197.6

Consolidated statement of financial position
as at 31 March 2021

	Note	Group 2021 £m	Group 2020 £m
Non-current assets			
Goodwill	12	**85.1**	85.1
Intangible assets	13	**189.7**	42.1
Property, plant and equipment	14	**6,609.6**	6,495.4
Investments	16	**0.1**	0.1
Derivative financial instruments	23	**68.2**	203.0
		6,952.7	6,825.7
Current assets			
Inventories	17	**6.3**	5.1
Trade and other receivables	18	**192.0**	212.5
Cash and cash equivalents	33	**417.2**	282.5
		615.5	500.1
Total assets		**7,568.2**	7,325.8
Current liabilities			
Trade and other payables	19	**(288.9)**	(263.1)
Borrowings	20	**(99.3)**	(778.4)
Lease liabilities	22	**(2.5)**	(2.2)
Regulatory settlement liability	26	**(24.2)**	(35.6)
Provisions for liabilities	27	**(3.9)**	(5.1)
		(418.8)	(1,084.4)
Non-current liabilities			
Borrowings	21	**(6,588.3)**	(5,270.2)
Lease liabilities	22	**(27.2)**	(28.2)
Derivative financial instruments	23	**(1,503.7)**	(1,376.4)
Deferred tax liabilities	24	**(335.4)**	(416.3)
Retirement benefit obligations	25	**(116.5)**	(62.5)
Regulatory settlement liability	26	**(75.6)**	(99.9)
Provisions for liabilities	27	**(4.3)**	(4.7)
Other non-current liabilities	28	**(159.3)**	(32.7)
		(8,810.3)	(7,290.9)
Total liabilities		**(9,229.1)**	(8,375.3)
Net liabilities		**(1,660.9)**	(1,049.5)
Equity			
Called up share capital	29	**921.9**	921.9
Share premium account	30	**4.5**	4.5
Non-distributable reserve	31	**76.9**	60.2
Retained losses	32	**(2,664.2)**	(2,036.1)
Total deficit		**(1,660.9)**	(1,049.5)

The financial statements of Greensands Holdings Limited (Registered Number: Jersey 98700) on pages 47 to 109 were approved by the Greensands Holdings Limited Board and authorised for issue on 6th July 2021. They were signed on its behalf by

S Howard
Director
6th July 2021

Company statement of financial position

as at 31 March 2021

	Note	**Company 2021 £m**	Company 2020 £m
Non-current assets			
Investments	16	**-**	-
Other non-current assets	15	49.3	-
		49.3	-
Current assets			
Trade and other receivables	18	0.5	0.2
		0.5	0.2
Total assets		**49.8**	0.2
Current liabilities			
Trade and other payables	19	(37.7)	(32.1)
Non-current liabilities			
Borrowings	21	(59.2)	(59.2)
Total liabilities		**(96.9)**	(91.3)
Net liabilities		**(47.1)**	(91.1)
Equity			
Called up share capital	29	**921.9**	921.9
Share premium account	30	**4.5**	4.5
Retained losses	32	**(973.5)**	(1,017.5)
Total deficit		**(47.1)**	(91.1)

The company reported a profit for the financial year ended 31 March 2021 of £44.0 million (2020: loss of £236.8 million). Further details can be found in note 7.

The financial statements of Greensands Holdings Limited (Registered Number: Jersey 98700) on pages 50 to 109 were approved by the Greensands Holdings Limited Board and authorised for issue on 6th July 2021. They were signed on its behalf by

S Howard
Director
6th July 2021

Consolidated statement of changes in equity

For the year ended 31 March 2021

	Called up share capital (Note 29) £m	Share premium account (Note 30) £m	Non-distributable reserve* (Note 31) £m	Retained Earnings (Note 32) £m	Total £m
At 1 April 2019	**921.9**	**4.5**	**53.8**	**(2,227.3)**	**(1,247.1)**
Profit for the financial year	-	-	7.8	95.6	103.4
Other comprehensive income/(loss) for the year:	-	-	-	-	-
Actuarial gain on pension scheme	-	-	-	111.7	111.7
Movement on deferred tax relating to retirement benefit obligations	-	-	-	(17.5)	(17.5)
Total comprehensive income for the year	-	-	7.8	189.8	197.6
Reserves transfer*	-	-	(1.4)	1.4	-
Balance at 31 March 2020	**921.9**	**4.5**	**60.2**	**(2,036.1)**	**(1,049.5)**
Profit/(loss) for the financial year	-	-	18.2	(572.9)	(554.7)
Other comprehensive income/(loss) for the year:					
Actuarial (loss)/gain on pension scheme	-	-	-	(70.0)	(70.0)
Movement on deferred tax relating to retirement benefit obligations	-	-	-	13.3	13.3
Total comprehensive expense for the year	-	-	18.2	(629.6)	(611.4)
Reserves transfer*	-	-	(1.5)	1.5	-
Balance at 31 March 2021	**921.9**	**4.5**	**76.9**	**(2,664.2)**	**(1,660.9)**

* The non-distributable reserve arose upon adoption of IFRS 15 and relates to deemed revenue on adoption of assets from customers and is being amortised to reserves in line with the depreciation of the related assets.

Company statement of changes in equity

For the year ended 31 March 2021

	Called up share capital (Note 29) £m	Share premium account (Note 30) £m	Retained earnings (Note 32) £m	Total £m
Balance at 1 April 2019	**921.9**	**4.5**	**(780.7)**	**145.7**
Loss and total comprehensive expense for the financial year	-	-	**(236.8)**	**(236.8)**
Balance at 31 March 2020	**921.9**	**4.5**	**(1,017.5)**	**(91.1)**
Loss and total comprehensive expense for the financial year	-	-	**44.0**	**44.0**
Balance at 31 March 2021	**921.9**	**4.5**	**(973.5)**	**(47.1)**

Consolidated statement of cash flows

For the year ended 31 March 2021

	Note	2021 £m	2020 £m
Cash from operations		**377.8**	476.8
Tax paid		**-**	(0.1)
Net cash from operating activities	33	**377.8**	476.7
Investing activities			
Interest received		**101.7**	29.8
Purchase of property, plant and equipment		**(344.8)**	(461.6)
Purchase of intangible assets		**(36.9)**	(11.8)
Proceeds on disposal of property, plant and equipment		**0.5**	0.5
Net cash used in investing activities		**(279.5)**	(443.1)
Financing activities			
Interest paid		**(178.3)**	(323.6)
Payments on derivative instruments		**(194.5)**	-
Repayment of borrowings		**(696.2)**	(642.8)
Repayments of obligations under finance leases		**(1.8)**	(1.5)
Advances on restructure of derivative instruments		**-**	140.0
Proceeds of new loans		**1,107.2**	562.0
Net cash from/(used in) financing activities		**36.4**	(265.9)
Net increase/(decrease) in cash and cash equivalents		**134.7**	(232.3)
Cash and cash equivalents at beginning of the year		**282.5**	514.8
Cash and cash equivalents at end of the year		**417.2**	282.5

Company statement of cash flows

For the year ended 31 March 2021

No statement of cash flows is prepared for the company due to it not holding any cash balances in the current or prior year.

Notes to the consolidated financial statements
For the year ended 31 March 2021

1 Accounting policies

The principal accounting policies, which have been applied consistently throughout the current and preceding year, are set out below.

Basis of preparation

Greensands Holdings Limited is a company incorporated in Jersey (JE98700) under the Companies Act. The address of the registered office is given on page 1. The principal activities of the company and its subsidiaries (the Group) and the nature of the Group's operations are set out in the Strategic Report on pages 2 to 17.

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs). The financial statements have also been prepared in accordance with IFRSs adopted by the European Union and therefore the Group financial statements comply with Article 4 of the EU IAS Regulation.

The financial statements have been prepared on the going concern basis under the historical cost convention, except for the revaluation of financial instruments, which occurs at the end of each reporting period as explained in the accounting policies below.

Historical cost is generally based on the fair value of the consideration given in exchange for the goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement purposes in these consolidated financial statements is determined on such a basis, except for leasing transactions that are within the scope of IFRS 16 ‘Leases’, and measurements that have some similarities to fair value but are not fair value, such as net realisable value in IAS 2 ‘Inventories’ or value in use in IAS 36 ‘Impairment of Assets’.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:
- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

Basis of consolidation

The Group financial statements include the financial statements of the company and all entities controlled by the company (its subsidiaries) made up to 31 March each year.

Control is achieved when the company: has the power over the investee, is exposed, or has rights, to variable return from its involvement with the investee; and has the ability to use its power to affects its returns. The company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of these three elements of control.

The company considers that it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally.

Consolidation of a subsidiary begins when the company obtains control over the subsidiary and ceases when the company loses control of the subsidiary. Specifically, the results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the date the company gains control until the date when the company ceases to control the subsidiary.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with the Group’s accounting policies. All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between the members of the Group are eliminated on consolidation.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

1 Accounting policies (continued)

Adoption of new and revised accounting and financial reporting standards

There have been no new or revised accounting standards adopted in the current year that had a significant or material impact on the financial statements.

Going concern

The directors have undertaken a detailed review of the company's liquidity requirements compared with the cash and facilities available, the financial covenant position including projections based on future forecasts, the current credit ratings of entities within the Group and financial risk.

During this process it was identified that the implementation of the 2019 Final Determination for Southern Water Services Limited and reduced dividends arising was leading to increasing difficulties in complying with the financial covenants applicable to the debt held in the group structure above Southern Water Services Limited. The Group's financing may also be subject to certain credit rating covenants outside of the Greensands Holdings Limited Directors' control. At 31 March 2021 the Group was in compliance with its financial covenants, however ratios were close to trigger levels and the parent company gearing was at a 'lock up' level, restricting the flow of dividends out of the Group. The liquidity available to pay interest on debt at the Greensands holding companies level would be exhausted by October 2021 if refinancing steps are not successful.

The Directors have performed a strategic review and engaged external specialist advisors to identify and assess the options available, to the Board and shareholders, to financially restructure the Greensands Group above the regulated company Southern Water. The financial restructuring plans under consideration, amongst a range of options, include additional investment from third parties where negotiations are at an advanced stage. Other options should these not complete could include covenant amendments, liquidity being made available and/or debt restructuring to provide liquidity to meet the requirements of the Group's borrowing facilities. Whilst discussions regarding additional investment from third parties are at an advanced stage, final agreement on these plans and contractual completion has not yet happened. This represents a material uncertainty associated with the going concern assumption. Having considered the status of the discussions with third parties the directors have a reasonable expectation that the company will maintain adequate resources to continue in operational existence for the foreseeable future, being a period of at least 12 months from the approval of these financial statements.

In forming this assessment the directors have considered the information set out in the Directors' Report, Going Concern section above.

In conclusion, the directors have a reasonable expectation that the Group will maintain adequate resources to continue in operational existence for the next 12 months and they continue to adopt the going concern basis of accounting in preparing the annual financial statements. However, there is a material uncertainty related to a financial restructuring which has not been completed at the time of issuing the financial statements as identified above, which raise significant doubt about the ability of the Group and the Company to continue as a going concern and therefore the Group and Company may be unable to realise their assets and discharge their liabilities in the normal course of business.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

1 Accounting policies (continued)

Business combinations

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquiree and the equity interest issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in profit or loss as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognised at their fair value at the acquisition date, except that:

- deferred tax assets or liabilities and assets or liabilities related to employee benefit arrangements are recognised and measured in accordance with IAS 12 ‘Income Taxes’ and IAS 19 ‘Employee Benefits’ respectively; and
- assets (or disposal groups) that are classified as held for sale in accordance with IFRS-5 ‘Non-current Assets Held for Sale and Discontinued Operations’ are measured in accordance with that Standard.

Goodwill arising in a business combination is recognised as an asset at the date that control is acquired (the acquisition date). Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the acquirer’s previously held equity interest (if any) in the entity over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after reassessment, the Group’s interest in the fair value of the acquiree’s identifiable net assets exceeds the sum of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the acquirer’s previously held equity interest in the acquiree (if any), the excess is recognised immediately in profit or loss as a bargain purchase gain.

Goodwill is not amortised but is reviewed for impairment at least annually.

For the purpose of impairment testing, goodwill is allocated to each of the Group’s cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period. On disposal of a cash-generating unit, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Segmental reporting

The Group's revenue arises from the provision of services within the United Kingdom. It has a large and diverse customer base and is not reliant on any single customer.

The Southern Water board and management team review all internal management information on a single segment basis and accordingly no segmental information is provided in this report.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Revenue recognition

The group has adopted IFRS 15 'Revenue from Contracts with Customers' from 1 April 2018.

Revenue represents the income receivable (net of value added tax) in the ordinary course of business for goods and services provided. In respect of unbilled charges, revenue includes an estimate of the consumption between the date of the last meter reading and the period-end. The revenue accrual is estimated using a defined methodology based upon historical billing, consumption information and the applicable tariff.

Revenue from the supply of services represents the value of services provided under contracts to the extent that there is a right to consideration and is recorded at the fair value of the consideration due.

The group recognises revenue when it transfers control over a product or service to a customer.

Revenue is recognised when the amount of revenue can be measured reliably and it is probable that the economic benefits associated with the transaction will flow to the Group. Revenue is not recognised when it is considered probable that economic benefits will not be received. In these circumstances revenue is only recognised when collectability is reasonably certain. Payments received in advance of revenue recognition are recorded as deferred income.

<u>Water and wastewater services</u>
The company supplies water and wastewater services to customers in Sussex, Kent, Hampshire and the Isle of Wight. The performance obligation is the supply of services over the contractual term and is considered to be satisfied as the customer consumes based on the volume of water supplied. This is the point at which revenue is recognised.

For provisioning purposes, revenues and outstanding arrears are segmented based on customer characteristics. Since the group's only operating company, Southern Water Services Limited is under a statutory obligation to provide water and wastewater services to its domestic properties these services could be provided to customers who are unlikely to pay. Should a group of customers attract a provision rate of 100%, i.e. assessed as not generating economic benefit, revenue would not be recognised. In 2019–20 no segment of customers met this criterion and so revenue has been recognised in full.

Unmetered income is based on either the rateable value of the property or on an assessed volume of water supplied. Metered income is based on actual or estimated water consumption. Customer rebates are shown as a reduction in revenue.

<u>New connections and infrastructure charges</u>
Under IFRS 15 the performance obligation is satisfied at the point of provision of the new connection to the network, so fees received in respect of the connection are recognised at this point.

<u>Requisitions</u>
For requisitions of water mains and public sewers, the group has determined that the performance obligation is satisfied at the point of completion of the requisition works and connection of the water main or lateral drain, and the total consideration receivable is recognised in full as revenue at that point.

<u>Diversions</u>
Contributions received in respect of diversions of water mains and sewers are recognised upon completion of the diversion of the water main or sewer.

<u>Adoptions</u>
Adoptions of assets are recognised at fair value of the asset upon adoption i.e. the point at which control of the asset is obtained, within revenue as an increase to non-distributable reserves.

