



GROUP ANNUAL REPORT 2020/21

FINANCIAL STATEMENTS AND
ANNUAL PERFORMANCE REPORT



Pure know h₂ow

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OUR BUSINESS

We supply top quality drinking water to 2.2 million customers in the south east of England. Through a network of 14,780 kms of pipe, we deliver around 520 million litres of water every day. The skill and expertise of our employees ensures our customers' water meets the highest of standards.

OUR VISION

Our vision is to be the water company people want to be supplied by and want to work for. Everything we do is underpinned by technical excellence.

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OUR PURPOSE

To provide today's public water service and create tomorrow's water supply solutions, fairly and responsibly, working with others to help society and the environment to thrive.



LOOK OUT for this icon to read more online

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OUR PERFORMANCE

OPERATIONAL HIGHLIGHTS

DRINKING WATER SUPPLIED

543.4 million

Litres each day
(2020: 521.5 million)

GREENHOUSE GAS EMISSIONS

192 kgCO₂e/MI

(2020: 209kgCO₂e/MI)

NUMBER OF EMPLOYEES

986

(2020: 959)

FINANCIAL HIGHLIGHTS

REVENUE

£248.2_m

Increase of 1.9 per cent
on last year

PROFIT FROM OPERATIONS

£77.5_m

Decrease of 4.7 per cent
on last year

CAPITAL EXPENDITURE

£93.3_m

Decrease of 10.7 per cent
on last year

CASH GENERATED FROM OPERATING ACTIVITIES

£119.9_m

Decrease of 10.8 per cent
on last year

HOW WE INVEST IN YOUR WATER

Where each £1 of your bill is spent
by the appointed water business

GETTING WATER
TO YOU

43%

2019/20: 45%

WATER
TREATMENT

23%

2019/20: 22%

INTEREST
& TAX

14%

2019/20: 15%

WATER
EXTRACTION

10%

2019/20: 9%

CUSTOMER
SERVICES

8%

2019/20: 8%

DIVIDENDS*

2%

2019/20: 1%

* Dividends allocated to the appointed business less interest received on the parent company loan. The loan was repaid in the year which has resulted in a lower interest offset and a higher percentage of cash allocated to net dividends.

KEY ACTIVITIES

Our stakeholders expect us to operate in a responsible manner. This shapes how we deliver our strategy to fulfil **Our Purpose:**

**To provide
today's
public water
service...**

500,000

water quality tests each year
to ensure your water meets
the highest standards

see more [page 18](#)

**and create
tomorrow's
water supply
solution...**

83

water treatment
works to ensure our water
is of excellent quality

see more [page 34](#)

fairly and responsibly...**29,210**

total household customers signed up to our Priority Services Register
see more page 62

working with others...**680**

contractor employees – work with us to help make sure your water supply runs 24 hours a day, 365 days a year
see more page 78

to help society and the environment to thrive.**1,172**

hectares of land improved through the year for biodiversity
see more page 98

Thriving people

HOW WE HELP THE PEOPLE
WHO WORK WITH US TO THRIVE

STRATEGIC REPORT

We work to make sure
our 986 colleagues
have the support they
need to thrive (read
more on [page 102](#))

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STRATEGIC REPORT

GOVERNANCE

FINANCIAL STATEMENTS

ANNUAL PERFORMANCE

CHAIR'S STATEMENT

NICK SALMON
CHAIR

Last year, the impact of the Covid-19 pandemic was a very significant challenge and I am proud of the response and grateful for how everyone rose to that challenge, adapted to new ways of working and maintained a high level of service as well as support for vulnerable customers. Looking forward to the year ahead, Covid-19 remains a significant challenge for our organisation, but we are determined to support recovery in our region and build on lessons learned and the opportunities created from this experience.

Welcome to our group annual report and the audited financial statements for the year ended 31 March 2021.

First and foremost I must begin by saying thank you to all our colleagues, both at South East Water and through our supply chain partners for their resolute dedication and determination to maintain a focus on excellent service through this most testing of years.

Covid-19 necessitated a significant shift in the way we work, with more than 600 office based colleagues moving to home working within three weeks of the first lockdown and our operational colleagues developing new working practices to keep themselves and our customers safe.

Not only did we have to change the way we work and support customers, but the pandemic meant we experienced significant operational challenges. The lockdown measures saw the domestic water use in our commuter-belt supply region change dramatically. The vast majority of our customers spent the year staying at home and using considerably more water (15.9 per cent more compared to 2019/20).

This was compounded by the summer heatwaves in May and August 2020 which led to unprecedented levels of water demand, far exceeding levels we had ever experienced previously, or indeed that our system had been designed to meet. Many other water companies were more fortunate in that their total water demand fell due to a reduction in industrial and business demand but our net water demand increased overall as our supply region has relatively low industrial and business demand.

Recognising that there is also likely to be significantly higher demand this summer, the team has been putting in place operational improvements, including completing schemes that can provide additional treated water, and we have made changes to our network to enable us to move water around more easily.

At the same time communication plans are in place which aim to encourage consumers to reduce usage this summer and over the year we have delivered more than 120,000 water efficiency products as a result of our proactive campaigns.

Some of our customers are experiencing both emotional and financial hardship due to the pandemic and we have been supporting them through our priority services register and providing payment support options, which we will continue to prioritise.

Clearly these changes to the way we work, the support for customers and the operational impacts that Covid-19 has caused have also affected our financial performance. We have estimated our additional expenditure incurred due to Covid-19 during the year was approximately £5 million. This comprises the costs incurred in putting an increased level of water into supply, mainly power and chemicals, increased contractor costs due to restricted working practices and an increase in our bad debt provision due to a change in methodology to give greater emphasis to our recent cash collection history. Despite this the overall financial performance of the company has been satisfactory, with improved profits year-on-year and strong cash collections from customers.

The global pandemic has highlighted the disruption and uncertainty we can face as a business. This has given us a glimpse into a future that we must be prepared for. Climate change and changing weather patterns will have an impact on the ability of our existing infrastructure to meet the demands for water sustainably. We intend to build a business that is well positioned to meet these future challenges, but this will require support from Government, our regulators and society as a whole.

A key step in meeting these challenges is to put them at the front of our mind in everything we do. The sense of duty seen across the organisation last year is the embodiment of our company purpose (see page 20), enshrined in November 2020, in our Articles of Association.

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We are determined to support recovery in our region and build on lessons learned

This is just one of many steps taken to continue to focus on growing our responsible business approach. We were delighted to see this work recognised with sector leader status in the GRESB ESG infrastructure asset benchmarking for 2020.

This was the first year of our 2020 to 2025 investment period and while our capital programme was to a degree impacted by Covid-19, with a number of schemes being disrupted or activity reduced to facilitate safe working, £34.4 million of infrastructure improvements have been completed.

This year we have prepared our draft drought plan, our operational plan for managing periods of drought, and we are working with our partners in the Water Resources in the South East (WRSE) to create a regional plan which looks forward to 2100. This will be the basis of our own water resources management plan designed to secure long term future water resources for the community we serve.

Climate change remains our highest risk and we are preparing our next climate change adaptation report to be published this year. As a business we have committed to achieve net zero for operational emissions by 2030, which is an important part of our environmental leadership - but we believe we must go further. We have started to work with our stakeholders to develop an ambitious 25 year environment plan. We believe this approach to be an industry first. The plan will ensure we support both Government and global ambitions through the UN Sustainable Development Goals and I am looking forward to seeing this take shape. Building a sustainable future where our society and the environment can thrive will be a cornerstone of our preparations for the next price review, PR24, and we will work closely with our customers, communities and stakeholders to ensure a collaborative approach in order to realise our purpose and create value together.

NICK SALMON

CHAIR

15 JULY 2021



CHIEF EXECUTIVE OFFICER'S INTRODUCTION

DAVID HINTON
CHIEF EXECUTIVE OFFICER

What a year 2020/21 has been, and quite a year to take over as CEO. The impact of Covid-19 has certainly made us all reflect on what is important and where our priorities should lie, both globally and closer to home. 26 years ago I started working for South East Water in the laboratory testing the water quality. The importance of a continuous and safe wholesome supply of water was instilled in me from that early stage of my career. Over the last year the passion across the organisation to provide a vital public service has never been more evident.

I must begin this review with a "thank you" to everyone in the business, our contractors and our partner organisations who have stepped up and made a difference. Everyone should be proud of the role they played this year, they all made a difference. The response from across the organisation was phenomenal.

From those who continued to work in the field or laboratory to ensure our networks continued to function, to those who adapted to working from home within a matter of days, all helped maintain an excellent service for our customers and colleagues.

Clearly Covid-19 has had a huge impact on our business, affecting everything we do. Throughout this report we reflect on this. However, it is also an important first year of the five year investment period through to 2025.

It's been a foundational year to put us in a strong position to deliver continued improvements across the commitments we have made in our five year plans, including our Responsible Business strategy.

I am pleased to report that despite the challenges this year, we have made good progress in many areas. I have summarised the main points in respect of our performance and our future plans based on our four strategic themes. These themes were developed as part of our strategy, helping us embed our purpose and support the delivery of our vision. They relate to our customers and to everyone across the business, including our partners. They help us focus on how we run our business today and our long term planning. Helping society and the environment to thrive is a priority in everything we do as a responsible business.

COMMUNITY AND CONSUMER FOCUSED

We are highly focused on customer satisfaction not just with the service we provide but also in how we act as an organisation.

To deliver this we need to understand our customer views and have set out a new range of comprehensive satisfaction measures, adding to those we put in place in 2015, to help us understand how customers feel we are doing, and encouraging us via stretching targets to keep improving.

The industry wide Customer Measure of Experience (C-MeX) and Developer Measure of Experience (D-MeX) surveys enable us to compare ourselves with other water companies. Our C-MeX scores this year is 80.70 out of 100 and our D-MeX score is 79.85 out of 100. We will receive confirmation of these scores and Ofwat will publish a league table for both measures later this year.

Last year we launched our My Account web portal to make it easier for customers to access water bills and make payments through real time functionality and providing access to wider information on water usage including relevant advice on water efficiency.

We also maintained an upper quartile position in the CCW complaint report. Future plans include more frequent and improved communications, testing plans with customers, together with a complete website refresh due later this year.

Last year has been a challenge for many of our customers, especially for those who needed a little extra help. We have supported those struggling financially by providing assistance to more than 42,000 customers and we have introduced payment holidays, an initiative that's supported more than 3,500 households. We also encouraged more people to join our Priority Services Register (meaning they receive priority treatment in the event of a supply interruption) reaching more than 29,000 households, which is 3.3 per cent of our customer base.

While short of our target of 31,000 we are working to reach almost 50,000 households by the end of next year. We are working with more than 15 partners to help us achieve a collaborative approach to supporting those in our communities that need us most.



It's been a foundational year to put us in a strong position to deliver continued improvements

Being a public drinking water provider we reach into the heart of the communities we serve every day. Most of us live and work in our supply area and so are dedicated to supporting those who need it most, supporting communities while also providing the high standards of service.

Recognising that our role in society is far wider than simply supplying water to customers we're continuing to actively involve ourselves in the communities we serve.

We are helping to reduce the use of single use plastics through support of the Refill campaign, such as installing new drinking water fountains in Seaford this year. We have supported local communities through the pandemic by working with foodbanks both by donating and delivering food parcels to residents. To help keep children occupied, our teams also put hundreds of activity packs together for community use.

THRIVING PEOPLE

All our achievements of the last 12 months would not have been possible without the dedication and commitment to our purpose, vision and values of the people who work for South East Water – including our employees, partners and the businesses we work with.

Our people are dedicated to providing the best service possible, whether they are out in the field searching for leaks, managing our operational sites, testing water quality, answering customer queries, or supporting the business behind the scenes. We're proud of our culture and the wide ranging support, training and activities available to all.

CHIEF EXECUTIVE OFFICER'S INTRODUCTION continued

We have set an ambitious five year people plan to build a culture which inspires excellence, improves business performance, is resilient to future challenges and drives a thriving, diverse and engaged workforce.

Our commitments in the people plan have foundations in our values and clear company purpose.

These foundations served us well during last year as we pivoted to ensure the 600 employees who were able to work from home did so within three weeks of the first lockdown. While all our people were considered key workers, we worked hard to make sure those working in the field, our laboratory or who continued to work in offices, felt safe.

I'm pleased to report that employee surveys showed 92 per cent trust that South East Water is treating their health and safety as a high priority. Keeping our staff safe and well minimised Covid-19 absence such that our sickness rate during the year was just 1.75 per cent.

A visit by the HSE to our Head Office in Kent received positive feedback that they were happy with the Covid-19 safe work environment and could make no suggestions for improvement which is a credit to all involved.

The health and safety of those we work with is of the utmost importance. We were therefore disappointed to experience a high reportable injury rate during the last year. This was in part due to two cases of Covid-19 contracted while at work and overall lost time injuries were also high, although below the industry average. Most were the result of slips and trips or manual handling and thankfully the severity of the injuries and the amount of time lost for each was low. Manual handling activities are being reassessed and retrained in the coming year and awareness regarding slips and trips will be promoted as we work hard to reduce this in future.

Understanding how our people felt during challenging times last year was a key part of our mental health strategy designed to support colleagues, remove stigma and create parity between mental and physical health.

During the year we ran six pulse surveys which focused on a range of topics achieving record engagement results with an average 92 per cent of our people feeling engaged over the last 12 months.

A Wellbeing Hub created on our intranet held key information, signposted support and updated colleagues on the latest information on a weekly basis.

Our Mental Health First Aiders are now embedded throughout the business and are trained to take calls from colleagues, triage any immediate concerns and signpost people to the most appropriate source of help and support.

While the Covid-19 pandemic has thrown many challenges at us, one thing it proved is that we have the tools available to enable remote working and therefore we should be able to continue working flexibly in the future. We've created an agile working team who are engaging with colleagues to understand how we might achieve this while maintaining the ability for teams to collaborate face-to-face.

It's important we thoroughly explore the long term impacts of any choices we make as these decisions will fundamentally change how the business operates. The potential for us to be working differently in the future allows us to consider how we attract, recruit, and retain a more diverse and socially mobile workforce.

We are committed to retaining the really positive elements of the culture we have but to also build on it to develop a new culture which inspires excellence in our people and I am immensely proud of the way our teams and managers responded during the past year.

TRUSTED BUSINESS

Our community entrusts us to deliver a continuous supply of safe, wholesome drinking water directly to their homes. To ensure we retain that trust we are constantly monitoring our performance against expectations through a wide range of measures, from the taste and smell of the water to how often the supply is interrupted.

We are delighted to have once again beaten our leakage target (a 1.9 per cent improvement on our 2019/20 leakage levels). This is the first year of a journey where we have challenged ourselves to improve year on year, a 15 per cent target reduction over the five year period. The leakage team is expanding and embracing advances by using satellite technology to hunt for leaks and building on our award winning smart networks trial by installing more meters, sensors and loggers to monitor our pipeline network. This work is at the cutting edge of leakage initiatives and will cement our position as one of the top performers in the industry.

This year only 0.4 properties per 10,000 were at risk of low pressure (beating our target of 0.5) and we have improved the taste, odour and appearance of your drinking water through installing new water treatment processes, flushing pipes to remove sediment and adjusting the way we operate our networks. The number of customer contacts per 10,000 population for discolouration was 1.00 (beating our target of 1.09) and for taste and odour we achieved 0.34 (beating our target of 0.42). The new measure Event Risk Index (ERI) monitors how we proactively reduce the risk of water quality incidents across the supply network, including within customer properties. Our ERI result for the year was 67.40, well below the industry average of 204.

Despite our ongoing programme to upgrade our infrastructure, burst pipes, site outage or other external factors do unfortunately happen and can result in customers going without water for short periods. We were able to keep our overall unplanned outage levels low (3.09 per cent against a target of 4.23), however a heatwave in August 2020, coupled with more people being at home due to the Covid-19 restrictions led to a perfect storm which created a stress on our network never seen before.

“

The impact of Covid-19 has certainly made us all reflect on what is important

Only a small area of our supply region was affected, but those who were affected went without water for too long. We have learnt lessons from this, not least how the pandemic has altered how water is used.

One of the lessons is we need to do more to help customers reduce water use during dry periods so that we keep demand to a sustainable level both in terms of our ability to supply but also to minimise impacts on the environment.

The August heatwave and other related events led to us missing our interruptions to supply target as our average interruption time was 31.27 minutes per property (see page 104 for more details).

The increased demand also had a big impact on our water use targets. With people working from home, not commuting out of our supply area or travelling on holidays, consumption has increased 16 per cent to 166 litres per person per day. This is an area we're monitoring closely as travel and commuting restrictions ease – but we know lifestyles for many have changed. We want to work with all of our customers to reduce water usage and help manage the wider impact on the environment. We have been working on enhancements to our online customer account so we can provide them with even more information about their water use and comparisons to similar properties in their area to help people make decisions about how they use water and save both water and money.

To ensure the sustainability of the business we must ensure our financial performance continues to be satisfactory. This allows us to continue to invest in the company's assets, improving the efficiency and resilience of our network, while providing a reasonable return on our shareholders' investment. Revenue for the financial year was £248.2 million (2020: £243.5 million) and our profit before tax for the year was £37.7 million, an increase of £3.9 million over the prior year.

CHIEF EXECUTIVE OFFICER'S INTRODUCTION continued

The main causes for the increased profit before tax were higher revenues and other income of £3.9 million, operating costs having increased by £7.7 million and net finance costs being lower by £7.7 million.

The improved income largely reflects the allowed price increase for the year and increased demand from customers working from home and as a result of the hot weather last summer. Increases in operating costs are due to additional expenditure caused by Covid-19, the write-off of assets due to a sinkhole causing damage to a treated water storage reservoir in Aylesford and annual increases in depreciation, insurance and other expenses. The increased costs were mitigated by lower staff costs. Savings have been made on our finance costs through the replacement of £310 million of debt which matured in September 2019 with debt raised at lower interest rates, and also lower inflation seen throughout the period of the pandemic resulting in lower interest costs on our inflation linked debt. The repayment of the loan with South East Water (Holdings) Limited in December 2020 resulted in lower interest receivable.

Capital expenditure during the year was £93.3 million compared to £104.5 million in the previous year. Net cash inflow during the year was £28.6 million, although this included additional borrowing of £40 million to protect our liquidity position during the pandemic. The closing balance for cash and cash equivalent assets at the end of the year was £41.6 million.

The company also satisfied all the covenant requirements placed upon it under the terms of our long-term borrowing and maintained its credit rating.

Further details of our financial performance are set out on page 73.

FLOURISHING ENVIRONMENT

Our business is intrinsically linked to the environment. For this reason we do all we can to ensure there is a clean, resilient and sustainable supply available for current and future customers while ensuring there is enough water available to support the needs of the environment too. Over this five year period we are investing £59.4 million in our National Environment Programme to complete 65 schemes that will bring real benefits to our natural habitats.

As significant landowners, we own and manage 33 Sites of Special Scientific Interest, a National Nature Reserve, two local nature reserves and numerous Areas of Outstanding Natural Beauty. Over the next five years we are working to ensure that almost 70 per cent of our estate is proactively managed to enhance biodiversity. This year we have been able to manage 1,172 hectares to benefit wildlife, exceeding our target for the year of 1,166.

Our influence goes far wider than just our own landholdings and assets, we also work closely with landowners to test and promote sustainable land management practices ultimately improving the rivers, wells and reservoirs we rely on. Our work in partnership with Natural England has ensured that we are able to deliver bespoke advice to support land managers enabling them to protect and enhance the environment across 2,858 hectares, exceeding our target of 2,843. This has included a number of innovative pilot projects reducing the use of pesticides and nutrients, and the volume of soil which washes into watercourses.

As part of a Defra Environment Land Management (ELMS) trial on the Pevensey Levels we have worked in conjunction with the Cuckmere and Pevensey Catchment Partnership. Our work here focused on how farmers and land managers could be paid in the future for changing practices which help deliver wider environmental benefit, for example locking carbon into soils.



A key strand of our environmental ambition is to achieve net zero carbon by 2030

In addition to this work, we achieved our target to sign off with our regulators nine Water Industry National Environment Programme projects also aimed at improving the wider water environment.

We are also conscious that we have a part to play in working with others who abstract from the same water environment as us to ensure a joined up approach to environmental resilience. During the year we have been building a team to work with other water abstractors and develop a set of tools to enable them to reduce their water abstraction needs during low flow events. Our aim is to be working with 20 different abstractors by 2025. This work has the potential to create much needed drought resilience in a number of our surface water catchments, and we are one of the first companies to promote this innovative practice.

A key strand of our environmental ambition is to achieve net zero carbon by 2030. A company roadmap has been created which aligns us to the water industry's ambition to be net zero carbon by 2030. During the year our greenhouse gas emissions were above our target (192kgCO₂e/Ml against a target of 152.3kgCO₂e/Ml due to this being a preparatory year (see page 92 for more detail about our strategy).

During the coming year we will focus on finalising a 25 year environment plan, potentially the first of its kind in the industry; this plan will link all our environmental ambitions together, we will use customers, stakeholders and staff to challenge that ambition and we aim to use it to guide our performance over the longer term. This kind of long term clear thinking is essential if we are to overcome the environmental challenges that lie ahead.

THE YEAR AHEAD

As we head into the second year of our investment period, I know we have a team at South East Water that is passionate about ensuring we deliver on the commitments we made.

Over the coming year we will continue to build on the performance improvements we have made over the last 12 months – including increasing customer and developer satisfaction, helping more of our vulnerable customers, driving down the level of leakage, per capita consumption and greenhouse gas emissions, and carrying out more catchment management and biodiversity work than ever before.

We are increasing our support for tens of thousands more customers who may need help with their bills or additional support and a priority service due to their circumstances – something that continues to be particularly important as we continue as a society to recover from the pandemic.

Further information about our performance including many more stories of the activities through the past year are available in our performance, people and planet report.



performance.southeastwater.co.uk

While the impact of Covid-19 on our performance for the year ahead and beyond means some uncertainty remains, we are in a good position to be able to deal with this uncertainty and continue to deliver the vital service our society needs.

I am confident that in spite of these uncertain times, our passionate colleagues, and those who work with South East Water, will strive to make sure we perform for our customers, for each other, our environment and our community.

DAVID HINTON

CEO
15 JULY 2021

DELIVERING OUR STRATEGY TO FULFIL OUR PURPOSE

To provide today's public water service...

Supplying the 2.2 million people who live in our area with safe, wholesome water is what we do.

Across Kent and Sussex and then to Surrey, Hampshire and Berkshire, we make sure homes, businesses, hospitals and all in our community that need water have access everyday for what they need to thrive.

Operating 24/7 to
supply 543m litres
of water per day

Responsible business commitment

We've been encouraging everyone to use tap water to refill on the go.

- More than 800 refill designated businesses in our region
- Supporting the installation of free drinking water fountains along Seaford seafront

Water treatment and quality

500,000 water quality tests each year – that's how we ensure your water meets the highest standards.

WATER TREATMENT

23%

of each £1 of your bill is spent

Extensive water testing at our state of the art laboratories

OUR STRATEGY AT A GLANCE – PURPOSE, VALUE, VISION, CULTURE

OUR PURPOSE

Why we exist

**TO PROVIDE TODAY'S PUBLIC WATER SERVICE AND
CREATE TOMORROW'S WATER SUPPLY SOLUTIONS,
FAIRLY AND RESPONSIBLY, WORKING WITH OTHERS TO
HELP SOCIETY AND THE ENVIRONMENT TO THRIVE**

OUR VISION

Where we want to be

To be the water company people want to be supplied by and want to work for

STRATEGIC THEMES

What we want to achieve



**Thriving
people**

How we help the
people who work
with us to thrive

Read more on page 102



**Flourishing
environment**

How we contribute to an
environment that flourishes
today and tomorrow

Read more on page 101



**Community and
consumer focused**

How we understand and
respond to the needs
of society

Read more on page 101



**Trusted
business**

How we build trust
in what we do

Read more on page 102

OUR OBJECTIVES

How we will measure success

38 performance commitments and 10 responsible business commitments

Read more at performance.southeastwater.co.uk

OUR VALUES

The South East Water culture

Values and behaviours support our strategy



Creativity

Fresh thinking,
improving, never
standing still



Passion

Dedicated to delivering
a safe, reliable service,
always caring for our
customers and each other



Excellence

Striving at all times to
be the best and deliver
the best



Trust

Dependable, safe and sound,
as a team always delivering
on our commitments.
Guardians of the environment



Agility

Responsive, flexible
and adapting quickly
to change

OUR BUSINESS MODEL

We are the regulated statutory water company in our exclusive supply area which is comprised of two non-contiguous regions in the south east of England. Our core purpose is to provide the public water service and to plan and invest in that service for the future. Wastewater services in our area are provided by either Thames Water or Southern Water.

We operate across the full water value chain:

We carry out all wholesale activities, managing water resources, treatment works and the distribution network to bring safe drinking water to all premises.

We provide wholesale water supplies to retailers in the non-household retail market and to new appointee water companies that supply premises on certain new development sites located within our geographic area. We provide new connection services to developers, self-lay providers and new appointees to connect new premises. We carry out related works to ensure there is sufficient capacity in our water network to meet the demand from these new premises and maintain water pressure for existing customers.

We provide all retail services to end-user customers in household premises in our area of supply. This includes meter reading, billing, payment collection, service and billing enquiries and dealing with complaints. Retail services to eligible businesses, public sector and third sector organisations in our area of supply are provided by separate water retail companies.

We also provide non-regulated commercial laboratory services, billing and other retail services and plumbing services where we are able to achieve synergy and optimise the resources and know-how of the business.

Wholesale activities account for 89 per cent of total income, retail activities for 7 per cent and non-regulated activities for 4 per cent.

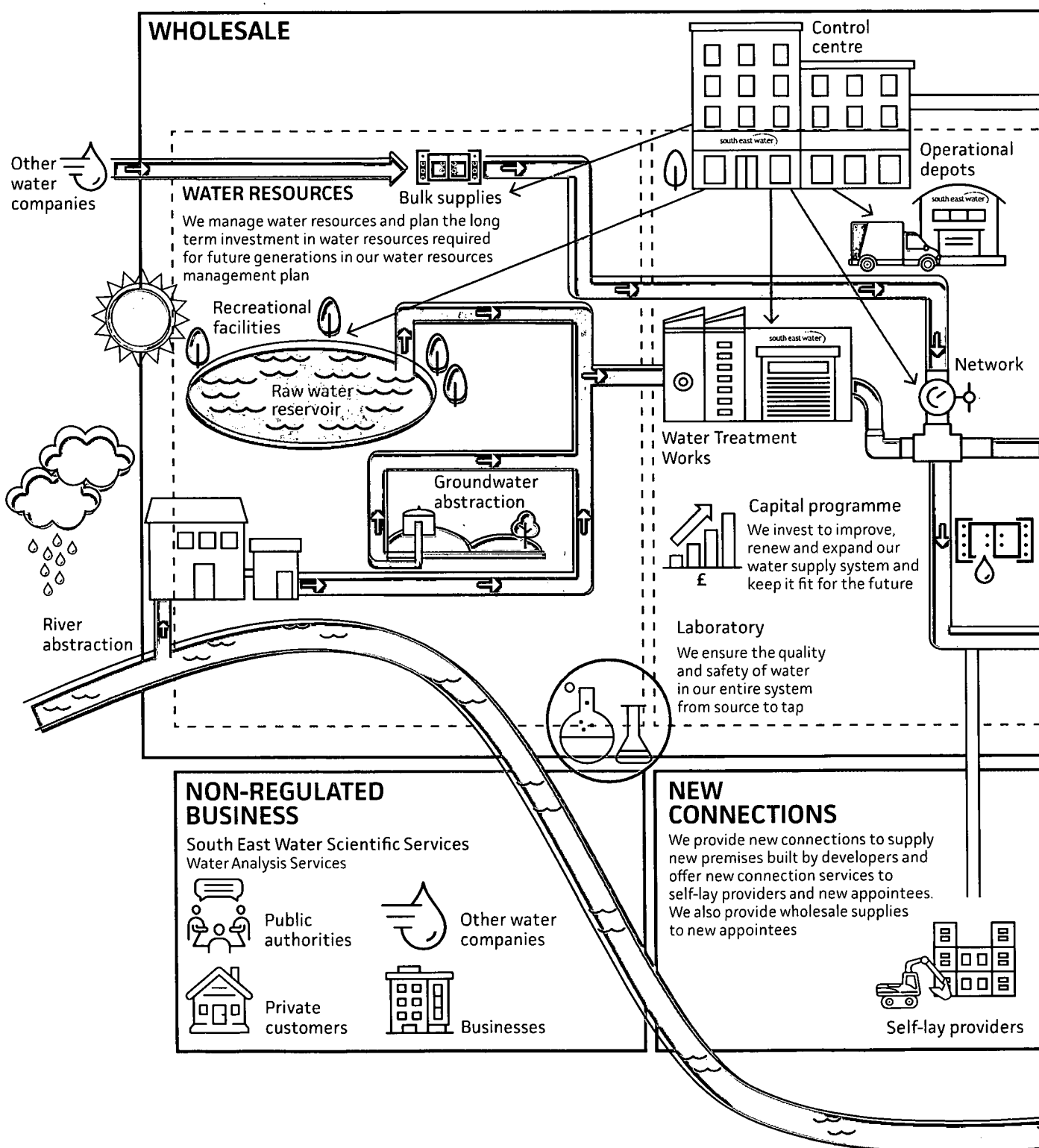
STRATEGIC REPORT

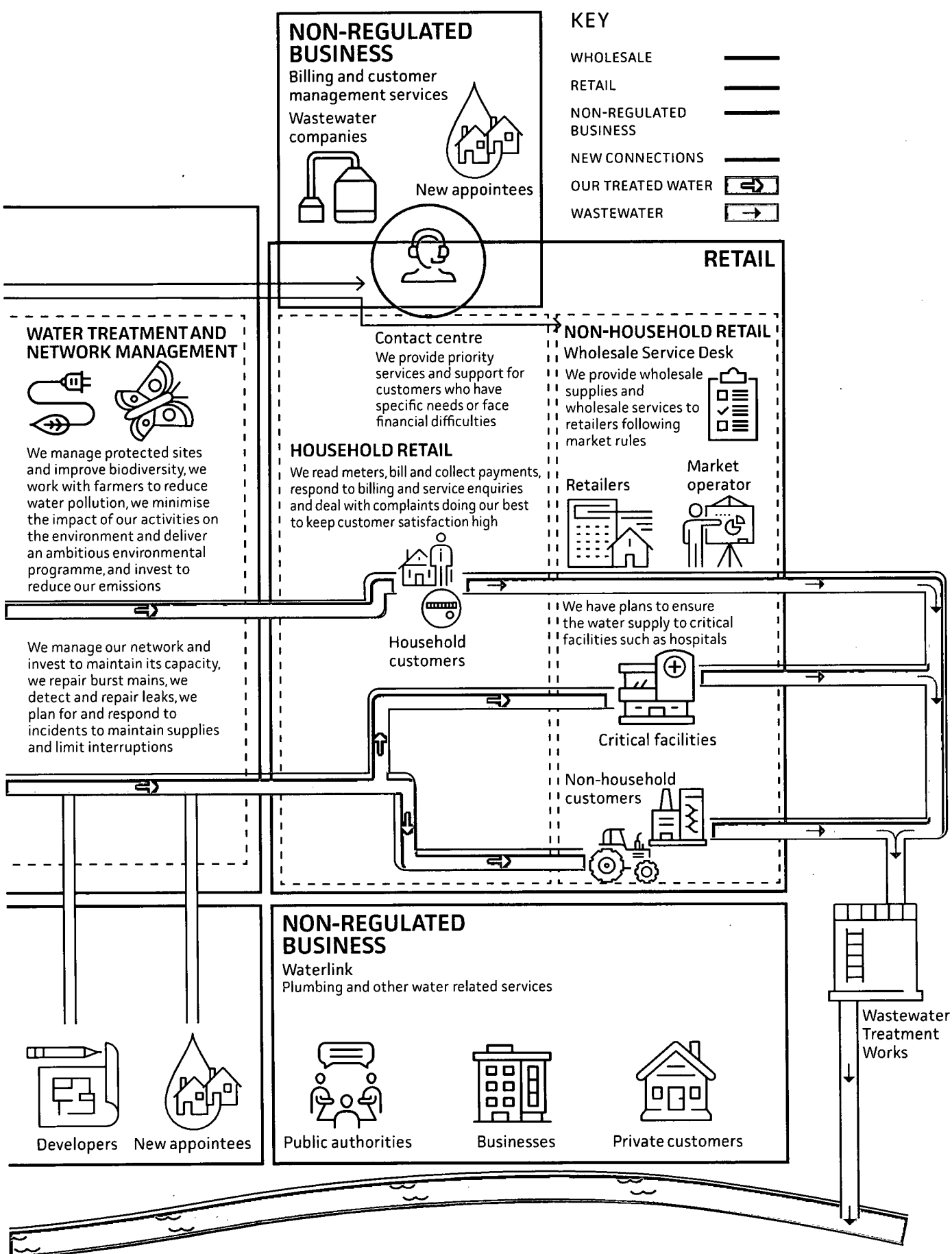
GOVERNANCE

FINANCIAL STATEMENTS

ANNUAL PERFORMANCE

BUSINESS MODEL





OUR BUSINESS MODEL continued**KEY RESOURCES****Our assets and networks built over generations**

The performance, condition and operation of our water resources assets, water treatment assets and our network built over generations, supported by information technology, are the essential elements of our business. Our investment in current and future assets is also crucial to our current performance and our long term ability to deliver the public water service and to fulfil our purpose. We must maintain a resilient service through asset management, investment and the effectiveness of our operations which also significantly influences customer satisfaction. This is essential to achieve good regulatory outcomes which in turn determine our ability to invest for the long term.

Fresh water and the environment

Our business model is intrinsically linked to natural capital and to the availability, sustainability and quality of fresh water resources. We rely on the environment and ecological services of the catchment; filtering, storage and transportation of fresh water resources to provide our service.

Our human and intellectual capital

We rely on the collective skills and expertise within our business in the management of the public water service and the knowledge of our water supply system which has an intrinsic value that it would be difficult to reproduce elsewhere. Our relationships with key suppliers and partners are also essential to our success.

Financial capital

Our performance and the sustainability of our operations in the long term require continuous investment in our assets and we need access to competitive financing to succeed.

KEY RELATIONSHIPS**Our customers and communities**

Consumers of the product we supply, the customers and communities we serve influence the decisions we make and their water use behaviours impact our operational plans on a daily basis. It is vital we build collaborative relationships for mutual benefit and to minimise negative impacts as we plan future investment in the region.

Our people and culture

Everything we achieve as a business is through our people and the culture we collectively develop — there are 986 directly employed by South East Water and hundreds more through our supply chain (see below). Many employees are long-serving and their knowledge and experience is important in helping us plan for the future as well as delivering excellent service today.

Our suppliers and partners

The supply chain is vital to the smooth running of our business, whether that be delivery of products for water treatment, infrastructure materials, or expertise to support the delivery of our investment programmes. We work with more than a hundred suppliers and partners both locally and internationally. Our key suppliers provide engineering and technical skills that complement those of our employees. We also receive bulk supplies of water from some neighbouring water supply companies so we work closely regionally to plan for long term water resources.

Our regulators

As a regulated business, South East Water benefits from open and constructive working relationships with our regulators: Ofwat, the Environment Agency, the Drinking Water Inspectorate (DWI) and Natural England.

HOW WE CREATE VALUE

HOW WE CREATE ECONOMIC VALUE

How we create economic value

We generate revenue through:

- billing for (i) water supplies to household end-user consumers based predominantly on metered consumption with an overall level of metering of circa 90 per cent of household premises and (ii) wholesale water supplies to retailers on the non-household retail market and new appointees
- non-regulated activities which maximise the value of the business know-how and assets (laboratory services, water and sewerage billing and retail services as well as plumbing and water management services)

The regulated business represents approximately 96 per cent of the company's turnover and profit from operations. This falls to 89 per cent after interest charges are taken into account.

We also provide new water mains and connections to our water network that are needed to supply new premises or similar new connection services to developers, self-lay providers or new appointees. The payments we received for providing these new connection services are limited to a proportion of the costs we incur as determined in accordance with regulatory charging rules.

Revenue from the regulated business

The revenue that the business is allowed to generate as a regulated water company is subject to several price controls set by Ofwat every five years which define revenue allowances for relevant segments of the value chain: water resources, network and household retail.

The cost of capital which includes an allowance for shareholder returns is also determined by Ofwat.

Factors impacting revenue and profit

When setting price controls, Ofwat takes account of how efficiently we operate our business and deliver our investment programme and of the quality of our services measured through performance commitments. Our revenue allowances are also adjusted by regulatory mechanisms for outperformance or underperformance of the targets set in Ofwat's determination (Outcome Delivery Incentives).

The business generates stable revenue streams but hot weather may cause seasonal increases in demand and revenue. However regulatory mechanisms operate to adjust revenue back to the revenue allowances set by Ofwat, without recognising the additional operating costs of meeting peaks in demand from these hot weather events.

In addition the revenue forecast incentive mechanism, that incentivises companies to predict their revenue, does not fully recognise the increased revenue volatility resulting from our high level of metering and therefore we might be exposed to a penalty.

HOW WE CREATE VALUE continued

Dry and hot summers and cold winters can also have a significant impact on reactive maintenance costs and other operating costs and can affect our profitability as well as our performance against our performance commitments' targets. The management of payment collection and bad debt as well as the level of support provided to customers with financial difficulties also influence profitability as our essential service must be maintained even in the case of non-payment.

These key factors influence our financial performance and the outcome of price determinations and, therefore, our long-term performance within the regulatory framework.

Revenue from the non-regulated business

Our commercial activities are developed on our core business strength and technical know-how. We provide billing, debt collection and related customer services to the wastewater companies that operate in our area providing the convenience of a single bill to our common customers and to new appointees.

Our accredited laboratory provides analytical scientific services to other water companies, public authorities, businesses and private clients building on the expertise and technical capabilities developed to meet our own water analysis requirements. Our Waterlink business offers a range of plumbing and water infrastructure services building on the know-how of the business.

HOW WE CREATE VALUE FOR OTHERS**Value to society***A reliable water supply*

Our water supply is used by households and all sectors of the economy and society. They rely on it, in particular for hydration and hygiene, and expect it to be available where and when needed. We ensure that they can all benefit from the value that water itself brings to them. We also plan and invest to ensure that our service will continue to be available to them in the future.

Public trust

The quality of our service determines the trust and satisfaction of our customers and those who rely on our service, and the strength of our "licence to operate". Public trust in the safety of water is another essential value we generate with our regulator the Drinking Water Inspectorate and is also our main responsibility.

We provide priority services to customers whose circumstances make them more vulnerable and provide assistance to those who have difficulties affording our services.

How responsibly we carry out our business, how we manage our impact on others and the environment, and how we engage with customers and stakeholders are also key drivers of our legitimacy as a provider of an essential service.

Supporting the economy

Our service is a key input for many organisations, including public services and businesses and we also support housing growth. We continuously invest in our assets, generating economic activity for our supply chain, and the taxes we pay contribute to the wider economy.

Responsible impact on the environment

We manage the impact of our operations and our works on the environment, working to minimise our negative impact and improve our positive impact. We need to balance the impact of our abstraction on water bodies and the wider environment and the need to take water from the environment in order to meet the essential need of society. In this context climate change, population growth, demand management and leakage management are central to our planning and the long term sustainability of our business model.

We work to improve the sustainability of our water abstraction. We work with farmers and other stakeholders to reduce the level of pollutants in the raw water extracted from our catchment areas that need to be removed in our treatment works.

We promote ways of saving water with our customers working with other water companies and stakeholders and have been reducing leakage year on year.

We manage more than 30 protected sites and invest to improve their environmental condition and biodiversity. We invest to reduce our emissions and support the transition to a low carbon economy.

Job opportunities and development

We provide training and career development opportunities and seek to promote the wellbeing of our employees. Due to the nature of our business which must operate without interruption we provide stable employment that offered financial security to our workforce during the Covid-19 pandemic. We provide learning and development opportunities in a wide range of disciplines.

Supporting our communities

We provide jobs to more than 980 direct employees and 680 employees of our direct contractors who work specifically to support our business. Our business also supports the wider community through the creation of jobs that contribute to activities in our wider supply chain, either indirectly or in part.

We also support our communities through volunteering of our employees, community sponsorship activities and recreational facilities on our land, such as at Ardingly and Arlington reservoirs.

Shareholder value

Water companies are attractive to investors because they are stable, regulated, efficient businesses providing a steady return. Through efficient operation and good performance we seek to provide a reasonable return to our shareholders and increase the value of the business.

For our investors the value we create is more than just about a financial return. South East Water's principal owners are signatories of the United Nations Principles of Responsible Investment (UN PRI) and are committed to strong environmental, social and governance performance as they recognise this protects the long term value and sustainable success of the company and strengthens our licence to operate.

OUR BUSINESS ENVIRONMENT

Natural environment

We rely on a secure supply of our natural resource – water. We must protect both the quantity and quality of our key environmental resource. Rainfall in the south east of England is lower than other parts of the country and the region is officially designated as an area of serious water stress. We must be prepared for the impacts of environmental change and adapt to these. We play an important role in mitigating climate change through our own actions to minimise our emissions and environmental impact – and supporting our community to do the same. We are significant landowners in the south east and with this we have tremendous responsibility in looking after our 33 sites which are within areas of Special Scientific Interest, including the national nature reserve at Lullington Heath in East Sussex, two nature reserves at Arlington Reservoir and Ardingly Reservoir in Sussex as well as numerous other areas of outstanding natural beauty.

Society

Water is at the heart of our society, without it the community we serve cannot thrive. But society also has a huge influence on our work. Changing consumer behaviours can have significant impacts on our business, both positive (where more environmental awareness leads to water saving) or negative (if the changes lead to increased water use). This year the “stay home” rules to protect against Covid-19 saw changing water use patterns that are expected to continue in 2021/22. Society provides our workforce, therefore the opportunities for learning skills and encouraging interest in careers in water across a diverse community is important. To manage our infrastructure we are often working in close proximity to our customers and therefore it is vital we coordinate our work with others and engage closely with those who will be impacted by our activities. The region we operate in has a higher percentage of older residents relative to other regions and therefore supporting customers who may have mobility issues or other age-related vulnerabilities is of high importance for us.

Innovation and technology

Technology is always progressing and it is important that as a business that we keep up with these ever-changing innovations. The opportunities they present enable us to work more safely and efficiently, but also to ensure we keep up with consumer and stakeholder expectations as these evolve in other digital and technological experiences. We look to incorporate the latest technologies to support our colleagues in their work, particularly important this year to facilitate home working. We aim to connect with experts through many stakeholder forums such as UKWIR and CIWEM and look for opportunities to collaborate to take opportunities such as the Ofwat Innovation Fund or other funding streams that are available. We recognise that technology also holds significant risks, in particular cyber security and data protection must be a key focus.

Economic environment

The economic climate impacts our business both through the ability of our customers to pay their bills, and the security of the supply chain we rely on. The south east of England is a more affluent part of the UK, but there are pockets of extreme deprivation and with an older population more pensioners who may have financial concerns. Market rate movements, such as interest rates and inflation, impact us, but we reduce risk as far as practical through our prudent financial management and five year planning.

Political and regulatory environment

The political and regulatory environment changes significantly over time and we ensure South East Water is able to respond to these changes and where appropriate influence future policy through our participation in consultations and as active members of the water industry trade body, Water UK. For example we have worked carefully to prepare for Brexit and also will continue to ensure we understand and influence changing policy that may come from leaving Europe. Our aim is to ensure any changes that affect the outcomes for our customers, shareholders and other stakeholders are positive.

We operate within a strict regulatory environment and work closely with our regulators to deliver a great service for our customers both now and in the future.

- The Water Services Regulation Authority (Ofwat) regulates our prices and levels of customer service
- The Drinking Water Inspectorate (DWI) monitors drinking water quality
- The Environment Agency (EA) covers environmental protection
- CCW (formerly the Consumer Council for Water) represents customers' interests

- Water Redress Scheme (WATRS) is an independent service designed to adjudicate disputes that have not been resolved through the water companies' customer service teams or by referring the matter to the CCW
- Natural England (NE) is responsible for the protection of designated sites for nature conservation
- Department for Environment, Food and Rural Affairs (Defra) deals with all aspects of policy relating to the water industry and we operate under a licence granted by the Secretary of State
- Centre for the Protection of National Infrastructure (CPNI) is the government authority for protective security advice to the UK national infrastructure

South East Water has worked collaboratively with water companies from across the country to prepare for the potential implications of the UK's exit from the European Union – with the county of Kent a key strategic route for trade and the consequent risks to our operations if the highways are jammed. We continue to work with our supply chain and have measures in place to minimise any impact. We continue liaising with government, regulators and, on a local level, with Local Resilience Forums, keeping them updated on our activities.

RISK MANAGEMENT AND PRINCIPAL RISKS

HOW WE MANAGE RISKS

We have comprehensive systems of internal control and risk management and we monitor their effectiveness regularly in compliance with the principles of our corporate governance code. This risk management framework is also closely linked to the way we monitor and measure our performance and compliance with our statutory obligations and commitments which is subject to external assurance by third parties. This ensures that the board and the audit and risk committee review all material controls including financial, operational and compliance controls.

Our company monitoring framework includes an analysis of the strengths, risks and weaknesses in relation to data and information provision which we use to ensure the information we publish is accurate and reliable. We provide more details on the assurance of our performance and other regulatory data in the annual performance report.

We maintain a formal risk register and risk management system for the identification, evaluation and mitigation of risks. The board defines South East Water's risk management framework and reviews the risks on the register and the effectiveness of the relevant mitigation measures at least once a year.

The board also reviews monthly, quarterly and annual reports on performance which highlight risks and business or operational issues as they arise. Please see page 127 for a summary of the board activities in the year. The audit and risk committee monitors the effectiveness of our systems of risk management and internal controls on an ongoing basis. Please see page 139 for the report from our audit and risk committee.



The board also reviews monthly, quarterly and annual reports on performance which highlight risks and business or operational issues as they arise

Individual managers and heads of department are responsible for identifying risks relevant to their area of responsibility and defining and implementing mitigations. Risks relevant to each directorate are monitored by the relevant director every month and the risk profile of a particular area is presented by the relevant head of department to the executive team.

The risk management systems described here have been in place for the year under review and up to the date of approval of the annual report and accounts.



Read more at southeastwater.co.uk/cmf

KEY CHARACTERISTICS OF OUR RISK MANAGEMENT MODEL

Our risk management model uses standardised risk descriptions and categories for the controls, impact and likelihood of risks. Each risk is allocated a priority score based on its potential impact and likelihood. The prioritisation of risks in the register takes account of the controls and mitigation measures currently in place. Our risk management model also includes an assessment of planned mitigation measures. This gives visibility of the reduction in risk exposure expected from planned mitigation and is also used for reviewing the actual effectiveness of mitigation. This model allows the board to assess and manage risks at a strategic level and the executives to manage risks at an operational level.

Risks are reviewed regularly by the executive team and the board. A number of our risks have been impacted by Covid-19, and subsequently controls and actions have been strengthened or brought into place to mitigate these increased risks as much as possible. We provide details on how the Covid-19 pandemic affected the business in the section on principal risks and uncertainties on page 38.

While the corporate risk register identifies risks that exist in the present and short term we have also extended the register to assess potential risks to outcome delivery incentive (ODI) success in the 2020 to 2025 price control period. In total 110 risks were identified as potentially having a direct impact to one or more ODI performance measures. Identifying these risks ensures we are able to put early mitigation measures in place to optimise performance across our commitments.

We have also undertaken a review of the corporate risks with a responsible business lens on the register. These are reviewed by the responsible business committee on a quarterly basis.

To supplement the corporate risk register we are also evaluating emerging and future risks – broadly targeting a rolling 10-plus year horizon span. Consideration of long term risk planning also involves future consideration of where political, social, and economic factors may take the business.

An understanding of these risks will allow the business to plan, and build resilience to the future threats that these identified risks may pose. Risks identified to have no immediate solution can be channelled through our innovation programme – to establish if as yet untested (or unused) technology/processes can be sought to reduce or control future risks.

Risk management model see page 32

PRINCIPAL RISKS AND UNCERTAINTIES

Principal risks are those which due to their likelihood or magnitude can significantly impact on the long term success of our company. We consider their impact on our business model, future performance, solvency and liquidity. We also review the adequacy of the mitigations in place as recorded in our risk register.

As required by our corporate governance code, the audit and risk committee and the board carried out a robust review of our principal and strategic risks and of high impact and emerging risks on our risk register. We also compared our principal risks with those identified by other companies in the water industry.

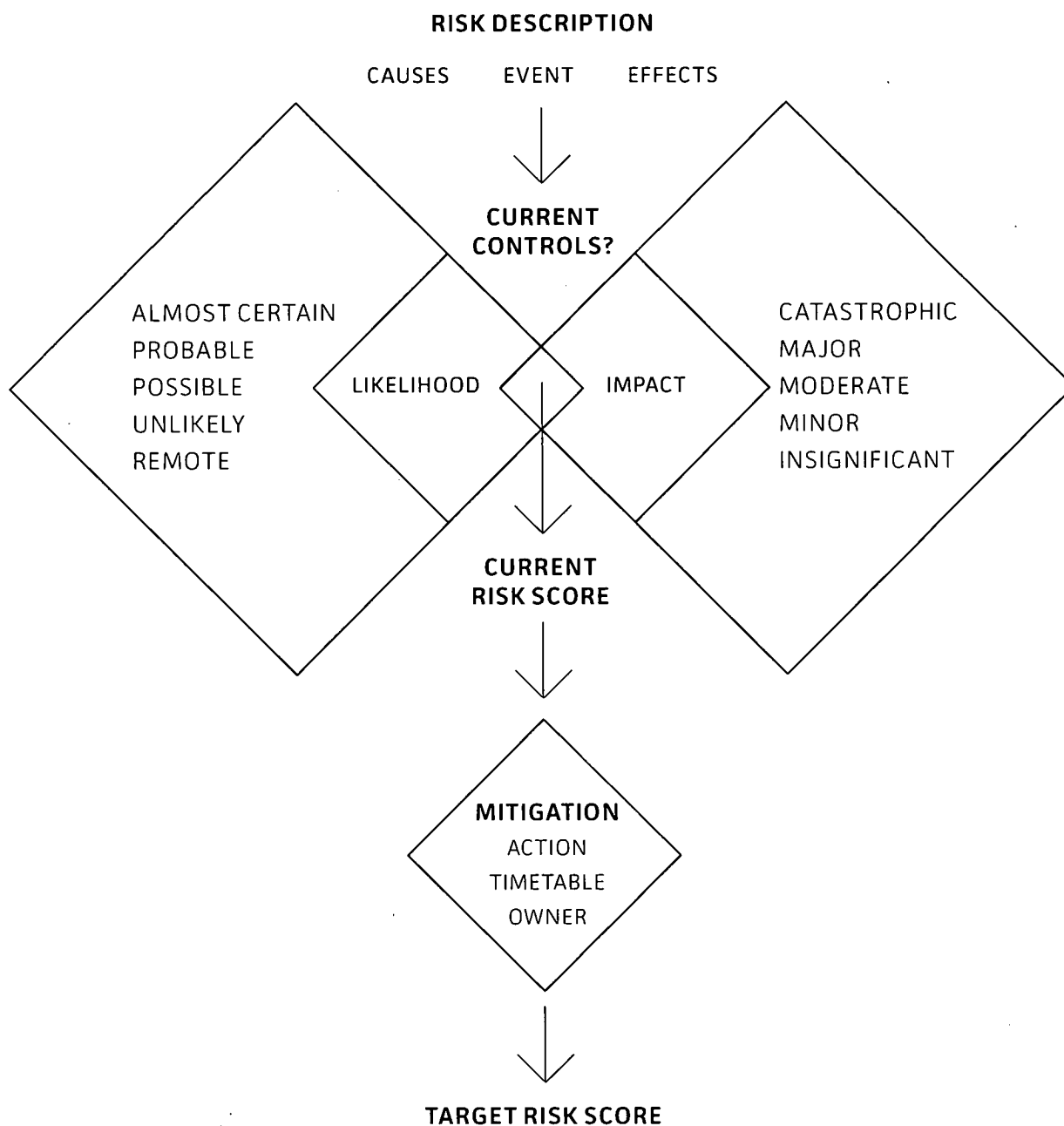
We describe our principal risks, their potential impact and how they are managed on the following pages. These principal risks have been considered in the context of our business model and strategy. We have reflected the impact of Covid-19 which affects a number of our principal risks based on our experience in 2020/21 and our work as a company and with the water industry to assess the future potential impact on our company, the water sector and the UK economy.

Some of the risks described in this section also bring business opportunities which we are preparing for. We also take advantage of the potential for business improvement that arises from risk management and the implementation of mitigations.

The principal risks described represent an aggregation of individual underlying risks in our risk register. The current risk exposure and trend presented is a reflection of the risk levels and trends of the related underlying individual risks in our risk register.

RISK MANAGEMENT AND PRINCIPAL RISKS continued

RISK MANAGEMENT MODEL



RISK DESCRIPTION

The tool ensures a consistent language regarding the description of risks is maintained. A risk must satisfy three criteria

- **Causes** – are definite events or set of circumstances that exist which will give rise to uncertainty
- **Event** – an uncertain event is the true risk, as it may or may not happen and gives rise to uncertain outcomes
- **Effects** – are unplanned variations that would arise as a result of the risk occurring

CURRENT CONTROLS

The controls that are already in place to deal with the identified risk

- **Likelihood** – the likelihood of the risk occurring must be assessed using set criteria
- **Impact** – risks are categorised and their impacts determined. There are 12 categories ranging from financial through to operational or reputational impacts. Each category has a defined level of impact ranging from insignificant and catastrophic. This allows for a consistent approach to be adopted across the whole of the business. Where appropriate a risk may have more than one category e.g. both financial and reputational

CURRENT RISK SCORE

This is the product of impact and likelihood. The most catastrophic risk is calculated with a score of 25, with the most insignificant scored at one

MITIGATION

Actions being undertaken to reduce or manage a risk. Once embedded these mitigation steps will form part of the current control assessment

TARGET RISK SCORE

A target risk score can be calculated to show where the risk level will be once the controls and actions are put in place

CHANGES TO OUR REPORTING ON PRINCIPAL RISKS

The presentation of principal risks and their assessment has been reviewed providing more details on current risk exposure and trends. Links with our strategy and business model have also been highlighted.

Covid-19 has been included as a separate and overarching risk with details on how it has affected the business and the expected impact it will continue to have in 2021/22 based on our experience in 2020/21.

Water resources risks and climate change were included jointly last year. In this report climate change has been included as a new risk which covers the wide range of impacts it may have on the business. A new risk - failure to meet water demand covering risk relating to water resources as well as supply demand balance and treatment and distribution capacity has been introduced as a standalone risk which more accurately reflects the specific challenges we faced during the 2020 heatwave.

Several risks have been grouped to better reflect their interrelations:

- the market reform risk has been combined with risk 10 - adverse policies or political and social environment
- the bad debt risk has been included with risk 12 - macroeconomic risks.
- the price determination risk has been combined with risk 10 - Adverse policies or political and social environment also reflecting the fact that the outcome of PR19 is known
- the investment programme delivery risk has been combined with risk 6 - Failure to deliver business plan and to meet regulatory outcomes

DELIVERING OUR STRATEGY TO FULFIL OUR PURPOSE

**and create
tomorrow's
water supply
solution...**

We plan for future water resources and develop our water supply system.

We are constantly innovating and using new technologies and services to make sure the next generation has a secure water supply too.

We use tunnelling
techniques to minimise
environmental impacts

Responsible business commitment

We play an active role regionally to help plan ahead for future housing growth.

- Responded to more than 60 neighbourhood and local plans
- Inputted our expertise to 11 water cycle strategies

How we invest in your water

83 water treatment works to ensure our water is of excellent quality.

CAPITAL EXPENDITURE

£93.3 million

Decrease of 10.7 per cent on last year

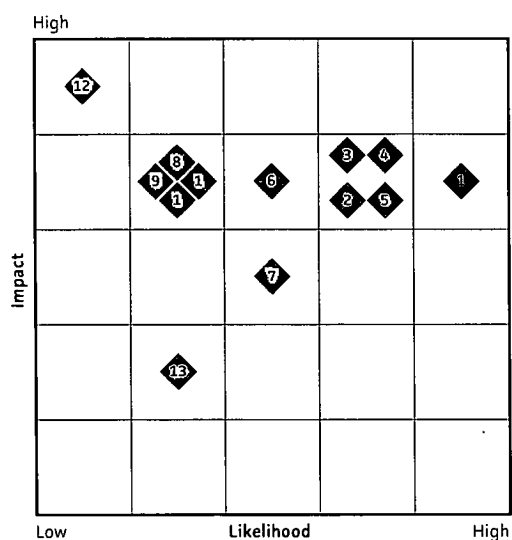
Mains water pipe programme, part of our investment strategy

We're investing £2.8 million in a new pipeline to secure the drinking water supply for Sevenoaks in Kent for years to come

OUR PRINCIPAL RISKS

OVERVIEW OF OUR PRINCIPAL RISKS

Principal Risk	Potential exposure
1 CLIMATE CHANGE	
2 COVID-19	
3 STRATEGIC ASSET FAILURE AND MAJOR OPERATIONAL INCIDENT	
4 FAILURE TO MEET THE PEAK DEMAND FOR WATER	
5 FAILURE TO DELIVER BUSINESS PLAN AND MEET REGULATORY OUTCOMES	
6 SECURITY OF ASSETS, SYSTEMS AND DATA	
7 MACROECONOMIC RISKS	
8 WATER QUALITY INCIDENT	
9 ADVERSE POLICIES OR POLITICAL & SOCIAL ENVIRONMENT	
10 REGULATORY, ENVIRONMENTAL AND LEGAL COMPLIANCE	
11 FINANCIAL RESILIENCE	
12 HEALTH, SAFETY AND WELLBEING	
13 PEOPLE AND CULTURE	



KEY

Potential exposure



Major



High



Moderate



Low

Risk trend



Increasing



Stable



Decreasing

Related strategic themes



Flourishing environment



Trusted business



Thriving people



Consumer and community focused

The potential exposure indicator reflects our assessment of the overall net risk exposure taking account of individual underlying risks in our risk register. The colour of the risk on the matrix indicates potential exposure.

1 CLIMATE CHANGE

Climate change will lead to long-term shifts in climate patterns (such as hot and dry summers, changes in rainfall and sea level rise) and to an increase in the frequency and severity of acute weather events such as floods, storms, droughts or heatwaves. This will affect the quantity and quality of water resources and disrupt our operations and those of third parties we rely on such as energy suppliers. The effect of climate change will increase the likelihood and impact of our main operational risks.

Failure to adapt our infrastructure, to improve its resilience and to manage demand would mean that we would not be able to meet our statutory duties and demand in the future. It would also lead to additional costs that could affect the financial resilience of the company in the long term. A failure to adapt to climate change and to deliver our own net zero carbon commitments could lead to significant reputational damage.

Our ability to invest in the adaptations needed to be able to meet our future obligations also depends on external factors such as the outcome of successive price determinations and how effectively climate adaptation is addressed in the political and regulatory environment. The adaptation of other sectors on which we rely for our operations will also have an impact on our own resilience.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
The UK has seen its warmest 10 years since 2002 and 2020 was the UK's third warmest, sixth wettest and eighth sunniest year in the national series. The 2020 heatwave put significant pressure on our water supply system. There are concerns regarding the potential effects of tipping points in the climate system. This heightens the need for adaptation. The uncertainty explains why the risk is being categorised as major, even though its effects will increase over time.	▲▲	Link to key resources & relationships: Fresh water and the environment Our assets and networks Our regulators Our customers and communities Impact on outcomes: Responsible impact on the environment Reliable water supply Public trust	 	
Closely related risks 3 / 4 / 8 / 9 / 11				
Mitigation				
Investment in adaptation - Our Water Resources Management Plan and Drought Plan incorporate climate projections to determine the most appropriate solutions and investments to develop water resources, improve the resilience of our supply system and manage demand. - Investment in flood protection with improvement to 92 operational sites in 2020 to 2025 and to improve our resilience to power outages. - A significant programme of environmental schemes include managing the impact of our water abstraction.		Managing climate risks - Our third adaptation report to be published at the end of 2021. - Progressive adoption of the recommendations of the Task Force on Climate Related Financial Disclosure (TCFD) to ascertain and quantify the financial impact of climate change on the company.		
		Reducing our emissions - A target to reduce our greenhouse gas emissions by 80 per cent by 2025 (when compared to 2017/18). - Our commitment to achieve net carbon zero by 2030 as part of the water industry's Public Interest Commitment and independently under our net zero roadmap. - Procurement of power purchase agreement relating to new renewable energy assets and planned investment in private solar generation.		

OUR PRINCIPAL RISKS continued

2 COVID-19 PANDEMIC

The Covid-19 pandemic has affected most aspects of our operations in 2020/21 and will continue to have effect in 2021/22.

Failure to adapt quickly to new ways of operating and to the effects of the pandemic and restrictions on our customers and supply chain could significantly disrupt our operations and potentially caused interruption or a significant loss of quality of service. The Covid-19 pandemic has amplified other principal risks.

This section reviews the effect of the pandemic on our business, how we have responded and how we anticipate the pandemic will affect the business in 2021/22.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
The effects of the pandemic are better known and we have demonstrated that we were able to continue our operations without significant disruption to our services. The vaccination campaign improves the prospect of a progressive removal of restrictions and a resumption of normal economic activities. However, there is still uncertainty regarding further restrictions and the impact on bad debt and some of the impact on our operations will continue into 2021/22. For this reason the risk is considered stable but remains high.	◀▶	Link to key resources & relationships: Our human and intellectual capital Our customers and communities Our people and culture Our suppliers and partners Impact on outcomes: Reliable water supply Public trust Supporting our communities	  	

Closely related risks 3 / 4 / 5 / 12

Health safety and wellbeing of our workforce

Shortage of staff

Main steps taken

- Implemented new ways of working for field roles and in our laboratory to avoid contamination at work.
- Generalised home working whenever possible.
- Consulted widely and regularly on health and safety and wellbeing and how to adapt to new ways of working and provided guidance.
- Rolled out software and hardware to enable remote working.

Prospect for 2021/22

- Current arrangements have proved effective and will continue to be implemented and adapted as required by the evolution of the pandemic.
- We have planned for a controlled return to work and are consulting on longer term changes to ways of working recognising that home working and flexible working will be more prominent across our entire workforce.
- The agility, flexibility and commitment demonstrated by our workforce in response to the pandemic will continue to be a strength in 2021/22.

Outcome to date

- We experienced low levels of absences including those related to Covid-19.
- We had consistently high levels of response to our surveys with positive scores expressing support for our actions.
- Our staff responded to our encouragement to use their annual leave protecting their wellbeing and limiting the risk of staff shortages as restrictions are lifted.

2 COVID-19 PANDEMIC continued

Our ability to effectively and efficiently continue to deliver the essential public water services to our customers during the pandemic

Impact on performance commitments

Main steps taken

- Tested and adapted our emergency response and business continuity plans.
- Continued the implementation of actions plans for the delivery of our ODIs.

Outcome to date

- We maintained our core services throughout the year only reducing some customer facing activities to meet social distancing guidelines.
- Certain ODIs have been affected by the pandemic especially interruption, non-household voids and per capita consumption.

Prospect for 2021/22

- Our response to the Covid-19 pandemic demonstrated that we are able to operate effectively under lockdown restrictions.
- We will work with Ofwat to understand how they intend to take account of the effect of the pandemic on ODIs and penalties. The nature, scale and timing of any intervention from Ofwat to mitigate the financial impact arising from Covid-19 is not known at this stage.

Changes in consumption patterns

Managing concurrent events

Main steps taken

- Reduced planned outages to the minimum level possible and well under the level considered acceptable by Ofwat.
- Activated specific preparation for high summer demand and pre-emptive steps of our emergency response plans.
- Early communication with customers to alert them of the pressure on the water system and the need to limit their non-essential use of water.
- Mobilised the workforce to support incident response.

Outcome to date

- Widespread working from home, reduced commuting and travels outside of our area contributed to a significant increase in water consumption by household customers. Combined with the effect of the heatwave this resulted in unprecedented peak summer demand that resulted in interruptions in more vulnerable parts of our network and the maximum ODI penalty being incurred.

Prospect for 2021/22

- We expect that household customer demand will remain high in 2021/22 and in the medium term higher than before the pandemic.
- This increases the risks of 'major operational incident' and 'failure to meet demand'. More details are provided below on mitigation against these risks, building on lessons learnt from the 2020 heatwave.

OUR PRINCIPAL RISKS continued**2 COVID-19 PANDEMIC** continued**Increased affordability and vulnerability challenge for some of our customers****Increased bad debt and deterioration of cash collection***Main steps taken*

- Maintained our call centre fully operational putting in place the systems required to continue to operate remotely at normal capacity.
- Provided help with payment terms and extended our social tariff.
- Adapted debt recovery activities that were suspended temporarily and resumed taking care of providing support to customers struggling to pay.
- Implemented emergency support for retailers following successive amendments to market codes.

Outcome to date

- Maintaining normal operations at our call centre allowed us to continue to provide normal customer service interaction as well as additional support to customers.
- Bad debt provisioning in relation to Covid-19 has increased significantly in line with our revised bad debt methodology as well as the take up of our social tariff.
- Emergency support to retailers has come to an end without experiencing any insolvency of a significant retailer.

Prospect for 2021/22

- We expect to be able to continue to offer normal customer service interactions in 2021/22.
- The increase in bad debt provisioning and social tariff is likely to continue into 2021/22 and we have reflected this assumption in our budget and corporate plan. We will continue to monitor the level of bad debt and the needs of our customers in 2021/22 and beyond.
- We expect a progressive improvement in non-household demand as restrictions are lifted but remain cautious due to the possibility of further restrictions being imposed as new variants emerge.

Efficient delivery of our capital programme*Main steps taken*

- Reviewed our investment programme to take account of the impact of the lockdown.

Outcome to date

- New working arrangements to protect our workforce had an impact on our ability to deliver our capital programme in 2020/21 and to achieve efficiencies due to additional costs and practical constraints on how works could be delivered.

Prospect for 2021/22

- We are continuously monitoring and forecasting the impact of the Covid-19 pandemic on our ability to deliver our investment.
- We are reviewing how we may achieve our efficiencies recognising that the unprecedented challenges we and our supply chain face will have an impact on our ability to deliver our targeted efficiencies and result in additional contract costs.
- We expect a potential increase in input costs as the supply chain seeks to recover and as economic activity restarts. We will monitor inflation and its impact on our delivery costs.

2 COVID-19 PANDEMIC continued

Supply chain and delivery partners

Main steps taken

- Coordination with our main contracting partners to organise the continuation of our activities whilst applying safety measures for our joint workforce.
- Worked with our supply chain to anticipate and address supply issues that could affect our operations and ensure appropriate stocks were maintained.

Outcome to date

- We have not experienced significant supply chain disruption but incurred additional costs as contractors needed to alter their ways of working.
- We successfully managed the transition to a new R&M contract with Clancy and the commencement of our new engineering services contract with Atkins.

Prospect for 2021/22

- We will continue to consult and coordinate with our supply chain and will monitor how the lifting of the restrictions and the increase in economic activity may affect our supply chain to identify any bottlenecks in supply.

Liquidity and financial resilience

Main steps taken

- Additional withdrawals on our credit facility to ensure an appropriate level of liquidity.
- Agreed amendments to our finance documents that enable further borrowing under certain trigger event scenarios.
- Close monitoring of ratios and credit ratings throughout the year with updated forecasting presented at board meetings.

Outcome to date

- Our liquidity has remained healthy throughout the year and continues to do so.
- Our finance documents have been updated to allow greater flexibility in arranging further borrowing.
- We have met all our covenant requirements and are forecast to continue to do so. Our credit ratings have been maintained at the pre-Covid 19 level.
- We are in the process of replacing our existing revolving credit facility with a new facility with an increased limit of £125 million.

Prospect for 2021/22

- Our assessment of our prospects in 2021/22 and beyond are detailed in our viability statement.

OUR PRINCIPAL RISKS continued

3 STRATEGIC ASSET FAILURE AND MAJOR OPERATIONAL INCIDENT

Strategic asset failures and major operational incidents may affect our ability to deliver a safe and uninterrupted water supply to a large number of customers or cause damage to third parties. Disruption to our water supply has an impact on public health, on daily life and economic activities. These events may be caused by unplanned outages of critical assets (including due to ground movements or naturally occurring sinkholes), bursts of large water mains or severe weather events.

These risks may affect our own water infrastructure or those of other water companies that provide us with a bulk supply of treated water. We also rely on other utilities especially electricity providers to operate our facilities and prolonged energy outages may have an impact on our operations.

Incidents lead to additional production and distribution costs (such as additional treatment, repairs, incident management, emergency supplies of water etc.) and compensation payments to customers whose supply was affected. They may lead to ODI penalties for exceeding our targets on supply interruption. They generally affect customers' complaints, satisfaction and the perception of the company by customers and other stakeholders and may lead to ODI underperformance or penalty under the C-MeX regulatory metric for customer experience. They may also lead to liabilities to third parties due to damage to their property. We must ensure that our response to incidents always put the safety of our workforce first.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
The general condition of our assets is stable, but sinkholes at our reservoirs in Aylesford combined with higher demand linked to the Covid-19 pandemic result in an increasing level of risk with specific mitigation being put in place. Closely related risks 1 / 2 / 5 / 12		<i>Link to key resources & relationships:</i> Our assets and networks Our customers and communities <i>Impact on outcomes:</i> Reliable water supply Public trust	 	

3 STRATEGIC ASSET FAILURE AND MAJOR OPERATIONAL INCIDENT continued

Mitigation

Operational management

- Trained and competent operational and asset management staff.
- Cross-skilling programme to improve the resilience of operational teams and facilitate collaboration.
- Developing a systems approach to operational management that takes account of all aspects of regional management from the water source through to customers' taps.
- Emergency plans and procedures (including under the Security and Emergency Measures Directions) which are regularly tested and independently audited.
- Wholesale steering group for Operations and Assets coordination to implement continuous improvement.
- Incident preparation teams for the pre-emptive management of weather related operational challenges and early customer engagement.
- Scheduling of planned maintenance to achieve minimum outages during the periods of the year with higher operational risks.
- Developing a calm network strategy to help achieve our leakage target and reduce mains bursts including valve operations and reduction of pump surges.
- Standby power generation at operational sites.

Asset management

- Implementation of an asset management system that is compliant with ISO 55000 by 2025, building on our existing PASS 55 asset management system.
- 24 hours network modelling for rezoning to minimise the number of customers impacted and restore supplies as soon as possible.
- New incentives for innovation and improving resilience within our engineering consultancy framework.
- New investment decision support tool. Risk based prioritisation of maintenance with customer impact as a primary consideration.
- Asset management strategy implementing new asset health metrics.

Resilience framework

- Resilience maturity assessment for a system based approach to resilience and improved horizon scanning and adaptation to climate change. Resilience training of staff. Classification of criticality for all assets allowing for prioritisation of investment to reduce exposure to risks.
- Schemes to improve interconnectivity, facilitate reconfiguration of the network and remove single points of supply.
- Developing approach for mitigating certain key low likelihood but high impact risks and development of strategic options for mitigation.
- Area plans for each Resource Zone published annually and identifying key risks for each zone.

Lessons learnt and improvement

- Formal lessons learnt process followed after each significant incident with implementation of action plans.
- Testing and adaptation of operational plans in response to the Covid-19 outbreak to be able to protect the supply to critical facilities, to ensure the safety of our workforce and the public and to maintain social distancing when responding to incidents and especially supply interruptions due to bursts.
- Following the freeze/thaw in 2018, we used our reports on lessons learnt to prepare and deliver a comprehensive action plan to improve our readiness, resilience and our response capabilities in case of severe weather events.
- Bringing our Aylesford reservoir back in service and delivering a fast track resilience scheme on the site of the future Butler WTW for the summer of 2021.

OUR PRINCIPAL RISKS continued

4 FAILURE TO MEET THE PEAK DEMAND FOR WATER

We rely on water in the environment to provide the public water supply. Our supply area is designated as an area of serious water stress and densely populated. Weather events such as droughts put pressure on already stressed raw water resources.

Dry and hot weather may lead to peaks in demand that could exceed our ability to produce and distribute enough water. In 2020, the combination of the hot weather and changes in consumption patterns due to the Covid-19 restrictions resulted in exceptionally high demand leading to supply interruptions in certain parts of our network.

In the long term, restrictions on water abstraction to protect the environment and the effects of climate change will result in additional stress on the water resources needed to meet an increasing demand linked to population and housing growth. This may also lead to increased risks of over abstraction and related prosecution and fines.

Risk Trend	Link to business model	Related strategic themes	Potential exposure
In the short term, changes in consumption patterns related to Covid-19 are expected to persist as more people work from home and to reduce our headroom in case of unplanned outages. In the long term, underlying risk factors will continue to increase with further reduction to abstraction due to sustainability measures, population growth and climate change. Closely related risks 1 / 2 / 5	Link to key resources & relationships: Fresh water and the environment Our assets and networks Our customers and communities Impact on outcomes: Reliable water supply Public trust Responsible impact on the environment	  	
Mitigation			
Long term planning - Our water resources management plan developed in collaboration with regulators and other water companies in the south east of England to invest in future water resources and production capacity. - Working with regulators to ensure local resilience issues (e.g. local network capacity) are addressed in the WRMP process. - Our drought plan which includes clear steps for managing demand and securing resources. Reducing demand - Our performance commitment to reduce per capita consumption by 7.6 per cent together with an ambitious programme to drive behavioural changes from customers for 2020 to 2025. - Our metering programme which was completed by 2020.		Operation performance - Consistently meeting our leakage targets and commitment to significant additional leakage reductions in 2020 to 2025. - Implementation of changes to the monitoring and management of our water supply system to be able to limit the risk of outages in the face of unprecedented water demand due to changes in demand linked to Covid-19. - Mobilisation and preparation to meet summer demand and communication plan to alert customers on the need to use water responsibly during peak periods. - Specific investment to address abstraction reduction such as our Fleet to Greywell main and to improve the resilience of our operations.	

5 FAILURE TO DELIVER BUSINESS PLAN AND MEET REGULATORY OUTCOMES

There are financial and reputational risks associated with a failure to deliver our business plan commitments. Our position at the next price determination may also be impacted.

The PR19 determination included a large number of outcome delivery incentives (ODIs) using targets defined by reference to upper quartile performance with the introduction of in-period reward/penalty adjustments. It also introduced new customer satisfaction measures (C-MeX) and new developer services satisfaction measures (D-MeX). These changes bring new compliance requirements and related risks.

Ofwat's approach to risk and return in its final determination with more stretching targets leads to an increased risk of penalties even with improvements in performance. In-period ODI adjustments will have an impact on our revenue during 2020 to 2025. Our ODI performance could also be affected by incidents affecting other companies that provide us with a bulk supply of treated water.

We must ensure that we efficiently deliver the investment necessary to maintain and improve our services to customers and to meet our long-term future obligations. The risks affecting the delivery of our investment are internal, relating to the management of the delivery of our programme, and external such as extreme weather conditions, incidents affecting works, supply chain risks or significant events affecting the economy such as the Covid-19 pandemic.

Risk Trend	Link to business model	Related strategic themes	Potential exposure
Unprecedented demand due to Covid-19 during the 2020 heatwave resulted in the maximum penalty for interruption. The financial constraints imposed by the final determination (with stretching targets and higher risks of penalties) combined with the impact of Covid-19 increased the risks related to the efficient delivery of investment in the past year but the risk remains stable. Closely related risks 2 / 3 / 4 / 5 / 10	◀▶ <i>Link to key resources & relationships:</i> Our assets and networks Our regulators Financial return <i>Impact on outcomes:</i> Reliable water supply Public trust Responsible impact on the environment Shareholder value		
Mitigation <i>Management of delivery</i> - Detailed processes to ensure that we operate within the assumptions of the price determination (including ODIs and investment). - Early implementation of business improvement initiatives to deliver our ODIs and ensure customer and employee engagement. - Dedicated steering groups monitoring key measures such as interruption, water quality, customer services, customer perception and leakage. - Implementation of resilience and innovation action plans. - Processes involving our asset, engineering and operations functions to ensure that projects are planned and delivered on time and budget. - Projects reviewed by an investment committee and a programme management office. Project scopes and planned efficiencies reviewed with our engineering partner and the early involvement of our framework contractors to identify risks and opportunities for innovation and savings. <i>Monitoring and reporting</i> - Processes to continuously monitor and report regularly on our compliance with regulatory obligations at senior management and board levels and take corrective actions. - Continuously assess the deliverability and financeability of the final determination and any risk it may create for the company for the next regulatory period. - Executive remuneration targets aligned with regulatory outcomes.			

OUR PRINCIPAL RISKS continued

6 SECURITY OF ASSETS, SYSTEMS AND DATA

The physical security of our assets and the resilience of our information technology infrastructure is essential to maintaining our service to the public and implement our business continuity plans.

We must protect our sites and our water supply against accidental or deliberate security threats. We must protect ourselves from loss of systems, data and cyber-attacks and keep customers' data up-to-date and safe.

Our reliance on IT systems to manage the activities of our front line staff and to maintain our normal activities through home working has meant that the security and resilience of our IT systems has become even more important and the impact of any downtime could be greater than before the Covid-19 pandemic.

Failure to protect personal data may lead to fines, enforcement actions and legal actions and would cause reputational damage. Loss or corruption of data would result in disruption to the business and additional costs.

We must ensure compliance with the new requirements imposed by the General Data Protection Regulation as retained in the UK (UK GDPR) and the Network and Information Systems Regulations 2018.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
We maintain this risk as high due to the constant emergence of new threats and the risk of exploitation of vulnerabilities that may not have yet been fixed by software providers. There is additional reliance on IT systems during the Covid-19 pandemic but our level of mitigation has been maintained. Closely related risks 2 / 3 / 4 / 8 / 10	◀▶	Link to key resources & relationships: Our assets and networks Our human and intellectual capital Our customers and communities Impact on outcomes: Reliable water supply Public trust	 	
Mitigation				
<i>Investment in adaptation</i>				
- Our corporate security steering group continuously monitors physical and data security and data protection matters to identify new risks and monitor the effectiveness of our security processes and the implementation of action plans. - Department champions are trained on these issues and we continuously promote awareness of risks, highlighting how unsafe behaviour could be exploited by external threats. - Disaster recovery systems and facilities which are regularly tested. - Investment in security measures against unauthorised access to our systems and in software to help us monitor activity on our network. - Recognised cyber security certifications. - Work with relevant external organisations to test the effectiveness of our resilience and security measures and review the maturity of our security systems and procedures. - We have updated our risk management process and practices to recognise the change in our risk profile in this area due to our additional reliance on IT systems during the Covid-19 pandemic.				

7 MACROECONOMIC RISKS

Our financial performance and resilience are influenced by external macroeconomic factors.

A significant rise in inflation and related increases in interest rates may also adversely affect the company's financial performance. The actual increase in our input costs may be greater than the increase in our wholesale revenue which is indexed on November CPIH eroding profitability.

Rising interest rates could lead to poorly performing equity markets that may result in a deficit of the pension schemes we operate.

Movement in interest rates can also result in an increase in our cost of debt.

The UK and global economy have been significantly affected by the Covid-19 pandemic. This resulted in (i) increased levels of bad debt for both domestic and business customers and additional costs of supporting vulnerable domestic customers (e.g. significant increase in our social tariff take up during Covid-19), (ii) reduced liquidity and additional borrowing; (iii) increased ODI penalties due to external factors affecting our operations and performance, (iv) reduction in revenue from non-regulated business activities, new connections and contributions from development activities and (v) increase in contractors' costs. Inflation is increasing as the economy moves out of the downturn.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
Even with a successful vaccination campaign and progressive return to normal business activities, the economic situation in 2021/22 remains unclear and it is likely that the effect of the downturn will continue to be felt especially on bad debt and affordability. The increase in inflation will also need to be monitored. Closely related risks 2 / 11 Mitigation shown overleaf	◀▶	<i>Link to key resources & relationships:</i> Financial return Our customers and communities Our suppliers and partners <i>Impact on outcomes:</i> Shareholder value		

OUR PRINCIPAL RISKS continued

7 MACROECONOMIC RISKS continued

Mitigation

-
- We manage our interest rate risk through our mix of long term financing arrangements, including fixed, variable and index linked interest rates. See note 22 for further details.
 - Monitoring the impact of macroeconomic factors on our business and on our credit ratings including the long-term impact of Covid-19 on the UK economy.
 - Engagement with rating agencies to understand how they will interpret the position of water companies in the context of Covid-19.
 - Robust and challenging budgeting process to ensure costs are clearly identified and controlled during the financial year.
 - Effective debt collection processes and support to our most vulnerable customers with our social tariff, other financial assistance and a range of payment options.
 - Interest rates and inflation, which both have a significant impact on our finance costs, have remained low throughout the year. This together with the refinancing effected in the 2019/20 financial year has seen a fall in finance costs of £9.9 million. See note 8 for further details.
 - Effective processes for the collection of debt and steps to encourage payments through direct debits. We have maintained a good performance on collection of bad debt but keep the effectiveness of our recovery process under constant review.
 - Social tariff and other similar tariffs to assist customers who may struggle to pay. New approach to customer engagement and new initiatives on affordability and vulnerability led by a dedicated team.
 - Long-term pension strategy which we are developing in consultation with the Pension Trustees to move towards insuring / securing a buy-out of the schemes.

8 WATER QUALITY INCIDENT

Our core purpose and most essential duty is to provide a supply of safe and high quality drinking water. A water quality incident could lead to a failure to supply wholesome water with implications for public health. This would significantly harm customer trust.

We may not be able to operate certain water treatment facilities as normal if there is a significant deterioration in raw water quality, pollution by third parties or a failure of our own treatment process.

Water quality risks relate to our own water supplies and to bulk supplies of treated water we receive from other water companies.

Water quality events may lead to significant costs being incurred impacting our revenue and resulting in penalties for failing to meet relevant performance commitments.

This may also result in investigations and enforcement actions and potential prosecutions from the Drinking Water Inspectorate.

Risk Trend	Link to business model	Related strategic themes	Potential exposure
While new metrics (Compliance Risks Index and Event Risk Index) and performance commitments apply in 2020 to 2025 our underlying performance remains stable. Closely related risks 2 / 5	◀▶ <i>Link to key resources & relationships:</i> Fresh water and the environment Our assets and networks Our customers and communities <i>Impact on outcomes:</i> Reliable water supply Public trust	 	
Mitigation			
Operational management			
- World Health Organization (WHO) water safety plan approach including risk assessments and management of all aspects of the water supply chain from catchment to customers' taps. - Round the clock monitoring of our treatment works and distribution network and automated alert and shutdown systems at treatment works. - Extensive sampling of our water every day; analysed at our specialised laboratory audited and accredited by the UK's national accreditation body UKAS. - Emergency plans and procedures (including under the Security and Emergency Measures Directions) for managing incidents, provide supplies to critical facilities and deploy alternatives supplies where necessary which are regularly tested and independently audited. See other mitigations in relation to risk.			
- Active management of catchments and partnerships to reduce the discharge of chemicals by third parties. - Programme of flushing, network management and investment in our treatment works to meet our targets on taste, odour and appearance of water. - Risk-based prioritisation process for the maintenance and replacement of our assets and investment in treatment works.			
Audits and lessons learnt			
- Regular internal review of our processes and facilities and external audits by the Drinking Water Inspectorate. - Sharing of lessons learnt with other companies which we use to update and improve our own practices and procedures.			

OUR PRINCIPAL RISKS continued

9 ADVERSE POLICIES OR POLITICAL & SOCIAL ENVIRONMENT

We operate in a highly regulated environment and changes to the regulatory or legislative framework may have an adverse impact on the overall risk profile of the business, financial resilience and on our ability to fulfil our purpose in the long-term. Such changes may also reduce investors' confidence and could affect our credit ratings. There will be increasing pressure on fresh water resources and additional requirements to ensure the sustainability of water abstraction.

Successive price reviews determine our ability to carry out the investment necessary to maintain an efficient and resilient water supply system and to prepare for the impact of population growth and climate change. There is a risk that the need for necessary investment may not be fully demonstrated or recognised by Ofwat at price reviews resulting in under-investment and/or delays in implementing solutions required to meet our long-term challenges. The focus on keeping water bills low in recent price determinations could if continued result in a situation where future generations are required to pay higher bills to allow for a higher level of investment over a shorter period of time, and possibly, a situation where the investment required to face an acceleration in climate change is not sustainable for future customers.

Market reforms such as the introduction of competition for water resources, demand management and leakage services, direct procurement, and the potential introduction of competition for household retail customers in the future and the evolution of the non-household retail and new connection markets create new risks of disruption to our business model and operations. There are implementation costs and risks in establishing new methods of working and processes. They could also create new business opportunities.

We are also exposed to risks arising from the general social and political environment such as the challenges to the ownership model of water companies and the scrutiny of the water and sewerage sector as a whole. Potential nationalisation would cause disruptions to our operations and affect our ability to maintain the investment required to meet our long-term service obligations.

Wider political changes such as Brexit bring changes to our legislative environment, supply chain and the general economy to which we must adapt. With the approval of the Trade and Cooperation Agreement by the European Parliament on 1 May 2021 the risks relating to Brexit have receded.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
The political uncertainty relating to nationalisation of the water industry and Brexit has reduced but monitoring on the impact of Brexit on our supply chain continues. Risks relating to development in markets have remained stable. The risk level could be affected by future regulatory decisions. Closely related risks 5 / 1 / 10		Link to key resources & relationships: - Our assets and networks - Fresh water and the environment - Financial return - Our regulators Impact on outcomes: - Reliable water supply - Public trust - Responsible impact on the environment	  	

9 ADVERSE POLICIES OR POLITICAL & SOCIAL ENVIRONMENT continued

Mitigation

Stakeholders engagement

- Work with the industry and stakeholders to anticipate the potential effects of policy proposals and to contribute actively to ensure that risks are identified and taken into account.
- Engagement with customers and stakeholders to understand their expectations and perception of the company to align our culture, governance and strategy to the political and social environment in which we operate.
- Responding critically and constructively to consultations on proposals from Ofwat and Government.

Monitoring

- Keeping our commercial strategy and the structure of our business under review to be able to adapt to changes and to take advantage of new opportunities.
- Monitoring the impact of new trade rules under the Brexit Trade and Cooperation Agreement on our supply chain and of any restrictions on access to the labour market.
- Monitor the appeals to the Competition and Markets Authority by four companies in the sector against their final determinations and similar appeals in other sectors.
- Reviewing and anticipating the potential impact of regulatory changes on our ability to secure finance at no less favourable terms.

OUR PRINCIPAL RISKS continued

10 REGULATORY, ENVIRONMENTAL AND LEGAL COMPLIANCE

Our business operates within a specific legislative and regulatory framework and many of our activities have an impact on the environment. Our three main regulators Ofwat, the Drinking Water Inspectorate and the Environment Agency set standards and monitor our compliance. Failure to ensure compliance with environmental, regulatory and other legal requirements may lead to criminal and civil liability, regulatory enforcement actions, disruption to the business and loss of management time. We need to keep pace with changes to these obligations as failure to do so could also lead to non-compliance.

Material failure to comply with our licence obligations and other duties of a water undertaker may result in an enforcement order, a fine up to 10 per cent of appointed turnover or termination of our appointment or special administration.

We could face enforcement action if we do not demonstrate compliance with the new market arrangements and must also ensure continued compliance with competition law as the environment in which we operate evolves.

Failure to comply with our obligations would also affect the perception of South East Water by customers, regulators and other stakeholders and affect the trust they have placed in us as a provider of an essential public service.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
Controls remain effective and there is no change to the status of this risk. The transition to a new external assurance partner in 2021 provides an opportunity to review our reporting processes.	◀▶	<i>Link to key resources & relationships:</i> Our human and intellectual capital Our people and culture Our regulators <i>Impact on outcomes:</i> Public trust Responsible impact on the environment		
Closely related risks 6 / 9 / 13				
Mitigation				
• Policies, processes and controls to ensure that we meet our duties and obligations. • Subject matter experts available to advise colleagues and inform them of changes in requirements and recommend improvements to processes. • Register of obligations as a water undertaker and monitoring of compliance including annual review of compliance performance and processes with the relevant department. • Awareness training provided through online mandatory training updated regularly for key compliance issues such as anti-bribery and data protection. • Review of processes in response to changes to relevant market arrangements, rules and guidance. • Monitoring of performance against market metrics and implementation of improvement action plan. • Annual update to the audit and risk committee on anti-bribery and controls against fraud and annual update to the board on compliance with modern slavery legislation. • Externally assured reporting processes and internal process for mitigating risks of incorrect reporting (company monitoring framework).				

11 FINANCIAL RESILIENCE

We have a significant ongoing funding requirement relating to our operational costs, capital programme and to refinance maturing debt. Maintaining the financial resilience of the business is required to ensure that we meet relevant conditions in our finance documents and our licence and are able to access financing.

We must maintain key ratios to comply with covenants in our agreements with debt providers and relevant credit rating agencies ratios. Failure to do this could lead to events of default and liquidity risks due to the trigger of restrictions on further borrowing or reduction of our credit rating that would affect liquidity.

We must also maintain an investment grade credit rating. Failure to do this would result in cash lock up under our licence restricting our ability to pay dividends or in an event of default under our finance documents. It would also impact our ability to raise funds on favourable terms.

The PR19 final determination has created significant financeability challenges due to a very low cost of capital and the risk of significant in-period ODI penalties.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
Increase in risk exposure deriving from the PR19 final determination and the impact of in-period penalties and the impact of Covid-19 on costs and revenue increased the financeability challenges in the previous year but the outlook remains stable. Closely related risks 2 / 5 / 9 / 7	◀▶	<i>Link to key resources & relationships:</i> Financial return Our regulators <i>Impact on outcomes:</i> Reliable water supply Shareholder value		
Mitigation - Continuous monitoring and regular reporting to our board on compliance with our financial covenants and on our credit rating. - Completed a refinancing of a significant part of our debt in 2019 which allowed us to reduce gearing. - Maintained our investment grade ratings of BBB/Baa2 in 2020/2021. - Maintained compliance with our financial covenants. - Regular engagement with credit rating agencies to understand their approach including to Covid-19 when assessing water companies' credit ratings. - Available borrowing facilities totalling £148 million, renewable in June 2022, allowing additional drawdowns for the prudent management of liquidity in the context of Covid-19. - Adoption of a STID proposal addressing the potential consequences of Covid-19 on compliance with our financial covenants to improve our financial resilience, in particular preserving the ability to draw down additional debt even under certain trigger event scenarios. - Monitoring markets and the impact of Covid-19 as we plan and prepare for further refinancing in 2025 and 2029. - Our sustainability Finance Framework helping secure access to long term financing. - Robust and comprehensive financeability testing for our business plan, corporate plan and annual budget and corporate plan updates, and for our long-term viability statement.				

OUR PRINCIPAL RISKS continued

12 HEALTH SAFETY AND WELLBEING

Our activities and assets present risks to the health and safety of our employees, contractors and the public. We must maintain the safety of our workforce during normal operations and when dealing with emergencies. Failure to prevent accidents could have tragic implications for individuals and their families. There are severe criminal sanctions and civil sanctions for failing to have appropriate safety measures and failure to meet health and safety standards.

Risk Trend		Link to business model	Related strategic themes	Potential exposure
There has been an increase in underlying risks to health and safety directly related to contracting Covid-19 and constraints on carrying out normal safety audit activities. However, existing controls remain strong and specific measures put in place in relation to Covid-19 have been effective as demonstrated by the low level of absences.	◀▶	<i>Link to key resources & relationships:</i> Our human and intellectual capital Our people and culture Our suppliers and partners <i>Impact on outcomes:</i> Job opportunities and development	 	

Closely related risks 2 / 3**Mitigation**

- Comprehensive processes including policies, standard operating procedures, risk assessments and toolbox talks involving our employees, partners and contractors to identify risks to employees and the public and adopt safe practices.
- Continuous actions on training and awareness to ensure that our employees and those of our contractors always adopt safe practices.
- Our Thrive 365! safety strategy designed to support the company vision and provide clear direction and a road map for continuous improvement of our health, safety and wellbeing performance.
- Our mental health strategy.
- Significant changes to the way our business operates during the Covid-19 pandemic and lockdown to protect our workforce and the public.
- Continuously reviewing and adapting our working practices to ensure we maintain the safety and wellbeing of our workforce as required by the evolution of the Covid-19 pandemic and in line with Government recommendations.
- Directors review health and safety performance at each board meeting and regular review at executive meeting.
- Health & Safety committee monitoring the effectiveness of health and safety practices, policies, procedures, training and communication.

13 PEOPLE AND CULTURE

Our business operates across the entire value chain within a highly regulated and technical environment. We need employees with a wide range of skills and disciplines and we rely on their technical and business knowledge. We need to attract and develop employees and manage performance and talent to achieve our business objectives.

A shortage of skills in some technical disciplines may make it more difficult to recruit and meet our requirements. We must also retain our business know-how which presents a challenge in operational areas where our workforce is more mature and business knowledge was sometimes acquired over many years in the field. We also rely on key individuals who have acquired a detailed technical and company knowledge and we must manage succession planning to avoid disruption to the business.

As the expectation of customers, stakeholders and employees change we need to promote a culture that meets those aspirations.

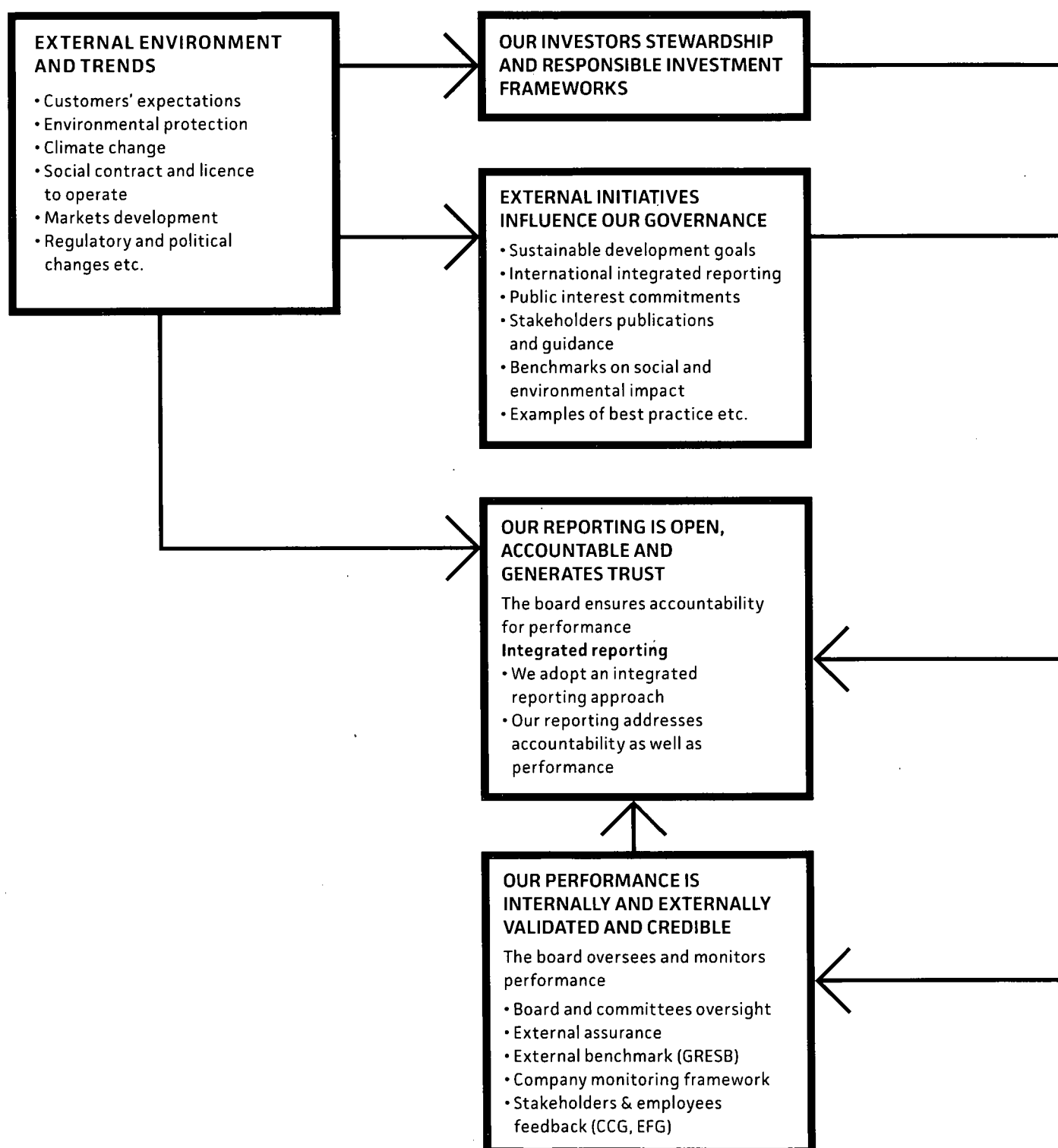
Risk Trend		Link to business model	Related strategic themes	Potential exposure
The risk status remains stable but we are aware that we need to manage the transition post lockdown and implement appropriate flexible working arrangement whilst maintaining the cohesiveness of our organisation. Closely related risks 2 / 12	◀▶	<i>Link to key resources & relationships:</i> Our human and intellectual capital Our people and culture Our customers and communities <i>Impact on outcomes:</i> Job opportunities and development Public trust		
Mitigation				
• Successful apprenticeship scheme in operations and the "Steps to Leadership" programme developing managers over four levels. • Extensively communicated our values and objectives with employees to ensure their support and their involvement in cultural changes required to deliver the next step of performance improvements. • Our people plan which sets out our strategy for the next five years including strategy on diversity, talent management, succession planning and gender pay gap. • Embedding our purpose and values into our day to day activities throughout the next five years. • Regular engagement through our Staff Council, pulse survey and bi-annual staff surveys followed by action plans shared and implemented with the support of staff. • Our Speak Up (whistleblowing) Policy allowing colleagues to raise concerns to be investigated as appropriate. • Our response to Covid-19 guided by two priorities: the need to maintain the water supply and the need to protect and support our employees. Our workforce has allowed us to adapt and to continue to provide our service and we have been consulting with them about the lessons we can learn from this and how our methods of working may evolve in the future.				

OUR BUSINESS STRATEGY

“CUSTOMER SATISFACTION RESPONSIBLY DELIVERED”

Planning for water is a long term business, our purpose makes it clear the role we have at South East Water. Our business strategy is how we fulfil our purpose, carry out our business and manage our risk.

A GOVERNANCE FRAMEWORK TO FULFIL OUR PURPOSE AND PROMOTE LONG-TERM SUCCESS



OUR CORPORATE GOVERNANCE FRAMEWORK GUIDES OUR DECISIONS AND COMMITMENTS

The board defines our purpose, strategy and values and promotes a purposeful and stakeholder inclusive culture.

OUR PURPOSE

- Embedded in our constitution, code and board structure
- Our directors' duty to balance the interests of all stakeholders

OUR CULTURE

- A culture of ethics and public service values
- A stakeholder inclusive culture

OUR PRINCIPLES & RULES OF GOVERNANCE

- Our corporate governance code and board structure
- Our code of ethics
- Our management of risks
- Our reporting and assurance

CORE REQUIREMENTS ARE INTEGRATED INTO OUR GOVERNANCE

- UK Corporate Governance Code
- BLTG principles
- Directors duties (s172)
- Conditions of our Licence
- Reporting requirements
- Best practice guidance etc.

OUR CORPORATE GOVERNANCE IS INTEGRAL TO HOW WE RUN OUR BUSINESS

The board defines the strategic direction and business model

OUR BUSINESS MODEL AND STRATEGY

The board approves policies and planning to deliver our strategy
Integrated thinking is how our board and committees, executive team, management and all our employees deliver our services and commitments to fulfil our purpose in line with our culture

Use of and impact on the IIRC* six capitals

Consistency with our purpose and between our actions

Contributing to the sustainable development goals

INTEGRATED THINKING



Impact on society, the environment and the economy

Fair balance of interests

Engaging & collaborating with stakeholders

- Our resilience actions plan
- Our vulnerability strategy and customer initiatives
- Our engagement strategy
- Our responsible business commitments
- Our plans etc.

*International integrated reporting council

OUR BUSINESS STRATEGY

OUR 2020 TO 2025 PLAN

We have put customer satisfaction, responsibly delivered as the central theme of our business plan for 2020 to 2025. The plan ensures we take account of all our other legal and financial obligations, which has meant we have a clear direction of travel; one which we believe is better signposted as a result of our innovative and holistic approach to measuring our future performance through outcomes.

To develop our 2020 to 2025 plan we consulted with more than 10,000 people with an interest in our business, from customers and employees, through to community leaders and investors, to ensure we had developed a strategy that met their expectations and where possible went further.

Their feedback helped us to develop our five-year business plan and to develop our corporate plan.



Read more online at
southeastwater.co.uk/businessplan2020

Customer satisfaction remains a core theme of our 2020 to 2025 plan. We have taken this further and developed a wide range of responsible business measures and targets. We believe our plan is the right one for our customers and society, now and in the future. We are driven by the same values of trust as our customers. We are a business made up of dedicated water people who want to make a difference – to customers, communities, the environment and society – so that everyone and everything thrives as a result of what we collectively do.

We are immensely proud of being a local water company with a passion for sharing our 'Pure know, h₂ow' – and we have used our customers' desire to know more about their water supply service to develop our 'resilient customer' concept. The priorities we have developed aim to exceed customers' expectations for us to ensure health and wellbeing through a quality, reliable water service, and improving the environment to secure a resilient service for the future.

They also include commitments to ensure we are supporting all our customers, including those who are vulnerable.

“

The plan ensures we take account of all our other legal and financial obligations, which has meant we have a clear direction of travel

THE RESULT IS A PLAN WHICH:

- remains built around customer satisfaction, but which has improved from measuring average satisfaction across seven service elements to measuring satisfaction by attitudinal segments so we meet the expectations of all our customers – whatever their needs or circumstances
- strengthens the link between satisfaction and resilience by making customers part of the solution by giving them targeted information, and as such, greater control over their water use. We have used recent supply challenges in 2018 – such as the freeze/thaw and heatwave events – to develop this further through our resilient customer concept
- has a focused innovation strategy which targets our customers' and stakeholders' priorities; and where we can make the most difference to lead the industry, not least using our toolboxes to deliver greater customer satisfaction
- has 10 new responsible business commitments to reflect the actions and behaviours that customers expect a responsible business to display; and, in conjunction with great service, have the potential to create a step-change in trust of the water sector
- challenges us to deliver performance levels well beyond anything we have delivered before and new ones too, such as our performance commitments relating to vulnerable customers, the environment and customer satisfaction
- commits to all this at a price that is lower than today (before inflation), the challenge of doing more for less should not be underestimated. We have included 38 new performance commitments in our plan

Our ambition to do more for less is what this plan is built upon and is what drives us to set a new tone of trust and transparency in the water sector.

OUR BUSINESS STRATEGY continued

WATER RESOURCES FOR THE FUTURE

Every five years we update our water resources management plan (WRMP) which looks at how we will keep taps running while striking that delicate balance between protecting the environment and keeping bills affordable.

Historically these plans looked 25 years into the future, but because the south east faces a number of unique challenges, as detailed on page 28, in our latest plan, published in August 2019 we've looked forward 60 years to 2080. By doing this we can make sure the work we do now lays the best foundations for future generations.

Over the next 60 years the population in our supply area is set to increase by 49 per cent to 3.29 million. To ensure all existing and new customers continue to receive a reliable tap water supply we need to increase the amount of water available by an extra 221 million litres a day by 2080.

Our latest plan makes the water we already have go further – by reducing leaks on our pipes and developing water efficiency programmes. Although this will help, these measures alone won't be enough to meet the predicted shortfall in water.

OUR PLANS FOR 2020 TO 2045 INCLUDE:

- **encouraging greater water efficiency amongst our customers, working with our customers to reduce per capita consumption from 148 l/h/d to 90 l/h/d by 2080, helping to save an additional 151.6 million litres of water a day**
- **halving the level of leakage from current levels by 2050, saving an additional 42.7 million litres of water a day**
- **construction of a new water treatment works by 2025 at the former Aylesford Newsprint site via a new licence trade arrangement. This will provide an additional 18.2 million litres of water a day**
- **developing and improving an existing water treatment works at Bewl Water in Kent by 2045, providing eight million litres of water a day**
- **creating a new reservoir at Broad Oak, Kent by 2033 to provide 19.6 million litres of water a day**
- **building a new reservoir adjacent to our existing Arlington Reservoir, East Sussex, by 2035 to provide 16.1 million litres of water a day**
- **developing a regional water transfer scheme from SES Water to provide nine million litres of water a day by 2042**
- **improving the levels of connectivity and resilience within our water supply network system to meet demand and manage extreme events**

By planning so far in advance we can find the most sustainable long term options to meet the demands of both our existing and our anticipated new customers. Our planning supports the 'twin track' approach to ensure that we adopt the best options to manage both customer demand for water and the development of the most sustainable sources of supply.

We asked for customers' views while we developed our plans and thank everyone who took part in the consultation process. In particular we are grateful to the members of our Environmental Scrutiny Group who challenged our approach and helped ensure we developed an acceptable, resilient and innovative plan.

Collaborative regional water resources planning is a long established and integral part of how our own water resources management plans are prepared. Since 1997 South East Water, along with the other five south east of England water companies has prepared regional plans as the Water Resources in the South East (WRSE) group. This collaboration ensures each individual company plan is integrated with regional solutions, to provide the most cost effective and resilient plans for both customers and the environment.

The latest water resource management guidelines prepared by Government seek to expand and build on the regional approach adopted by the WRSE group, by creating an additional four regional groups to cover the whole of England and Wales, supported by a national framework to help deliver consistency and co-ordination up to national level.

South East Water continues to play an active and vocal role in the work of the WRSE group and national work, to ensure our own company water resources management plan remains coherent with those plans. The regional plan will be published in 2022 and you can find out more at

 wrse.uk.engagementhq.com

25 YEAR ENVIRONMENT PLAN

We are the first water company to develop a dedicated 25 year environment plan.

Due to be published to coincide with the COP26 climate change conference in November 2021, our 25 year environment plan is being co-created with a range of stakeholders.

We know that making lasting change to the environment takes time and that no one organisation can do this alone. We need a long-term environmental strategy to provide a framework for the entire company, to protect and enhance the environmental resilience of our supply area, short and long term.

This will exceed our statutory obligations and planning cycles, such as the Water Industry National Environment Programme, water resources management plan and dry weather plan. We recognise an important part of this is making sure that we consider wider environmental impacts from our own operations. To do this, we need to do all we can to create and maintain a resilient environment.

In early June, more than 30 individuals representing different interested groups took part in two 'sprint' sessions to inform what they feel are our biggest challenges and external influences on the environment are, as well as outlining the key strategic themes which must feature in our strategy.

Industries represented included:

- environmental non-governmental organisations
- local and national government representatives (including a National Park and highways authority)
- large land owners, housing developers and industrial water users
- universities and other independent expert groups
- representatives for other groups such as farmers and growers and recreational water users

Workshops with our employees and customers will follow, in order to create a roadmap which delivers the very best outcomes for the environment as a whole.

For more information through the year and to sign up for our environment newsletter visit

 corporate.southeastwater.co.uk/25yp

OUR OBJECTIVES

We use performance commitments to measure our progress towards achieving our strategy. You can find out more on the following pages of our business performance, but also within the annual performance report (page 249). Read more online at

 performance.southeastwater.co.uk

DELIVERING OUR STRATEGY TO FULFIL OUR PURPOSE

fairly and responsibly...

**We can help to address social issues such as
affordability and vulnerability.**

It is important we find the right balance between
different interests so everyone has access to the water
services they need.

BSI accreditation
BS 18477
demonstrates
our commitment
to accessible
services

Responsible business commitment

We are developing partnership working so we can be closer to the community we serve.

- We created an affordability forum to bring experts together to support financially vulnerable customers
- More than 60 organisations attended our vulnerability stakeholder event - held online in November 2020

Our commitment to our customers

Our Priority Services Register is there so we can understand the best way to serve all our customers.

PRIORITY SERVICES REGISTER

29,210

Total household customers signed up

Our Customer Care Advisors help make sure we are offering all the services we can.

If you need financial support get in touch

BUSINESS PERFORMANCE

OPERATIONAL PERFORMANCE

The water regulator, Ofwat, has set out a group of 'common' performance measures that it wants all water companies to report against. In addition to these performance measures, we have developed an additional group of performance indicators through asking our customers what they feel we should target. While it is important to remember that no measure can ever capture everything, these metrics reflect the most important aspects of the service that we provide. If we can perform well against these targets, we will be providing a good service to all our customers, both current and future. We are always mindful that, as well as being providers of an essential service, we are also the custodians of a public asset (the water infrastructure).

These targets are referred to as 'performance commitments' (PCs).

The following table sets out what these measures are and why they are important.

PERFORMANCE MEASURES

All the measures in the first table have financial incentives attached to them (also known as Outcome Delivery Incentives or ODIs)

Measure	Purpose
Supply interruptions	We aim to provide clean, safe water to 2.2 million customers, 24 hours, 365 days of the year. This measure captures the rare occasions on which supplies are interrupted. Our objective is to minimise these interruptions.
Mains repairs	The number of repairs which we have to carry out on the network is an indicator of the general health of the network, and this measure should be understood as a measure to ensure that the health of the network is being maintained. If we keep below our target (based on number of bursts per 1,000km of main), it shows that the network is being kept in a good condition for future generations.
CRI	The CRI is a measure of water quality compliance. The perfect score is a 0, and our objective is to keep this as low as possible. It should be noted that in addition to this measure there is a very strict legal framework, which includes the potential for prosecution if water is supplied that threatens human health.
Unplanned outage	This measures the frequency with which above ground assets (mostly treatment works and pumps) are out of action. This is also an 'asset health' measure. Keeping this low indicates that these assets are being kept in good health for future generations.
PCC	This is a measure of the amount of water consumed by each person in our supply area (Per Capita Consumption). If we do a good job helping customers to consume water more efficiently we will reduce the amount consumed and do well on this measure.
Leakage	All water networks have distribution losses. We can minimise leakage by keeping the network in a good condition, by fixing leaks quickly when obvious leaks occur; and by having effective systems and processes to identify and repair the many smaller leaks that are not immediately identifiable.
C-MeX	This is a comparative measure of customer experience performance designed by Ofwat. It is based on sample surveys, where a third party specialist company contacts a sample of customers and asks them about their experience of our service.

OPERATIONAL PERFORMANCE continued

Measure	Purpose
D-MeX	This is a comparative measure of customer experience performance designed by Ofwat, which targets developer services customers. Developer services are about connecting newly built properties to our network. It is based on sample surveys, where a third party specialist company contacts housing developers who are using our connections service and asks them about their experience of our service.
AIM	The Abstraction Incentive Mechanism is a compound measure that measures how much water we extract during times of water shortage. This is designed to give us an incentive not to extract raw water from the environment in a way that might lead to low flows in rivers and streams.
Appearance of water	This is a measure of how many contacts we get from customers to tell us that there is an issue with the appearance of their water (discolouration). These incidents do not represent a threat to human health.
Taste and odour of water	This is a measure of how many contacts we get from customers to tell us that there is an issue with the taste or odour of their water. These incidents do not represent a threat to human health.
Properties at risk of low pressure	This is a measure of how many properties on our network are at risk of receiving low pressure during times of high demand. Usually such properties are at the end of the network or at the top of a hill.
Household voids	This is a measure of how many properties are empty. If a high number of properties are empty, then other customers have to pay more to compensate. This measure incentivises us to keep that number to a minimum by keeping accurate records. A small number of properties are genuinely empty.
Non-household voids	This is a measure of how many business and commercial properties are empty. If a high number of properties are empty, then other customers have to pay more to compensate. This measure incentivises us to keep that number to a minimum by keeping accurate records. There is always a proportion of commercial property that is empty, but this has increased during the Covid-19 crisis and we are suggesting to Ofwat that this measure should be adjusted to compensate.
WINEP	The Water Industry National Environment Programme is a series of projects designed to protect and enhance the natural environment. This measures whether or not we deliver those projects on time.
Engaging and working with land owners	This measure is designed to protect our raw water resources. By working with land owners we seek to prevent raw water from being contaminated with chemicals which would require costly and environmentally inefficient treatment. This is known as 'catchment management' and the incentive is based on the hectareage of land that we applied catchment management policies to.
Protecting wildlife and increasing biodiversity	This measures the hectareage of land which we proactively manage and monitor in order to produce gains in biodiversity through our conservation work.
Sites protected from flooding	This measures the number of sites that the company has protected against a one in 1,000 flood risk. Although customers will not notice any effect of this work immediately, its completion will mean that customers are receiving a much more resilient service.

BUSINESS PERFORMANCE continued**OPERATIONAL PERFORMANCE** continued

The rest of the Performance Commitments do not have ODIs attached to them. For ease of reference, they are grouped into three separate tables below.

CUSTOMER SATISFACTION MEASURES

We have seven measures of customer satisfaction. They are designed to remind us that what we really want to achieve is customer satisfaction, not just good service levels and metric performance.

If the metrics are well chosen, then they will automatically achieve customer satisfaction as they will measure the things that customers care about. However, this is not automatic, especially in a rapidly changing world in which these performance metrics are only changed once every five years. We therefore think there is value in measuring customer satisfaction directly.

Measure	Purpose
Customer satisfaction by segment (measures)	This measure is divided into six customer segments. The purpose of these different segments is to remind us that water customers are not all the same. Different people have different needs and priorities. This measure therefore identifies the satisfaction levels of six different groups based on research of our customer base: 'mindful optimists'; 'global advocates'; 'just me and mine'; 'careful neighbours'; 'busy juggler'; and 'living for today'.
Value for money	This is a measure of customers satisfaction measured via a survey.

MEASURES RELATING TO VULNERABLE CUSTOMERS

As a company which operates a natural monopoly we have an unusual public service responsibility to make sure that we take care of vulnerable, or potentially vulnerable, customers within our customer base. The following measures are designed to measure how effectively we do that:

Measure	Purpose
Satisfaction of household customers who are experiencing payment difficulties	This measure targets a specific group. It measures (via a customer survey) the satisfaction levels of customers who are finding it hard to pay their bills. This is a group of vulnerable, or potentially vulnerable people and we need to interact with them with particular care and empathy.
Satisfaction of household customers who are receiving, or applying for, non-financial support	This is another measure that is designed to make sure that we pay particular attention to a group of potentially vulnerable customers. In this case, customers who are on, or applying to be on our Priority Services Register. Customers can be on this register for a variety of reasons such as age, health, or disability. Such customers can be prioritised for additional support in certain circumstances, such as the delivery of bottled water to their homes in the case of an interruption.
Satisfaction of household customers on our vulnerability schemes during a supply interruption	This measure is another survey measured metric which specifically measures the satisfaction of customers on the Priority Services Register with the services that they receive during a supply interruption. This is designed to measure how well we protect this vulnerable group during supply interruptions.
Household customers receiving financial support	This is a measure of the number of customers that are receiving financial support in the form of bill control or bill reductions. Such reductions are offered to vulnerable customers and this measure tracks our performance in ensuring that these customers are supported.

MEASURES RELATING TO VULNERABLE CUSTOMERS continued

Measure	Purpose
Satisfaction of stakeholders in relation to assistance offered	This is a measure (based on surveys) of the satisfaction of vulnerable customers and their representatives.
Priority Services for customers in vulnerable circumstances – Reach	This is a measure of the percentage of overall households which appear on our Priority Services Register. Vulnerable customers can be hard to identify and this metric measures our effectiveness at reaching out to them.
Priority Services for customers in vulnerable circumstances – Attempted contact and actual contact	This measures the percentage of customers on our Priority Services Register that we have attempted to contact over a two year period. This is a measure of how effective our proactive contact with these customers is. The actual contact part of the metric measures how many of those customers we have actually made contact with.

OTHER PERFORMANCE MEASURES

Measure	Purpose
Gap sites	Gap sites are properties that exist, but are not included in our billing system. Such properties receive free water at the expense of other customers. This metric incentivises us to find those properties and add them to our system.
Risk of severe restrictions in a drought	This is a measure of the percentage of our customers who are exposed to the risk of severe restrictions during a drought period. Severe restrictions means discontinuity in supply, not just hosepipe restrictions. Our target is 0 per cent.
ERI (Event Risk Index)	This is a composite measure produced by the Drinking Water Inspectorate (DWI). It measures the risk to customers of water quality events and incentivises us to reduce the risk of such events.
Delivery of water industry environment programme requirements	This is a simple measure of whether we have 'met' or 'not met' all of these requirements.
Greenhouse gas emissions	This measure commits us to achieving a 68 per cent reduction in greenhouse gas emissions by 2025. We have a further commitment to achieve net zero emissions by 2030. This will reduce and then eliminate the carbon footprint of our operations.
Engaging and working with abstractors to improve catchment resilience to low flows	This metric encourages us to engage with other abstractors of water (mostly farmers) to help them find ways to reduce their water use and to thereby help avoid low flows in the environment. This specifically measures the percentage of a target list that we have engaged with. The target list is produced in conjunction with the Environment Agency.

BUSINESS PERFORMANCE continued**OTHER PERFORMANCE MEASURES** continued

Customers can also visit the website discoverwater.co.uk which gives everyone access to comparative information on the performance of water companies. We believe this is an important tool which enables customers and stakeholders, in particular our Customer Challenge Group, to compare the progress against our targets with other water companies to ensure we are striving for continuous improvement and stretching ourselves to provide the best possible service.

The following table shows all of our Performance Commitments, the targets for 2020/21 and the incentives or penalties earned. Overall, there is a net penalty of £5.8 million (total of ODIs net penalty), which will mostly be returned to customers in the form of bill reductions in the 2022/23 year.

The exception to this is the PCC penalty of £1.2 million, which will be reviewed at the next price review by Ofwat. The Covid-19 crisis has led to increased domestic consumption as people have tended to work from home rather than their offices, and therefore increased the consumption of water in their homes. Ofwat may review whether or not it is right to impose all or part of this penalty on us. We have proposed to Ofwat that the 'non-household voids' (i.e. the number of empty business properties) has also been significantly affected by Covid-19 and lockdowns, and should therefore also be deferred for consideration at PR24.

Performance Commitment	Unit	Target in 2020/21	Actual performance in 2020/21	Penalty or Reward (£m)
Leakage	% reduction	0.2	1.2	0.303
Mains repairs	Per 1,000 km of main	173.9	185.3	(0.798)
CRI	Score	0	2.26	(0.135)
Unplanned outage	%	4.23	3.09	0.000
PCC	% reduction	1.1	-5.1	(1.224)
Supply interruptions	Min : Sec	06:30	31:27	(3.088)
C-MeX	Score out of 100	N/A	80.70	TBC
D-MeX	Score out of 100	N/A	TBC	TBC
AIM	MI/d	0	-39	0.000
Appearance of water	Per 10,000 population	1.09	1.00	0.085
Taste and odour of water	Per 10,000 population	0.42	0.34	0.064
Properties at risk of low pressure	Per 10,000 connections	0.5	0.4	0.008
Household voids	%	2.1	2.33	(0.196)
Non-household voids	%	8.1	10.60	(0.838)
WINEP	Schemes	0	9	0.000
Engaging and working with land owners	Hectares	2,843	2,858	N/A
Protecting wildlife and increasing biodiversity	Hectares	1,166	1,172	N/A
Sites protected from flooding	Number of sites	0	4	N/A

Performance Commitment	Unit	Target in 2020/21	Actual performance in 2020/21	Penalty or Reward (£m)
Customer satisfaction by segment) - 'mindful optimists'	Score out of 5	4.2	4.1	N/A
Customer satisfaction by segment) - 'global advocates'	Score out of 5	4.4	4.2	N/A
Customer satisfaction by segment) - 'just me and mine'	Score out of 5	4.3	4.1	N/A
Customer satisfaction by segment) - 'careful neighbours'	Score out of 5	4.3	4.3	N/A
Customer satisfaction by segment) - 'busy juggler'	Score out of 5	4.4	4.3	N/A
Customer satisfaction by segment) - 'living for today'	Score out of 5	4.3	4.0	N/A
Value for money	Score out of 5	3.7	3.7	N/A
Satisfaction of household customers who are experiencing payment difficulties	Score out of 5	4.2	4.3	N/A
Satisfaction of household customers who are receiving, or applying for, non-financial support	Score out of 5	4.1	4.3	N/A
Satisfaction of household customers on our vulnerability schemes during a supply interruption	Score out of 5	3.7	3.7	N/A
Household customers receiving financial support	Number	47,000	42,628	N/A
Satisfaction of stakeholders in relation to assistance offered	Score out of 5	3.6	3.7	N/A
Priority Services for customers in vulnerable circumstances – Reach	%	3.2	3.3	N/A
Priority Services for customers in vulnerable circumstances – Actual Contact	%	17.5	59.2	N/A
Priority Services for customers in vulnerable circumstances – Attempted Contact	%	45.0	77	N/A
Gap sites	Number of sites	25	47	N/A
Risk of severe restrictions in a drought	%	0	0	N/A
ERI (Event Risk Index)	Score	0	67.4	N/A
Delivery of water industry environment programme requirements	Met / Not Met	Met	Met	N/A
Greenhouse gas emissions	kgCO ₂ e/Ml	152.3	192	
Engaging and working with abstractors to improve catchment resilience to low flows	%	0	0	N/A

For further information on all of our outcomes and targets please refer to our performance, people and planet report at performance.southeastwater.co.uk and the annual performance report on page 300.

GROUP STRUCTURE AND FINANCING

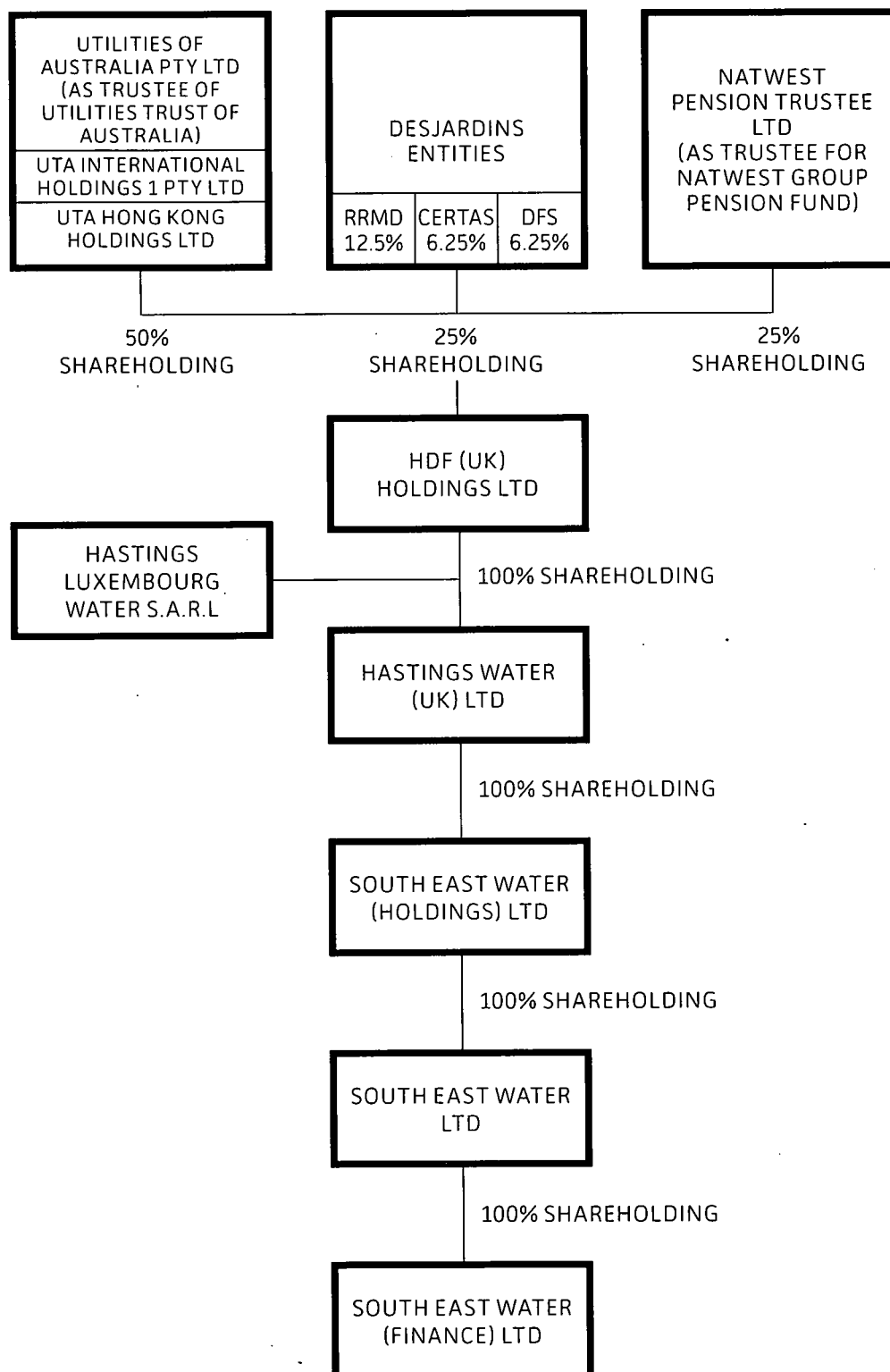
GROUP STRUCTURE

South East Water Limited is the main operating company in the group of companies headed by HDF (UK) Holdings Limited ("HDF"). There are two intermediate holding companies between South East Water and HDF: South East Water (Holdings) Limited and Hastings Water (UK) Limited, both of which, together with HDF, are registered and resident in the UK.

The ultimate owners of HDF are Utilities of Australia Pty Ltd (as Trustee of Utilities Trust of Australia), NatWest Pension Trustee Ltd as trustee for the NatWest Group Pension Fund (Main Fund Section) and three entities of the Desjardins cooperative financial group based in Quebec (Régime de Rentes du Mouvement Desjardins, Desjardins Financial Security Life Assurance Company and Certas Home and Auto Insurance Company).

Recent debt financing through South East Water Limited. Historical debt financing of South East Water has been arranged through our only subsidiary, South East Water (Finance) Limited. South East Water (Finance) Limited is a company registered in the Cayman Islands but does not gain any tax benefit from this as the company is resident for tax purposes in the UK. South East Water also has some existing directly issued debt finance which originated in Mid Kent Water Limited prior to the two companies merging. There is further debt finance in the group which is a mixture of both external and shareholder loans and this debt is issued by a separate group company, Hastings Luxembourg Water S.a.r.l.

GROUP OF COMPANIES



GROUP STRUCTURE AND FINANCING continued

SUSTAINABILITY FINANCE FRAMEWORK

South East Water has developed a Sustainability Finance Framework to finance a range of activities, not only environmental projects but also ones which will benefit society such as improving drinking water quality. The framework highlights how our activities are supporting five of the United Nations Sustainable Development Goals, including climate action and sustainable cities and communities.

In order to ensure this Sustainability Finance Framework is followed correctly, we have set out that we will comply with the ICMA Green Bond Principles (GBP), Social Bond Principles (SBP), Sustainability

Bond Guidelines (SBG) and LMA Green Loan Principles. These principles are each a set of voluntary guidelines that recommend transparency and disclosure and promote integrity in the development of the sustainable finance market by clarifying the approach for Sustainable Finance issuance.

We published a dedicated report during 2020 to demonstrate the impact this finance has made.



Find out more
corporate.southeastwater.co.uk/news-info/publications/sustainability-finance-framework

ICMA GBP /SBP CATEGORY	BRIEF DESCRIPTION OF SOUTH EAST WATER ELIGIBLE SUB-CATEGORIES LIST	EXAMPLES OF ELIGIBLE PROJECTS	UN SDG*
Sustainable water and wastewater management / Affordable basic infrastructure (Clean drinking water)	- Water demand-side management and customer-side growth - Water supply schemes - Water quality - Raw water environmental works - Capital maintenance: replacement and enhancement on a proactive basis of existing assets - Network extension: to provide a sustainable supply of clean drinking water to all new properties - Resilience	Investment and operating expenditures in, but not limited to: • Improved-metering for more frequent data to identify and address issues such as leakage • Water efficiency programmes • Water Resources Management Plan- a twin track plan to ensure a sustainable supply of water 60 years into the future, through demand reduction and new supply options • Restoring sustainable abstractions • New infrastructure to replace unsustainable resources • New infrastructure to replace ageing water mains • Groundwater and surface water catchment management • Water treatment works refurbishment that improve efficiency (water/energy/chemical) • Connections of water supply from network to new property • Flood defences at treatment works, boreholes and pumping stations to ensure resilience and maintain a clean water supply at times of flood	
Terrestrial and aquatic biodiversity conservation	- Protecting wildlife and increasing biodiversity	Investment and operating expenditures in, but not limited to: • Invasive Non-Native Species (INNS) projects included in Water Industry National Environment Programme (WINEP) • Delivery of biodiversity enhancements on water company landholdings • Management of company owned Sites of Special Scientific Interest (SSSIs)	

*United Nations Sustainable Developments Goals

FINANCIAL PERFORMANCE

The year has been the first year of a new Asset Management Period (AMP). The year has also been played out against a background of the Covid-19 pandemic and, for most of the year, in some degree of lockdown. The price determination for the new AMP and the pandemic have both provided new financial challenges for the group and lockdown has prompted many changes in the way the group operates. Despite these challenges and the forced operational changes, the financial performance in the year has been good and we have delivered on our key financial metrics.

During the year we have responded to the technical and logistical requirements of having the majority of staff working from home for a year while continuing with our strong service commitment to our customers, strengthening our network to improve resilience and investing further in developing our responsible business practices. The impact of Covid-19 has also changed the way in which our customers work, which has had an impact on the demand for water, increasing domestic demand and reducing the water usage of non-household customers in our supply area. There have also been additional costs incurred as a result of the pandemic which are described below.

There are a range of financial performance indicators that we use to monitor our business. These are linked to the key strategic financial requirements of our instrument of appointment and to those of our investors which underpin our capital structure and the financial governance that we apply to our business. In addition, we monitor profitability, capital expenditure and cash performance.

The group financial statements are set out on pages 186 to 247. These have been prepared under International Financial Reporting Standards (IFRS) and report the results for the consolidated South East Water group, which includes the results of South East Water (Finance) Limited.

KPI	Measure	2020/21	2019/20
Credit rating	Standard & Poors	BBB	BBB
	Moody's	Baa2	Baa2
Interest cover	multiple	3.6	3.4
RCV (Regulated Capital Value)	£m	1,382.0	1,413.2
Net debt to RCV	%	78.4	74.6
Revenue	£m	248.2	243.5
Profit from operations	£m	77.5	81.3
Profit before tax	£m	37.7	33.8
Capital expenditure	£m	93.3	104.5
Cash	£m	41.6	13.0

FINANCIAL PERFORMANCE continued**REVENUE**

The revenue for the year was £248.2 million compared to the previous year of £243.5 million. Under the regulatory price control mechanism, our revenue is allowed to increase each year. In 2020/21 our tariffs increase was 1.8 per cent which generated an additional £4.4 million in water revenue.

The impact of Covid-19 in the year saw a change in demand patterns resulting in household usage increasing by 11 per cent and a reduction in non-household usage of 26 per cent. The total consumption increased by 4 per cent over and above the previous year and improved water revenue by £8.4 million. This appears to be primarily due to the reduction of commuter travel by customers living in our catchment area but normally working in other areas, increased water consumption for families affected by the furlough scheme and the exceptional summer weather in 2020.

Factors offsetting the above turnover increases included additional social tariff allowances given to customers of £2.7 million as a result of more households facing economic hardship due to the Covid-19 restrictions and lower developer activity that included a full shutdown during the first lockdown period which amounted to a reduction in revenue of £5.4 million.

Other income has shown a small reduction of £0.8 million due to the change in commission rates for the Southern Water One Bill contract (£0.6 million) and lower laboratory income as a result of the Covid-19 restrictions (£0.2 million).

As the south east of England is classed as an area of water stress, one of our strategic objectives is to improve water efficiency by increasing the number of customers on metered supply. This is part of our longer term strategy to monitor and improve water efficiency. Approximately 92 per cent of our water revenue is from measured supply in the year. This has increased from 90 per cent in the previous year.

OPERATING EXPENDITURE

Our operating costs for the year, including charges for doubtful debts, have increased from £174.3 million to £182.1 million, an increase in costs of £7.8 million. The most significant impacts on costs in the year were additional expenditure on contractors which increased by £2.5 million, including £1.5 million as a direct result of Covid-19, and energy costs, which increased by £1.5 million due to price increases, the impact of Covid-19 on fixed third party charges and higher usage due to increased water demand. Depreciation and other asset related costs increased by £4.9 million as new assets were introduced and disposals of old assets were made during the year. The increased asset related costs also included £2.3 million for the impairment of the Aylesford reservoir following the sinkhole incident that occurred during the year. Insurance costs increased by £0.7 million and bulk supplies of water from other water companies increased by £0.6 million, reflecting the higher demand during the year.

Offsetting the increases in costs are savings in staff costs due to a credit of £7.8 million in respect of past service costs on one of the group's defined benefit pension schemes, which is a result of the change from RPI to CPI in measuring the liabilities of the scheme. This change has taken place in the Mid Kent Group Pension Scheme and was agreed with the trustees following a review of the pension scheme rules. This has been offset by increases in salary costs of £3.7 million.

Also, the charge for bad debts in the year was £3.8 million compared to £4.2 million in the prior year. The provision this year is based on our cash collection history for the past three years. This is a change from the prior year, where four years history was used. This change places greater emphasis on our cash collection history over the last year to reflect the circumstances resulting from Covid-19. In view of this change, no specific additional provision for Covid-19 has been made in the year (2020: £0.7 million).

PROFIT FROM OPERATIONS

Profit from operations has decreased from £81.3 million to £77.5 million, a reduction of £3.8 million.

FINANCE COSTS

We hold a number of listed bonds and indexed linked loans. The maturity dates of the loans range from 2022 to 2042 and further details with respect to these loans are set out in note 19 to the accounts.

The associated finance cost of these loans is £43.0 million in the year compared with £52.9 million in the prior year. The reduction in costs is largely due to the lower finance costs of the new loans replacing the bonds that matured in September 2019 and lower indexation charges in the year on the remaining index linked loans due to the very low inflation rate over most of the financial year.

Offsetting the loan costs is interest receivable of £3.1 million (2020: £5.3 million) mainly from South East Water Limited's parent, South East Water (Holdings) Limited on its loan from the group which was repaid in December 2020.

PROFIT BEFORE TAX

Profit before tax for the year was £37.7 million compared to £33.8 million in the previous year. This increase in profit reflects the operating performance and reduction in net finance costs described above.

PROFIT AFTER TAX

Profit after tax for the year has increased from £16.9 million to £31.3 million as a result of a significantly lower tax charge this year. Our tax charge comprises:

- current tax of £2.6 million (2019: £1.9 million).
The increase in current tax is due to an increase in taxable profit after allowing for appropriate tax adjustments
- deferred tax of £3.7 million (2019: £15.0 million).
The deferred tax in the prior year includes the effect of the rate of corporation tax changing from 17 per cent to 19 per cent

Further details on the current and deferred tax calculations are set out in note 9 to the accounts.

RESTRUCTURING

South East Water was repaid an inter-company loan by its parent company to simplify the presentation of its accounts and allow for greater clarity of financial reporting, in particular around actual dividends paid.

As part of South East Water's securitisation in 2004, a new inter-company loan was put in place between South East Water (Holdings) Limited (SEWH) and South East Water. South East Water has paid dividends each year, not available for onward distribution to shareholders, which flowed up to SEWH to enable SEWH to immediately pay interest on the loan back to South East Water. In December 2020 South East Water paid a one-off special restructuring dividend of £136 million, which flowed up to SEWH, and SEWH used the proceeds to immediately repay the inter-company loan. There was no net cash impact for either of the companies involved, as all cash was immediately returned to South East Water. In future, the presentation in the accounts of dividends paid will therefore be more straightforward.

TREASURY

Our treasury policy seeks to ensure that sufficient funding is available to meet foreseeable requirements and maintain appropriate headroom for contingencies. We manage the financial risks of the business through a series of hedging policies and ensure that our short and long term facilities are appropriate to the strategic objectives of the business. Our policy considers inflation risk, interest rate risk, currency risk and investment criteria. The policy is underpinned by the obligations of our securitisation structure. Our assessment of the associated risks are set out in note 22 and details of our long-term loans are set out in note 19.

During the year, drawdowns totalling £50 million were made on our revolving credit facility, bringing the total outstanding to £80 million (2020: £30 million). Drawdowns of £10 million were planned as a result of our forecasting processes and a further drawdown of £40 million was made to safeguard against any potential liquidity risk as a result of Covid-19. The £40 million was unspent at the balance sheet date.

FINANCIAL PERFORMANCE continued

Our current revolving credit facility expires in June 2022. Discussions are currently being held to replace this facility with a new facility with an increased limit of £125 million. The new facility has been credit approved. This is expected to be completed in 2021.

The interest rate benchmark LIBOR will lose representativeness at the end of 2021. The group's floating rate debt will instead be benchmarked to the Sterling Overnight Index Average (SONIA) administered by the Bank of England.

The group has commenced transitioning its floating rate debt. In June 2021 South East Water (Finance) Limited refinanced its liquidity facilities using SONIA as its reference rate.

The group is in dialogue with its lenders to agree amendments to the fall back provisions to move from GBP LIBOR to SONIA on its other floating rate facilities, which comprise the revolving credit facility and the £120 million floating rate loan.

PENSIONS

The company pays contributions to the South East Water and Mid Kent Water defined benefit schemes which both closed on 31 March 2015 to future accrual. During the year £4 million was paid to the South East Water scheme and £1.4 million was paid to the Mid Kent Water scheme.

These contributions are broadly in line with the prior year. Further details on these schemes are set out in note 24 to the accounts. In addition the company operates and funds a stakeholder pension scheme which is a defined contribution scheme. During the year near 1,000 employees contributed to the scheme and the company made payments of £2.5 million by way of employer contributions to this scheme (2020: £2.4 million).

CASH FLOW

We use a combination of funding and working capital to finance the extensive capital programme and to fund the ongoing operations of the business. During the year the net operating cash generated was £119.9 million (2020: £134.4 million). Payments in respect of capital expenditure in the year totalled £94.6 million compared to £98.2 million in the prior year. Net payments in respect of interest and other finance costs were £33.7 million in the year. This is lower than the previous year's net payment of £37.2 million due to a full year's interest being paid on the maturing bonds in September 2019 together with six months interest on the new replacement loans.

The group statement of cash flows on page 192 shows an increased cash balance, from £13.0 million at the beginning of the financial year to £41.6 million at the end of the year.

DIVIDEND

We pay dividends to our shareholders in accordance with our dividend policy, and the principle that the dividends do not impair our ability to finance our business and that dividends are expected to reward efficiency and the management of economic risk.

Our dividend policy is that dividends should provide a suitable return to shareholders for their investment whilst ensuring that the company is able to finance its functions and meet its obligations as a water undertaker without impairing its long-term financial resilience. When assessing the appropriate level of dividend, considerations will include the company's actual and forecast level of gearing, the need to maintain its credit rating, the allowed cost of capital, any outperformance achieved or forecast and the level of any equity injections received.

Dividends are considered in the context of the overall performance and financial resilience of the company, which also depends on our performance under outcome delivery incentives and any reward or penalty. Dividends are also considered by reference to forecast financial and operational performance to ensure that they would not compromise the future performance of the company.

The overall level of ordinary appointed dividend paid compared with the level of dividend deemed reasonable in Ofwat's assessment of the allowed return on equity is also considered.

Dividends in the year totalled £147 million. This included a special restructuring dividend of £136 million and ordinary dividends totalling £11 million which were paid in equal quarterly instalments.

South East Water (Holdings) Limited used part of the £11 million dividends paid to it to pay interest to the company under the loan referred to above, until it was repaid on 15 December 2020, resulting in a net ordinary dividends of £8.8 million.

The dividend yield, excluding the special restructuring dividend, in the financial year ended 31 March 2021 is 2.1 per cent, but after deducting non-appointed contribution and intra-group interest, the dividend yield in respect of the appointed business is 1.5 per cent, which is well below the nominal 4 per cent dividend yield that we have committed to not exceed in our dividend policy.

CREDIT RATING

Under our instrument of appointment, we are required to maintain an investment grade rating, and we are currently rated BBB with Standard and Poor's and Baa2 with Moody's. Our financial performance targets support these ratings and we review our actual and forecast indicators regularly to ensure that we are on track to maintain compliance. Equally important are the requirements of the securitisation which underlies the capital structure of the business. The maintenance of the financial covenants set out under our loan documentation is essential for the continued support of our investors.

We expect our current credit rating of Baa2 from Moody's and BBB from Standard and Poors to remain unchanged.

We manage our capital structure in a way that enables us to maintain our investment grade credit rating and comply with our loan covenants. We monitor interest cover ratios and the ratio of net debt to regulated capital value (RCV), ensuring covenant compliance both in the current and future reporting periods.

In March 2021 our lenders voted in favour of an amendment to our to our covenant package which improves our financial resilience. The main change was to allow South East Water to draw down further debt when certain financial covenants have been triggered. This ensures that the company has sufficient cash to pay its normal operating expenditure and invest in its assets. A change was also made to prevent too much of South East Water's debt being repaid to lenders in any two year period. This change further improves the protection our lenders receive from our covenant package.

GEARING

The company operates a securitisation structure. Our long term funding at the end of March 2021 was £1,038.7 million which represents 78.2 per cent of our regulated capital value. Our securitisation requirements are that we should maintain a level of gearing of 85 per cent or less. We monitor the gearing closely and there is sufficient headroom as at 31 March 2021.

TAXATION AND TAX POLICY

Our taxation policy is set out in the directors' report and the regulatory annual performance report. A more detailed explanation of our tax policy is available on our website. We have a significant capital programme and as such hold significant capital allowances to offset tax liabilities, coupled with losses generated elsewhere in the group. Find out more



corporate.southeastwater.co.uk/about-us/our-governance

DELIVERING OUR STRATEGY TO FULFIL OUR PURPOSE

working with others...

We can't do everything we do alone. We are committed to stakeholder inclusiveness and engagement.

We keep finding new partnerships and ways of collaborating to face future challenges together.

We work with
community
organisations
across our
region

Performance highlights

We want to ensure the health, safety and wellbeing of our colleagues, those we work with and our community.

- 92 per cent trust that South East Water is treating their health and safety as a high priority
- We provided over 100 activity packs for children to help with wellbeing while schools were closed

Our partners make a difference

680 contractor employees – work with us to help make sure your water supply runs 24 hours a day, 365 days a year.