Interest income is recognised on a time proportionate basis using the effective interest method.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established (provided that it is probable that the economic benefits will flow to the group and the amount of revenue can be measured reliably).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Provision for impairment of trade receivables

The impairment provision is calculated by assessing and applying estimated recovery rates to various categories of trade receivables, reflecting past collections experience and expectations of future recovery of outstanding receivables at the date of the statement of financial position.

This assessment generates an expectation for the level of recovery of the outstanding receivables balance and therefore the lifetime expected credit loss.

The model considers current and forward looking macro-economic events to the extent that the past response of customers to changes in the economy is built into the expected future cash collection performance for each customer segment.

Taxation

The taxation charge in the income statement represents the sum of the tax currently payable and deferred tax.

Current taxation is based on the result for the year as adjusted for disallowable and non-taxable items and items of income or expense which are taxable or deductible in other years. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the statement of financial position date.

Deferred taxation is tax expected to be payable on temporary differences between the treatment of certain items for taxation and accounting purposes. Deferred taxation is provided on all temporary differences that have originated but not reversed by the end of the reporting period. It is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised based on tax laws and rates that have been enacted or substantively enacted at the reporting date.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is regarded as probable that taxable profits will be available against which deductible temporary differences can be utilised.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

1 Accounting policies (continued)

Goodwill

Goodwill represents a single cash generating unit, being the excess of cash paid by Greensands Investments Limited for the fair value of assets acquired from Southern Water Capital, the then ultimate parent company of the Southern Water group of companies, less amortisation charged up to the date of transition to IFRS from UKGAAP on 1 April 2014.

Goodwill is initially recognised and measured as set out above and in note 12 with the carrying value being reviewed for any indicators of impairment on an annual basis.

Intangible assets

Intangible assets comprises:

i. Assets under development.
ii. Other assets – comprising software, studies and development projects.
iii. Future right to draw water from Portsmouth Water through the Havant Thicket reservoir scheme.

Intangible assets are measured at cost less subsequent amortisation and any impairment. Amortisation of intangible assets is calculated on a straight-line basis over the estimated useful lives, which are primarily three to 10 years*. The estimated useful life and amortisation method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Capitalised development costs are for plant installed on some of its sites to test new processes for performance data and scalability. The data is used to identify innovative and efficient future assets and processes to meet new higher environmental or quality standards. Development costs capitalised are depreciated over three to five years.

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

* Amortisation of the Havant Thicket reservoir scheme will be over the period to 2100 and will commence on the earliest of 1 April 2029, the date Southern Water is entitled to receive water, and completion of construction.

Property, plant and equipment

Property, plant and equipment comprises:

i. Freehold land and buildings – comprising land and non-operational buildings.
ii. Plant and machinery – comprising structures at sites used for water and wastewater treatment; pumping or storage, where not classed as infrastructure, along with associated fixed plant.
iii. Infrastructure assets – comprising a network of systems consisting of mains and sewers, impounding and pumped raw water storage reservoirs, sludge pipelines and sea outfalls.
iv. Assets under construction.
v. Other assets – comprising vehicles, computers, mobile plant and meters.

All property, plant and equipment is stated in the statement of financial position at cost or at deemed cost on transition to IFRS, less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

The costs of repairs to the infrastructure network are recognised in the income statement as they arise.

Expenditure which results in replacement or renewal of infrastructure or enhancements to the operating capability of the infrastructure network is capitalised.

Items of property, plant and equipment that are transferred to the company from customers or developers are initially recognised at fair value in accordance with IFRS 15 ‘Revenue from Contracts with Customers’.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Property, plant and equipment (continued)

The corresponding credit is recorded as revenue through non-distributable reserves and released to retained earnings over the expected useful lives of the related assets.

Borrowing costs directly attributable to the construction of qualifying assets, that necessarily take a substantial period of time to get ready for their intended use, are capitalised during the period of time that is required to complete and prepare the asset for its intended use. The commencement of capitalisation begins when both finance costs and expenditures for the asset are being incurred and activities that are necessary to get the asset ready for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to get the asset ready for use are complete. Other borrowing costs are expensed.

Subsequent costs are included in the asset's carrying amount or recognised as separate assets, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the income statement as incurred.

Assets are depreciated on a straight-line basis over their estimated operating lives, which are principally as follows

		Years
Land and buildings:	- Land[1]	Not depreciated
	- Buildings	10-60
Plant and machinery:	- Operational structures[2]	15–80
	- Fixed plant	10–40
Infrastructure assets:	- Water mains	100–120
	- Sewers	80–200
	- Reservoirs	200
	- Ancillary structures	10–70
Assets under construction[1]:		Not depreciated
Other:	- Vehicles, computers and mobile plant	3–10

The estimated useful lives and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

[1] Freehold land is not depreciated, nor are assets in the course of construction until they are commissioned. Commissioning is deemed to occur when a new works is officially taken over from the contractor, following completion of performance and take-over tests.

[2] Operational structures are assets used for wastewater and water treatment purposes. These include water tanks and similar assets.

Right-of-use assets are depreciated over the shorter period of the lease term and the useful life of the underlying asset. If a lease transfers ownership of the underlying asset or the cost of the right-of-use asset reflects that the group expects to exercise a purchase option, the related right-of-use asset is depreciated over the useful life of the underlying asset.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

1 Accounting policies (continued)

Impairment of tangible and intangible assets

At the end of each reporting period, the Group reviews the carrying amounts of its tangible and intangible assets, to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised immediately in the income statement, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised immediately in the consolidated income statement, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Grants and contributions

Grant and contributions received are treated as either revenue or deferred income in line with IFRS 15 as defined by the nature of the receipt.

Infrastructure receipts associated with new connections are recognised as revenue when they are receivable.

Deemed contributions from the transfer of non-current assets from customers are recognised as revenue through non-distributable reserves and released to retained earnings over the life of the asset.

Grants and contributions receivable in respect of non-current assets are treated as deferred income and released to other income over the useful economic life of those fixed assets.

Grants and contributions received in respect of new connections to the water and sewerage networks are treated as deferred income and released to revenue in line with the expected expenditure they are intended to compensate.

Grants and contributions received in respect of diversions of water mains and sewers are treated as deferred income and recognised as revenue upon completion of the diversion.

Grants and contributions which are given in compensation for expenses incurred with no future related costs are recognised in revenue in the period that they become receivable.

Leases

The group has adopted IFRS 16 ‘Leases’ with effect from 1 April 2019.

(i) The Group as lessee

The group assesses whether a contract is or contains a lease, at inception of the contract. The group recognises a right-of-use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets (£5,000 or less). For these leases, the group recognises the lease payments as an operating expense on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern in which economic benefits from the leased assets are consumed.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Lease payments included in the measurement of the lease liability comprise:

- fixed lease payments;
- variable lease payments that depend on an index or rate, initially measured using the index or rate at the commencement date;
- the amount expected to be payable by the lessee under residual value guarantees;
- the exercise price of purchase options, if the lessee is reasonably certain to exercise the options; and
- payments of penalties for terminating the lease, if the lease term reflects the exercise of an option to terminate the lease.
- The lease liability is presented as a separate line in the statement of financial position.

The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability (using the effective interest method) and by reducing the carrying amount to reflect the lease payments made.

The group remeasures the lease liability (and makes a corresponding adjustment to the related right-of-use asset) whenever:

- The lease term has changed or there is a significant event or change in circumstances resulting in a change in the assessment of exercise of a purchase option, in which case the lease liability is remeasured by discounting the revised lease payments using a revised discount rate.
- The lease payments change due to changes in an index or rate or a change in expected payment under a guaranteed residual value, in which cases the lease liability is remeasured by discounting the revised lease payments using an unchanged discount rate (unless the lease payments change is due to a change in a floating interest rate, in which case a revised discount rate is used).
- A lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is remeasured based on the lease term of the modified lease by discounting the revised lease payments using a revised discount rate at the effective date of the modification.

The group did not make any such adjustments during the year.

The right-of-use assets comprise the initial measurement of the corresponding lease, lease payments made at or before the commencement day and any direct initial costs. They are subsequently measured at cost less accumulated depreciation and impairment losses.

Right-of-use assets are depreciated over the shorter period of lease term and useful life of the underlying asset. The depreciation starts at the commencement date of the lease.

The right-of-use assets are presented separately from other assets in the notes to the financial statements.

The group applies IAS 36 to determine whether a right-of-use asset is impaired and accounts for any identified impairment loss as described in the ‘Property, Plant and Equipment’ policy.

As a practical expedient, IFRS 16 permits a lessee not to separate non-lease components, and instead account for any lease and associated non-lease components as a single arrangement. The group has used this practice with respect to the maintenance element associated with vehicle leases.

(ii) The Group as lessor

The sale of income rights relating to aerial masts and sites owned by the Group to third parties is treated as an operating lease. Income received from such sales is received entirely in advance and is therefore taken to deferred revenue and credited to the income statement over the life of the lease.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Non-current asset investments

Investments held as non-current assets, including investments in subsidiaries, are stated at cost, less, where appropriate, provision for any impairment in value. The carrying values of non-current asset investments are reviewed for impairment in periods if events or changes in circumstances indicate the carrying value may not be recoverable.

Cash and cash equivalents

Cash and cash equivalents comprise cash and short-term bank deposits with an original maturity of three months or less, net of outstanding bank overdrafts. The carrying amount of these assets is equal to their fair value.

Inventories

Inventory is held for use in the production of water supply and treatment of wastewater. Raw materials and work in progress are valued at the lower of cost and net realisable value. Cost is determined using the first-in, first-out (FIFO) method. Net realisable value is the estimated selling price, less further costs expected to be incurred to completion and costs to be incurred in marketing, selling and distribution.

Deferred revenue

Deferred revenue includes monies received from customers where the related service has not yet been provided.

Amounts are deferred to the statement of financial position and released to the consolidated income statement in line with the period of the service provided.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle that obligation and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

An environmental provision is made for the costs relating to decommissioned or dormant assets which have been identified as having an environmental impact.

Retirement benefits

The Group operated a defined benefit pension scheme which closed on 31 March 2020, the assets of which are held separately from those of the Group in independently administered funds. An independent actuary conducts a valuation of this pension scheme every three years.

The liability recognised in the statement of financial position in respect of the defined benefit pension scheme is the present value of the defined benefit obligation at the end of the period less the fair value of plan assets. The current service cost, which is the increase in the present value of the liabilities of the Group’s defined benefit pension scheme expected to arise from employee service in the period, is charged to operating costs. The net interest on the scheme’s net assets/(liabilities) is included in other finance charges. Actuarial gains and losses are recognised in the consolidated statement of other comprehensive income.

The pension cost under IAS 19 ‘Employee Benefits’ is assessed in accordance with the advice of a firm of actuaries based on the latest actuarial valuation and assumptions determined by the actuary. The assumptions are based on information supplied to the actuary by the Group, supplemented by discussions between the actuary and management. The assumptions are disclosed in note 25.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Retirement benefits (continued)

Profit before taxation and net liabilities are affected by the actuarial assumptions used. The key assumptions include: discount rates, pay growth, mortality and increases to pensions in payment and deferred pensions, and may differ from actual results due to changing market and economic conditions and longer or shorter lives of participants.

The Group also operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the Group in an independently administered fund. Group contributions to the scheme are charged to the income statement in the period to which they relate. Differences between contributions actually paid are shown as either accruals or prepayments in the statement of financial position.

Financial instruments

The group has adopted IFRS 9 ‘Financial Instruments’ from 1 April 2018.

IFRS 9 introduces new requirements for 1) the classification and measurement of financial assets and financial liabilities, 2) impairment for financial assets and 3) general hedge accounting. There was no material impact resulting from the application of this standard.

In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires entities to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition of the financial assets. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognised.

Financial assets and financial liabilities are recognised in the Group’s statement of financial position when the Group becomes a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss (FVTPL)) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at FVTPL are recognised immediately in the consolidated income statement.

Financial assets

(i) Loans receivable

Loans receivable that have fixed or determinable payments that are not quoted in an active market are classified as ‘held to collect’. Loans receivable are measured at fair value on initial recognition and subsequently measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

(ii) Trade receivables and accrued income

Trade receivables and accrued income are classified as ‘held to collect’ and measured at fair value on initial recognition. If there is objective evidence that the amount receivable is impaired it is written down to its recoverable amount, with the irrecoverable amount being recognised as an expense in operating costs.

The group applies an approach permitted by IFRS 9 for estimating expected credit losses on trade receivables. For trade receivables that are assessed not to be impaired individually, expected credit losses are estimated based on the group’s historical experience of trade receivable write-offs, and forward-looking macro-economic events to the extent that the past response of customers to changes in the economy is built into the expected future cash collection performance for each customer segment.

The provision for impairment of trade receivables is calculated by applying estimated recovery rates to various categories of debt, reflecting past collections experience and expectations of future recovery of outstanding receivables at the date of the statement of financial position.

This assessment generates an expectation for the level of recovery of the outstanding receivables balance and therefore the lifetime expected credit loss.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Impairment of financial assets

All debt type financial assets which are not measured at FVTPL are assessed for indicators of impairment at each reporting date using a forward looking approach by identifying expected credit losses ('ECL's). ECLs are defined as the difference between the contractual cash flows that are due in accordance with the contract and the cash flows that the group expected to receive, discounted at the original effective interest rate.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate. The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account.

Based on that analysis at the end of the reporting period, the impairment on the Group's assets, other than trade receivables, are considered to be immaterial and no allowance has been recognised in these financial statements.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. On derecognition of a financial asset the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

Financial liabilities

Fixed rate interest-bearing borrowings are initially measured at fair value, net of transaction costs, and are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Issue costs in relation to index-linked and variable rate bonds are separately disclosed within creditors.

The carrying value of index-linked debt instruments is adjusted for the annual movement in the retail price index. The change in value arising from indexation is charged or credited to the income statement in the year in which it arises.

Premiums and proceeds such as those from gilt lock agreements received on issue of debt instruments are credited to the income statement over the term of the debt at a constant rate on the carrying amount.

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

1 Accounting policies (continued)

Derivative financial instruments

The Group enters into a variety of derivative financial instruments to manage its exposure to inflation risk in line with the Group's risk management policy and no speculative trading in financial instruments is undertaken. Further details of derivative financial instruments are disclosed in note 23.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently re-measured to their fair value at the end of each reporting period. The resulting gain or loss is recognised in the income statement immediately.

Certain derivative instruments, principally index-linked swaps, do not qualify for hedge accounting, and as such, the Group does not currently apply hedge accounting.

A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be realised or settled within 12 months. Other derivatives are presented as current assets or current liabilities.

Embedded derivatives

In accordance with IFRS 9 the Group has reviewed all contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value through profit and loss.

An embedded derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the hybrid instrument to which the embedded derivative relates is more than 12 months and is not expected to be realised or settled within 12 months. Other derivatives are presented as current assets or current liabilities.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

2 Critical accounting judgements and key sources of estimation uncertainty

In the application of the Group's accounting policies, which are described in note 1 above, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements

Critical judgements, apart from those involving estimations, that are applied in the preparation of the financial statements are discussed below:

(i) Revenue recognition

The Group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured. When the Group considers that the criteria for revenue recognition are not met for a transaction, revenue recognition is delayed until such time as collectability is reasonably assured.

Payments received in advance of revenue recognition are recorded as deferred income. Under IFRS 15, revenue is recognised when a customer obtains control of the goods or services and the performance obligation is complete.

Particular challenges exist within the water industry as formal written contracts do not exist for most transactions with customers. Contracts are instead implied through statute and regulation. Judgment is therefore required in identifying the services contained within the contract and the customer with whom the contract is entered into, which in turn impacts on how the performance obligations are considered and therefore revenue recognised.

(ii) Regulatory settlement

The treatment of the regulatory settlement was considered in the light of the specific circumstances of the approach agreed with Ofwat as noted on page 99 Reflecting that this relates to past performance and matters outside the normal regulatory framework for agreeing amounts for future billing to customers it was considered appropriate to accrue for this settlement in the 2019 financial statements when it became possible to quantify the financial impact.

There is no clear accounting standard guidance for the income statement treatment of this regulatory settlement. It was considered whether the settlement should be recognised as an expense; however, given that this is an agreed reduction in customer bills in the future, with a requirement to show this separately on invoicing as required by Ofwat, the most appropriate treatment was concluded to be to treat the invoice reductions as a reduction in revenue in 2018-19. This will be separately identified and unwound on the face of the income statement in future periods. The £3 million penalty payable to Ofwat was treated as an operating expense.

(iii) Property, plant and equipment

The Group recognises property, plant and equipment (PPE) on its water and wastewater infrastructure assets where such expenditure enhances a significant length of the network or increases the capacity of the network, whereas any expenditure classed as maintenance is expensed in the period it is incurred. Determining enhancement from maintenance expenditure is a subjective area, particularly when assessing whether the length of network replaced enhances the network. In addition, management capitalise time and resources incurred by the Group's support functions on capital programmes based on judgments made in respect of the proportion of capital work performed by these functions.

(iv) Going concern

Note 1 above sets out the key judgements arising in respect of going concern.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

2 Critical accounting judgements and key sources of estimation uncertainty (continued)

(v) Impairment
An assessment of the recoverable amount of goodwill (£85.1 million) allocated to the excess of cash paid by Greensands Investments Limited for the fair value of assets acquired from Southern Water Capital, the then ultimate parent company of the Southern Water group of companies, has been undertaken. The directors consider the recoverable amount to be most sensitive to the achievement of the 2021 budget and business plan of the next AMP period (2020 to 2025) of Southern Water, the group's only operating company. Budgets comprise forecasts of revenue, staff costs, overheads and interest based on current and anticipated market conditions that have been considered and approved by the Board. Whilst the group is able to manage most of the revenues generated by Southern Water, the cost projections are open to uncertainty due to factors such as unexpected weather events, inherent credit risk associated with its customer base, availability of finance at acceptable rates and regulatory pressures.

The group has faced various financial performance challenges during the year, namely from the imposed penalty sanctioned by Ofwat in response to Southern Water's wastewater treatment works compliance reporting. The year has also seen some one off additional costs in relation to Southern Water's current transformation programme, which in the long-term is expected to yield savings and efficiencies operationally.

However, the directors having assessed the outlook of the future performance and cash flows of the group are satisfied that the book value of the group is supportable in comparison to the Regulatory Capital Value (RCV) of Southern Water. Therefore, no provision for impairment has been made (2020: £nil).

Consideration of impairment associated with Company investments and intercompany receivables is given in note 7.

Sources of estimation uncertainty
The key assumptions about the future and other key sources of estimation uncertainty at the reporting period end that may have a risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed below:

(i) Measured income accrual
The measured income accrual is an estimation of the amount of water and wastewater unbilled at the period end. The accrual is estimated using a defined methodology based upon historical billing and consumption information and the applicable tariff. The calculation is sensitive to estimated consumption for measured customers. Actual consumption may differ from the estimate made which could impact future operating results positively or negatively.

The value of household billings raised in the year ended 31 March 2021 for consumption in prior years was £245.4 million. The value of these billings was lower than the accrual made at 31 March 2020. The estimation difference was £2.2 million and this has been recognised in the current year's revenue. This difference is well within its view of acceptable tolerances for accounting estimates.

(ii) Impairment of trade receivables
The trade receivables impairment provision at each reporting date is calculated by segmenting customer debt based on historic debt collection and payment performance, demographic information and the age of debt outstanding. For each segment, forecast cash collection rates are determined which result in a corresponding provision percentage. This assessment generates an expectation for the level of recovery of the outstanding receivables balance and therefore the lifetime expected credit loss.

The model considers current and forward looking macro-economic events to the extent that the past response of customers to changes in the economy is built into the expected future cash collection performance for each customer segment. Its underlying charge to the income statement on this basis was £13.6 million.

To reflect the significant impact that the COVID-19 pandemic is having on the macro-economic environment Southern Water has recognised an additional charge of £16.0 million, for the impairment of trade receivables, to the income statement in 2019–20. This is a significant judgment as the overall impact that the pandemic will have on the economy is continuing to evolve.

The value of the provision for impairment as at 31 March 2021 was £xxx million (2020: £216.4 million). The actual level of receivables collected may differ from the estimated levels of recovery, which could impact future operating results positively or negatively.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

2 Critical accounting judgements and key sources of estimation uncertainty (continued)

(ii) Impairment of trade receivables (continued)

Its sensitivity analysis suggests that the impairment provision would vary between £1.9 million and £5.7 million if cash collections estimates were between 1% and 3% above or below those predicted.

Impairment provision sensitivity analysis	31 March 2021	Sensitivity			
		1%	3%	-1%	-3%
Impairment provision estimate (£m)	253.9	2.3	7.1	-2.3	-7.1

(iii) Retirement benefit obligations

The Group operates a defined benefit scheme as well as a defined contribution scheme. Under IAS 19 'Employee Benefits' the Group has recognised an actuarial loss of £70.0 million for the year to 31 March 2021 (2020: gain of £111.7 million).

The pension cost and liabilities under IAS 19 are assessed in accordance with directors' best estimates using the advice of an independent qualified actuary and assumptions in the latest actuarial valuation. The assumptions are based on member data supplied to the actuary and market observations for interest rates and inflation, supplemented by discussions between the actuary and management. The mortality assumption uses a scheme-specific calculation based on CMI 2018 actuarial tables with a smoothing factor of 7.5 and a 1.25% pa allowance for future longevity improvement.

The major assumptions used to measure schemes' liabilities, along with sensitivities to changes in those assumptions and future funding obligations are set out in note 25 of the financial statements.

(iv) Provisions and contingent liabilities

The group evaluates its exposures to contingent liabilities relating to pending litigation or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation. A provision is recognised when it is probable that an obligation exists for which a reliable estimate can be made after careful analysis of the individual matter. Analysis includes assessing the likelihood that a pending claim will succeed, or a liability will arise, and the point of recognition for the associated liability.

Matters that either are possible obligations or do not meet the recognition criteria for a provision are disclosed as contingent liabilities in note 34, unless the possibility of transferring economic benefits is remote. In particular there is a contingent liability associated with an Environment Agency investigation set out in note 34 which it has not been possible to estimate. Accordingly an associated sensitivity analysis cannot be disclosed.

Provisions determined may change in the future due to new developments and as additional information becomes available. Reflecting the inherent uncertainty in this evaluation process actual cost may be different from the estimated provision. Details of provisions are disclosed in note 27 and the value provided at 31 March 2021 was £8.2 million (2020: £9.8 million). Accordingly if the amount provided was 50% under or overestimated then the provision would change by £4.1 million (2020: £4.9 million).

(v) Goodwill

An impairment review on goodwill is conducted at least annually. The net asset value of the subsidiaries is used in the impairment review. Therefore any estimations or judgements used in respect to the value of the assets or liabilities of the subsidiaries may affect the outcome of the impairment review. Whilst high levels of headroom were identified at 31 March 2021 significant reductions to the calculated recoverable value in future years could lead to a material impairment given the large values held.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

3 Changes in significant accounting policies

A number of new standards and amendments are effective for periods beginning from 1 January 2020. These changes had no material impact on the company's financial statements.

4 Segmental analysis

The directors believe that the whole of the Group's activities constitute a single class of business. The Group's revenue is generated wholly from within the United Kingdom. The Greensands Holdings Limited Board and management team review all internal management information on a single segment basis and accordingly no segmental information is provided in this report.

5 Income

An analysis of the group's income is as follows:

Continuing operations	**2021**	2020
	£m	£m
Water and sewerage services:		
Household - measured	**511.4**	544.3
Household - unmeasured	**110.6**	130.7
Non-household - measured	**100.3**	140.4
Non-household - unmeasured	**4.0**	5.1
Total water and sewerage services	**726.3**	820.5
Bulk supplies	**4.5**	3.9
Infrastructure charge receipts	**5.3**	9.7
Requisitioned mains and sewers (see note (a) below)	**(0.3)**	(0.6)
Diversions	**1.8**	0.6
Adoptions (see note (b) below)	**18.2**	7.8
Other services	**28.4**	36.1
Total revenue before regulatory settlement	**784.2**	878.0
Regulatory settlement (see note (c) below)	**35.6**	-
Total revenue	**819.8**	878.0
Other operating income (see note (d) below)	**1.7**	1.4
Profit on disposal of property, plant and equipment	**0.8**	0.9
Interest receivable (note 10)	**100.7**	32.9
Total income	**923.0**	913.2

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

5 Income (continued)

a) Income from requisitions of mains and sewers is offset by refunds to developers in the year made against income recognised in previous periods.

b) Revenue associated with the adoption of assets from customers is treated as non-distributable upon recognition, and amortised to retained earnings in line with the depreciation of the related assets.

c) As reported in note 26 the group has been co-operating with Ofwat in relation to its investigation into the management, operation and performance of its wastewater treatment works.

To ensure that our customers are not disadvantaged as a result of these matters, Southern Water has agreed to make direct customer rebates totalling £135.5 million in forecast outturn prices (£122.9 million in 2017–18 prices) over the period 2020–25. This reflects the seriousness of the breaches identified in the investigation. These rebates are now being made and recorded through the water and sewerage services revenue shown above. The provision for these rebates made in the financial statements for 2018–19 is also being released through revenue in line with the annual profile of the rebates to be made.

d) Other operating income includes the release of deferred grants and contributions relating to non-current assets from the balance sheet, as amortised in line with the useful economic life of the related assets, and rents receivable.

6 Group operating profit for the year

Group loss for the year has been arrived at after charging/(crediting):	**2021 £m**	2020 £m
Depreciation and amortisation on		
- Owned assets	**275.9**	**254.5**
- Assets held under finance leases	**3.4**	**3.7**
	279.3	**258.2**
Included within *Operating costs: Depreciation and amortisation* in the income statement:		
Amortisation of intangible assets	**13.7**	**13.1**
Profit on disposal of property, plant and equipment	**0.8**	**0.9**
Research and development expenditure	**0.6**	**0.5**
Rentals under operating leases:		
- Properties	**0.1**	**0.2**
- Vehicles	**1.7**	**1.1**
Employee costs (note 8a)	**67.6**	**78.6**
Amortisation of grants and contributions (see note 28)	**(1.5)**	**(1.2)**
Regulatory settlement (see note (b) below)	**35.6**	**-**
Fees payable to the company's auditor in respect of:		
- statutory audit of the company's financial statements	**0.5**	**0.5**
- other services pursuant to legislation (see note (c) below)	**0.1**	**0.1**
- all other services	**0.1**	**0.1**
Total audit and non-audit fess	**0.7**	**0.7**

Other services pursuant to legislation and other non-audit services primarily relate to regulatory assurance fees.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

6 Group operating profit for the year (continued)

(a) The group has adopted IFRS 16 'Leases' with effect from 1 April 2019. Rentals under operating leases comprise payments on leases that have been assessed as short-term (12 months or less) agreements and leases of low value assets (£5,000 or less) (see Note 1 Accounting Policies for more information on the company's approach to IFRS 16 Leases).

(b) As reported in note 26 the group co-operated with Ofwat in relation to its investigation into the management, operation and performance of Southern Water's wastewater treatment works.

In addition to the provision for direct customer rebates of £135.5 million disclosed in note 5, a provision of a further £3.0 million was made within operating costs in 2018–19 for the fine imposed by Ofwat in relation to these matters.

(c) Other services pursuant to legislation and other non-audit services primarily relate to regulatory assurance fees.

7 Profit of the parent company

The profit for the financial year dealt with in the financial statements of the parent company is £44.0 million (2020: loss of £236.8 million). The company has taken advantage of an exemption not to prepare a company only income statement.

At the reporting date the company has conducted an impairment review based on the consideration of the overall value of the Greensands Holdings group. A comparison has been made between the Regulatory Capital Value (RCV) of Southern Water Services, as the operating company, to the value of investments held in the group at various consolidation levels moving all the way up to the ultimate controlling parent, Greensands Holdings Limited.

In order to undertake the impairment assessment, judgement has been made regarding the level of premium to RCV that is appropriate to consider. Typically this reflects historic transactions within the water industry and reviewing the market capitalisation of listed water companies. Additionally, consideration has been given to continued economic uncertainty and the performance of Southern Water relative to its peers.

Having taken into account the above and a negative reserves position held in the Greensands Europe Ltd group, the directors believe that the company's investment in Greensands Europe Ltd (GSE) of £1.0 million is fully impaired, along with £971.8 million in relation to the amounts owed by group undertakings. An impairment reversal of £44.7 million (2020: loss of £236.8 million) has been recognised in the income statement for the year.

The recoverable amount of the GSE group is a negative amount of £854.4 million (2020: £1,130.3million), which is considered to be its fair value measurement under level 2 as described in the accounting policies. The full cumulative impairment write down made by the company is £854.4 million (2020: £1,017.5 million) equal to the total available value of group assets held.

The value of impairment will continue to be reviewed annually to see whether the impairments remain or whether there are indications of an improvement in the position, for example an increase in the likely premium to RCV achievable at Southern Water. Should there be an improvement; values for the reduction in impairment would be written back as is the case this year.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

8 Employee information

		2021 £m	2020 £m
(a) Group employee costs			
Wages and salaries		**101.3**	105.2
Social security costs		**10.9**	11.3
Pension costs	- Defined contribution	**7.7**	4.9
	- Defined benefit	**0.2**	7.7
Total employee costs		**120.1**	129.1
Less: charged as capital expenditure		**(52.5)**	(50.5)
Charged to the income statement		**67.6**	78.6

Employee costs that are charged as capital expenditure are those directly related to the construction or acquisition of assets.

(b) Average number of persons employed by activity

The average monthly numbers of persons (including executive directors) employed by the Group during the year was:

	2021 Number	2020 Number (restated)
Operations	**1,176**	1,169
Customer services	**37**	98
Corporate centre	**925**	937
	2,138	2,204

The prior year figures have been restated to reflect the average numbers rather than the March year end numbers.