CONTRACT EMPLOYEES

680

We want to
hear from our
stakeholders
to help us keep
improving

Working with industry
colleagues we learn
lessons from our
collective experiences

RESPONSIBLE BUSINESS

REPORT FROM THE RESPONSIBLE BUSINESS COMMITTEE

COMMITTEE MEMBERS

DIRECTOR MEMBERS

Rachel Drew	(Chair)* Non-Executive Director
Marissa Szczepaniak	Non-Executive Director*
Anne-Noëlle Le Gal	Non-Executive Director*
John Barnes	Independent Non-Executive Director
David Hinton	Executive Director

NON-DIRECTOR MEMBERS

Emma Goddard	Head of Environment
Chris Lunn	Head of Health, Safety, Quality
Jo Osborn	Head of Communications
Nicolas Truillet	Company Secretary

*Rachel Drew became Chair of the committee on 31 May 2021. Anne-Noëlle Le Gal replaced Marissa Szczepaniak on 18 June 2021

The responsible business committee assists the board in defining its strategy relating to environmental, social and governance (ESG) matters and in reviewing the practices and initiatives of the company relating to ESG matters ensuring they remain effective and up to date. We also oversee the execution of our ESG strategy and initiatives and monitor performance against the responsible business commitments in our business plan. We help ensure that the board maintains a primary focus on customer engagement, our communities and the environment.

Over the last 12 months:

- We reviewed the steps taken by the company to support communities during the Covid-19 pandemic beyond the provision of water, taking account of the feedback received from stakeholders, the CCG and our staff. This included food deliveries in cooperation with Kent Housing using company vans, educational videos for schools focused on the water cycle, financial contribution to a Community Foundation with other utilities, payroll giving and other staff led initiatives.
- We monitored progress against our responsible business commitments and considered how to improve the monitoring of performance and reporting on our responsible business and ESG performance including relevant metrics that may be developed and how our reporting should evolve to meet stakeholders' expectations.
- We considered the prioritisation of the work on the responsible business commitments and identified four priority areas: renewable energy, natural capital, partnerships and community projects and the schools programme.
- We considered horizon scanning to allow us to ensure our commitments and ESG initiatives remain appropriate and up to date (for example to take account of changing public opinions and customers views on key issues companies should address).
- We considered a report on ESG and responsible business risks and discussed how to better identify them and improve their visibility in our risk register including risks relating to environmental and long term issues such as climate change.
- We reviewed our GRESB submission in 2020 which obtained a score of 90 and the top position in our peer group and the preparation of our submission in 2021.
- We considered the development of the company's environmental resilience policy.
- We reviewed our vulnerability strategy including key actions on affordability (payment holiday and social tariff), accessibility and support (new team and new partnerships, extended vulnerability criteria and increase in registration on our priority service register), new partnership community projects on water use and vulnerability and improved tools to facilitate access to our services.
- We considered the TCFD recommendations and the approach for developing the company's reporting in accordance with them ensuring consistency with our long term planning (WRMP and dry weather plan) and our new adaptation report to be published by December 2021.



We monitored progress against our responsible business commitments and considered how to improve

- We considered proposed partnerships with local environmental groups to contribute to the water industry public interest commitment to plant 11 million trees by 2030, focusing on planting native species in the right environment and locations for the long term. We put emphasis on maximising ecosystem benefits (such as impact on water quality, biodiversity and resistance to diseases), community benefits and prioritising the management of ancient woodland, company land and the replacement of trees removed due to our works.
- We considered our sustainable bond report prepared under the company's sustainable finance framework focusing on how the funds had been spent and the relevant outcomes delivered as well as the internal and external assurance process.
- We reviewed a presentation on the development of the company's approach to natural accounting to integrate considerations of natural capital in business decisions and in particular in capital investment decisions to ensure the most sustainable solutions were adopted. We also considered possible approaches for measuring and reporting on social return on investment.
- We reviewed the mapping of the company's responsible business commitments against the UN sustainable development goals and considered further benefits of SDG mapping across responsible business commitments, ODI's and the water industry public interest commitments.
- We considered a deep dive on the responsible business commitment to play an active role regionally in relation to the impact of housing growth on water. This was made to address concerns about the rate and sustainability of housing development and the impact on communities and water supply. We considered the range of actions already taken and the plan of action for AMP7 including further engagement with stakeholders, improving the visibility of the steps we take and raising issues of local resilience including in the WRMP process.
- We considered Ofwat's discussion paper on public value in the water sector and the response from the company.

RACHEL DREW

CHAIR

15 JULY 2021

ENGAGEMENT TO DELIVER OUR PURPOSE FOR THE BENEFIT OF ALL

SECTION 172(1) STATEMENT

INTRODUCTION

The board's main responsibility is to set the company's strategy and monitor its delivery in alignment with the company's purpose. The two main aspects of our core purpose are to provide today's public water service and to create tomorrow's water supply solutions. Our purpose ultimately is to help society and the environment to thrive. In this context most decisions taken by the board need to balance the long term and short term interests of the company, its customers, employees, the environment and maintaining key relationships with other stakeholders and partners, as well as current and future regulatory requirements. Most decisions of the board at a strategic level require balancing all these considerations and we see the long term success of the company as achieving a fair balance.

There are numerous examples throughout this strategic report of how the board has regard to each of the matters in section 172(1) of the Companies Act 2006. This is achieved within a general decision

framework combining governance, internal systems of control and risk management, and engagement with stakeholders.

This is also done in respect of each decision the board considers. We provide a summary of the activities of the board in 2020/21 on page 127.

Our decision framework is designed to ensure we consider all the matters in section 172(1) of the Companies Act 2006.

This S172(1) statement covers:

Stakeholder engagement – we explain how the company and the board have engaged with key stakeholders; and

Key decisions – we explain how the board has reached key decisions, how they considered the company purpose, and the likely impact of those decisions, including how it has taken account of the company's stakeholders in doing so.

Relevant aspect of our decision framework		Read more
Our corporate governance framework, corporate governance code, and culture (purpose and values) and board practices	- A corporate governance framework focused on engagement, stakeholder inclusiveness, integrated thinking (i.e. balancing all relevant considerations in our decision making including those in section 172(1) CA06) - A purpose and values focused on delivery to customers, planning for the future, protecting the environment and contributing to society - A corporate governance structure that ensures that all aspects of the business receive the appropriate scrutiny including matters in section 172(1) CA06	Our corporate governance framework on page 56. Board leadership and company purpose on page 119. Long term sustainable success on page 124. How our board, committees and executive team operate on page 125.
Our vision and strategy	A vision and strategy focused on our customers, our people and the protection of the environment	Our vision and strategy on page 20.
Our long term planning	Long term water resources planning is a second key core function to ensure we can meet future demand for water and also encourage our customers to save water	Water resources for the future on page 60.
Stakeholders' participation	- Engagement which ensures that stakeholders are directly involved in our decision process: including our Customer Challenge Group, our Environmental Scrutiny Group and partnerships for the delivery of our environmental programme, our employee and stakeholder engagement programme - Extensive engagement and consultation for all our key plans	Stakeholder engagement on pages 83 to 87.
Our business model and our external environment	A business model focused on value creation through responsible business, a long term focus, engagement with stakeholders and collaboration	Our business model on pages 21 to 24. Our business environment on page 28.

STAKEHOLDER ENGAGEMENT

The board appreciates the importance of effective stakeholder engagement and that stakeholders' views should be considered in its decision-making. Here we explain our key stakeholder groups and why they are important to South East Water to build the relationships that are key to value creation.

Throughout the year we have engaged with these groups as a business, but also the board directly through our board engagement programme. This engagement helps us to understand their key issues and enables us to make decisions based on their feedback.

ENGAGEMENT TO DELIVER OUR PURPOSE FOR THE BENEFIT OF ALL

SECTION 172(1) STATEMENT continued

CONSUMERS AND COMMUNITIES**WHAT ARE THE KEY ISSUES FOR THIS STAKEHOLDER GROUP**

- A safe, wholesome supply of water
- Customer service and performance
- Reliability of supply and minimising disruption during our work
- Affordability and value for money and bill stability
- Assistance in times of need
- Responsible investment and protecting the local environment
- Local employment

(see page 24)

HOW WE ENGAGE

Although 2020/21 has been a difficult year due to Covid-19 we have been able to embrace new technologies and ways of working for the business to engage with a wide community of stakeholders.

Our independent Customer Challenge Group (CCG) met nine times during the year and has provided challenge to us in a range of areas including vulnerability, engagement, leaks, customer interruptions and our responsible business commitments.

Zoe Macleod, the Chair of the CCG, met with the board in September to update on progress and recommendations for continued improvement and board members attended several CCG meetings during the year.

A two-day online conference was held with more than 60 vulnerable customer stakeholder groups represented and two non-executive directors attended the events.

We worked closely with non-household groups, attending events including developer stakeholder events, retailer workshops and drought management sprints, which were attended by diverse stakeholder groups to help develop our drought plan. Non-executive directors attended all these events to contribute and hear directly from stakeholders.

For all capital programme schemes we assess the impact on customers and communities near the work and develop appropriate engagement, including holding virtual meetings and drop-in sessions during the year to understand views and talk about our work.

South East Water issued customer surveys and held workshops during the year, with satisfaction surveys carried out throughout the year with 39 per cent of customers surveyed.

WHAT ACTIONS SOUTH EAST WATER TOOK AS A RESULT OF FEEDBACK

Developed stakeholder engagement strategy and implementing stakeholder mapping approach across the organisation for key engagement activities.

Agreed 17 point action plan following summer demand experiences.

Refreshed the drought plan to become a "dry weather plan" and created customer friendly magazine versions to accompany the main plan.

Introduced a number of changes to the communication plan to increase channels and ways to collaborate to get water saving messages across.

Introduced new stakeholder contact email to give community stakeholders an easier route into the business.

OUR PEOPLE

WHAT ARE THE KEY ISSUES FOR THIS STAKEHOLDER GROUP

- Purposeful jobs that make a difference
- Health, safety and wellbeing
- Diverse and inclusive workplace
- Opportunities to reach full potential
- Open and honest environment
- Fair pay and reward
- Flexible working and work life balance

(see page 24)

HOW WE ENGAGE

Board engagement with our employees is focused through the Staff Council with a non-executive director appointed as the main point of contact.

A board engagement programme was developed this year to engage with different parts of the business and different levels of management.

CEO, David Hinton, delivered monthly virtual presentations with Q&A sessions for employees.

Our employee intranet, called Gurgle, promotes all news articles and key events. Managers and employees regularly blog via this platform about important issues and anyone can comment freely on all articles.

Managers are provided with a monthly Manager toolkit, health and safety briefings and core brief slides to encourage dialogue.

WHAT ACTIONS SOUTH EAST WATER TOOK AS A RESULT OF FEEDBACK

Diversity and inclusion included as a pillar of the new people plan

Developed agile working group to plan for new ways of working to continue post-pandemic

Improved the wellbeing area on Gurgle, highlighting where to go for support

Provided exposure to senior leaders through regular Q&A sessions

Set up a WhatsApp broadcast to communicate key messages to staff especially those in the field

Blogs and social media promoted to raise the profile of the work our operations teams carry out

Training for managers to connect with teams remotely

Reviewing induction process for new starters

ENGAGEMENT TO DELIVER OUR PURPOSE FOR THE BENEFIT OF ALL

SECTION 172(1) STATEMENT continued

OUR REGULATORS**WHAT ARE THE KEY ISSUES FOR THIS STAKEHOLDER GROUP**

- Outcomes for customers, the environment and long-term resilience
- Performance against regulatory targets
- Trust and transparency
- Governance and compliance
- Environmental impact

(see page 24)

HOW WE ENGAGE

Our Regulation Directorate manages engagement with our regulators to ensure we understand key issues, talk about our response to these and collaborate on finding solutions. Specific meetings with the board were not held this year due to Covid-19, but the company held various meetings throughout the year with key regulators many of whom are part of both our Customer Challenge Group and our Environmental Scrutiny Group.

During the year we responded to 35 regulatory consultations, topics included:

- Public value
- Covid-19 and the business retail market
- Innovation funding and competition
- PR24 and beyond
- Sustainable use of pesticides

Ofwat held a non-executive directors' event which was attended by our non-executive directors that discussed PR19 and looking ahead to PR24, together with public value and carbon.

We developed a weekly stakeholder report for the early stages of the pandemic to keep all updated on our progress and offer feedback on our actions. This was increased to daily during the August heatwave incident. The report has been well received and so has continued as a monthly report.

The Regulations and Strategy Director provides updates on regulatory engagement to the board, including in particular this year:

- Preparations for WRMP24 and dry weather plan (drought plan)
- Progress with development of the regional water resources plan by WRSE
- Price review and PR24 – including the outcome of the determinations by the Competition and Markets Authority
- Engagement with key regulators, such as regular meetings and collaborative projects

WHAT ACTIONS SOUTH EAST WATER TOOK AS A RESULT OF FEEDBACK

In response to Ofwat expectations set out at PR19 we have adopted a new dividend policy and extended our reporting on dividends. We reviewed our executive bonus scheme to address Ofwat's expectations and have expanded and improved the transparency of our reporting on executive remuneration

We have continued to provide regulators with a monthly update on our activities to protect customers and employees during the pandemic.

We have developed our drought plan and ensured it meets the Environment Agency guidelines, including moving technical details into the WRMP and building a tactical operational plan and creating clear customer and stakeholder friendly versions that we are now consulting on during summer 2021.

We decided to develop a 25 year environment plan to align with Government ambitions. This is being co-created with a diverse range of stakeholders and we plan to publish a draft in 2021 for consultation.

OUR SUPPLIERS AND PARTNERS

WHAT ARE THE KEY ISSUES FOR THIS STAKEHOLDER GROUP

- Fair engagement and payment terms
- Collaboration
- Responsible supply chain

(see page 24)

HOW WE ENGAGE

During the year the focus for suppliers and partners has been on managing impacts of the pandemic and procurement changes associated with Brexit. Regular updates were provided via both the CFO and Operations Director on our key relationships and how we were ensuring both our vital supply chain and the businesses that support this were being protected. Key contracts were presented to the board including a new five year engineering partnership with Atkins and a new delivery partnership with Clancy.

Regular meetings with the CEO and key suppliers are held throughout the year and our usual programme of site visits will resume once restrictions allow.

The Operations Director attended regular industry-led incident meetings throughout the year which specifically included discussion with key suppliers including chemical companies and updated the board following these sessions.

WHAT ACTIONS SOUTH EAST WATER TOOK AS A RESULT OF FEEDBACK

We involved our key contractors in the planning of our new Covid-19 safe methods of working and in the ongoing crisis management throughout the year. We used feedback from them on resolving their own operational issues to help inform our own operational decisions.

Where appropriate we ensured we had sufficient stock for strategic items in place and also managed this through industry-wide collaboration to ensure there was no risk of any company stock-piling and causing knock-on impacts.

We engaged with the local Kent Resilience Forum to ensure we were supporting them and the local community during any issues caused by Brexit or the pandemic on key transport routes for the supply chain through the county from Dover. This included providing emergency bottled water when there were delays for lorry drivers.

Working with our supply chain, requests to reduce payment terms were reviewed on a case by case basis by the CFO and shorter more favourable terms have been put in place to assist suppliers during this difficult time.

We worked with our new contractors to ensure a smooth transition with handover and training in place as we moved to new arrangements through the year.

ENGAGEMENT TO DELIVER OUR PURPOSE FOR THE BENEFIT OF ALL**SECTION 172(1) STATEMENT** continued**KEY DECISIONS**

Consideration of the matters in section 172(1) also determines the regular activities of the board such as the monitoring of performance against our commitments to ensure that we deliver the targeted outcomes for customers, the environment and the investment in the infrastructure needed to support our communities.

We provide examples of how the board has had regard to relevant matters in respect of key decisions made this year below.

COVID AND “NEW NORMAL”

At the earliest stage of the pandemic the board made the decision to ensure, while maintaining our clearly vital role, that the protection of staff and the public were prioritised. It was agreed that all who could work from home should. Cleaning regimes were changed and hand sanitiser and face masks were procured. Meetings in person were stopped and alternatives were sought wherever possible. The potential to move the control room to have a second facility at the company's disaster recovery location was considered. Early in the year the board advised that introducing home working pre-emptively would allow the company to test new methods of working and improve its readiness. Later, agreement was given to developing a new agile working approach that should be implemented in phases. Following the summer 2020 high demand event a review was undertaken and preparations for 2021 were developed.

How stakeholders were considered

Health and safety of employees and the public were placed at the centre of decision making.

DWI was engaged with to agree appropriate levels of customer water sampling to maintain safe water, while also minimising contact.

Risk to retailers in the non-household market meant the industry working together to support.

Engagement with supply chain to ensure support, where possible, to minimise delays in procuring goods.

Customer and stakeholder surveys following summer demand event to learn lessons and build plans for 2021.

Employee surveys were introduced every few months to help check support for our actions and to help understand areas to focus further attention.

Outcomes and expected long term impacts

- Maintained a 1.75 per cent sickness absence rate throughout the year
- Covid-19 related absence was kept low throughout the year
- Our action as an industry to support retailers and our supply chain reduces risk, although issues of bad debt and potential ongoing economic impact following the pandemic continue to be a risk in the medium term
- Operational and communications plans for summer 2021 readiness prepared
- The business has been able to move to a new way of working and adapted quickly. Employee support will lead to long-term commitment to the organisation, but also help attract new talent

CORPORATE GOVERNANCE AND ARTICLES OF ASSOCIATION

The board adopted a revised corporate governance framework and the company purpose in 2020. It also considered how to ensure that the company and the board would work to fulfil the company purpose.

How stakeholders were considered

The board considered the contributions and insight of the British Academy, the Purposeful Company Taskforce, Sustainability First and Ofwat which promoted the ideas that companies and especially utilities should be led by purpose and embed it into their articles of associations. They also put emphasis on the fact that doing this required judgements about balancing the interests of different stakeholders. Directors would need to act in a way they consider most likely to fulfil the purpose, and have regard to the consequences of any decision on the interests of shareholders and other stakeholders. The directors also considered the concepts underpinning the King Code of South Africa and the B Corporations initiative.

Outcomes and expected long term impacts

Embedding the purpose of the company in the articles of association would mean that the primary duty of the directors would be to fulfil the purpose both for the benefit of members and to have a positive impact on society and the environment.

This would mean removing the primacy of the shareholders' interest seen in section 172 of the Companies Act 2006 so that directors would not be required to regard the benefit of shareholders as more important than other interests but would need to strike an appropriate balance.

The directors considered the trade-off and change in the relative balance of interests that would result from embedding the company's purpose and revising the duties of directors and in particular the potential impact this could have on shareholders. They concluded that despite the removal of the primacy of the benefit of shareholders, embedding the purpose of the company into its articles of association would be in the long term interest of the company and therefore its members. The new articles of association of the company were adopted by shareholders on 4 November 2020.

DROUGHT PLAN/WRMP/WRSE

The board has been involved throughout the year in the preparation and approval of the draft drought plan (that we have renamed dry weather plan). The year has also been one of ensuring all board members understand the new approach for WRMP24 and the changes in process from WRMP19. A full assurance process was reviewed and agreed to give confidence in the decisions being made.

The draft dry weather plan was approved following close review, particularly with independent non-executive directors, and a board engagement programme for the ongoing development of the WRMP24 was agreed.

How stakeholders were considered

There is a new regional process with Water Resources in the South East (WRSE) and nationally with Ofwat RAPID group. Many regular stakeholder meetings and events were held during the year with and through the WRSE to ensure a wide range of water users across the south east of England contribute to our plans.

Regular meetings and discussions with key regulators to discuss draft drought plans, in particular the Environment Agency and Natural England.

We developed our draft dry weather plan through consultation with stakeholders, including a two-day sprint event with more than 30 different organisations involved. Non-executive directors attended these events to hear first-hand feedback.

Outcomes and expected long-term impacts

- The draft dry weather plan was submitted to Defra in March 2021 and will be consulted on during summer 2021
- Assurance process agreed to ensure good governance of our water resource planning
- Board engagement programme developed to ensure full oversight of the ongoing WRMP24 and regional plan development
- Stakeholder engagement should lead to a supported plan, one that meets the right objectives for the future and understands the challenges of the region to ensure we can secure water resources into the long term

ENERGY, CARBON AND CLIMATE RELATED REPORTING

We measure and report our emissions under scope 1, 2 or 3 using the methodology described below and we integrate climate change risks into our long-term plans and business plans.

We provide below mandatory reporting on our emissions as required under Part 7A, Schedule 7 Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 as well as voluntary emission reporting and information on our strategy to manage climate change risks and reduce our emissions and impact on the environment.

STREAMLINED ENERGY AND CARBON REPORTING (SECR)

Greenhouse gas (GHG) emissions	2019/20	2020/21	Unit
1 Annual quantity of GHG emissions for the purposes of transport No gas is used for the purpose of transport. The consumption of fuel for the purpose of transport falls into specific categories: fleet vehicles, company cars.	1,785	1,610	tCO ₂ e
2 Annual quantity of GHG emissions resulting from the purchase of electricity for own use (including for the purpose of transport) Electricity was not used for the purpose of transport in the reporting year. The electricity usage is divided into three categories: pumping, treatment and administration.	36,255	34,200	tCO ₂ e
3 Aggregate equivalent kWh for emissions under 1 and 2 above	149,143,179	146,818,118	kWh
4 GHG emission intensity metric Operational GHG emissions per mega litre of treated water based on the emissions set out under 1 and 2 above.	198	180	kgCO ₂ e /Ml

Further details on the methodology and assurance process for the data used for our streamlined energy and carbon reporting (SECR) reporting and voluntary reporting on scope 1, 2 and 3 emissions and on the principal measures taken in 2020/21 for increasing the company's energy efficiency are set out below.

SCOPE 1, 2 AND 3 ENERGY AND CARBON REPORTING

Using the methodology described above we measure and report on all our scope 1, 2 and 3 emissions annually and a summary is provided below.

Scope 1 (direct) emissions are emissions from activities owned or controlled by the company that release emissions into the atmosphere.

Scope 2 (energy indirect) emissions are emissions associated with our consumption of purchased electricity, heat, steam and cooling.

Scope 3 (other indirect) emissions are emissions that are a consequence of our actions and that occur at sources that we do not own or control, and that are not classed as scope 2 emissions (for example, emissions from business travel by means not owned or controlled by us or emissions associated with our supply chain).

CO₂e - Carbon dioxide equivalent or CO₂e means the number of metric tons of CO₂ emissions with the same global warming potential as one metric ton of another greenhouse gas

	2019/20	2020/21	Unit
Scope 1			
1 Direct emissions* from burning of fossil fuels (including natural gas CHP** generated onsite)	484	508	tCO ₂ e
2 Process and fugitive emissions***	1,106	1,250	tCO ₂ e
3 Transport: Company owned or leased vehicles	1,785	1,610	tCO ₂ e
Scope 2			
4 Total grid electricity used by company (including CHP** electricity purchased)	36,255	34,200	tCO ₂ e
Scope 3			
5 Business travel on public transport and private vehicles used for company business	41	40	tCO ₂ e
6 Outsourced activities (if not included in scope 1 or 2) Energy and other	3,935	3,560	tCO ₂ e
7 Total grid electricity used by company (including CHP electricity purchased) – Transmission and Distribution†	3,078	2,940	tCO ₂ e
Gross emissions			
8 Gross operational emissions	46,684	44,108	tCO ₂ e
Intensity metric			
9 Operational GHG emissions per mega litre of treated water	209	192	kgCO ₂ e /Ml

This metric includes all scope 1, 2 and 3 emissions for energy for pumping and treatment except energy emissions relating to administration. (This metric includes emissions from diesel generators used at sites and from ozonation at sites.)

*Direct emissions from burning of fossil fuels were higher in 2020/21 than in 2019/20 due to an increase in generator use by two per cent to provide electricity to the National Grid during Triads or for our own emergency use and an increase in natural gas consumption for space heating at some of our water treatment works.

**CHP - Combined Heat and Power – a process that captures and utilises the heat that is a by-product of the electricity generation process.

***Process emissions are a consequence of physical or chemical processes (for example in our water treatment). Fugitive emissions include intentional and unintentional releases (for example refrigerant in air conditioning units).

†Electricity which is lost in the transport and distribution system used for delivering purchased electricity.

ENERGY, CARBON AND CLIMATE RELATED REPORTING continued**EXTENDING OUR REPORTING IN LINE WITH THE TCFD RECOMMENDATIONS**

We are building on our existing work in relation to energy and carbon reporting and climate adaptation to develop our strategy and reporting following the recommendations of the Task Force on Climate Related Financial Disclosures (TCFD).

Our aim is to develop a comprehensive and integrated approach to the management of climate change risks that is at the core of our long-term planning and our related disclosures.

Our focus in 2020/21 has been on identifying climate related risks specific to the business which form the basis of both our adaptation report and our future TCFD reporting.

These climate related risks and their assessment in the adaptation report will be the starting point for developing scenarios for the purpose of TCFD that will support a consistent approach for our long-term strategic planning and our future financial disclosures under TCFD.

We summarise below our current approach to climate related risks and opportunities following the four thematic areas set out in the TCFD recommendations: governance, strategy, risk management, and metrics and targets.

Governance

Our board has effective oversight of climate-related risks and opportunities. Climate-related risks are included within our corporate risk register which is regularly reviewed by the executive team and annually by the board. The corporate risk register includes details of any appropriate controls and mitigating actions.

Any relevant targets related to climate change are agreed by the board and, specifically our target to reduce carbon emissions, are included within our published performance commitments each year.

Strategy

Our core responsibilities include planning for future water resources and for events such as droughts while investing efficiently and protecting the environment. To fulfil these responsibilities we prepare strategic statutory plans and in particular our water resources management plan (WRMP) and dry weather plan. We have a statutory requirement through our WRMP to be resilient to climate change.

The impact of climate change is a central consideration in the development of these plans both to calibrate our scenarios and assumptions and to select the most appropriate solutions and investments to develop water resources, improve the resilience of our supply system and manage demand.

We are in the process of updating our next water resources management plan (WRMP24) and as part of that process we will be reviewing and adopting the relevant information from the UKCP18 projections. This work, feeding into WRMP24, will be completed within the next year and ensure our climate change impact assumptions remain up to date, and that our strategies and plans to maintain future supply demand plans are resilient and adaptable to climate change.

We also maintain a resilience action plan which helps us ensure the resilience of our assets and services, not only to face incidents and weather events but also to face the long-term change to climate patterns caused by global warming.

We have already prepared two climate change adaptation reports which provide strategic direction and context to our long-term planning activities and we will be updating our climate change adaptation report ready for publishing in advance of December 2021.

Included in our business plan for 2020 to 2025 is a target to reduce our emissions to 58 kgCO₂e/MI by 2025, including all scope 1, 2, and 3 emissions. This represents a reduction of our emissions of 80 per cent by 2025 (when compared to 2017/18).

Building on that commitment, we are publishing a net-zero roadmap in July 2021 on our website. It will outline our strategy to both secure our 2025 price review period performance commitments and our 2030 target as part of the industry public interest commitment (PIC). Our net zero commitment seeks to achieve an estimated 98 per cent reduction in our operational direct carbon emissions through direct interventions with the remaining two per cent requiring insetting (e.g. carbon sequestration on company land) and offsetting regionally and in the UK. This reduction being measured by reference to a 2018/19 operational emission baseline. Our net zero emission commitment by 2030 does not relate to emissions by our supply chain or embedded carbon but work is underway to be able to first report on embedded carbon in respect of 2022/23.

We continually review how we can minimise our carbon emissions which includes assessing potential renewable options, an in-depth energy management review, extended metering, and our capital maintenance programme replacing older assets such as pumps with newer more efficient pumps which will reduce our energy consumption and carbon emissions.

We are also exploring more advanced analytics surrounding energy, identifying sites that are inefficient based on energy trends and would therefore benefit from a revised process or improved assets.

Risk management

We have comprehensive systems of internal control and risk management and we monitor their effectiveness regularly in compliance with the principles of our corporate governance code.

Our risk management framework is closely linked to the way we monitor and measure our performance and compliance with our statutory obligations and commitments which is subject to external assurance by third parties. The adoption in our business plan of a performance commitment for the reduction of our emissions by 2025 ensures that our systems of controls and external assurance relating to our regulatory reporting will be applied equally to our emissions reporting.

Our climate change adaptation report has identified priority risks from climate change and how these impact our functions and activities across the business. We have identified mitigations and monitoring plans to adapt to climate change impacts.

We maintain a formal risk register and risk management system for the identification, evaluation and mitigation of risks. Significant risks from climate change, and their impacts on functions and activities across the business, have been incorporated into our corporate risk register and we are able to report specifically on these risks – providing additional focus and scrutiny of risks, controls and mitigating actions.

Read more on our risk management systems and principal risks on page 30.

ENERGY, CARBON AND CLIMATE RELATED REPORTING continued**Metrics and targets for the year 2020/21**

We use the UKWIR Carbon Accounting Workbook (CAW) provided for all UK water companies to give a consistent and transparent approach for accounting greenhouse gas (GHG) emissions from annual operational activities.

The CAW provides estimates of the GHGs identified in the Kyoto Protocol, which are produced as a result of the operational activities of water and wastewater companies, including water treatment and distribution, wastewater collection and treatment, and sludge management. Estimates are made following guidance published by Defra and BEIS, as well as international guidance where required.

The tool is used by UK water companies to report progress internally and prepare information for reporting performance to regulatory bodies, voluntary reporting schemes and customers. The tool is updated annually as required in line with UK publication of conversion factors used for estimating GHG emissions. The report is therefore a suitable tool to report SECR requirements.

The data is compiled from various sources across the business and placed into a carbon accounting information pack before being transcribed into the appropriate areas of the CAW. This allows the CO₂e figures for the company to be compiled which are then externally audited. This data is then used to calculate the total associated kWh for purchased energy and transport using recent year emission factors.

External assurance of the processes and data for our GHG emissions has been carried out by Ricardo Energy & Environment (REE).

In undertaking the verification exercise, REE has reviewed our carbon footprint data collection and calculation methodologies against the requirements of ISO 14064-1 (Specification with guidance at the organisation level for quantification and reporting of greenhouse gas emissions and removals) and the GHG Protocol Corporate Standard.

REE has carried out a limited level verification, which included the review of:

- the data held within our Carbon Accounting Workbook v15 (CAW) which is used to manage our carbon management and footprinting
- the primary data on which the CAW is based (contained within the 'Carbon accounting info pack')
- the process manual which defines the methodology we used for our carbon management and reporting processes

Based on the process and procedures they carried out REE concluded that there is no evidence that the 2020/21 GHG assertion (i) is not materially correct and is not a fair representation of GHG data and information and (ii) has not been prepared in accordance with the ISO 14064 1 and the GHG Protocol Corporate Standard.

For the current period, up to 2021 our target has been to reduce carbon emissions to 152 kgCO₂e per customer. We are reporting 192 kgCO₂e/Ml, and have therefore not met our target for the year. Our reasons for not meeting our performance commitment target include: i) the targets over 2020 to 2025 has been set broadly linearly and 2020/21 has been a year of preparation rather than implementation of direct interventions to reduce our carbon footprint which will start showing their effect in 2021/22 and ii) to a lesser extent, the fact that we use BEIS energy conversion rates for the UK to determine our carbon emissions based on our kW/h electricity consumption, and that actual rates for 2020/21 reflected a lower level of decarbonisation of the energy from the grid than had been indicated in BEIS' forecasts available at the time of the preparation of the business plan.

We are still expecting to meet our target over 2020 to 2025 based on the actions engaged to date. We have secured renewable energy guarantee of origin (REGO) backed energy arrangements covering our entire operational electricity needs (representing 84 per cent of our operational emissions) from 1 April 2021. This will ensure we outperform our target of 120 kgCO₂e/Ml for the 2021/22 period. Procurement is also underway to replace REGO arrangements with medium-term commercial green power purchase agreements (PPAs) linked to identified additional renewable energy schemes that will start operating over the next two to three years. These agreements ensure not only that we, and our stakeholders, can have confidence in the source of our renewable electricity, but also that, through our PPAs, we are supporting the expansion of additional renewable energy generation capacity, and enabling further decarbonisation at a UK level.

“

We are determined to support recovery in our region and build on lessons learned

STRATEGIC REPORT

GOVERNANCE

FINANCIAL STATEMENTS

ANNUAL PERFORMANCE

NON-FINANCIAL INFORMATION STATEMENT

This statement provides an overview of the information in the annual report on non-financial matters that helps readers understand our development, performance, position and the impact of our activity

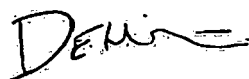
Our business model is focused on value creation through responsible business, a long-term focus, engagement with stakeholders and collaboration.	• Our business model on pages 21 to 27 • Our 2020 to 2025 business plan on page 58 • Our vision and strategy on page 20	
Our principal non-financial KPIs	• Our business performance on page 64	
Our principal risks	• Our risk management on page 30 • Our principal risks on page 36.	
Our key policies, strategies and outcomes on:		
The environment	• Corporate environmental resilience policy • We will deliver an extensive WINEP programme and biodiversity improvements on our SSSIs • We are part of the water industry's commitment to achieve net zero carbon emissions by 2030 • We have adopted a carbon reduction strategy for 2020 to 2025 and are publishing our net zero routemap in July 2021 to achieve net zero by 2030 • We manage long-term water resources through our water resources management plan	Our 25 year environmental plan on page 61. Our water resources management plan on page 60.
Our employees	• Speaking Up (Whistleblowing) policy • Health, safety and quality policy • Thrive 365! leadership Charter • We are a Living Wage employer • We achieved IIP silver certification • We have a comprehensive Thrive 365! – Health, safety and wellbeing strategy including mental health • We developed a comprehensive people plan in our corporate plan for 2020 to 2025 • Our responsible business commitments include a commitment to ensure fair pay, reward and recognition for all our employees and to reduced our gender pay gap	Our people on page 13 and page 102.

Social matters	• BS 18477 certification on inclusive service provision • Our business plan for 2020 to 2025 includes commitments on priority service and vulnerability • Our vulnerability strategy is designed to increase our support to all our vulnerable customers and to help them access our support • We have adopted 10 responsible business commitments which will be delivered under the oversight of our responsible business committee • Water industry public interests commitments social mobility pledge	How we create value for others on page 26.
The respect for human rights	• Ethical purchasing policy • Modern slavery policy and statement • We monitor our and our supply chain compliance with modern slavery legislation • Our procurement selection process considers matters related to human rights and modern slavery • We require our supply chain to apply similar standards as ours	Our modern slavery statement is available online at southeastwater.co.uk/modern-slavery
Anti-corruption and anti-bribery	• Hospitality gratuities and gifts policy • Conflict of interests policy • Speaking Up (whistleblowing) policy • We provide regular training to our employees on these matters • We require our supply chain to apply similar standards as ours	

Every year, we publish a performance, people and planet report with information on our non-financial performance and our corporate social responsibility in a clear and accessible format. Our performance, people and planet report is at southeastwater.co.uk/performance

Approved by the board and signed on its behalf by:

DAVID HINTON
CHIEF EXECUTIVE OFFICER
15 JULY 2021



DELIVERING OUR STRATEGY TO FULFIL **OUR PURPOSE**

To

**help society
and the
environment
to thrive**

**Water is vital to life and our society and environment
need it to thrive.**

Ultimately this is what our purpose is about as quality
water doesn't just fall from the sky.

We work in
partnership to
protect rare
species such as the
wartbiter cricket

Responsible business commitment

We are building a future generation schools programme to increase knowledge about water and the environment and to inspire careers in water.

- Covid-19 impacted our school visits - but we engaged with more than 300 pupils online
- We worked with National Geographic and three other water companies to run the "Big Water Quiz" while children were homeschooling

Flourishing environment

1,172 hectares of land improved through the year for biodiversity.

BIODIVERSITY

33

Number of Sites of Special Scientific Interest

We are leading an Ofwat innovation fund project to use citizen science to improve waterways

Arlington reservoir
and nature reserve

POSITION AND PROSPECTS

BOARD STATEMENT ON PERFORMANCE POSITION AND DIRECTION

This statement from our board explains how we have set our aspirations and how we have performed for all those we serve in 2020/21 as required under Ofwat's board leadership, transparency and governance principles. It also provides an overview of the position of the business at the end of the financial year and a forward look on our main objectives for 2021/22 for the implementation of the corporate plan for 2020 to 2025.

We provide a service that is essential for society to thrive now and in the future. As a board, our main goals are to deliver a great service to all our customers today and to plan for future water services by investing efficiently and protecting the environment.

The Covid-19 pandemic highlighted the importance of our public service function. Our priority has been to maintain our services to all our customers and critical facilities and protect our workforce and the public.

As we prepare this statement, we are acutely aware of the challenges that the Covid-19 pandemic has brought and will continue to bring for the rest of the year for our customers, employees and our partners.

HOW WE SET OUR ASPIRATIONS FOR SOUTH EAST WATER

Our purpose is to "provide today's public water service and create tomorrow's water supply solutions, fairly and responsibly, working with others to help society and the environment to thrive".

It is what guided us when setting our aspirations, strategy and our objectives for 2020 to 2025. This includes finding opportunities to have a positive impact on society and the environment as we provide our public water service.

To transform these aspirations into actions, we have created a five year corporate plan in which we have adopted service targets that will require us to keep delivering significant service improvements every year during 2020 to 2025 and 10 responsible business commitments to improve and measure our impact on society and the environment which we will review regularly to ensure they remain up to date and continue to reflect stakeholders' expectations.

A regulated water company must have an ethical and inclusive culture of public service guided by a strong sense of purpose. This means that to deliver the best service possible and to face challenges (our own and global ones such as climate change), we must have an integrated approach and we must work with and learn from our customers and all other stakeholders. We refer to this as "integrated thinking" and "stakeholder inclusiveness".

Last year, we adopted a corporate governance framework that is centred on purpose, culture, integrated thinking and stakeholder inclusiveness, and as we had committed to do, we have now adopted new articles of association that embed our purpose and revised directors' duties.

Our four strategic themes on which our business plan is based are detailed pages 101 and 102.

COMMUNITY AND CONSUMER FOCUSED



Being a business that understands our customers

Our corporate plan for 2020 to 2025 is built around customer satisfaction. We have evolved our approach to measuring customer satisfaction that we introduced in 2015, and have developed an innovative approach to measuring satisfaction based on attitudinal segments. This will help us understand the needs of all our customers and make sure we go beyond delivering what the 'average' customer wants. Our customer insight team has been set up to continuously engage with our customers and other stakeholders and to act on the feedback we receive.

Being a business that supports our vulnerable customers

We have stretched our performance and ambitions with six new performance commitments specifically around vulnerability. These have been co-created with our customers, stakeholders, employees and our CCG; so too has the strategy that underpins these performance commitments.

We have published our vulnerability strategy and we were the first water company to achieve the BS 18477 certification demonstrating that we provide an inclusive service for customers with vulnerable circumstances.

We are working with other utilities and charities to promote our Priority Service Register and the other support we provide vulnerable customers. We share experience and insight on how we can improve our support and engage with customers we have not been able to reach before.

Being a business that supports our community

Supporting our communities is part of our responsible business commitments with the development of a future generation schools programme on water, creating more partnership community projects on water use and vulnerability and supporting the tap water refill campaign to reduce plastic bottle use.

FLOURISHING ENVIRONMENT



Being a business that enhances the environment

Operating in an environmentally diverse and water stressed area, we need to make the right choices for our local communities and the environment.

We have a significant environmental programme to deliver and have developed a suite of six new performance commitments that recognise the influence we can, and should, have on landowners, other water users and abstractors to make water catchments more resilient to drought, while also ensuring we enhance habitats to give wildlife an opportunity to thrive.

We intend to build on the partnership approach we have developed over the previous regulatory period to achieve these ambitions as we know our shared experience and knowledge of the environment is key.

Being a business that plans for the environment

To support our environmental ambitions and to provide a long term view on all aspects of the environment, we are creating a 25 year environment plan, the first of its type in the industry. This plan aligns with Defra's 25 year environment plan and ensures we manage our interaction with the environment in a holistic and co-ordinated way.

We have also expanded our reporting on carbon emissions to meet new requirements and also started to implement the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) which we will develop further in 2021/22 in conjunction with our new adaptation plan which we will publish by December 2021.

We are defining how to use natural accounting to integrate considerations of the natural capital in our business decisions and in particular on capital investment decisions to ensure the most sustainable solutions are adopted. We have a commitment to significantly increase our use of renewable energy and are publishing our net zero routemap in July 2021 which explains how we intend to reach net zero by 2030.

POSITION AND PROSPECTS continued

THRIVING
PEOPLE**Being a business where the people we work with thrive**

We have set an ambitious five year people plan to build a culture which inspires excellence in its people. It is based on four strategic pillars which are key aspects of our culture and identify drivers for delivery and measures of success.

We want to create a thriving, resilient and inclusive environment with respect at its core and where diversity of thinking is valued. To this end our people plan has identified relevant actions we will take as part of our wellbeing strategy, to encourage social mobility and inclusion, to attract and recruit new talent and to improve skill transfers and develop mentoring.

We want to develop behaviours and capabilities in our workforce that will create a high performance culture. This will be achieved by developing leaders who help others reach their potential, by upskilling managers and employees for continuous improvement, by building a resilient workforce through learning and development, and by enhancing our engagement with employees.

We want to improve the performance of our business, continuously striving to meet and exceed company targets and employees expectations. Our action plan in this area targets business efficiency through our structure and working arrangements, improving onboarding and employee experience, improving the support to our managers through dedicated Human Resource and Organisational Development business partners, systems and automation and the development of new metrics.

Future proofing our business is the fourth priority of our people plan making sure that our workforce is able to respond to the changing expectations of the business and that the business is able to respond to the expectations of its people. In this area our people plan focuses on agile working, reward strategy and providing future opportunities including through succession planning or to ensure we have the skills we need for the future.

This plan also sets out how we are delivering our responsible business commitments on fair pay, reward and recognition and on health, safety and wellbeing.

TRUSTED
BUSINESS**Being a responsible and transparent business**

We are entrusted to deliver a continuous supply of safe, wholesome drinking water direct to our customers' homes. We will keep the trust of the public in our business with great service and high standards of governance and transparency.

The business already has a well-developed culture driven by public service values but we explain below how we are strengthening our public service culture. In the related field of ESG performance, this year we achieved the top position in our peer group under the GRESB benchmark.

Our package of responsible business commitments is intended to reflect the actions and behaviours that our customers and stakeholders expect a responsible business to display across our four strategic themes. Among these, our commitment to trusted corporate governance and transparency of reporting seek to ensure that our standards of conduct and the transparency of the information we provide meet the expectations of stakeholders.

Our remuneration committee has designed and adopted a new bonus scheme for 2020 to 2025 that reflects the importance of service delivery to customers and of our commitments to act responsibly. It includes metrics in relation to outcome delivery incentives (ODIs), environmental, social and governance matters, financial and personal objectives. Our ESG metrics put into practice our aspiration to include broader stakeholder considerations in the design of our incentives. This annual report includes an entirely revised directors' remuneration report which sets our remuneration policy and how it was applied in detail on page 146.

We also explain how we take into account the interest of customers and other stakeholders in our section 172(1) statement on page 82.

Our dividend policy sets out principles and considerations we must have regard to when authorising dividends in relation to our financial obligations and financial resilience, the interests of employees, the ability of the company to finance current and future investment, and performance against our commitments. It is published on our website at: corporate.southeastwater.co.uk/about-us/our-governance

We are also playing an active role regionally in relation to the impact of housing growth on water engaging with relevant stakeholders such as planning authorities to make sure these issues are considered.

Being an innovative business

Maintaining trust also means being able to innovate to improve and continue to provide a great service in the future. We have developed a focused innovation strategy which targets our customers' and stakeholders' priorities where we can make the most difference.

We have developed a number of innovation tools to help us deliver our stretching performance commitments for the next five years and beyond.

HOW WE HAVE PERFORMED FOR THOSE WE SERVE IN 2020/21

During 2020/21 our main priority has been to maintain our essential service throughout the pandemic and to adapt quickly to the challenges it presented.

Our second priority has been to support customers who needed it the most. We have reached out to more of them in partnership with charities, other water companies and utilities. We provided financial assistance in the form of payment holidays and many more customers benefited from our social tariff. We also encouraged more people to join our Priority Services Register reaching more than 29,000 households or 3.3 per cent of our customer base. We have recently passed the BSI audit on our services for vulnerable customers which confirmed our accreditation to the standard.

Our aim was also to start delivering our performance commitments, our investment programme and strategy for the next five years as we would have done in normal circumstances, acknowledging that we would face many challenges and that we would have to adapt and be agile to achieve our goals.

Despite the challenges, we have made good progress in many areas. We highlight below key elements relating to performance that are of particular interest to our customers and stakeholders.

Our performance in detail

We include more information on our performance during the year:

- in the Chief Executive Officer's Introduction on page 12
- in our business performance section on page 64
- in tables 3A to 3H of the annual performance report on page 300

This year we have created a microsite for our performance, people and planet report which provides detailed information on our performance and our corporate social responsibility in a clear, accessible and interactive format. Our microsite is available at:



performance.southeastwater.co.uk

Our performance can be compared with other water companies by visiting www.discoverwater.co.uk which has been developed to provide more transparency on the performance in the industry. This is an important tool to enable stakeholders to compare our performance to ensure we are striving for continuous improvement and stretching ourselves to be providing the best possible service.

POSITION AND PROSPECTS continued**Challenges that affected delivery to our customers in 2020/21**

Among many challenges during the year, we faced unprecedented water demand in August 2020 due to the combination of a significant increase in underlying demand for water as more customers were staying at home and exceptional peak demand due to high temperatures.

According to the Met Office, the heatwave in August 2020 was one of the most significant heatwaves to affect southern England in the last 60 years. It saw a combination of both unusually high temperatures and sustained duration for approximately a week, with the highest temperatures in London and the south-east.

This resulted in demand exceeding our capacity to provide enough water in certain parts of our network. This was a difficult situation for the customers affected who went without water for too long despite our preparation to increase production and early messaging encouraging customers to save water. We have reviewed this incident to learn from it and be able to improve our readiness and response to similar events in the future.

A major reservoir in Aylesford was affected by multiple sinkholes resulting in loss of water and the unavailability of the reservoir. Remedial works to bring the site back in operation have been fast tracked and work on an additional urgent scheme at the site of the future Butler WTW started quickly.

Performance highlights in 2020/21

- **customer measure of experience**
Our combined C-MeX score has improved this year, with a final score of 80.70 out of 100 but our final ranking is not yet known and will be determined by Ofwat after the publication of our annual report. We also maintained an upper quartile position in the CCW report on complaints
- **leakage**
The amount of treated water leaking from our network is a key area customers want us to tackle. This year we have beaten our leakage target for the 19th year in a row. Our target for 2020/21 was to reduce our annual leakage rate to 95.2 million litres a day (ML/d) and we reduced our leakage rate to 92.67 ML/d. We also have a three year rolling average target of 94.9 ML/d and we achieved a lower level of leakage of 94.1 ML/d
- **taste, odour and appearance of water**
We have met our targets relating to the appearance and the taste and odour of water which we measure by the number of contacts we receive from customers. For appearance our target was to receive less than 1.09 contacts per 1,000 population and during the 2020 calendar year we received 1.00 contacts per 1,000 population. For taste and odour our target was to receive less than 0.42 contacts per 1,000 population and we finished the 2020 calendar year with a contact rate of 0.34 per 1,000 population
- **catchment management**
Under our catchment management programme we actively engage with farmers and landowners to prevent pesticides, soil and fertiliser washing from fields into the rivers and aquifers we take water from. During 2020/21 we targeted working with farmers and landowners who manage a total of 2,843 hectares of land and we outperformed this measure achieving a total of 2,858 hectares of managed land

- **biodiversity**
Owning or managing 33 sites of Special Scientific Interest, a National Nature Reserve, two local nature reserves and numerous Areas of Outstanding Natural Beauty we work with Natural England to provide net biodiversity gains during this five year period. We had a target to undertake improvements on 1,166 hectares of land during 2020/21 and we outperformed this target, undertaking improvements on 1,172 hectares of land
- **WINEP**
Under the Water Industry National Environment Programme (WINEP) we must deliver 60 improvement schemes between 2020 and 2025 enhancing the natural environment and ensuring the water we take does not have a negative impact on the environment. Our first target is to complete 43 projects in 2021/22. In advance of programme, nine projects were signed off by the Environment Agency this year, most of them relating to sustainable water abstraction. We expect to complete a further 34 projects next year, reaching our target of 43 schemes completed by the end of 2021/22
- **our "CatchmentLIFE"**
Project has been selected as a winner of the first round of Ofwat Innovation in Water Competition as one of 11 projects out of 61 entries. We also participate in another selected project led by Severn Trent Water on vulnerable customer engagement

We are not complacent and are aware there's still work to do to improve areas such as customer complaints and increase our customer satisfaction scores further. We set out below our main objectives for 2021/22.

OUR OBJECTIVES FOR 2021/22

As we make this statement, the vaccination campaign has progressed well in the UK and the planned lifting of the Covid-19 restrictions announces a return to more familiar ways of operating. Our first task will be to manage the transition out of lockdown acknowledging that things will be different than they were before the pandemic.

We are getting ready for a return to more usual working practices at our operational sites and offices but are also working on an "agile working" plan that builds on the practical experience we acquired during the pandemic and responds to the aspirations of our workforce. We will also continue to ensure that our people are safe and to promote a working environment that supports wellbeing.

We are also getting ready to operate in an environment that will remain challenging and potentially unpredictable.

We expect that the changes to working practices and mobility induced by the Covid-19 pandemic will persist to a degree and that the underlying demand for water from our customers will continue to be higher than before the pandemic.

The economic impact of the pandemic on our customers will also persist in 2021/22 and we will continue to provide additional support to those of our customers who need it the most either financially or through our priority services. We will pursue a sensitive policy of payment collection.

Our "licence to operate" relies on us getting the basics right by delivering our core services well and constantly improving. This means that we will continue to focus our efforts on the fundamentals of reliable water supply, high quality drinking water, excellent customer service and driving down leakage.

POSITION AND PROSPECTS continued

Given the change in demand patterns driven by Covid-19, one of our top priorities for customers will be to improve our resilience in case of incidents and/or extreme weather events to avoid or limit the duration of interruptions. This involves:

- bringing our Aylesford reservoir back in service and delivering a fast track resilience scheme on the site of the future Butler WTW for the summer of 2021
- continue to refine our operating plans to manage peak demand in sensitive areas of our network and continue to improve the understanding of the system across operational teams to facilitate an optimum use of the water supply system
- develop our cross-skilling programme to improve the resilience of operational teams and facilitate collaboration
- continue to improve the structured management of all incidents, small and large, to ensure all issues are resolved as quickly as possible limiting their impact on customers
- do more to help customers reduce their water use during dry periods so that we keep demand to a sustainable level both in terms of our ability to supply and of impact on the environment, including ensuring that our communication strategy is timed to pre-empt customers' behaviours and that the strength of our messaging increases as required
- continue to develop a company-wide system approach to network management and operational resilience in the short, medium and long term including additional network connectivity

Customer trust requires both reliability of supply and excellent customer service. Our action plan for 2021/22 includes a number of initiatives to improve customer experience and our C-MeX performance:

- we will develop an overarching customer digital strategy and customer communication platform to improve self-service and accessibility of our services for customers
- we will continue to deliver our vulnerability strategy whilst ensuring it remains current and still meets stakeholders' expectations

- we will work to improve customer satisfaction across all segments implementing the programme of action that was developed this year

Our other key objectives for 2021/22 are to:

- continue to work to improve our ranking position across key comparative measures
- continue to work on reducing per capita consumption via behavioural changes. As part of this programme of work we have already launched a "My Account" update which enables customers to compare water usage to spot if they are using a high amount
- continue the development of our smart network strategic plan for AMP7 and AMP8
- continue to implement our calm network plan
- continue to roll out our leakage strategy and customer side leakage reduction programme
- continue to deliver our environmental programme to meet our commitments on catchment management, sustainable abstraction and biodiversity improvements

Our business also need to work today for a long term sustainable water supply. In 2021/22 we will:

- continue the preparation of our water resources management plan reflecting the regional plan being developed for the south east of England
- continue to reduce our carbon emission including by transitioning to new renewable sources of energy produced by schemes that we have contributed to develop
- publish our net zero routemap and our adaptation report as well as developing our reporting under TCFD
- continue to develop our 25 year environmental plan in consultation with our stakeholders and partners

Over the coming year we will continue to build on the performance improvements we have made over the last 12 months.

LONG-TERM VIABILITY STATEMENT

To prepare our long-term viability statement, we have conducted our long-term viability assessment, taking into consideration our business model, our current financial position, and principal risks that can affect our business.

We are a regulated long term utility business characterised by multi-year investment programmes and stable revenues. The water industry in England and Wales is currently subject to economic regulation rather than market competition and Ofwat, the economic regulator, has a statutory obligation to ensure that water companies are able to finance their appointed activities. Ofwat meets this obligation by setting price controls for five-year Asset Management Periods ('AMPs'). This mechanism reduces the potential for variability in revenues from the regulated business. The current AMP (AMP7) runs until March 2025.

Our assessment of the current financial position is set out on page 73.

Our long-term viability assessment reviewed the company's prospects and considered the principal risks and uncertainties, including the ongoing impacts of Covid-19. Downside sensitivities have been developed based on an assessment of the likelihood and financial scale of these principal risks. Stress tests have been performed based on these downside sensitivities (individually and in combination) to assess the potential impacts of these risks and uncertainties. The financial projections considered include the PR19 regulatory mechanisms such as cost sharing and inflation. The assessment also considered the mitigating actions that might be taken to reduce the impact of such risks and uncertainties and the likely effectiveness of mitigating actions. Additional detail on the downside sensitivities tested is set out below.

ASSESSMENT PERIOD

We have considered the appropriate length of time over which to provide the viability assessment. In making an assessment, we have taken account of the balance between the length of the period assessed and robustness of such analysis, alongside guidance from Ofwat. In considering our outlook period we had regard to the long term nature of our business and the characteristics of our regulatory regime described above.

On the recommendation of the audit and risk committee, and in line with Ofwat's guidance, we have assessed the prospects of the company over a period of 10 years to March 2031.

Analysis of resilience extending beyond 2025 remains subject to greater uncertainty surrounding the assumptions underpinning financial projections for the AMP8 price control period, with greater variability of potential outcomes.

Uncertainties arising from market competition within this period have been taken into consideration but do not affect the result of our assessment. This is due to the fact that monopoly activities form the main part of the business of the company.

REGULATORY MECHANISMS

The financial projections considered include the mitigation through the PR19 regulatory mechanisms such as cost sharing and the RPI/CPIH wedge. These result in adjustments to AMP8 revenues and opening RCV where ex post projections are not in line with ex ante allowances.

However, the penalties associated with the Gearing Outperformance Sharing Mechanism are not included in line with the latest regulatory precedent set by the CMA PR19 FD. The inclusion of the associated penalties was tested as a separate sensitivity and this did not result in material deterioration of financial resilience.

ASSESSMENT RESULTS AND MITIGATION STRATEGY

The results of our assessment revealed that none of the stress-testing scenarios would lead to a default event in servicing the company's debt, nor would they lead to adverse impacts on customer service or the company's ability to carry out normal operational activities.

Our securitised financing arrangements include covenants with trigger thresholds which are reported bi-annually. The baseline plan, incorporating the expected impact of Covid-19, shows sufficient liquidity and clear headroom for debt covenants, when considering trigger thresholds.

LONG-TERM VIABILITY STATEMENT continued

However, in the absence of any mitigating action being taken, the most severe, but plausible, scenario modelled indicates a breach of the trigger threshold in the adjusted interest cover ratio covenant for the years ending March 2024 and March 2026. This is not an event of default threshold. Any such breach of the trigger threshold would activate initial creditor protections under the terms of the securitised financing arrangements, which are designed to maintain the company's creditworthiness without disrupting its ability to trade, such as restrictions on dividends.

None of the scenarios resulted in an impact on our expected financial metrics that cannot be reasonably mitigated using the existing safeguards within our financing structure.

The assessment also considers potential mitigating actions that we could undertake to reduce the impact of the sensitivities considered.

The directors have identified actions, including reducing discretionary outflows of funds and working with providers of finance, that would be available to mitigate the impact of adverse outcomes.

As part of the assessment of the resilience of the company and the regulated business we take into account the impact of the overall group structure and intra-group transactions. The resilience and viability of the group is assessed on a continuous basis including any implications of the financial projections of the wider group for the regulated business and vice versa. We have not identified any issues from our recent analysis of viability across the group that are likely to impact on the resilience of South East Water.

STRESS TESTING

We review and consider the risks to which the business is exposed and potential impacts on viability on an ongoing basis; this includes structured, systems-based risk identification processes and management controls, robust budgeting and forecasting and continuous sensitivity analysis.

Principal risks represent all factors that could prevent us from delivering our strategic objectives and business plan. As a result, not all principal risks translate directly into a downside sensitivity. We have considered the principal risks and uncertainties for the company and their potential impact on viability. Where it is assessed that (1) a principal risk is likely to occur and (2) the financial impact could be material,

the implications for financial resilience are assessed in the long-term viability statement through defined downside sensitivities.

Based on the principal risks, we have identified below the relevant risk factors that can cause negative impacts on the financial position of the company. We then construct downside sensitivities focusing on different combinations of the risk factors.

Our sensitivities combine qualitative and quantitative criteria and cover the following risk factors to assess their impact on liquidity and compliance with financial ratios until March 2031:

- **Outturn inflation under forecast:**

Inflation risk primarily relates to the fact that the price control is in real terms and the allowed revenue moves up by a designated inflation figure (CPIH for PR19) while some of the costs are fixed in nominal terms. This means that when inflation is lower than was assumed when the real-terms costs were calculated, the company will face the risk of underfunding on these elements.

- **Interest rate above forecast:**

Interest rate risk can result in an increase in borrowing rates for new debt raised, and it can increase the borrowing cost for any floating rate debt.

- **ODI penalties:**

The effect of ODI penalties as a result of unexpected adverse events can materialise within the AMP7 period, which have been considered in our assessment.

- **Totex overspend:**

Totex overspend is a risk that we have assessed carefully, when considering scenarios of company underperformance as well as unexpected costs due to severe weather-related incidents.

- **Retail cost overspend:**

Retail cost to serve forms a part of the allowed revenue, which the company may underperform against for reasons such as cost escalation and bad debt.

Our downside sensitivities include individual and combination scenarios that we considered to be severe but plausible. These are summarised in the following table:

Sensitivity tested	Specification of sensitivity	Related principal risks
Macroeconomic shock - High inflation and interest/low inflation and interest	The company's revenues are linked to inflation. Low or negative inflation tends to adversely impact profits and cash flows as decreases in revenues exceed decreases in costs. We have assessed the effects of +/- 1.5% RPI, CPIH and interest rates in AMP7.	Macroeconomic risks Financial resilience
Totex underperformance	Significant overspending could result in a deterioration in financial metrics and performance, which could impact on the company's liquidity and credit rating. We have assessed the impact of a 3.3% additional overspend on totex (2.3% capex, 4.3% opex) in each remaining year of AMP7.	Strategic asset failure and major operational incident Failure to meet the peak demand for water Climate change Failure to deliver business plan and to meet regulatory outcomes
ODI penalty	Failure to deliver performance at the committed level can lead to significant ODI penalties. We have assessed the impact of penalties equivalent to an additional £9 million per year.	Strategic asset failure and major operational incident Failure to meet the peak demand for water Climate change Failure to deliver business plan and to meet regulatory outcomes
Sustained adverse conditions	The company's risk management process has identified a number of risks including a deflationary environment. This scenario considers a combination of low inflation and cost overspending. Significant overspending could result in a deterioration in financial metrics and performance, which could impact on the company's liquidity and credit rating. We have assessed 3.3% wholesale totex under-performance (2.3% capex, 4.3% opex) and ODI equivalent to £9 million per year for the next three years of AMP7 alongside a reduction in RPI and CPIH of 1.5% for the next three years.	Strategic asset failure and major operational incident Failure to meet the peak demand for water Climate change Failure to deliver business plan and to meet regulatory outcomes Macroeconomic risks Financial resilience
Pervasive underperformance	The company's risk management process has identified a number of risks including extreme weather events and failure of key assets that might have a significant impact on the company's operational and financial performance. This sensitivity will focus on shorter-term external shocks potentially caused by the wider economy, weather conditions, or a combination of the two, leading to short-term adverse effects on multiple risk factors. We have assessed an additional 3.3% wholesale totex under-performance (2.3% capex, 4.3% opex) and additional £9 million ODI penalties per year for the rest of AMP7. £1.8 million retail opex overspend in 2021/22 relating to additional bad debts.	Strategic asset failure and major operational incident Failure to meet the peak demand for water Climate change Failure to deliver business plan and to meet regulatory outcomes

LONG-TERM VIABILITY STATEMENT continued

Sensitivity tested	Specification of sensitivity	Related principal risks
Severe downside	The company's risk management process has identified a number of risks including extreme weather events and failure of key assets and that might have a significant impact on the company's operational and financial performance. The combined scenario represents a situation where several of the severe scenarios above occur simultaneously. We have assessed 7% wholesale totex underperformance (6% capex, 8% opex) and additional £13 million ODI penalties per year for the next three years. c. £2.3 million retail opex overspend for the next three years relating to additional bad debts.	Strategic asset failure and major operational incident Failure to meet the peak demand for water Climate change Failure to deliver business plan and to meet regulatory outcomes

MITIGATING ACTIONS

In the event of more extreme but low likelihood scenarios occurring, there are a number of key mitigations available.

The regulatory framework includes mechanisms to adjust future revenues and regulatory capital value (RCV) to partially offset under recovery when compared to the Final Determination. As well as the protections that exist from the regulatory framework, a number of actions are available to mitigate more severe scenarios, which include the raising of new finance; capital programme deferral or reduction of discretionary expenditure to cover costs relating to penalties; considering efficiency programmes which

seek to reduce costs and bring costs in line with regulatory allowances; discussing the impact on debt covenants with lenders and seek a temporary waiver if necessary; the temporary restriction or re-phasing of dividend payments; and accessing additional equity.

For each scenario and sensitivity, we have considered and identified appropriate mitigations in the event that a severe scenario or sensitivity used for stress testing were to result in a significant deterioration in projected financial metrics. The table below illustrates the relevant financial mitigating actions which would be considered in each scenario.

Description	Related scenarios/ downside sensitivities	Potential mitigating actions
Change in inflation or interest rates	<i>Sensitivity 1</i> High inflation and interest rates <i>Sensitivity 2</i> Low inflation and interest rates	Reduce discretionary expenditure. Reduce working capital to support cash flow. Consider a temporary reduction in or re-phasing of dividends.
Under-performance on ODIs	<i>Sensitivity 4</i> ODI penalties All combination downside sensitivities	Reduce discretionary expenditure to cover costs relating to penalties. Discuss the impact of debt covenants with lenders and seek a temporary waiver if required. Consider a temporary reduction in or re-phasing of dividends.

Description	Related scenarios/ downside sensitivities	Potential mitigating actions
Higher costs than PR19 FD	<i>Sensitivity 3</i> Totex underperformance All combination downside sensitivities	A reduction in discretionary expenditure. Consider efficiency programmes which seek to reduce costs and bring costs in line with regulatory allowances. Consider a temporary reduction in or re-phasing of dividends. Discuss the impact of debt covenants with lenders and seek a temporary waiver if required.
Severe event – relating to weather, operational failure, or another exceptional event	All combination downside sensitivities	Consider efficiency programmes which seek to reduce costs and bring costs in line with regulatory allowances. Reduction of discretionary expenditure. Reduce working capital to support cash flows. Consider a temporary reduction in or re-phasing of dividends.

VIABILITY STATEMENT

The board has assessed the viability of the company over a 10 year period to March 2031, taking into account the company's current position, principal risks, and effectiveness of any potential mitigating actions. Based on that assessment, the directors have a reasonable expectation that South East Water will be able to continue to operate and meet our obligations over the period to March 2031.

The audit and risk committee supports the board in performing this review. In addition, our external auditor, Deloitte, reviews this viability statement and the outputs of our stress testing as part of its normal audit procedures. It considers whether these are consistent with the directors' conclusion with respect to business viability, and if the processes undertaken are sufficient to support the statements made.

Their audit report, including comments on the viability statement, is set out in the annual report on pages 174 to 185.

GOVERNANCE AND ASSURANCE

The analysis underpinning this assessment has been through a robust internal review process. The board has reviewed and discussed the process undertaken by management, and also reviewed the results of the stress tests performed including the key credit financial ratios, the company's liquidity, and ongoing ability to meet its financial covenants.

The board also provides robust internal assurance by reviewing and challenging the stress test scenarios selected and risk mitigation strategies. As part of the assurance process, the board has taken into account the principal risks and uncertainties facing the company, and the actions taken to mitigate those risks.

The board reviews and approves the medium-term plan on which this viability statement is based. The board also considers the period over which the assessment of prospects and viability statement should be made.

GOING CONCERN STATEMENT

In preparing the financial statements the directors considered the company's ability to meet its debts as they fall due for a period of one year from the date of this report. This was carried out in conjunction with the consideration of the long-term viability statement above. The directors have also considered the discussions that are on-going for the replacement of the revolving credit facility which has received credit approval and will be completed in 2021. On this basis the directors considered it appropriate to adopt the going concern basis in preparing the financial statements.

Flourishing environment

HOW WE CONTRIBUTE TO AN
ENVIRONMENT THAT FLOURISHES
TODAY AND TOMORROW

CORPORATE GOVERNANCE

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We manage more than 30 protected sites for biodiversity. Horse power helped us remove non-native trees with minimal impact. Read about our 25 year environment plan on **page 61**

OUR DIRECTORS ON 15 JULY 2021

INDEPENDENT NON-EXECUTIVE DIRECTORS*

NICK SALMON CHAIR

Nick was appointed Chair of the board of South East Water on 1 April 2015. He brings a wealth of experience from a number of senior roles, including as a senior independent non-executive director of United Utilities, and an engineering background. He is currently Chair of Scotia Gas Network Limited. Nick holds a BSc. Degree in Mechanical Engineering and is a Fellow of the Royal Academy of Engineering.

JOHN BARNES

John was appointed a non-executive director on 28 January 2016. Prior to his more recent involvement with a start-up company developing renewable energy schemes, John had gained over 30 years' experience in the water industry, mainly in the UK, but with spells in the Middle East and New Zealand. John is a former non-executive director of the Mid-Cheshire Hospitals Foundation Trust and was Executive Chair of All Change for Crewe, focused on making the most of inward investment to the town.

CHRIS GIRLING

Chris was appointed a non-executive director on 30 October 2014. Chris, an experienced finance professional, has a background in a variety of sectors, including construction, support services, pharmaceuticals and aerospace. Chris retired as group finance director of FTSE 250 Carillion plc in 2007 and since then he has chaired three audit committees and one pension fund.

CÉLIA PRONTO

Célia was appointed a non-executive director on 1 June 2018 and has a wealth of experience and expertise of the service sector in a range of industries. Célia is currently Managing Director at Love Home Swap, a subsidiary of RCI worldwide and an independent non-executive director of Moto Hospitality Ltd and Samworth Brothers. She was previously Group Marketing & E-Commerce Director and board member of the Ford Retail Group and Chief Customer and Digital Officer of Casual Dining Group Ltd.

* AS DEFINED IN THE UK CORPORATE GOVERNANCE CODE 2018

NON-EXECUTIVE DIRECTORS

RACHEL DREW

Rachel is an Investment Director at HRL Morrison & Co and was appointed to the South East Water board in December 2019. Rachel has an MBA from the Judge Institute at University of Cambridge and master's and bachelor's degrees in Engineering from the University of Auckland. Rachel is also a non-executive director at rail company Porterbrook and the Northern Irish gas distribution business Phoenix Natural Gas. As well as experience in the financial investment industry Rachel has been an operational executive at NZ Bus, NZ's largest public transport operator and a consultant at The Boston Consulting Group.

ANNE-NOËLLE LE GAL (APPOINTED ON 18 JUNE 2021)

Anne-Noëlle is an Investment Director at Vantage Infrastructure focusing on the asset management and transaction execution of European equity infrastructure investments, and was appointed to the South East Water board in June 2021. She holds a Master 1 in Finance from Paris Dauphine University and a Masters in Accounting and Finance from the London School of Economics, and is a non-executive director at gas distribution company, Phoenix Natural Gas. Anne-Noëlle is also Deputy Chair of GRESB's EMEA Infrastructure Benchmark Committee.

EXECUTIVE DIRECTORS

DAVID HINTON CHIEF EXECUTIVE OFFICER

David has been CEO since 1 August 2020 and was previously Asset and Regulation Director from 1 June 2013. David has more than 25 years' experience at South East Water and its predecessor companies acquired in various roles including Head of Regulation and Strategy and Head of Water Quality. With a strong science background, David has held previous senior roles in scientific consultancies as well as laboratory management for the Public Health Laboratory Services. David holds a BSc (Hons) in Biotechnology and a Master of Business Administration specialising in ethical consumerism.

ANDREW FARMER CHIEF FINANCIAL OFFICER

Andrew, who joined as Chief Financial Officer on 1 August 2015, has held a number of senior management posts in finance, most recently at MAG plc, the country's largest UK owned airport operator, and Doosan Power Systems, a leading manufacturing, energy technologies and services company. Andrew holds a BSc (Hons) in Engineering and Business Studies from the University of Warwick and qualified as a Chartered Accountant with Price Waterhouse.

OUR DIRECTORS ON 15 JULY 2021 continued

RESIGNING DIRECTORS*

PAUL BUTLER

MANAGING DIRECTOR (RESIGNED ON 31 JULY 2020)

Paul has a wealth of water industry experience, having previously been Managing Director of Mid Kent Water from 2001 to 2006 and Chair of UKWIR, a water industry research organisation from 2005 to 2012. A Chartered Accountant, he previously worked for Mid Kent Water as Group Financial Controller, Ernst & Young and Marks and Spencer. Paul Butler had informed the board of his intention to retire at the end of July 2020 and took his retirement on 31 July 2020.

MARISSA SZCZEPANIAK

NON-EXECUTIVE DIRECTOR (RESIGNED ON 18 JUNE 2021)

Marissa was Investment Director at Vantage Infrastructure responsible for infrastructure and was appointed to the South East Water board in December 2016. Marissa has a Bachelor of Science in finance, accounting and economics and is also a non-executive director at rail company Porterbrook.

* DIRECTORS IN OFFICE DURING THE PERIOD FROM 1 APRIL 2020 TO 31 MARCH 2021 AND RESIGNED BEFORE 15 JULY 2021.



Please see page 135 for details of the changes on our board.

COMPANY DETAILS

NICOLAS TRUILLET
COMPANY SECRETARY

COMPANY'S BANKERS

HSBC BANK PLC,
60 QUEEN VICTORIA STREET,
LONDON EC4N 4TR

COMPANY'S AUDITOR

DELOITTE LLP STATUTORY AUDITOR
LONDON, UNITED KINGDOM

REGISTERED OFFICE

ROCFORT ROAD, SNODLAND,
KENT ME6 5AH

REGISTERED NO. 02679874

COUNTRY OF DOMICILE AND
INCORPORATION: ENGLAND AND WALES

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**Corporate governance
and compliance are an
integral part of how our
board and our business
as a whole operate**

INTRODUCTION FROM THE CHAIR

Corporate governance and compliance are an integral part of how our board and our business as a whole operate.

During the year we have completed the process initiated last year, of adopting new articles of association which enshrine our purpose and revised directors' duties. This was an integral part of our strategy and corporate plan for 2020 to 2025. It will help us demonstrate that South East Water can be trusted as a provider of an essential public service in years to come.

This marks our commitment to become a purpose-led organisation and promote a culture of public service and inclusiveness to achieve a fair balance between our interests and those of our customers, other stakeholders and the environment.