9 Directors' emoluments

During the year there were no payments made to directors by the Group in return for services as a director of Greensands Holdings Limited. However, payments of £100,000 and £75,000 were made by one of the ultimate shareholders to two of the directors (2020: £95,800 and £70,535).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

10 Net finance costs

	2021 £m	2020 £m
Finance income		
Interest receivable on swap instruments	**98.7**	31.9
Deposit income on short-term bank deposits	**2.0**	1.0
	100.7	32.9
Finance costs		
Interest payable on loans	**(401.4)**	(372.6)
Interest rate swap receipts	**-**	0.5
Indexation	**(20.5)**	(29.3)
Amortisation of issue costs	**(2.0)**	(2.9)
Amortisation of gilt lock proceeds	**0.1**	0.1
Amortisation of bond premium	**0.7**	0.7
Other finance expense (note 25)	**(1.3)**	(4.2)
	(424.4)	(407.7)
Amounts capitalised on qualifying assets	**32.9**	32.8
	(391.5)	(374.9)
Fair value (losses)/gains on derivative financial instruments		
Derivative financial instruments not designated as hedges (note 23)	**(456.6)**	349.4
Net finance costs	**(747.4)**	7.4

A large proportion of the payment of interest payable on loans falls due on 31 March. Where this date is not a business day, the interest is paid on the next following business day.

Borrowing costs included in the cost of qualifying assets during the year arose on the general borrowing pool and are calculated by applying a capitalisation rate of 4.10% to expenditure on such assets (2020: 3.96%).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

11 Taxation

	2021 £m	2020 £m
Current tax:		
Current year	**-**	-
Total current tax charge	**-**	-
Deferred tax:		
Origination and reversal of temporary differences	**(67.6)**	61.9
Adjustment in respect of prior years	**-**	(0.7)
Effect of corporation tax rate change	**-**	45.3
Total deferred (credit)/charge tax	**(67.6)**	106.5
Total tax (credit)/charge on loss	**(67.6)**	106.5

The tax assessed for the year is different to the standard rate of corporation tax in the UK due to the following factors:

	2021 £m	2020 £m
Profit/(loss) before tax	**(622.3)**	209.9
Current tax:		
Tax at the UK corporation tax rate of 19% (2020: 19%)	**(118.2)**	39.9
Permanent differences	**25.4**	20.9
Deferred tax assets not recognised	**25.2**	7.5
Differences between current and deferred tax rates	**-**	(6.4)
Impact of tax rate changes	**-**	45.3
Adjustment in respect of prior years – deferred tax	**-**	(0.7)
Tax (credit)/charge for year	**(67.6)**	106.5

Factors that may affect future tax charges:

In the March 2021 Budget it was announced that legislation will be introduced in Finance Bill 2021 to increase the main rate of UK corporation tax from 19% to 25%, effective 1 April 2023. As substantive enactment is after the balance sheet date, deferred tax balances as at 31 March 2021 continue to be measured at a rate of 19%. If the amended tax rate had been used, the deferred tax liability would have been £105.6m higher.

Based on current capital investment plans, the group expects to continue to be able to claim capital allowances in excess of depreciation in future years.

There is no expiry date in relation to un-provided amounts.

In addition to the amount charged to the consolidated income statement, the following amounts relating to tax have been recognised in the consolidated statement of other comprehensive income:

	2021 £m	2020 £m
Deferred tax		
Arising on income and expenses recognised in other comprehensive income:		
Tax (credit)/charge relating to retirement benefit obligations	**(13.3)**	19.0
Deferred tax movement due to rate change	**-**	(1.5)
Total deferred tax (credit)/charge recognised in other comprehensive loss	**(13.3)**	17.5

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

11 Taxation (continued)

Company
The tax charge for the year can be reconciled to the income statement as follows:

	Company 2021 £m	Company 2020 £m
Profit/(loss) before taxation	**44.7**	(236.8)
UK corporation tax rate at 19% on profit/(loss) for the year (2020: 19%)	**8.5**	(45.0)
Permanent differences	**0.7**	
Permanent differences arising on impairment loss	**(8.5)**	45.0
Total tax charge for year	**0.7**	-

12 Goodwill

Group	**£m**
Carrying amount at 1 April 2020	85.1
Impairment at 31 March 2021	-
Net book value at 31 March 2021	**85.1**

Goodwill represents a single cash generating unit, being the excess of cash paid by Greensands for the fair value of assets acquired from Southern Water Capital, the then ultimate parent company of the Southern Water group of Companies, less amortisation charged up to the date of transition to IFRS from UKGAAP on 1 April 2014.

Goodwill is reviewed annually for impairment by comparing the underlying statement of financial position value of the Group, having adjusted for net debt, with the Regulatory Capital Value (RCV) of Southern Water Services, being the basis of the recoverable amount. An assumed premium to the RCV utilising recent transactions in the water industry and other data to assess whether the book value of the Group is supportable.

Other indicators considered are, the financial performance, operating performance and future changes to the operating environment of its only operating company Southern Water Services.

To date no indicators of impairment have been identified in respect of goodwill or property, plant and equipment.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

13 Intangible assets

	Externally generated		
	Assets in development £m	**Other £m**	**Total £m**
Cost			
At 1 April 2020	18.4	119.3	**137.7**
Additions	161.3	-	**161.3**
Transfers	(25.8)	25.8	**-**
Disposals	-	-	**-**
At 31 March 2021	153.9	145.1	**299.0**
Amortisation			
At 1 April 2020	-	95.6	**95.6**
Charge for the year	-	13.7	**13.7**
Disposals	-	-	**-**
At 31 March 2021	-	109.3	**109.3**
Net book amount			
At 31 March 2021	**153.9**	**35.8**	**189.7**
At 31 March 2020	18.4	23.7	42.1

The Group currently does not have any internally generated intangible assets.

Included within additions above is £1.0 million (2020: £0.5 million) of interest that has been capitalised on qualifying assets in accordance with IAS 23 ‘Borrowing costs’. The cumulative net book value of the borrowing costs capitalised amount to £1.6 million (2020: £1.5 million).

Other intangible assets include software, studies and research and development projects.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

14 Property, plant and equipment

The Group tangible assets are shown below. The company has no tangible assets.

	Land & buildings £m	Plant & machinery £m	Infra-structure assets £m	Assets under construction £m	Other £m	Total £m
Cost						
At 1 April 2020	1,609.2	3,465.3	2,843.3	922.9	657.1	**9,497.8**
Additions	-	-	-	393.5	-	**393.5**
Transfers	26.5	323.7	108.3	(534.2)	75.7	**-**
Disposals	-	(9.0)	(0.5)	-	(9.0)	**(18.5)**
At 31 March 2021	1,635.7	3,780.0	2,951.1	782.2	723.8	**9,872.8**
Depreciation						
At 1 April 2020	808.8	1,523.8	183.0	-	486.8	**3,002.4**
Charge for the year	42.9	147.4	34.2	-	54.8	**279.3**
Disposals	-	(9.0)	(0.5)	-	(9.0)	**(18.5)**
At 31 March 2021	851.7	1,662.2	216.7	-	532.6	**3,265.4**
Net book amount						
At 31 March 2021	**784.0**	**2,117.8**	**2,734.4**	**782.2**	**191.2**	**6,609.6**
At 31 March 2020	800.4	1,941.5	2,660.3	922.9	170.3	6,495.4

Freehold land is stated at a cost of £51.7 million at 31 March 2021 and 31 March 2020 and is not depreciated.

The Group's interest in land and buildings are almost entirely freehold.

Included within additions above is £31.9 million (2020: £32.3 million) of interest that has been capitalised on qualifying assets in accordance with IAS 23 'Borrowing Costs'. The cumulative net book value of the borrowing costs capitalised amount to £239.2 million (2020: £216.9 million).

Assets held under finance leases

Included in the amounts shown above are the following amounts in relation to property, plant and equipment held under finance leases:

	Land & buildings £m	Infra-structure assets £m	Other £m	Total £m
Net book amount at 31 March 2020	28.9	-	3.5	32.4
Additions	-	-	1.1	1.1
Transfers	(11.7)	11.7	-	-
Depreciation charge for the year	(1.4)	(0.3)	(1.7)	(3.4)
Net book amount at 31 March 2021	**15.8**	**11.4**	**2.9**	**30.1**

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

15 Other non-current assets

	Company 2021 £m	Company 2020 £m
Amounts owed by group undertakings	**1,021.1**	1,016.5
Impairment	**(971.8)**	(1,016.5)
Amounts owed by group undertakings	**49.3**	-

All amounts due from group undertakings are unsecured, interest free and repayable on demand. The company has offered its support to group companies and is not intending to recall these balances within the next 12 months.

Please refer to note 7 for further details surrounding the impairment disclosed above.

16 Investments

	Group 2021 £m	Group 2020 £m
Other external investments		
At 1 April	**0.1**	0.1
Total investments as at 31 March	**0.1**	0.1

The investment above represents a non-controlling interest of 7.17% in a private limited company called, Landlord TAP Limited. The company owns a national web portal set up as part of a Water UK initiative to improve data on tenants and thereby increase collections with the aim of reducing customer receivables impairment.

	Company 2021 £m	Company 2020 £m
Greensands Europe Limited		
At 1 April	**-**	-
Impairment	**-**	-
Total investments at 31 March	**-**	-

A full list of subsidiaries is disclosed in note 37. Please refer to note 7 for further details surrounding the impairment loss disclosed above.

17 Inventories

	Group 2021 £m	Group 2020 £m
Raw materials	**4.3**	4.3
Work in progress	**2.0**	0.8
	6.3	5.1

The company does not hold any inventory.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

18 Trade and other receivables

	Group 2021 £m	Group 2020 £m
Trade receivables	**334.4**	315.9
Provision for impairment	**(247.5)**	(213.3)
Net trade receivables	**86.9**	102.6
Net accrued income	**64.7**	77.3
Prepayments	**22.1**	14.6
Other receivables	**18.3**	18.0
	192.0	212.5

Trade receivables comprise balances from contracts with customers where the company has performed some or all of its contractual obligations.

Accrued income as at 31 March 2021 includes water and sewerage income not yet billed of £55.2 million (2020: £62.4 million).

The directors consider that the carrying values of trade and other receivables are reasonable approximations of their fair values.

Provision for impairment

Movements on the impairment provision were as follows:

	Group 2021 £m	Group 2020 £m
At 1 April	**(216.4)**	(188.7)
Impairment charge	**(34.8)**	(29.6)
Amounts written off during the year	**(2.7)**	1.9
At 31 March	**(253.9)**	(216.4)

At each reporting date, the Group evaluates the recoverability of trade receivables and records allowances for impairment of receivables based on experience.

The Group does not include in revenue and trade receivables those accounts that are deemed irrecoverable.

The following table provides information regarding the ageing of receivables that are specifically provided for:

	Group 2021 £m	Group 2020 £m
Current	**0.1**	-
1-2 years	**0.1**	0.1
2-3 years	**0.2**	0.1
3-4 years	**0.6**	0.1
more than 4 years	**14.6**	2.4
	15.6	2.7

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

18 Trade and other receivables (continued)

A collective provision is recorded against assets which are past due but for which no specific provision has been made. This is calculated based on historical experience of levels of recovery.

The aged analysis of receivables that were overdue at the reporting date but not individually provided for is as follows:

	Group 2021 £m	Group 2020 £m
Current	**72.7**	76.8
1-2 years	**45.5**	44.4
2-3 years	**37.4**	38.9
3-4 years	**33.9**	33.8
more than 4 years	**103.6**	90.6
	293.1	284.5

The amounts above are reconciled to gross and net receivables in the tables below:

At 31 March 2021	**Gross £m**	**Provision £m**	**Group Net £m**
Accrued income – not due	**71.1**	**(6.4)**	**64.7**
Trade receivables			
Not due	**25.8**	**-**	**25.8**
Overdue not specifically provided	**293.1**	**(232.0)**	**61.1**
Overdue and specifically provided	**15.5**	**(15.5)**	**-**
	405.5	**(253.9)**	**151.6**

At 31 March 2020	Gross £m	Provision £m	Group Net £m
Accrued income – not due	80.4	(3.1)	77.3
Trade receivables			
Not due	28.7	-	28.7
Overdue not specifically provided	284.5	(210.6)	73.9
Overdue and specifically provided	2.7	(2.7)	-
	396.3	(216.4)	179.9

	Company 2021 £m	Company 2020 £m
Prepayments	**0.5**	0.2

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

19 Trade and other payables

	Group 2021 £m	Group 2020 £m
Trade payables	**32.4**	30.5
Capital creditors and capital accruals	**100.5**	104.2
Corporation tax	**-**	-
Taxation and social security	**4.0**	2.8
Accruals	**122.2**	95.0
Deferred revenue	**29.8**	30.6
	288.9	263.1

The directors consider that the carrying values of trade and other payables are not materially different from their fair values.

	Company 2021 £m	Company 2020 £m
Amounts owed to group undertakings	**37.2**	32.1
	37.2	32.1

The directors consider that the carrying values of trade and other payables are not materially different from their fair values.

20 Current borrowings

	Group 2021 £m	Group 2020 £m
Current		
Revolving credit facilities – Libor plus margin	**100.0**	430.0
Class A £350m – 5.010% fixed rate 2021	**-**	349.5
Premium deferred on issue	**0.7**	0.7
Deferred gilt lock proceeds (note 21 (ix))	**0.1**	0.1
Unamortised debt issuance costs (note 21 (vii))	**(1.5)**	(1.9)
Current borrowings excluding finance leases	**99.3**	778.4
Obligations under finance leases	**2.5**	2.2
Total current borrowings including finance leases	**101.8**	780.6

The Class A £300 million bond was repaid on 1 April 2019.