Our company purpose is "to provide today's public water service and create tomorrow's water supply solutions, fairly and responsibly, working with others to help society and the environment to thrive".

It is centred on our core functions as provider of the public water service and also expresses our ambition to contribute to society and the protection of our environment.

We explain below how we meet the objectives of the board leadership, transparency and governance principles published by Ofwat and how we have followed the principles of our own corporate governance code during the year.

This annual statement has been prepared to provide clear information on our business to our customers, investors, regulators and other stakeholders. We describe how we put governance into practice in this statement which I hope you will find helpful in demonstrating our commitment to excellence in governance.

This statement describes our corporate governance and how the board has operated within our corporate governance framework to promote a culture of public service and the long-term success of the business. It explains the concrete steps we have taken to meet the objectives, principles and provisions of our corporate governance code in the financial year.

The board confirms that it has complied with the principles of the company's corporate governance code (which incorporate Ofwat's board leadership, transparency and governance principles and relevant principles of the 2018 UK Corporate Governance Code) with the following exceptions or alternatives to the relevant provisions of the code:

- the board as a whole considers succession planning of the board rather than this being delegated to the nomination committee. This ensures that issues of balance of skills and diversity and any other aspects of succession are discussed by the whole board. The nomination committee has delegated authority to deal with the process of appointment and to consider and recommend appointments of new directors that may be selected in accordance with the succession planning approach agreed by the board. (Code provision 3.1.4)
- the percentage of company pension benefits for executive directors is aligned with the percentage available to the workforce for new appointments or a change of role and the pension benefits of the CFO have also been aligned with effect from 1 April 2021. Further details are provided in the directors' remuneration report. (Code provision 5.1.2)
- the remuneration committee had regard to the workforce remuneration in defining the remuneration policy and has reviewed relevant aspects of the workforce remuneration in the year but there has not been a specific engagement with the workforce on executive remuneration. There will be engagement with the Staff Council in 2021/22 as explained in the directors' remuneration report. (Code provision 5.2.4)

Further details on how we have met the objectives of the board leadership, transparency and governance principles are set out below.

This statement presents our governance in practice following the main themes in our corporate governance code.

NICK SALMON

CHAIR

15 JULY 2021



BOARD LEADERSHIP AND COMPANY PURPOSE

PRINCIPLES OF OUR CORPORATE GOVERNANCE CODE RELEVANT TO THIS SECTION

- A.** The company has an effective board with full responsibility for all aspects of the company's business as a regulated company for the long term.
- B.** A successful company is led by an effective and entrepreneurial board, whose role is to promote the long-term sustainable success of the company, generating value for shareholders and having a positive impact on wider society and the environment.
- C.** The board should ensure that the necessary resources are in place for the company to meet its objectives and measure performance against them. The board should also establish a framework of prudent and effective controls, which enable risk to be assessed and managed.
- D.** The board establishes the company's purpose, strategy and values, and is satisfied that these and its culture reflect the needs of all those it serves.
- E.** All directors must act with integrity, lead by example and promote the desired culture.
- F.** In order for the company to meet its responsibilities to shareholders and stakeholders, the board should ensure effective engagement with, and encourage participation from, these parties.
- G.** The board should ensure that workforce policies and practices are consistent with the company's values and support its long-term sustainable success. The workforce should be able to raise any matters of concern.

OUR PRINCIPLES OF GOVERNANCE AND CORPORATE GOVERNANCE CODE

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

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

Our corporate governance framework sets out our general philosophy and approach to governance. It marks a move towards a stakeholder model of corporate governance and supports our strategy. It is set out on page 56.

Under our licence, we are required to conduct our regulated business as if it was substantially our sole business and the regulated business was a public limited company separate from any other business we carry out. We also have an obligation to meet the objectives of Ofwat's board leadership, transparency and governance principles (BLTG principles) and to explain in a manner that is effective, accessible and clear how we are meeting these objectives.

Our corporate governance code combines the objectives and provisions of Ofwat's BLTG principles and also principles and provisions of the UK Corporate Governance Code 2018 which are applicable to a private limited company and consistent with Ofwat's principles. We chose to continue to follow the more detailed provisions of the UK Code rather than those of the Wates principles.

Our corporate governance code is available on our website at



southeastwater.co.uk/ourgovernance

BOARD LEADERSHIP AND COMPANY PURPOSE continued**OUR PURPOSE, VALUES AND CULTURE**

Our purpose is to “provide today’s public water service and create tomorrow’s water supply solutions, fairly and responsibly, working with others to help society and the environment to thrive”.

Our purpose is:

- centred around our core purpose as provider of the public water service (both for now and the future)
- reflect our wider societal and environmental goals delivered through performing our core service and the “do no harm principle” of not profiting from causing problems for people or the planet
- reflect a commitment to an inclusive approach to stakeholder engagement as a means of achieving the company’s purpose and achieve a fair balance between our interests and those of customers, the environment and other stakeholders

Achieving a durable change in culture to become a purpose-led organisation driven by public service values, is a continuous effort. The following contribute to promoting our purpose and values within the business:

- our corporate governance framework
- our articles of association which embed our purpose and revised directors’ duties
- our responsible business commitments delivered under the oversight of our responsible business committee
- executive directors’ pay related to all aspects of performance including responsible business objectives
- staff engagement with an independent non-executive director nominated as a designated point of contact with our workforce, engagement with the Staff Council and wider board engagement programme to increase the interaction of the board with different levels of the business
- measuring our ESG practices and achievements against the GRESB benchmark

The adoption of our new articles of association by our shareholders means that directors must act in the way they consider, in good faith, would be most likely to fulfil the purpose of the company, thereby promoting its success (i) for the benefits of shareholders, and (ii) to have a positive impact on society and the environment through its business and operations.

In doing so the directors must consider (amongst other matters):

- the long term consequences of their decisions
- the need to foster the relationships with customers, suppliers and other stakeholders
- the interests of employees
- the impact on the community and the environment
- the need to maintain a reputation for high standards of business conduct

We also publish every year a performance, people and planet report which highlights in more details our responsible business initiatives and how we deliver value to customers, the environment and our communities in fulfilling our wider environmental and societal purpose.

HOW WE MEET THE OBJECTIVES OF THE BOARD LEADERSHIP, TRANSPARENCY AND GOVERNANCE PRINCIPLES (BLTG)

Under the terms of its Licence, the company is required to explain in a manner that is effective, accessible and clear how it is meeting the objectives contained in the BLTG principles which are incorporated into the company's corporate governance code.

We explain in the tables below the concrete steps we are taking to meet each of the four objectives of the BLTG principles. The tables below are intended to help readers find easily the explanations in this annual report about each objective and other relevant information on how we meet these objectives.

Objective 1	How we meet the objectives	Read more
The board of the Appointee establishes the company's purpose, strategy and values, and is satisfied that these and its culture reflect the needs of all those it serves.	We formulated the company's purpose which has been a central part of the development of our strategy and corporate plan for 2020 to 2025.	On our governance on page 119
	We embedded our purpose into our articles of association and revised directors' duties.	
	Our articles of association are available at corporate.southeastwater.co.uk/about-us/our-governance	
	- We have developed our strategy for 2020 to 2025 to be aligned with our purpose and values and our corporate governance framework. - We review progress on cultural change in the monthly performance report to the board as well as progress against targets including on customer satisfaction, vulnerability, engagement and responsible business.	On how our governance helps deliver our strategy on page 56.
Objective 2	How we meet the objectives	Read more
The Appointee has an effective board with full responsibility for all aspects of the Appointee's business for the long-term.	The board has full responsibility for all aspects of the company's business and sets the company's strategic aims, purpose, values and the overall culture and standards of behaviours. It balances the long-term and short-term interests of the company.	On our board and committees composition and role on page 131
	Decisions for the overall management of the company are made by the board. There are no matters reserved for shareholders or parent companies. There is ongoing dialogue with shareholders representatives which allows the board to take account of investors' interests as well as all other relevant interests.	
	We maintain a compact board that facilitates discussion and independent non-executive directors are the largest group on our board.	
	The board has procedures in place to identify and avoid conflicts of interest.	On how we avoid conflicts of interest on page 127.
	Our core responsibilities include planning for future water resources and for events such as droughts while investing efficiently and protecting the environment. The board as a whole is responsible for developing the strategy and approving the business plan, corporate plan, water resources management plan and dry weather plan.	

BOARD LEADERSHIP AND COMPANY PURPOSE continued

HOW WE MEET THE OBJECTIVES OF THE BOARD LEADERSHIP,
TRANSPARENCY AND GOVERNANCE PRINCIPLES (BLTG) continued

Objective 3	How we meet the objectives	Read more
The board of the Appointee's leadership and approach to transparency and governance engenders trust in the Appointee and ensures accountability for their actions.	OUR GENERAL APPROACH TO TRUST, TRANSPARENCY AND GOVERNANCE	
	This annual report explains our purpose and strategy, how we operate to meet the targets we set ourselves to deliver the public water service to our customers, and how we have performed against these.	
	TRANSPARENCY ON OUR PERFORMANCE	
	- Every year, we publish a performance, people, planet report with information on our performance and our corporate social responsibility in a clear and accessible format. - Our performance, people and planet report is available at southeastwater.co.uk/performance	
	With the help of our staff, we have chosen 10 responsible business commitments to deliver benefits to customers, society and the environment that go beyond our core public water services.	
	- Our annual reporting on performance against the performance commitments is prepared following rigorous internal control processes and external assurance with oversight from the audit and risk committee and the board to ensure it is accurate, transparent and reliable. We also publish our company monitoring framework which sets out what we do to ensure that the data and information we publish is reliable, transparent, timely and appropriate to the audience. We publish our strengths, risks and weaknesses statement and the subsequent draft assurance plan we have developed in order to address any risks that have been identified. - Our company monitoring framework is at southeastwater.co.uk/cmf	On how we ensure the accuracy and reliability of our data and reporting in our data assurance summary in our APR.
	TRANSPARENCY ON OWNERSHIP, EXECUTIVE PAY AND DIVIDENDS	
	Ownership structure: We explain our group and ownership structure and provide information about our investors.	On our structure and investors on page 71.
	- Executive pay: The pay of our executive directors includes a variable element which is based on actual performance against our performance commitments. - Our directors' remuneration report has been updated to provide increased transparency on executive remuneration in line with the requirements applicable to quoted companies.	Our directors' remuneration report on page 142.
	- Dividends: We pay dividends to our shareholders only in accordance with our dividend policy and the principles that the dividends do not impair our ability to finance our business and that dividends are expected to reward efficiency and the management of economic risk. When paying dividends we consider the overall performance and financial resilience of the company which also depends on its performance against its commitments and the level of reward or penalty under the outcome delivery incentives. - Our dividend policy for 2020 to 2025 is available on our website at southeastwater.co.uk/ourgovernance.	On our dividends and how we have applied our dividend policy on pages 172 and 268.

Objective 4	How we meet the objectives	Read more
The board of the Appointee and their committees are competent, well run, and have sufficient independent membership, ensuring they can make high quality decisions that address diverse customer and stakeholder needs.	BOARD AND COMMITTEES EFFECTIVENESS	
	- One of the main ways we ensure the effectiveness of our board and committees is to maintain a strong proportion of independent non-executive directors. This ensures that considerations relevant specifically to investors or the group as a whole do not dominate decision making at the board of South East Water and that independent challenge at the board of the company is effective. - We keep a compact board which facilitates discussions at board meetings. Our board has four independent non-executive directors which is the largest group, two shareholder nominated directors and from 1 August 2020, the number of executive directors has been reduced to two.	On our board and committees composition and role on page 131.
	We ensure that our board and committees have the appropriate mix of skills and experience including specific customer and service sector experience.	On the experience of our directors on page 114.
	BOARD EVALUATION	
	We carry an annual board evaluation to review how effectively the board operates and discuss suggestions for improvement. The board evaluation is usually conducted via a non-attributable questionnaire with the results collated by the Company Secretary and discussed by the board.	On our 2020 board evaluation on page 136.

BOARD LEADERSHIP AND COMPANY PURPOSE continued**THE ROLE OF THE BOARD AND OF ITS COMMITTEES****LONG-TERM SUSTAINABLE SUCCESS**

The board's aim is to ensure that the company meets its responsibilities as a provider of an essential public service and maintains a reputation of high standards of business conduct. It provides leadership within a framework of prudent and effective controls and ensures that the necessary financial, operational and human resources are in place.

In doing so the board considers the long-term consequences of its decisions and the appropriate balance that must be achieved between the expectations of customers, employees and stakeholders, the impact of the company on the environment and communities and the need to act fairly between members of the company.

The board has regard to the duties of directors under section 172 of the Companies Act 2006 and seeks to give due consideration to and find the appropriate balance between the various interests relevant to its decisions. Further details are set out in the section 172 statement on page 82.

The systems of risk management and controls described in the strategic report, the engagement with customers and initiatives on affordability and vulnerability and our responsible business committee overseeing the delivery of our ESG practices and of our responsible business commitments are examples of how these principles are concretely applied by the board to meet its overarching objectives.

Short-term decisions are taken in the context of the overall strategy as defined in the corporate plan, the supporting delivery plans and the actual performance against targets or other strategic outcomes at any given time. They are evaluated by reference to their impact on the delivery of the commitments and long-term objectives of the company and any trade-offs that may arise between the delivery of certain commitments.

Significant decisions such as those relating to investment and the delivery of the capital programme are taken within internal governance processes which also consider commitments, legal obligations and the delivery of efficiencies.

The board receives regular updates on performance against targets in respect of all the company's commitments and short-term decisions are assessed in the context of that performance taking corrective actions where necessary.

The board endeavours to reach unanimous decisions taking account of the views of all directors.

LEADERSHIP OF THE STANDALONE REGULATED COMPANY

All matters pertaining to the business of the company are considered and decided by the board of South East Water and there are no matters reserved to shareholders or parent companies other than those requiring a resolution of members under the Companies Act 2006.

Shareholders typically discuss their respective positions in respect of matters that are a specific concern to them at board meetings of HDF (UK) Holdings, the ultimate UK holding company of South East Water and will also discuss any relevant matters with the chair of the board and management. The arrangements between shareholders relating to their decision making in relation to South East Water recognise the specific requirements applicable to South East Water as a regulated water company and the need to operate in compliance with them.

The board includes two shareholder representatives who are able to communicate the views of shareholders for consideration by the whole board when making decisions that may be of particular concern for shareholders. Where shareholder representatives have reached different conclusions in respect of a decision being considered by the board, they present their reasons and the board as a whole (with independent non-executive directors being the largest group) decides, with each director having one vote.

Our shareholders recognise that strong environmental, social and governance performance protects the long-term value and sustainable success of the company and strengthens its licence to operate. There is a strong alignment between our shareholders' governance and ours as both are focused on long-term value creation.

HOW OUR BOARD, COMMITTEES AND EXECUTIVE TEAM OPERATE

The diagram below shows the roles of our board and its committees and of the executive team and the main management steering group.

BOARD

CHAIR: NICK SALMON

Is responsible for the long-term success of the company. It sets strategy within a framework of effective controls and ensures the company has the necessary financial and human resources. It sets our purpose, values and standards of governance and it monitors compliance with regulatory and statutory obligations. It balances the interests of customers, the environment, shareholders and stakeholders.

CHIEF EXECUTIVE OFFICER DAVID HINTON

EXECUTIVE TEAM

CHAIR: DAVID HINTON

The Executive Team under the direction of the CEO comprises the CFO, Regulation and Strategy Director, Customer Services Director and Operations Director. It defines and implements the strategy, manages the operational and financial performance of the company, and matters not reserved to the board.

CUSTOMER INSIGHT COMMITTEE

Monitors the progress and effectiveness of our customer engagement and insight programme across all areas of the business to improve the satisfaction of our customers including vulnerable customers and stakeholders. It monitors how effectively this influences our day-to-day business. One of its members is an independent non-executive director.

COMPETITION AND REGULATORY STRATEGY

Our Wholesale Markets Steering Group and the Regulatory Strategic Group provide oversight of the implementation of competition and regulatory strategies including compliance with markets requirements and our main regulatory plans. They also review and define management's strategy proposals to the board.

CORPORATE SECURITY

The Corporate Security Steering Group monitors the implementation and effectiveness of security measures and policies covering all aspects of security: information and data protection, cyber risks, physical security and prevention of fraud. It monitors emerging threats and opportunities to improve resilience.

AUDIT AND RISK COMMITTEE

CHAIR: CHRIS GIRLING

Exercises oversight over financial statements and reports to the board on significant aspects of financial reporting. It reviews the scope and results of financial audits, accounting policies and judgements. It assesses the systems of internal control and risk management and the prevention and detection of fraud and reviews whistleblowing arrangements.

REMUNERATION COMMITTEE

CHAIR: JOHN BARNES

Reviews the remuneration policy for the executive directors and ensures executive pay rewards performance in areas that are important to customers. It determines the remuneration package of executive directors, and other designated senior executives including the design and application of any performance based remuneration.

NOMINATION COMMITTEE

CHAIR: NICK SALMON

Reviews the structure and composition of the board taking account of the board evaluation, succession planning of the board and senior management. It makes recommendations on proposed board appointments and committees' membership.

RESPONSIBLE BUSINESS COMMITTEE

CHAIR: RACHEL DREW

It assists the board in defining its strategy relating to environmental, social and governance (ESG) matters and in reviewing the practices and initiatives of the company relating to ESG matters ensuring they remain effective and up to date. It monitors performance against the company's responsible business commitments.

HEALTH & SAFETY

The Health & Safety committee monitors the effectiveness of health and safety practices, policies, procedures, training and communication. It analyses safety audit reports and through sub-committees ensures practices are adapted to the different areas of the business.

INVESTMENT

The Executive Investment Committee approves and ensures the government of capital investment and the Programme Management Office controls the delivery of capital expenditure. The Information Systems Steering Group approves and monitors key procurement activities.

OUTCOMES DELIVERY

The Every One Counts Steering Group and the Responsible Business Steering Group monitor the implementation of our people initiatives and of our responsible business commitments and related corporate plan objectives and business improvement initiatives.

WATER QUALITY

The Water Quality Strategy Group monitors water quality performance and the delivery of the water quality strategy and improvement initiatives. It also oversees the development of future investments in water quality.

BOARD LEADERSHIP AND COMPANY PURPOSE continued**THE ROLE OF THE BOARD AND OF ITS COMMITTEES** continued**ALIGNING OUR STRATEGY WITH OUR PURPOSE AND VALUES**

Our overall strategy as set out in our business plan and corporate plan was based on engagement with customers and addresses the key elements of our purpose (i) our core purpose as a provider of the public water service, (ii) our wider societal and environmental goals, (iii) a stakeholder inclusive approach.

Our corporate plan is centred on delivery for customers and is intended to cover all the different aspects of our business and as particularly relevant to fulfilling our purpose includes:

- a comprehensive customer engagement and vulnerability strategy with a significant increase in customers supported through our social tariff and priority services register
- stretching core services performance targets requiring significant improvement compared with AMP 6
- ten new responsible business commitments being part of our wider renewed approach to ESG which is governed by our Responsible Business committee
- a comprehensive people plan to ensure our people and culture are focused on delivering our public service and that we have a positive culture promoting diversity where our people are motivated and feel supported by the company
- a continued focus on health, safety and wellbeing with an increased focus on mental health
- a focus on environmental excellence relying on an inclusive approach to delivery through partnerships
- our carbon reduction strategy and new roadmap to net zero
- the introduction of natural capital accounting
- a focus on openness and inclusiveness with industry collaboration, stakeholder engagement, innovation through our internal platform and through cooperation with third parties

INFORMATION AND SUPPORT

The board receives as a minimum monthly performance reports to ensure that directors are regularly informed of performance. The monthly report covers all aspects of performance including performance against key regulatory obligations and outcome delivery incentives.

Directors also receive specific updates and reports as appropriate at and outside of scheduled board meetings. This includes detailed reports on specific metrics or updates on significant operational events. Senior executives also regularly present board items and updates on their particular areas to ensure that the board receives the information it needs and is able to ask questions directly and provide challenge or ask for additional information.

Directors raise questions directly with the executive directors when there is no scheduled board meeting or raise questions at the following board meeting. These are routinely addressed through written explanations and/or meetings with members of the executive team or senior managers to discuss specific topics.

The board has also decided to have an engagement programme with a wider range of people in the business beyond executive directors and senior managers to have a better understanding of how the company operates at all levels, get direct feedback and better understand the culture of the business.

There are processes in place to ensure the accuracy of the information relied on to measure performance and report on it. The board relies on the company monitoring framework which describes the internal processes to ensure the accuracy and reliability of the information published by the company. It also relies on external assurance of the company's reporting and underlying data to assess the reliability of the information provided to it.

CONFLICT OF INTERESTS

The avoidance of conflicts of interest requires constant consideration for all decisions by the board, the approach followed by the company combines standard and regular checks and communication by the relevant directors who will have direct knowledge of changes in circumstances that could create a potential situation of conflict.

The directors' induction pack includes information on directors' duties including to avoid conflicts of interest.

There is a standard item at each board meeting to consider any potential conflicts of interest in relation to the matters to be discussed at the meeting.

Each director is also required to notify any potential conflict of interest and to inform the Company Secretary and other directors of any new appointment or directorship. Relevant provisions are included in the letters of appointment of directors.

Directors' other commitments and directorships are reviewed annually to ensure records are kept up to date and that potential situations of conflict can be more easily kept under review and identified.

The articles of association of the company include provisions permitting directors to authorise certain potential conflict situations.

BOARD ACTIVITIES IN 2020/21

During the period from 1 April 2020 to 31 March 2021 there were seven scheduled board meetings, including one meeting specifically dedicated to strategy. The board also receives a full performance report every month.

From the first lockdown in 2020 we received regular updates and had bi-weekly board updates by video conference to follow up our response to the crisis. A series of board papers on our ongoing assessment of the operational, legal and financial consequences of the impact of the Covid-19 outbreak were considered. At the beginning of the financial year there were four additional meetings dedicated to Covid-19 in April, May and June 2020.

At the strategy session in October 2020 we considered in detail our People Plan setting out our strategy relating to our workforce and culture, the corporate plan implementation for the 2020 to 2025 regulatory period and the actions plans for the delivery of ODIs and the delivery of investment. We considered a presentation on the impact of Covid-19 on water companies and on the final determination. We received an update on the referrals of the price determinations to the CMA and considered possible implications for PR24. We discussed current and future industry issues with Christine McGoutry, CEO of Water UK. We also considered how to improve awareness of the company's brand and how this may relate to C-MeX and customer satisfaction.

BOARD LEADERSHIP AND COMPANY PURPOSE continued**ATTENDANCE AT BOARD AND COMMITTEE MEETINGS IN 2020/21**

Director	Board	Audit & risk	Nomination	Remuneration	Responsible business
N Salmon	7/7		2/2	3/3	
J Barnes	7/7	3/3	2/2	3/3	3/3
C Girling	7/7	3/3			
C Pronto	7/7	3/3	2/2	3/3	
M Szczepaniak	7/7	3/3	2/2	3/3	3/3
R Drew	7/7	3/3	2/2	3/3	3/3
P Butler – R: 31/07/2020	2/2				
A Farmer	7/7				
D Hinton	7/7				3/3

R – Resigned

**SUMMARY OF OUR ACTIVITIES
IN 2020/21****SERVICE DELIVERY AND OPERATIONAL
PERFORMANCE**

- considered regular updates at board meetings, additional video conferences and email updates of the management of the impact of the Covid-19 pandemic to ensure a continuous service to critical facilities and all our customers whilst maintaining the safety of our workforce and the public
- regularly reviewed performance against our operational commitments and outcome delivery incentives and the initiatives taken to ensure we meet our targeted performance
- considered the annual review of our water quality performance for AMP6 and for the current year. Considered the actions taken to deal with the impact of Covid-19 on water quality activities. Considered the actions taken in respect of notices issued by the DWI and progress in the delivery of related action plans. Considered the key recommendations of the DWI and lessons learnt highlighted in their annual report and how to address them
- considered the annual report on the delivery of our capital programme and capital expenditure in 2019/20, on our capital programme for 2020/21 as well as updates on the progress of the main schemes taking account of the impact of Covid-19
- reviewed the retendering of our contract for engineering and consultancy services and the alignment of the contract requirements with our operational needs and performance targets. Considered the management of mobilisation and transition risks following the award of the contract to Atkins, our new engineering and asset management delivery partner
- considered the organisational changes implemented in Operations. Considered regular reviews of operational performance in the context of Covid-19 and the operational response to high water demand related to the pandemic and the preparation for summer peak demand
- considered the lessons learnt from the supply interruptions during the heatwave that affected the south of England in August 2020. Considered the need for local resilience issues to be dealt with as part of the WRMP process and we would promote this approach
- reviewed our retail performance including an overview of the organisational and process changes implemented, the impact of Covid-19, C-MeX and other ODIs performance, and future initiatives

FINANCIAL, REPORTING AND TRANSACTIONAL

- considered financial forecasts throughout the financial year to monitor the impact of Covid-19 on the financial performance and resilience of the company
- reviewed and approved the annual report and financial statements for 2019/20 including the viability statement prepared in line with specific requirements set out by Ofwat. Reviewed and approved the half-year financial reporting for 2020/21
- reviewed and approved our annual performance report and other regulatory reporting for 2019/20
- considered the report from the audit and risk committee on the audit plan, the independence of the auditors, the audit fees and on new reporting requirements for the 2020/21 annual report. Approved the audit and non-audit fees. Considered the update from the audit and risk committee on the tender process for audit services
- approved our revised dividend policy taking into account the expectations formulated by Ofwat at PR19. Considered and approved dividends for the 2020/21 financial year
- approved the repayment to the company of the loan to its immediate holding company to simplify the company's financial structure and approved the related special restructuring dividend
- considered the budget assumptions and approved the financial budget for 2021/22 and the update to the corporate plan
- considered a STID proposal under the company's finance documents to improve liquidity and financial resilience in the context of Covid-19 including the ability to draw down additional debt under certain trigger event conditions
- considered an update on non-regulated business activities

ESG, RISK MANAGEMENT AND STAKEHOLDER ENGAGEMENT

- reviewed the composition of the board and its committees. Approved the renewal of the appointment of Chris Girling, Nick Salmon and Célia Pronto
- carried out the annual evaluation of the board's effectiveness through an anonymous online questionnaire, discussed the points arising and agreed follow up actions
- met with Zoe McLeod, Chair of the Customer Challenge Group (CCG), to discuss the work of the CCG during 2020 to 2025 including the key activities agreed with the CCG and how it would be holding the company to account for its commitments in the business plan. Considered areas for potential development and improvements in customer and stakeholder engagement highlighted by the CCG
- considered the annual update on human resources and the workforce engagement and changes to working practices implemented to deal with Covid-19. Considered the presentation of the People Plan setting our strategy on workforce related matters for 2020 to 2025
- considered the annual health, safety and wellbeing performance review and considered the effectiveness of our Thrive 365! strategy and related initiatives. Reviewed the initiatives implemented in 2019/20, the programme of actions for 2020/21 including continued implementation of our mental health strategy
- adopted our modern slavery statement and reviewed the related procedures implemented to ensure compliance with legislation on modern slavery
- considered developments in corporate governance and the related requirements of Ofwat's board leadership transparency and governance principles as well as those of the 2018 UK Corporate Governance Code. Adopted a new corporate governance framework, our company purpose and new articles of association embedding our company purpose and revising directors' duties to include fulfilling the company's purpose

BOARD LEADERSHIP AND COMPANY PURPOSE continued**ESG, RISK MANAGEMENT AND
STAKEHOLDER ENGAGEMENT** continued

- reviewed and approved our pay gap reporting and the actions to take to address gender pay gap including related initiatives in our People Plan
- reviewed the water industry and the company's preparation for a no-deal Brexit and the coordination with Defra. Reviewed the implementation of the industry's and company's risk management plans relating in particular to the supply of chemicals, additional stocks of chemicals and equipment, and the coordination with suppliers and emergency services
- considered the annual review of our information technology systems and infrastructure and of our information technology strategy. Reviewed cyber security processes and compliance with the Network and Information Systems Regulations (NIS). Considered the changes to related risks arising from Covid-19 and the increased reliance on IT Systems for remote working
- reviewed our insurance programme and the renewal of the policies and benchmarking. Approved the subscription of a cyber liability policy
- carried out the annual review of risks and of the effectiveness of our risk management process
- considered plans for controlled return to the office and the future implementation of flexible working
- considered the board engagement programme with the workforce, the CCG and stakeholders

STRATEGY AND REGULATION

- considered the key issues raised in the referrals of Ofwat's determinations to the CMA and the company's own submissions to the CMA in relation to these referrals
- approved the approach for setting and assuring our wholesale and household end-user charges taking account of customers' preference for bill stability and seeking to control increases in bills and the impact on customers. Approved our indicative and final wholesale charges, our household end-user charges and our new connection charges and infrastructure charges for 2021/22 and the related board assurance statements. Set detailed conditions for the delegation of authority of the final calculation of the charges following publication of the relevant RPI and finalisation of the charges documents
- reviewed and approved the update of the Company Monitoring Framework 2020/21 and assurance plan
- considered and approved the consent of the company to the modification of condition B of its licence in relation to the RFI blind year adjustment
- considered the report from Frontier Economics on the impact of Covid-19 on water companies and on final determinations
- considered proposals to improve the company's support for markets and in particular the non-household retail market
- considered the process for and progress of the preparation of the Water Resources Management Plan and dry weather plan. Considered specific issues relating to regional plan and the work of the WRSE including the inclusion of local resilience schemes. Approved the draft dry weather plan for submission to Defra and publication

DIVISION OF RESPONSIBILITIES AND BOARD COMPOSITION

PRINCIPLES OF OUR CORPORATE GOVERNANCE CODE RELEVANT TO THIS SECTION

- H.** The chair leads the board and is responsible for its overall effectiveness in directing the company. They should demonstrate objective judgement throughout their tenure and promote a culture of openness and debate. In addition, the chair facilitates constructive board relations and the effective contribution of all non-executive directors, and ensures that directors receive accurate, timely and clear information.
- I.** The board of the company and their committees are competent, well run, and have sufficient independent membership, ensuring they can make high quality decisions that address diverse customer and stakeholder needs.
- J.** The board should include an appropriate combination of executive and non-executive (and, in particular, independent non-executive) directors, such that no one individual or small group of individuals dominates the board's decision-making. There should be a clear division of responsibilities between the leadership of the board and the executive leadership of the company's business.
- K.** Non-executive directors should have sufficient time to meet their board responsibilities. They should provide constructive challenge, strategic guidance, offer specialist advice and hold management to account.
- L.** The board, supported by the company secretary, should ensure that it has the policies, processes, information, time and resources it needs in order to function effectively and efficiently.

CHAIR

The Chair ensures the effectiveness of the decision making process of the board and promotes discussion on key issues based on quality information. The Chair is also responsible for maintaining a direct channel of communication with shareholders and ensures that their concerns and objectives are taken into account and conveyed to the directors.

The Chair and the CEO meet regularly throughout the year to maintain a good communication between the board and the executive directors and to review the board forward programme and the agendas of board meetings.

There is also a formal schedule setting out the division of responsibilities between the Chair and the CEO.

BOARD BALANCE AND EFFECTIVENESS

Independent non-executive directors are the majority group on the board and on our audit and risk committee, nomination committee and remuneration committee. These committees are also chaired by an independent non-executive director. Nick Salmon, Chair of the board, is independent of management and has no link to shareholders that could affect his impartiality as required by our corporate governance code and Ofwat's principles of governance. This ensures non-executive directors play a significant role in challenging executive directors and management as well as in developing strategy. The wide range of their experience also ensures that a variety of views are considered in the board's deliberations.

The independence of non-executive directors is assessed by the board following the criteria of the UK Corporate Governance Code. Non-executive directors also meet with the chair in the absence of the executive directors at least once a year.

There are two shareholder nominated directors which ensures that there is constant communication between independent non-executive directors and shareholders and between executive directors and shareholders.

DIVISION OF RESPONSIBILITIES AND BOARD COMPOSITION continued

Since 1 August 2020 following the retirement of Paul Butler, the number of executive directors has been reduced to two with David Hinton, CEO and Andrew Farmer, CFO sitting on the board. Senior managers regularly attend board meetings to present agenda items as well as management and operational information, they also ensure operational issues are discussed by the whole board.

We believe that our board has a good mix of skills and experience and has reached a good balance between new directors and directors who have had time to acquire a good knowledge of our company and of our environment including the last price determination and our strategy and long-term plans.

The whole board has been directly involved in the preparation of our business plan and is well prepared to closely monitor the delivery of performance commitments and wider objectives in this regulatory period.

Non-executive directors and independent non-executive directors are given direct access to management as requested and review specific areas of the business directly with management drawing on their particular expertise and provide oversight and challenge on key regulatory matters or the review of the company's response to significant operational events.

Our directors' biographies can be found on page 114.

BOARD BALANCE AND COMPOSITION ON 31 MARCH 2021

Independent Non-Executive Directors	Appointment	Resignation	Term*	Audit & Risk	Remuneration	Nomination	Responsible Business
Nick Salmon (Chair)	01/04/15	na	6 yrs		☐	Chair	
John Barnes	28/01/16	na	5 yrs 2 m	☐	Chair	☐	☐
Chris Girling	30/10/14	na	6 yrs 5 m	Chair			
Célia Pronto	01/06/18	na	2 yr 10 m	☐	☐	☐	
Non-Executive Directors (shareholder nominated)	Appointment	Resignation	Term*	Audit & Risk	Remuneration	Nomination	Responsible Business
Rachel Drew (Morrison & Co)	06/12/19	na	1 yr 4 m	☐	☐	☐	☐
Marissa Szczepaniak** (Vantage Infrastructure)	08/12/16	na	4 yrs 3 m	☐	☐	☐	Chair
Executive Directors	Appointment	Resignation	Term*	Audit & Risk	Remuneration	Nomination	Responsible Business
Andrew Farmer (CFO)	01/08/15	na	5 yrs 8 m				
David Hinton (CEO)	01/06/13	na	7 yrs 10 m				☐
Resigning Directors	Appointment	Resignation	Term*	Audit & Risk	Remuneration	Nomination	Responsible Business
Paul Butler	02/10/06	31/7/20	13 yrs 10 m				

* As at 31 March 2021.

** From first appointment on 08/12/2016. Resigned as a director on 17 August 2018 and was reappointed as a director on 30 January 2019.

DIVISION OF RESPONSIBILITIES

The board has adopted a formal list of reserved matters that it must consider and approve. These matters expressly refer to the relevant corporate governance requirements, our licence and regulatory obligations as well as our statutory obligations. They also reflect the allocation of responsibilities between the board and its committees as set out in the terms of reference of the committees.

The executive team manages matters that are not reserved to the board and its committees under their supervision which is achieved through regular reporting and specific updates. The main decisions delegated to management are taken after consideration by the executive team which includes the CEO, CFO, Regulation and Strategy Director, Customer Services Director and Operations Director. There are several steering groups which deal with key aspects of the business.

BOARD COMMITTEES

NOMINATION, REMUNERATION AND AUDIT AND RISK COMMITTEES

The audit and risk committee, nomination committee and remuneration committee are chaired by and have a majority of independent non-executive directors as required by our corporate governance code.

Board committees have formal terms of reference. Chris Girling, the Chair of the audit and risk committee, has recent and relevant financial experience. We have approved a formal schedule describing specifically the allocation of responsibilities and interactions between the board and the audit and risk committee.

RESPONSIBLE BUSINESS COMMITTEE

Our responsible business committee was formally constituted on 7 March 2019 and its terms of reference approved by the board.

The main purpose of the responsible business committee is to assist the board in defining its strategy relating to environmental, social and governance (ESG) matters and in reviewing the practices and initiatives of the company relating to ESG matters ensuring they remain effective and up to date.

The responsible business committee also oversees the execution of our ESG strategy and initiatives and will monitor performance against the responsible business commitments in our business plan.

The responsible business committee will ensure that the board maintains a primary focus on customer engagement, our communities and the environment.

The responsible business committee was chaired by Marissa Szczepaniak until 31 May 2021 and has three other director members: John Barnes, Rachel Drew and David Hinton. Rachel Drew succeeded to Marissa Szczepaniak as chair of the committee on 31 May 2021. Non-director members of the committee ensure that a wide range of skills and knowledge is represented on the committee and provide a clear line of sight into the business. The appointment of representatives of shareholders (Vantage Infrastructure and HRL Morrison & Co), reflects the emphasis placed by shareholders on strong ESG performance.

You will find the terms of reference of our responsible business committee and more information on governance on our website at



southeastwater.co.uk/ourgovernance

Read more online. You will find our business plan and the responsible business appendix on our website at



southeastwater.co.uk/businessplan2020

RELATIONSHIP WITH SHAREHOLDERS AND INVESTORS

Communication with shareholders is facilitated, as South East Water is a private limited company, with shareholder nominated non-executive directors on the board.

It is important that the board appreciates the requirements of shareholders and equally that shareholders understand how the actions of the board and financial performance relate to the achievement of South East Water's long term goals.

The reporting calendar is dominated by the publication of interim and final results each year, in which the board reports to shareholders and stakeholders on its stewardship of South East Water. At other times during the year, presentations to rating agencies and updates to the stock exchange are made available to all. The Chair ensures that the CEO and CFO provide feedback to the board following presentations to investors and meetings with shareholders.

APPOINTMENT, SUCCESSION AND EVALUATION

PRINCIPLES OF OUR CORPORATE GOVERNANCE CODE RELEVANT TO THIS SECTION

- M.** Appointments to the board should be subject to a formal, rigorous and transparent procedure, and an effective succession plan should be maintained for board and senior management. Both appointments and succession plans should be based on merit and objective criteria and, within this context, should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths.
- N.** The board and its committees have the appropriate balance of skills, experience, independence and knowledge of the company. Consideration should be given to the length of service of the board as a whole and membership regularly refreshed.
- O.** Annual evaluation of the board should consider its composition, diversity and how effectively members work together to achieve objectives. Individual evaluation should demonstrate whether each director continues to contribute effectively.

REPORT FROM THE NOMINATION COMMITTEE

COMMITTEE MEMBERS

Nick Salmon (Chair) Independent Non-Executive Director
John Barnes Independent Non-Executive Director
Célia Pronto Independent Non-Executive Director

Rachel Drew Non-Executive Director
Marissa Szczepaniak Non-Executive Director*
Anne-Noëlle Le Gal Non-Executive Director*

*Anne-Noëlle Le Gal replaced Marissa Szczepaniak on 18 June 2021

Following a formal interview process conducted by a panel comprising the Chair of the nomination committee and the shareholder representatives last year, David Hinton was unanimously appointed CEO and succeeded Paul Butler from 1 August 2020.

Last year also saw the renewal of the executive team with the appointment of a new Customer Service Director, Operations Director and Regulation and Strategy Director through internal succession planning.

Over the last 12 months:

- We recommended the renewal of the appointment of Chris Girling as an independent non-executive director and Chair of the audit and risk committee which was approved by the board for a period of three years until 29 October 2023.
- We recommended the renewal of the appointment of Célia Pronto as independent non-executive director and member of the nomination committee, audit and risk committee and remuneration committee which was approved by the board for a period of three years until 31 May 2024.
- The committee recommended the renewal of my appointment as Chair of the board and of the nomination committee and as a member of the remuneration committee which was approved by the board for a period of one year until 31 March 2022. I did not take part in any deliberations concerning my own appointment.
- The committee concluded that the non-executive directors whose appointments were renewed continued to satisfy the criteria of independence set out in our corporate governance code.
- The appointment of Anne-Noëlle Le Gal, from Vantage Infrastructure, to replace Marissa Szczepaniak, as shareholder nominated non-executive director was recommended by the nomination committee and approved by the board and became effective on 18 June 2021. Anne-Noëlle Le Gal became on the date of her appointment a member of the nomination committee, audit and risk committee, remuneration committee and responsible business committee and from 31 May 2021. Rachel Drew succeeded Marissa Szczepaniak as Chair of the responsible business committee.
- The whole board reviewed the company's initiatives on diversity and gender pay gap and succession planning in our People Plan. There is more information on gender pay gap at corporate.southeastwater.co.uk/news-info/publications/gender-pay-gap-report
- The committee reviewed its effectiveness as part of the overall board evaluation process and the members of the committee and directors were satisfied that it is operating effectively in accordance with its terms of reference.

Looking ahead, the committee and the board as a whole considered the progressive replacement of independent non-executive directors in a way that will ensure continuity of knowledge and experience on the board and the optimum phasing of new appointments having regard to the regulatory cycle of the company and in particular the preparation of the next price review.

In this context the decision was made that I would remain Chair for another year during which the search for a new Chair will take place. This will ensure that after a handover period my successor will have time to settle in before the next price determination process takes place. We will follow a similar approach for the succession of the other independent non-executive directors over the next few years.

NICK SALMON
 CHAIR
 15 JULY 2021

APPOINTMENT, SUCCESSION AND EVALUATION continued**BOARD EVALUATION**

Our board evaluation was carried out by means of a confidential online questionnaire. The results were collated and summarised by the Company Secretary on a non-attributable basis and the Chair led a discussion on the conclusions to draw from the survey results and recommendations for change or improvement. The discussions related more particularly to questions which had received a relatively lower score and comments made by directors highlighting specific issues or suggestions.

The questionnaire covered the performance of the board and its committees reflecting key aspects of our corporate governance code including compliance with the board leadership, transparency and governance principles. The questionnaire also incorporated questions from the Sustainability First "Check-list for energy and water board effectiveness" in line with our responsible business commitments and questions from the City Values Forum "Governing culture: an agenda for boards" on the alignment of decision making with the company's purpose and values, and on culture and the promotion of behaviours the board wishes to encourage.

The questionnaire also included open questions on the working and effectiveness of the board and committees in fulfilling their roles. Each committee also considered its own practices against its terms of reference and the committee Chair's report on their findings in their respective sections of this corporate governance statement.

At the 2020 board evaluation the board discussed diversity and acknowledged that the gender balance on the board had improved. However, there was more to do to in considering diversity of the whole organisation and whether the company reflected the ethnic diversity of the communities it served. The board also wished to have more visibility and direct engagement with different levels of the business and a board engagement programme was developed allowing more interaction by the board and individual directors.

At the 2021 board evaluation directors highlighted the need for a better understanding of succession planning especially of the succession pipeline from managers to senior managers. The People Plan that had been presented to the board included a work stream on succession planning and a plan for the succession of the executive team and the senior management team would be presented to the directors.

It was acknowledged that issues of diversity were being addressed in the People Plan and especially how the diversity of employees reflected the diversity of the catchment. It was agreed that specific work would be done as part of the People Plan to improve job opportunities for disabled employees as the employee population was not reflective of the wider population.

The board discussed the planned succession of the two shareholder representatives and the renewal of the Chair over a relatively short time period. The proposed appointment of Anne-Noëlle Le Gal would provide an element of continuity but it was agreed that particular care would need to be taken over the next year to ensure new appointees on the board receive appropriate induction and continuing support and information to allow them to acquire the knowledge and understanding of the business that is required to contribute effectively to the deliberations of the board.

The 2021 board evaluation concluded that the board and its committees were operating effectively.

COMMITMENT

The expected commitment including outside scheduled board meetings when required is reviewed as part of the appointment process of the non-executive directors. The terms of appointment of non-executive directors do not include a set, expected time commitment but instead include an undertaking that the director will dedicate sufficient time to discharge his or her responsibilities. None of our non-executive directors has raised concerns over the time required to fulfil their duties and this aspect is also considered in the board evaluation process.

The Chair's and directors' other commitments were disclosed and considered prior to appointment and have not materially changed since their appointment. Details on the Chair's and directors' other commitments can be found on page 114.

At the beginning of 2021 Nick Salmon became Chair of the board of Scotia Gas Network Limited and Céla Pronto became a non-executive director of Samworth Brothers. The board was satisfied that these new commitments would not affect their ability to fulfil their respective roles of Chair and independent non-executive director of the company and to dedicate the time required to fulfil their duties as directors of the company.

INDUCTION

On joining the board each director receives a detailed, tailored induction programme which is supplemented as needed to ensure that the director's knowledge, familiarity with South East Water and our industry are maintained at the appropriate level. The induction programme includes meetings with senior managers and visits to production sites and other facilities away from the head office. Such visits give directors the opportunity to speak to a wider group of employees and contractors. The feedback provided by Ofwat following their pre-appointment interview is also incorporated into the induction programme.

TRANSPARENCY, AUDIT, RISK AND INTERNAL CONTROL

PRINCIPLES OF OUR CORPORATE GOVERNANCE CODE RELEVANT TO THIS SECTION

- P.** The board should establish formal and transparent policies and procedures to ensure the independence and effectiveness of internal and external audit functions and satisfy itself on the integrity of financial and narrative statements.
- Q.** The board of the company's leadership and approach to transparency and governance engenders trust in the company and ensures accountability for their actions.
- R.** The board should present a fair, balanced and understandable assessment of the company's position and prospects.
- S.** The board should establish procedures to manage risk, oversee the internal control framework, and determine the nature and extent of the principal risks the company is willing to take in order to achieve its long-term strategic objectives.

TRANSPARENCY AND REPORTING

The board and the audit and risk committee ensure that the business, financial and regulatory reporting of South East Water is transparent and informative and accurately reflects material issues and describes our business model, strategy and performance.

Our annual reporting on performance against the performance commitments in our final determination is prepared following rigorous internal control processes and external assurance with oversight from the audit and risk committee and the board.

Our processes to ensure the accuracy and reliability of our data and reporting are described in the board statement on accuracy and completeness of data and information in our annual performance report.

We also maintain and publish our company monitoring framework which sets out what we do to ensure that the data and information we publish is reliable, transparent, timely and appropriate to the audience. We publish our strengths, risks and weaknesses statement and the subsequent draft assurance plan we have developed in order to address any risks that have been identified.

Our company monitoring framework is available



southeastwater.co.uk/cmef

RISK MANAGEMENT AND INTERNAL CONTROLS

The board is responsible for defining the risk management strategy and processes including the risk register and the identification of the principal risks. It also carries out an annual review of the effectiveness of the risk management and internal control systems (financial, operational and compliance), of the principal risks and of the prospects of our company. Our risk management process is described in the strategic report.

The audit and risk committee plays a key role in the ongoing monitoring of the adequacy and effectiveness of the internal controls and risk management systems established by the board. This involves reviewing the ability to identify and manage new risk types, ensuring effective controls are embedded into management and governance processes, and continuously monitoring risks with relevant items at each meeting. The audit and risk committee also ensures that appropriate audit work is carried out on risk management.

REPORT FROM THE AUDIT AND RISK COMMITTEE

COMMITTEE MEMBERS

Chris Girling (Chair) Independent Non-Executive Director
John Barnes Independent Non-Executive Director
Célia Pronto Independent Non-Executive Director

Rachel Drew Non-Executive Director
Marissa Szczepaniak Non-Executive Director*
Anne-Noëlle Le Gal Non-Executive Director*

*Anne-Noëlle Le Gal replaced Marissa Szczepaniak on 18 June 2021.

I am pleased to report on the work of the audit and risk committee since 1 April 2020 and in relation to this annual report for 2020/21.

- We reviewed the half-year group financial reporting and this annual report for 2020/21 and recommended their approval by the board.
- We considered the prospects of South East Water for the purpose of both the going concern statement by the directors and the longer term viability described in the long-term viability statement. We had regard in particular to the impact of both the Covid-19 outbreak and the PR19 final determination on the prospect of the business to 2025 and beyond and throughout the whole lookout period. Our assessment considered how our downside sensitivities would change if our trading activities and cash collections were impaired in the current and future financial years. We have recommended that the board maintain a lookout period of 10 years for its long-term viability statement. We have also considered and made recommendations to the board on the appropriate nature and extent of stress testing to be used to assess the future prospects of South East Water. Our principal risks and our long-term viability statement are set out in the strategic report.
- We have paid particular attention to ensure that our reporting on our outcome delivery incentives accurately reflects South East Water's performance in the year and on the quality and quality assurance of the data used for our reporting.
- We considered the report of the auditors including their review including internal controls and management override.
- We considered the impact of Covid-19 on our key judgements and estimates in the financial statements, in particular the impact on our debtor book and expected credit loss adjustment.
- We considered the potential impact of exceptional items arising from damage to assets and commercial and legal claims.

FINANCIAL STATEMENTS AND ANNUAL PERFORMANCE REPORT

• Audit plan

The committee reviewed the audit plan with the auditors and was satisfied that it covered the key issues. We reviewed the proposed significant audit risks typical of a water company and the areas of audit focus.

• Fair, balanced and understandable

The committee has reviewed this annual report and financial statements and the regulatory reporting in order to assess whether they present a fair, balanced and understandable assessment of South East Water's and the group's position and prospects. We reviewed the relevant specific notes and explanations to the financial statements to ensure they provided clear explanation of accounting policies and technical matters. Following this review, we recommended to the board that, taken as a whole, the group annual report 2020/21 is fair, balanced and understandable.

We also reviewed the report from Atkins, our external assurance partners, on our regulatory reporting and recommended to the board the approval for publication of our regulatory reporting, cost assessment tables and our performance, people and planet report.

TRANSPARENCY, AUDIT, RISK AND INTERNAL CONTROL continued

REPORT FROM THE AUDIT AND RISK COMMITTEE continued

SIGNIFICANT JUDGEMENTS AND SOURCES OF ESTIMATION UNCERTAINTY CONSIDERED

- **Revenue recognition**

A significant proportion of water supplied to our domestic and our smaller commercial customers remains unbilled at the end of the financial year. As such judgements and estimates are made in respect of the value of unbilled water revenue. These estimates are based on previous consumption levels and are validated to ensure that the assessments are reasonable taking account of the impact of Covid-19 experienced during the year.

- **Bad debt provisioning**

Our trade receivables balance includes a provision for bad debt, which is our assessment of debts that will be unpaid by our customers. The provision is based on the application of expected recovery rates to our aged debt balances using specific data for household and for non-household debt. Our cash collection history over the past three years has been used to determine future collection rates. This marks a change from the prior year where cash collection history over the past four years has been used. This change in approach is as a result of Covid-19 and places a greater weight on cash collection history over the last year when Covid-19 has been a factor.

- **Classification of costs between operating and capital expenditure**

We have a significant capital programme and therefore it is important that the policies underpinning the capitalisation of expenditure are closely validated and compliant with current appropriate accounting standards. The committee ensures that the costs capitalised as fixed assets are directly attributable to capital projects.

- **Change in pension increases index (Mid Kent Pension Scheme)**

We ensured that the implementation and the accounting treatment of the change of reference index from RPI to CPI were appropriate.

- **Management override and controls**

The committee keeps the judgements and sources of estimation uncertainty under review and challenges as appropriate, typically as part of the review of the half-year accounts and the year-end audit. The board also exercises scrutiny throughout the year when reviewing the monthly management accounts in the finance report.

- **Other areas of audit and risk committee focus**

Areas of focus reviewed by the committee included the appropriateness of actuarial assumptions for the valuation of the assets and liabilities of the two defined benefit pension schemes to ensure they were within an acceptable range considering the economic environment. The other areas of audit focus were the going concern and long-term viability statement, and the impact of the sinkholes that affected a large distribution reservoir.

EXTERNAL AUDITORS

- **Audit fee**

We reviewed the audit fee proposal from the auditors for the 2020/21 audit and the justifications presented for the increase applied for the 2019/20 audit for recommendation to our board for approval.

- **Effectiveness of the external audit process**

We reviewed the effectiveness of the external audit process receiving feedback from the auditors, the CFO and the Group Financial Controller on the conduct of the audit and any issues and potential improvements. The Chair of the committee met with the auditors to discuss the audit. We were satisfied with the performance of the auditors and the effectiveness of the overall process.

• Objectivity and independence of auditors

We reviewed the objectivity and independence of the auditors considering the proportion of the total fees received by the auditors which is paid by South East Water, the duration of the appointment of the auditors, and the confirmation of independence from the auditors. We also considered the level of non-audit services relating essentially to regulatory reporting which are best provided by Deloitte to ensure consistency. The committee concluded that Deloitte remained objective and independent in their role as external auditor.

Deloitte LLP have been auditors for 11 years, an extension of their tenure being authorised by the FRC in May 2020 allowing them to carry out the audit for 2020/21. Helen Burrridge has been the Lead Audit Partner for two years.

We applied our policy on non-audit services that requires approval of non-audit work by the Chair of the audit committee or the full committee for any work in excess of £50,000.

AUDIT TENDER

- An extension of the appointment of Deloitte LLP for the financial period ending 31 March 2021 was requested due to the impact of the Covid-19 pandemic and granted by the Financial Reporting Council in May 2020 and the tendering process was extended accordingly.
- We oversaw the tender process for audit services taking account of the developments of rules relating to the provision of audit services, and the appointment is planned to be made in the middle of the financial year ending 31 March 2022.

RISK MANAGEMENT AND INTERNAL CONTROLS

- We considered whether or not an internal audit function was required. We considered the established processes in place for regulatory and performance reporting which include both internal and external assurance, the size and structure of the company and the nature of the core activities. We concluded that an internal audit function was not required at this stage and that the current combination of internal reviews of controls and systems carried out by the finance team and of specific reviews by external consultants was appropriate and allowed access to specialist skills and knowledge that it would not be cost effective to maintain internally.
- We reviewed the effectiveness of the committee as part of the board evaluation and the members of the committee and directors were satisfied that it is operating effectively in accordance with its terms of reference.
- Compared to the previous year, the focus of the board as a whole has been on the management of the risks related to Covid-19 which took priority over the review of other areas of risk management and internal control in 2020/21.

CHRIS GIRLING

CHAIR

15 JULY 2021

REMUNERATION

REPORT FROM THE REMUNERATION COMMITTEE

COMMITTEE MEMBERS

John Barnes (Chair) Independent Non-Executive Director
Nick Salmon Independent Non-Executive Director
Célia Pronto Independent Non-Executive Director

Rachel Drew Non-Executive Director
Marissa Szczepaniak Non-Executive Director*
Anne-Noëlle Le Gal Non-Executive Director*

*Anne-Noëlle Le Gal replaced Marissa Szczepaniak on 18 June 2021.

I am pleased to present the directors' remuneration report for the year ended 31 March 2021.

Our aim is to ensure that executive pay is aligned with our strategy and culture and that remuneration reflects the company's performance against clear operational and financial measures as well as individual objectives. We are keen to ensure that we link executive pay to successful business performance which is in turn linked to demonstrable customer benefits. To that end we may exercise discretion where appropriate to reflect the operating environment. We set out in the remuneration report how this has been achieved this year.

Our remuneration reporting has been expanded to improve transparency and clarity having regard to the reporting requirements that apply to quoted companies under schedule 8 of the Large and Medium-Sized Companies and Groups (Accounts and Reports) Regulations 2008 despite these not applying to the company.

I would highlight the following in respect of the activities of the committee in 2020/21:

BASE SALARY AND FEES

- We decided that the salaries of the executive directors and the other members of the executive team would be increased from 1 April 2021 by 0.6 per cent in line with the company pay award negotiated with the Staff Council.
- The fees received by independent non-executive directors were also increased in line with the company pay award.

VARIABLE PAY IN THE FINAL YEAR OF AMP6

2019/20 was the final year of AMP6 and the committee determined the awards under the executive bonus scheme with a partial deferral until January 2021, under the Commercial Director bonus scheme, and the final pro-rata award for the last year of the AMP to the three eligible participants in the Long-Term Incentive Plan (LTIP) covering the five year period from April 2015 to March 2020. These awards were disclosed in the directors' remuneration report for 2019/20.

ANNUAL INCENTIVE PLAN 2020 TO 2025

New annual incentive plan (AIP) for 2020 to 2025

- We defined the AIP as a single annual bonus scheme with deferral of a third of the annual pay-out for two years which replaces the previous annual executive bonus scheme and the previous long term incentive plan, simplifying the incentives for AMP7 and improving the alignment with the business performance objectives.
- We decided that the performance measures and targets (including the performance levels for threshold, target and stretch) under the AIP would be set annually to maintain an appropriate level of stretch and would be defined on the basis of the corporate plan approved following the final determination to ensure a focus on operational performance and delivery for customers.
- We decided that customer outcomes (including operational outcomes delivery incentives, customer satisfaction, environmental and ESG outcomes) would represent 60 per cent of the total award, the rest being allocated between financial performance (30 per cent) and personal objectives (10 per cent).



We are keen to ensure that we link executive pay to successful business performance

- We agreed that the AIP rules would include a mechanism for malus and claw back to reflect possible changes in performance and ensure that the committee would retain discretion to adjust or cancel awards where appropriate.
- We engaged external legal advisers, White & Case, to draft the rules of the AIP which we adopted in July 2020.

Operation of the AIP in 2020/21

- We considered proposals on performance measures and targets (including threshold and stretch levels) and approved the final measures and targets for the 2020/21 AIP on 2 July 2020.
- At the beginning of the financial year, we considered the potential impact of Covid-19 on performance and operation of the AIP and decided to maintain the targets initially set to maintain the focus of management on achieving the original performance objectives and that we would consider the impact of Covid-19 when assessing the potential awards at the year end.
- We reviewed the full year performance of the company in 2020/21 and that of individual executive directors, and approved the awards under the 2020/21 AIP deciding to exercise discretion to take account of the impact of additional costs due to Covid-19 on financial performance. Details on the operation of the AIP and the award for 2020/21 are provided in this directors' remuneration report.

Operation of the AIP in 2021/22

- We decided to maintain the same performance measures as in 2020/21 and updated the targets in line with our corporate plan targets for 2021/22. The details of the targets for 2021/22 are provided below in this directors' remuneration report.

GOVERNANCE

- We reviewed our approach to remuneration reporting and decided to update this directors' remuneration report having regard to the requirements applying to quoted companies and to the principles of the UK Corporate Governance Code incorporated into the company's corporate governance code.
- We reviewed the remit of the committee and how we would review the workforce remuneration and engage with the workforce. We decided that the Staff Council would be the most appropriate forum for any such engagement and that this could be taken forward by Célia Pronto as part of the planned engagement with the Staff Council as both the INED nominated for engagement with workforce and member of the committee.
- We reviewed the pay award negotiated with the Staff Council for the workforce which included a one-off bonus of £250 for all employees (excluding senior management) to recognise their commitment to public service during the pandemic and we reviewed the senior managers' bonus scheme for 2020/21 including in particular its alignment with ODIs and strategic objectives and its consistency with the executive team bonus scheme.
- We reviewed the effectiveness of the committee as part of the overall board evaluation process and the members of the committee and directors were satisfied that it is operating effectively in accordance with its terms of reference.

JOHN BARNES

CHAIR

15 JULY 2021

REMUNERATION continued**CORPORATE GOVERNANCE PRINCIPLES**

We explain below how corporate governance principles have been taken into account to define our remuneration policy.

PRINCIPLES OF OUR CORPORATE GOVERNANCE CODE RELEVANT TO REMUNERATION

- T.** Remuneration policies and practices should be designed to support strategy and promote long-term sustainable success. Executive remuneration should be aligned to company purpose and values, and be clearly linked to the successful delivery of the company's long-term strategy.
- U.** Directors should exercise independent judgement and discretion when authorising remuneration outcomes, taking account of company and individual performance, and wider circumstances.
- V.** A formal and transparent procedure for developing policy on executive remuneration and determining director and senior management remuneration should be established. No director should be involved in deciding their own remuneration outcome.

Remuneration principles

Remuneration is aligned with the company's purpose, values and vision and promotes the long term sustainable success of the company.

Remuneration is demonstrably linked to the delivery of the core purpose of the company to provide the public water service, high customer satisfaction and achieving strategic objectives.

Remuneration is competitive with companies of similar size and complexity and fair in the context of the wider workforce remuneration.

The total remuneration includes a variable element that effectively incentivises improvements in performance and balances the short and long term interests of the company.

How our remuneration policy addresses the factors of clarity, simplicity, risk, predictability, proportionality and alignment to culture that are set out in our corporate governance code.

Clarity Remuneration arrangements should be transparent and promote effective engagement with shareholders and the workforce. • Our reporting on remuneration has been extended to provide additional transparency on our policy on all components of remuneration, to explain in detail the operation of the AIP and how awards were determined by the committee. • We have agreed further engagement with the Staff Council on executive remuneration.	Simplicity Remuneration structures should avoid complexity and their rationale and operation should be easy to understand. • Our remuneration is based on the clear remuneration principles set out above. • We have adopted a single annual incentive plan with deferral that replaces the executive bonus scheme and long term incentive plan used in previous years. • Our performance measures and targets are based on our performance commitments.
Risk Remuneration arrangements should ensure reputational and other risks from excessive rewards, and behavioural risks that can arise from target-based incentive plans, are identified and mitigated. • The level of remuneration is monitored to ensure it is maintained at a median level with comparable companies. • The AIP includes performance measures that relate to all aspects of our strategy including both performance commitments and responsible business commitments to ensure there is no incentive to achieve certain targets to the detriment of others. • The AIP includes a deferral to limit the focus on short term performance to the detriment of longer term objectives.	Predictability The range of possible values of rewards to individual directors and any other limits or discretions should be identified and explained at the time of approving the policy. • A model including all measures and targets is used by the remuneration committee to assess the potential awards under the AIP at different levels of performance. It provides visibility to both the committee and participants. (The committee retaining entire discretion to decide on individual awards.) • The range of potential awards under the AIP are disclosed in this directors' remuneration report with an illustration of the application of the policy for the next financial year. • The remuneration policy includes details on the discretion that may be exercised by the committee in respect of the different remuneration components.
Proportionality The link between individual awards, the delivery of strategy and the long-term performance of the company should be clear. Outcomes should not reward poor performance. • Performance related remuneration is predominantly based on our corporate plan commitments clearly linking remuneration to performance and strategy. • The remuneration policy sets out the principles followed in determining the targets under the AIP. • Stretching targets in the AIP are based on delivery of significant performance improvements that were assessed in preparing our business plan. • The committee retains discretion to avoid inappropriate or mechanistic outcomes and there are also malus and recovery provisions in the AIP rules.	Alignment to culture Incentive schemes should drive behaviours consistent with company purpose, values and strategy. • The majority of the performance measures in the AIP relate to our core purpose of providing the public water service and relate to the key aspects of our activities: operational delivery, high standards of customer service and the delivery of our capital & environmental programme. • The responsible business performance measures and personal objectives seek to align the incentives with the company's wider environmental and societal purposes. • Collective executive objectives and personal objectives also incentivise the promotion of the company culture, integrated thinking and innovation. • The alignment of the performance measures between the AIP and the senior managers' bonus scheme creates consistent incentives in support of culture and strategy. • Financial measures incentivise financial resilience and long term investment as well as the profitability of non-regulated activities to generate shareholder value.

REMUNERATION continued**REMUNERATION POLICY****EXECUTIVE DIRECTORS' REMUNERATION POLICY**

The following remuneration policy is the policy adopted by the committee for the duration of AMP7 (2020/21 to 2024/25) in relation to all components of remuneration including the annual incentive plan (AIP).

The rules of the AIP were finally approved by the remuneration committee on 2 July 2020 and are intended to apply until 2025.

The policy for 2021 to 2025 set out below formalises the remuneration principles previously adopted by the remuneration committee when determining the remuneration of directors for 2020/21. For this reason information on the implementation of the remuneration principles for 2020/21 have also been described in the table below.

BASE SALARY

Purpose and link to strategy	Operation and performance measures	
To provide a fixed remuneration sufficient to attract, motivate and retain individuals with the appropriate experience, skills and competencies to lead the business and to define and implement the company's strategy in line with the board's strategic direction.	Base salaries reflect the individual experience and role and are reviewed annually by the remuneration committee with effect from 1 April. Increases are typically the same as the company wide pay award negotiated with the Staff Council.	
	This is a fixed remuneration which is not determined by reference to performance measures (but personal performance is assessed under the annual incentive plan and as part of any salary review).	
	There are no provisions to withhold or recover any sums paid.	
Maximum opportunity	Implementation 2020/21	Implementation 2021/22
A maximum limit for salary has not been set by the remuneration committee and salary increases are typically in line with the workforce. Periodic reviews may take place to ensure pay remains competitive, targeting remuneration at market median using comparisons with market practices for comparable companies in terms of size, activities and complexity. Remuneration consultants are used where deemed appropriate by the remuneration committee. A similar assessment is made to assess the appropriate base salary on changes of roles and promotions.	Executive directors' salaries were increased by 2% on 1 April 2020: CEO: £270,000 (from 1 August 2020 post annual increase) CFO: £201,069 Paul Butler (to 31 July 2020): £88,130	CEO: £271,620 (increased by 0.6% on 1 April 2021) CFO: £222,503 (from 1 April 2021 in connection with the alignment of pension benefits with the workforce)

BENEFITS

Purpose and link to strategy	Operation and performance measures	
A range of benefits sufficient to maintain the competitiveness of the company at recruitment stage and to help retain individuals of the appropriate experience, skills and competencies. Benefits are usually aligned with the benefits offered to senior managers or the wider workforce.	Executive directors are eligible for benefits which are available to the wider workforce on broadly similar terms. Their benefits may be reviewed in connection with any review of their base salary. The remuneration committee has discretion to agree specific benefits where appropriate for recruitment or retention. There are no provisions to withhold or recover any sums paid. This is a fixed remuneration which is not determined by reference to performance measures	
Maximum opportunity	Implementation 2020/21	Implementation 2021/22
There is no set maximum value for benefits but executive directors' benefits are similar to those of senior managers or the wider workforce.	CEO from 1 August 2020: Company car, life assurance, private medical insurance and health cash plan. CFO: Car allowance, life assurance, private medical insurance and health cash plan. Paul Butler (to 31 July 2020): Company car, life assurance, private medical insurance and health cash plan.	The CEO and CFO benefits for 2021/22 are the same as in 2020/21.

PENSION

Purpose and link to strategy	Operation and performance measures	
To attract and retain individuals with the appropriate experience, skills and competencies by providing competitive pension arrangements.	Executive directors are offered the choice of a company contribution into a defined contribution pension scheme or a cash allowance in lieu of pension, or a combination of both at their election with no employee contribution required. This is a fixed remuneration which is not determined by reference to performance measures	
Maximum opportunity	Implementation 2020/21	Implementation 2021/22
There is no set maximum but the percentage of contributions or cash allowance for new appointments or changes of roles are aligned with the wider workforce. A review of the legacy pension arrangement for the CFO was carried out with a view to align the CFO pension benefits with the level of pension contribution available to the workforce.	CEO: 10% of salary as pension cash allowance and/or employer pension contribution. CFO: 20% of salary as pension cash allowance and/or employer pension contribution. Paul Butler (to 31 July 2020): 20% pension allowance	CEO: 10% of salary as pension cash allowance and/or employer pension contribution CFO: 10% of salary as pension cash allowance and/or employer pension contribution.

REMUNERATION continued

ANNUAL INCENTIVE PLAN

Purpose and link to strategy

To incentivise the delivery of annual performance commitments and financial as well as responsible business and longer term strategic objectives creating a direct link between actual company performance and variable remuneration.

The potential award is determined by the remuneration committee following consideration of the overall fixed and variable remuneration taking account of market conditions but taking care to avoid any upward ratcheting effect.

Operation and performance measures

Link to performance: The performance of executive directors is measured in four categories: Outcome Delivery Incentives (ODIs) (40%), responsible business (20%), financial (30%) and personal objectives (10%) which are predominantly based on performance commitments in the corporate plan and in particular delivery for customers.

The metrics, targets (at threshold, target and maximum levels) and potential award for performance at target level and the maximum potential award (at or above outperformance level) are set by the remuneration committee for the CEO and the CFO as a percentage of salary at the beginning of the year to align potential reward to the business strategy. No award is made for performance at or below the threshold level of performance. The remuneration committee seeks to ensure that targets do not encourage undue risk taking by the executives so that the long-term performance of the business is not put at risk by considerations of short-term value.

Personal objectives are set by the remuneration committee and include individual objectives specific to the role of the individual and collective objectives for the entire Executive Team.

Stretch: Threshold levels are normally set no lower than prior year actual performance. Target levels are set at stretching performance outcomes and maximum pay-out levels should reflect truly exceptional performance improvements. Year-to-year, the elements comprising the AIP may change, as can the threshold, target and maximum pay-out performance levels to ensure that the AIP remains stretching.

Discretion/underpin: The remuneration committee retains full discretion to determine whether any award is paid under the AIP and the amount of the awards. In addition to setting threshold levels of performance, the committee will seek to ensure that the final outcome reflects performance that is genuine and demonstrable and may take account of any material issue of performance. The remuneration committee may determine that the performance metrics or targets are no longer appropriate following the date of grant and adjust them during a performance year.

Payment and deferral: 66% of any award determined by the remuneration committee is paid in cash in the month of July following the end of the financial year, the remaining 34% being paid in cash after two years provided that the director remains in employment or is determined to be a "good leaver" under the rules of the scheme.

Withholding/recovery: The amount of the award can be altered and sums paid may be recovered in certain circumstances such as inaccurate or misleading financial data being used to determine the final payment amount or if a participant to the AIP commits an act that amounts to fraud, dishonesty or gross misconduct. If it is determined that an award should be reduced, the remuneration committee may determine that the amount of any reduction can be set off against a deferred portion of the award. Details relating to payment at end of appointment are set out on page 154.

ANNUAL INCENTIVE PLAN continued

Maximum opportunity	Implementation 2020/21	Implementation 2021/22
CEO: Target performance: 75% of salary Maximum (outperformance): 100% of salary CFO: Target performance: 60% of salary Maximum (outperformance): 85% of salary	Further details on the operation of the AIP, performance measures and awards are set out on page 158.	The targets for 2021/22 are set out on page 166.

NOTES TO THE REMUNERATION POLICY TABLE

Note on retirement and appointment

Paul Butler retired and stepped down as Managing Director on 31 July 2020. David Hinton was an executive director and CEO Designate on 1 April 2020 and became CEO on 1 August 2020.

Note on base salary

The base salary of David Hinton for 2020/21 shown above is his salary as CEO from 1 August 2020. The salary he received over the 2020/21 financial year was £251,107 reflecting his salary of £213,320 as Asset Director/CEO Designate from 1 April 2020 to 31 July 2020 and his salary of £270,000 as CEO from 1 August 2020.

Note on taxable benefits

Up to 31 July 2020 David Hinton received the following benefits as Asset Director/CEO Designate: company car, fuel allowance, concessionary water, life assurance, private medical insurance, health cash plan. His benefits from 1 August 2020 are set out in the table above.

Private medical insurance is available to all senior managers and some longer serving employees. A car allowance or company car is available to managers and senior managers in accordance with the company policy, the amount of the allowance being dependent on the seniority of the role of the employee. The life assurance benefit and health cash plan are available to all employees.

Note on Pension benefits

The level of pension benefit for David Hinton was set retrospectively from 1 August 2020 at 10 per cent of salary (from 20 per cent previously) after he became CEO to align his pension benefit to the level of employer contribution received by the workforce. This change is being implemented progressively by applying a reduced percentage of salary in the course of 2021/22 so that the pension benefit actually received by David Hinton between 1 August 2020 and 31 March 2022 will be 10 per cent of salary. A review of the legacy pension arrangement for the CFO was carried out in 2021/22 with a view to align his pension benefits with the level of pension contribution available to the workforce. The remuneration committee decided to bring the pension benefits of the CFO to 10 per cent of salary and to revalue his salary retrospectively with effect from 1 April 2021, necessary adjustments being implemented in the course of 2021/22.

Employees of the company are entitled to a maximum company contribution of 10 per cent at a personal contribution rate of 8 per cent. Contributions or cash equivalent to the CEO and CFO are not conditional on a personal contribution of 8 per cent.