Further descriptions about the above items are given in note 21 'Non-current borrowings'.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

21 Non- current borrowings

An analysis of the external loans is shown below:

Loans and other borrowings:	Notes	Group 2021 £m	Group 2020 £m
Class A £350m 6.192% fixed rate 2029	21(i),(ii),(iii)	**371.0**	373.0
Class A £150m 3.706% index linked 2034	21(iii),(iv)	**285.9**	282.0
Class A £35m 3.706% index linked 2034	21(iii),(iv)	**66.8**	65.9
Class A £350m 6.640% fixed rate 2026	21(i),(ii)	**365.5**	368.2
Class A £150m 3.816% index linked 2023	21(iii),(iv)	**253.6**	252.0
Class A £350m 5.000% fixed rate 2021	21(i),(ii)	**-**	349.5
Class A £150m 5.000% fixed rate 2041	21(i),(ii)	**146.1**	146.0
Class A £200m 4.500% fixed rate 2052	21(i),(ii)	**197.3**	197.2
Class A £300m 5.125% fixed rate 2056	21(i),(ii)	**292.9**	292.9
Class A £175m 2.780% fixed rate 2031	21(ii)	**174.1**	174.1
Class A £75m 2.960% fixed rate 2036	21(ii)	**74.6**	74.6
Class A £375m 2.375% fixed rate 2029	21(ii)	**370.2**	-
Class A £450m 3.000% fixed rate 2038	21(ii)	**443.2**	-
Class A £300m 1.625% fixed rate 2027	21(ii)	**294.3**	-
Class A £60m – 0.000% index linked 2025	21(iv),(ix)	**44.1**	51.7
Class A £40m - 0.000% index linked 2026	21(iv),(ix)	**35.7**	41.0
Artesian £165m 4.076% index linked 2033	21(iii),(iv)	**318.0**	314.4
Artesian £156.5m 3.635% index linked 2032	21(iv)	**252.2**	248.2
Total Class A debt		**3,985.5**	3,230.7
Revolving credit facilities – Libor plus margin	21(xii)	**100.0**	430.0
£125m Facility Agreement 2022 – Libor plus 3.250%	21(v)	**123.9**	123.4
£75m Facility Agreement 2025 – Libor plus 4.000%	21(v)	**77.2**	73.5
£150m Facility Agreement 2025 – Libor plus 5.250%	21(v)	**156.2**	146.7
£100m Facility Agreement 2026 – Libor plus 5.250%	21(v)	**104.0**	97.6
£250m Facility Agreement 2025 – Libor plus 5.25%	21(v)	**260.3**	244.4
£50m Facility Agreement 2025 – Libor plus 2.500%	21(v)	**49.5**	49.5
£175m Facility Agreement 2025 – fixed rate 3.930%	21(ii)	**174.0**	173.9
£25m Facility Agreement 2025 – fixed rate 3.650%	21(ii)	**24.8**	24.7
£75m Facility Agreement 2028 – fixed rate 3.940%	21(ii)	**74.3**	74.2
£52m Facility Agreement 2030 – fixed rate 4.030%	21(ii)	**51.5**	51.4
£35.3m/($45m) Facility Agreement 2023 – fixed rate 3.384%	21(ii),(x)	**35.0**	34.9
£19.6m/($25m) Facility Agreement 2025 – fixed rate 3.681%	21(ii),(x)	**19.4**	19.4
£19.6m/($25m) Facility Agreement 2028 – fixed rate 4.020%	21(ii),(x)	**19.4**	19.4
Eurobonds 12.000% 2038 (note 35)	21(xi)	**1,569.6**	1,401.4
Unamortised debt issuance costs	21(vi)	**(149.0)**	(159.3)
Bond premium deferred on issue	21(vii)	**7.5**	8.2
Deferred gilt lock proceeds	21(viii)	**4.5**	4.6
Obligations under finance leases		**29.7**	30.4
Total borrowings		**6,717.3**	6,079.0
Disclosed as current borrowings	20	**101.8**	780.6
Disclosed as non-current borrowings		**6,615.5**	5,298.4

	Company 2021 £m	Company 2020 £m
Loans from group undertakings	**59.2**	59.2

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

21 Non-current borrowings (continued)

Class A loans are guaranteed and secured pursuant to a guarantee and security agreement (the Security Agreement). The agreement is over the entire property, assets, rights and undertaking of each of Southern Water Services Limited, Southern Water Services (Finance) Limited (SWSF), SWS Holdings Limited, and SWS Group Holdings Limited. In the case of Southern Water Services Limited, this is to the extent permitted by the Water Industry Act 1991 and the Licence to own and operate water assets.

Notes:

(i) The Group has entered into swap agreements that convert Class A fixed rate debt into either floating or index-linked debt in accordance with the Group's financial risk management policy.

(ii) Fixed rate bonds are recognised net of issue costs, discounts and inclusive of premiums (where applicable) on issue and are carried at amortised cost using the effective interest rate method.

(iii) The bond premiums referred to in note (ii) above also apply to various index-linked bonds. The premiums date back to 2003 when the related bonds were issued and arose when a number of the Group's swap instruments were effectively closed out and the resulting loss was rolled forward into the pricing of these bonds. The premiums are carried at amortised cost using the effective interest rate method.

(iv) The value of the capital and interest elements of the index-linked loans is linked to movements in the Retail Price Index. The increase in the capital value of index-linked loans during the year of £20.5 million (2020: £29.3 million) has been taken to the income statement as part of finance costs.

(v) Floating rate funds have been recognised net of associated issue costs and are being carried at amortised cost using the effective interest rate method.

(vi) Unamortised debt issuance costs represent issue fees paid by SWSF and SWGF that are not otherwise accounted for within the amortised cost of specific loans. Where these costs are attributable to a specific instrument they are being amortised over the life of that instrument. The remaining costs are being amortised over the weighted average life of the loans advanced at the time the costs were incurred. As at 31 March 2021 unamortised debt issuance costs amounted to £149.0 million (2020: £159.3 million) of which £1.5 million (2020: £1.5 million) represents the short-term amount which is disclosed separately in note 20.

In addition to the above, swap break costs are included within this balance. These costs originated prior to securitisation when a swap was entered into, to act as a hedge for the future issue of bonds under securitisation. The swap was closed out and break costs were incurred when the bonds were issued in July 2003. The accounting treatment of these costs mirror the amortised cost value of opposing related bonds referred to in note (iii) above. These bonds are inclusive of premiums that compensate the swap break costs suffered.

(vii) The deferred bond premium represents the additional book value of the Class A Artesian £156.5 million loan issued in 2004. The premium is being amortised over the life of the bond.

(viii) Prior to the issue of the Class A £300 million bond in the year to 31 March 2008, SWSF entered into a gilt lock agreement, resulting in the receipt of £6.3 million, which was advanced to SWS along with the proceeds of the bond issue. The proceeds have been deferred and are being released to the income statement over the life of the loan.

(ix) The Class A £60 million loan is index-linked with an interest rate of 0.00% until August 2025.
The Class A £40 million loan is index-linked with an interest rate of 0.00% until May 2026.

(x) The Group has entered into cross currency swap agreements that fix the Sterling rate required to pay interest on loan funds drawn in US Dollars in accordance with the Group's financial risk management policy.

(xi) The Eurobond loan includes £720.1 million of accrued interest (2020: £551.9 million). Compound interest is charged at 12%. No interest was paid in the current or prior year.

(xii) Revolving credit facilities drawdowns accrue interest at Libor plus an applicable margin between 0.30% and 1.50%, determined by reference to the credit rating of the company.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

21 Non-current borrowings (continued)

Repayments fall due as follows:	2021 £m	2020 £m
Borrowings excluding finance leases:		
Between one and two years not by instalments	**370.8**	122.8
Between two and five years not by instalments	**1,291.2**	327.8
After five years not by instalments	**4,926.3**	4,819.6
	6,588.3	5,270.2
On demand or within one year not by instalments	**99.3**	778.4
	6,687.6	6,048.6
Finance leases:		
Between one and two years not by instalments	**2.9**	2.2
Between two and five years not by instalments	**5.8**	6.2
After five years not by instalments	**18.5**	19.8
	27.2	28.2
On demand or within one year not by instalments	**2.5**	2.2
	29.7	30.4
Borrowings including finance leases:		
Between one and two years not by instalments	**373.7**	125.0
Between two and five years not by instalments	**1,297.0**	334.0
After five years not by instalments	**4,944.8**	4,839.4
	6,615.5	5,298.4
On demand or within one year not by instalments including finance leases	**101.8**	780.6
	6,717.3	6,079.0

The group leases various offices and vehicles and has a lease on its outfall pipes.

Vehicle leases have terms of between four and five years. Leases on office buildings have terms of between 15 and 99 years from commencement date. The outfall lease had an initial term of 99 years and commenced on 1 April 1997.

Obligations relating to vehicle leases includes some commercial vehicle leases with optional residual value balloon payments due at the end of the lease period, where the minimum lease payments (including finance charges) have been prepaid at the start of the lease. If the group opts not to pay the balloon payment, it must return the vehicle to the lessor.

All lease obligations are denominated in sterling.

The fair value of the group’s lease obligations is approximately equal to their carrying amount.

The group’s obligations under finance leases are secured by the lessors’ rights over the leased assets disclosed in note 14.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

22 Leases

This note provides information for leases where the group is a lessee.

i) Amounts recognised in the statement of financial position

The statement of financial position shows the following amounts relating to leases:

	2021 £m	2020 £m
Right of use assets within Property, Plant and Equipment:		
Buildings	**15.8**	28.9
Infrastructure	**11.4**	-
Other	**2.9**	3.5
	30.1	32.4
Lease liabilities		
Current	**2.5**	2.2
Non-current	**27.2**	28.2
	29.7	30.4

Additions to the right-of-use assets during the financial year to 31 March 2021 were £1.1 million (2020: £33.2 million).

ii) Amounts recognised in the income statement

The income statement shows the following amounts relating to leases:

	2021 £m	2020 £m
Depreciation charge of right-of-use assets		
Buildings and infrastructure	**(1.7)**	**(2.0)**
Other	**(1.7)**	**(1.7)**
	(3.4)	**(3.7)**
Interest expense (included in finance costs)	**(0.5)**	**(1.2)**
Expense relating to short-term leases (included in operating costs)	**(1.8)**	**(1.3)**

iii) Amounts recognised in the cash flow statement

	2021	2020
Total cash outflow for leases in the year to 31 March 2021	**(1.8)**	**(1.5)**

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

22 Leases (continued)

iv) The group's leasing activities and how these are accounted for

The group leases various offices and vehicles.

Rental contracts are typically made for fixed periods, but may have extension options.
Contracts may contain both lease and non-lease components. For leases of vehicles for which the group is a lessee, it has elected not to separate lease and non-lease components and instead accounts for these as a single lease component.

Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants other than the security interests in the leased assets that are held by the lessor. Leased assets may not be used as security for borrowing purposes.

Until the year to 31 March 2019, leases of property, plant and equipment were classified as either finance leases or operating leases, see note 1 for details. From 1 April 2019, leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the group.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease payments included in the measurement of the lease liability comprise (where applicable):

- fixed lease payments;
- variable lease payments that depend on an index or rate, initially measured using the index or rate at the commencement date;
- the amount expected to be payable by the lessee under residual value guarantees;
- the exercise price of purchase options, if the lessee is reasonably certain to exercise the options; and
- payments of penalties for terminating the lease, if the lease term reflects the exercise of an option to terminate the lease.
- the lease liability is presented as a separate line in the statement of financial position.

Lease payments to be made under reasonably certain extension options are also included in the measurement of the liability.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be readily determined, which is generally the case for leases in the group, the lessee's incremental borrowing rate is used, being the rate that the individual lessee would have to pay to borrow the funds necessary to obtain an asset of similar value to the right-of-use asset in a similar economic environment with similar terms, security and conditions.

Southern Water has a lease on its outfall pipes which contains variable lease payments. These payments will increase by RPI every 10 years. The next review date is on 1 April 2022 and the lease expires on 31 March 2096.

Right-of-use assets are measured at cost comprising the following:
- the amount of the initial measurement of lease liability
- any lease payments made at or before the commencement date less any lease incentives received
- any initial direct costs, and
- restoration costs.

Right-of-use assets are generally depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. If the group is reasonably certain to exercise a purchase option, the right-of-use asset is depreciated over the underlying asset's useful life.

Payments associated with short-term leases of equipment and vehicles and all leases of low-value assets are recognised on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less. Low-value assets comprise assets less than £5,000.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

23 Financial instruments

The following table provides a comparison by category of the carrying amounts of the Group's financial assets and financial liabilities at 31 March 2021 and 31 March 2020.

Financial assets and liabilities by category	Group 2021 £m	Company 2021 £m	Group 2020 £m	Company 2020 £m
Financial assets				
Derivative financial instruments designated as FVTPL*				
- Non-current	**68.2**	-	203.0	-
- Current	**-**	-	-	-
Held to maturity investments				
- Non-current	**0.1**	-	0.1	-
Trade and other receivables				
- Current (excluding prepayments)	**169.9**	-	197.9	-
Cash and cash equivalents				
- Current	**417.2**	-	282.5	-
Total financial asset	**655.4**	-	683.5	-
Financial liabilities				
Derivative financial instruments designated as FVTPL*				
- Non-current	**1,503.7**	**-**	1,376.4	-
Borrowings				
- Current (including lease liabilities)	**101.8**	**-**	780.6	-
- Non-current (including lease liabilities)	**6,615.5**	**59.2**	5,298.4	59.2
Trade and other payables				
- Current	**288.9**	**37.2**	263.2	32.1
Total financial liabilities	**8,509.9**	**96.4**	7,718.6	91.3

*Fair value through profit and loss.

The below table analyses derivative financial instruments held on the statement of financial position.

Derivative financial instruments	Group 2021 Assets £m	Group 2021 Liabilities £m	Group 2020 Assets £m	Group 2020 Liabilities £m
Derivative financial instruments not designated as hedges:				
Interest rate swaps	**-**	**-**	0.1	-
RPI swaps	**68.2**	**(1,500.6)**	194.2	(1,376.4)
Cross currency swaps	**-**	**(3.1)**	8.7	-
Total derivative financial instruments	**68.2**	**(1,503.7)**	203.0	(1,376.4)
Derivative financial instruments can be analysed as follows:				
Current	**-**	**-**	-	-
Non-current	**68.2**	**(1,503.7)**	203.0	(1,376.4)
	68.2	**(1,503.7)**	203.0	(1,376.4)

The notional principal amount of the outstanding interest swap contracts at 31 March 2021 was £1,316.6 million (2020: £1,516.6 million).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

23 Financial instruments (continued)

In accordance with IFRS 9 the Group has reviewed all contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard. None were identified during the year or previous year.

i) Financial risk management objectives and policies

The principal financial risks to which the Group is exposed are interest rate, liquidity and RPI risks. The Board has approved policies for the management of these risks.

Interest rate risk

The Group's interest rate risk is primarily in relation to its fixed rate borrowings (fair value risk) and floating rate borrowings (cash flow risk). Interest rate derivatives are used to manage the overall interest rate profile within the Group policy, which is to maintain a higher proportion of net debt at fixed rates of interest having regard to the prevailing interest rate outlook.

The weighted average effective interest rates at the statement of financial position dates by class of debt were as follows (based on loan book values including accrued accretion):

	Group 2021 %	Group 2020 %
By class of debt (all classed as financial liabilities)		
Class A	**4.05**	4.49
Artesian	**1.80**	1.83
Greensands	**5.25**	5.35

The weighted average interest costs at the statement of financial position dates were as follows (based on loan nominal values):

	Group 2021 %	Group 2020 %
Fixed	**6.87**	8.51
Floating	**5.45**	4.20
Indexed	**4.81**	4.81

Liquidity risk

The Group raises funds, as required, to ensure that it has sufficient cash and/or facilities to fund the business of Southern Water Services Limited for the next twelve months.

Credit risk

Trade receivables neither past due nor impaired relate to domestic and retail customers whose history of payments supports no impairment being made.