REMUNERATION continued**NOTES TO THE REMUNERATION POLICY TABLE** continued**Note on annual incentive plan and other incentives**

The AIP is available only to the CEO and CFO and to the other three members of the Executive Team. Paul Butler who retired on 31 July 2020 was not a participant to the AIP in 2020/21. David Hinton is a participant to the AIP for the whole financial year 2020/21; from 1 April 2020 CEO Designate and as CEO upon the effective retirement of Paul Butler on 1 August 2020.

There is a senior manager bonus scheme which uses targets similar to the AIP to achieve a convergence of incentives at senior management level. The senior managers' incentive scheme sets targets against a range of individual ODIs rather than the net ODI position. There is no company-wide bonus scheme. There is a specific bonus scheme to incentivise employees of the customer contact centre which focuses on achieving high levels of customer satisfaction.

INDEPENDENT NON-EXECUTIVE DIRECTORS' REMUNERATION POLICY**FEE**

Purpose and link to strategy	Operation and performance measures	
To provide a fixed fee sufficient to attract, motivate and retain individuals with the appropriate range and balance of experience, skills and competencies to provide strategic direction to the business and to lead, support and challenge the executive directors and management of the business.	The policy of the company is that non-executive directors' fees should be comparable to those of companies of similar size, activities and complexity.	
	The fees for the Chair and other independent non-executive directors reflect the individual experience and role and the required time commitment which may depend on any additional responsibilities as chair of a committee or other specific responsibilities. Fees are paid in cash monthly.	
	Fees are reviewed at the discretion of the company and increases take effect on 1 April.	
	This is a fixed remuneration which is not determined by reference to performance measures.	
	There are no provisions to withhold or recover any sums paid.	
Maximum opportunity	Implementation 2020/21	Implementation 2021/22
There is no set maximum fee but increases are typically the same as the company wide pay award negotiated with the Staff Council.	The fees paid to independent non-executive directors in 2020/21 are set out on page 157.	The fees to independent non-executive directors were increased in line with the company pay award.

Anne-Noëlle Le Ga and Rachel Drew represent the ultimate shareholders of the company and do not have a letter of appointment or service contract and do not receive any remuneration from the company. The same applied to Marissa Szczepaniak until her resignation.

INDEPENDENT NON-EXECUTIVE DIRECTORS' REMUNERATION POLICY continued

OTHER ITEMS

Purpose and link to strategy	Operation and performance measures	
To facilitate the performance of non-executive directors' duties to the Company.	Reasonable travel and other expenses incurred by directors when performing their duties are reimbursed. Non-executive directors do not receive any other remuneration or benefits. This component is not determined by reference to performance measures and there are no provisions to withhold or recover any sums paid.	
Maximum opportunity	Implementation 2020/21	Implementation 2021/22
None.	Expenses have been reimbursed in line with the policy.	Expenses will be reimbursed in line with the policy.

POLICY ON RECRUITMENT REMUNERATION

Executive directors

The remuneration package on recruitment of a new executive director or promotion of an employee to a position of executive director, should be sufficient to attract, motivate and retain individuals with the appropriate experience, skills and competencies to lead the implementation of the company's strategy but the company should not pay more than is necessary.

The components of the remuneration of a new executive director is set in accordance with the remuneration policy applicable at the time of the recruitment. The committee will also consider the wider approach to workforce remuneration, as well as any legislative and corporate governance requirements.

The remuneration committee may take account of a candidate's employment or personal circumstances in awarding relocation or payments for forfeited variable pay.

Where an employee is promoted to the position of executive director, pre-existing awards and contractual commitments will be honoured in accordance with their terms.

Base salary

The base salary would reflect any market data or market assessment that may be carried out by the remuneration committee to inform its decision. It would take account of the specific experience, skills and competencies of the selected candidate and of the salary of other executive directors. It may be set at a different level than the previous incumbent.

Benefits

The benefits package would be in line with those provided to other executive directors under the remuneration policy.

REMUNERATION continued**POLICY ON RECRUITMENT REMUNERATION** continued**Executive directors** continued*Pension*

The pension contribution rates for executive directors, or payments in lieu, would be aligned with those available to the workforce (currently 10 per cent of base salary).

AIP

The AIP would normally be in accordance with the applicable structure, metrics and targets, and maximum potential awards at the time of the recruitment.

The remuneration committee may exercise discretion to agree specific modifications in the first year of the AIP depending on when the recruitment takes place in the year and any award would be pro-rated to the actual period of employment in that year.

Relocation

The remuneration committee may agree a cash payment for reasonable relocation and temporary accommodation costs as well as travel and incidental expenses incurred.

Forfeited variable pay

The remuneration committee may agree a cash payment as compensation for the forfeit of any award under variable remuneration arrangements entered into with a previous employer provided that the nature and value of the forfeited award can be objectively demonstrated by the candidate. Such cash payment would not be more generous in terms of quantum or vesting period than the forfeited awards and would be subject to clawback in the event of an early termination of appointment for any reason.

Sign-on bonus

Our policy is not to provide other sign-on compensation except in exceptional circumstances at the discretion of the remuneration committee.

Independent non-executive directors

Fees for new independent non-executive directors are aligned with the remuneration policy and current fees for similar non-executive director roles on the board taking account of time commitment and any specific duties.

DIRECTORS' SERVICE AGREEMENTS AND LETTERS OF APPOINTMENT

The CEO and CFO had service contracts that were not fixed term contracts with the following notice periods:

	CEO	CFO
Effective date of contract	1 August 2020**	29 June 2015
Notice period by director	12 months	6 months
Notice period by company*	12 months	6 months

*Other than for breach of contract

**Before becoming CEO, David Hinton had been an executive director since 1 June 2013

Independent non-executive directors' letters of appointment have a fixed term of three years that may be extended for successive periods of three years subject to meeting the criteria of independence set out in the company's corporate governance code. A shorter term and shorter notice period by the company may be agreed in anticipation of the replacement of an independent non-executive director to facilitate succession arrangements. The renewal of the appointment of Nick Salmon for one year from 1 April 2021 was to facilitate the induction of a new chair and handover in advance of the PR24 business planning process and price review.

The letters of appointment of the current non-executive directors have the following remaining terms and notice periods:

	Nick Salmon	Chris Girling	John Barnes	Célia Pronto
Effective date of contract*	1 April 2021	30 October 2020	28 January 2016	1 June 2021
Expiry date	31 March 2022	29 October 2023	27 January 2022	31 May 2024
Notice period by director	3 months	3 months	3 months	3 months
Notice period by company**	1 month	1 month	3 months	3 months

*Full terms since appointment are shown in the corporate governance report

**Other than for breach of the terms of appointment

Anne-Noëlle Le Gal and Rachel Drew represent the ultimate shareholders of the company and do not have a letter of appointment or service contract and do not receive any remuneration from the company. The same applied to Marissa Szczepaniak until her resignation.

REMUNERATION continued**PAYMENT FOR LOSS OF OFFICE****Executive directors**

There are no provisions in executive directors' service agreements creating an obligation of the company to pay compensation on termination by the company. Participation in the AIP is at the discretion of the remuneration committee and not a contractual entitlement.

Base salary, pension & benefits

Salary, pension and benefits are paid over the notice period. The remuneration committee may at its discretion determine that a payment in lieu of notice should be made.

AIP

Under the AIP, an executive director who is a "good leaver" (death, disability, incapacity, retirement, automatic transfer and any other circumstance at the discretion of the remuneration committee) remains entitled to receive a pro-rated amount of the award that is not subject to deferral. The remuneration committee has discretion to determine that this award will not be pro-rated and/or that the director remains entitled to full payment. The payment date will be in July following year-end unless the committee determines that an early payment should be made. A "good leaver" remains entitled to receive any deferred award under the IAP on the same date unless the remuneration committee accelerates the payment.

A "bad leaver" loses the right to receive any payment (or any further payment or any deferred payments) or compensation for loss of any payment (or further payment) in respect of awards under the AIP.

Independent non-executive directors

Letters of appointment with independent non-executive directors do not include provisions for compensation for loss of office. They provide for the payment of fees accrued until the end of the appointment.

CONSIDERATION OF PAY AND EMPLOYMENT CONDITIONS OF EMPLOYEES

The committee did not consult with employees when defining its remuneration policy, but directors receive updates on pay and employment matters and have considered the executive directors' remuneration policy in context.

The remuneration committee receives updates on the pay award negotiations with the Staff Council and their outcome. This is directly taken into account when reviewing executive directors' salary increases which are usually (outside of specific salary reviews) in line with the pay award agreed with the Staff Council.

The remuneration committee also reviewed the structure, metrics and targets of the senior managers' bonus scheme in conjunction with the approval of the AIP metrics and targets for 2021/22 to ensure that executive directors and senior managers' incentives were closely aligned and focused on the delivery of the company's strategic objectives.

The committee reviewed the requirement of our Corporate Governance Code as they relate specifically to the review of workforce remuneration and engagement with the workforce on executive remuneration.

It was agreed that further engagement with the Staff Council would take place in 2021/22 facilitated by Célia Pronto who is a member of the committee and the independent non-executive director designated for engagement with the workforce. As part of that engagement process she will attend a meeting of the Staff Council at least once a year to cover topics that will include the committee's approach to remuneration including how it aligns with the company's objectives, governance principles and how it reflects wider company pay policy. It was also agreed that the committee would receive updates on the implementation of relevant aspects of the people plan to 2025.

CONSIDERATION OF SHAREHOLDER VIEW

Two non-executive directors representing the ultimate shareholders of the Company are members of the remuneration committee (together with three independent non-executive directors). They are able to make recommendations and to participate directly in the work of the committee when defining the remuneration policy, the components of executive remuneration and the structure and operation of the AIP. This helps ensure that the link between performance and pay is strong and managed in a way that recognises shareholders expectations and priorities.

REMUNERATION continued

EXECUTIVE REMUNERATION FOR 2020/21

SINGLE REMUNERATION FIGURE (AUDITED)

Single remuneration figure for executive directors

	David Hinton		Andrew Farmer		Paul Butler	
	2019/20	2020/21	2019/20	2020/21	2019/20	2020/21
Base salary	£153,321	£251,107	£197,127	£201,069	£259,207	£88,130
Taxable benefits	£20,971	£15,649	£13,156	£13,504	£15,892	£4,610
Annual bonus	£91,762	£120,181	£117,981	£71,599	£217,190	-
Long term incentives	£58,193	-	£74,819	-	£99,759	-
Pension	£20,664	£50,256	£39,425	£40,214	£51,841	£17,626
Company car trade	£2,052	£2,052	-	-	£2,753	£917.52
Total	£346,963	£439,245	£442,508	£326,386	£646,642	£111,284
Total fixed remuneration	£197,008	£319,064	£249,708	£254,787	£329,693	£111,284
Total variable remuneration	£149,955	£120,181	£192,800	£71,599	£316,949	-

Note on base salary

The base salary of David Hinton for 2020/21 shown above is the actual figure received reflecting his salary of £213,320 as Asset Director and CEO designate from 1 April 2020 to 31 July 2020 and his salary of £270,000 as CEO from 1 August 2020.

Note on AIP award

The AIP for David Hinton is based on his salary as CEO of £270,000 which he started to receive from 1 August 2020 to recognise the fact that he was CEO Designate fulfilling the functions of CEO for the entire financial year.

Note on deferral of IAP award

A sum of £40,862, in respect of the award of David Hinton, and of £24,344 in respect of the award of Andrew Farmer corresponding to 34 per cent of the total AIP award for 2020/21 will be deferred. Both deferred sums will be paid in cash in July 2023 (provided relevant conditions under the rules of the IAP are met at the time). The amount corresponding to 66 per cent of the award paid in July 2021 to David Hinton will be £79,320 and to Andrew Farmer will be £47,256.

Note on retirement of Paul Butler

Paul Butler took his retirement and stepped down as Managing Director on 31 July 2020. The remuneration committee determined that he was a "good leaver" for the purposes of the annual bonus scheme and the LTIP in respect of the period up to 31 March 2020. Paul Butler was not a participant to the AIP in 2020/21.

Note on pension benefits

The level of pension benefit for David Hinton was set retrospectively from 1 August 2020 at 10 per cent of salary (from 20 per cent previously) after he became CEO to align his pension benefit to the level of employer contribution received by the workforce. This change is being implemented progressively by applying a reduced percentage of salary in the course of 2021/22 so that the pension benefit actually received by David Hinton between 1 August 2020 and 31 March 2022 will be 10 per cent of salary. The amount of pension benefit for David Hinton set out above for 2020/21 is greater than 10 per cent of salary as the change in rate of contribution occurred in the course of the financial year but is being progressively adjusted throughout 2021/22. A review of the legacy pension arrangement for the CFO was carried out with a view to aligning his pension benefits with the level of pension contribution available to the workforce. The remuneration committee decided to bring the pension benefits of the CFO to 10 per cent of salary and to revalue his salary by 10 per cent retrospectively with effect from 1 April 2021, necessary adjustments being implemented in the course of 2021/22.

Single remuneration figure for non-executive directors

	Nick Salmon		Chris Girling		John Barnes	
	2019/20	2020/21	2019/20	2020/21	2019/20	2020/21
Fee	£105,266	£107,371	£42,106	£42,948	£40,858	£39,553
Taxable benefits	-	-	£2,339	-	£4,346	£3,441
Annual bonus	-	-	-	-	-	-
Long term incentives	-	-	-	-	-	-
Pension	-	-	-	-	-	-
Total	£105,266	£107,371	£44,445	£42,948	£45,204	£42,994
Total fixed remuneration	£105,266	£107,371	£44,445	£42,948	£45,204	£42,994
Total variable remuneration	-	-	-	-	-	-

	Célia Pronto		Marissa Szczepaniak		Rachel Drew	
	2019/20	2020/21	2019/20	2020/21	2019/20	2020/21
Fee	£34,738	£35,433	-	-	-	-
Taxable benefits	£409	-	-	-	-	-
Annual bonus	-	-	-	-	-	-
Long term incentives	-	-	-	-	-	-
Pension	-	-	-	-	-	-
Total	£35,147	£35,433	-	-	-	-
Total fixed remuneration	£35,147	£35,433	-	-	-	-
Total variable remuneration	-	-	-	-	-	-

Anne-Noëlle Le Gal and Rachel Drew represent the ultimate shareholders of the company and do not have a letter of appointment or service contract and do not receive any remuneration from the company. The same applied to Marissa Szczepaniak until her resignation.

REMUNERATION continued**ANNUAL INCENTIVE PLAN OUTCOME FOR 2020/21**

The commitment of our entire workforce to our public purpose has never been so important than during the Covid-19 pandemic and maintaining our service throughout the pandemic has been the primary concern of the board and the executive team since the first lockdown in March 2020.

The remuneration committee discussed the approach to adopt in respect of the impact of Covid-19 early in 2020/21 and determined that the most appropriate approach for the business as a whole would be not to suspend the scheme in 2020/21 but instead to apply the approved scheme rules (including the approved performance targets for 2020/21) subject to the exercise by the committee of appropriate discretion reflecting the operating environment. This would ensure that management's focus remains on delivering the five year corporate plan targets approved by the board following the final determination.

The remuneration committee recognised that it would be most appropriate to exercise discretion *a posteriori* when assessing potential awards under the scheme to take account of the impact of Covid-19 on the actual performance achieved as well as potential changes to performance commitments that may be agreed with Ofwat and any other relevant considerations.

Among many challenges during the year, the company faced unprecedented water demand in the summer of 2020 due to the combination of a significant increase in underlying demand for water as more customers were staying at home and exceptional peak demand due to high temperatures.

The committee concluded that while the ODI performance had been affected by the effects of Covid-19, performance was such that the outcome would have been below threshold notwithstanding such effects, principally due to interruptions and burst mains performance. Hence no discretion was exercised in respect of the ODI element of the scheme which therefore paid out zero.

The remuneration committee did recognise that additional and unforeseen Covid-19 related operational costs had been incurred to meet the exceptional demand and due to increased costs of working with Covid-19 restrictions and safety measures and the increase in bad debt. Accordingly the committee exercised discretion to allow for these impacts in respect of the financial metrics within the AIP.

The performance score for the responsible business and for personal objectives were close to the maximum as objectives were achieved despite challenging conditions. This reflected the commitment of the company to the health, safety and wellbeing of our workforce that was crucial in the context of the pandemic also demonstrated by engagement results and positive feedback from the HSE. There was good progress in the delivery of environmental outcomes despite the challenges posed by Covid-19. ESG performance was good, the company being awarded the highest score in its category under the GRESB benchmark.

ACTUAL CASH AWARDS FOR 2020/21 UNDER THE AIP

	Total Award	Total Award (% of salary)	Amount Paid in July 2021	Amount Payable in July 2023
CEO	£120,181	44.5%	£79,320	£40,862
CFO	£71,599	35.6%	£47,256	£24,344

A proportional award is made for performance between threshold and target and between target and outperformance.

OPERATION OF THE AIP IN 2020/21

The AIP awards are based on the score achieved against performance measures in four categories: Outcome Delivery Incentives (ODIs), responsible business, financial and personal objectives.

For each measure, the remuneration committee compares the actual performance (following internal and external assurance of the performance data) with a threshold (minimum), target and outperformance (maximum) level of performance that it has set at the beginning of the financial year to determine the actual score. Performance against operational targets is assessed based on annual reporting data following completion of the internal and external assurance processes. Details on how the board and the members of the remuneration committee ensure that the performance information they use is reliable are set out in the board statement on accuracy and completeness of data and information.

The assessment of financial performance is based on the audited financial statements and supporting information and reconciliation provided by the CFO. The assessment of the performance of the CFO against personal objectives is carried out by the committee following presentation of the assessment by the CEO. The assessment of the performance of the CEO against personal objectives is carried out by the committee following presentation of the assessment by the Chair of the board.

The potential awards are set as a percentage of salary at the beginning of the year for a given performance. For 2020/21 the potential awards for an overall performance at target level and the maximum potential award (at or above outperformance level) were set as follows:

	Potential Award (% of salary)		Potential Award	
	CEO	CFO	CEO	CFO
Potential Score				
@ Target: 100	75%	60%	£202,500	£120,642
@ Maximum: 133.3	100%	85%	£270,000	£170,909

A proportional award is made for performance between threshold and target and between target and outperformance.

REMUNERATION continued

ANNUAL INCENTIVE PLAN OUTCOME FOR 2020/21 continued

AIP MEASURES, TARGETS, SCORING AND ACTUAL PERFORMANCE IN 2020/21

The following table summarise the structure, performance measures, actual performance achieved and the financial outcome of the AIP for 2020/21.

Category	Measure	Threshold	Target	Maximum	Actual Performance*	Actual Score CEO	Award CEO (% of salary)	Actual Score CFO	Award CFO (% of salary)
ODIs (40%)	Net reward / penalty (£m)	-3.6	-2.9	-1.7	£-4.1m	0.0	0%	0.0	0%
	ODI Score	0	40	54.8					
Responsible business (20%)	Points achieved	0	2	4	3.67	26.2	19.6%	26.2	15.7%
	RB Score	0	20	27.4					
Financial (30%)									
Appointed cash receipts & opex (20%)	Net variance from target values (£m)	-4	0	+4	£-1.3m	13.3	10%	13.3	8%
	Finance Score 1	0	20	27.4					
Non-appointed operating profit (10%)	Profit target (£m)	4.1	4.6	5.1	£4.7m	10.4	7.8%	10.4	6.2%
	Finance Score 2	0	10	13.7					
Personal objectives (10%)	Points achieved	0	10		-	9.5	7.1%	9.5	5.7%
	Personal objectives Score	0	10						
Total		0	100	133.3	-	59.4	44.5%	59.4	35.6%

*The actual performance is after adjustments to take account of the exceptional impact of Covid-19.

- In respect of the ODIs measure, an adjustment of £2.3 million was made reflecting the impact of Covid-19 on operational performance but without any impact on the outcome for that measure as performance remains below threshold after adjustment.
- In respect of the Responsible Business measure, an adjustment was made to exclude two RIDDORs related to Covid-19.
- In respect of appointed cash receipts and opex an adjustment of £6.3 million was made to offset the impact of additional Covid-19 related costs including additional demand related costs (power, chemicals), contractors' claims, costs of internal organisational changes, additional bad debt charge, untaken annual leave, undelivered efficiencies, savings (employee expenses etc), summer event costs.
- In respect of non-appointed profit from operations, an adjustment of £0.2 million was made to offset the impact of Covid-19 on non-appointed activities.

The final C-MeX and D-MeX position is determined by Ofwat after publication of our reporting and the award for 2020/21 is based on an estimated position using available data. Any necessary adjustment will be made in 2021/22 when Ofwat's assessment is known and will be applied to the IAP awards for 2021/22 to achieve an equivalent outcome.

PERFORMANCE MEASURES INCLUDED IN THE ODI CATEGORY

Performance against ODIs is assessed against an overall net reward/penalty target based on the final determination for all financial ODIs (except biodiversity and catchment management which are included in the responsible business category).

The threshold, target and maximum levels were set by the remuneration committee to incentivise the delivery of significant improvements compared with baseline performance for comparable measures in 2019/AMP 6.

It is the main category of the AIP measuring the delivery of core services to customers which includes the following ODIs:

The customer measure of experience (C-MeX)	The developer services measure of experience (D-MeX)
The compliance risk index (CRI)	The number of household void properties
The appearance of tap water	The number of void business properties
Leakage reduction on a 3 year average	The delivery of the Water Industry National Environment Programme schemes
Reduction of per capita consumption on 3 year average	The number of sites protected from the risk of flooding
Unplanned outage	The bespoke Abstraction Incentive Mechanism (AIM)
Supply interruptions	The number of properties at risk of low pressure
The number of mains bursts repairs	The delivery of the Wellwood to Potters Corner strategic main
The taste and odour of tap water	

Note: The biodiversity and catchment management ODIs are included in the Responsible Business performance measures except that any variance from the net reward/penalty target for these ODIs in AMP7 is included in the calculation of the net reward/penalty in year 5 of AMP7.

In determining the threshold, target and maximum levels for the ODI metrics, the remuneration committee gave due consideration to the primary purpose of the AIP, which is to incentivise stretching but deliverable improvements in performance compared with the baseline performance achieved in AMP6.

The metrics and targets presented by the company in its business plan submissions reflected a significant level of improvement in performance over AMP7. However, the 2019 price determination set regulatory targets that went beyond what the company had considered to be reasonably achievable. The corporate plan approved by the board following the final determination anticipates net ODI penalties being incurred even if the company achieves significant performance improvements over AMP7. The negative weighting of the ODI targets is particularly relevant for performance commitments that are directly affected by severe weather events. In addition, some conflicts between the targets set in the final determination mean that activities necessary to achieve a target will likely lead to another target being missed. This is the case for example of the relationship between leakage and burst mains, as leakage activities result in a higher number of bursts being detected which could then result in the target for the number of bursts being exceeded.

Having considered this negatively weighted outcome of the final determination on ODIs, the remuneration committee still determined to use the net ODI position that would result from the final determination as the main operational measure in the AIP to ensure it was based on the final determination. Then the threshold, target and maximum levels of performance for the ODI metrics in the AIP have been set at levels that require significant improvements in performance in line with our business plan. However, even this level of improvement will still result in penalties under the regulatory framework set by Ofwat at PR19. This explains why an award may still be paid under the ODI metric when the company is in a net penalty position.

REMUNERATION continued**ANNUAL INCENTIVE PLAN OUTCOME FOR 2020/21** continued**RESPONSIBLE BUSINESS MEASURES AND POINTS ALLOCATION**

The Responsible Business performance category relates to (i) ESG, (ii) Health & Safety, (iii) achieving Corporate Plan targets on environmental initiatives and (iv) achieving Corporate Plan targets on customer satisfaction.

To assess management's performance, the remuneration committee determines whether several measures under each of the headings above have been achieved. The measures for 2020/21 and associated points are set out in the table below. The maximum score achievable under this measure is 4 and a score of 2 corresponds to the target level of performance.

Health & safety	Points	Customer satisfaction	Points
Health & Safety compliance above 75% (as recorded during audits)	0.33	Average satisfaction across all customer segments (Reputational ODI): 4.3 out of 5 for 2020/21	0.33
3 or less RIDDORS (excluding slips/trips).	0.33	Satisfaction of household customers who are experiencing payment difficulties (Reputational ODI): 4.2 out of 5 for 2020/21	0.33
Satisfactory progress in implementing wellbeing and mental health awareness for employees.	0.33	Satisfaction of household customers who are receiving non-financial support (which is a reputational ODI): 4.1 out of 5 for 2020/21	0.33
ESG	Points	Environmental	Points
GRESB benchmark score >85 for 2020/21	0.5	Target met on protecting wildlife and increasing biodiversity (financial ODI)	0.5
Progress in implementing the recommendations of the Task Force on Climate Related Financial Disclosure (TCFD)	0.5	Target met on engaging and working with landowners and land managers to improve catchment resilience related to raw water quality deterioration (financial ODI)	0.5

FINANCIAL TARGETS

The appointed cash receipts and opex measures seek to incentivise effective cash collection performance and management of bad debt and efficient operations whilst maintaining delivery of the strategic priorities of the business.

The non-appointed profit from operations target incentivises non-regulated commercial activities which include in particular billing and customer services to other undertakers, laboratory services, plumbing and technical services.

PERSONAL OBJECTIVES

Personal objectives are set by the remuneration committee and include individual and collective objectives for the Executive Team. Collective objectives have a weighting of 25 per cent and individual objectives a weighting of 75 per cent. The maximum score of 10 may be achieved if all the objectives are completed. Personal objectives seek to incentivise the delivery of projects or activities within the remit of a director that contribute or support the delivery of key company objectives and strategies.

FURTHER DISCLOSURES ON REMUNERATION

PENSION BENEFITS EARNED

Approved contributory final salary pension scheme

One executive director was a deferred member of the defined benefit pension scheme during the year. Their accrued entitlements under the scheme were as follows:

Accrued benefits	David Hinton
At March 2021	
Annual pension	£29,785
Lump sum	£89,211
At March 2020	
Annual pension	£29,625
Lump sum	£88,767
Increase in accrued benefits excluding inflation	
Annual pension	-
Lump sum	-
Increase in accrued benefits after allowing for inflation	
Annual pension	£160
Lump sum	£444

Paul Butler has exercised his right to draw a pension and as such there are no benefits accruing in the pension scheme as at 31 March 2021.

The defined benefit pension was closed to future accrual on 31 March 2015.

APPROVED DEFINED CONTRIBUTION SCHEME

In the year to 31 March 2021 two executive directors were members of the defined contribution scheme.

The table below summarises the contributions that were made in the scheme as at 31 March 2021:

	Contributions in 2019/20	Value of contributions as at 31 March 2020	Contributions in 2020/21	Value of contributions as at 31 March 2021
David Hinton	£9,966	£125,335	-	£125,335
Andrew Farmer	-	£96,897	£14,000	£110,897

CEO PAY RATIOS

The table below sets out a comparison between the CEO's single total figure of remuneration for 2020/21 and an equivalent figure for UK employees at the 25th, 50th and 75th percentile. The CEO single total figure of remuneration is a combined figure including the relevant single total remuneration received by both Paul Butler and David Hinton as CEOs during 2020/21.

Total pay and benefits have been calculated as at 31 March 2021 to allow for the comparison with the single total figure table.

Year	Method	25th percentile pay ratio	Median pay ratio	75th percentile pay ratio
2021	8	16:1	13:1	11:1

The amount received as CEO by Paul Butler from 1 April 2020 to 31 July 2020 was £111,284. The relevant amount received by David Hinton as CEO from 1 August 2020 to 31 March 2021 was £307,921 and includes the salary actually received in the period, the amount of pension benefit actually received, and the pro-rated amounts of taxable benefits, company car trade and AIP award.

The table below sets out the base salary and total pay and benefits details for the CEO and the employees at the 25th, 50th and 75th percentile received in or in respect of 2020/21. For the purpose of the calculation the reference salary without deduction of any pension salary sacrifice of employees was used for a better comparability of the figures.

REMUNERATION continued

CEO PAY RATIOS continued

CEO*Method	
Base salary	£268,130
Total pay and benefit	£419,205
Employees	
Base salary 25th percentile	£22,768
Base salary 50th percentile	£29,650
Base salary 75th percentile	£33,500
Total pay and benefits 25th percentile	£26,662
Total pay and benefits 50th percentile	£31,234
Total pay and benefits 75th percentile	£37,856

*Combined remuneration received by Paul Butler and David Hinton as CEO during 2020/21.

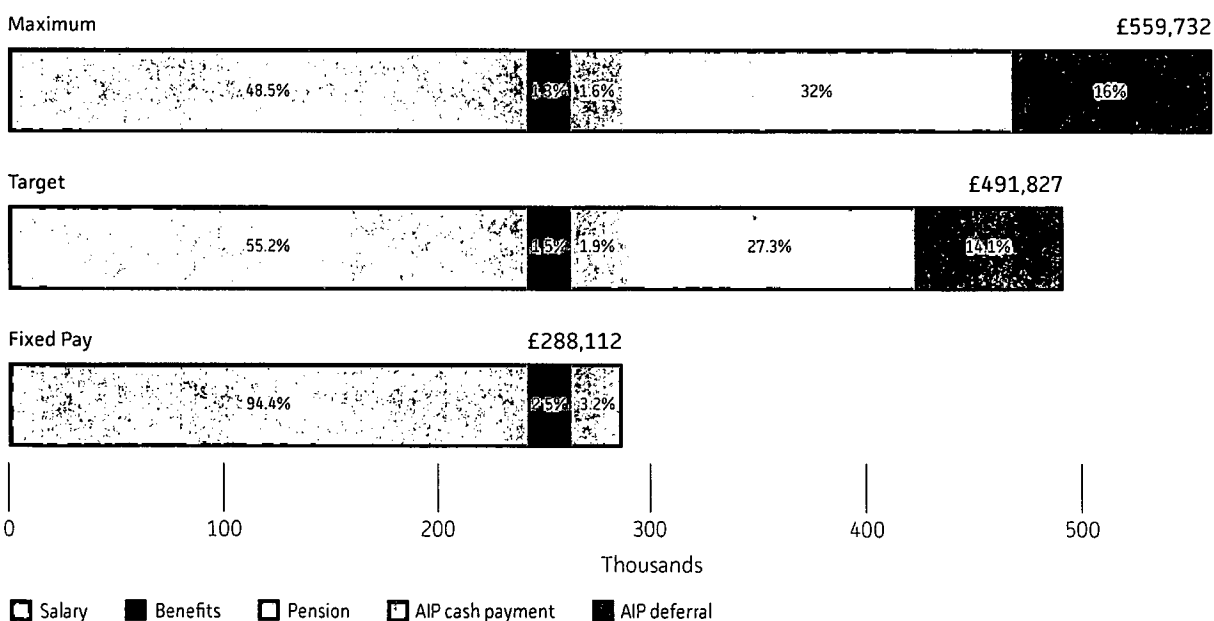
IMPLEMENTATION OF REMUNERATION POLICY IN 2021/22

The remuneration policy for 2021 to 2025 is as set out in the remuneration policy section. An illustration of the potential total remuneration of the executive directors in 2021/22 is set out below.

The structure and operation of the AIP for 2021/22 will be the same as is described above in respect of the AIP for 2020/21. The targets for 2021/22 have been updated by the remuneration committee on 6 May 2021 to ensure they remain stretching and in line with the corporate plan for 2020 to 2025 approved by the board following the final determination. Details on the new targets are set out below.

ILLUSTRATION OF POTENTIAL REMUNERATION IN 2021/22

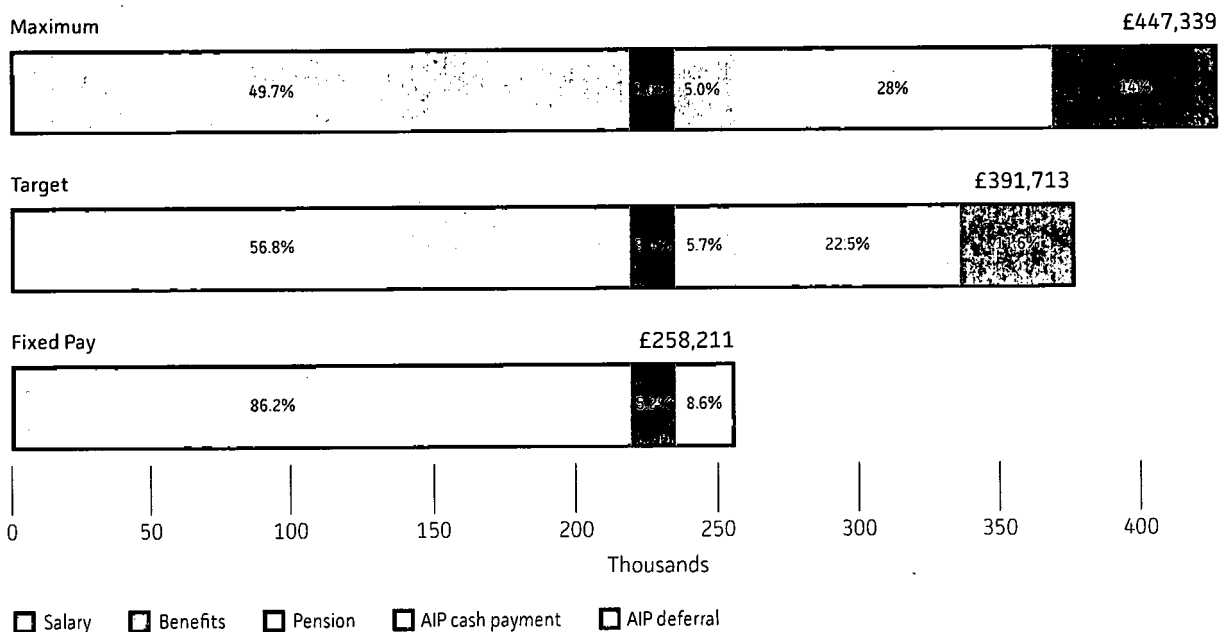
CEO - Illustration of the possible outcomes of the remuneration policy for 2021/22



Note on IAP: The total potential award for the CEO including the amount payable in July 2022 and the amount deferred would be £203,715 at target performance and £271,620 maximum.

Note on benefits: The benefits relating to car allowance are estimated in anticipation of the replacement of the CEO's company car with an electric vehicle which will reduce the value of the company car benefit in 2021/22.

CFO - Illustration of the possible outcomes of the remuneration policy for 2021/22



Note on IAP: The total potential award for the CFO including the amount payable in July 2022 and the amount deferred would be £133,502 at target performance and £189,128 maximum.

REMUNERATION continued

IMPLEMENTATION OF REMUNERATION POLICY IN 2021/22 continued

AIP METRICS AND TARGETS 2021/22

Category	Measure	Threshold	Target	Outperformance
ODIs (40%)	Net reward / penalty (£m)	-3.8	-2.5	-1.4
	ODI Score	0	40	54.8
Responsible business (20%)	Points achieved	0	2	4
	RB Score	0	20	27.4
Financial (30%)				
Appointed cash receipts and opex (20%)	Net variance from target values (£m)	-4	0	+4
	Finance Score 1	0	20	27.4
Non-appointed profit from operations (10%)	Profit target (£m)	3.5	3.9	4.3
	Finance Score 2	0	10	13.7
Personal objectives (10%)	Points achieved	0	10	
	Personal objectives Score	0	10	
Total Score		0	100	133.3

The updated responsible business targets are set out in the table below:

Health & safety	Points	Customer satisfaction	Points
Health & Safety compliance above 75% (as recorded during audits)	0.33	Average satisfaction across all customer segments (Reputational ODI): 4.3 out of 5 for 2021/22	0.33
3 or less RIDDORS (excluding slips/trips)	0.33	Satisfaction of household customers who are experiencing payment difficulties (Reputational ODI): 4.3 out of 5 for 2021/22	0.33
Satisfactory progress in implementing wellbeing and mental health awareness for employees	0.33	Satisfaction of household customers who are receiving non-financial support (which is a reputational ODI): 4.2 out of 5 for 2021/22	0.33
ESG	Points	Environmental	Points
GRESB benchmark score >=87	0.5	Target met on protecting wildlife and increasing biodiversity (Financial ODI) - 1,218 hectares (cumulative for year 2 of AMP)	0.5
Progress in implementing the recommendations of the Task Force on Climate Related Financial Disclosure (TCFD)	0.5	Target met on engaging and working with landowners and land managers to improve catchment resilience related to raw water quality deterioration (Financial ODI) - 5,687 hectares (cumulative for year 2 of AMP)	0.5

For details on the operation of the AIP and the specific performance measures included under the ODI, responsible business, financial metrics please refer to the explanations above on the outcome of the AIP for 2020/21.

POTENTIAL AWARD BASED ON TOTAL SCORE FOR 2021/22

The potential awards are set as a percentage of salary at the beginning of the year for a given performance. For 2021/22 the potential awards for an overall performance at target level and the maximum potential award (at or above outperformance level) have been set as follows:

Potential Score	Potential Award (% of salary)		Potential Award	
	CEO	CFO	CEO	CFO
@ Target: 100	75%	60%	£203,715	£133,502
@ Maximum: 133.3	100%	85%	£271,620	£189,128

Trusted business

HOW WE BUILD TRUST
IN WHAT WE DO

FINANCIAL STATEMENTS

We're constantly monitoring our performance against your expectations through a wide range of measures, from the taste and smell of your water to how often your supply is interrupted (find out more [page 64](#))

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STRATEGIC REPORT

GOVERNANCE

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ANNUAL PERFORMANCE

DIRECTORS' REPORT

for the year ended 31 March 2021

The directors have pleasure in presenting the group directors' report relating to South East Water Limited ("South East Water" or the "company") and its subsidiary South East Water (Finance) Limited (together referred to as the "group") for the year ended 31 March 2021, together with the audited financial statements.

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 are required to prepare the group financial statements in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards (IFRS Standards) adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they 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.

In preparing the group and company financial statements, International Accounting Standard 1 requires that directors:

- 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 IFRS's 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 adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006.

They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

RESPONSIBILITY STATEMENT

We confirm that to the best of our 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 company and the undertakings included in the consolidation taken as a whole;
- the strategic report includes a fair review of the development and performance of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- the annual report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the company's position, performance, business model and strategy.

PRINCIPAL ACTIVITIES AND FUTURE DEVELOPMENTS

The principal activities of the group comprise the supply of water to a population of 2.2 million in an area of 5,700 kms and the provision of certain ancillary services for customers, developers and other bodies within the constraints of the relevant legislation. The directors consider the performance of the business to be satisfactory and that this is expected to continue in the future. An indication of the likely future developments in the business of the company including its strategy for the period 2020 to 2025 are set out in the strategic report as well as information on the prospects of the company in the long-term viability statement.

The turnover of the group for the year ended 31 March 2021 was £248.2 million (2020: £243.5 million) and profit from operations was £77.5 million for the year (2020: £81.3 million). Profit before taxation for the year was £37.7 million (2020: £33.8 million). The financial position at 31 March 2021 for the group and for the company is shown on pages 188 and 189 respectively. Further analysis of the performance of the business and future developments is included in the strategic report on page 73.

APPOINTMENT AS A WATER UNDERTAKER AND THE RING-FENCE

South East Water has been appointed as a water undertaker under the Water Industry Act 1991 and the duties and the obligations of the appointee are set out in that Act, in regulations created under that Act, and in its instrument of appointment. The conditions of the instrument of appointment cover a variety of areas including charges, accounts and requirements to produce information for customers.

The instrument of appointment deals with ring-fencing and requires South East Water to ensure, so far as is reasonably practicable, that it retains at all times sufficient rights and assets (other than financial resources) for a special administrator, if appointed, to be able to manage the affairs of the business, which must be confirmed annually. Condition P requires South East Water to ensure that it has sufficient financial and managerial resources and adequate systems of planning and internal control to carry out the regulated activities and to certify this annually. Condition P requires South East Water to conduct the appointed business as if it was substantially the company's sole business and it was a separate public limited company. The ultimate controllers of South East Water are bound by a binding undertaking required under Condition P to procure that their subsidiaries, other than South East Water, provide information required by South East Water to comply with its obligations under the Water Industry Act 1991 and the instrument of appointment and to refrain from any action that would cause the appointee to breach any of these obligations.

The effect of the relevant legislation and the terms of the instrument of appointment mean that our directors have an overriding responsibility to ensure the regulatory ring-fence is maintained. The directors remain mindful of these obligations along with their duties as directors set out in the Companies Act 2006 and the Articles of Association.

One of the ways the directors meet the ring-fencing obligations is by ensuring that all board level matters that affect the company are decided at the board of South East Water, rather than at a holding company level.

GROUP STRUCTURE

South East Water is the main operating company in the group of companies headed by HDF. Further details of the structure of the HDF group are provided in the strategic report on page 70. There are no branches (as defined in section 1046(3) of the Companies Act 2006) of the company outside of the United Kingdom.

CAPITAL STRUCTURE

Details of the authorised and issued share capital are shown in note 25 of the financial statements. There have been no movements during the year. South East Water has one class of share which carries no right to fixed income. There are no specific restrictions on the size of a holding nor on the transfer of shares, which are both governed by the Articles of Association and prevailing legislation.

Details of South East Water's immediate and ultimate controlling parties are provided in note 32 and in the strategic report.

ACCOUNTING FRAMEWORK

The financial information presented in these audited financial statements has been prepared in accordance with the disclosure and transparency rules of the Financial Services Authority and International Financial Reporting Standards (IFRS) as adopted for use in the United Kingdom. The financial statements are presented in Sterling.

The results published in this report describe our performance for the year and incorporate the performance of South East Water Limited and South East Water (Finance) Limited.

USE OF FINANCIAL INSTRUMENTS

The group's financial risk management policies are set out in note 22.

RESEARCH AND DEVELOPMENT ACTIVITIES

South East Water is a member of UK Water Industry Research (UKWIR) and participates in their research programmes.

DIRECTORS' REPORT continued
for the year ended 31 March 2021

DIVIDENDS

The directors have approved dividends totalling £11 million (2020: £11 million) for the year, paid in equal instalments of £2.75 million per quarter. In December 2020 directors approved a special restructuring dividend of £136 million to its parent company South East Water Holdings. These funds were used by the parent company to repay its intercompany loan to South East Water Limited on the same day resulting in a net nil cash impact. Further details are given in note 10 of the financial statements. South East Water's immediate parent company, South East Water (Holdings) Limited used £2.3 million of the £11 million dividends (2020: £4.5 million) to pay interest on an inter-company loan back to South East Water. No dividends have been proposed and unpaid at the balance sheet date.

The company's dividend policy is discussed on page 76 of the strategic report and on page 268 of the annual performance report.

CAPITAL EXPENDITURE

During the year the group's capital expenditure totalled £93.3 million (2020: £104.5 million). Further details are given in notes 12 and 13 of the financial statements.

In the opinion of the directors, the market value of land is significantly more than its book value. However, it would not be practicable because of the number of sites and the costs of valuing such sites to precisely quantify this.

TAXATION

The Group's profits are typically sheltered with a combination of tax losses from other HDF Group entities and the application of capital allowances from the extensive investment programme currently being undertaken by South East Water. In practice we prioritise the purchase of group relief in sheltering tax charges and the payment of group relief is made at the statutory rate for corporation tax so does not impact the effective tax rate. The effective rate after making allowance for the future rate change and prior year adjustments is 18.0 per cent. Additional information on taxation is provided in note 9.

DIRECTORS AND THEIR INTERESTS

The directors who at any time during the financial year and at the date of this report were directors of South East Water are set out on pages 114 to 116 and further details regarding their appointments are set out on page 132.

No director held any shares or loan stock in South East Water or other associated companies, which is required to be disclosed under the Companies Act 2006, during the financial year.

DIRECTORS' INDEMNITIES

South East Water has granted an indemnity to its directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 2006. Such qualifying third party indemnity provision remains in force as at the date of approving this directors' report.

PRINCIPAL RISKS AND UNCERTAINTIES

A description of the principal risks and uncertainties and an explanation of the steps the board takes to mitigate these risks are provided in the strategic report on pages 30 to 55.

CORPORATE GOVERNANCE ARRANGEMENTS

Information on South East Water's corporate governance arrangements are set out in the corporate governance report at page 113.

DISCLOSURES ON GREENHOUSE GAS EMISSIONS

Information on greenhouse gas emissions, energy consumption and energy efficiency action (including as required under Part 7, Schedule 7 of the Large and Medium-Sized Companies and Groups (Accounts and Reports) Regulations 2008 are set out on page 90 of the strategic report.

We also report on our greenhouse gas emissions in our performance, people and planet report, which is published on the company's website. Further details on our responsible business committee are set out in the corporate governance report at page 133.

ENVIRONMENTAL AND CORPORATE SOCIAL RESPONSIBILITY

South East Water's approach to sustainable development of our business includes a strong commitment to the environment and corporate social responsibility. Details of our actions in this respect are given throughout the strategic report and corporate governance report.

EMPLOYMENT POLICIES ON DISABILITY AND ENGAGEMENT WITH EMPLOYEES, SUPPLIERS, CUSTOMERS AND OTHERS

South East Water offers equal opportunities to all employees and applicants for employment. Our managers and officers are trained to ensure there is no unlawful discrimination on grounds of race, gender, age, religion, union membership, disability or sexual orientation. Employment policies are intended to confirm South East Water as an employer of choice through provision of a safe work environment, satisfying work, personal development and fair rewards. Further details are given in the strategic report on page 102.

South East Water gives full consideration to applications for employment from disabled persons where the candidate's particular aptitudes and abilities are consistent with meeting the requirements of the job. Opportunities are available to disabled employees for training, career development and promotion. Where existing employees become disabled it is South East Water's policy to provide continuing employment, wherever practicable, in the same position or in an alternative position and to provide appropriate training to achieve this aim.

South East Water places considerable value on the involvement of our employees and has continued to keep them informed on matters affecting them as employees and on various factors affecting the performance of the company. This is achieved through formal and informal meetings, regular bulletins on the intranet and an employee magazine. Employee representatives are consulted regularly through the Staff Council on a wide range of matters affecting their current and future interests.

South East Water has developed a comprehensive engagement program to ensure that we capture the differing views of our customers, suppliers and other stakeholders in the wider community. This program has helped us shape our plans for the 2020 to 2025 AMP. There are a number of examples of how South East Water has interacted with stakeholders in forming its policies and decisions.

The strategic report also discusses how the directors have had due regard to the engagement with employees, customers, suppliers and other business relationships on page 82.

DIRECTORS' STATEMENT ON AUDIT INFORMATION

DISCLOSURE OF INFORMATION TO AUDITORS

Due to the completion of ten years by Deloitte LLP as the statutory auditor for the Company and the rest of the HDF Group, it was intended, as required by UK law, that a tender process for the appointment of statutory auditor be undertaken during 2020. However, due to the Covid-19 pandemic, the HDF Group sought and obtained permission from the Financial Reporting Council to extend the appointment of Deloitte LLP as statutory auditor for a further year.

Deloitte LLP have agreed to act in the capacity of auditor for the group for a further year.

The process for the new appointment of statutory auditor for the HDF Group has now begun with the appointment planned to be made in the middle of the financial year ending 31 March 2022.

Each of the persons who are directors at the time the Directors' report is approved has confirmed that:

- so far as the director is aware, there is no relevant audit information of which the company's and the group's auditors are unaware; and
- the director has taken all the steps that ought to have been taken as a director in order to be aware of any relevant audit information and to establish that the company's and the group's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with provisions of s418 of the Companies Act 2006.

POST BALANCE SHEET EVENTS

Details of significant events that occurred after the balance sheet date and before the signing of the balance sheet are provided in note 30.

POLITICAL DONATIONS

No political donations were made by the group in either the current or prior period.

Approved by the board on 15 July 2021 and signed on its behalf by:

NICOLAS TRUILLET
COMPANY SECRETARY
15 JULY 2021



INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SOUTH EAST WATER LIMITED

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

1. OPINION

In our opinion the financial statements of South East Water Limited (the 'Company') and its subsidiary (together, the 'Group'):

- give a true and fair view of the state of the Group's and of the 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 International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the Group and Company income statement;
- the Group and Company statement of other comprehensive income;
- the Group and Company statement of financial position;
- the Group and Company statement of changes in equity;
- the Group and Company statement of cash flows; and
- the related notes 1 to 32.

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.

2. 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 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 as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Company.

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

3. SUMMARY OF OUR AUDIT APPROACH

Key audit matters

The key audit matters that we identified in the current year were:

- Household bad debt provisioning;
- Revenue recognition – estimating unbilled household customer income; and
- Classification of costs between operating and capital expenditure.

Within this report, key audit matters are



Newly identified



Similar level of risk



Increased level of risk



Decreased level of risk

Materiality	The materiality that we used for the Group financial statements was £3.2m (2020: £3.5m) which was determined on the basis of approximately 3% of EBITDA, in line with prior year.
Scoping	The Group comprises South East Water Limited (the regulated water business) and its only subsidiary company South East Water (Finance) Limited (which issues part of the Group's debt). Both of these companies were subject to a full scope audit by the Group audit engagement team.
Significant changes in our approach	Our approach in the current year is substantially consistent with prior year. No significant changes were noted to the key audit matters as compared to the prior year.

4. CONCLUSIONS RELATING TO GOING CONCERN

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.

Our evaluation of the directors' assessment of the Group's and Company's ability to continue to adopt the going concern basis of accounting included:

- obtained an understanding of the relevant controls including management review controls and controls relating to the data integrity in the going concern model;
- analysing the Group's financing facilities including nature of facilities, repayment terms and covenants;
- assessing the likelihood of new facilities due for renewal in the going concern period being secured, and in particular refinancing of the revolving credit facility which has been approved by the lender;
- assessing the appropriateness of the assumptions taken by management in establishing their base case forecasts including comparison of growth forecasts with historical performance and market data;
- recalculating the forecast covenants and assessing management's evaluation of the headroom available against these covenants;
- evaluating the forecast liquidity position based on forecasts;
- challenging the appropriateness, and results of the sensitivity analysis performed by management through performing additional independent sensitivity testing and benchmarking with comparable water companies external information;
- assessing the sophistication of the model used to prepare the forecasts and testing of clerical accuracy of those forecasts; and
- assessing the appropriateness of the disclosures provided in the financial statements.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group's and Company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In relation to the reporting on how the Group has applied the UK Corporate Governance code, we have nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SOUTH EAST WATER LIMITED continued

5. KEY AUDIT MATTERS

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

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

5.1. HOUSEHOLD BAD DEBT PROVISIONING

Key audit matter description

As at 31 March 2021, the household bad debt provision for the Company was £27.5m (2020: £24.6m). The bad debt charge for the year ended 31 March 2021 of £3.8m represented 1.5% of total turnover (2020: £4.2m and 1.7% of turnover).

The key audit matter, which is also a potential fraud risk, is focused on the estimation of the bad debt provision, including whether the experience of cash collection in historical periods provides an appropriate expectation of future credit losses under IFRS 9 "Financial Instruments".

A proportion of the Group's customers do not or cannot pay their water bills, which results in the need for provision to be made for non-payment of the customer balance. The household bad debt provision is material, a key area of estimation within the Group and an area of scrutiny by Ofwat.

Provisions are made against the Group's trade receivables based on historical cash collection rates for debt over the past three years. This marks a change in practice from prior year where cash collection history over the past four years was used along with a Covid-19 overlay adjustment. This change in approach was made to reflect the impact that the pandemic has had on household finances and expected credit losses. The three year cash collection model places a greater weight on cash collection history over the last year when the Covid-19 pandemic has been a contributing factor, when compared to the four year model.

The Board of Directors' also considered this an area of significant judgement as discussed in the Corporate Governance Report on page 140. This is also reflected as a key source of estimation uncertainty in note 2 to the financial statements, and the relevant accounting policy adopted is disclosed in note 3. The bad debt provision is outlined further in note 17.

5.1. HOUSEHOLD BAD DEBT PROVISIONING CONTINUED

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

In response to this matter we have performed the following procedures:

- obtained an understanding of the relevant controls including management review controls and controls relating to the data integrity in the bad debt model;
- verified the accuracy of information within the cash collection model;
- verified that the final provision has been calculated in line with the policy of the Group through testing the mechanical accuracy of the provision;
- verified that the final provision has been calculated in line with IFRS 9 methodology and specifically considers Covid-19;
- analysed management's bad debt policy, and challenged whether they reflect the lifetime expected credit outcomes for receivables, specifically assessing whether the recoverability assumptions are reflective of current cash collection rates;
- assessed whether any discrepancies exist between the provision recognised and that supported by current cash collection ratios over the last 12 months and other macroeconomic indicators that may impact the ability of customers to make payments;
- challenged management's assumptions by benchmarking against other water companies and looking at external unemployment forecasts and performing sensitivity analysis on the provision model to assess if changes to assumptions used by management would materially alter the provision;
- performed trend analysis and model assessment by involving our modelling and analytics specialists to validate the data inputs, calculations and outputs in the cash collection model; and
- assessing the appropriateness of the disclosures provided in the financial statements.

Key observations

We are satisfied that the assumptions and estimates applied in assessing the impairment of trade receivables, including the impact of Covid-19, are appropriate and that the bad debt provision has been properly calculated using appropriate relevant data and in accordance with IFRS 9. The estimation uncertainty that exists in relation to bad debt provisioning has been appropriately disclosed in note 2 to the financial statements.

**INDEPENDENT AUDITOR'S REPORT
TO THE MEMBERS OF SOUTH EAST WATER LIMITED** continued

5.2. REVENUE RECOGNITION – ESTIMATING UNBILLED HOUSEHOLD CUSTOMER INCOME



Key audit matter description	For customers with meter, which represent 90% of the customer base, the revenue recognised depends upon the volume used, including an estimate of the sales value of units supplied between the date of the last meter reading and the balance sheet date. The household unbilled accrual as at 31 March 2021 was £36.2m as compared to £34.2m as at 31 March 2020. The risk is focused on the usage estimate, which is based on historical data and assumptions around consumption patterns upon which management recognise unbilled revenue. This estimate includes manual adjustments made by management including the adjustments for seasonality and changes in levels of social tariff factored in the accrued income estimate. The seasonality adjustment has increased in the current year mainly due to the large amount of consumption in the summer months recorded in 2020, due to the heatwave as well as fewer people away from home/on holiday due to Covid-19 restrictions. Due to the level of management judgement, the estimation of unbilled household revenue has been identified as a key audit matter. We have identified a risk of fraud in relation to this audit matter due to its influence on key metrics which management utilise to monitor and report business performance. The Board of Directors also considered this an area of significant judgement as discussed in the Corporate Governance Report on page 140. This is also reflected as a key source of estimation uncertainty in note 2 to the financial statements, where management have outlined sensitivity analysis, and the relevant accounting policy adopted is disclosed in note 3. Revenue is disclosed in note 4.
How the scope of our audit responded to the key audit matter	For the estimation of unbilled household customer income, we have performed the following procedures: · obtained an understanding of, and tested, the relevant controls around the estimation techniques used with regard to consumption and other key data inputs into the model; · challenged the appropriateness of management's consumption assumptions including in relation to the seasonality and social tariff adjustment by benchmarking against other water companies and performing sensitivity analysis on manual adjustments to assess if changes to assumptions used by management would materially alter the adjustment; · performed retrospective analysis of bills raised during 2020/21 relating to the FY20 accrual to determine the accuracy of management's forecasting ; and · involved our IT specialists to test the accuracy and completeness of the billed consumption report utilised by management in determining the accrual required.
Key observations	We are satisfied that management's estimates in relation to the recognition of unbilled household revenue are appropriate.

5.3. CLASSIFICATION OF COSTS BETWEEN OPERATING AND CAPITAL EXPENDITURE



Key audit matter description	The Group continues to invest significantly in infrastructure renewal and replacement, with property, plant and equipment and intangible asset additions of £93m (2020: £104m) in the current year. Additions during the year have decreased by £11m compared to the prior year primarily due to Covid-19 restrictions which resulted in delays in delivering the capital programme. Expenditure in relation to increasing the capacity or enhancing the network is treated as capital expenditure ("capex"). Expenditure incurred in maintaining the operating capability of the network is expensed in the year in which it is incurred ("opex"). Capital projects can contain a combination of enhancement and maintenance activity which are not distinct and hence the allocation of costs between capital and operating expenditure is inherently judgemental. This risk also includes the inappropriate capitalisation of labour overheads as this involves significant management judgement in assessing which costs are to be capitalised. We have identified a risk of fraud in relation to this audit matter due to its influence on key metrics which management utilise to monitor and report business performance. The Board of Directors also considered capital expenditure as an area of significant judgement as discussed in the Corporate Governance Report on page 140. This is reflected as a key judgement in note 2 to the financial statement and the relevant accounting policy adopted is disclosed in note 3. Capital expenditure is disclosed in note 13.
How the scope of our audit responded to the key audit matter	We have: · obtained an understanding and tested relevant controls within the capex and opex process; · assessed the Group's capitalisation policy to determine compliance with relevant accounting standards and tested the operating effectiveness of controls over the application of the policy to expenditure incurred on projects within the capital programme; · for a sample of capital projects, assessed the application of the capitalisation policy to the costs incurred by agreement to third party invoices and obtained explanations and further support for the appropriateness of classification of projects as capital; · challenged the assumptions and judgements made in allocating labour overheads to capital projects, through understanding the nature of activities performed; and · for a sample of capital projects tested the actual labour overheads capitalised in the year, assessing the application of the capitalisation policy to the costs incurred by reviewing the business cases as progress and supporting evidence for the costs incurred.
Key observations	Based on our audit of a sample of capital projects and our review of the project budgets, we consider that the classification of costs and labour overheads between operating and capital expenditure is appropriate.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SOUTH EAST WATER LIMITED continued

6. OUR APPLICATION OF MATERIALITY

6.1. MATERIALITY

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

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

	Group financial statements	Company financial statements
Materiality	£3.2m (2020: £3.46m)	£3.16m (2020: £3.43m)
Basis for determining materiality	Materiality has been determined at approximately 3% (2020: 3%) of EBITDA.	
Rationale for the benchmark applied	We have used EBITDA as the benchmark for materiality as this is deemed a key driver of business value, is a critical component of the financial statements and is a focus for users of those financial statements. The majority of the Group's operations are carried out by the Company.	

6.2. PERFORMANCE MATERIALITY

We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole.

	Group financial statements	Company financial statements
Performance materiality	70% (2020: 70%) of Group materiality	70% (2020: 70%) of Company materiality
Basis and rationale for determining performance materiality	We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole. In determining performance materiality, we considered the following factors: a. quality of the Group's control environment, including our ability to apply a control reliance approach on several business cycles; b. no significant control deficiencies noted in the functioning of the key business operations due to Covid-19 and the related changes in working patterns; c. the limited number of changes to the business and the turnover of management and key accounting personnel during the year; and d. the history of a low number of corrected and uncorrected misstatements identified in previous periods.	

6.3. ERROR REPORTING THRESHOLD

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.2m (2020: £0.2m), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

7. AN OVERVIEW OF THE SCOPE OF OUR AUDIT

7.1. IDENTIFICATION AND SCOPING OF COMPONENTS

Our Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls, and assessing the risks of material misstatement at the Group level.

South East Water Limited and South East Water (Finance) Limited were subject to full-scope audits and together account for 100% (2020: 100%) of the Group's turnover, total assets, profit before tax and EBITDA.

All procedures were carried out directly by the Group audit team.

7.2. OUR CONSIDERATION OF THE CONTROL ENVIRONMENT

Our work in relation to the Group's internal control environment involved testing of the Group's key reporting system. We, with the involvement of our IT specialists, obtained an understanding of, and tested, relevant General Information Technology Controls ("GITCs") and automated controls within the Group's key reporting system, including the access controls, change management controls and controls around segregation of duties.

We also tested the relevant controls within the household revenue, capital expenditure and operating expenses business processes, which are supported by the Group's key reporting system. We performed a walkthrough and inquiry of management to obtain an understanding of the relevant controls within each of these business processes. We tested, on a sample basis, these controls by verifying that the controls have been performed as designed.

We were able to adopt a controls reliance strategy for each of these business processes, including automated controls in these business processes and no significant control deficiencies were identified as a result of our work.

8. 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.

9. 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 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 Company or to cease operations, or have no realistic alternative but to do so.

INDEPENDENT AUDITOR'S REPORT**TO THE MEMBERS OF SOUTH EAST WATER LIMITED** continued**10. 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.

11. 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.

11.1. IDENTIFYING AND ASSESSING POTENTIAL RISKS RELATED TO IRREGULARITIES

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, we considered the following:

- the nature of the industry and sector, control environment and business performance including the design of the Group's remuneration policies, key drivers for directors' remuneration, bonus levels and performance targets;
- results of our enquiries of management and the audit committee about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the Group's documentation of their policies and procedures relating to:
 - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
 - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
 - the internal controls established to mitigate risks of fraud or non-compliance with laws and regulations;
- the matters discussed among the audit engagement team and relevant internal specialists, including tax, pensions and IT specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, we considered the opportunities and incentives that may exist within the organisation for fraud and identified the greatest potential for fraud in the following areas: household bad debt provisioning, revenue recognition - estimating unbilled household customer income and classification of costs between operating and capital expenditure. In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

We also obtained an understanding of the legal and regulatory frameworks that the Group 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.

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the financial statements but compliance with which may be fundamental to the Group's ability to operate or to avoid a material penalty. These included compliance with terms of the Group's operating licence as imposed by The Water Services Regulation Authority (OFWAT) and the regulatory solvency requirements which are fundamental to the Group's ability to continue as a going concern.

AUDIT RESPONSE TO RISKS IDENTIFIED

As a result of performing the above, we identified household bad debt provisioning, revenue recognition - estimating unbilled household customer income and classification of costs between operating and capital expenditure as key audit matters related to the potential risk of fraud. The key audit matters section of our report explains the matters in more detail and also describes the specific procedures we performed in response to those key audit matters. In addition to the above, our procedures to respond to risks identified included the following:

- reviewing the financial statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- enquiring of management, the audit committee and in-house legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance and reviewing correspondence with HMRC and Ofwat; and
- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

INDEPENDENT AUDITOR'S REPORT
TO THE MEMBERS OF SOUTH EAST WATER LIMITED continued

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

12. 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 the 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.

13. CORPORATE GOVERNANCE STATEMENT

Based on the work undertaken as part of our audit, we have concluded that each of the following elements of the Corporate Governance Statement is materially consistent with the financial statements and our knowledge obtained during the audit:

- the directors' statement with regards to the appropriateness of adopting the going concern basis of accounting and any material uncertainties identified set out on page 111;
- the directors' explanation as to its assessment of the group's prospects, the period this assessment covers and why the period is appropriate set out on page 107;
- the directors' statement on fair, balanced and understandable set out on page 170;
- the board's confirmation that it has carried out a robust assessment of the emerging and principal risks set out on page 31;
- the section of the annual report that describes the review of effectiveness of risk management and internal control systems set out on page 138; and
- the section describing the work of the audit committee set out on page 139.

14. MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

14.1. ADEQUACY OF EXPLANATIONS RECEIVED AND ACCOUNTING RECORDS

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

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

We have nothing to report in respect of these matters.

14.2. DIRECTORS' REMUNERATION

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

We have nothing to report in respect of this matter.

15. OTHER MATTERS WHICH WE ARE REQUIRED TO ADDRESS

15.1. AUDITOR TENURE

Following the recommendation of the Audit Committee, we were appointed by the Company on 1 September 2011 to audit the financial statements for the year ending 31 March 2011 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is eleven years, covering the years ending 31 March 2011 to 31 March 2021.

15.2. CONSISTENCY OF THE AUDIT REPORT WITH THE ADDITIONAL REPORT TO THE AUDIT COMMITTEE

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

16. 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.

Helen BurrIDGE

HELEN BURRIDGE (SENIOR STATUTORY AUDITOR)

FOR AND ON BEHALF OF DELOITTE LLP
STATUTORY AUDITOR
LONDON, UNITED KINGDOM
15 JULY 2021

Group income statement

for the year ended 31 March 2021

	Notes	2021 £000	2020 £000
Revenue	4	248,156	243,481
Bad debts	17	(3,788)	(4,198)
Net operating costs	6	(178,285)	(170,151)
Other income	4	11,439	12,199
Profit from operations		77,522	81,331
Finance income	8	3,093	5,333
Finance expense	8	(42,956)	(52,862)
Profit before taxation		37,659	33,802
Taxation	9	(6,343)	(16,918)
Profit for the year		31,316	16,884

Earnings per share attributable to the ordinary equity holders of the parent

	Notes	2021 Pence	2020 Pence
Basic and diluted	11	63.51p	34.24p

The group activities above are derived from continuing operations.

The notes on pages 194 to 247 form part of these financial statements.

Group statement of other comprehensive income

for the year ended 31 March 2021

	Notes	2021 £000	2020 £000
Profit for the year		31,316	16,884
Other comprehensive income:			
Items that will not be reclassified to profit or loss:			
Net actuarial (loss)/gain on pension schemes	24	(14,967)	4,879
Deferred tax credit/(charge) on net actuarial (loss)/gain	9	2,844	(927)
Impact of deferred tax rate change in respect of pension schemes	9	–	(124)
Other comprehensive income for the year		(12,123)	3,828
Total comprehensive income		19,193	20,712

The notes on pages 194 to 247 form part of these financial statements.

Company income statement

for the year ended 31 March 2021

	Notes	2021 £000	2020 £000
Revenue	4	248,156	243,481
Bad debts	17	(3,788)	(4,198)
Company net operating costs	6	(178,280)	(170,129)
Other income	4	11,439	12,199
Company profit from operations		77,527	81,353
Finance income	8	3,092	5,308
Finance costs	8	(42,979)	(52,895)
Profit before taxation		37,640	33,766
Taxation	9	(6,339)	(16,911)
Profit for the year		31,301	16,855

Earnings per share attributable to the ordinary equity holders of the company	Notes	2021 Pence	2020 Pence
Basic and diluted	11	63.47p	34.18p

The company activities above are derived from continuing operations.

The notes on pages 194 to 247 form part of these financial statements.

Company statement of other comprehensive income

for the year ended 31 March 2021

	Notes	2021 £000	2020 £000
Profit for the year		31,301	16,855
Other comprehensive income:			
Items that will not be reclassified to profit or loss:			
Net actuarial (loss)/gain on pension schemes	24	(14,967)	4,879
Deferred tax credit/(charge) on net actuarial (loss)/gain	9	2,844	(927)
Impact of deferred tax rate change in respect of pension schemes	9	–	(124)
Other comprehensive income for the year		(12,123)	3,828
Total comprehensive income		19,178	20,683

The notes on pages 194 to 247 form part of these financial statements.

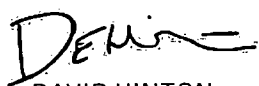
Group statement of financial position

Registered number: 02679874
as at 31 March 2021

	Notes	2021 £000	2020 £000
Assets			
Non-current assets			
Property, plant and equipment	13	1,631,312	1,595,916
Right of use assets	13	11,952	12,929
Intangible assets	12	8,787	9,568
Amount due from parent undertaking	15	–	135,941
Defined benefit pension surplus	24	34,368	35,912
		1,686,419	1,790,266
Current assets			
Inventories	16	673	689
Trade and other receivables	17	86,735	84,441
Cash and cash equivalents	18	41,617	12,981
		129,025	98,111
Total assets		1,815,444	1,888,377
Liabilities			
Non-current liabilities			
Trade and other payable	21	4,623	4,997
Loans and borrowings	19	1,038,371	1,028,997
Deferred income	23	3,625	3,438
Defined benefit pension liabilities	24	3,172	3,115
Deferred tax liability	9	167,228	166,352
		1,217,019	1,206,899
Current liabilities			
Trade and other liabilities	21	88,961	97,627
Loans and borrowings	19	80,318	30,329
Deferred income	23	5,336	5,418
Provisions	20	7,983	4,457
		182,598	137,831
Total liabilities		1,399,617	1,344,730
Net assets		415,827	543,647
Issued capital and reserves attributable to owners of the parent			
Share capital	25	49,312	49,312
Revaluation reserve		235,774	241,386
Retained earnings		130,741	252,949
Total equity		415,827	543,647

The notes on pages 194 to 247 form part of these financial statements.

The financial statements on pages 186 to 247 were approved and authorised for issue by the board of directors on 15 July 2021 and were signed on its behalf by:



DAVID HINTON
CHIEF EXECUTIVE OFFICER
15 JULY 2021



ANDREW FARMER
CHIEF FINANCIAL OFFICER
15 JULY 2021

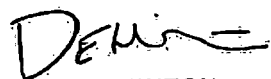
Company statement of financial position

Registered number: 02679874
as at 31 March 2021

	Notes	2021 £000	2020 £000
Assets			
Non-current assets			
Property, plant and equipment	13	1,631,312	1,595,916
Right of use assets	13	11,952	12,929
Intangible assets	12	8,787	9,568
Amount due from parent undertaking	15	–	135,941
Defined benefit pension surplus	24	34,368	35,912
		1,686,419	1,790,266
Current assets			
Inventories	16	673	689
Trade and other receivables	17	86,360	84,063
Cash and cash equivalents	18	41,441	12,981
		128,474	97,733
Total assets		1,814,893	1,887,999
Liabilities			
Non-current liabilities			
Trade and other payables	21	4,623	4,997
Loans and borrowings	19	1,038,371	1,028,997
Deferred income	23	3,625	3,438
Defined benefit pension liabilities	24	3,172	3,115
Deferred tax liability	9	167,228	166,352
		1,217,019	1,206,899
Current liabilities			
Trade and other liabilities	21	89,905	98,729
Loans and borrowings	19	80,318	30,329
Deferred income	23	5,336	5,418
Provisions	20	7,983	4,457
		183,542	138,933
Total liabilities		1,400,561	1,345,832
Net assets		414,332	542,167
Issued capital and reserves attributable to owners of the company			
Share capital	25	49,312	49,312
Revaluation reserve		235,774	241,386
Retained earnings		129,246	251,469
Total equity		414,332	542,167

The notes on pages 194 to 247 form part of these financial statements.

The financial statements on pages 186 to 247 were approved and authorised for issue by the board of directors on 15 July 2021 and were signed on its behalf by:


DAVID HINTON
CHIEF EXECUTIVE OFFICER
15 JULY 2021


ANDREW FARMER
CHIEF FINANCIAL OFFICER
15 JULY 2021

Group statement of changes in equity

for the year ended 31 March 2021

	Notes	Issued share capital £000	Revaluation reserve £000	Retained earnings £000	Total equity £000
At 1 April 2019		49,312	251,259	238,253	538,824
Comprehensive income for the year					
Profit for the year		-	-	16,884	16,884
Other comprehensive income	26	-	-	3,828	3,828
Total comprehensive income		-	-	20,712	20,712
Dividends	10	-	-	(11,000)	(11,000)
Amortisation of revaluation reserve		-	(6,129)	6,129	-
Release revaluation reserve on disposals		-	(19)	19	-
Deferred tax on revaluation and retained earnings transfer ¹		-	1,164	(1,164)	-
Impact of deferred tax rate change		-	(4,889)	-	(4,889)
		-	(9,873)	(6,016)	(15,889)
At 31 March 2020		49,312	241,386	252,949	543,647
At 1 April 2020		49,312	241,386	252,949	543,647
Comprehensive income for the year					
Profit for the year		-	-	31,316	31,316
Other comprehensive income	26	-	-	(12,123)	(12,123)
Total comprehensive income		-	-	19,193	19,193
Dividends	10	-	-	(147,013)	(147,013)
Amortisation of revaluation reserve		-	(6,127)	6,127	-
Revaluation of infrastructure assets		-	(783)	783	-
Release revaluation reserve on disposals		-	(15)	15	-
Deferred tax on revaluation and retained earnings transfer ¹		-	1,313	(1,313)	-
		-	(5,612)	(141,401)	(147,013)
At 31 March 2021		49,312	235,774	130,741	415,827

All transactions relate to the equity holders of the group.

The notes on pages 194 to 247 form part of these financial statements.

¹ The movement between the revaluation reserve and retained earnings arises from the depreciation and associated deferred tax on the fair value uplift of assets at the time of transition to IFRS¹

Company statement of changes in equity

for the year ended 31 March 2021

	Notes	Issued share capital £000	Revaluation reserve £000	Retained earnings £000	Total equity £000
At 1 April 2019		49,312	251,259	236,802	537,373
Comprehensive income for the year					
Profit for the year		-	-	16,855	16,855
Other comprehensive income	26	-	-	3,828	3,828
Total comprehensive income		-	-	20,683	20,683
Dividends	10	-	-	(11,000)	(11,000)
Amortisation revaluation reserve		-	(6,129)	6,129	-
Release revaluation reserve on disposals		-	(19)	19	-
Deferred tax on revaluation and retained earnings transfer		-	1,164	(1,164)	-
Impact of deferred tax rate change		-	(4,889)	-	(4,889)
		-	(9,873)	(6,016)	(15,889)
At 31 March 2020		49,312	241,386	251,469	542,167
At 1 April 2020		49,312	241,386	251,469	542,167
Comprehensive income for the year					
Profit for the year		-	-	31,301	31,301
Other comprehensive income	26	-	-	(12,123)	(12,123)
Total comprehensive income		-	-	19,178	19,178
Dividends	10	-	-	(147,013)	(147,013)
Amortisation of revaluation reserve		-	(6,127)	6,127	-
Revaluation of infrastructure assets		-	(783)	783	-
Release revaluation reserve on disposals		-	(15)	15	-
Deferred tax on revaluation and retained earnings transfer		-	1,313	(1,313)	-
		-	(5,612)	(141,401)	(147,013)
At 31 March 2021		49,312	235,774	129,246	414,332

All transactions relate to the equity holders of the company.

The notes on pages 194 to 247 form part of these financial statements.

Group statement of cash flows

for the year ended 31 March 2021

	Notes	2021 £000	2020 £000
Cash flows from operating activities			
Profit for the year		31,316	16,884
Adjustments for			
Depreciation and impairment of property, plant and equipment	13	55,259	51,615
Amortisation of intangible assets	12	3,497	3,049
Finance income	8	(3,093)	(5,333)
Finance expense	8	42,956	52,862
Loss/(gain) on sale of property, plant and equipment		723	(50)
Difference between pension contributions paid and amounts recognised in the income statement		(12,605)	(4,896)
Taxation on profit on ordinary activities	9	6,343	16,918
		124,396	131,049
Movements in working capital:			
Increase in trade and other receivables		(2,435)	(1,165)
Decrease/(increase) in inventories		16	(97)
(Decrease)/increase in trade and other payables		(2,053)	4,656
Cash generated from operations		119,924	134,443
Income taxes (paid)/refunded		(1,623)	44
Interest element on lease liability payments		(128)	(110)
Interest received		2,341	4,705
Interest paid		(35,919)	(41,828)
Net cash generated by operating activities		84,595	97,254
Cash flows from investing activities			
Purchase of property, plant and equipment		(92,129)	(96,153)
Proceeds from disposal of property, plant and equipment		215	94
Purchase of intangible assets		(2,716)	(2,116)
Net cash used in investing activities		(94,630)	(98,175)
Cash flows from financing activities			
Loan from Parent undertaking repaid		136,013	54,000
Loan drawdown/(repayments) of borrowings		50,000	(336,550)
Proceeds from bank borrowings		-	120,000
Loan note issued		-	175,000
Issue costs of listed debt paid		-	(130)
Payment of lease liabilities		(329)	(222)
Dividends paid to shareholders	10	(147,013)	(11,000)
Net cash from financing activities		38,671	1,098
Net cash increase in cash and cash equivalents		28,636	177
Cash and cash equivalents at the beginning of year		12,981	12,804
Cash and cash equivalents at the end of the year	18	41,617	12,981

The notes on pages 194 to 247 form part of these financial statements.

Company statement of cash flows

for the year ended 31 March 2021

	Notes	2021 £000	2020 £000
Cash flows from operating activities			
Profit for the year		31,301	16,855
Adjustments for			
Depreciation and impairment of property, plant and equipment	13	55,259	51,615
Amortisation of intangible assets	12	3,497	3,049
Finance income	8	(3,092)	(5,308)
Finance expense	8	42,979	52,895
Loss/(gain) on sale of property, plant and equipment		723	(50)
Difference between pension contributions paid and amounts recognised in the income statement		(12,605)	(4,896)
Taxation on profit on ordinary activities	9	6,339	16,911
		124,401	131,071
Movements in working capital:			
Increase in trade and other receivables		(2,435)	(1,165)
Decrease/(increase) in inventories		16	(97)
(Decrease)/increase in trade and other payables		(2,053)	4,656
Cash generated from operations		119,929	134,465
Income taxes (paid)/refunded		(1,616)	55
Interest element on lease liability payments		(128)	(110)
Interest received		2,339	4,680
Interest paid		(36,105)	(41,639)
Net cash generated by operating activities		84,419	97,451
Cash flows from investing activities			
Purchase of property, plant and equipment		(92,129)	(96,153)
Proceeds from disposal of property, plant and equipment		215	94
Purchase of intangible assets		(2,716)	(2,116)
Net cash used in investing activities		(94,630)	(98,175)
Cash flows from financing activities			
Loan from Parent undertaking repaid		136,013	54,000
Loan drawdown/(repayments) of borrowings		50,000	(336,550)
Proceeds from bank borrowings		-	120,000
Loan note issued		-	175,000
Issue costs of listed debt paid		-	(130)
Payment of lease liabilities		(329)	(222)
Dividends paid to shareholders	10	(147,013)	(11,000)
Net cash from financing activities		38,671	1,098
Net cash increase in cash and cash equivalents		28,460	374
Cash and cash equivalents at the beginning of year		12,981	12,607
Cash and cash equivalents at the end of the year	18	41,441	12,981

The notes on pages 194 to 247 form part of these financial statements.

Notes to the consolidated financial statements

for the year ended 31 March 2021

1. BASIS OF PREPARATION AND AUTHORISATION OF FINANCIAL STATEMENTS

The financial statements of South East Water and its subsidiary (the "group") for the year ended 31 March 2021 were authorised for issue by the board of Directors on 12 July 2021 and the Statement of Financial Position was signed on the board's behalf by David Hinton and Andrew Farmer. South East Water is a private company that has limited liability by shares and is incorporated in the United Kingdom and domiciled in England and Wales.

The group's consolidated and company's individual financial statements have been prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

Details of the group's accounting policies, including changes during the year, are included in note 3.

The group financial statements are presented in Sterling and all values are rounded to the nearest thousand pounds (£000) except where otherwise indicated.

1.1 BASIS OF MEASUREMENT

The financial statements have been prepared on the historical cost basis except for the following items, which are measured on an alternative basis on each reporting date.

Items	Measurement basis
Pension assets	Fair value
Certain assets in property, plant and equipment	Measured at deemed cost by reference to fair value on adoption of IFRS on 1 April 2014

1.2 CHANGES IN ACCOUNTING POLICIES

i) New standards, interpretations and amendments effective from 1 April 2020

The group has adopted all new accounting standards and interpretations with mandatory adoption date on or before 1 April 2020. Their adoption has not had any material impact on the disclosures or on the amounts reported in these financial statements.

ii) New standards, interpretations and amendments not yet effective

At the date of these financial statements, the following Standards and Interpretations were in issue but not yet effective (and in some cases had not yet been adopted by the UK) and have not been applied to these Financial Statements:

New standard or interpretation		
IFRS 7 (amended)	Financial Instruments: Disclosures	1 April 2021
IFRS 8 (amended)	Operating Segments	Date not released by IASB
IFRS 9 (amended)	Financial Instruments	1 April 2022
IFRS 16 (amended)	Leases	1 April 2021
IFRS 17	Insurance contracts (replaces IFRS 4)	1 April 2023
IAS 1 (amended)	Presentation of Financial Statements	1 April 2023
IAS 8 (amended)	Accounting Policies, Changes in Accounting Estimates and Errors	1 April 2023
IAS 12 (amended)	Income taxes	1 April 2023
IAS 16 (amended)	Property, Plant and Equipment	1 April 2022
IAS 37 (amended)	Provisions, Contingent Liabilities and Contingent Assets	1 April 2022
IAS 41 (amended)	Agriculture	1 April 2022

The directors do not anticipate that the adoption of the Standards and interpretations listed above will have a material impact on the finances of the group or company, but may have an impact on the presentation in the financial statements of the group or company in future periods.

Notes to the consolidated financial statements

for the year ended 31 March 2021

2. KEY JUDGEMENTS AND SOURCES OF ESTIMATION UNCERTAINTY

2.1 KEY JUDGEMENTS

The preparation of financial statements requires the application of judgements and assumptions by management which affects the value of assets and liabilities at the balance sheet date and income and expenditure for the year. Actual results may differ from those arrived at based on management's judgements and assumptions.

Our key judgements and sources of estimation uncertainty have been considered in light of the ongoing Covid-19 pandemic. Where a judgment or assumption is impacted by Covid-19, this is noted in the relevant section. Where there is no reference to Covid-19, this is because it is not considered that Covid-19 affects a particular judgement or assumption.

The capitalisation of costs including employee and other directly attributable costs

The group incurs significant expenditure on its infrastructure assets and management has to exercise judgement in determining the classification of these costs between capital and operating expenditure. The group capitalises expenditure where the expenditure enhances assets or increases the capacity of the network. Expenditure which maintains the asset's potential to deliver future economic benefits is commonly referred to as "repairs and maintenance" and is recognised in the income statement in the period in which it is incurred. Differentiating between enhancement and maintenance works can be subjective, particularly where projects may include both activities.

The group determines employee costs directly attributable to capital projects based on the time spent on the projects. Other directly attributable costs are then assessed. The costs relating to capital projects are then capitalised into individual projects. During the year £12.7 million of employee and other directly attributable costs have been capitalised (2020: £11.8 million). In addition, the group capitalises borrowing costs incurred for significant projects that meet certain criteria and judgement is required to identify which projects qualify for this. The capitalised borrowing costs for property, plant and equipment for the year ended 31 March 2021 were £2.7 million (2020: £2.8 million).

Provisions for other liabilities and charges – recognition of other provisions

A provision is recognised when it is probable that the Group has an obligation for which a reliable estimate can be made of the amount of the obligation. The Group is subject to commercial and legal claims that are incidental to the day-to-day operation of its business. These could include contractual, regulatory, employment and environmental matters which are managed in the ordinary course of business. Assessing the outcome of uncertain commercial and legal cases requires judgement to be made regarding the extent to which any claim against the Group is likely to be successful. On a case-by-case basis, management evaluates the likelihood of adverse outcomes to these matters and makes a judgement about whether or not a provision should be recognised.

Other provisions, which are detailed in note 20, total £3.5 million at the year ended 31 March 2021 (2020: £nil).

Retirement benefit obligations – recognition of a defined benefit asset

The Trust Deeds for the South East Water Pension Scheme (SEWPS) and the Mid Kent Group Pension Scheme (MKGPS) provide the group with an unconditional right to a refund of surplus assets assuming the full settlement of plan liabilities in the event of a plan winding-up. Furthermore, in the ordinary course of business the Trustee has no rights to unilaterally wind-up the schemes or otherwise augment the benefits due to members of the schemes. Based on these rights, the Group considers that under IFRIC 14, it is appropriate to recognise the net surpluses in SEWPS and MKGPS of £10.7 million (2020: £15.1 million) and £23.7 million (2020: £20.8 million) respectively in full.

Notes to the consolidated financial statements

for the year ended 31 March 2021

2. ACCOUNTING ESTIMATES AND JUDGEMENTS continued

2.2 KEY SOURCES OF ESTIMATION UNCERTAINTY

Estimates are required to be made by management when preparing the financial statements. These estimates affect the value of assets and liabilities at the balance sheet date and income and expenditure for the year. The estimates and underlying assumptions are reviewed on an ongoing basis with any revisions to accounting estimates recognised in the period in which the estimate is revised and future periods where the revision affects both current and future periods. The actual results may differ from those arrived at based on management's estimates.

Unbilled water income

Unbilled water income at the year-end (Household customers): metered customers are billed on a six monthly cycle. This means that at the year-end there is a large volume of water which has been supplied but not billed to customers. The value of unbilled water income at 31 March 2021 is estimated to be £36.6 million (2020: £34.2 million).

The methodology for arriving at the value of unbilled consumption incorporates estimates of water used based on historical consumption data and the relevant tariffs for customers. Previously billed consumption history provides a reliable basis for the estimate that is included in the financial statements. Our historical analysis of consumption indicates that billed revenue has been within 2 per cent of our previous estimates of the value of unbilled consumption.

The methodology adopted is consistent with prior years but higher household water consumption over the year, largely a result of the Covid-19 restrictions, has resulted in the value of unbilled water at the end of the current year being higher than that for the prior year.

The sensitivity of the estimate of unbilled consumption is illustrated in the table below where the impact of fluctuations in estimated water consumption in one year of one per cent and three per cent have been set out. These variants have been selected because, in previous years, our annual assessment of unbilled revenue has been between 1 per cent and 2 per cent of actual billed revenue.

	31 March 2021	Sensitivity			
		+1%	+2%	-1%	-2%
Unbilled water income	£36.6 m	+£0.4 m	+£0.7 m	-£0.4 m	-£0.7 m

Unbilled water income at the year end (Wholesale customers): Water revenue chargeable to wholesale customers is governed by the Market Settlement Process and information provided by the Central Market Operating System. System data is used to estimate the amount of unbilled revenue in respect of wholesale customers. As at 31 March 2021, the level of unbilled revenue was estimated to be £3.3 million (2020: £3.8 million).

The methodology adopted is consistent with prior years but significantly lower non-household water consumption over the year, largely a result of the Covid-19 restrictions on businesses, has resulted in the value of unbilled water at the end of the current year being lower than that for the prior year.

	31 March 2021	Sensitivity			
		+1%	+2%	-1%	-2%
Unbilled water income	£3.3 m	+£0.03 m	+£0.07 m	-£0.03 m	-£0.07 m

Notes to the consolidated financial statements

for the year ended 31 March 2021

2. ACCOUNTING ESTIMATES AND JUDGEMENTS continued

2.2 KEY SOURCES OF ESTIMATION UNCERTAINTY continued

The useful lives of infrastructure and non-infrastructure assets

Management estimates the useful economic lives of infrastructure and non-infrastructure assets employed by the group in meeting its business objectives. Tangible and intangible assets are categorised by type of asset or equipment and an appropriate estimate of how long the assets in each category will remain operational and economically viable is made. This estimate will determine the value of depreciation charged to the income statement each year and the carrying value of fixed assets in the balance sheet.

The estimates are based on management's judgement and experience and are reviewed annually to ensure they are still suitable. Additionally, an impairment review of assets is undertaken each year to identify any assets that may be impaired and to write down the value of those assets to the recoverable amount.

The sensitivity on the annual depreciation charge due to the estimates of asset lives is illustrated in the tables below using examples of the lives attributed to:

- Wells & boreholes of 60 years
- Light plant and machinery of 20 years
- Computer software of 5 years

	31 March 2021	Sensitivity			
		+5 years	+20 years	-5 years	-20 years
Wells & boreholes	£3.0 m	-£0.2 m	-£0.8 m	+£0.3 m	+£1.5 m

	31 March 2021	Sensitivity			
		+5 years	+10 years	-5 years	-10 years
Light plant and machinery	£20.8 m	-£4.6 m	-£6.9 m	+£6.9 m	+£20.8 m

	31 March 2021	Sensitivity			
		+1 year	+3 years	-1 year	-3 years
Computer software	£1.7 m	-£0.3 m	-£0.6 m	+£0.4 m	+£2.6 m

Notes to the consolidated financial statements

for the year ended 31 March 2021

2. ACCOUNTING ESTIMATES AND JUDGEMENTS continued

2.2 KEY SOURCES OF ESTIMATION UNCERTAINTY continued

Provision for doubtful trade receivables

Household Debt

Our Household customer base includes customers who cannot or will not pay their bills and, therefore, we need to make a provision for the level of doubtful debt. The value of the provision for doubtful debts as at 31 March 2021 was £27.5 million (2020: £24.6 million).

Our methodology establishes the expected credit loss of our household debt at the year-end by identifying customer debt categories and projecting historic cash collections across these customer groups to determine an estimate of irrecoverable debt. The estimated cash collection percentages take into account historical performance. Our cash collection history over the past three years has been used to determine future collection rates. This marks a change in methodology from the prior year where cash collection history over the past four years has been used. This change in approach is as a result of Covid and the impact that the pandemic has had on household finances, and places a greater weight on cash collection history over the last year when Covid has been a factor.

The sensitivity of the bad debt provision is illustrated in the table below where the impact of using a cash collection history over the past four years, as was the case in the prior year, and over the last two years as the basis for determining the expected credit loss is shown.

	31 March 2021	Cash collection history	
		2 years	4 years
Bad debt provision estimate	£27.5 m	+£0.8 m	-£0.7 m

Retailer Debt

South East Water provides wholesale supply to Retailers through the Non-household market/(MOSL). Trading terms are governed under the Wholesale Code and as such we secure collateral from Business Retailers in the form of bank guarantee, deposit or other form of security. At the year end, our assessment is that the security provided by Business Retailers obviates the need to make a provision against retailer debt.

Management has reviewed the estimates included in the wholesale provisions and we do not consider there to be any need for further adjustment to reflect the impact of Covid-19 due to the security and guarantees held by the group as is noted above.

Pension and other post-employment benefits

There are a range of variables required to be determined to value the company's defined benefit pension schemes and the underlying costs of providing post employment benefit.

The costs of defined benefit pension schemes are determined using actuarial valuations. The actuarial valuations are determined by using certain assumptions for discount rates, mortality rates, expected return on assets and corporate bond performance projections as set out in note 24. Pension increases are based on expected future inflation rates. The net defined benefit pension scheme asset at 31 March 2021 is £34.4 million (2020: asset of £32.8 million) and is recognised in full.

The sensitivity of the estimate of the surplus in the pension schemes is illustrated in the table below where the impact of fluctuations in prevailing market conditions on key assumptions of discount rate, inflation and life expectancy have been set out.

Notes to the consolidated financial statements

for the year ended 31 March 2021

Sensitivities	Decrease in schemes' surplus	
0.1% decrease to the discount rate	£4.0 m	1.5%
0.1% increase to inflation	£3.5 m	1.3%
One year increase in life expectancy	£12.5 m	4.6%

Our assumptions have been set with a long-term view of the key factors and therefore the impact of the Covid-19 outbreak and prevailing economic factors in the short to medium term are not considered to have an impact on this key estimate. In particular, no allowance has been made for deaths over 2020 due to the uncertainty over the long term impact of Covid-19. If an allowance was made for 2020 excess deaths, this would reduce liabilities.

3. ACCOUNTING POLICIES

Our accounting policies have been considered against the background of the Covid-19 outbreak and, where appropriate, relevant factors have been taken into account in preparing our financial statements.

The principal accounting policies adopted by the group are set out below. These policies have been consistently applied in both the current and prior years, except for those changes required due to the mandatory adoption of new reporting standards.

3.1 GOING CONCERN

The directors have, at the time of approving the financial statements, a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. In coming to this decision they have considered the implications of the on-going Covid-19 pandemic and the impact this may have on the business. The directors have also considered the discussions that are on-going for the replacement of the revolving credit facility which has received credit approval and will be completed in 2021. The directors have concluded that it is correct to continue to adopt the going concern basis of accounting in preparing the financial statements. Further details are provided in the strategic report on page 111.

3.2 BASIS OF CONSOLIDATION

These financial statements incorporate the financial information of South East Water Limited and its subsidiary, South East Water (Finance) Limited (together the "group").

Transactions and balances between the company and its subsidiary have been eliminated fully on consolidation. Subsidiaries are consolidated from the date on which control is transferred to the group and cease to be consolidated from the date on which control is transferred out of the group.

Notes to the consolidated financial statements

for the year ended 31 March 2021

3. ACCOUNTING POLICIES continued

3.3 REVENUE

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the group, there has been a transfer of risk and control and the revenue can be reliably measured. All revenue arises within the United Kingdom and is recorded net of VAT. The company only recognises revenue in respect of "named" customers, that is the company will not bill an address without first knowing the name of the person living at the address. Specific recognition criteria must also be met before revenue is recognised as detailed below.

Metered and unmetered income

The performance obligation of the company for metered and unmetered income is the supply of potable water to each named customer in the period under review.

Metered water income is recognised when water has been delivered to the customer and the performance obligation has been satisfied for the period. This income includes an estimation of the volume of mains water supplied but unbilled at the year end. This is estimated using a defined methodology as detailed under key sources of estimation uncertainty above.

Unmetered water income was invoiced in full for the financial year 2020/21 on 1 April 2020 and is recognised over the year as water is supplied to the named customer and the performance obligation is satisfied.

Cash received in advance from customers is not treated as current year revenue, being recognised as payments received in advance within creditors.

Infrastructure charges

Infrastructure charges represent the fees charged to property developers and others for connecting new properties and water outlets to the group's network. The performance obligation within these contracts is the completed connection of the relevant properties and outlets to the mains supply. These fees are recognised in the income statement upon completion of the performance obligation.

Grants and contributions

Grants and contributions are received in respect of both infrastructure and non-infrastructure assets and are usually received in advance of the work being undertaken by the company. The receipts are recognised as deferred income on the balance sheet upon receipt. The performance obligations for this income stream is the completion of the work to which contributions relate. The income is recognised in the income statement upon completion of the specific performance obligations.

Notes to the consolidated financial statements

for the year ended 31 March 2021

3.3 REVENUE continued

Other income

Other income includes rechargeable works' charges and charges for engineering, scientific, laboratory, billing and cash collection services.

The performance obligations for rechargeable works are the installation of meters and the connection of new property developments to the mains supply. The income for rechargeable works is recognised when the performance obligations are completed.

The performance obligations for the remaining other income is for the supply of services as detailed in the specific contracts with customers and is recognised in the income statement when the work to which it relates is complete.

Finance income

Finance income is recognised using the effective interest rate method.

3.4 TAXATION

Current tax, being UK Corporation Tax, is provided at amounts expected to be paid (or recovered) using tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Tax relating to items recognised directly in equity is also recognised directly in equity and not in the income statement.

Deferred tax is provided using the balance sheet method on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts in the financial statements.

Deferred tax liabilities are recognised for all taxable temporary differences except where the deferred tax liability arises from goodwill amortisation or the initial recognition of an asset or liability in a transaction that is not a business combination and at the time of the transaction affects neither the accounting profit nor taxable profit or loss.

Deferred tax assets are recognised for all deductible temporary differences and the carry forward of unused tax assets and losses to the extent that it is probable that taxable profits will be available against which the deductible temporary differences and the carry forward of unused tax assets and losses can be utilised.

Deferred tax assets are recognised for the deductible temporary differences arising from the initial recognition of an asset or liability in a transaction that is not a business combination and at the time of the transaction affects neither the accounting profit nor taxable profit or loss.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the balance sheet date. In accordance with IAS 12 Income Taxes, deferred taxes are not discounted.

3.5 DIVIDENDS

Dividends are recorded in the financial statements in the year in which they are approved by the board.

3.6 INVESTMENTS IN SUBSIDIARIES

Investments are recorded at historical cost. Where the directors are of the opinion that there has been a permanent diminution in the value of investments, the carrying amount of such investments is written down to the recoverable amount.

Notes to the consolidated financial statements

for the year ended 31 March 2021

3. ACCOUNTING POLICIES continued

3.7 INTANGIBLE ASSETS

(i) Intangible assets externally acquired

Intangible assets externally acquired are recognised at cost. They have finite useful lives and are amortised over three to five years on a straight-line basis. Residual values and useful lives of all assets are re-assessed annually and, where necessary, changes are accounted for prospectively.

Employee and other costs directly attributable to intangible asset projects are capitalised in the financial statements as part of the cost of the intangible asset to which they relate. Training costs, administration and other general overhead costs including interest are not capitalised.

(ii) Derecognition of intangible assets

An intangible asset is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset, calculated as the difference between the net disposal proceeds and the carrying amount of the item, is included in the income statement in the year in which the item is derecognised.

3.8 PROPERTY, PLANT AND EQUIPMENT

Infrastructure assets

Infrastructure assets comprise a network of systems relating to water distribution. Infrastructure assets in the course of construction are depreciated from the time they are brought into use. All other infrastructure assets are stated at cost less accumulated depreciation and any impairment in value. Depreciation is calculated on a straightline basis over the estimated useful life of the assets, being between 20 years and 100 years for all infrastructure assets, except surface reservoirs, which have useful economic lives of 250 years.

Non-infrastructure assets

Freehold land is not depreciated. Assets in the course of construction are depreciated from the time they are brought into use. All other non-infrastructure assets are stated at cost less accumulated depreciation and any impairment in value. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

Freehold buildings: 80 years

Operational structures: 50-80 years

Fixed plant and machinery: 10-35 years

Meters, vehicles, mobile plant, computers, furniture and office equipment: 3-10 years

Derecognition

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year the item is derecognised.

Residual values and useful lives

Residual values and useful lives of all assets are re-assessed annually and, where necessary, changes are accounted for prospectively.

Capitalisation of employee and other directly attributable costs

Employee and other costs, including borrowing costs, directly attributable to capital projects are capitalised in the financial statements as part of the cost of the property, plant and equipment to which they relate. Training costs, administration and other general overhead costs are not capitalised.

Notes to the consolidated financial statements

for the year ended 31 March 2021

3. ACCOUNTING POLICIES continued

3.8 PROPERTY, PLANT AND EQUIPMENT continued

Leased assets

Property, plant and equipment held under leases are capitalised at the lower of the fair value of the leased asset and the present value of the minimum lease payments. These assets are depreciated over the shorter of the estimated useful life of the asset and the lease term.

Impairment of property, plant and equipment, investments and intangible assets

At each reporting date an assessment is carried out to determine whether there is any indication that property, plant and equipment, investments and software intangible assets may be impaired. If there is an indication of impairment, the recoverable amount of the asset or respective cash-generating unit is compared to the carrying amount. Where the recoverable amount is less than the carrying amount, the asset value is reduced to the recoverable amount with an impairment loss recognised as an operating cost in the income statement in the year in which the respective assessment takes place.

3.9 BORROWING COSTS

Borrowing costs are incurred on the group's general borrowings. Where appropriate borrowing costs are attributed to qualifying assets in line with IAS 23 Borrowing Costs. Otherwise borrowing costs are expensed as incurred. See note 6 for further details.

3.10 INVENTORIES

Inventory is valued at the lower of average cost or net realisable value. The stocks of treated water held by the group are valued at £nil. Consumable chemical purchases are recognised as an expense in the income statement at the point they are received on site for use, either from central stores or from suppliers direct.

Work-in-progress for chargeable services is valued at the lower of cost and net realisable value.

3.11 PROVISIONS

A provision is recognised when the group has a legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are measured at management's best estimate of the expenditure required to settle the present obligation at the balance sheet date. Where the effect is material, expected future cash flows are discounted using a current pre-tax rate that reflects the risks specific to the liability.

3.12 SHORT-TERM TRADE AND OTHER RECEIVABLES

Short-term trade receivables are initially measured at their transaction price in line with the provisions of IFRS 9. The carrying value for trade receivables includes an allowance for the lifetime expected credit loss (doubtful debts) of the outstanding debts. An estimate for the expected credit loss is calculated by the group's management in accordance with the defined methodology detailed under key sources of estimation uncertainty above.

3.13 CASH AND CASH EQUIVALENTS

Cash and cash equivalents in the statement of financial position comprise cash at bank and in hand and short-term deposits with an original maturity of three months or less.

Included within cash and cash equivalents are amounts that are held in designated bank accounts as short-term deposits in order to meet the interest falling due in respect of listed debt and other long-term borrowings.

3.14 TRADE PAYABLES

Trade payables are measured at fair value and subsequently measured at amortised cost.

Notes to the consolidated financial statements

for the year ended 31 March 2021

3. ACCOUNTING POLICIES continued

3.15 FINANCIAL INSTRUMENTS

The group's financial instruments comprise fixed and variable rate borrowings, index linked loans, fixed rate debentures, lease liabilities, a loan to its parent undertaking, cash, short-term and medium-term bank deposits, trade receivables and trade and other payables.

Recognition

Financial instruments are recognised on the statement of financial position when the group becomes party to the contractual provisions of the instrument. The group determines the classification of its financial liabilities at initial recognition.

Impairment of financial assets

A provision for twelve month expected credit loss on new financial assets is recognised in the income statement to establish a loss allowance on initial recognition in line with the impairment requirements of IFRS 9.

At each reporting date an assessment is carried out to determine whether there is any indication that the credit risk on financial assets has increased significantly. If this is considered to be the case, full life-time expected credit loss is recognised in the income statement.

Where there is objective evidence that an impairment loss has arisen, the loss is recognised in the income statement in the year in which the respective assessment takes place. Impaired debts are derecognised when they are assessed as irrecoverable.

Derecognition

Financial liabilities are removed from the statement of financial position when the related obligation is discharged, cancelled or it expires.

Financial assets are removed from the statement of financial position when the rights to the cash flows from the asset expire, or when the risks and rewards of ownership of the asset are transferred or when control of the asset is transferred.

Embedded derivatives

Financial instruments that are not carried at fair value through the income statement are reviewed to determine if they contain embedded derivatives. Embedded derivatives are accounted for separately as derivative financial instruments when the economic characteristics and risks are not closely related to the respective host financial instrument.

Interest bearing loans and borrowings

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of issue costs associated with the borrowing.

Interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Liabilities arising on leases

The initial values of lease liabilities equate to the present value of future lease payments under the relevant lease contracts. The group have applied the practical expedient of using a single discount rate to leases with reasonably similar characteristics. The discount rates used in calculating the liabilities reflect the interest rates at which the group would currently be able to borrow in order to finance similar assets to those under the lease affected by the transition (the incremental borrowing rate).

Notes to the consolidated financial statements

for the year ended 31 March 2021

3. ACCOUNTING POLICIES continued

3.16 REVALUATION RESERVE

The revaluation reserve was created on the adoption of IFRS when the company took the option to treat the revalued amounts as deemed cost. This reserve is released over the life of the underlying assets to which it relates in line with the depreciation of the revalued assets and transferred to retained earnings. The revaluation uplift remaining on any assets that are disposed of is also transferred to retained earnings at the time of the disposal.

3.17 RESEARCH AND DEVELOPMENT

Research costs are charged to the income statement in the year in which they are incurred.

Development costs are capitalised based on management's judgement that the technological and economic feasibility of a project is confirmed, usually when a project has reached a defined milestone according to an established project management model. In determining the amounts to be capitalised management makes assumptions regarding the expected future cash generation of the assets, discount rates to be applied and the expected period of benefits.

3.18 DEFINED CONTRIBUTION SCHEMES

Contributions to defined contribution pension schemes are charged to the consolidated statement of comprehensive income in the year to which they relate.

3.19 DEFINED BENEFIT SCHEMES

The pension scheme asset or liability in the statement of financial position represents the net present value of the defined benefit obligation and the fair value of scheme assets at the balance sheet date. The present value of the defined benefit obligation is analysed between the funded and unfunded pension plans.

The present value of the defined benefit obligation and the cost of providing benefits under defined benefit plans is determined on a triennial basis, and updated to each year end by an independent qualified actuary using the Projected Unit Credit actuarial valuation method, discounted at an interest rate equivalent at measurement date to the rate of return on a high quality corporate bond of equivalent term and currency to the scheme liabilities.

The pension cost in the income statement includes current and past service cost and the effect of any settlements and curtailments. A net finance charge or credit is recognised within finance costs in the income statement and comprises the net of the expected return on pension scheme assets and the interest on pension scheme liabilities.

All actuarial gains and losses and the related deferred taxation are recognised in the statement of comprehensive income.

4. TOTAL INCOME

The following is an analysis of the group and company's revenue for the year from continuing operations:

Group and Company	2021 £000	2020 £000
Revenue		
Unmetered water income	19,983	20,800
Metered water income	219,168	208,405
Other sales	9,005	14,276
Total revenue	248,156	243,481
Other income		
Rent receivable	1,174	1,284
Other income	10,265	10,915
Total other income	11,439	12,199
	259,595	255,680

Notes to the consolidated financial statements

for the year ended 31 March 2021

All revenue is from customers within the United Kingdom.

Other sales includes new connections income of £5.3 million (2020: £5.8 million), infrastructure income of £1.8 million (2020: £5.8 million) and capital contributions of £1.8 million (2020: £1.4 million).

Other income includes charges for billing and cash collection services amounting to £8 million (2020: £7.6 million), and laboratory income of £2.3 million (2020: £2.5 million).

5. SEGMENTAL ANALYSIS

The group's revenue mainly arises from the supply of water and related activities. The activities of the group, for management purposes, fall into three operating areas being the supply of potable water on a wholesale and retail basis, both of which are governed by the Water Act 2014, and related non-regulated activities.

	Wholesale activities £000	Retail activities £000	Other activities £000	Total £000
Year ended 31 March 2021				
Total income	226,711	28,952	3,932	259,595
Profit from operations	44,643	28,952	3,927	77,522
Finance costs				(42,956)
Finance income				3,093
Profit before taxation				37,659
Taxation				(6,343)
Profit for the year				31,316
Year ended 31 March 2020				
Total income	221,820	21,749	12,111	255,680
Profit from operations	72,803	3,568	4,960	81,331
Finance costs				(52,862)
Finance income				5,333
Profit before taxation				33,802
Taxation				(16,918)
Profit for the year				16,884

The group analyses results by segment to profit from operations only, so no segmental statement of financial position or statement of cash flows are presented.

Notes to the consolidated financial statements

for the year ended 31 March 2021

6. NET OPERATING COSTS

Group	2021 £000	2020 £000
Employee benefits expense	26,919	30,166
Asset expense/(income):		
Depreciation – owned assets	51,922	50,537
Depreciation – right-of-use assets	985	885
Amortisation of intangible assets	3,497	3,049
Impairment of property, plant and equipment	2,353	193
Loss/(gain) on disposal of property, plant and equipment	723	(50)
	59,480	54,614
Other operating expenses:		
Operating lease rentals:		
Vehicles and office equipment	255	242
Land and buildings	16	14
Fee payable to group's auditor (see below)	434	300
Energy costs	19,795	18,346
Rates	18,403	18,186
Contractors	28,727	26,218
Bulk water supplies and abstraction licences	9,251	8,619
Chemicals	3,797	3,524
Insurance and related costs	3,350	2,646
Other	13,500	12,435
Other operating expenses charged to capital projects	(5,642)	(5,159)
	91,886	85,371
Total operating costs	178,285	170,151

The other operating costs includes admin fee of £5,000 (2020: £22,000) for South East Water Finance.

Group and Company	2021 £000	2020 £000
Fees payable to the group's auditor in respect of:		
Audit of the group and company financial statements	325	208
Audit of subsidiary	1	1
Total audit	326	209
Regulatory accounts	84	49
Other assurance services	22	37
Services relating to iXBRL account coding	2	5
Total non-audit services	108	91
Total fees payable to the group's auditor	434	300

Notes to the consolidated financial statements

for the year ended 31 March 2021

7. EMPLOYEES AND DIRECTORS

Group and Company	Notes	2021 £000	2020 £000
Employee costs (including directors) comprise:			
Wages and salaries		34,842	31,124
National insurance		3,501	2,550
Defined contribution scheme cost	24	2,481	2,385
Defined benefit scheme (credit)/cost	24	(6,895)	710
Labour costs capitalised		(7,010)	(6,603)
		26,919	30,166

Key management personnel compensation

Emoluments of the directors, who are the group's key management, were:

	2021 £000	2020 £000
Aggregate emoluments including bonuses	1,092	1,666
Defined contribution scheme costs	14	10
	1,106	1,676

Emoluments of the highest paid director including bonuses were: £439,000 (2020: £647,000)

Retirement benefits are accruing to one director (2020: one) under the defined benefit pension schemes. There are currently two directors (2020: two) under a defined contribution scheme. Further disclosures in respect of directors' emoluments are set out in the remuneration report on page 142.

The monthly average number of persons, including the directors, employed by the Group during the year was as follows:

	2021 No.	2020 No.
Operations	416	434
Management and Administration	570	525
	986	959

Notes to the consolidated financial statements

for the year ended 31 March 2021

8. FINANCE INCOME AND EXPENSE

Group	2021 £000	2020 £000
Finance income		
Interest receivable on bank balances and short-term deposits	59	201
Interest receivable from group companies	2,273	4,499
Net interest income on defined benefit asset	761	633
Total finance income	3,093	5,333
Finance expense		
Debenture interest	30	42
Effective interest on listed debt	13,755	18,411
Interest on lease liabilities	128	110
Financing guarantee fees	949	1,430
Fair value movements on interest rate swap	-	2,713
Bank interest and other finance charges	8,350	5,068
Amortisation of loan issue costs	616	594
Indexation on variable rate bonds	2,383	4,378
Interest payable on index linked loans	12,745	12,500
Indexation on index linked loans	6,694	10,444
Interest capitalised	(2,694)	(2,828)
Total finance expense	42,956	52,862

Interest is capitalised at the weighted average rate of interest on the group senior long term debt of 3.7 per cent (2020: 4.25 per cent).

Notes to the consolidated financial statements

for the year ended 31 March 2021

8. FINANCE INCOME AND EXPENSE continued

Company	2021 £000	2020 £000
Finance income		
Interest receivable on bank balances and short-term deposits	58	176
Interest receivable from group companies	2,273	4,499
Net interest income on defined benefit asset	761	633
Total finance income	3,092	5,308
Finance expense		
Debenture interest	30	42
Interest payable to subsidiary	16,693	21,321
Indexation payable to subsidiary	4,600	7,392
Interest on lease liabilities	128	110
Financing guarantee fees	949	1,430
Fair value movements on interest rate swap	-	2,713
Bank interest and other finance charges	8,330	5,068
Amortisation of loan issue costs	636	594
Interest payable on index linked loans	9,830	9,623
Indexation on index linked loans	4,477	7,430
Interest capitalised	(2,694)	(2,828)
Total finance expense	42,979	52,895

Interest is capitalised at the weighted average rate of interest on the group senior long term debt of 3.7 per cent (2020: 4.25 per cent).

Notes to the consolidated financial statements

for the year ended 31 March 2021

9. TAXATION

9.1 INCOME TAX RECOGNISED IN INCOME STATEMENT

Group	2021 £000	2020 £000
Current tax		
Current tax on profits for the year	2,855	2,042
Adjustments in respect of prior years	(232)	(141)
Total current tax	2,623	1,901
Deferred tax expense		
Origination and reversal of timing differences	4,495	4,898
Adjustments in respect of prior years	(775)	(1,846)
Relating to impact of change in tax rate	-	11,965
Total deferred tax	3,720	15,017
Total tax expense	6,343	16,918

Total tax expenses above consists of £6,339,000 (2020: £16,911,000) for South East Water Limited and £4,000 (2020: £7,000) for South East Water (Finance) Limited.

The reasons for the difference between the actual tax charge for the year and the standard rate of corporation tax in the United Kingdom applied to profits for the year are as follows:

Group	2021 £000	2020 £000
Profit before taxation	37,659	33,802
Tax using the company's domestic tax rate of 19% (2020:19%)	7,155	6,423
Expenses not deductible for tax purposes	130	534
Adjustments to current tax charge in respect of prior years	(232)	(141)
Adjustment to deferred tax in respect of rate change	-	11,965
Adjustments to deferred tax charge in respect of prior years	(775)	(1,846)
Tax effect of income not taxable in determining taxable profit	137	(10)
Other – research and development depreciation allowed	(72)	(7)
Total tax expense	6,343	16,918

Notes to the consolidated financial statements

for the year ended 31 March 2021

9. TAXATION continued**9.1 INCOME TAX RECOGNISED IN INCOME STATEMENT continued****Changes in tax rates and factors affecting the future tax charges**

The adjustments to current and deferred tax charge in respect of previous years represent the changes between the prior year financial statements and the prior year tax computations submitted. The expenses not deductible for tax purposes are primarily driven by the movement on general provisions, non-deductible entertainment expenditure, and depreciation on non-qualifying capital expenditure.

9.2 INCOME TAX RECOGNISED DIRECTLY IN EQUITY

	2021 £000	2020 £000
Deferred tax		
Impact of deferred tax rate change	-	4,889

9.3 INCOME TAX RECOGNISED IN OTHER COMPREHENSIVE INCOME

Group and Company	2021 £000	2020 £000
Deferred tax		
Remeasurement of defined benefit obligation	(2,844)	927
Impact of rate change on pension scheme	-	124
	(2,844)	1,051

Notes to the consolidated financial statements

for the year ended 31 March 2021

9. TAXATION continued

9.4 DEFERRED TAX

The following is the analysis of deferred tax (assets)/liabilities presented in the consolidated statement of financial position:

Group and Company	2021 £000	2020 £000
Deferred tax liabilities	167,228	166,352

Group and Company	Opening balance £000	Recognised in profit or loss £000	Recognised in other comprehensive income £000	Closing balance £000
2021				
Deferred tax liabilities/(assets) in relation to:				
Property, plant and equipment	160,319	1,011	-	161,330
Rate change impact on PPE	-	-	-	-
General provisions – NI & Incentive plan	(198)	169	-	(29)
Fair value of swap	-	-	-	-
Remeasurement of defined benefit obligation	6,231	2,540	(2,844)	5,927
Rate change impact on defined benefit obligation	-	-	-	-
	166,352	3,720	(2,844)	167,228

Group and Company	Opening balance £000	Recognised in profit or loss £000	Recognised in other comprehensive income £000	Recognised directly in equity £000	Closing balance £000
2020					
Deferred tax liabilities/(assets) in relation to:					
Property, plant and equipment	142,273	1,519	-	-	143,792
Rate change impact on PPE	-	11,638	-	4,889	16,527
General provisions – NI & Incentive plan	(283)	85	-	-	(198)
Fair value of swap	(402)	402	-	-	-
Remeasurement of defined benefit obligation	3,807	1,049	927	-	5,783
Rate change impact on defined benefit obligation	-	324	124	-	448
	145,395	15,017	1,051	4,889	166,352

Notes to the consolidated financial statements

for the year ended 31 March 2021

9. TAXATION continued

9.4 DEFERRED TAX continued

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances net. All of the deferred tax assets were available for offset against deferred tax liabilities and hence the net deferred tax liability at 31 March 2021 was £167.2 million (2020: £166.4 million).

The UK Government's Budget announcement to grant 130 per cent super-deduction capital allowance for qualifying plant and machinery (and 50 per cent allowance for special rate assets) expenditure from 1 April 2021 provides greater incentive to boost capital allowance availability to mitigate 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 per cent to 25 per cent, 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 per cent. If the amended tax rate had been used, we estimate that the deferred tax liability would have been £49.4 million higher.

The deferred tax on temporary differences as at 31 March 2021 have been calculated using 19 per cent, the substantively enacted rate for the periods during which the temporary differences are expected to unwind.

Temporary timing differences

All temporary timing differences are recognised in the deferred tax calculation. In the prior years to 31 March 2020, the available additional allowances resulting from research and development (R&D) expenditure in respect of qualifying tangible fixed assets (TFA) were not included in the deferred tax calculation due to the immaterial level. As our R&D claims have now increased, we have now included the additional claims available in the deferred tax calculations appropriately. The total amount of TFA recognised in deferred tax asset for the year ended 31 March 2021 is £236,000 (all prior years: £348,000).

Notes to the consolidated financial statements

for the year ended 31 March 2021

10. DIVIDENDS

	2021 £000	2020 £000
Final dividend of 5.58p (2020: 5.58p) per Ordinary share proposed and paid during the year relating to the previous year's results	2,750	2,750
Special restructuring dividend of 276 pence (2020: - pence) per Ordinary share paid during the year	136,013	-
Interim dividend of 5.58p (2020: 5.58p) per Ordinary share paid during the year	2,750	2,750
Interim dividend of 5.58p (2020: 5.58p) per Ordinary share paid during the year	2,750	2,750
Interim dividend of 5.58p (2020: 5.58p) per Ordinary share paid during the year	2,750	2,750
	147,013	11,000

There were no dividends proposed for approval as at 31 March 2021 and 31 March 2020.

The company issued a special restructuring dividend of £136 million in December 2020 to its parent company South East Water Holdings. These funds were used by the parent company to repay its intercompany loan to South East Water Limited on the same day resulting in a net nil cash impact.

11. EARNINGS PER SHARE

Group	2021 £000	2020 £000
Profit for the year from continuing operations	31,316	16,884
	2021 Number	2020 Number
Basic and diluted weighted average number of shares	49,312,354	49,312,354
Basic and diluted earnings per share from continuing operations	63.51p	34.24p

Company	2021 £000	2020 £000
Profit for the year from continuing operations	31,301	16,855
	2021 Number	2020 Number
Basic and diluted weighted average number of shares	49,312,354	49,312,354
Basic and diluted earnings per share from continuing operations	63.47p	34.18p

Notes to the consolidated financial statements

for the year ended 31 March 2021

12. INTANGIBLE ASSETS

Group and Company	Notes	Computer software £000	Assets in course of construction £000	Total £000
Cost				
At 1 April 2019		24,087	1,248	25,335
Additions		-	2,985	2,985
Transfers		1,129	(1,129)	-
Reclassifications to/from property, plant and equipment	13	2,029	(2,898)	(869)
At 31 March 2020		27,245	206	27,451
Additions		-	2,822	2,822
Transfers		1,771	(1,771)	-
Disposals		(1,231)	-	(1,231)
Reclassifications to/from property, plant and equipment	13	(106)	-	(106)
At 31 March 2021		27,679	1,257	28,936
Accumulated amortisation and impairment				
At 1 April 2019		14,834	-	14,834
Charge for the year – owned	6	3,049	-	3,049
At 31 March 2020		17,883	-	17,883
Charge for the year – owned	6	3,497	-	3,497
Disposals		(1,231)	-	(1,231)
At 31 March 2021		20,149	-	20,149
Net book value				
At 1 April 2019		9,253	1,248	10,501
At 31 March 2020		9,362	206	9,568
At 31 March 2021		7,530	1,257	8,787

Notes to the consolidated financial statements

for the year ended 31 March 2021

13. PROPERTY, PLANT AND EQUIPMENT

Group and Company	Notes	Land, wells, reservoirs and buildings £000	Plant, equipment and vehicles £000	Mains £000	Assets under construction £000	Total £000
Cost or valuation						
At 1 April 2019		242,154	394,701	1,094,883	42,693	1,774,431
Additions		1,363	-	-	100,122	101,485
Disposals		(42)	(1,441)	(172)	-	(1,655)
Reclassifications to/from intangible assets	12	-	(2,029)	-	2,898	869
Transfers between classes		5,799	30,619	49,626	(86,044)	-
At 31 March 2020		249,274	421,850	1,144,337	59,669	1,875,130
Additions		-	-	-	90,434	90,434
Disposals		(48)	(2,039)	(104)	-	(2,191)
Reclassifications to/from intangible assets	12	(181)	190	97	-	106
Transfers between classes		12,030	13,971	42,871	(68,872)	-
At 31 March 2021		261,075	433,972	1,187,201	81,231	1,963,479
Accumulated depreciation and impairment						
At 1 April 2019		20,428	108,048	87,734	-	216,210
Charge for the year		4,753	27,405	19,264	-	51,422
Disposals		(2)	(1,435)	(103)	-	(1,540)
Impairment charge		-	193	-	-	193
At 31 March 2020		25,179	134,211	106,895	-	266,285
Charge for the year		5,135	28,050	19,722	-	52,907
Disposals		(8)	(1,272)	(50)	-	(1,330)
Impairment charge		2,288	65	-	-	2,353
At 31 March 2021		32,594	161,054	126,567	-	320,215
Net book value						
At 1 April 2019		221,726	286,653	1,007,149	42,693	1,558,221
At 31 March 2020		224,095	287,639	1,037,442	59,669	1,608,845
At 31 March 2021		228,481	272,918	1,060,634	81,231	1,643,264

Impairment losses recognised during the year

During the year, a significant series of sinkholes opened up underneath the service reservoirs at our site in Aylesford. These reservoirs hold a storage maximum of 20ML of treated water and were severely damaged and put out of action. The site needed extensive ground stabilisation before work could commence on restoring the reservoirs to operational use. At 31 March 2021 only 25 per cent of the original storage capacity had been returned to use. The remaining reservoirs require substantial reconstruction which will continue into 2021/22 and subsequent years.

The physical damage of an asset is noted in IAS 36 as one of the potential indicators of impairment. The company has therefore undertaken a review of the recoverable amount of the assets at Aylesford.

Notes to the consolidated financial statements

for the year ended 31 March 2021

13. PROPERTY, PLANT AND EQUIPMENT continued

The recoverable amount of an asset is the higher of fair value less costs of disposal and value in use. It is considered that fair value less costs of disposal cannot be reliably ascertained for the damaged reservoirs as there is no ready market for such assets given the nature of the industry. Value in use is the present value of future cash flows expected to be derived from the asset or cash generating unit. However, as resilience within the water network has enabled the Company to continue to supply the Aylesford area despite the loss of the reservoirs, the cash flows from the cash generating unit have been unaffected by the physical damage suggesting that there would be no impairment recorded. It is not considered that this would fairly reflect what has happened at Aylesford and an alternative approach has therefore been followed.

The write-off has been determined using the forecast rectification costs to derive an estimate of the net book value of the assets being replaced. This results in a write-off of £2.3 million being recorded in the year to 31 March 2021.

The write-off of "Land, wells, reservoirs and buildings" of £2.3 million is included in "Net operating costs" under the sub-heading "Asset expense/income".

The net book value of owned and leased assets included as "Property, plant and equipment" in the Consolidated statement of financial position is as follows:

13.1. ASSETS HELD UNDER LEASES

The net book value of owned and leased assets included as "Property, plant and equipment" in the Consolidated statement of financial position is as follows:

	31 March 2021 £000	31 March 2020 £000
Group and Company		
Property, plant and equipment owned	1,631,312	1,595,916
Right-of-use assets, excluding investment property	11,952	12,929
	1,643,264	1,608,845

Information about right-of-use assets is summarised below:

	31 March 2021 £000	31 March 2020 £000
Net book value		
Property	7,753	8,311
Plant and machinery	4,199	4,618
	11,952	12,929

13.2 ASSETS UNDER CONSTRUCTION RELATE TO THE FOLLOWING CATEGORIES

	31 March 2021 £000	31 March 2020 £000
Land, wells, reservoirs and buildings	7,900	2,822
Mains	12,020	16,471
Plant, equipment and vehicles	61,311	40,376
	81,231	59,669

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for the year ended 31 March 2021

14. SUBSIDIARIES

Details of the Group's material subsidiaries at the end of the reporting period are as follows:

Name of subsidiary	Principal activity	Place of incorporation and operation	Proportion of ownership interest and voting power held by the Group (%)	
			2021	2020
1) South East Water (Finance) Limited	Finance company	Cayman Islands	100	100

1) South East Water (Finance) Limited

South East Water (Finance) Limited's principal purpose is to raise debt on behalf of South East Water and any proceeds from such issues are lent on to South East Water. South East Water (Finance) Limited is a company registered in the Cayman Islands but the company does not gain any tax benefit from this as the company is resident for tax purposes in the UK.

South East Water (Finance) Limited is wholly-owned by South East Water Limited, which owns 100 per cent of the voting rights. Its registered address is P O Box 309GT, Ugland House, South Church Street, Georgetown, Grand Cayman, Cayman Islands.

15. AMOUNT DUE FROM PARENT UNDERTAKING

Group and Company	Note	2021 £000	2020 £000
Amount due from parent		-	135,941
		-	135,941

The intercompany loan was repaid in December 2020 by South East Water Holdings. This was funded by special restructuring dividends paid by South East Water Limited to its parent company, which resulted in net nil cash impact.

16. INVENTORIES

Group and Company	2021 £000	2020 £000
Consumables	636	639
Work in progress	37	50
	673	689

Notes to the consolidated financial statements

for the year ended 31 March 2021

17. TRADE AND OTHER RECEIVABLES

Group	2021 £000	2020 £000
Financial asset receivables		
Trade receivables	39,524	39,751
Accrued income	40,835	39,018
Sundry debtors	2,246	1,800
Amounts due from parent and fellow subsidiary undertakings due within one year	75	-
	82,680	80,569
Non-financial asset receivables		
Prepayments and accrued income	4,055	3,872
	4,055	3,872
Total trade and other receivables	86,735	84,441

Company	2021 £000	2020 £000
Financial asset receivables		
Trade receivables	39,524	39,751
Accrued income	40,835	39,018
Sundry debtors	2,245	1,799
Amounts due from parent and fellow subsidiary undertakings due within one year	75	-
	82,679	80,568
Non-financial asset receivables		
Prepayments and accrued income	3,681	3,495
	3,681	3,495
Total trade and other receivables	86,360	84,063

Notes to the consolidated financial statements

for the year ended 31 March 2021

17. TRADE AND OTHER RECEIVABLES continued

Group and Company

All trade receivables at 31 March 2021 and 31 March 2020 are denominated in sterling.

Trade receivables are stated after provision for doubtful debts of £30.9 million (2020: £28.1 million).

They are non-interest bearing and generally settlement within 12 months. Receivables are determined to be impaired where there is a poor payment history or insolvency of the debtor and are fully or partially provided for.

Movements in the provision for impairment of receivables were as follows:

Group and Company	2021 £000	2020 £000
Provision brought forward	28,085	25,937
Charge for the year	3,788	4,198
Amounts utilised	(975)	(2,050)
Provision carried forward	30,898	28,085

As at 31 March, the analysis of trade receivables past due but not impaired is as follows:

	2021 £000	2020 £000
Current	7,872	9,501
< 30 days	3,773	4,297
30 - 60 days	2,280	2,500
60 - 90 days	1,548	1,482
90 - 120 days	1,410	1,697
120 - 365 days	7,953	8,911
> 365 days	14,689	11,363
	39,525	39,751

18. CASH AND CASH EQUIVALENT

Cash and cash equivalents comprise the following at 31 March:

	Group		Company	
Group and Company	2021 £000	2020 £000	2021 £000	2020 £000
Cash at bank and in hand	41,617	12,981	41,441	12,981
	41,617	12,981	41,441	12,981

Included in the group and company cash at bank and in hand balance at 31 March 2021 was £38.8 million (2020: £12.0 million) held on an on demand deposit account.

At 31 March 2021, £0.8 million (2020: £0.4 million) of restricted cash was held for the group in designated bank accounts and £0.6 million (2020: £0.4 million) of restricted cash was held for the company in designated bank accounts in order to meet interest and associated swap payments falling due in respect of the listed debt and interest payments on index linked loans (note 8).

Notes to the consolidated financial statements

for the year ended 31 March 2021

19. LOANS AND BORROWINGS

Group	2021 £000	2020 £000
Non-current		
Loans and borrowings	1,033,789	1,024,097
Debentures	990	990
Lease liabilities	3,592	3,910
	1,038,371	1,028,997
Current		
Bank loans	80,000	30,000
Lease liabilities	318	329
	80,318	30,329
Total loans and borrowings	1,118,689	1,059,326

The carrying value of loans and borrowings classified as financial liabilities measured at amortised cost approximates fair value.

The loan documentation for the group's long and short term loans and borrowings contain a number of covenants that the group is required to meet to safeguard the interest of its lenders.

Group	2021 £000	2020 £000
Loans and borrowings		
Listed bonds	341,469	338,926
Index linked loans	399,704	392,839
Variable rate loan	118,725	118,493
Fixed rate loan	173,891	173,839
	1,033,789	1,024,097

Group	2021 £000	2020 £000
Irredeemable Debenture Stock		
3 % perpetual stock	25	25
3.5 % perpetual stock	384	384
4 % perpetual stock	178	178
5 % perpetual stock	365	365
5.5 % perpetual stock	1	1
6 % perpetual stock	37	37
	990	990

Interest on irredeemable debenture stock is payable six monthly

Notes to the consolidated financial statements

for the year ended 31 March 2021

19. LOANS AND BORROWINGS continued

Group	Loan due 2029 £000	Loan due 2041 £000	Total £000
2021			
Listed bonds			
Original loan consideration	166,000	130,000	296,000
Indexation on bonds	-	47,369	47,369
Less: unamortised issue costs	(886)	(1,014)	(1,900)
	165,114	176,355	341,469
2020			
Original loan consideration	166,000	130,000	296,000
Indexation on bonds	-	44,986	44,986
Less: unamortised issue costs	(996)	(1,064)	(2,060)
	165,004	173,922	338,926

The group holds non-current bonds listed on the London Stock Exchange with an original value of £296 million (2020: £296 million), with effective terms, as follows:

- £166 million at a fixed rate of 5.5834 per cent, falling due for repayment on 29 March 2029 (or earlier at the option of the group)
- £130 million at a variable rate linked to inflation, falling due for repayment on 3 June 2041 (or earlier at the option of the group)

Issue costs incurred by the group in securing the long-term borrowings were deducted from the amount of the consideration received. The issue costs have been amortised under the effective interest rate method over the lives of the bonds to which the costs relate.

Indexation accrues on the bond repayable in 2041 under the terms of the bond.

Group	Loan due 2032 £000	Loan due 2033 £000	Loan due 2037 £000	Total £000
2021				
Index linked loans				
Original loan amounts	135,000	34,000	100,000	269,000
Indexation on bonds	92,159	19,064	21,869	133,092
Less: unamortised issue costs	(952)	(184)	(1,252)	(2,388)
	226,207	52,880	120,617	399,704
2020				
Original loan amounts	135,000	34,000	100,000	269,000
Indexation on bonds	88,530	18,216	19,652	126,398
Less: unamortised issue costs	(1,035)	(196)	(1,328)	(2,559)
	222,495	52,020	118,324	392,839

Notes to the consolidated financial statements

for the year ended 31 March 2021

19. LOANS AND BORROWINGS continued

The group holds index linked loans with an original value of £269 million and with effective terms as follows:

- £135 million at a variable rate linked to inflation, falling due for repayment on 30 September 2032 (or earlier at the option of the group)
- £34 million at a variable rate linked to inflation, falling due for repayment on 30 September 2033 (or earlier at the option of the group)
- £100 million at a variable rate linked to inflation, falling due for repayment on 1 December 2037 (or earlier at the option of the group)

Indexation on the loans accrues under the terms of the loans. Issue costs incurred by the group in securing the long-term borrowings were deducted from the amount of the consideration received. The issue costs have been amortised under the effective interest rate method over the lives of the bonds to which the costs relate.

The irredeemable debentures, listed bonds and index linked loans detailed above are secured on the assets of South East Water (Holdings) limited, South East Water Limited and South East Water (Finance) Limited (the South East Water (Holdings) Limited group) as far as allowed by the Water Industry Act 1991 and South East Water's licence. The agreements for the bonds and loans contain a number of covenants that the group is required to meet to safeguard the interests of the lenders.

Group	2021 £000	2020 £000
Variable rate loan		
Original loan amount	120,000	120,000
Less: unamortised issue costs	(1,275)	(1,507)
	118,725	118,493

In December 2018 the group entered into a new loan facility for £120 million which matures in December 2025. This loan facility was drawn down in full in September 2019 at a variable rate of LIBOR plus 1.2 per cent.

The interest rate benchmark LIBOR will lose representativeness at the end of 2021. The group's floating rate debt will instead be benchmarked to the Sterling Overnight Index Average (SONIA) administered by the Bank of England.

The group has commenced transitioning its floating rate debt. In June 2021 South East Water (Finance) Limited refinanced its liquidity facilities using SONIA as its reference rate.

The group is in dialogue with its lenders to agree amendments to the fall back provisions to move from GBP LIBOR to SONIA on its other floating rate facilities, which comprise the authorised credit facility and the £120 million floating rate loan.

Notes to the consolidated financial statements

for the year ended 31 March 2021

19. LOANS AND BORROWINGS continued

Group	2021 £000	2020 £000
Fixed rate loan		
Original loan amount	175,000	175,000
Less: unamortised issue costs	(1,109)	(1,161)
	173,891	173,839

On 16 September 2019 the company issued new fixed rate loan notes totalling £175 million. The notes were issued in two tranches being:

- £75 million falling due for repayment on 16 September 2031
- £100 million falling due for repayment on 16 September 2042

Group	2021 £000	2020 £000
Lease liability		
Balance as at 1 April	4,239	3,098
Capital addition	-	1,363
Less: capital repayment	(329)	(222)
	3,910	4,239

The total cash outflow in the year in respect of the group's leasing activities was £0.5 million (2020: £0.3 million).

Group	2021 £000	2020 £000
Lease liability		
Non-current lease liability	3,592	3,910
Current lease liability	318	329
	3,910	4,239

Company	2021 £000	2020 £000
Non-current		
Loans and borrowings	1,033,789	1,024,097
Debentures	990	990
Lease liabilities	3,592	3,910
	1,038,371	1,028,997
Current		
Bank loans	80,000	30,000
Lease liabilities	318	329
	80,318	30,329
Total loans and borrowings	1,118,689	1,059,326

Notes to the consolidated financial statements

for the year ended 31 March 2021

19. LOANS AND BORROWINGS continued

The carrying value of loans and borrowings classified as financial liabilities measured at amortised cost approximates fair value.

Company	2021 £000	2020 £000
Loans and borrowings		
Loans from subsidiary	462,086	457,250
Index linked loans	279,087	274,515
Variable rate loan	118,725	118,493
Fixed rate loan	173,891	173,839
	1,033,789	1,024,097

Company	2021 £000	2020 £000
Irredeemable Debenture Stock		
3 % perpetual stock	25	25
3.5 % perpetual stock	384	384
4 % perpetual stock	178	178
5 % perpetual stock	365	365
5.5 % perpetual stock	1	1
6 % perpetual stock	37	37
	990	990

Interest on irredeemable debenture stock is payable six monthly.

Company	Loan due 2029 £000	Loan due 2041 £000	Loan due 2037 £000	Total £000
2021				
Loans from subsidiary				
Original loan consideration	166,000	130,000	100,000	396,000
Indexation on bonds	-	47,369	21,869	69,238
Less: unamortised issue costs	(886)	(1,014)	(1,252)	(3,152)
	165,114	176,355	120,617	462,086
2020				
Original loan amounts	166,000	130,000	100,000	396,000
Indexation on bonds	-	44,986	19,652	64,638
Less: unamortised issue costs	(996)	(1,064)	(1,328)	(3,388)
	165,004	173,922	118,324	457,250

Notes to the consolidated financial statements

for the year ended 31 March 2021

19. LOANS AND BORROWINGS continued

The company's subsidiary undertaking, South East Water (Finance) Limited, has debt with an original consideration of £396 million (2020: £396 million), of which £296 million (2020: £296 million) is listed on the London Stock Exchange. The funds raised are lent to the company under loan agreements between the company and its subsidiary. An annual fee of £23,000 (2020: £33,000) was charged by South East Water (Finance) Limited to South East Water Limited.

The effective terms of the £396 million loans due to South East Water (Finance) Limited are as follows:

- £166 million at a fixed rate of 5.5834 per cent, falling due for repayment on 29 March 2029 (or earlier at the option of the company)
- £130 million at a variable rate linked to inflation, falling due for repayment on 3 June 2041 (or earlier at the option of the company)
- £100 million at a variable rate linked to inflation, falling due for repayment on 1 December 2037 (or earlier at the option of the company)

Issue costs incurred by the company in securing the long-term borrowings were deducted from the amount of the consideration received. The issue costs have been amortised under the effective interest rate method over the lives of the bonds to which the costs relate.

Indexation accrues on the loan repayable in 2041 under the terms of the loan.

The amounts due to subsidiary undertakings and the indexed loans are secured on the assets of South East Water (Holdings) Limited Group as far as allowed by the Water Industry Act 1991 and South East Water's licence.

Company	Loan due 2032 £000	Loan due 2033 £000	Total £000
2021			
Index linked loans			
Original loan amounts	135,000	34,000	169,000
Indexation on bonds	92,159	19,064	111,223
Less: unamortised issue costs	(952)	(184)	(1,136)
	226,207	52,880	279,087
2020			
Original loan consideration	135,000	34,000	169,000
Indexation on bonds	88,530	18,216	106,746
Less: unamortised issue costs	(1,035)	(196)	(1,231)
	222,495	52,020	274,515

Notes to the consolidated financial statements

for the year ended 31 March 2021

19. LOANS AND BORROWINGS continued

The company holds index linked loans with an original consideration of £169 million and effective terms as follows:

- £135 million at a variable rate linked to inflation, falling due for repayment on 30 September 2032 (or earlier at the option of the company)
- £34 million at a variable rate linked to inflation, falling due for repayment on 30 September 2033 (or earlier at the option of the company)

Indexation on the loans accrues under the terms of the loans. Issue costs incurred by the company in securing the long-term borrowings were deducted from the amount of the consideration received. The issue costs have been amortised under the effective interest rate method over the lives of the bonds to which the costs relate. Index linked loans are stated after the uplift for accrued indexation and the deduction of issue costs to be amortised at the balance sheet date.

The listed bonds and unlisted loan are secured on the assets of South East Water (Holdings) Limited Group as far as allowed by the Water Industry Act 1991 and South East Water's licence.

Company	2021 £000	2020 £000
Variable rate loan		
Original loan amount	120,000	120,000
Less: unamortised issue costs	(1,275)	(1,507)
	118,725	118,493

In December 2018 the group entered into a new loan facility for £120 million which matures in December 2025. This loan facility was drawn down in full in September 2019 at a variable rate of LIBOR plus 1.2 per cent.

The interest rate benchmark LIBOR will lose representativeness at the end of 2021. The group's floating rate debt will instead be benchmarked to the Sterling Overnight Index Average (SONIA) administered by the Bank of England.

The group has commenced transitioning its floating rate debt. In June 2021 South East Water (Finance) Limited refinanced its liquidity facilities using SONIA as its reference rate.

The group is in dialogue with its lenders to agree amendments to the fall back provisions to move from GBP LIBOR to SONIA on its other floating rate facilities, which comprise the authorised credit facility and the £120 million floating rate loan.

Company	2021 £000	2020 £000
Fixed rate loan		
Original loan amount	175,000	175,000
Less: unamortised issue costs	(1,109)	(1,161)
	173,891	173,839

On 16 September 2019 the company issued new fixed rate loan notes totalling £175 million. The notes were issued in two tranches being:

- £75 million falling due for repayment on 16 September 2031
- £100 million falling due for repayment on 16 September 2042

Notes to the consolidated financial statements

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19. LOANS AND BORROWINGS continued

Company	2021 £000	2020 £000
Lease liability		
Balance as at 1 April	4,239	3,098
Capital addition	-	1,363
Less: capital repayment	(329)	(222)
	3,910	4,239

The total cash outflow in the year in respect of the company's leasing activities was £0.5 million (2020: £0.3 million).

Company	2021 £000	2020 £000
Lease liability		
Non-current lease liability	3,592	3,910
Current lease liability	318	329
	3,910	4,239

20. PROVISIONS

Group and Company	Third party damage claims £000	Leak allowance £000	Other provisions £000	Total £000
As at 1 April 2020	1,655	2,802	-	4,457
Additional provisions	1,305	3,064	3,527	7,896
Amounts utilised	(930)	(3,440)	-	(4,370)
31 March 2021	2,030	2,426	3,527	7,983
As at 1 April 2019	2,144	1,828	-	3,972
Additional provisions	824	4,632	-	5,456
Amounts utilised	(1,313)	(3,658)	-	(4,971)
31 March 2020	1,655	2,802	-	4,457

Other provisions relates to various contractual and legal claims against the group. The amount recorded represents management's best estimate of the value of settlement and any associated costs.

The timing of settlement/court judgement for these claims is uncertain but management consider that settlement is more likely than not within the next year, and therefore amounts provided have been classified as current.

The group needs to determine the chances of a claim against it being successful, the likelihood of an outflow of economic benefits occurring and whether there is a need to disclose a contingent liability or whether a provision is required based on this assessment. There is an inherent risk that the final outcome of legal claims will be different to amounts provided.

The group has taken the option under paragraph 92 of IAS 37 for non-disclosure of certain information relating to provisions and contingent liabilities in extremely rare cases where this can be expected to seriously prejudice the entity in a dispute.

Notes to the consolidated financial statements

for the year ended 31 March 2021

21. TRADE AND OTHER PAYABLES

Group	2021 £000	2020 £000
Current liabilities		
Financial liability payables		
Trade payables	11,369	12,877
Amounts due to parent and fellow subsidiary undertakings	10,901	10,727
Other payables	2,334	4,606
Accruals	27,237	33,546
	51,841	61,756
Non-financial liability payables		
Payments received in advance	35,199	34,856
Other taxes and social security	1,921	1,015
	37,120	35,871
	88,961	97,627
Non-current liabilities		
Financial liability payables		
Deposits payable to developers	4,623	4,997
Company	2021 £000	2020 £000
Current liabilities		
Financial liability payables		
Trade payables	11,369	12,877
Amounts due to parent and fellow subsidiary undertakings	14,315	14,407
Other payables	2,334	4,606
Accruals	24,767	30,968
	52,785	62,858
Non-financial liability payables		
Payments received in advance	35,199	34,856
Other taxes and social security	1,921	1,015
	37,120	35,871
	89,905	98,729
Non-current liabilities		
Financial liability payables		
Deposits payable to developers	4,623	4,997

As at 31 March 2021 and 2020, amounts due to parent and fellow subsidiary undertakings represent unsecured non-interest bearing balances relating to the surrender of group tax relief in respect of the group and the surrender of group tax relief and interest due on debt with the subsidiary company in respect of the company.

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22. FINANCIAL INSTRUMENTS – FAIR VALUES AND RISK MANAGEMENT

FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The group's financial instruments comprise index linked loans, variable rate loans, fixed rate loans, cash, short-term and medium-term deposits, trade receivables and trade and other payables. The main purpose of the group's financial instruments is to raise finance for the group's operations.

Derivative activity is undertaken as determined by the Board of Directors. The board considers the overall risk profile of the group and enters into derivatives to mitigate or hedge any risks identified, as appropriate. The group does not use derivative financial instruments for speculative purposes.

The group's treasury operations are managed within parameters defined by the board and its parent undertaking. It is the group's policy to minimise liquidity risk within an acceptable range of interest rates. The group does not use foreign currency financial instruments. The main risks arising from the group's financial instruments are interest rate and liquidity risk. There are no regulatory capital requirements placed on the group.

INTEREST RATE AND CASH FLOW RISK

The group finances its activities through a mixture of cash generated from operations, irredeemable debentures and other fixed rate long-term loans, variable rate loans and long-term index linked loans. Debentures are long-term fixed rate loans. Fixed rate loans include listed bonds and loan notes and long-term index linked loans comprise loans linked to inflation.

The group's policy is to manage short-term interest rate risk by using short-term fixed rate drawdowns under a revolving committed facility. During the year to 31 March 2021 there was a net inflow of £50 million from the committed facility (2020: net outflow of £25 million). It is the view of the group that long-term fluctuations in interest rates will be within the parameters that are considered acceptable by the group.

The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, on the group's profit before tax (through the impact on floating rate borrowings). The sensitivity analysis excludes all non-derivative fixed rate financial instruments carried at amortised cost but includes those recognised at fair value as well as all non-derivative floating rate financial instruments.