RPI risk and sensitivity analysis

The principal market risks are interest rates and movements in RPI. Interest rates on the Group’s loans are currently either fixed or fully effective swap instruments are in place to swap floating rates for fixed. RPI impacts indexation charged on index-linked loans and swaps. These instruments form an economic hedge with the Group’s revenues and regulatory assets, which are also linked to RPI inflation.

The Group also notes that Brexit and other economic matters such as COVID-19 will increase uncertainty around these risk areas in the short term.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

23 Financial instruments (continued)

Interest sensitivity analysis

The following table details the sensitivity of the group's profit before tax and equity to changes in interest rates. The sensitivity analysis has been based on the amount of net debt in place at the reporting date and, as such, is not indicative of the years then ended.

Increase/(decrease) in profit before tax and equity	**Group 2021**	Group 2020
1% increase in interest rate	**(29.2)**	(32.5)
1% decrease in interest rate	**29.2**	32.5

Inflation sensitivity analysis

The following table details the sensitivity of profit before tax to changes in the RPI on the group's index-linked borrowings. The sensitivity analysis has been based on the amount of index-linked debt held at the reporting date and, as such, is not indicative of the years then ended.

Increase/(decrease) in profit before tax and equity	**Group 2021**	Group 2020
1% increase in RPI	**(11.5)**	(22.8)
1% decrease in RPI	**11.5**	22.8

For further details about Group financing matters please refer to the 'Capital structure, liquidity and other financial matters' section of the Strategic Report contained within these financial statements on page 9.

ii) Maturity of financial liabilities and financial instruments

The maturity profile of the Group's financial liabilities at 31 March 2021 and 31 March 2020 is disclosed within note 21.

The table below analyses the Group's derivative financial instruments into relevant maturity profiles based on the remaining period at the reporting date.

	Within one year £m	**Within two to five years £m**	**Within five to 25 years £m**	**After 25 years £m**	**Total £m**
At 31 March 2021					
Derivative financial instruments – asset	**-**	**10.1**	**58.1**	**-**	**68.2**
Derivative financial instruments – liability	**-**	**(20.3)**	**(652.8)**	**(830.6)**	**(1,503.7)**
	-	**(10.2)**	**(594.7)**	**(830.6)**	**(1,435.5)**

	Within one year £m	Within two to five years £m	Within five to 25 years £m	After 25 years £m	Total £m
At 31 March 2020					
Derivative financial instruments – asset	0.1	24.5	28.4	150.0	203.0
Derivative financial instruments – liability	-	(11.4)	(597.0)	(768.0)	(1,376.4)
	0.1	13.1	(568.6)	(618.0)	(1,173.4)

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

23 Financial instruments (continued)

iii) Fair values of financial assets and financial liabilities

The following table provides a comparison by category of the carrying amounts and the fair values of the Group's financial assets and financial liabilities at 31 March 2021 and 2020.

	Group 2021 Book value £m	**Group 2021 Fair value £m**	Group 2020 Book value £m	Group 2020 Fair value £m
Financial assets				
Cash and cash equivalents	**417.2**	**417.2**	282.5	282.5
Current derivatives – interest rate swaps			-	-
Non-current asset investments	**0.1**	**0.1**	0.1	0.1
Non-current derivatives – interest rate swaps	**-**	**-**	0.1	0.1
Non-current derivatives – RPI swaps	**68.2**	**68.2**	194.2	194.2
Non-current derivatives – cross currency swaps	**-**	**-**	8.7	8.7
	485.5	**485.5**	485.6	485.6
Financial liabilities				
Current borrowings (including leases)	**101.8**	**101.8**	780.6	793.4
Non-current borrowings (including leases)	**6,615.5**	**7,680.4**	5,298.4	6,223.3
Non-current derivatives – interest rate swaps	**-**	**-**	-	-
Non-current derivatives - RPI swaps	**1,503.7**	**1,503.7**	1,376.4	1,376.4
Non-current derivatives – cross currency swaps	**3.1**	**3.1**	-	-
	8,224.1	**9,289.0**	7,455.4	8,393.1

Derivative activity is undertaken by subsidiaries in the Group, Greensands Senior Finance Limited, Southern Water (Greensands) Financing Plc, Southern Water Services Limited, Southern Water Services (Finance) Limited (SWSF), Greensands Financing Plc and Greensands Finance Limited, as determined by the Board, which considers the overall risk profile of the Group and enters into derivatives to mitigate or hedge any risks identified, as appropriate. No derivatives are undertaken for trading purposes, or to benefit from price fluctuations.

In November 2018 work was undertaken to amend the inflation-linked swaps held at Southern Water Services (Finance) Limited. Firstly, swaps were legally re-assigned from Southern Water Services (Finance) Limited to Southern Water Services Limited, before extending mandatory breaks from 2019 to 2025 on swaps with a notional value of £177.0 million, and re-couponing the receipt leg to increase the interest receivable of the extension period.

Other swaps with maturity dates of 2031, 2037, and 2041 were extended until 2046 by acquiring new instruments starting from the maturity date of the existing agreements.

These extensions, along with the existing remaining long-dated swaps, were then bifurcated with the result of increasing the interest receivable.

Upfront payments from Southern Water to the co-ordination bank/counterparties were required for all of these amendments, with the amounts totalling £113.6 million. The change in fair value of the related swap instruments immediately resulting from this restructure has been deferred to the balance sheet for amortisation in line with the related re-couponed period.

In December 2019 a further restructure took place to separate accretion related cash flows from the 2055 swap resulting in an upfront cash receipt of £140.0 million. The change in fair value of the related swap instrument immediately resulting from this restructure has been deferred to the balance sheet for amortisation in line with the term of the related new instrument.

No derivative activity is undertaken by the company.

The SWSF business consists of lending to other group companies and raising external finance.

All fair values are based on arm's length transactions in normal market conditions. Where available, market values have been used to determine fair values.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

23 Financial instruments (continued)

The fair value of the Group's long-term borrowings has been estimated based on quoted market prices for the same or similar debt where possible. Where prices did not exist, the fair value has been estimated based on the calculations of the present value of future cash flows using the appropriate discount rates in effect at the statement of financial position dates.

The fair values of derivative instruments (interest rate swaps) at the reporting date are determined using quoted prices adjusted for credit risk and are stated net of the deferred fair values mentioned above.

iii) Fair values of financial assets and financial liabilities

The Group has no material un-hedged monetary assets and liabilities denominated in a currency different from the local currency of the particular operation.

Fair values of other non-current liabilities, current trade and other payables, provisions and current trade and other receivables have been estimated as not materially different from book value and have been excluded from the table above. The same can be said for non-current asset investments; however, this balance has been displayed in the table above.

In accordance with IFRS 13 'Fair Value Measurement', the financial instruments carried at fair value on the statement of financial position have been classified as level 2 for fair valuation purposes, being valued by reference to valuation techniques using observable inputs other than quoted prices in active markets for identical assets and liabilities. The future cash flows have been discounted at a rate that reflects credit risk.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

24 Deferred tax liabilities

Deferred tax is provided as follows:

	Accelerated tax depreciation £m	Revaluation of financial instruments £m	Retirement benefit obligations £m	Losses and other timing differences £m	Total £m
At 1 April 2019	541.2	(227.8)	(31.7)	10.6	292.3
(Credit)/charge to income statement	(5.0)	65.3	2.7	(1.1)	61.9
Prior year adjustment:					
- Charge/(credit) to income statement	1.0	-	(1.7)	-	(0.7)
- Charge to other comprehensive income	-	-	19.0	-	19.0
Effect of change in tax rate					
- income statement	63.2	(19.1)	0.1	1.1	45.3
- other comprehensive income	-	-	(1.5)	-	(1.5)
At 31 March 2020	600.4	(181.6)	(13.1)	10.6	416.3
(Credit)/charge to income statement	9.5	(80.2)	3.7	(0.6)	(67.6)
Prior year adjustment:					
- Charge/(credit) to income statement	0.2	-	-	(0.2)	-
- Charge to other comprehensive income	-	-	(13.3)	-	(13.3)
Effect of change in tax rate					
- income statement	-	-	-	-	-
- other comprehensive income	-	-	-	-	-
At 31 March 2021	**610.1**	**(261.8)**	**(22.7)**	**9.8**	**335.4**

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to do so. The following is the analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2021 £	2020 £
Deferred tax liabilities	**610.1**	600.4
Deferred tax assets	**(274.7)**	(184.1)
	335.4	416.3

The deferred tax liability shows that the balance is made up of a liability arising on accelerated capital allowances and deferred tax assets arising on the fair value revaluation of financial instruments and the pension deficit.

At the reporting date the group has unused tax losses of £86.2 million (2020: £5.6 million) with a deferred tax asset of £16.4 million (2020: £1.1 million). A deferred tax asset has not been recognised due to the uncertainty of suitable taxable profits in the foreseeable future on which to utilise the losses.

Future tax relief of £267.6 million (2020: £215.7 million) is expected to be available for accrued interest that will be deductible for tax purposes on a paid basis. No deferred tax benefit has been recognised in respect of these interest deductions, as it is probable that they will not reverse in the foreseeable future and there is uncertainty over the availability of suitable taxable profits against which these may be offset.

The total amount of deferred tax asset un-provided is £67.2 million (2020: £41.0 million). At present it is not envisaged that the unwinding of the underlying temporary differences will give rise to a tax benefit in the foreseeable future.

Deferred tax liabilities have not been discounted.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

25 Retirement benefit obligations

The deficit associated with retirement benefit obligations has decreased to £116.5 million (2020: £62.5 million). The main reason for the decrease in the deficit over the year is a decrease in the level of expected future price inflation, which has reduced the value placed on the scheme liabilities, as well as higher than assumed asset returns over the year and Group contributions. This has been partially offset by an increase in assumed life expectancy and, less significantly, allowance for the Scheme closing to further accrual.

Pension schemes operated

The Group principally operates one defined benefit pension scheme (final salary) and one defined contribution scheme, details of which are shown below:

1. Southern Water Pension Scheme (SWPS), a funded defined benefit scheme, was closed to new members on 31 December 1998, re-opened in July 2003 and closed once more to new entrants on 1 April 2005. This scheme has nine trustee directors. The Southern Water Services Executive Pension Scheme (SWEPS) was also closed to new entrants and merged with the SWPS on 1 April 2005.

   The Scheme closed to accrual with effect from 31 March 2020.

   The Trustees are responsible for administrating the Fund which is held separately from the company. Legal and General and Blackrock are unit registrars for Southern Water Pension Scheme unit holdings, and appoint custodians at individual pooled fund level (not client holding level). The directors of SWS are responsible for setting the accounting assumptions for the fund for inclusion in these financial statements.

   As part of the Group's interactions with both the Trustees and when required the Pensions Regulator, the group looks to agree a long-term funding and risk management strategy for the pension liability. Following on from regular dialogue with the Trustees, and discussions and correspondence with the Pension Regulator regarding the deficit, the SWS Board agreed with both the Trustees and the Pensions Regulator a long-term funding solution for the scheme in 2018.

   The main risks of the scheme are as follows:

   a) Asset volatility
      For the purpose of setting the contribution requirements, the calculation uses a discount rate set with reference to government bond yields, with allowance for additional return to be generated from the investment portfolio – whereas under FRS 101, the defined benefit obligation is calculated using a discount rate set with reference to corporate bond yields.

      The schemes hold a significant proportion of their assets in growth assets. The returns on these assets may be volatile and are not correlated to the value placed on the liabilities. This means that the deficit may be volatile in the shorter term, which may result in an increase in the contribution requirements and an increase in the net defined benefit liability recorded on the statement of financial position.

      However, the Group believes that return-seeking assets offer an appropriate level of return over the long term for the level of risk that is taken. Furthermore, the scheme's other assets are well-diversified by investing in a range of asset classes, including liability-driven investments, government bonds and corporate bonds.

   b) Changes in bond yields
      A fall in bond yields increases the value placed on the liabilities for reporting purposes and for setting the Group's contribution requirements. However, in this scenario the scheme's investment in corporate and government bonds is expected to increase and therefore offset some of the increase in the value placed on the liabilities.

   c) Life expectancy
      The majority of the scheme's obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the scheme's liabilities. This is particularly significant where the longer duration and inflation-linked nature of the payments result in higher sensitivity to changes in life expectancy. The scheme does not contain a hedge against increases in future life expectancy.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

25 Retirement benefit obligations (continued)

d) Inflation risk
The majority of the scheme's benefit obligations are linked to inflation and higher out-turn inflation will lead to a higher benefit obligation (although in most cases caps on the level of inflationary increases are in place to protect the plan against extreme inflation). The majority of the scheme's assets do not provide a direct hedge against changes in inflation as they are either fixed-interest in nature, e.g. corporate bonds and government bonds, or have an indirect link to inflation, e.g. equities.

2. A second company stakeholder scheme, which is a defined contribution scheme, is also available to all employees.

   Contributions made to the defined contribution scheme for the year ended 31 March 2021 amounted to £7.7 million (2020: £4.9 million). No contributions were outstanding at either year-end.

Members of all schemes receive an annual statement of their accrued benefits.

The latest actuarial valuation of the SWPS was carried out as at 31 March 2019 using the projected unit method. For closed schemes under this method the current service cost will increase as the members of the schemes approach retirement.

The assumptions that have the most significant effect on the results of the valuation are those relating to the rate of return on investments, and the level of inflation, which drives pension increases in the SWPS.

The principal assumptions in the valuation were as follows:

	2019 **SWPS** % per annum (pa)
Return on investments: pre-retirement	FI Gilt curve + 65 bps
Return on investments: post-retirement (pensioner/non-pensioner)	
Salary growth	2.50%
Pension increases on the excess over guaranteed minimum pensions (where capped at 5% pa)	3.00%

The term 'FI Gilt curve' refers to the generally available fixed interest gilt yield curve agreed by the Trustees and the Group for the purposes of the 2019 actuarial valuation.

The assets of the scheme had a market value of £755.6 million at 31 March 2019. This was sufficient to cover 76% of the scheme's benefits. The weighted average duration of the scheme liabilities is 17.5 years.

The timing and quantum of future contributions in relation to the deficit have now been agreed with the Trustees and Pensions Regulator. These contributions will be dependent on future levels of RPI, but if market breakeven rates are borne out at 31 March 2019 the expected base deficit contributions will be paid annually and total £177.2 million over the period from 1 April 2019 to 1 April 2029. The first payment was made in November 2018.

Expected employer and employee contributions to the defined benefit scheme for 2021-22 are £18.1 million under the current Schedule of Contributions.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

25 Retirement benefit obligations (continued)

IAS 19 – assumptions, asset, liability and reserves disclosures

The group has employed an independent actuary to approximately update this valuation allowing for differences between the actuarial assumptions used by the scheme for funding purposes and those adopted by the group to measure the scheme's liabilities in the financial statements, as well as adjusting for benefit accrual and benefits paid by the scheme.