Group and Company	Increase/ decrease in basis points	Effect on profit before tax £000	Effect on shareholders' equity £000
2021			
Sterling	+300	(17,970)	(14,376)
Sterling	-100	(5,990)	(4,792)
2020			
Sterling	+300	(12,390)	(9,912)
Sterling	-100	(4,130)	(3,304)

LIQUIDITY RISK

The group aims to maintain a balance between continuity of funding and flexibility. Continuity of funding has been guaranteed throughout the period by the existence of long-term funding facilities. Short-term flexibility is achieved by varying the drawdown amounts under the revolving committed facility. Further details are given below. Cash is put on deposit with variable maturity dates so as to mitigate liquidity risk.

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INFLATION RISK

The group manages its inflation risk on its financial liabilities through the use of an index linked bonds and loans (note 19). The group considers that the inflation rate risk is effectively managed as Ofwat allows revenues to be increased in line with inflation.

CREDIT RISK

The group's financial assets include short-term and medium-term bank deposits and trade receivables, which represent the group's maximum exposure to credit risk in relation to financial assets. The group's credit risk is primarily attributable to its trade receivables, which are stated in the statement of financial position at original invoice amount less an allowance for any doubtful debts (see note 17). An estimate for the provision for doubtful debts is calculated by management based on the application of expected recovery rates to an aged debt profile. We have no significant concentration of credit risk with exposure spread over a large number of domestic customers and a number of retail customers. For our retail customers, we have secured adequate collateral under the Market Codes to mitigate any risk.

CAPITAL MANAGEMENT RISK

The objectives and management of the group's capital management risk are discussed in the strategic report.

FAIR VALUES OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed and willing parties. In the opinion of the directors, the fair values of the financial assets and liabilities of the group (apart from the specific items shown in the fair value table below) are not materially different from the book values.

The following tables provide a comparison by category of the carrying amount and the fair values of the group's financial assets and financial liabilities at 31 March 2021.

	Notes	Book Value 2021 £000	Fair Value 2021 £000	Book Value 2020 £000	Fair Value 2020 £000
<i>Financial assets at amortised cost</i>					
Trade and other receivables	17	82,680	82,680	80,569	80,569
Cash	18	41,617	41,617	12,981	12,981
Amounts due from parent undertaking		-	-	135,941	107,771
		124,297	124,297	229,491	201,321
<i>Financial liabilities at amortised cost</i>					
Trade and other payables	21	40,940	40,715	51,029	50,748
Irredeemable debentures	19	990	861	990	842
Listed bonds	19	341,469	430,369	338,926	430,369
Index linked loans	19	399,704	503,851	392,839	504,074
Drawdown facility	19	80,000	80,000	30,000	30,000
Bank loan	19	118,725	118,725	118,493	118,493
Loan Note	19	173,891	173,891	173,839	173,839
Lease liability	19	3,910	3,910	4,239	4,239
Amounts due to parent and group undertakings	21	10,901	10,841	10,727	10,668
Trade and other payables over 1 year	21	4,623	4,598	4,997	4,970
		1,175,153	1,367,761	1,126,079	1,328,243

Notes to the consolidated financial statements

for the year ended 31 March 2021

22. FINANCIAL INSTRUMENTS – FAIR VALUES AND RISK MANAGEMENT continued

The net book value is considered to equate to the fair value for trade receivables due to the short maturity of the amounts receivable. The fair value of trade and other payables and amounts due to parent and group undertakings have been adjusted for the appropriate credit risk. The fair value of irredeemable debentures has been calculated using the discounted cash flow method. The calculation includes all future capital and interest payments discounted by an amount representing credit risk and a further amount representing future inflation.

The fair value of index-linked loans have been calculated using discounted cash flow method, taking into account future capital and interest payments based on estimated interest and inflation rates appropriate to the loans. These amounts have been similarly discounted for credit risk and inflation using appropriate discount rates in effect at the balance sheet dates. The fair values of listed bonds are based on market prices.

FAIR VALUE HIERARCHY

The group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities
- Level 2: other techniques for which all inputs with a significant effect on the recorded fair value are observable, either directly or indirectly
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The group held the following financial instruments which are not measured at fair value but fair value disclosures are required:

31 March 2021	Total £000	Level 1 £000	Level 2 £000	Level 3 £000
<i>Fair value of financial liabilities at amortised cost</i>				
Trade and other payables	(40,715)	-	(40,715)	-
Irredeemable debentures	(861)	-	(861)	-
Listed bonds	(430,369)	(430,369)	-	-
Index linked loans	(503,851)	-	(503,851)	-
Bank loans	(80,000)	-	(80,000)	-
Bank loan	(118,725)	-	(118,725)	-
Loan note	(173,891)	-	(173,891)	-
Lease liability	(3,910)	-	(3,910)	-
Amounts due to parent and group undertakings	(10,841)	-	(10,841)	-
Trade and other payables over 1 year	(4,598)	-	(4,598)	-
Total fair value of financial liabilities at amortised cost	(1,367,761)	(430,369)	(937,392)	-

Notes to the consolidated financial statements

for the year ended 31 March 2021

22. FINANCIAL INSTRUMENTS – FAIR VALUES AND RISK MANAGEMENT continued

31 March 2020	Total £000	Level 1 £000	Level 2 £000	Level 3 £000
<i>Fair value of financial assets at amortised cost</i>				
Amounts due from parent undertaking	107,771	-	107,771	-
<i>Fair value of financial liabilities at amortised cost</i>				
Trade and other payables	(50,748)	-	(50,748)	-
Irredeemable debentures	(842)	-	(842)	-
Listed bonds	(430,369)	(430,369)	-	-
Index linked loans	(504,074)	-	(504,074)	-
Bank loans	(30,000)	-	(30,000)	-
Bank loan	(118,493)	-	(118,493)	-
Loan note	(173,839)	-	(173,839)	-
Lease liability	(4,239)	-	(4,239)	-
Amounts due to parent and group undertakings	(10,668)	-	(10,668)	-
Trade and other payables over 1 year	(4,970)	-	(4,970)	-
Total fair value of financial liabilities at amortised cost	(1,328,243)	(430,369)	(897,874)	-

During the reporting years ended 31 March 2021 and 2020, there were no transfers between Level 1 and Level 2 fair value measurements and no transfers into and out of Level 3 fair value measurements.

Notes to the consolidated financial statements

for the year ended 31 March 2021

22. FINANCIAL INSTRUMENTS – FAIR VALUES AND RISK MANAGEMENT continued

MATURITY OF FINANCIAL INSTRUMENTS

The table below summarises the maturity profile of the group's financial assets and liabilities based on contractual undiscounted payments:

Year ended 31 March 2021	Within 1 year £000	1 – 2 years £000	2 – 5 years £000	Over 5 years £000	Total £000
<i>Fixed rate</i>					
Fixed rate financial liabilities:					
Irredeemable debentures	42	42	125	1,087	1,296
Listed bond	9,268	9,268	27,805	221,661	267,383
Loan notes	5,425	5,425	16,275	240,258	267,383
Total fixed rate financial liabilities	14,735	14,735	44,206	462,955	536,632
<i>Floating rate</i>					
Floating rate financial assets:					
Short-term financial assets	82,680	-	-	-	82,680
Cash	41,617	-	-	-	41,617
Total floating rate financial assets	124,297	-	-	-	124,297
Floating rate financial liabilities:					
Short-term financial liabilities	51,841	-	-	-	51,841
Listed bond	4,464	4,569	14,339	231,947	255,319
Index-linked loans	12,860	13,127	40,985	642,212	709,184
Variable rate bank loan	1,620	1,620	124,456	-	127,696
Lease liability	446	429	1,268	2,497	4,640
Trade and other payables over 1 year	4,623	-	-	-	4,623
Total floating rate financial liabilities	75,854	19,745	181,048	876,656	1,153,303
Total floating rate financial assets less liabilities	48,443	-19,745	-181,048	-876,656	-1,021,004
Total fixed rate financial assets less liabilities	1,296	42	125	1,087	2,550
Total financial assets less liabilities	50,739	-19,703	-180,923	-875,569	-1,018,450
Total financial assets less liabilities at 31 March 2021	50,739	-19,703	-180,923	-875,569	-1,018,450
Total financial assets less liabilities at 31 March 2020	50,739	-19,703	-180,923	-875,569	-1,018,450
Year ended 31 March 2020	Within 1 year £000	1 – 2 years £000	2 – 5 years £000	Over 5 years £000	Total £000
<i>Fixed rate</i>					
Fixed rate financial liabilities:					
Irredeemable debentures	42	42	125	1,087	1,296
Listed bond	9,268	9,268	27,805	230,879	277,220
Total fixed rate financial liabilities	9,310	9,310	27,930	231,924	278,474
<i>Floating rate</i>					
Floating rate financial assets:					
Short-term financial assets	80,569	-	-	-	80,569
Long-term financial assets	3,721	3,721	11,164	173,227	191,833
Cash	12,981	-	-	-	12,981
Total floating rate financial assets	84,290	3,721	11,164	173,227	272,402
Floating rate financial liabilities:					
Short-term financial liabilities	102,625	-	-	-	102,625
Listed bond	4,414	4,519	14,189	234,851	257,973
Index-linked loans	12,659	12,926	40,382	659,203	725,170
Trade and other payables over 1 year	4,997	-	-	-	4,997
Total floating rate financial liabilities	124,695	17,445	54,571	894,054	1,090,765
Total floating rate financial assets less liabilities	-40,405	-13,724	-43,407	-720,827	-818,363
Total fixed rate financial assets less liabilities	1,296	42	125	1,087	2,550
Total financial assets less liabilities	-39,109	-13,682	-43,282	-719,740	-815,813
Total financial assets less liabilities at 31 March 2020	-39,109	-13,682	-43,282	-719,740	-815,813

Notes to the consolidated financial statements

for the year ended 31 March 2021

BORROWING FACILITIES

The group has committed borrowing facilities of £148 million (2020: £147 million), of which £80 million (2020: £30 million) was drawn down. Any drawdowns under these facilities are repayable in less than one year.

The capital and working capital facility of £90 million (2020: £90 million) expires in June 2022. This facility is being replaced in 2021 with an extended facility of £125 million. The DSR Liquidity Facility of £38 million (2020: £38 million) and the O&M Reserve Facility of £20 million (2020: £20 million) expire in June 2022.

ITEMS OF INCOME, EXPENSE, GAINS AND LOSSES

The net gains or losses of the different classes of financial instruments on the income statement are:

	Note	2021 £000	2020 £000
Financial assets at amortised cost	8	3,093	5,333
Financial liabilities at amortised cost	8	(42,956)	(50,149)
Financial liabilities at fair value through profit and loss	8	-	(2,713)
Financial assets due to impairment	17	3,788	4,198

23. DEFERRED INCOME

Group and Company	2021 £000	2020 £000
As at 1 April	8,856	10,368
Received in the year	6,338	7,048
Released during the year	(6,233)	(8,560)
As at 31 March	8,961	8,856
Non-current	3,625	3,438
Current	5,336	5,418
	8,961	8,856

Contributions received towards below ground assets are released to the income statement on completion of the performance obligations within the contracts with customers.

Notes to the consolidated financial statements

for the year ended 31 March 2021

24. RETIREMENT BENEFIT SCHEMES

Group and company (hereafter referred to as “group” in this note)

The South East Water pension scheme provides benefits to current and former group employees. From 17 June 2011 onwards, benefits from the South East Water pension scheme have been provided solely on a defined contribution basis.

The scheme was originally contracted-out under the Guaranteed Minimum Pension Test. From 6 April 1997, after taking independent actuarial advice, the group decided to contract-out via the Protected Rights Test. With effect from 6 April 2012, the Government removed the option for schemes to contract-out via a Protected Rights basis. From 6 April 2012, the group decided to contract-out via a salary related basis.

The final salary defined benefit section of the scheme was closed to new entrants with effect from July 2002.

The last full actuarial valuation of the South East Water scheme took place as at 31 March 2020. The next full actuarial valuation will be performed at 31 March 2023.

The group contribution rate for the defined benefit pension scheme was nil (2020: nil) of pensionable remuneration during the year plus an annual contribution of £4 million (2020: £3.9 million). The group's future annual contribution is expected to be £4 million.

As a result of the merger of South East Water and Mid Kent Water Limited in October 2006, the group acquired the Mid Kent Group Pension Scheme, which is a defined benefit scheme in the UK.

The last full actuarial valuation of this scheme took place as at 31 March 2020. The next full actuarial valuation will be performed at 31 March 2023.

The group contribution towards the defined benefit pension scheme during the year was nil (2020: nil) of pensionable remuneration plus £1.4 million (2020: £1.4 million) in respect of the deficit as at 31 March 2020 to the scheme during the year. The group's future annual contribution is expected to be £1.4 million.

Both of the defined benefit schemes are as separate funds that are legally separate from the group. The trustees of the pension schemes are required by law to act in the interests of the funds and all relevant stakeholders in the plans. The trustees of the pension funds are responsible for the investment policies with regard to the assets of the funds.

On 31 March 2015 both of the group's defined benefit schemes closed to further benefit accrual. This was advised to the schemes' members on 13 December 2012. From 31 March 2015 all active members became deferred members and their accrued benefits will increase in line with statutory deferred revaluation. All members were invited to join the group's defined contribution scheme from 1 April 2015.

The group also has obligations to pay a number of former employees' pensions on a defined benefit basis which are not included in either of the pension schemes. These pensions are paid by the group directly. The payments are treated as contributions for unfunded pensions in the tables below and equal to the benefits paid. The value of future obligations has been calculated and the liability is recognised on the statement of financial position.

Following the High Court ruling on 26 October 2018 regarding the equalisation of Guaranteed Minimum Pension ('GMP') benefit within the Lloyds pension scheme, the Schemes are required to adjust benefits to remove the inequalities between the GMP benefits awarded to males and females. The Company included an allowance of £273,000 for the impact of GMP equalisation within its 2019 accounting figures and this estimate remains unchanged.

Notes to the consolidated financial statements

for the year ended 31 March 2021

24. RETIREMENT BENEFIT SCHEMES continued

On 20 November 2020 the High Court issued a supplementary ruling in the Lloyds bank GMP equalisation case with respect to members that have transferred out of their scheme prior to the ruling. The results of this mean that:

- trustees are obliged to make transfer payments that reflect equalised benefits and are required to make top up payments where this was not the case in the past
- a DB scheme that received a transfer is concurrently obliged to provide equalised benefits in respect of the transfer payments
- there were no exclusions on the grounds of discharge forms, CETV legislation, forfeiture provisions or the Limitation Act 1980

This additional cost is required to be recognised through the income statement as a past service cost. We have determined an estimated cost of the impact of this ruling of £6,000 for the SEWPS and £3,000 for the MKGPS based on high level scheme summary data.

The indexation of pension increases in payment in the MKGPS changed from RPI to CPI during the period. A Deed of Record was signed to formalise the change of inflation index from RPI to CPI, with members being written to and notified of the change at the end of April 2020. The first pension increase that will be determined with reference to CPI instead of RPI will be awarded on 1 April 2021. This event has been treated at a plan amendment as at 30 April 2020.

The impact of this plan amendment has been recognised as a past service credit of £7.8 million in the income statement, based on market conditions at 30 April 2020.

The net finance cost for the year allows for remeasurement at 30 April 2020 based on a discount rate of 1.65 per cent, CPI inflation of 1.75 per cent (giving a resulting liability value at 30 April 2020 of 105.1 million) and an asset value as at 30 April 2020 of £131.2 million.

We have received statistics for deaths in the SEWPS and MKGPS over the past three years to 31 March 2021 from Hymans Robertson LLP, the Schemes' administrator. This did not reveal clear evidence to suggest mortality was significantly higher in the Schemes as a result of Covid-19. Therefore, we have not made any explicit adjustment to the mortality assumptions to allow for the impact of the pandemic.

Pension costs recognised in the income statement for the defined contribution scheme were as follows:

Group and Company	2021 £000	2020 £000
Defined contribution scheme	2,481	2,385

Notes to the consolidated financial statements

for the year ended 31 March 2021

24. RETIREMENT BENEFIT SCHEMES continued

The major assumptions used for the actuarial valuations were:

	SEW Pensions 2021 %	SEW Pensions 2020 %	MKW Pensions 2021 %	MKW Pensions 2020 %
<i>Main assumptions</i>				
Rate of increase in pensions in payment				
RPI – Linked	-	2.50	-	2.50
CPI – Linked	2.55	1.75	2.55	1.75
Rate of increase in deferred pensions	2.55	1.75	2.55	1.75
Discount rate	2.05	2.30	2.05	2.30
RPI assumption	3.25	2.50	3.25	2.50
CPI assumption	2.55	1.75	2.55	1.75
<i>Life expectancies from age 65</i>				
Currently aged 65 – male	21.6	21.7	21.6	21.7
Currently aged 65 – female	24.0	23.7	24.0	23.7
Currently aged 45 – male	24.0	22.9	24.0	22.9
Currently aged 45 – female	26.3	25.8	26.3	25.8

The following table demonstrates the sensitivity to a reasonably possible change in the above key assumptions, with all other variables held constant, on the schemes' liabilities:

	(Decrease)/ increase in liabilities £000	(Decrease)/ increase %
0.1% decrease to the discount rate	4,000	1.5
0.1% increase to inflation	3,500	1.3
One year increase in life expectancy	12,500	4.6

The fair value of the assets in the schemes and the present value of the liabilities in the schemes were:

Group and Company	SEW Pensions 2021 £000	MKW Pensions 2021 £000	Total 2021 £000
Equities	32,527	17,406	49,933
Corporate bonds	86,115	63,555	149,670
Government bonds	47,547	37,323	84,870
Cash	5,881	2,983	8,864
Insured persons	5,634	5,246	10,880
Total fair value of assets	177,704	126,513	304,217
Present value of funded obligations	(166,991)	(102,858)	(269,849)
Surplus in the schemes	10,713	23,665	34,368
			£000
<i>Unfunded obligation 2021</i>			
Present value of unfunded obligations			(3,172)

Notes to the consolidated financial statements

for the year ended 31 March 2021

24. RETIREMENT BENEFIT SCHEMES continued

Group and Company	SEW Pensions 2020 £000	MKW Pensions 2020 £000	Total 2020 £000
Equities	29,862	14,221	44,083
Corporate bonds	73,983	55,604	129,587
Government bonds	50,221	42,066	92,287
Cash	10,088	6,758	16,846
Insured persons	5,044	4,761	9,805
Total fair value of assets	169,198	123,410	292,608
Present value of funded obligations	(154,121)	(102,575)	(256,696)
Surplus in the schemes	15,077	20,835	35,912
			£000
<i>Unfunded obligation 2020</i>			
Present value of unfunded obligations			(3,115)

Equity investments include Global Tactical Asset Allocation, Private Equity Fund and Absolute Return Investments.

Analysis of amounts charged/(credited) to income statement:

Group and Company	SEW Pensions £000	MKW Pensions £000	Unfunded Pensions £000	Total £000
2021				
Net interest on net defined benefit asset	(388)	(441)	68	(761)
Past service cost/(credit)	6	(7,802)	-	(7,796)
Administrative expenses	495	406	-	901
Total amount charged to income statement	113	(7,837)	68	(7,656)
2020				
Net interest on net defined benefit asset	(311)	(399)	77	(633)
Past service cost	-	-	-	-
Administrative expenses	411	299	-	710
Total amount charged to income statement	100	(100)	77	77

The amount charged to the income statement above in respect of MKW Pensions includes a past service costs credit of £7.8 million due to the change in indexation in pension increases from RPI to CPI.

Also included in the past service costs above are costs of £6,000 for SEW Pensions and £3,000 for MKW Pensions in respect of GMP equalisation.

Notes to the consolidated financial statements

for the year ended 31 March 2021

24. RETIREMENT BENEFIT SCHEMES continued

Analysis of amounts recognised in the statement of comprehensive income:

Group and Company	SEW Pensions £000	MKW Pensions £000	Unfunded Pensions £000	Total £000
2021				
Return on schemes' assets excluding interest income	8,304	4,981	-	13,285
Actuarial losses due to changes in financial assumptions	(20,454)	(14,906)	(240)	(35,600)
Actuarial losses due to changes in demographic assumptions	(336)	(323)	(34)	(693)
Experience gain on obligation	4,206	3,835	-	8,041
Actuarial losses recognised in the statement of comprehensive income	(8,280)	(6,413)	(274)	(14,967)
Cumulative actuarial losses	(13,599)	(15,599)	(3,593)	(32,791)
2020				
Return on schemes' assets excluding interest income	(2,692)	211	-	(2,481)
Actuarial gains due to changes in financial assumptions	4,834	5,019	62	9,915
Actuarial losses due to changes in demographic assumptions	(1,347)	(981)	(33)	(2,361)
Experience loss on obligation	-	-	(194)	(194)
Actuarial gains/(losses) recognised in the statement of comprehensive income	795	4,249	(165)	4,879
Cumulative actuarial losses	(5,319)	(9,186)	(3,319)	(17,824)

Reconciliation of defined benefit obligations:

Group and Company	SEW Pensions £000	MKW Pensions £000	Unfunded Pensions £000	Total £000
2021				
Opening defined benefit obligations	154,121	102,575	3,115	259,811
Interest cost	3,462	1,748	68	5,278
Actuarial (gains)/losses	16,584	11,394	274	28,252
Past service cost	6	(7,802)	-	(7,796)
Benefits paid	(7,182)	(5,057)	(285)	(12,524)
Closing defined benefit obligations	166,991	102,858	3,172	273,021
2020				
Opening defined benefit obligations	161,451	109,496	3,154	274,101
Interest cost	4,017	2,721	77	6,815
Actuarial (gains)/losses	(3,487)	(4,038)	165	(7,360)
Past service cost	-	-	-	-
Benefits paid	(7,860)	(5,604)	(281)	(13,745)
Closing defined benefit obligations	154,121	102,575	3,115	259,811

Notes to the consolidated financial statements

for the year ended 31 March 2021

24. RETIREMENT BENEFIT SCHEMES continued

Reconciliation of fair value of plans' assets:

Group and Company	SEW Pensions £000	MKW Pensions £000	Total £000
2021			
Opening fair values of schemes' assets	169,198	123,410	292,608
Interest income on assets	3,850	2,189	6,039
Return on scheme assets excluding interest income	8,304	4,981	13,285
Contributions by employer	4,029	1,396	5,425
Administrative expenses	(495)	(406)	(901)
Benefits paid	(7,182)	(5,057)	(12,239)
Closing fair values of schemes' assets	177,704	126,513	304,217
2020			
Opening fair values of schemes' assets	171,894	124,617	296,511
Interest income on assets	4,328	3,120	7,448
Return on scheme assets excluding interest income	(2,692)	211	(2,481)
Contributions by employer	3,939	1,365	5,304
Administrative expenses	(411)	(299)	(710)
Benefits paid	(7,860)	(5,604)	(13,464)
Closing fair values of schemes' assets	169,198	123,410	292,608

The Trust Deed provides South East Water with an unconditional right to a refund of surplus assets assuming the full settlement of plan liabilities in the event of a plan wind-up. Furthermore, in the ordinary course of business the Trustee has no rights to unilaterally wind up or otherwise augment the benefits due to members of the scheme. Based on these rights, any net surplus in the UK scheme is recognised in full.

25. SHARE CAPITAL

Authorised	2021 Number	2021 £000	2020 Number	2020 £000
Shares treated as equity				
Ordinary Shares shares of £1.00 each	100,000,000	100,000	100,000,000	100,000
Issued and fully paid				
Ordinary Shares shares of £1.00 each				
At 1 April and 31 March	49,312,354	49,312	49,312,354	49,312

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26. ANALYSIS OF AMOUNTS RECOGNISED IN OTHER COMPREHENSIVE INCOME

Group and Company Year to 31 March 2021	Retained earnings £000
Net actuarial loss on defined benefit pension schemes	(14,967)
Deferred tax credit on net actuarial loss	2,844
	(12,123)
Year to 31 March 2020	Retained earnings £000
Net actuarial gain on defined benefit pension schemes	4,879
Deferred tax charge on net actuarial gain	(927)
Impact of deferred tax rate change in respect of pension schemes	(124)
	3,828

27. MOVEMENT IN LIABILITIES ARISING FROM FINANCING ACTIVITIES

Group non-current loans and borrowings	Irredeemable debenture stock £000	Listed bonds £000	Fixed, Variable, Indexed linked loans and lease liability £000	Non-current loans and borrowing £000
Balance 1 April 2019	991	334,387	382,226	717,604
Changes from financing cash flows:				
Net proceeds from bank loan	-	-	118,437	118,437
Net proceeds from loan notes issued	-	-	173,872	173,872
Debentures redeemed	(1)	-	-	(1)
Changes from other financing activities:				
Indexation on index linked instruments	-	4,378	10,443	14,821
Lease liability on adoption of IFRS 16	-	-	3,910	3,910
Amortisation of issue costs	-	161	193	354
Balance at 31 March 2020	990	338,926	689,081	1,028,997
Balance 1 April 2020	990	338,926	689,081	1,028,997
Changes from financing cash flows:				
Net proceeds from bank loan	-	-	-	-
Net proceeds from loan notes issued	-	-	-	-
Debentures redeemed	-	-	-	-
Changes from other financing activities:				
Indexation on index linked instruments	-	2,383	6,694	9,077
Lease liability reclassification	-	-	(319)	(319)
Amortisation of issue costs	-	161	455	616
Balance at 31 March 2021	990	341,470	695,911	1,038,371

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27. MOVEMENT IN LIABILITIES ARISING FROM FINANCING ACTIVITIES continued

Company non-current loans and borrowings	Irredeemable debenture stock £000	Amounts due to subsidiary undertakings £000	Fixed, Variable & Indexed linked loans £000	Non-current loans and borrowing £000
Balance 1 April 2019	991	449,621	266,992	717,604
Changes from financing cash flows:				
Net proceeds from bank loan	-	-	118,437	118,437
Net proceeds from loan notes issued	-	-	173,872	173,872
Debentures redeemed	(1)	-	-	(1)
Changes from other financing activities:				
Indexation on index linked instruments	-	7,392	7,429	14,821
Lease liability on adoption of IFRS 16	-	-	3,910	3,910
Amortisation of issue costs	-	237	117	354
Balance at 31 March 2020	990	457,250	570,757	1,028,997
Balance 1 April 2020	990	457,250	570,757	1,028,997
Changes from financing cash flows:				
Net proceeds from bank loan	-	-	-	-
Net proceeds from loan notes issued	-	-	-	-
Debentures redeemed	-	-	-	-
Changes from other financing activities:				
Indexation on index linked instruments	-	4,600	4,477	9,077
Lease liability reclassification	-	-	(319)	(319)
Amortisation of issue costs	-	237	379	616
Balance at 31 March 2021	990	462,087	575,294	1,038,371

Group current loans and borrowings	Listed bonds £000	Bank loans and lease liability £000	Current loans and borrowings £000
Balance 1 April 2019	199,890	55,000	254,890
Changes from financing cash flows:			
Repayment of bonds on maturity	(200,000)	-	(200,000)
Net borrowing/(repayment) of facility drawdowns	-	(25,000)	(25,000)
Changes from other financing activities:			
Loan amortisation fee	110	-	110
Lease liability reclassification	-	329	329
Balance at 31 March 2020	-	30,329	30,329
Balance 1 April 2020	-	30,329	30,329
Changes from financing cash flows:			
Repayment of bonds on maturity	-	-	-
Net borrowing/(repayment) of facility drawdowns	-	50,000	50,000
Repayment of lease liability	-	(330)	(330)
Changes from other financing activities:			
Loan amortisation fee	-	-	-
Lease liability reclassification	-	319	319
Balance at 31 March 2021	-	80,318	80,318

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27. MOVEMENT IN LIABILITIES ARISING FROM FINANCING ACTIVITIES continued

	Amounts due to subsidiary undertakings £000	Bank loans £000	Current loans and borrowings £000
Company current loans and borrowings			
Balance at 1 April 2019	199,890	55,000	254,890
Changes from financing cash flows:			
Repayment of bonds on maturity	(200,000)	-	(200,000)
Net borrowing/(repayment) of facility drawdowns	-	(25,000)	(25,000)
Changes from other financing activities:			
Loan amortisation fee	110	-	110
Lease liability reclassification	-	329	329
Balance at 31 March 2020	-	30,329	30,329
Balance 1 April 2020	-	30,329	30,329
Changes from financing cash flows:			
Repayment of bonds on maturity	-	-	-
Net borrowing/(repayment) of facility drawdowns	-	50,000	50,000
Repayment of lease liability	-	(329)	(329)
Changes from other financing activities:			
Loan amortisation fee	-	-	-
Lease liability reclassification	-	318	318
Balance at 31 March 2021	-	80,318	80,318
Group and company derivative financial instruments		2021 £000	2020 £000
Balance at 1 April		-	108,836
Changes from financing cash flows:			
Payment of loss on maturity		-	(111,549)
Changes from other financing activities:			
Movement in fair value of interest rate swap		-	2,713
Balance at 31 March		-	-

Amounts owed by the company in the prior year in respect of derivative financial instruments were owed to its subsidiary undertaking. There are no derivatives held in 2020/21.

28. CAPITAL COMMITMENTS

	2021 £000	2020 £000
Group and Company		
Contracts placed for future capital expenditure not provided in the financial statements	47,119	35,169

All of the above capital commitments relate to property, plant and equipment.

Contingent liabilities

Through the ordinary course of operations, the company is party to various contract disputes. The directors do not expect the ultimate resolution of any of these proceedings to have a material adverse effect on the company's results of operations, cash flows or financial position.

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29. OBLIGATIONS UNDER OPERATING LEASES

Group and Company	Notes *	2021 £000	2020 £000
Minimum lease payments under operating leases recognised as an expense in the year	6	271	256
		271	256

All of the above capital commitments relate to property, plant and equipment.

30. EVENTS AFTER THE REPORTING DATE**Innovation Fund payments/awards**

In April 2021, Ofwat announced the results of the first Innovation in Water Challenge competition. There are 11 successful projects that will receive £2.2 million in funding from the Innovation Fund, including one that is being led by SEWL.

South East Water's project is titled Catchment LIFE and will build bespoke software that volunteers and experts can use, showing the impacts of habitat degradation on wildlife and ecological communities.

The project will receive £178,000 in funding from the Innovation Fund in the 2021/22 financial year. Additionally, SEWL's contributions from the collections made for the Innovation Fund to the other 10 successful projects will total £43,000 in 2021/22.

Committed credit facility re-financing and replacement

The company will be re-financing the outstanding balance on its existing revolving committed credit facility in 2021. The current facility is for a total of £90 million that can be drawn down by South East Water as required to finance its working capital and capital programme expenditure. This facility is due to expire in June 2022.

The amount drawn down at the balance sheet date was £80 million, which included £40 million taken as a safeguard against any potential liquidity issues the company may have experienced during the Covid-19 pandemic period. In July 2021, £30 million of the facility was repaid by the company.

The existing committed facility will be replaced with a new facility for £125 million and a term of five years.

31. RELATED PARTY TRANSACTIONS

The group of companies into which results of the group are consolidated is that headed by HDF, a company registered in England and Wales.

Balances and transactions between the company and its subsidiaries, which are related parties of the company, have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the Group and other related parties are disclosed below.

Notes to the consolidated financial statements

for the year ended 31 March 2021

31. RELATED PARTY TRANSACTIONS continued

31.1 TRANSACTIONS WITH THE GROUP'S PARENT COMPANY

	2021 £000	2020 £000
Loan to immediate parent company	-	136,000
Group relief	6,845	7,214
	6,845	143,214

Group issued a special restructuring dividend of £136 million in December 2020 to its parent company South East Water Holdings. These funds were used by the parent company to repay its inter company loan to South East Water Limited on the same day resulting in a net nil cash impact.

Loan interest receivable during the year was £2.3 million (2020: £4.5 million).

31.2 OTHER RELATED PARTY TRANSACTIONS

Other related party transactions are as follows:

Related party relationship	Type of transaction	2021 £000	2020 £000
Group's ultimate parent company	Group tax relief payable	3,845	3,374
Subsidiary	Loans payable excluding accrued interest	465,238	460,638
		469,083	464,012

Interest of £16.7 million (2020: £21.3 million) has been charged on these loans during the year. Interest outstanding on the loans at 31 March 2021 totalled £3.4 million (2020: £3.7 million).

Key management compensation is disclosed in note 7 and discussed further in the remuneration report. Contributions to retirement benefit schemes are disclosed in note 24.

32. PARENT COMPANY AND ULTIMATE CONTROLLING PARTIES

Utilities of Australia Pty Limited as Trustee for the Utilities Trust of Australia ("UTA"), NatWest Pension Trustee Limited as Trustee for the NatWest Group Pension Fund ("NWPF"), Régime de Rentes du Mouvement Desjardins ("RRMD"), Desjardins Financial Security Life Assurance Company ("DFSL") and Certas Home and Auto Insurance Company ("Certas") are the company's joint ultimate holding companies. UTA is incorporated in Australia. NWPF is incorporated in the United Kingdom, RRMD, DFSL and Certas are incorporated in Canada. It is the directors' belief that there is no single ultimate controlling party and that the joint ultimate holding companies control the company jointly.

The immediate parent company is South East Water (Holdings) Limited.

The largest and smallest group of companies into which results of the company are consolidated is that headed by HDF (UK) Holdings Limited, a company which is incorporated in Great Britain and registered in England and Wales. The consolidated financial statements of HDF may be obtained from the Company Secretary at the company's registered office at Rocfort Road, Snodland, Kent, ME6 5AH.

Consumer and community focused

HOW WE UNDERSTAND
AND RESPOND TO THE
NEEDS OF SOCIETY

ANNUAL PERFORMANCE

Most of us live and work in our supply area and so are dedicated to supporting those who need it most, supporting communities and also providing you with the high standards of service you expect (find out more [page 101](#))

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This annual performance report has been prepared in accordance with Condition F of South East Water Limited's ("SEW") instrument of appointment ("Licence") and in accordance with the latest regulatory accounting guidelines ("RAGs") issued by Ofwat. In instances where there are differences between International Financial Reporting Standards ("IFRS") as adopted for use in the United Kingdom and the RAGs, the RAGs take precedence.

These disclosures and statements should be read in conjunction with the information set out in the financial statements of South East Water Limited for the year ended 31 March 2021.

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BOARD STATEMENT ON ACCURACY AND COMPLETENESS OF DATA AND INFORMATION

This statement sets out the approach adopted by the board and the activities it has carried out with a view to ensuring that the data and information published by the company is accurate and complete and to allow it to make the statement set out below.

In August 2019, Ofwat explained that it would no longer issue assessments of companies under the company monitoring framework and following consultation in June 2020 confirmed that companies would be free to define assurance approaches that suit their particular circumstances and that companies were no longer required to follow the mechanisms and requirements of the company monitoring framework.

The board considered that the approach developed by the company for the purpose of the company monitoring framework had helped improve reporting processes and had had a positive impact on the quality of the data and information it published.

The board considered that the formal assessment of risks, strengths and weaknesses in the company monitoring framework was a key component of data assurance and that the related assurance plan should remain part of the broader system of risk management of the company for 2020/21 due to the importance of regulatory reporting within the regulatory framework.

The board therefore decided that for 2020/21 the company would produce and publish a company monitoring framework as it had done in previous years. Ofwat did not undertake a formal review of the industry's publications in 2020, but did send out informal reviews to each company. Ofwat identified a small number of issues which we have addressed in our current company monitoring framework.

Our current company monitoring framework can be found using the following link



corporate.southeastwater.co.uk/media/4184/sew-company-monitoring-framework-20-21.pdf

THE UPDATE TO OUR COMPANY MONITORING FRAMEWORK AND OFWAT FEEDBACK

Our action plan has reviewed Ofwat's concerns in detail and put in place actions to try to resolve these concerns.

Financial information

Ofwat stated:

"We identified only a couple of minor errors or omissions in the information published:

- the company used the incorrect tax number in the calculation for the effective tax rate (4H.16): 1A.18 UK Corporation Tax; and
- the company did not state what the outlook on their credit rating was anywhere in the APR."

We will ensure that we will use the correct tax number in the calculation for the effective tax rate as per the RAG guidance. We will state the outlook on our credit rating in the Annual Report commentary. We will also report the outlook/watch status of our credit ratings within table 4H of this annual performance report, in line with the updated requirements of this table.

Financial flows

Ofwat stated:

"The values reported for 'Cost of debt' were not in line with expectations the table should be supported by sufficient narrative or a more detailed breakdown to allow the reader to understand the information that is being presented and how it was derived."

Commentary will be included for areas that may not be in line with Ofwat's expectations and to clarify how the figures were calculated.

We will provide sufficient narrative or a more detailed breakdown alongside table 1F of this annual performance report, if deemed necessary, to allow the reader to understand the information that is being presented and how it was derived.

DIRECTORS' STATEMENTS AND CERTIFICATES continued

Dividend policy

Within their feedback, Ofwat stated:

"The company did not provide detailed support/justification for the £11 million paid in dividends in the year to March 2020. From the year 2020/21, we expect the company to transparently set out how any dividend payments are arrived at, including how they take account of delivery to customers and other obligations. The company needs to explain how the amount paid in dividends tallies with their 2020 to 2025 dividend policy."

Detailed support/justification will be provided within our accounting and performance disclosures for the dividend payments in the year to March 2021 and will be transparent in setting out how any dividend payments are arrived at, including how we take account of delivery to customers and other obligations. We will also explain how the amount paid in dividends tallies with our 2020 to 2025 dividend policy.

Long-Term Viability Statement (LTVS)

Ofwat stated:

"Only one concern was noted: There was no mention of the gearing sharing mechanism which would have been expected given that reported gearing was above 70 per cent at 74.55 per cent."

We will include commentary for the gearing sharing mechanism where this is relevant.

OUR INTERNAL CONTROLS AND BOARD OVERSIGHT

Our governance and assurance process for the preparation of our annual performance report and performance, people and planet microsite were based on our well-established systems of internal control for all regulatory and performance reporting.

These processes incorporated oversight by the board and scrutiny by the audit and risk committee following reviews by the executive directors, and the requirement for heads of department and/or manager level sign off.

Internal processes and controls

The assurance methodology that we have adopted is in line with our approach set out in our company monitoring framework with the three levels of assurance as described below:

Level 1

- peer review – data and information must be checked by a separate individual
- manager review/sign off – data and information is required to be checked by the line manager responsible for the individual completing the submission
- independent review is undertaken of the reporting requirements to ensure all required changes and actions are identified
- the changes identified are circulated and assigned to an owner
- formal review of last year's Ofwat queries and audit issues are circulated to the owners to ensure required actions are adopted
- data owners are required to complete pre audit check lists which cover all areas of compliance including Ofwat's reporting requirements

Level 2

Internal review

- data and process audit – data validity is tested through taking a sample and verifying the data for critical data such as PCs, ODIs and 'C' grade areas
- the methodology document is reviewed to ensure that the process and internal controls are complete and being followed
- any required changes are controlled by the Regulatory Assurance Manager. A log has been maintained to track sign off at all the assurance stages and provide an audit trail to the source data
- the process for areas of high risk and importance are reviewed and additional assurance added. For example, all interruption events are separately reviewed and signed off by the manager
- internal consistency checks have been undertaken on the data within the annual performance report and against other published documents

DIRECTORS' STATEMENTS AND CERTIFICATES continued

- a master set of APR tables is linked to our source data to provide an audit trail. This is separately managed and controlled
- independent review is undertaken to check the tables are populated with the audited data
- the master set of data tables and submission version is checked manually cell by cell by an independent reviewer and by an automatic electronic lookup. These are used to try to eliminate any input errors arising from the manual entry process required for the submission version of the tables
- independent check to ensure all the formatting requirements have been met
- internal consistency checks on the APR tables with APR commentary

External review

- data, process and submission audit – this process is undertaken by an external assurance partner
- a review of methodology, data sampling and internal controls is undertaken
- meetings undertaken with senior managers and those who produce the data to ensure a thorough understanding is obtained. The external auditors attend the pre audit meetings to review preparations for the audits and any potential issues that may arise
- external consistency checks have been carried out on our APR Tables, by our independent assurance partner Atkins
- independent review is undertaken to check the tables are populated with the audited data

Level 3

- director/executive approval – final review of submission information
- audit and risk committee review
- board approval – overall review of assurance and auditing undertaken
- discussion and approval of external assurance partner findings

Annual reporting has a clear ownership structure with relevant managers and head of departments taking ownership of sections of the reporting and supporting material. Each data table has data providers assigned for each line and each section and table has an overarching table owner who is a head of department, reporting to an executive director. The data providers are responsible for collecting, compiling and reporting the data to the table owner and the table owner is responsible for reviewing such data.

Board oversight

The board considered and approved the final processes used for the generation of the 2020/21 annual reporting.

The audit and risk committee also scrutinised the annual performance report and related narrative.

It considered the report presented directly by Atkins and the financial auditors to the committee on the outcome of their audits of the company's processes and annual reporting. In respect of performance, Atkins presented their findings following their review of the performance of the company in 2020/21 against performance commitments and their comments and recommendations.

The audit and risk committee and the board also reviewed the annual performance report including the statements from the board and the ring-fencing certificate as well as the content of the performance, people and planet microsite. Our annual performance tables have been prepared under the scrutiny of our audit and risk committee.

This committee reported to the board and presented its recommendations before the board approved the company's annual reporting.

OUR EXTERNAL ASSURANCE

As the processes and associated data items are complex and detailed, the board focuses on the process followed to prepare and review data, the robustness and clarity of the reported information, and obtains additional information and analysis from the executive directors. In addition, the board assures itself of the robustness of process and data by gaining assurance from Atkins.

DIRECTORS' STATEMENTS AND CERTIFICATES continued

Atkins role is to assist the board to ensure completeness of the annual reporting, compliance with relevant duties and obligations, and to ensure that the information we provide to demonstrate compliance with our relevant duties and obligations is consistent, comparable, reliable and robust. They presented their summary report and findings to the audit and risk committee.

During 2020 Jacobs (our previous assurance partner) undertook a half year review of some of our performance commitments providing feedback on any potential improvements identified.

Details of the work performed by Deloitte LLP on our annual performance report are provided in the independent auditor's report on page 264.

Deloitte also performed agreed upon procedures in relation to the lines not covered in their audit of table 1F detailed above as follows:

- agree line 1F.9 is the sum of lines 1F.3 to line 1F.8 plus line 1F.1
- agree line 1F.16 is sum of lines 1F.10 to line 1F.15
- agree line 1F.17 is the sum of lines 1F.9 and line 1F.16
- agree line 1F.19 is the sum of lines 1F.17 and line 1F.18
- agree line 1F.22 is the sum of line 1F.19 to line 1F.21
- agree line 1F.25 is line 1F.22 minus line 1F.23 and line 1F.24

For the current reporting period Atkins have reviewed all of our performance commitments and carried out process audits during the year, as well as the year end audits covering process and performance. This is done through separate audits for each of the PCs, ODIs and sub measures, enabling additional information to be reviewed on a yearly basis and enabling the auditors to provide a more robust challenge. Final audits of the APR tables are then undertaken (Tables 3A, 3C, 3D, 3E, 3F, 3H and 3I). The following annual performance report tables are also audited by Atkins:

- 2B – Totex analysis – wholesale water
- 2C – Retail operating cost analysis
- 4A – Water bulk supply information
- 4C – Impact of AMP performance on RCV

- 4D – Water resources and water network+ totex analysis
- 4F – Major project expenditure
- 4J – Water resources and water network+ base operating expenditure
- 4N – Developer services expenditure – water resources and network+
- 4P – Expenditure on non-price control diversion

Atkins also reviewed the following tables included in the supplementary tables report published alongside our annual report:

- 4L – Enhancement expenditure – water resources and network+
- 4Q – Developer services – new connections, properties and mains
- 4R – Connected properties, customers and population
- 5A – Water resources asset and volumes
- 5B – Water resources operating cost analysis
- 6A – Raw water transport, raw water storage and water treatment data
- 6B – Treated water distribution – assets and operations
- 6C – Water network+ – mains, communication pipes and other data
- 6D – Demand management – metering and leakage activities

Deloitte, our financial auditors have audited:

- Section 1, except lines 1F.4, 1F.7, 1F.9 to 1F.11, 1F.15 to 1F.17, 1F.19 to 1F.22 and 1F.25
- Section 2

Deloitte have performed agreed upon procedures for the following tables:

- 4B – Analysis of debt
- 4H – Financial metrics
- 4I – Financial derivatives
- 9A – Innovation competition

The findings from annual audits will be incorporated into the process of updating our company monitoring framework replacement, which is currently under review.

DIRECTORS' STATEMENTS AND CERTIFICATES continued**OUR PLANS FOR PUBLISHING OUR FUTURE APPROACH TO DATA ASSURANCE**

Following the confirmation from Ofwat that it will no longer use the company monitoring framework and encouraging boards to develop their approach to data assurance, we will review the current format, content and purpose of our assurance in 2021/22 to assess the elements that worked well to date and which we may retain and where changes may help facilitate the board oversight and improve the reliability, accuracy and completeness of the data and information we publish going forward.

STATEMENT BY DIRECTORS

For the preparation of this statement we have considered the internal processes and controls and the external assurance relating to the data and information which the company has provided to Ofwat in the reporting year and/or that we have published as a water undertaker which are described in this statement.

We have also specifically considered the report to the audit and risk committee by our external assurance partners and our auditors and the independent auditor's report set out in this annual performance report and the report from the audit and risk committee and its recommendation to the board relating to the regulatory reporting of the company for 2020/21.

Our consideration of the above has not identified any material deviation from or non-compliance with reporting obligations and to the best of the board's knowledge after reasonable enquiries the data and information falling within the scope of this statement is accurate and complete in all material respects and the company is taking appropriate steps to manage and/or mitigate the risks of inaccuracy or incompleteness of data or information.

Where there may be ambiguity in requirements or some of them may be open to different interpretations, commentary has been transparently included in our reporting.

We note that the imbalance in the water balance for the reporting year at 4.1 per cent is above the threshold that requires notification to Ofwat according to the common metric reporting requirements. This was identified in our commentary.

We have been engaging with Ofwat in relation to the reporting on non-household voids due to evidence that the total number of voids from the Central Market System which would normally be used to report non-household voids is not accurate. Specific internal and external assurance was carried out on the process used to determine a more reliable number where there is clear evidence that properties are occupied, demolished or have become household premises. Due to the number of void premises that would need to be checked there is a possibility that the number of non-household void properties reported is still higher than it is in reality.

Based on the scope and outcome of the review processes detailed in this statement and in our annual financial and regulatory reporting, and subject to the observations set out above on areas of uncertainty, the board is able to confirm that the data and information which the company has provided to Ofwat in the reporting year and/or which they have published in their role as water undertaker was accurate and complete.

Approved by the board and signed on its behalf by:

DAVID HINTON
CHIEF EXECUTIVE OFFICER
15 JULY 2021

ANDREW FARMER
CHIEF FINANCIAL OFFICER
15 JULY 2021

DIRECTORS' STATEMENTS AND CERTIFICATES continued

RISK AND COMPLIANCE STATEMENT

As directors of South East Water, we have relied on the established systems of internal control the company operates to ensure that it delivers its statutory, regulatory and obligations under its instrument of appointment ("Licence") and manages its risks in order to prepare this statement, the regulatory accounts, the annual performance report and all related narrative.

We have also relied on comprehensive and transparent controls and assurance mechanisms which set out clear accountability for data collection, analysis and verification following the approach defined in our company monitoring framework and detailed in the board statement on accuracy and completeness of data and information. The data and control processes themselves have been thoroughly reviewed by external financial and technical auditors to ensure that the information we publish is robust and of high quality. This enables us to have a high degree of confidence in the information presented in this year's regulatory reporting and supporting data on which the declarations of compliance set out at the end of this statement are based.

We describe our risk management systems and our principal risks in our strategic report. We describe our governance and how we comply with the principles of our corporate governance code and the objectives of the board leadership, transparency and governance principles and more particularly on transparency and accountability in our corporate governance report.

Our company monitoring framework describes our approach to reporting and to the assurance of our information. A summary of the process we followed to assure the quality of our reporting is set out in the board statement on accuracy and completeness of data and information.

We have also set out our assessment of the prospects and viability of the company in our long-term viability statement taking account of the final determination and of our assessment of the potential impact of the Covid-19 pandemic on the UK economy, our customers and our business.

In addition to regular reporting during the year, compliance with our obligations under sector specific legislation or regulation and under our Licence was reviewed for our annual reporting under our two KPIs relating to compliance with our

national security obligations and to compliance with other statutory obligations and Licence conditions which is reported on our performance, people and planet microsite. This reporting did not identify any reportable deviation from or non-compliance with these obligations in 2020/21.

For the preparation of this statement we have considered compliance with our statutory, regulatory and Licence obligations, particularly those considered by our annual reviews as set out above. We have also specifically considered compliance with our statutory, regulatory and Licence obligations that have not been confirmed by other processes and for which Ofwat is the enforcement authority. Our annual reviews have not identified any material deviation from or non-compliance with these obligations and to the best of the board's knowledge after reasonable enquiries South East Water has complied in all material respects with these obligations and is taking appropriate steps to manage and/or mitigate the risks it faces.

This statement is published alongside our annual report and financial statements, and annual performance report for the year ended 31 March 2021, and in making this statement we have taken account of the other statements made in compliance with our obligations under conditions F, and P of our Licence and under section 35A of the Water Industry Act 1991 (which are set out in the directors' remuneration report).

Based on the scope and outcome of the review processes detailed in this statement and in our annual financial and regulatory reporting the board is able to confirm that South East Water:

- considers it has a full understanding of, and is meeting, all its relevant statutory, Licence and regulatory obligations and has taken steps to understand and meet customer expectations
- has satisfied itself that it has sufficient processes and internal systems of control to meet its obligations
- has appropriate systems and processes in place to identify, manage, mitigate and review its risks

Approved by the board and signed on its behalf by:

DAVID HINTON
CHIEF EXECUTIVE OFFICER
15 JULY 2021

ANDREW FARMER
CHIEF FINANCIAL OFFICER
15 JULY 2021

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DIRECTORS' STATEMENTS AND CERTIFICATES continued**RING FENCING CERTIFICATE**

Under condition P30 of the company's instrument of appointment ("Licence"), the company is required to provide a ring-fencing certificate as defined in condition A of the Licence and relating to the availability of sufficient financial and other resources to carry out the functions of a water undertaker.

This ring-fencing certificate is made in accordance with the requirements of condition P30 of the Licence.

Condition P33 provides that whenever the company submits a ring-fencing certificate to Ofwat, it must also submit a statement of the main factors which the board has taken into account in giving its opinion for the ring-fencing certificate.

In addition, condition P35 provides that each ring-fencing certificate must be accompanied by a report prepared by the company's auditors and addressed to Ofwat, stating whether they are aware of any inconsistencies between the ring-fencing certificate and either the regulatory accounting statements referred to in condition F6.1 or any information which the auditors obtained in the course of their work as the company's auditors, and if so, what they are.

Information relevant to this certificate has been compiled and analysed for the purpose of our financial and regulatory reporting in accordance with our internal and external assurance processes. The most relevant information to support this certificate is mentioned in the review of the main factors that the board had regard to in respect of this ring-fencing certificate.

The independent auditor's report can be found on page 264 of this annual performance report and is relevant to the understanding of this certificate.

STATEMENT BY DIRECTORS

Following due consideration of the factors taken into account by the directors as set out in more detail below, in the opinion of the directors:

- (a) the company will have available to it sufficient financial resources and facilities to enable it to carry out the regulated activities as defined in the Licence, for at least the twelve month period following the date on which the certificate is submitted
- (b) the company will have available to it sufficient management resources and systems of planning and internal control to enable it to carry out the regulated activities, for at least the twelve month period following the date on which the certificate is submitted
- (c) the company has available to it sufficient rights and resources other than financial resources, as required by paragraph P14 (i.e. that if, at any time, a special administration order were to be made in relation to it, the special administrator would be able to manage the affairs, business and property of the company in accordance with the purposes of the special administration order)
- (d) all contracts entered into between the company and any associated company include the necessary provisions and requirements in respect of the standard of service to be supplied to the company, to ensure that it is able to carry out the regulated activities

DIRECTORS' STATEMENTS AND CERTIFICATES continued

MAIN FACTORS TAKEN INTO ACCOUNT BY THE DIRECTORS

The ring-fencing certificate above has been made having regard to the company's performance, position and prospects as reflected and explained in the entire annual report and the APR.

In providing the certificate set out above, the directors have taken into account the following factors:

FINANCIAL RESOURCES AND FACILITIES

READ MORE

Financial details, e.g. cash position, financial headroom, refinancing undertaken/planned

- the updates provided at each board meeting confirming that the financial performance of the company is in accordance with budget or forecast and the steps taken to address variances
- our audited financial statements, which have been prepared on the going concern basis
- the financial budget for 2021/22 approved by the board on 4 March 2021 and our subsequent regular reporting and forecasting to take account of the impact of Covid-19 on the financial position of the company and providing comfort on its ability to deliver its investment programme
- the refinancing completed in 2019 and our monitoring of markets and of the impact of Covid-19 as we plan and prepare for further refinancing in 2025 and 2029.
- our committed borrowing facilities totalling £148 million (including the working capital facility of £90 million due for renewal in June 2022 and which is being replaced by an extended facility with discussions underway for this replacement, and also two facilities totalling £58 million to be renewed at the renewal date in June 2022. See note 22 for further details.)

Our going concern statement on page 111

Performance against Final Determinations (FDs) set at the past price review

- the updates provided each month and at each board meeting on the operational performance of the company
- the performance in the first year of AMP7 which despite a net penalty position due mainly to a combination of exceptional demand and heatwave impacting interruption performance still reflects an appropriate and sustainable overall underlying performance
- the assessment of the impact of Covid-19 carried out throughout the year and at year-end on the ability of the company to (i) still deliver its investment programme albeit with a detrimental effect on its ability to achieve targeted efficiencies, and (ii) to deliver its performance commitments subject to any adjustments to the regulatory mechanisms to be determined by Ofwat

Details on our performance are set out on page 64

DIRECTORS' STATEMENTS AND CERTIFICATES continued**FINANCIAL RESOURCES AND FACILITIES** continued**READ MORE**

Credit related factors e.g. credit facilities, ratings, compliance with covenants etc

- that we have complied with our financial covenants and have maintained our investment grade rating of BBB/Baa2
- additional drawdowns on the credit facility for the prudent management of liquidity in the context of the impact of Covid-19
- adoption of a STID proposal addressing the potential consequences of Covid-19 on compliance with our financial covenants to improve our financial resilience in particular preserving the ability to draw down additional debt even under certain trigger event scenarios
- our regular engagement with credit rating agencies to understand their approach to Covid-19 when assessing water companies credit ratings

Business plans, long-term viability statements, etc

- the known outcome of the 2019 price review for the five years from 1 April 2020 to 31 March 2025 and the corporate plan for 2020 to 2025 prepared on the basis of the final determination taking account of the negative weighting of the ODI targets
- our long-term viability statement using a baseline scenario reflecting our corporate plan for 2020 to 2025 and including further scenarios and stress testing to reflect the impact of Covid-19 and of the final determination on the position, prospects and financial viability of the company over 2020 to 2025 and for the whole duration of the lookout period of 10 years; including the outcome of the scenario analysis and stress testing on compliance with our financial covenants and on the key ratios for our credit ratings which confirmed the prospects and long-term viability of South East Water in light of severe but plausible scenarios

Our long-term viability statement on page 107

Any relevant reports – internal or third party

- the report commissioned by Water UK on the “Impact of Coronavirus on the UK water industry” which was developed to assess the potential impact on the regulated business on a sector-wide basis of the Covid-19 pandemic.
- the detailed report presented to the audit and risk committee and the board on the assumptions considered and scenarios used for the purpose of the long-term viability statement and their impact on the prospects of the company

DIRECTORS' STATEMENTS AND CERTIFICATES continued

MANAGEMENT RESOURCES	READ MORE
Management skills, experience and relevant qualifications - the balance of skills and experience of our executive team achieved through internal succession planning and of our senior management team assessed through communication at board meetings and through direct interaction outside of board meetings - the outcome of the latest board evaluation carried out in 2021 which reviewed the balance of skills and experience of the board and concluded that the board operated effectively	Our board evaluation on page 136
Recruitment process, staff engagement - our IIP silver accreditation - the annual update on human resources presented to the board and regular monthly updates on employee and cultural matters - the people plan within our corporate plan for 2020 to 2025 - our responsible business commitments relating to our employees pay, reward and recognition - our approach to board engagement with employees through a designated independent non-executive director, attendance at meetings of our Staff Council and a board engagement programme - the extensive staff engagement carried out during 2020/21 through pulse surveys and direct sessions with the CEO and senior management	Our section 172(1) statement on page 82
Succession planning for key management/staff, Quality of management/staff induction and other training and development - our discussions on succession planning for senior managers and the programmed update to our succession plans for the executive team and the senior management team over the next two years - our training initiatives managed by our organisational development team and our people plan referred to above	Our people on pages 85 and 102 of the strategic report
Process for ensuring diversity of perspectives; independence of the board; board or management activities; reports or statements - the stakeholder inclusive approach of our corporate governance framework - our board evaluation which considers the balance of skills, experience and diversity of our board, and how the board operates to receive information and reach, to the extent possible, concerted decisions taking account of all relevant considerations - the composition of our board which ensures a significant representation of independent non-executive directors - the arrangements in place for the effective operation of the board as described in the corporate governance report	Our corporate governance framework on page 56 The role of the board on page 124 of our corporate governance statement

DIRECTORS' STATEMENTS AND CERTIFICATES continued

SYSTEMS OF PLANNING AND INTERNAL CONTROL	READ MORE
Governance procedures; risk management frameworks; oversight procedures; risk; compliance other assurance statements	
• our risk management processes described in the strategic report • the review of our principal risks including to take account of the impact of the final determination and of Covid-19 on our risk profile. Our principal risks and related mitigations are relevant to several of the considerations set out in this table and provide additional details on how the company manages the impact of Covid-19 • our risk and compliance statement set out in this annual performance report • board statement on accuracy and completeness of data and information set out in this annual performance report referring to our company monitoring framework setting out how we ensure the accuracy and reliability of the information we publish which is available at: corporate.southeastwater.co.uk/news-info/publications/company-monitoring-framework	Our risk management model on page 32 Our principal risks on page 36
Internal and/or external audit policies, processes, activities and/or reports	
• the role of our audit and risk committee in monitoring the effectiveness of our risk management processes and internal controls • the internal and external assurance processes that were followed for the preparation of our annual report and this annual performance report including information relevant to this certificate as described in our board statement on accuracy and completeness of data and information set out in this annual performance report	
Systems for maintaining supply / business continuity, stated action plans	
• our incident management processes and other processes in place under SEMD and the satisfactory outcome of the independent SEMD audit • our cyber security and data compliance processes, relevant certifications and the satisfactory outcomes of the testing and audit of these processes • our good water quality performance in the year and the monthly reporting on water quality to the board • the annual review of our risk register by the board and the regular review of the risk register by our executive team • our resilience action plan and resilience maturity assessments • the effectiveness demonstrated by management in implementing new methods of working to respond to Covid-19 • 24 hours network modelling for rezoning to minimise the number of customers impacted and restore supplies as soon as possible • formal lessons learnt process followed after each significant incident with implementation of action plans reported to the board	

DIRECTORS' STATEMENTS AND CERTIFICATES continued

SYSTEMS OF PLANNING AND INTERNAL CONTROL continued**READ MORE**

Policies to prevent fraud and other unethical behaviour; whistleblowing policy

- our whistleblowing policy, anti-bribery policy, anti-facilitation of tax fraud policy and conflicts of interest policy and the review by the audit and risk committee of the processes in place and of any report made under these policies
- the consideration during the audit process of risks of fraud and misstatement and the external audit of management override and internal controls including automated journal entry testing

RIGHTS AND RESOURCES OTHER THAN FINANCIAL RESOURCES**READ MORE**

Corporate missions and/or values

Policies to encourage an integrated approach and 'systems thinking'

- our company purpose and revised director duties that are embedded into our articles of association and our corporate governance framework promoting an integrated thinking approach in our day to day decision making
- the ongoing work for the implementation of our resilience action plan and resilience maturity assessments
- our operating plans to manage peak demand in sensitive areas of our network and continue to improve the understanding of the system across operational teams to facilitate an optimum use of the water supply system
- the structured management of all incidents, small and large, to ensure all issues are resolved as quickly as possible limiting their impact on customers
- the approach to the delivery of our corporate plan for 2020 to 2025 including operational delivery plans by each relevant function and related action plans from relevant support functions
- our long term water resources management plan and dry weather plan integrating climate change adaptation with the progressive implementation of TCFD scenarios and financial reporting, our net zero routemap published in July 2021 and our revised adaptation plan to be published at the end of 2021

Our corporate governance framework on page 56

Our purpose and values on page 20

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DIRECTORS' STATEMENTS AND CERTIFICATES continued**RIGHTS AND RESOURCES OTHER
THAN FINANCIAL RESOURCES** continued

Technology and other systems for ensuring checks and balances; planning systems

- our internal systems of control and assurance described above
 - our IT infrastructure and automated reports including audit of relevant reports and systems by auditors and other external consultants on data security
 - our key operational systems including works management systems, leakage system, laboratory system, billing system
 - our asset management and planning processes used for the management of our capital programme and the risk base analysis of our investment, and for the development of our water resources management plan and dry weather plan
-

Assets maintenance / insurance factors

- implementation of an asset management system that will be ISO 55000 by 2025, building on our existing PASS 55 asset management system
- new incentives for innovation and improving resilience within our engineering consultancy framework
- new investment decision support tool. Risk based prioritisation of maintenance with customer impact as a primary consideration
- asset management strategy implementing new asset health metrics
- approach to resilience and improved horizon scanning and adaptation to climate change. Resilience training to staff. Classification of criticality for all assets allowing for prioritisation of investment to reduce exposure to risks
- area plans for each Resource Zone published annually and identifying key risks for each zone
- the review of our insurance policies renewals

DIRECTORS' STATEMENTS AND CERTIFICATES continued

CONTRACTING**READ MORE****Position/status of key contracts in place**

All contracts between the appointee and all associated companies were checked for compliance with licence requirements on standards

Details of transactions between the appointee and associated companies are given in the annual performance report

Compliance with licence provision on cross-subsidies between the appointee and any associated company

No guarantees or cross-default obligations given without Ofwat's written consent.

- the external assurance (as described above) applying to our reporting included in relation to transactions with associates as set out in this annual performance report
- that no new arrangements were entered into that included cross-default obligations or other new arrangement requiring the consent of Ofwat

MATERIAL ISSUES OR CIRCUMSTANCES

- the impact of Covid-19 to date and for the rest of 2021/22 including the experience of the business in implementing new methods of working to ensure services to customers and critical facilities are maintained while protecting the health of our employees, customers and suppliers
- the review of the company's principal risks and in particular Covid-19 related mitigations, and the related forecasting and analysis carried out for the long-term viability statement

Our principal risks on page 36

Approved by the board and signed on its behalf by:

DAVID HINTON
CHIEF EXECUTIVE OFFICER
15 JULY 2021

ANDREW FARMER
CHIEF FINANCIAL OFFICER
15 JULY 2021

AUDITOR'S REPORT

INDEPENDENT AUDITOR'S REPORT TO THE WATER SERVICES REGULATION AUTHORITY (THE WSRA) AND THE DIRECTORS OF SOUTH EAST WATER LIMITED

OPINION

We have audited the sections of South East Water Limited's Annual Performance Report for the year ended 31 March 2021 ("the Regulatory Accounting Statements") which comprise:

- the regulatory financial reporting tables comprising the income statement (table 1A), the statement of comprehensive income (table 1B), the statement of financial position (table 1C), the statement of cash flows (table 1D), the net debt analysis (table 1E), Lines 1F.1 to 1F.3, 1F.5 to 1F.6, 1F.8, 1F.12 to 1F.14, 1F.18 and 1F.23 to 1F.24 of the statement of financial flows (table 1F) and the related notes; and
- the regulatory price review and other segmental reporting tables comprising the segmental income statement (table 2A), the totex analysis for wholesale water and wastewater (table 2B), the operating cost analysis for retail (table 2C), the historical cost analysis of fixed assets for wholesale and retail (table 2D), the analysis of grants and contributions and land sales for wholesale (table 2E), the household water revenues by customer type (table 2F), the revenue analysis & wholesale control reconciliation (table 2I), the infrastructure network reinforcement costs (table 2J), the infrastructure charges reconciliation (table 2K), the analysis of land sales (table 2L), the revenue reconciliation for wholesale (table 2M), residential retail social tariffs (table 2N) and historical cost analysis of intangible assets (table 2O) and the related notes.

We have not audited Lines 1F.4, 1F.7, 1F.9 to 1F.11, 1F.15 to 1F.17, 1F.19 to 1F.22 and 1F.25 of the statement of financial flows (table 1F), the Outcome performance table (tables 3A to 3I) and the additional regulatory information in tables 4A to 4R, 5A to 5B, 6A to 6D, 7A to 7E, 8A to 8D and 9A.

In our opinion, South East Water Limited's Regulatory Accounting Statements have been prepared, in all material aspects, in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA (RAG 1.09, RAG 2.08, RAG 3.12, RAG 4.09 and RAG 5.07) and the accounting policies (including the Company's published accounting methodology statement(s), as defined in RAG 3.12, appendix 2) set out on page 271.

BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)"), including ISA (UK) 800, and applicable law, except as stated in the section on Auditors' responsibilities for the audit of the Regulatory Accounting Statements below, and having regard to the guidance contained in ICAEW Technical Release Tech 02/16 AAF 'Reporting to Regulators on Regulatory Accounts' issued by the Institute of Chartered Accountants in England & Wales.

Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the Regulatory Accounting Statements within the Annual Performance Report section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit, including the Financial Reporting Council's (FRC's) Ethical Standard [as applied to public interest entities], and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

EMPHASIS OF MATTER – SPECIAL PURPOSE BASIS OF PREPARATION

We draw attention to the fact that the Regulatory Accounting Statements have been prepared in accordance with a special purpose framework, Condition F, the Regulatory Accounting Guidelines, the accounting policies (including the Company's published accounting methodology statement(s), as defined in RAG 3.11, appendix 2) set out in the statement of accounting policies and under the historical cost convention. The nature, form and content of the Regulatory Accounting Statements are determined by the WSRA. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the WSRA's purposes. Accordingly we make no such assessment. In addition, we are not required to assess whether the methods of cost allocation set out in the accounting methodology statement are appropriate to the circumstances of the Company or whether they meet the requirements of the WSRA.

The Regulatory Accounting Statements are separate from the statutory financial statements of the Company and have not been prepared under the basis of international accounting standards in conformity with the requirements of the Companies Act 2006 ("IASs"). Financial information other than that prepared on the basis of UK IASs does not necessarily represent a true and fair view of the financial performance or financial position of a Company as shown in statutory financial statements prepared in accordance with the Companies Act 2006.

The Regulatory Accounting Statements on pages 274 to 339 have been drawn up in accordance with Regulatory Accounting Guidelines with a number of departures from IASs. A summary of the effect of these departures in the Company's statutory financial statements is included in the tables within section 1.

Our opinion is not modified in respect of this matter.

CONCLUSIONS RELATING TO GOING CONCERN

In auditing the Regulatory Accounting Statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the Regulatory Accounting Statements is appropriate.

Our evaluation of the directors' assessment of the company's ability to continue to adopt the going concern basis of accounting included:

- obtained an understanding of the relevant controls including management review controls and controls relating to the data integrity in the going concern model;
- analysing the Group's financing facilities including nature of facilities, repayment terms and covenants;

- assessing the likelihood of new facilities due for renewal in the going concern period being secured, and in particular refinancing of the revolving credit facility which has been approved by the lender;
- assessing the appropriateness of the assumptions taken by management in establishing their base case forecasts including comparison of growth forecasts with historical performance and market data;
- recalculating the forecast covenants and assessing management's evaluation of the headroom available against these covenants;
- evaluating the forecast liquidity position based on forecasts;
- challenging the appropriateness, and results of the sensitivity analysis performed by management through performing additional independent sensitivity testing and benchmarking with comparable water companies external information;
- assessing the sophistication of the model used to prepare the forecasts and testing of clerical accuracy of those forecasts; and
- assessing the appropriateness of the disclosures provided in the financial statements.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

AUDITOR'S REPORT continued**OTHER INFORMATION**

The other information comprises all of the information in the Annual Performance Report other than the Regulatory Accounting Statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the Regulatory Accounting Statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the Regulatory Accounting Statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Regulatory Accounting Statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the Regulatory Accounting Statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report based on these responsibilities.

RESPONSIBILITIES OF THE DIRECTORS FOR THE ANNUAL PERFORMANCE REPORT

As explained more fully in the Statement of Directors' Responsibilities set out on page 254, the directors are responsible for the preparation of the Annual Performance Report in accordance with the Regulatory Accounting Guidelines issued by the WSRA and the Company's accounting policies (including the Company's published accounting methodology statement(s), as defined in RAG 3.12, appendix 2).

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

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

AUDITORS' RESPONSIBILITIES FOR THE AUDIT OF THE REGULATORY ACCOUNTING STATEMENTS WITHIN THE ANNUAL PERFORMANCE REPORT

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

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.

We considered the nature of the company's industry and its control environment, and reviewed the company'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 obtained an understanding of the legal and regulatory frameworks that the company operates in, and identified the key laws and regulations that:

- Had a direct effect on the determination of material amounts and disclosures in the Regulatory Accounting Statements. These included Regulatory Accounting Guidelines as issued by the WRSA, UK Companies Act, pensions legislation and tax legislation; and
- Do not have a direct effect on the Regulatory Accounting Statements but compliance with which may be fundamental to the company's ability to operate or to avoid a material penalty. These included the company's operating licence, regulatory solvency requirements and environmental regulations.

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 in-house/external 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 correspondence with HMRC and WSR.

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

USE OF THIS REPORT

This report is made, on terms that have been agreed, solely to the Company and the WSR in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewerage undertaker under the Water Industry Act 1991 ("Condition F"). Our audit work has been undertaken so that we might state to the Company and the WSR those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under Condition F to procure such a report and (b) to facilitate the carrying out by the WSR of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the WSR, for our audit work, for this report or for the opinions we have formed.

Our opinion on the Regulatory Accounting Statements is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2021 on which we reported on 15 July 2021, which are prepared for a different purpose. Our audit report in relation to the statutory financial statements of the Company (our "Statutory audit") was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our Statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a statutory audit report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our Statutory audit report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Deloitte LLP

London, United Kingdom
15 July 2021

ACCOUNTING AND PERFORMANCE DISCLOSURES

EXECUTIVE PAY AND PERFORMANCE

The directors' remuneration report in the company's annual report and financial statements sets out the remuneration paid or due for the financial year to the directors under arrangements linking the remuneration of directors to standards of performance in connection with the carrying out by South East Water of its functions as a relevant undertaker. It provides details of these arrangements and of the relevant remuneration. The relevant information provided in the directors' remuneration report is incorporated by reference into this annual performance report as the statement required under section 35A of the Water Industry Act 1991. The report from the remuneration committee in the corporate governance report also provides information on the arrangements in place for the remuneration of directors and how they have been reviewed by the Committee.

DIVIDEND POLICY AND EXPLANATIONS ON DIVIDEND PAID

Our licence requires us to only pay dividends in accordance with a dividend policy which has been approved by the board and which complies with the principles that dividends declared or paid will not impair the ability of the company to finance the appointed business and that under a system of incentive regulation dividends would be expected to reward efficiency and the management of economic risk.

The overarching objective of our dividend policy is that dividends should provide a suitable return to shareholders for their investment in the company whilst ensuring that the company is able to finance its functions and meet its obligations as a water undertaker without impairing its long term financial resilience.

Dividends should be set and paid at a level that enables the company to maintain its long term financial resilience in the interest of shareholders, customers, employees and other stakeholders and subject to the company (i) having adequate resources to meet its financial obligations and (ii) being able to comply with its obligations under the Companies Act 2006 relating to the declaration and payment of dividends.