The major assumptions used by the actuary are set out in the table below:

	2021 % pa	2020 % pa
Price inflation (RPI)	**3.15**	2.50
Price inflation (CPI) (RPI less 1% pa up to 2030; equal to RPI thereafter)	**2.15 up to 2030** **3.15 after 2030**	1.70
Rate of increase in salaries (no longer applicable following cessation of accrual)	**N/A**	2.40
Rate of increase of pensions in payment (MIS* members only)***	**2.15**	1.70
Rate of increase of pensions in payment (Old section** members only)***	**3.15**	2.50
Rate of increase of pensions in payment (New section and ex FSLP (RPI max 5%))***	**3.05**	2.50
Rate of increase of pensions in payment (Post 5 April 1988 GMP (CPI max 3%))***	**1.90**	1.60
Rate of increase of pensions in payment (All sections post 31 March 2013 service (RPI max 2.5%))***	**2.15**	1.90
Rate of increase for deferred pensions (MIS* members only)***	**2.15**	1.70
Rate of increase for deferred pensions (Old section** members only)***	**3.15**	2.50
Rate of increase for deferred pensions (New section and ex FSLP (RPI max 5%))***	**3.05**	2.50
Rate of increase for deferred pensions (Post 5 April 1988 GMP (CPI max 3%))***	**1.90**	1.60
Rate of increase for deferred pensions (All sections post 31 March 2013 service (RPI max 2.5%))***	**2.15**	1.90
Discount rate	**2.15**	2.40

* MIS refers to the Southern Water Mirror Image Pension Scheme. Pensions in payment and deferment for this section will be indexed in line with the Consumer Price Index.

** For this section the Trustee will endeavour to meet any indexation of excess pension above the 5% per annum cap on increases that apply to other sections of the scheme.

*** Pension increase assumptions allow for caps and floors where appropriate based on a statistical model (the Black Scholes model).

Assumptions regarding future mortality experience are set based on advice, published statistics and experience. For 2019–20, base tables have been updated in line with best estimate basis from the Trustees' 2019 Actuarial Funding Valuation, together with future improvements in line with CMI 2018 improvements with a long-term improvement rate of 1.25% per annum. Improvements rates are the same as those used in the prior year, as assuming greater improvements is not considered appropriate in light of the ongoing COVID-19 pandemic.

	2021 Years	2020 Years
Longevity at age 65 for current pensioners		
Male	**24.3**	23.0
Female	**26.4**	24.9
Longevity at age 65 for future pensioners		
Male	**23.0**	24.4
Female	**24.9**	26.4

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

25 Retirement benefit obligations (continued)

The assets and liabilities in the scheme and the expected rates of return at 31 March 2021 and 31 March 2020 were:

	Value at 2021 £m	Value at 2020 £m
Equities	**197.1**	176.0
Government bonds	**173.1**	239.7
Non-government bonds	**367.3**	343.5
Cash	**34.0**	18.4
Total market value of plan assets	**771.5**	777.6
Total value of plan liabilities	**(888.0)**	(840.1)
Accrued deficit in the plan	**(116.5)**	(62.5)
Related deferred tax asset	**22.8**	13.2
Net retirement benefit obligations	**(93.7)**	(49.3)

The equity investments and bonds which are held in plan assets are quoted and are valued at the current bid price.

The Government bond and cash allocation set out above includes £244.0 million held in a Liability Driven Investment (LDI) portfolio to mitigate interest rate risks arising from the liabilities.

Reconciliation of the present value of the scheme liabilities	**2021 £m**	2020 £m
At 1 April	**840.1**	942.5
Current service cost	**-**	6.4
Past service cost	**0.2**	-
Interest expense	**19.3**	22.2
Member contributions	**-**	0.3
Experience gain on liabilities	**(15.8)**	(27.2)
Actuarial loss/(gain) on liabilities:		
- due to changes in demographic assumptions	**0.2**	12.7
- due to changes in financial assumptions	**114.1**	(78.2)
Benefits paid	**(70.1)**	(39.9)
Settlements/Curtailment	**-**	1.3
Scheme liabilities at 31 March	**888.0**	840.1

Sensitivity analysis of the scheme liabilities

The sensitivity of the present value of the scheme liabilities to changes in the major assumptions used is set out below.

	Change in assumption	**Impact on scheme liabilities (£m)**
Discount rate	+ 0.1% p.a.	(14.0)
	- 0.1% p.a.	14.5
Price inflation (RPI measure)*	+ 0.1% p.a.	11.3
	- 0.1% p.a.	(11.0)
Mortality	+ 1 year	37.6
	- 1 year	(36.0)

* These movements have been calculated assuming that changes in the inflation assumption have a knock-on effect on the pension increase and salary growth assumptions (i.e. the 'real' increase rates are maintained).

The above sensitivity analysis is based on reasonably possible changes of the respective assumptions occurring at the end of the reporting period, while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. The methods and types of assumptions used in preparing the sensitivity analysis did not change compared to the previous period.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

25 Retirement benefit obligations (continued)

Reconciliation of the value of the scheme assets	**2021 £m**	2020 £m
At 1 April	**777.6**	755.8
Interest income	**18.0**	18.0
Gain on assets above interest	**28.5**	19.0
Employer contributions	**17.5**	24.4
Member contributions	**-**	0.3
Benefits paid	**(70.1)**	(39.9)
Bid value of scheme assets at 31 March	**771.5**	777.6

The total return on scheme assets was £46.5 million (2020: return of £40.7 million).

Total cost recognised as an expense	**2021 £m**	2020 £m
Current service cost	**-**	6.4
Past service cost	**0.2**	-
Curtailment	**-**	1.3
Net interest cost	**1.3**	4.2
Total income statement expense before deduction for tax	**1.5**	11.9

Analysis of the amounts recognised in other comprehensive income	**2021 £m**	2020 £m
Gain due to liability experience	**(15.8)**	(27.2)
Loss due to changes in demographic assumptions	**0.2**	12.7
Gain due to changes in financial assumptions	**114.1**	(78.2)
Return on plan assets greater than discount rate	**(28.5)**	(19.0)
Total (gain)/loss recognised in OCI before adjustment for tax	**70.0**	(111.7)

The cumulative amount of actuarial losses recognised in other comprehensive income is £237.7 million (2020: £164.0 million).

Analysis of the movement in the scheme deficit during the year	**2021 £m**	2020 £m
Deficit in the scheme at 1 April	**(62.5)**	(186.7)
Employer's contributions	**17.5**	24.4
Employer's current service cost	**-**	(6.4)
Employer's past service cost	**(0.2)**	-
Curtailment	**-**	(1.3)
Financing charge	**(1.3)**	(4.2)
Actuarial (loss)/gain	**(70.0)**	111.7
Deficit in the scheme at end of year	**(116.5)**	(62.5)

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

26 Regulatory settlement liability

	2021 £m	2020 £m
At 1 April	**135.5**	138.5
Settlements in year	**(35.7)**	(3.0)
Increase in year	**-**	-
At 31 March	**99.8**	135.5

Included in:	**2021 £m**	2020 £m
Current liabilities	**24.2**	**35.6**
Non-current liabilities	**75.6**	**99.9**
	99.8	**135.5**

In 2018–19 Ofwat concluded its investigation in relation to the management, operation and performance of the Southern Water's wastewater treatment works. That investigation resulted in Ofwat taking enforcement action. Ofwat issued Southern Water with a financial penalty amounting to £3.0 million as published on its website. To ensure that customers are not disadvantaged as a result of these matters, Southern Water has agreed to make direct customer rebates totalling £135.5 million in outturn prices (£122.9 million in 2017–18 prices) over the period 2020–25. This reflects the seriousness of the breaches identified in the investigation and these amounts have been provided for in the financial statements for 2018–19. These rebates are now being made and the provision is being released through revenue in line with the annual profile. Southern Water has given a number of formal undertakings to Ofwat in relation to the numerous measures that have been put in place and are being put in place to ensure that the issues identified in the investigation have ceased and cannot be repeated.

27 Provisions for liabilities

	Environmental obligations	**Other**	**Total**
Balance 1 April 2019	6.6	-	6.6
Utilised in year	(1.0)	-	(1.0)
Increase in year	0.2	4.0	4.2
Balance at 31 March 2020	5.8	4.0	9.8
Balance 1 April 2020	5.8	4.0	**9.8**
Utilised in year	(0.8)	(1.5)	**(2.3)**
Increase in year	0.7	-	**0.7**
Balance at 31 March 2021	**5.7**	**2.5**	**8.2**

Included in:	**2021 £m**	2020 £m
Current liabilities	**3.9**	5.1
Non-current liabilities	**4.3**	4.7
	8.2	9.8

The environmental provision relates to management's best estimate for the decommissioning of abandoned sites and commitments made for environmental ecology work following the South Hampshire abstraction inquiry for the period up to 2030. No reimbursement is expected.

Other provisions includes £1.5 million (2020: £3.0 million) relating to the payment of compensation for missed appointments under Southern Water's Guaranteed Standards of Service Scheme and represent management's best estimate of the likely value of payments to be made. Payments of £1.5 million were made over the course of the year.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

27 Provisions for liabilities (continued)

Environment Agency

Like other wastewater operators, in the normal course of operations Southern Water occasionally faces Environment Agency investigations. Southern Water has been subject to a detailed investigation regarding permit breaches at some of its wastewater treatment works in two locations during the period 2010–15. In February 2020 the agency presented 51 charges before the court and Southern Water entered guilty pleas to these charges. Southern Water will continue to be open and transparent and is committed to working with the agency to ensure a swift conclusion to the case.

The Southern Water Board, supported by external legal advice, has concluded that it is not yet possible to make a reliable overall estimate for the obligation that will arise from this prosecution, notwithstanding Southern Water's guilty pleas and the Sentencing Council's Guidelines for Environmental Offences. However, the Southern Water Board does recognise that there will be a minimum liability associated with the charges before the court and having reviewed the latest information, has maintained the provision of £1.0 million, recognised in the accounts for 2019–20, reflecting a minimum amount as indicated in the sentencing guidelines and an allowance for legal costs.

The court has a very broad discretion to assess the level of the fine and the provision is not intended to indicate or predict any particular level. When considering the above it is noted that there are disputed levels of culpability and environmental harm. The sentencing guidelines are very wide and there is a requirement for the court to examine the financial circumstances of the organisation in the round. The next court hearing may take place in July 2021. The Southern Water Board will continue to review the level of provision made as more information becomes available.

Southern Water is also committed to assisting the Environment Agency with its separate investigation into sampling compliance and reporting issues 2010 and 2017 (inclusive). The Southern Water Board, supported by external legal advice, has again and for similar reasons concluded that it is not yet possible to make a reliable estimate of the financial obligation that will arise from this separate investigation but will also keep this under review.

The Southern Water Board has taken these investigations extremely seriously and has continued to monitor and support the work of the Risk and Compliance directorate, which continues to deliver a programme of improvements to its non-financial regulatory reporting including the collection, verification, reporting and assurance of data.

28 Other non-current liabilities

	Grants & contributions £m	Deferred Revenue £m	Other £m	Total £m
Balance at 1 April 2020	19.6	13.1	-	**32.7**
Increase in year	3.8	-	124.6	**128.4**
Released to income statement	(1.4)	(0.4)	-	**(1.9)**
Balance at 31 March 2021	**22.0**	**12.7**	**124.6**	**159.3**

These grants and contributions relate to property, plant and equipment.

Deferred revenue of £12.7 million (2020: £13.1 million) relates to the proceeds from the sale of income rights relating to aerial masts and sites owned by the Group. The income will be credited to the income statement evenly over the life of the lease.

Other liabilities of £124.6 million relates to a contractual obligation to make future payments to Portsmouth Water Limited, giving Southern Water the right to draw water from the capacity of Portsmouth Water Limited under a bulk supply agreement. The right to draw water commences on 1 April 2029 and that any water received will be subject to a volumetric charge and expensed at that time.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

29 Called up share capital

	Group and Company 2021 £m	Group and Company 2020 £m
Authorised, allotted, called up and fully paid		
921,874,025 Ordinary shares of £1 each	**921.9**	921.9

The company has one class of ordinary share which carries no right to fixed income. The holders of ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at meetings of the company.

30 Share premium account

	Group and Company 2021 £m	Group and Company 2020 £m
Share premium account	**4.5**	4.5

31 Non-distributable reserve

	Group 2020 £m
Balance at 1 April 2019	53.8
Profit for the financial year	7.8
Transfer to retained earnings	(1.4)
Balance at 31 March 2020	60.2
Profit for the financial year	18.2
Transfer to retained earnings	(1.5)
Balance at 31 March 2021	**76.9**

Non-distributable reserves are comprised of the value of sewer adoptions previously recognised at fair value, deferred and amortised to the income statement over the life of the related assets. Under IFRS 15 the group recognises the fair value upon adoption i.e. the point at which control of the asset is obtained, through profit and loss to non-distributable reserves and is released to retained earnings in line with the amortisation of the related assets.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

32 Retained losses

	Group 2020 £m
Balance at 1 April 2019	(2,227.3)
Profit for the financial year	95.6
Other comprehensive income for the year	94.2
Transfer from non-distributable reserve	1.4
Balance at 31 March 2020	(2,036.1)
Loss for the financial year	(572.9)
Other comprehensive expense for the year	(56.7)
Transfer from non-distributable reserve	1.5
Balance at 31 March 2021	**(2,664.2)**

	Company 2021 £m	Company 2020 £m
Profit/(loss) for the financial year	**44.0**	(236.8)
Balance at 31 March	**44.0**	(236.8)

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

33 Notes to the cash flow statement

	2021 £m	2020 £m
Continuing operations		
Operating profit	**124.3**	201.6
Adjustments for:		
Fair value of sewer adoptions	**(18.2)**	(7.8)
Depreciation of property, plant and equipment	**279.3**	258.2
Amortisation of intangible assets	**13.7**	13.1
Receipt of grants and contributions	**3.8**	6.8
Difference between pension charge and cash contributions	**(17.3)**	(16.7)
Amortisation of grants and contributions	**(1.5)**	(1.2)
Operating cash flows before movements in working capital	**384.1**	454.0
Increase in inventories	**(1.3)**	(0.3)
Decrease in receivables	**18.5**	15.9
Increase in payables	**13.7**	7.0
Decrease in regulatory settlement liability	**(35.7)**	(3.0)
(Decrease)/increase in provisions	**(1.5)**	3.2
Cash from operations	**377.8**	476.8
Tax paid	**-**	(0.1)
Net cash from operating activities	**377.8**	476.7

Cash and cash equivalents	**2021 £m**	2020 £m
Cash and bank balances	**417.2**	282.5

Cash and cash equivalents comprise cash and short-term bank deposits. The carrying amount of these assets is equal to their fair value.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

33 Notes to the cash flow statement (continued)

The table below details changes in liabilities arising from financing activities, including both cash and non-cash changes. Liabilities arising from financing activities are those for which cash flows were, or future cash flows will be, classified in the cash flow statement as cash flows from financing activities.

Analysis of net debt (including changes in liabilities from financing activities)	At 1 April 2020 £m	Cash Flow changes £m	Fair value adjust-ments £m	New finance leases £m	Other non-cash changes £m	At 31 March 2021 £m
Cash and cash equivalents	282.5	134.7	-	-	-	**417.2**
Net liabilities from financing activities:						
Term facilities/index linked loans (note 21)	(6,048.6)	(411.1)	-	-	(227.9)	**(6,687.6)**
Finance lease liabilities (note 21)	(30.4)	1.8	-	(1.1)	-	**(29.7)**
Foreign currency swaps (note 23)	8.7	-	(11.8)	-	-	**(3.1)**
Interest rate swaps (note 23)	(1,182.1)	194.5	(444.8)	-	-	**(1,432.4)**
Total liabilities from financing activities	(7,252.4)	(214.8)	(456.6)	(1.1)	(227.9)	**(8,152.8)**
Net debt	(6,969.9)	(80.1)	(456.6)	(1.1)	(227.9)	**(7,735.6)**

Other non-cash changes of £227.9 million relate to amortisation of loan issue costs, gilt lock proceeds and deferred proceeds. Bank loan fair value movements include Eurobond interest, indexation, effective interest and capitalised interest..

Balances at 31 March 2021 comprise:	Non-current assets £m	Current assets £m	Current liabilities £m	Non-current liabilities £m	Total £m
Cash and cash equivalents	-	417.2	-	-	**417.2**
Derivative financial instruments	68.2	-	-	(1,503.7)	**(1,435.5)**
Unamortised debt issuance costs	-	-	1.5	147.5	**149.0**
Gilt lock proceeds	-	-	(0.1)	(4.4)	**(4.5)**
Borrowings due within one year	-	-	(100.7)	-	**(100.7)**
Borrowings due after one year	-	-	-	(6,731.4)	**(6,731.4)**
Finance leases	-	-	(2.5)	(27.2)	**(29.7)**
Net debt	68.2	417.2	(101.8)	(8,119.2)	**(7,735.6)**

Borrowings due within one year relate to amounts that are repayable on demand or within 12 months of the balance sheet date (see note 20).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

34 Contingent liabilities

Companies of the size and scale of Southern Water are sometimes subject to a number of claims, disputes and potential litigation. The significant ones currently include ongoing investigations by regulatory bodies (the EA and DWI) as well as a potential claim in respect of property search income. The Southern Water directors consider that, where a liability is probable, and where it is possible to be estimated reasonably, an appropriate position has been taken in reflecting such items in these financial statements. Separate consideration of the EA investigations is set out in note 26.

Following the South Hampshire abstraction inquiry, Southern Water has committed to undertake certain environmental work on the rivers Itchen, Test and Candover Stream between 2018 and 2030. A provision was made in the accounts of 2018–19 in relation to costs of the ecology work associated with this agreement and further details are disclosed in note 26 to the accounts. Certain compensatory costs may become due in the future, subject to conditions at that time and the impact of the ecology work undertaken. These have not been provided for and could increase the obligation by approximately £1.2 million.

Contractors submit claims to the operating company for the estimated final cost of their works. These claims are reviewed to assess where the liability for the costs rests and the amount that will actually be settled. The expected amount is included within capital creditors and a further sum is identified as a contingent liability, representing a proportion of the difference between the contractor’s claim and Southern Water's valuation.

The group had no contingent liabilities for capital claims at the year-end (2020: £nil).

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

35 Financial commitments

(a) Capital commitments are as follows:

	2021 £m	2020 £m
Contracted for but not provided for in respect of contracts placed in respect of property, plant and equipment	**518.0**	301.3
Contracted for but not provided for in respect of contracts placed in respect of intangible assets	**15.5**	10.7

(b) The group as lessee

	2021 £m	**2020 £m**
Lease payments under operating leases recognised as an expense in the year	**1.8**	1.3

As at 31 March 2021 and 2020, the group had no outstanding commitments for future minimum lease payments under non-cancellable operating leases in respect of vehicles and land and buildings.

Operating leases are charged to the income statement over the lease term and comprise short-term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets (£5,000 or less).

Commercial vehicle leases are negotiated for an average term of five years, and rentals are fixed for an average of five years, with an option to extend on an ad hoc basis at the then prevailing market rate.

36 Related party transactions

Balances and transactions between the company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note. Transactions between the Group and its associates are disclosed below.

Greensands Holdings Limited is owned and controlled by a consortium of investors. At 31 March 2021, no single investor owned a controlling shareholding.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2021

36 Related party transactions (continued)

The transactions and balances with the Group's related parties (i.e. the shareholders) are summarised below.

	2021 £m	2020 £m
Eurobond interest		
IIF Int'l SW UK Investment Ltd	**52.5**	47.0
Phildrew Nominees Ltd	**34.3**	30.7
National Nominees Ltd	**13.0**	11.7
Sky Brace Investments Ltd	**8.0**	7.2
Sumaya Investments Ltd	**8.0**	7.1
Falkirk Council - Falkirk Council Pension Fund	**0.7**	0.6
The City of Edinburgh Council – Lothian Pension Fund and Lothian Buses Pension Fund	**1.9**	1.7
Hermes Infrastructure Fund LP	**35.3**	31.6
SW Holdings LP	**3.3**	2.9
Simcoe Yeoman Water Ltd	**11.2**	10.0
Total Eurobond interest payable to related parties	**168.2**	150.5
Loans and other borrowings greater than one year:		
Eurobonds – Shareholder loans		
IIF Int'l SW UK Investment Ltd	**278.3**	278.3
Phildrew Nominees Ltd (UBS IIF)	**49.6**	49.6
Phildrew Nominees Ltd (UBS IINF)	**6.9**	6.9
Phildrew Nominees Ltd (UBS II4F)	**55.0**	55.0
Phildrew Nominees Ltd (UBS IIUSTEF)	**27.5**	27.5
Phildrew Nominees Ltd (UBS IIF (A) LP)	**12.9**	12.9
Phildrew Nominees Ltd (UBS IIF (B) LP)	**17.1**	17.1
Phildrew Nominees Ltd (UBS IIF (C) LP)	**12.4**	12.4
National Nominees Ltd - Motor Trades Association of Australia Super Fund	**21.4**	21.4
National Nominees Ltd – Prime Super	**6.5**	6.5
Sky Brace Investments Ltd	**42.3**	42.3
Sumaya Investments Ltd	**42.3**	42.3
Falkirk Council - Falkirk Council Pension Fund	**3.4**	3.4
The City of Edinburgh Council – Lothian Pension Fund and Lothian Buses Pension Fund	**10.3**	10.3
Hermes Infrastructure Fund LP	**34.7**	34.7
Hermes Infrastructure Fund Spring I LP	**19.2**	19.2
Hermes Infrastructure Fund Spring II LP	**113.9**	113.9
Hermes Infrastructure Fund Spring III LP	**19.2**	19.2
SW Holdings LP	**17.5**	17.5
Simcoe Yeoman Water Ltd	**59.1**	59.1
Accrued interest	**720.1**	551.9
Total Eurobonds – Shareholder loans	**1,569.6**	1,401.4

Greensands Europe Limited (the **Issuer)** has issued £359,725,975 in aggregate principal amount of notes (the Notes 'Eurobonds') to the shareholders of its ultimate parent company, Greensands Holdings Limited. In 2016 a Payment in Kind (PIK) exercise was undertaken, which capitalised £489,788,024 of accrued interest.

If not previously repaid or purchased, the Notes will be repaid by the Issuer at par on 31 March 2038 (the **Maturity Date).** The Maturity Date may at any time be extended by the Issuer with the approval of an Ordinary Resolution of the Noteholders passed in accordance with the relevant Conditions.

Interest for any Interest Period (the **Rate of Interest)** shall be paid at a rate of 12% per annum, being 31 March in each year. Interest is compounded if unpaid.

The Notes are unsecured, limited recourse obligations of the Issuer, at all times ranking *pari passu* and without any discrimination or preference between them, recourse in respect of which is limited to the assets (whether present or future) of the Issuer, to the extent that such assets are available after satisfaction of claims of the Issuer's creditors who rank ahead of the Noteholders (if any).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 21

37 Subsidiaries

As at 31 March 2021 the company held 100% of the ordinary share capital of Greensands Europe Limited. Greensands Europe Limited's principal subsidiaries are listed below and are included within these consolidated financial statements.

Company	Registered address	Activity
Greensands UK Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water (Greensands) Financing plc	Southern House, Yeoman Road, Worthing	To raise debt finance
Greensands Junior Finance Limited	Southern House, Yeoman Road, Worthing	To raise debt finance
Greensands Senior Finance Limited	Southern House, Yeoman Road, Worthing	To raise debt finance
Greensands Investments Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Greensands Finance Holdings Limited	Southern House, Yeoman Road, Worthing	Holding company
Greensands Finance Limited	Southern House, Yeoman Road, Worthing	Holding company
Greensands Financing Plc	Southern House, Yeoman Road, Worthing	To raise debt finance
Southern Water Capital Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water Investments Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water (NR) Holdings Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water (NR) Limited	1 Exchange Crescent, Conference Square, Edinburgh	Non-trading activities
SWS Group Holdings Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
SWS Holdings Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water Limited	Southern House, Yeoman Road, Worthing	Intermediate parent company for Southern
Southern Water Services Limited	Southern House, Yeoman Road, Worthing	Supply of Water and Wastewater Services
Southern Water Services Finance Limited*	Ugland House, PO Box 309, George Town, Grand Cayman	To raise debt finance
Southern Water Services Group Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water Industries Limited	Southern House, Yeoman Road, Worthing	Dormant
Bowsprit Holdings Limited	Southern House, Yeoman Road, Worthing	Dormant
Monk Rawling Limited	Southern House, Yeoman Road, Worthing	Dormant
Bowsprit Property Development Limited	Southern House, Yeoman Road, Worthing	Property development
EcoClear Limited	Southern House, Yeoman Road, Worthing	Dormant
Southern Water Executive Pension Scheme Trustees Limited	Southern House, Yeoman Road, Worthing	Dormant
Southern Water Pension Trustees Limited	Southern House, Yeoman Road, Worthing	Dormant
Southern Water Retail Services Limited	Southern House, Yeoman Road, Worthing	Dormant

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2021

37 Subsidiaries (continued)

*The country of incorporation for this company is the Cayman Island, but is UK tax resident.

All of the above subsidiary companies are wholly-owned by ordinary shares and incorporated within the United Kingdom unless stated otherwise.

38 Post balance sheet events

On 9th June 2021, the Board resolved to convert the company's existing par value shares into no par value shares.

On 11th June 2021, each holder of the Greensands Europe Limited Eurobonds, dated 15th October 2007, transferred all their respective legal and beneficial right, title and interests in the Eurobonds to Greensands Holdings Limited. As consideration for the transfer Greensands Holdings Limited issued ordinary shares of no par value to each noteholder. As the Eurobonds were held by shareholders in the same proportion as their shareholding in the company the transaction resulted in no overall change in the percentage of shares held by each group of shareholders.

Independent auditor's report to the members of Greensands Holdings Limited

Report on the audit of the financial statements

Opinion

In our opinion the financial statements of Greensands Holdings Limited (the 'parent company') and its subsidiaries (the 'group'):

- give a true and fair view of the state of the group's and of the parent company's affairs as at 31 March 2021 and of the group's profit for the year then ended;
- have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the consolidated income statement;
- the consolidated statement of other comprehensive income;
- the consolidated and parent company statement of financial position;
- the consolidated and parent company statements of changes in equity;
- the consolidated cash flow statement; and
- the related notes 1 to 38.

The financial reporting framework that has been applied in their preparation is applicable law and international accounting standards in conformity with the requirements of the Companies Act 2006.

Basis for opinion

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

We are independent of the group and the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard, and we have fulfilled our other 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 – contingent liability in respect of Environment Agency investigation

We draw attention to note 27 concerning the uncertain outcome of certain regulatory investigations regarding the performance of certain wastewater plants. Southern Water faces a prosecution and other investigations from the Environment Agency ('EA'). The ultimate obligation arising from this matter cannot presently be determined because of the very wide range of possible outcomes in the sentencing guidelines, the uncertain and disputed levels of culpability and environmental harm, the lack of precedent, and the fact that for sentencing purposes Southern Water would be considered a Very Large Organisation meaning that the court has broad discretion in determining the penalty that might be applied. The Board, supported by legal advice, was not able to make a reliable overall estimate of the financial obligation that will arise from this EA prosecution, notwithstanding the guilty pleas and the Sentencing Council's Guidelines for Environmental Offences. However, recognising that there will be a minimum liability associated with the permit breaches the Board has therefore recognised a provision of £1 million for the 51 cases brought to date, reflecting a minimum amount as indicated by the Sentencing Guidelines and an allowance for legal costs. Our opinion is not modified in respect of this matter.

Material uncertainty related to going concern

We draw attention to note 1 of the financial statements which indicates that due to the implementation of the 2019 final determination for Southern Water Services Limited and reduced dividends arising was leading to increasing difficulties in complying with the financial covenants applicable to the debt held in the group structure above Southern Water Services Limited. At 31 March 2021 certain covenants lead to a 'lock up' level of increasing restrictions on the ability of certain Greensands holding companies to operate. Furthermore the liquidity available to pay interest on this debt at the Greensands Group parent company is scheduled to be exhausted by October 2021. As stated in note 1 to the financial statements these events or conditions along with other matters as set forth in note 1, indicate that a material uncertainty exists that may cast significant doubt on the group's and parent company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Independent auditor's report to the members of Greensands Holdings Limited

Our Responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Other information

The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Responsibilities of directors

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

In preparing the financial statements, the directors are responsible for assessing the group's and the parent 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 group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

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

Extent to which the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

Independent auditor's report to the members of Greensands Holdings Limited

We considered the nature of the group's industry and its control environment, and reviewed the group's documentation of their policies and procedures relating to fraud and compliance with laws and regulations. We also enquired of management about their own identification and assessment of the risks of irregularities.

We also obtained an understanding of the legal and regulatory frameworks that the company operates in, focusing on provisions of those laws and regulations that had a direct effect on the determination of material amounts and disclosures in the financial statements. The key laws and regulations we considered in this context included the UK Companies Act, pensions legislation and tax legislation.
We discussed among the audit engagement team regarding the opportunities and incentives that may exist within the organisation for fraud and how and where fraud might occur in the financial statements.

In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override. In addressing the risk of fraud through management override of controls, we tested the appropriateness of journal entries and other adjustments; assessed whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluated the business rationale of any significant transactions that are unusual or outside the normal course of business.

In addition to the above, our procedures to respond to the risks identified included the following:

- reviewing financial statement disclosures by testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- enquiring of management and legal counsel concerning actual and potential litigation and claims, and instances of non-compliance with laws and regulations; and
- reading minutes of meetings of those charged with governance and reviewing internal audit reports.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006
In our opinion, based on the work undertaken in the course of the audit:

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

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

Independent auditor's report to the members of Greensands Holdings Limited

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required to report in respect of the following matters if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Use of our report

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

Anthony Matthews

Anthony Matthews FCA (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom
8th July 2021