FACTORS CONSIDERED BY DIRECTORS WHEN APPROVING DIVIDENDS

Dividends are considered in the context of the overall performance and financial resilience of the company, which also depends on our operational performance against our outcome delivery incentives and any reward or penalty. Dividends are also considered by reference to forecast financial and operational performance to ensure that they would not compromise the future performance of the company.

In approving dividends in accordance with our dividend policy, the board had regard to the following factors:

Financial obligations and resilience

- The obligation of the company to maintain an investment grade credit rating under its instrument of appointment.
- Compliance with the company's financial covenants including specific credit ratios requirements.
- The need to maintain sufficient liquidity and to preserve the longer-term viability of the company.
- The actual and forecast level of gearing and the ability of the company to maintain its corporate plan objectives relating to gearing maintenance or reduction.

Interests of employees

- The latest valuation of the company's pension schemes and of any deficit as well as any forecast deficit based on a reasonable assessment of the implementation of the company's strategy to fund any such deficit.

In respect of ordinary dividends for the appointed business our policy is that the base level of ordinary dividend should be set and paid at a level that is within the allowed returns determined by Ofwat in the current price determination and does not exceed a nominal 4 per cent yield on equity based on the actual financial structure of the company.

ACCOUNTING AND PERFORMANCE DISCLOSURES continued

In setting the base level of ordinary dividend and in considering any distribution of a dividend in respect of the appointed business, the board ensures that the company will have adequate resources to finance the appointed business and to fulfil its duties as a water undertaker. The board has also regard to the following key considerations:

- the ability of the company to finance current and future investment in the appointed business
- the performance commitments in the company's current final determination to deliver service improvements for customers, taking account of the realistic level of financial risks in the form of ODI penalties associated with setting stretching performance targets and the need for adequate resilience

MAIN CONSIDERATION FOR DETERMINING THE AMOUNT OF DIVIDEND IN 2020/21

In 2020/21 and for AMP7, Ofwat's final determination is the single factor that most influences the level of dividend paid by the company. It is characterised by a low allowed return and in-period Outcome Delivery Incentive (ODI) penalties that are unavoidable as a consequence of the negatively weighted approach to risk and return adopted by Ofwat.

The anticipated amount of dividend in 2020 to 2025 has therefore been reduced to a minimum sustainable level that will ensure that (i) the company is able to meet its obligations under existing financing arrangements and to maintain an investment grade credit rating, and (ii) the parent group is also able to meet its obligations under existing loans.

This level of sustainable dividend takes account of the operational performance and the impact for customers in that it anticipates an unavoidable level of ODI penalties being incurred despite the delivery of performance improvements due to the negative weighting of ODIs.

In 2020/21 the company only paid ordinary dividends sufficient for ensuring that loan obligations at group level were met.

During 2020/21 the obligations at group level consisted of (i) payment of interests to the company under a loan from the company to its immediate parent, South East Water (Holdings) Limited (which was repaid on 15 December 2020 as explained below), (ii) interest payable under a third party loan and (iii) interest payable under a shareholder loan.

When approving these dividends, the board considered the prospects of the company in light of the principal risks and uncertainties, including the ongoing impacts of Covid-19 and determined that the company would remain able to deliver the levels of performance targeted and sustain a realistic level of ODI penalties reflecting the outcome of the final determination, the impact of Covid-19 and the summer 2020 high demand incident.

The level of sustainable dividend also took account of the use of retained cash at group level to meet the difference between the dividend paid by the company and the group obligations to be met.

Consequently, no dividend have been paid by our ultimate holding company, HDF (UK) Holdings Ltd, to the ultimate shareholders of the company. This outcome is expected to remain throughout 2020 to 2025.

OVERALL AMOUNT OF DIVIDEND

Dividends in the year totalled £147 million which included:

- ordinary dividends totalling £11 million which were paid in equal quarterly instalments
- a special restructuring dividend of £136 million related to the repayment by South East Water (Holdings) Limited (SEWH) of a loan from the company of the same amount

SEWH used part of the £11 million dividend to pay interest to the company under the loan referred to above, until it was repaid on 15 December 2020, resulting in a net ordinary dividends of £8.8 million.

Dividends are paid as declared and are recognised as a distribution when approved by the board. No unpaid dividends exist at the year-end.

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ACCOUNTING AND PERFORMANCE DISCLOSURES continued**SPECIAL RESTRUCTURING DIVIDEND**

On 15 December 2020, the loan of £136 million by the company to its immediate parent, SEWH, was repaid simplifying the group financial structure.

This transaction required the same day payment of a special dividend of £136 million out of distributable reserves by the company to SEWH, followed immediately by the loan repayment from SEWH to the company. There was no cash impact for either of the companies involved.

DIVIDEND YIELD

The ordinary dividend yield (excluding the special dividend related to the repayment of the loan by SEWH) in the financial year ended 31 March 2021 was 2.1 per cent.

The ordinary appointed business dividend yield was 1.5 per cent and reflects the amount of dividend paid by the company after deducting the non-appointed business contribution and the amount of dividend paid to SEWH but used by SEWH to pay interest under the £136 million loan.

This ordinary appointed business dividend yield is well below the nominal 4 per cent dividend yield that we have committed not to exceed in our dividend policy.

LONG-TERM VIABILITY STATEMENT

Our long-term viability statement is set out on page 107 of the strategic report. Details of our risk management process and of our principal risks may be found on pages 30 to 55 of the strategic report.

STATEMENT OF DIRECTORS' RESPONSIBILITY

Under conditions F and P its instrument of appointment ("Licence") the company is responsible for:

- preparing a set of regulatory accounting statements, in respect of the twelve months ending on 31 March in each charging year, which are in accordance with the Regulatory Accounting Guidelines
- complying with all other requirements that are set out in the Regulatory Accounting Guidelines

- ensuring that, as far as reasonably practicable, it has available to it sufficient rights and resources other than financial resources so that if, at any time, a special administration order were to be made in relation to it, the special administrator would be able to manage the affairs, business and property of the company in accordance with the purposes of the special administration order
- maintaining the listing of a financial instrument and shall use all reasonable endeavours to retain the listing of that financial instrument, whose market price should react to the financial position of the company's appointed business, on the London Stock Exchange, or, with the prior agreement of Ofwat, some other exchange of similar standing
- ensuring that it or any associated company which issues corporate debt on its behalf maintains, at all times, an issuer credit rating which is an investment grade rating
- submitting a ring-fencing certificate to Ofwat a statement of the main factors which the Board of the Appointee has taken into account in giving its opinion for the ring-fencing certificate

DISCLOSURE OF INFORMATION TO AUDITORS

The directors who were members of the board at the time of approving the annual performance report are listed in the company's annual report. Having made enquiries of fellow directors, and exercising reasonable care, skill and diligence, each of these directors confirms that:

- so far as the director is aware, there is no relevant audit information of which South East Water Limited's auditor is unaware
- each director has taken all the steps that a director ought to have taken as a director in order to make himself or herself aware of any relevant audit information and to establish that South East Water Limited's auditor is aware of that information

ACCOUNTING POLICIES

PRICE CONTROL SEGMENTS

Operating costs are directly attributed to price control units, where possible, based on the activities that cause the cost to be incurred. Costs are attributed based on the guidelines set out in RAG 2.08. Where costs cover more than one price control unit, an appropriate basis of allocation consistent with the activities that cause the costs is used in order to allocate the costs to the relevant price control units.

In the majority of cases, assets and their associated depreciation are directly attributed to price control units that solely use the assets. However, where assets are used by more than one price control unit, the assets are initially allocated to the price control unit where the principal use occurs with a recharge being made to other price control units using the assets in proportion to the use of the assets.

There have been no significant changes in the methodology of allocating costs to price segments in the year. For further information on the allocations of costs and assets, see South East Water Limited's accounting methodology statement which is available on our website.

REVENUE RECOGNITION

The revenue recognition policy is the same in the regulatory accounts as in the statutory accounts. Additional charges added to a customer's account as a result of debt recovery activity, such as court costs or solicitors fees, are recognised as a credit within operating costs in both the statutory and regulatory accounts and as such do not affect turnover.

There have been no changes made to the procedure followed in calculating the measured income accrual in the year. A review was undertaken of the measured income accrual for the year 2019/20 and there were no significant differences between the accrual and the amounts billed in the year.

The following applies in relation to our policy on billing:

- if supply is not required, charges on an unoccupied or void property will normally be waived from the date we are informed. When informed of the vacation of a property, we may choose to turn off or disconnect the water supply at the stopcock. If we are requested not to turn off or disconnect the water supply either by the outgoing or incoming occupier they must undertake to pay all water charges arising until we are otherwise notified
- we do not send a bill to "the occupier" for premises where the name of the customer is not known. At the point that the occupier's details are known we will issue a bill as appropriate
- where we have donated to a charitable trust/assistance fund in relation to assisting customers with payment of water debt, any associated billing is included within water turnover
- when a new property is connected to our network, billing commences upon meter installation

When a property is identified as unoccupied on the billing system it will then proceed into our void property process to verify with as much certainty as possible whether the property is truly empty or not. As part of this process we will send out letters along with an application form to properties that are recorded as being empty for over 21 days. If there is no response a further letter is then sent. If there is still no response, we will review the account and take a range of additional steps including further written communication, meter reader visits to the property and enquiries to view the land registry to confirm the owner of the property whom we then contact.

CAPITALISATION

We determine employee costs directly attributable to capital projects based on the time spent on each project recorded on timesheets completed by employees. Other directly attributable costs are then assessed and any costs relating to capital projects are capitalised into individual projects. Training costs, administration and other general overhead costs are not capitalised. Over the past year our policies on the capitalisation of costs have not changed.

ACCOUNTING AND PERFORMANCE DISCLOSURES continued**BAD DEBT**

The bad debt policy is the same in the regulatory accounts as in the statutory accounts.

Debt is written off in only a limited number of scenarios when all collection avenues have been fully exhausted. Examples include where a debtor is not a current customer and all procedures to trace their whereabouts have been undertaken or where a customer is insolvent and we have been advised that no payment will be forthcoming.

An estimate for the provision for doubtful debts is calculated by our management based on the application of expected recovery rates to an aged debt profile. We have no significant concentration of credit risk with exposure spread over a large number of domestic customers and for our retail customers, we have secured adequate collateral under the Market Codes to mitigate any risk.

DIFFERENCES BETWEEN STATUTORY AND RAG DEFINITIONS

Material differences between the statutory financial statements and the RAG definitions are:

- in the income statement, the difference of £10.2 million in profit before tax includes capitalised interest of £2.7 million, the removal of depreciation on capitalised interest of £0.2 million and pension costs adjustments of £7.7 million
- in the statement of financial position, cumulative capitalised interest less depreciation of £22.8 million has been excluded from fixed assets

TAX STRATEGY AND CURRENT TAX RECONCILIATION

South East Water is committed to the effective, sustainable and active management of our tax affairs in support of our overall business performance and, as with all other aspects of our business, to maximise shareholder value and minimise customer bills as any tax payable is required to be funded via the prices set by Ofwat.

We are committed to pay tax according to the law and conducting our tax affairs according to clear principles. We seek to maintain good working relationships with tax authorities, sharing our views either directly or through trade associations.

South East Water believes it is important to state our views on tax in the context of corporate responsibility. We believe our obligation is to pay the amount of tax legally due and observe all applicable rules and regulations relating to tax compliance. However, at the same time we also have an obligation to maximise shareholder value, minimise customer bills and to manage financial and reputational risk. This includes controlling our overall liability to taxation.

We do not condone either personal or corporate tax evasion under any circumstances and were such issues to be identified, full disclosure of the activities undertaken would be required to be made to the tax authorities.

Our aim is to have a constructive relationship with the tax authorities on an on-going basis. Nevertheless we recognise that there may be some areas that are not free from doubt or differing legal interpretations may be possible. Where disputes arise with the tax authorities with regard to interpretation and application of tax law, we are committed to addressing the matter promptly and seek resolutions in a responsible manner. A more detailed explanation of our tax policy is available on our website.

For the year ended 31 March 2021 a UK corporation rate of 19 per cent has been used as enacted on 26 October 2015 by Finance Act 2013. The reduction in the UK corporation tax rate due to come into effect on 1 April 2020 bringing the rate to 17 per cent was cancelled in the budget announcement in March 2020 and the tax rate remains at 19 per cent from this date.

The deferred tax on temporary differences as at 31 March 2021 have been calculated in full under the balance sheet method at the rate applicable to the year in which the temporary differences are expected to reverse.

The table below shows a comparison between the amount funded within the final determination (FD) and the tax charge within the regulatory accounts.

ACCOUNTING AND PERFORMANCE DISCLOSURES continued

WHOLESALE TAX RECONCILIATION:

	2020/21 Prices £000
Final determination (2017/18 prices)	3,579
Indexation	250
Final determination	3,829
Actual in regulatory accounts	2,051
Retail tax	175
Wholesale tax	2,226

THE RECONCILIATION OF WHOLESALE TAXATION TO FUNDED TAXATION IS AS FOLLOWS:

	2020/21 Prices £000
Wholesale tax	2,226
Contributions and Infrastructure charges	609
Capital allowances	904
Variance in profit from operations	1,094
Corporation tax rate reduction	(462)
Other	(542)
Final determination	3,829

THE RECONCILIATION OF CURRENT APPOINTED TAX IS AS FOLLOWS:

	2020/21 Prices £000
Profit before tax	23,202
Taxation at 19%	4,408
Expenses not deductible	281
Income not chargeable to corporation tax	124
Capital allowances exceed depreciation	(95)
Pension movements	(2,667)
Current tax charge for the year	2,051
Adjustment in respect of prior years	(232)
UK corporation tax charge	1,819

TABLES AND RELATED DISCLOSURES

The following tables are set out following the order defined in Appendix 1 of the regulatory accounting guidance 3.12. Where the tables include line items which do not require a data entry, the line has been omitted from the table.

Additional tables have been included under each of the financial statements in section 1 to provide a reconciliation of the differences between applying RAGs and IFRS.

In line with allowances given in sections 2.2.4 and 2.2.6 of RAG 3.12, we have opted to not include tables 4L and 4Q to 8D within the annual performance report and these will instead be published separately within our supplementary tables report.

1A. Income statement

for the 12 months ended 31 March 2021

	Adjustments				
	Statutory £000	Differences between statutory and RAG definitions £000	Non-appointed £000	Total adjustments £000	Total appointed activities £000
Revenue	248,156	3,338	11,299	(7,961)	240,195
Operating costs	(182,068)	(6,808)	(6,970)	162	(181,906)
Other operating income	11,439	(12,161)	-	(12,161)	(722)
Operating profit	77,527	(15,631)	4,329	(19,960)	57,567
Other income	-	8,100	-	8,100	8,100
Interest income	3,092	(761)	-	(761)	2,331
Interest expense	(42,979)	(2,694)	(116)	(2,578)	(45,557)
Other interest expense	-	761	-	761	761
Profit before tax and fair value movements	37,640	(10,225)	4,213	(14,438)	23,202
Fair value gains/(losses) on financial instruments	-	-	-	-	-
Profit before tax	37,640	(10,225)	4,213	(14,438)	23,202
UK Corporation tax	(2,619)	-	(800)	800	(1,819)
Deferred tax	(3,720)	-	-	-	(3,720)
Profit for the year	31,301	(10,225)	3,413	(13,638)	17,663
Dividends	(147,013)	-	(3,413)	3,413	(143,600)

	Adjustments				
	Statutory £000	Differences between statutory and RAG definitions £000	Non-appointed £000	Total adjustments £000	Total appointed activities £000
Tax analysis					
Current year	2,851	-	800	(800)	2,051
Adjustments in respect of prior years	(232)	-	-	-	(232)
UK Corporation tax	2,619	-	800	(800)	1,819

1A. Income statement continued
for the 12 months ended 31 March 2021

	Non-appointed £000
Analysis of non-appointed revenue	
Imported sludge	-
Tankerred waste	-
Other non-appointed revenue	11,299
Revenue	11,299

Differences between statutory and RAG definitions	Revenue £000	Operating costs £000	Other operating income £000	Other income £000
Reclassification of grants and contributions income	(7,604)	-	-	7,604
Reclassification of other operating income	10,942	-	(11,438)	496
Removal of capitalised interest	-	215	-	-
Reclassification of profit/(loss) on disposal of fixed assets	-	723	(723)	-
Adjustment to pension contributions	-	(7,746)	-	-
Reclassification of return made of pensions	-	-	-	-
Total differences	3,338	(6,808)	(12,161)	8,100

Differences between statutory and RAG definitions	Interest income £000	Interest expense £000	Other interest expense £000	Profit for the year £000
Reclassification of grants and contributions income	-	-	-	-
Reclassification of other operating income	-	-	-	-
Removal of capitalised interest	-	(2,694)	-	(2,479)
Reclassification of profit/(loss) on disposal of fixed assets	-	-	-	-
Adjustment to pension contributions	-	-	-	(7,746)
Reclassification of return made of pensions	(761)	-	761	-
Total differences	(761)	(2,694)	761	(10,225)

1A. Income statement continued

for the 12 months ended 31 March 2021

Appointed interest expense of £45.557 million, as reported within the income statement above, is comprised of the following:

	Interest expense £000
Debenture interest	30
Interest payable to subsidiary	16,693
Indexation payable to subsidiary	4,600
Bank interest and other finance charges	8,350
Financing guarantee fees	949
Interest payable on index linked loans	9,830
Indexation on index linked loans	4,477
Lease interest	128
Amortisation of loan issue costs	616
Interest and related fees payable	45,673
Interest capitalised	(2,694)
Interest expense per IFRS	42,979
Reversal of interest capitalisation	2,694
Removal of non-appointed interest expense	(116)
Appointed interest expense	45,557

1B. Statement of comprehensive income

for the 12 months ended 31 March 2021

	Adjustments				
	Statutory £000	Differences between statutory and RAG definitions £000	Non-appointed £000	Total adjustments £000	Total appointed activities £000
Profit for the year	31,301	(10,225)	3,413	(13,638)	17,663
Actuarial gains/(losses) on post-employment plans	(12,123)	-	-	-	(12,123)
Other comprehensive income	-	-	-	-	-
Total comprehensive income for the year	19,178	(10,225)	3,413	(13,638)	5,540

1C. Statement of financial position

for the 12 months ended 31 March 2021

	Adjustments				
	Statutory £000	Differences between statutory and RAG definitions £000	Non-appointed £000	Total adjustments £000	Total appointed activities £000
Non-current assets					
Fixed assets	1,643,264	(14,009)	-	(14,009)	1,629,255
Intangible assets	8,787	(8,787)	-	(8,787)	-
Investments – loans to group companies	-	-	-	-	-
Investments – other	-	-	-	-	-
Financial instruments	-	-	-	-	-
Retirement benefit assets	34,368	-	-	-	34,368
Total non-current assets	1,686,419	(22,796)	-	(22,796)	1,663,623
Current assets					
Inventories	673	-	-	-	673
Trade & other receivables	86,360	-	1,936	(1,936)	84,424
Financial instruments	-	-	-	-	-
Cash & cash equivalents	41,441	-	-	-	41,441
Total current assets	128,474	-	1,936	(1,936)	126,538
Current liabilities					
Trade & other payables	(73,670)	-	(1,936)	1,936	(71,734)
Capex creditor	(16,235)	-	-	-	(16,235)
Borrowings	(80,318)	-	-	-	(80,318)
Financial instruments	-	-	-	-	-
Current tax liabilities	-	-	-	-	-
Provisions	(13,319)	-	-	-	(13,319)
Total current liabilities	(183,542)	-	(1,936)	1,936	(181,606)
Net current assets/(liabilities)	(55,068)	-	-	-	(55,068)
Non-current liabilities					
Trade & other payables	(4,623)	-	-	-	(4,623)
Borrowings	(1,038,371)	-	-	-	(1,038,371)
Financial instruments	-	-	-	-	-
Retirement benefit obligations	(3,172)	-	-	-	(3,172)
Provisions	-	-	-	-	-
Deferred income – G&C's	(3,625)	-	-	-	(3,625)
Deferred income – adopted assets	-	-	-	-	-
Preference share capital	-	-	-	-	-
Deferred tax	(167,228)	-	-	-	(167,228)
Total non-current liabilities	(1,217,019)	-	-	-	(1,217,019)
Net assets	414,332	(22,796)	-	(22,796)	391,536
Equity					
Called up share capital	(49,312)	-	-	-	(49,312)
Retained earnings & other reserves	(365,020)	22,796	-	22,796	(342,224)
Total equity	(414,332)	22,796	-	22,796	(391,536)

1C. Statement of financial position continued
for the 12 months ended 31 March 2021

Differences between statutory and RAG definitions	Fixed assets £000	Intangible assets £000	Net assets £000	Retained earnings & other resources £000	Total equity £000
Removal of capitalised interest	(23,816)	-	(23,816)	23,816	23,816
Removal of depreciation on capitalised interest	1,020	-	1,020	(1,020)	(1,020)
Reclassification of computer software cost	27,679	(27,679)	-	-	-
Reclassification of computer software depreciation	(20,149)	20,149	-	-	-
Reclassification of computer software work in progress cost	1,257	(1,257)	-	-	-
Total differences	(14,009)	(8,787)	(22,796)	22,796	22,796

Under IFRS, computer software is recorded as an intangible asset in the company's financial report and accounts. However, the annual performance report requires that computer software is reported as part of tangible fixed assets, hence the balance of intangible assets of £8.787 million in the statutory accounts has been restated under tangible fixed assets in the above table.

1D. Statement of cash flows

for the 12 months ended 31 March 2021

	Adjustments				
	Statutory £000	Differences between statutory and RAG definitions £000	Non-appointed £000	Total adjustments £000	Total appointed activities £000
Operating profit	77,527	(15,631)	4,329	(19,960)	57,567
Other income	-	8,100	-	8,100	8,100
Depreciation	58,756	(215)	-	(215)	58,541
Amortisation – G&C's	-	-	-	-	-
Changes in working capital	(5,700)	851	-	851	(4,849)
Pension contributions	(12,605)	6,895	-	6,895	(5,710)
Movement in provisions	1,228	-	-	-	1,228
Profit on sale of fixed assets	723	-	-	-	723
Cash generated from operations	119,929	-	4,329	(4,329)	115,600
Net interest paid	(33,893)	-	(116)	116	(33,777)
Tax paid	(1,616)	-	(800)	800	(816)
Net cash generated from operating activities	84,420	-	3,413	(3,413)	81,007
Investing activities					
Capital expenditure	(94,845)	-	-	-	(94,845)
Grants & contributions	-	-	-	-	-
Disposal of fixed assets	215	-	-	-	215
Other	-	-	-	-	-
Net cash used in investing activities	(94,630)	-	-	-	(94,630)
Net cash generated before financing activities	(10,210)	-	3,413	(3,413)	(13,623)
Cash flows from financing activities					
Equity dividends paid	(147,013)	-	(3,413)	3,413	(143,600)
Net loans received	185,683	-	-	-	185,683
Cash inflow from equity financing	-	-	-	-	-
Net cash generated from financing activities	38,670	-	(3,413)	3,413	42,083
Increase/(decrease) in net cash	28,460	-	-	-	28,460

The value of net loans received in the period of £185.7 million includes additional borrowings of £50 million in the form of additional drawdowns on our committed loan facilities and the early repayment in December 2020 of an intercompany loan totalling £135.9 million from South East Water Limited's parent company, South East Water (Holdings) Limited, to South East Water Limited.

1D. Statement of cash flows continued
for the 12 months ended 31 March 2021

Differences between statutory and RAG definitions	Operating profit £000	Other income £000	Depreciation £000	Changes in working capital £000	Pension contribution £000	Increase/ (decrease) in net cash £000
Operating profit as per table 1A	(15,631)	-	-	-	-	(15,631)
Reclassification of rental income	-	496	-	-	-	496
Reclassification of grants and contributions income	-	7,604	-	-	-	7,604
Removal of depreciation on capitalised interest	-	-	(215)	-	-	(215)
Inclusion of pension asset	-	-	-	851	-	851
Inclusion of pension contributions	-	-	-	-	6,895	6,895
Total differences	(15,631)	8,100	(215)	851	6,895	-

1E. Net debt analysis

for the 12 months ended 31 March 2021

	Fixed rate £000	Floating rate £000	Index linked		Total £000
			RPI £000	CPI/CPIH £000	
Interest rate risk profile					
Borrowings (excluding preference shares)	345,899	200,000	579,462	-	1,125,361
Preference share capital					-
Total borrowings					1,125,361
Cash					(41,441)
Short term deposits					-
Net debt					1,083,920
Gearing					
Gearing (%)					78.43
Adjusted Gearing (%)					-
Interest					
Full year equivalent nominal interest cost	14,856	1,957	26,831	-	43,644
Full year equivalent cash interest payment	14,856	1,957	17,342	-	34,155
Indicative interest rates					
Indicative weighted average nominal interest rate (%)	4.30	0.98	4.63	-	3.88
Indicative weighted average cash interest rate (%)	4.30	0.98	2.99	-	3.04
Time to maturity					
Weighted average years to maturity	11	2	15	-	12

The total borrowings in the above table differs to the borrowings in table 1C as follows:

	£000
Short term borrowing per table 1C	80,318
Long term borrowing per table 1C	1,038,371
Total borrowings per table 1C	1,118,689
Removal of unamortised loan arrangement costs	6,672
Borrowing per table 1E above	1,125,361

1F. Financial flows

for the 12 months ended 31 March 2021 (2017/18 financial year average CPIH)

	Notional returns and notional regulatory equity %	Actual returns and notional regulatory equity %	Actual returns and actual regulatory equity %
Return on regulatory equity			
Return on regulatory equity	3.86	2.21	3.86
Regulatory equity (£000)	526,059	526,059	301,421
Financing			
Gearing	-	1.65	1.08
Gearing benefits sharing	-	(0.40)	(0.70)
Variance in corporation tax	-	0.41	0.71
Group relief	-	-	-
Cost of debt	-	(1.49)	(3.35)
Hedging instruments	-	-	-
Return on regulatory equity including financing adjustments	3.86	2.37	1.60
Operational performance			
Totex out/(under) performance	-	(1.36)	(2.37)
ODI out/(under) performance	-	(1.11)	(1.93)
C-MeX out/(under) performance	-	-	-
D-MeX out/(under) performance	-	-	-
Retail out/(under) performance	-	(0.39)	(0.69)
Other exceptional items	-	0.01	0.01
Operational performance total	-	(2.85)	(4.98)
RoRE	3.86	(0.48)	(3.38)
Actual performance adjustment 2015 to 2020	0.41	0.41	0.71
Total earnings	4.27	(0.07)	(2.67)
RCV growth from inflation	1.01	1.01	1.01
Voluntary sharing arrangements	-	-	-
Total shareholder return	5.28	0.94	(1.66)
Dividends			
Gross dividend	4.00	26.07	45.51
Interest received on intercompany loans	-	(0.40)	(0.70)
Retained value	1.28	(24.74)	(46.47)

1F. Financial flows continued

for the 12 months ended 31 March 2021 (2017/18 financial year average CPIH)

	Notional returns and notional regulatory equity £000	Actual returns and notional regulatory equity £000	Actual returns and actual regulatory equity £000
Return on regulatory equity			
Return on regulatory equity	20,306	11,635	11,635
Regulatory equity (£000)			
Financing			
Gearing	-	3,266	3,266
Gearing benefits sharing	-	(2,119)	(2,119)
Variance in corporation tax	-	2,139	2,139
Group relief	-	-	-
Cost of debt	-	(7,850)	(10,099)
Hedging instruments	-	-	-
Return on regulatory equity including financing adjustments	20,306	7,071	4,822
Operational performance			
Totex out/(under) performance	-	(7,153)	(7,153)
ODI out/(under) performance	-	(5,818)	(5,818)
C-MeX out/(under) performance	-	-	-
D-MeX out/(under) performance	-	-	-
Retail out/(under) performance	-	(2,073)	(2,073)
Other exceptional items	-	31	31
Operational performance total	-	(15,013)	(15,013)
RoRE	20,306	(7,942)	(10,191)
Actual performance adjustment 2015 to 2020	2,152	2,152	2,152
Total earnings	22,458	(5,790)	(8,039)
RCV growth from inflation	5,313	5,313	3,044
Voluntary sharing arrangements	-	-	-
Total shareholder return	27,771	(477)	(4,995)
Dividends			
Gross dividend	21,042	137,162	137,162
Interest received on intercompany loans	-	(2,102)	(2,102)
Retained value	6,729	(135,537)	(140,055)

For PR19, the notional return on regulatory equity and regulatory equity specific to the company for the 2020/21 period prescribed by Ofwat are 3.86 per cent and £526.059 million respectively. These values, and the equivalents for each regulated company, are published by Ofwat on their website each year within the appropriate regulatory capital values and financial flows data source files.

Financing impacts

The impact of the company's actual gearing structure compared to the notional gearing ratio set by Ofwat of 60.0 per cent is illustrated within the gearing line. The actual average gearing ratio for the company, calculated as the company's average net debt of £1,068.776 million as a percentage of its average regulatory capital value of £1,384.345 million, equates to 77.20 per cent. The variance between the notional and actual gearing ratios of 17.20 per cent, together with the difference between the allowed return on regulatory equity of 3.86 per cent, which Ofwat have confirmed to be the correct value to use in response to the query listed in the Ofwat log (#203) for queries companies have submitted regarding the APR21 tables and the

1F. Financial flows continued

for the 12 months ended 31 March 2021 (2017/18 financial year average CPIH)

RAG guidance shown below, and the company's allowed cost of debt of 2.42 per cent results in a saving in financing on the average regulatory capital value of £3.266 million in 2017/18 prices being 1.08 per cent of actual regulatory equity.

Table reference	Line reference	Query raised	Query date £000	Log number	Ofwat response
1F	1F.3	In the gearing calculation, part of the line description reads: b) the difference between the adjusted allowed return on regulatory equity – base and the allowed cost of debt (CPIH adjusted) as set in the final determination. For the adjusted allowed return on regulated equity, is this calculated as row 1F.1 (Return on regulatory equity) less row 1F.18 (Actual performance adjustment 2015 to 2020) or should we just be using row 1F.1 (Return on regulatory equity) as the performance adjustment is now included further down in the table?	09 June 2021	203	The correct row to use is 1F.1.

The gearing benefits sharing line is calculated in accordance with the methodology set out in figure 9.1 of the PR19 Final Determinations: Aligning Risk and Return Technical Appendix. In line with this methodology, as the company's actual gearing ratio based on the company's net debt as at the 31 March 2021 of 78.43 per cent exceeds the 74.00 per cent trigger point, benefits are to be shared with customers at a rate of 50.00 per cent. The resulting value to be shared with customers, reducing the return to shareholders, is £2.119 million in 2017/18 prices equating to 0.70 per cent of actual regulatory equity. However, given the recent CMA PR19 FD decision to disapply the gearing penalty, and our disagreement with the gearing penalty in principle, we believe that this mechanism should be disapplying going forward.

The variance in corporation tax depicts the benefit received from a lower appointed corporation tax charge for the year, as reported in the regulatory accounts, compared to the tax allowance included in the company's final determination. The tax allowance for the 2020/21 period included in the final determination was £3.876 million in 2017/18 prices, compared with a corporation tax charge in outturn prices of £1.819 million, as reported within table 1A, or £1.737 million in 2017/18 prices results in a benefit of £2.139 million being 0.71 per cent of the company's actual regulatory equity.

The cost of debt line illustrates the difference between the company's actual cost of debt and the allowed cost of debt included in the final determination based on both the notional gearing and the company's actual gearing structure. The company's actual average interest rate for the year, calculated as the net interest charge per the reconciliation table below as a percentage of the company's average net debt is 4.21 per cent. This rate is adjusted for both the actual movement in CPIH for the period and the company's allowed cost of debt as determined at the final determination, being 0.80 per cent and 2.42 per cent respectively, resulting in a higher than allowed interest rate of 0.99 per cent equating to a cost of debt value, unadjusted for hedging instruments, of £7.850 million and £10.099 million based upon the notional gearing and the company's actual gearing structure respectively.

Reconciliation of net interest £000	
Total interest paid (per note 8 to the financial statements)	42,979
Removal of impact of capitalised interest	2,694
Amortisation of loan issue costs	(616)
Interest margin charged on intercompany bonds/loans	(23)
Total interest paid relevant to table 1F	45,034
Interest received on cash balances/bank interest	(58)
Total net interest charge relevant to table 1F	44,976

1F. Financial flows

for the price review to date (2017/18 financial year average CPIH)

In December 2020 the company issued a special restructuring dividend of £136 million to its parent company, South East Water (Holdings) Limited. These funds were used by the parent company in order to repay its intercompany loan to the company on the same day resulting in a net nil cash impact.

Operational impacts

Totex out/(underperformance) represents the difference between the actual totex performance versus the amount allowed in the published Final Determination. It is adjusted for the following:

- timing differences
- company sharing ratio with customers

The RAG guidelines indicate that this data should be the same as the data in line 4C.21, converted into a 2017/18 price base.

Table 4C.21 includes £0.83 million which relates to innovation expenditure which is classified as actual totex not subject to costs sharing. This then (incorrectly) drives a negative impact on RORE. The innovation fund expenditure should only impact RORE when the innovation expenditure included in totex is different to the revenue allowed for innovation. When the cost and revenue allowance are equal there should be no impact on RORE. We raised this with Ofwat via the APR query process and have agreed to an adjustment to line 4C.21 for the purposes of the RORE calculation. The adjustment from line 4C.21 is shown below:

	%	£m
Table 4C.21 total company share of totex over/under spend – 2020/21 prices		(8.316)
CPI(H): Fin year average – inflate from base year 2017/18 average	104.69	
Table 4C.21 total company share of totex over/under spend – 2017/18 prices		(7.943)
Correction for innovation totex 2017/18 prices.		0.790
Net totex out/(under) performance 2017/18 prices		(7.153)

The main driver of the totex underperformance can be attributed to a water network totex overspend of (c£14 million) which arises as a result of a shortfall in developer contributions. As part of our final determination an additional £31 million (2017/18 prices) developer contributions was allowed to fund enhancement development expenditure of c£42 million (2017/18 prices). (See page 60 of our South East Water specific FD report). This was to be funded through increasing infrastructure charges and an increasing income offset. We discussed this approach to funding new development with Ofwat at an early stage following the final determination. We identified that we were constrained both by the rules for setting infrastructure charges and practical developer considerations. We identified that the assumptions in the FD would result in us reporting a significant shortfall in collection of developer contributions, particularly in the early years. This conversation took place before the impact of Covid-19 which has further impacted our developer activity and contributions.

Further commentary on the cost variances can be found within the commentary for table 4C.

The ODI out/(under) performance is as reported in APR table 3A. There are no adjustments to this figure.

Any reward/(penalty) from the C-MeX and D-MeX mechanisms is reported one year in arrears once all of the companies data is known. The value for 2020/21 is therefore zero for both items.

1F. Financial flows

for 12 months ended 31 March 2021 (2017/18 financial year average CPIH)

Retail out/(under) performance is calculated as follows:

		%	£m
FD cost to serve all Residential retail customers – real	£m 2017/18 prices		16.278
Actual retail costs (APR Table 2C)	£m nominal		18.352
Depreciation on assets since 2015 and recharges	£m nominal		0.860
Total retail costs excluding third party and pension deficit repair costs – nominal	£m nominal		19.212
CPI(H): Fin year average – inflate from base year 2017/18 average	%	104.69	
Actual Retail costs	£m 2017/18 prices		17.529
Depreciation on assets since 2015 and Recharges	£m 2017/18 prices		0.821
Total retail costs excluding third party and pension deficit repair costs – 2017/18 prices	£m 2017/18 prices		18.351
Cash retail costs outperformance/(underperformance) – 2017/18 prices	£m 2017/18 prices		(0.821)
Depreciation on assets since 2015 and Recharges	£m 2017/18 prices		(1.785)
Retail costs outperformance/(underperformance) – 2017/18 prices	£m 2017/18 prices		(2.073)

There are two main drivers of the retail cost underperformance. The first is an increase in bad debt as a result of Covid-19. The second is as a result of a difference in depreciation. It is not clear exactly what level of depreciation was funded for retail however our Business Plan allowed £0.1 million for depreciation but the actual reported was £0.86 million (2020/21 prices).

The 'other exceptional items' reported relates to a land sale in the period. Net cash proceeds of £0.06 million were received in the year. After applying the 50 per cent share with customers this results in a contribution to RORE of £0.03 million.

1F. Financial flows continued

for the price review to date (2017/18 financial year average CPIH)

	Notional returns and notional regulatory equity %	Actual returns and notional regulatory equity %	Actual returns and actual regulatory equity %
Return on regulatory equity			
Return on regulatory equity	3.86	2.21	3.86
Regulatory equity (£000)	526,059	526,059	301,421
Financing			
Gearing	-	1.65	1.08
Gearing benefits sharing	-	(0.40)	(0.70)
Variance in corporation tax	-	0.41	0.71
Group relief	-	-	-
Cost of debt	-	(1.49)	(3.35)
Hedging instruments	-	-	-
Return on regulatory equity including financing adjustments	3.86	2.37	1.60
Operational performance			
Totex out/(under) performance	-	(1.36)	(2.37)
ODI out/(under) performance	-	(1.11)	(1.93)
C-MeX out/(under) performance	-	-	-
D-MeX out/(under) performance	-	-	-
Retail out/(under) performance	-	(0.39)	(0.69)
Other exceptional items	-	0.01	0.01
Operational performance total	-	(2.85)	(4.98)
RoRE	3.86	(0.48)	(3.38)
Actual performance adjustment 2015 to 2020	0.41	0.41	0.71
Total earnings	4.27	(0.07)	(2.67)
RCV growth from inflation	1.01	1.01	1.01
Voluntary sharing arrangements	-	-	-
Total shareholder return	5.28	0.94	(1.66)
Dividends			
Gross dividend	4.00	26.07	45.51
Interest received on intercompany loans	-	(0.40)	(0.70)
Retained value	1.28	(24.74)	(46.47)

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1F. Financial Flows continued

for the price review to date (2017/18 financial year average CPIH)

	Notional returns and notional regulatory equity £000	Actual returns and notional regulatory equity £000	Actual returns and actual regulatory equity £000
Return on regulatory equity			
Return on regulatory equity	20,306	11,635	11,635
Regulatory equity (£000)			
Financing			
Gearing	-	3,266	3,266
Gearing benefits sharing	-	(2,119)	(2,119)
Variance in corporation tax	-	2,139	2,139
Group relief	-	-	-
Cost of debt	-	(7,850)	(10,099)
Hedging instruments	-	-	-
Return on regulatory equity including financing adjustments	20,306	7,071	4,822
Operational performance			
Totex out/(under) performance	-	(7,153)	(7,153)
ODI out/(under) performance	-	(5,818)	(5,818)
C-MeX out/(under) performance	-	-	-
D-MeX out/(under) performance	-	-	-
Retail out/(under) performance	-	(2,073)	(2,073)
Other exceptional items	-	31	31
Operational performance total	-	(15,013)	(15,013)
RoRE	20,306	(7,942)	(10,191)
Actual performance adjustment 2015 to 2020	2,152	2,152	2,152
Total earnings	22,458	(5,790)	(8,039)
RCV growth from inflation	5,313	5,313	3,044
Voluntary sharing arrangements	-	-	-
Total shareholder return	27,771	(477)	(4,995)
Dividends			
Gross dividend	21,042	137,162	137,162
Interest received on intercompany loans	-	(2,102)	(2,102)
Retained value	6,729	(135,537)	(140,055)

As the 2020/21 financial year is the first within the AMP7 period, the above figures are an exact replica of those given in the financial flows analysis for the 12 months to 31 March 2021. As such, further details of the results shown within this table are given in the narrative attributed to the financial flows table relating to the 2020/21 financial period above.

2A. Segmental income statement

for the 12 months ended 31 March 2021

	Retail household £000	Retail non- household £000	Water Resources £000	Water Network+ £000	Total £000
Revenue – price control	17,453	(22)	20,876	201,177	239,484
Revenue – non-price control	-	-	9	702	711
Operating expenditure					
– excluding PU recharge impact	(18,139)	(213)			(18,352)
PU opex recharge	301	-			301
Operating expenditure – including PU recharge impact	(17,838)	(213)	(14,890)	(90,123)	(123,064)
Depreciation – tangible fixed assets	(1,161)	-	(6,165)	(51,215)	(58,541)
Amortisation – intangible fixed assets	-	-	-	-	-
PU recharge impact	-	-	(807)	506	(301)
Depreciation & amortisation – including PU recharge impact	(1,161)	-	(6,972)	(50,709)	(58,842)
Other operating income	22	-	(60)	(684)	(722)
Operating profit	(1,254)	(235)	(1,037)	60,363	57,567
Surface water drainage rebates					-

At the point at which we exited the non-household retail market on 1 May 2018, transferring our non-household retail business to Invicta Water Limited, one of our group companies which was then later sold by the group to Castle Water Ltd, all customer accounts were invoiced up to the 30 April 2018. In instances where no meter read was available to bill up to the point of exit, the meter readings were estimated based on the customer's average consumption.

During the year, further corrective meter readings on a number of non-household customer's bills were adjusted in order to reimburse the over-estimation of bills at the point at which we exited the non-household retail market. These reimbursements have led to negative revenue of £0.022 million in the year as reported in the table above, in respect of the non-household retail business.

2B. Totex analysis – wholesale

for the 12 months ended 31 March 2021

	Water Resources £000	Water Network+ £000	Total £000
Base operating expenditure			
Power	4,998	14,644	19,642
Income treated as negative expenditure	(16)	(43)	(59)
Abstraction charges/discharge consents	2,934	172	3,106
Bulk supply/bulk discharge	1,042	5,087	6,129
Renewals expensed in year (infrastructure)	-	-	-
Renewals expensed in year (non-infrastructure)	-	-	-
Other operating expenditure	4,980	51,333	56,313
Local authority and Cumulo rates	952	17,108	18,060
Total base operating expenditure	14,890	88,301	103,191
Other operating expenditure			
Enhancement operating expenditure	-	1,419	1,419
Developer services operating expenditure	-	-	-
Total operating expenditure excluding third party services	14,890	89,720	104,610
Third party services	-	403	403
Total operating expenditure	14,890	90,123	105,013
Grants and contributions			
Grants and contributions – operating expenditure	-	-	-
Capital expenditure			
Base capital expenditure	988	56,785	57,773
Enhancement capital expenditure	5,580	9,947	15,527
Developer services capital expenditure	-	16,793	16,793
Total gross capital expenditure (excluding third party)	6,568	83,525	90,093
Third party services	-	-	-
Total gross capital expenditure	6,568	83,525	90,093
Grants and contributions			
Grants and contributions – capital expenditure	-	(6,886)	(6,886)
Net totex	21,458	166,762	188,220
Cash expenditure			
Pension deficit recovery payments	691	4,177	4,868
Other cash items	-	-	-
Totex including cash items	22,149	170,939	193,088

2C. Cost analysis – retail

for the 12 months ended 31 March 2021

	Household £000	Non-household £000	Total £000
Operating expenditure			
Customer services	6,818	-	6,818
Debt management	743	-	743
Doubtful debts	3,512	-	3,512
Meter reading	886	-	886
Service to developers		213	213
Other operating expenditure	5,918	-	5,918
Local authority and cumulo rates	262	-	262
Total operating expenditure excluding third party services	18,139	213	18,352
Depreciation			
Depreciation on tangible fixed assets existing at 31 March 2015	51	-	51
Depreciation on tangible fixed assets acquired after 1 April 2015	1,110	-	1,110
Amortisation on intangible fixed assets existing at 31 March 2015	-	-	-
Amortisation on intangible fixed assets acquired after 1 April 2015	-	-	-
Recharges			
Recharge from wholesale for legacy assets principally used by wholesale (assets existing at 31 March 2015)	5	-	5
Income from wholesale for legacy assets principally used by retail (assets existing at 31 March 2015)	(4)	-	(4)
Recharge from wholesale assets acquired after 1 April 2015 principally used by wholesale	8	-	8
Income from wholesale assets acquired after 1 April 2015 principally used by retail	(310)	-	(310)
Net recharge costs	(301)	-	(301)
Total retail costs excluding third party and pension deficit repair costs	18,999	213	19,212
Third party services operating expenditure	-	-	-
Pension deficit repair costs	-	-	-
Total retail costs including third party and pension deficit repair costs	18,999	213	19,212
Debt written off	737	-	737
Capital expenditure	469	-	469

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2C. Cost analysis – retail continued

for the 12 months ended 31 March 2021

Other operating expenditure includes the net retail expenditure for the following household retail activities which are part funded by wholesale	Retail household £000
Demand-side water efficiency – gross expenditure	705
Demand-side water efficiency – expenditure funded by wholesale	668
Demand-side water efficiency – net retail expenditure	37
Customer-side leak repairs – gross expenditure	2,106
Customer-side leak repairs – expenditure funded by wholesale	1,837
Customer-side leak repairs – net retail expenditure	269

HOUSEHOLD

Overall expenditure for household retail is above final determination (FD) expectations, with total operating costs (excluding third party services) at £18.1 million versus an FD of £17 million. Household retail cost has decreased from the previous period which was £18.6 million. This is primarily a consequence of the doubtful debt charge decreasing by £0.9 million from £4.4 million to £3.5 million with additional Covid-19 provisions included in the accounts largely linked to risk around debt over 12 months. A reduction in other operating expenditure of £0.7 million offset increases in customer service costs.

NON-HOUSEHOLD

Overall expenditure for non-household retail is £0.2 million which relates to service to developer costs.

2D. Historic cost analysis of tangible fixed assets

	Retail household £000	Retail non-household £000	Water resources £000	Water network+ £000	Total £000
Cost					
At 1 April 2020	7,264	1,663	131,811	1,740,724	1,881,462
Disposals	(311)	-	(153)	(2,959)	(3,423)
Additions	469	-	6,568	83,525	90,562
Adjustments	9,997	(1,663)	29,042	(37,376)	-
Assets adopted at nil cost	-	-	-	-	-
At 31 March 2021	17,419	-	167,268	1,783,914	1,968,601
Depreciation					
At 1 April 2020	(142)	(57)	(41,850)	(241,319)	(283,368)
Disposals	311	-	89	2,163	2,563
Adjustments	(7,947)	57	14,158	(6,268)	-
Charge for year	(1,161)	-	(6,165)	(51,215)	(58,541)
At 31 March 2021	(8,939)	-	(33,768)	(296,639)	(339,346)
Net book amount at 31 March 2021	8,480	-	133,500	1,487,275	1,629,255
Net book amount at 1 April 2020	7,122	1,606	89,961	1,499,405	1,598,094
Depreciation charge for year					
Principal services	(1,161)	-	(6,165)	(51,215)	(58,541)
Third party services	-	-	-	-	-
Total	(1,161)	-	(6,165)	(51,215)	(58,541)

The net book value includes £79.8 million in respect of assets in the course of construction.

With the introduction of water resources as a separate price control in 2020/21, and in keeping with the regulatory requirement to report the allocation of the company's asset base based on the asset's principal use, as defined in the RAGs, we have seen a shift in the allocation of wholesale assets in table 2D. We have also taken this opportunity during the financial year to complete a comprehensive review of our fixed assets accounting system to identify any potential historic miss-allocation between the aforementioned price controls and business units.

The re-allocation as a result of this change has been shown within the adjustments lines on both cost and depreciation within the above table, further details relating to this change can be found within our accounting methodology statement.

2E. Analysis of 'grants and contributions' – water resources and water network+

for the 12 months ended 31 March 2021

	Fully recognised in income statement £000	Capitalised and amortised (in income statement) £000	Fully netted off capex £000	Total £000
Grants and contributions – water resources				
Diversions – s185	-	-	-	-
Other contributions (price control)	-	-	-	-
Price control grants and contributions	-	-	-	-
Diversions – NRSWA	-	-	-	-
Diversions – other non-price control	-	-	-	-
Other contributions (non-price control)	-	-	-	-
Total	-	-	-	-
Value of adopted assets	-	-	-	-
Grants and contributions – water network+				
Connection charges	3,932	-	-	3,932
Infrastructure charge receipts	3,406	-	-	3,406
Requisitioned mains	-	864	-	864
Diversions – s185	-	236	-	236
Other contributions (price control)	-	34	-	34
Price control grants and contributions before deduction of income offset	7,338	1,134	-	8,472
Income offset	(1,586)	-	-	(1,586)
Price control grants and contributions after deduction of income offset	5,752	1,134	-	6,886
Diversions – NRSWA	-	-	-	-
Diversions – other non-price control	-	-	-	-
Other contributions (non-price control)	-	-	-	-
Total	5,752	1,134	-	6,886
Value of adopted assets	2,631	-	-	2,631

The asset payment for adopted assets cover the cost of making an asset payment to self-lay providers for the provision of a new main adopted by the company.

Movements in capitalised grants and contributions	Water resources £000	Water network+ £000	Total £000
Balance sheet			
Brought forward	-	4,901	4,901
Capitalised in the year	-	1,134	1,134
Amortisation (in income statement)	-	(1,205)	(1,205)
Carried forward	-	4,830	4,830

2F. Residential retail

	Revenue £000	Number of customers 000s	Average residential revenues £
Residential revenue			
Wholesale charges	186,432		
Retail revenue	17,453		
Total residential revenue	203,885		
Retail revenue			
Revenue recovered ("RR")	17,453		
Revenue sacrifice	-		
Actual revenue (net)	17,453		
Customer information			
Actual customers ("AC")		880.649	
Reforecast customers		875.073	
Adjustment			
Allowed revenue ("R")	19,189		
Net adjustment	1,736		
Other residential information			
Average residential retail revenue per customer			19.818

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21. Revenue analysis

for the 12 months ended 31 March 2021

	Household £000	Non- household £000	Total £000	Water resources £000	Water network+ £000	Total £000
Wholesale charge – water						
Unmeasured	17,284	907	18,191	1,713	16,478	18,191
Measured	168,815	34,714	203,529	19,163	184,366	203,529
Third party revenue	333	-	333	-	333	333
Total wholesale water revenue	186,432	35,621	222,053	20,876	201,177	222,053
Wholesale total	186,432	35,621	222,053			
Retail revenue						
Unmeasured	1,793	-	1,793			
Measured	15,660	(22)	15,638			
Other third party revenue	-	-	-			
Retail total	17,453	(22)	17,431			
Third party revenue – non-price control						
Bulk supplies – water			-			
Other third party revenue			98			
Principal services – non-price control						
Other appointed revenue			613			
Total appointee revenue			240,195			

The wholesale revenue for 2020/21 is higher than allowed revenue in the Final Determination (FD) and is due to higher consumption as a result of the Covid-19 restrictions. These restrictions resulted in lower commuting to outside of South East Water's catchment area and higher consumption throughout the year. In addition, increased garden usage coupled with the warmer weather during summer of 2020/21 pushed demand to unprecedented levels.

The impact of Covid-19 in the year also saw a swing of around 25 per cent of water revenue from non-household usage to household usage as a result of the various social distance restrictions during 2020/21.

The table below reconciles the allowed and actual wholesale revenues.

	£000
Allowed wholesale revenue for the year	213,489
Increase due to higher consumption	8,564
Movement due to mix of properties	-
Actual revenue for the year	222,053

2I. Revenue analysis continued

for the 12 months ended 31 March 2021

As a company with a high level of metering, our revenue is very dependent on the consumption forecast used for each year. Each year consumption is forecast based on a 'normal' water resources demand profile. Should weather and/or rainfall not follow this 'normal' profile then this will impact our measured revenue accordingly. Any variation in wholesale revenue is adjusted for using the wholesale revenue forecasting incentive mechanism as prescribed by Ofwat.

2J. Infrastructure network reinforcement costs

for the 12 months ended 31 March 2021

	Network reinforcement capex £000	On site / site specific capex (memo only) £000
Wholesale water network+ (treated water distribution)		
Distribution and trunk mains	4,565	11,223
Pumping and storage facilities	8	-
Other	-	1,008
Total	4,573	12,231

2K. Infrastructure charges reconciliation

for the 12 months ended 31 March 2021

	Water £000
Impact of infrastructure charge discounts	
Infrastructure charges	3,406
Discounts applied to infrastructure charges	-
Gross infrastructure charges	3,406
Comparison of revenue and costs	
Variance brought forward	3,370
Revenue	3,406
Costs	(4,573)
Variance carried forward	2,203

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2K. Infrastructure charges reconciliation continued

for the 12 months ended 31 March 2021

Across the south east we have a high number of new developments and based on data from Government and local planning authorities this is expected to continue over the next 25 years. As a large proportion of our network is already distributing water at its maximum capacity, particularly during peak demands, we have to charge developers for offsite reinforcement work to ensure our existing customers and associated network are not negatively affected. When a developer applies for new connections we carry out detailed modelling to understand the effect on the existing network and identify areas that require reinforcement. All of our schemes are then planned and completed on a risk based approach to avoid impacting our existing customers but to deliver a quality supply to our new customers.

We receive the infrastructure charge from developers when they apply for new connections to our network, but due to a number of constraints the work required may not always be carried out in the same financial year. On many of our schemes we have to consider environmental impacts and plan in the mitigation to protect and enhance the local biodiversity and this can mean a number of species surveys which are only carried out at certain times of the year. Where environmental concerns arise the schemes often have to be delivered during times that least impact the local environment and this can be outside of the financial year in which the contribution was received. Another reason for the difference is highways approvals to deliver schemes, particularly along busy roads or where other utility works are already planned. A number of schemes have to be delivered during school holidays; particularly longer schemes which are only allowed in summer holidays; leaving a short window to deliver the schemes and often pushing them into the next financial year.

As our schemes are planned and completed using a risk based approach we know some of the lower risk schemes with a longer build programme can be moved in the programme to accommodate the higher risk schemes and therefore they may fall outside of the financial year in which the payment was received. There are also some schemes which were not yet completed in the 2020/21 financial year and therefore a proportion of the costs will be reported in future years.

Although there is approximately a £2.2 million difference between the revenue earned from the charges and the actual costs of delivering the work for the financial year, the work associated with the charges will be delivered in subsequent years to ensure our network continues to provide a reliable service to all of our customers. Also included in the variance is infrastructure charges owed for previous years. Any variance for in year infrastructure will be taken into account (deducted or added) when calculating the five year rolling average moving forward.

2L. Analysis of land sales

for the 12 months ended 31 March 2021

	Water resources £000	Water network+ £000	Total £000
Proceeds from disposals of protected land	64	-	64

Proceeds from disposals of protected land of £0.064 million relate in full to the sale of land at our Charing BH2 Pumping Station in Kent.

2M. Revenue reconciliation

for the 12 months ended 31 March 2021

	Water resources £000	Water network+ £000	Total £000
Revenue recognised			
Wholesale revenue governed by price control	20,876	201,177	222,053
Grants & contributions (price control)	-	6,886	6,886
Total revenue governed by wholesale price control	20,876	208,063	228,939
Calculation of the revenue cap			
Allowed wholesale revenue before adjustments (or modified by CMA)	20,049	193,440	213,489
Allowed grants & contributions before adjustments (or modified by CMA)	-	18,795	18,795
Revenue adjustments	-	-	-
Other adjustments	-	-	-
Revenue cap	20,049	212,235	232,284
Calculation of revenue imbalance			
Revenue cap	20,049	212,235	232,284
Revenue recovered	20,876	208,063	228,939
Revenue imbalance	(826)	4,173	3,347

2N. Residential retail – social tariffs

	Revenue £000	Number of customers 000s	Average amount per customer £
Number of residential customers on social tariff			
Residential water only social tariffs		31.521	
Number of residential customers not on social tariff			
Residential water only social tariffs		849.639	
Social tariff discount			
Average discount per water only social tariff customer			-
Social tariff cross-subsidy – residential customers			
Total customer funded cross-subsidies for water only social tariffs customers	3,439		
Average customer funded cross-subsidy per water only social tariffs customers			3.903
Social tariff cross-subsidy – company			
Total revenue forgone by company to fund cross-subsidies for water only social tariffs customers	-		
Average revenue forgone by company to fund cross-subsidy per water only social tariffs customer			-
Social tariff support – willingness to pay			
Level of support for social tariff customers reflected in business plan			5.76
Maximum contribution to social tariffs supported by customer engagement			5.76

In addition to tariffs such as Watersure which are set nationally we also provide a single Social Tariff for customers that are on low income. This provides customers who are on a low income of £16,105 per annum excluding disability and housing benefits with a discounted bill, to average bill levels, ensuring that customers can manage their money effectively and do not suffer bill shocks resulting through additional usage. This is particularly important in a highly metered environment.

20. Historic cost analysis of intangible fixed assets

This table has not been reproduced in this regulatory report as the company has no intangible assets to report on under the RAGs.

3A. Outcome performance – water performance commitments

The following table shows the performance against the company's 38 outcomes for 2020/21.

2020/21 PERFORMANCE

For commentary on our performance for the year please see our performance microsite



performance.southeastwater.co.uk

PERFORMANCE COMMITMENT MET

Where our in-year performance has met the target set by Ofwat 'yes' has been selected, if the target has not been met then 'no' has been entered.

2020/21 OUTPERFORMANCE PAYMENT OR UNDERPERFORMANCE PAYMENT

Where in-year performance is better than target the accrued amount has been added in to the adjacent column.

Where in-year performance is worse than target the accrued amount has been added in to the adjacent column.

2020/21 OUTPERFORMANCE PAYMENT OR UNDERPERFORMANCE PAYMENT continued

For Customers measure of experience (C-MeX) and Developer measures of experience (D-MeX), tables 3C and 3D, Ofwat will review the data for the whole industry and inform us what our underperformance/ outperformance payment will be. These adjustments will be applied to the 2023/24 tariffs.

Reputational performance commitments are shown in table 3E.

This financial year we have accrued £0.135 million underperformance penalty for our Compliance Risk Index (CRI) performance measure.

In 2020/21, we exceeded the underperformance collar for Interruptions to supply and therefore have accrued the maximum £3.088 million underperformance payment.

In 2020/21, we have outperformed our leakage reduction target of 0.2 per cent. Our performance was 1.1 per cent reduction from 95.1ML/d, 3 year average baseline figure equating to a reward of £0.303 million. This has been achieved by expanding the leakage team, increasing maintenance, using satellite technology to hunt for leaks and building on our innovative smart networks trial by installing more meters, sensors and loggers to monitor our pipeline network.

3A. Outcome performance – water performance commitments continued

We have incurred a £1.224 million underperformance payment for ending the year above our target Per Capita Consumption (PCC) 2019/20 baseline. Our commitment was to reduce PCC by 1.1 per cent, from 2019/20, 144.0 l/p/d 3 year average baseline figure. We ended the year with a 5.1 per cent increase in PCC, for further information on our performance in this measure please see



performance.southeastwater.co.uk

In 2020/21 we have accrued a £0.798 million underperformance payment for our Mains Repairs measure. We have exceed our 173.9 per 1,000km main target.

We outperformed our unplanned outage target for the year, this measure has an underperformance incentive only however we are pleased to have performed better than our target of 4.23 per cent.

In 2020/21 we outperformed and therefore have accrued an outperformance payment of £0.085 million for our Appearance of tap water contacts performance commitment.

We performed better than target in our Taste and Odour of Tap water performance commitment. This means we have accrued a £0.064 million outperformance payment.

We have incurred a £0.196 million underperformance payment for not meeting our Voids-Household properties performance commitment.

We have also incurred a £0.838 million underperformance payment for not meeting our Voids-Business properties performance commitment. We are proposing that this measure be treated the same as PCC as this has been impacted by Covid-19 restrictions. For more information on this please see



performance.southeastwater.co.uk

We outperformed our Company sites at risk of flooding target for the year, this measure has an underperformance incentive only in 2024/25 however we are pleased to have performed better than our target to remove zero sites in 2020/21 having removed four sites at risk of flooding in the year.

We received a £0.008 million outperformance payment due to performing better than our 0.5 target for properties at risk of low pressure.

We outperformed our Engaging and working with landowners and land managers to improve catchment resilience related to raw water quality deterioration target for the year, this measure has an outperformance and underperformance incentive in 2024/25 only however we are pleased to have performed better than target of 2,843 Hectares in 2020/21.

We outperformed our Protecting wildlife and increasing biodiversity target for the year, this measure has an outperformance and underperformance incentive in 2024/25 only however we are pleased to have performed better than target of 1,166 Hectares in 2020/21.

We outperformed our Water Industry National Environmental Programme target for the year, this measure has an underperformance incentive only however we are pleased to have performed better than our target to improve zero schemes in 2020/21 having completed improvements to nine of our schemes in the period.

We outperformed our Bespoke Abstraction Incentive Mechanism (AIM) target for the year, this measure has an underperformance incentive only however we are pleased to have performed better than our target to achieve an acceptable average level of abstraction of zero MI/d in 2020/21 having achieved an average under abstraction of 39MI/d in the year.

3A. Outcome performance – water performance commitments continued

We have met our Strategic main Wellwood to Potters Corner performance commitment for the year, this measure has an outperformance and underperformance incentive in 2024/25 only.

We are currently forecasting a £13.625 million underperformance payment for the total period of 2020/25. This excludes PCC underperformance payments as we are currently unable to provide a robust forecast for this measure due to lack of insight on how usage will change following restriction easing.

Table 3F – Leakage and PCC performance

The data provided for historical Leakage and PCC figures in table 3F differs from previously reported data. These new figures are based on the industry standard methodology for calculating these measures. We have used two figures to back cast our performance based on the difference between the old and new methodologies, for our leakage performance we have increased our previously reported numbers by 9.33 per cent. We have decreased our PCC historical performance by 4.3 per cent. Further detail on these calculations is contained within the additional reporting requirements document submitted to Ofwat.

For the reporting year 2020/21 the Water Balance gap was 4.1 per cent. This has increased from the 3.8 per cent observed in the 2019/20 reporting year. Although this is below the 5 per cent cap which allows the MLE to be applied, it is above the 3 per cent level, and incurs a red status on the RAG assessment. We believe that this is largely due to the use of a low (3 per cent) meter under registration value. During the assurance process this was highlighted as a “potential risk to the water balance gap.” This figure is low by industry standards, leading us to strongly suspect that it is an underestimate.

The value will be reviewed during the reporting year of 2021/22 and a statistically relevant assessment made to update the meter under registration to an appropriate value. This may be complex due to the number of meters fitted in South East Water’s region, and the common approach of removing meters for testing on a flow rig may not be feasible for a statistically relevant sample. To achieve an under registration value with 95 per cent confidence a sample size of 5 per cent or greater equalling 40,267 individual meters would need to be tested. It was not practical to carry this out during Covid-19 restrictions, but we hope that an updated value will be possible for 2021/22 reporting.

IMPACT OF COVID-19

During the reporting year, the company has experienced widespread disruption as a result of the Covid-19 pandemic, and particularly the restrictions that were put in place to control it. Because we serve an area which is home to many London commuters, the large increase in working from home has caused an increase in demand for water in our supply zone (we understand that here there has been a consequent large fall in demand in central London, which is part of Thames Water’s supply zone). This became particularly severe in combination with a hot summer in 2020, which also led to higher demand, and put historically unusual demands on our infrastructure.

We have also seen a significant impact on the number of vacant business properties as a result of lockdowns and restrictions on businesses operations. This was not anticipated when the targets for our non-household voids ODI was set.

Overall, a number of ODIs have been impacted as a result including PCC, mains repairs, supply interruptions; non-household voids; leakage; and pressure.

Of these, we have identified two ODIs which have been particularly severely impacted: PCC and Non-Household voids. The assumptions on which the targets were set and accepted have been completely altered by the realities of Covid-19. We are proposing to Ofwat that the implementation of underperformance penalties relating to these two ODIs is delayed until the next price review. It is hoped that by then the Covid-19 crisis can be reviewed in hindsight and Ofwat can take a fully informed view of whether these underperformance payments should be adjusted, or even applied at all.

3A. Outcome performance – water performance commitments (financial)

Performance level – actual								Forecast of total 2020 to 2025
Unique reference	Unit	Previous reporting year	Current reporting year	PCL met?	Outperformance or underperformance payment £m	outperformance or underperformance payment £m		
Common PCs – water (financial)								
Water quality compliance (CRI)	PR19SEW_A.1	number	3.22	2.26	No	(0.135)	(2.428)	
Water supply interruptions	PR19SEW_B.1	hh:mm:ss	00:10:00	00:31:27	No	(3.088)	(7.028)	
Leakage	PR19SEW_D.1	%	94.5	1.1	Yes	0.303	2.501	
Per capita consumption	PR19SEW_E.1	%	143.1	(5.1)	No	(1.224)	N/A	
Mains repairs	PR19SEW_B.2	number	155.1	185.3	No	(0.798)	(4.932)	
Unplanned outage	PR19SEW_B.3	%	4.00	3.09	Yes	-	(0.863)	
Bespoke PCs – water and retail (financial)								
Appearance of tap water	PR19SEW_A.2	nr	0.94	1.00	Yes	0.085	0.085	
Taste and odour of tap water	PR19SEW_A.3	nr	0.39	0.34	Yes	0.064	0.064	
Voids – household properties	PR19SEW_L.2	%	2.40	2.33	No	(0.196)	(0.196)	
Voids – business properties	PR19SEW_L.3	%	8.20	10.60	No	(0.838)	(0.838)	
Company sites protected from risk of flooding	PR19SEW_B.4	nr	N/A	4	Yes	-	-	
Low pressure	PR19SEW_B.6	nr	0.2	0.4	Yes	0.008	0.008	
Engaging and working with landowners and farm managers to improve catchment resilience related to raw water quality deterioration	PR19SEW_H.1	nr	N/A	2,858.0	Yes	-	-	
Protecting wildlife and increasing biodiversity	PR19SEW_H.2	nr	N/A	1,172.0	Yes	-	-	
Water industry national environment programme	PR19SEW_H.3	nr	N/A	9	Yes	-	-	
Bespoke abstraction incentive mechanism (AIM)	PR19SEW_H.5	nr	N/A	(39)	Yes	-	-	
Strategic main Wellwood to Potters Corner	PR19SEW_H.7	number	N/A	-	Yes	-	-	
Financial water performance commitments achieved		%			65			
Overall performance commitments achieved (excluding C-MeX and D-MeX)		%			63			

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3C. Customer measure of experience (C-MeX)

	Value
Annual customer satisfaction score for the customer service survey	79.22
Annual customer satisfaction score for the customer experience survey	82.18
Annual C-MeX score	80.70
Annual net promoter score	24.00
Total household complaints	5,253
Total connected household properties	948,014
Total household complaints per 10,000 connections	53.383
Confirmation of communication channels offered	TRUE

3D. Developer Services measure of experience (D-MeX)

	Value
Qualitative component annual results	66.61
Quantitative component annual results	93.10
D-MeX score	79.85
Developer services revenue (water) (£000)	8,472

3D. Developer Services measure of experience (D-MeX) continued

Calculating the D-MeX quantitative component	First reporting period (1 April to 30 September) %	Second reporting period (1 October to 31 March) %	Quantitative score (annual) Number
Water UK performance metric			
W1.1 Pre-development enquiry – reports issued within target	33.33	15.69	
W3.1 s45 quotations – within target	99.97	100.00	
W4.1 s45 service pipe connections – within target	95.61	97.20	
W6.1 Mains design <500 plots – quotations within target	100.00	100.00	
W7.1 Mains design >500 plots – quotations within target	-	100.00	
W8.1 Mains construction within target	100.00	100.00	
W17.1 Mains diversions (without constraints) – quotations within target	100.00	100.00	
W18.1 Mains diversions – construction/commissioning within target	100.00	100.00	
W20.1 Self-lay Point of Connection report <500 plots etc – reports issued within target	100.00	-	
W21.1 Self-lay Point of Connection report >500 plots etc – reports issued within target	100.00	-	
W23.1 Self-lay design and terms request <500 plots etc – quotation within target	100.00	100.00	
W30.1 Self-lay plot references and costing details – issued within target	-	100.00	
WN1.1 Confirmations issued to the applicant within target period	-	100.00	
WN2.2 Bulk supply offer letters issued to the applicant within target period	-	100.00	
WN4.3 Permanent supplies made available within the target period	-	100.00	
D-MeX quantitative score	92.89	93.30	
D-MeX quantitative score			0.93

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3E. Outcome performance – non-financial performance commitments

			Performance level – actual		
	Unique reference	Unit	Previous reporting year	Current reporting year	PCL met?
Common					
Risk of severe restrictions in a drought	PR19SEW_G.1	%	-	-	Yes
Priority services for customers in vulnerable circumstances – PSR reach	PR19SEW_J.1	%	1.5	3.3	Yes
Priority services for customers in vulnerable circumstances – attempted contacts	PR19SEW_J.1	%	N/A	75.7	Yes
Priority services for customers in vulnerable circumstances – actual contacts	PR19SEW_J.1	%	N/A	57.9	Yes
Bespoke PCs					
Segmented satisfaction of household customers – segment 1	PR19SEW_C.2	score	4.1	4.1	No
Segmented satisfaction of household customers – segment 2	PR19SEW_C.3	score	4.4	4.2	No
Segmented satisfaction of household customers – segment 3	PR19SEW_C.4	score	4.3	4.1	No
Segmented satisfaction of household customers – segment 4	PR19SEW_C.5	score	3.8	4.3	Yes
Segmented satisfaction of household customers – segment 5	PR19SEW_C.6	score	4.2	4.3	No
Segmented satisfaction of household customers – segment 6	PR19SEW_C.7	score	4.2	4.0	No
Satisfaction of household customers who are experiencing payment difficulties	PR19SEW_C.8	score	4.2	4.3	Yes
Satisfaction of household customers who are receiving non-financial support	PR19SEW_C.9	score	4.2	4.3	Yes
Satisfaction of household customers on our vulnerability schemes during a supply interruption	PR19SEW_C.10	%	3.6	3.7	Yes
Household customers receiving financial support	PR19SEW_I.1	nr	38,795	42,628	No
Satisfaction of stakeholders in relation to assistance offered by South East Water	PR19SEW_J.2	%	3.5	3.7	Yes
Gap sites	PR19SEW_L.1	nr	N/A	47	Yes
Event risk index (ERI)	PR19SEW_B.5	score	99.100	67.400	No
Greenhouse gas emissions	PR19SEW_H.4	nr	208.9	192.0	No
Engaging and working with abstractors to improve catchment resilience to low flows	PR19SEW_H.6	%	N/A	-	Yes
Satisfaction with value for money	PR19SEW_C.11	score	3.6	3.7	Yes
WINEP delivery	PR19SEW_NEP01	text	N/A	met	Yes
Non-financial performance commitments achieved		%			62

3F. Underlying calculations for common performance commitments – water and retail

Performance commitments set in standardised units – water	Unit	Standardising data indicator	Standardising data numerical value	Performance level – actual (current reporting year)	Performance level – calculated (i.e. standardised)
Mains repairs – reactive	Mains repairs per 1,000km	Mains length in km	14,842.57	1,958	131.92
Mains repairs – proactive	Mains repairs per 1,000km	Mains length in km	14,842.57	793	53.43
Mains repairs	Mains repairs per 1,000km	Mains length in km	14,842.57	2,751	185.35
Per capita consumption (PCC)	lpd	Total household population	2,219.33	368	165.86

Performance commitments measured against a calculated baseline	Unit	Performance level – actual (2017/18)	Performance level – actual (2018/19)	Performance level – actual (2019/20)	Baseline	Performance level – actual (2020/21)	Performance level 3 year average	Calculated performance level to compare against PCLs
Leakage	MI/d	95.9	95.0	94.5	95.1	92.7	94.1	1.1
Per capita consumption (PCC)	lpd	143.6	145.3	143.1	144.0	165.9	151.4	(5.1)

Water supply interruptions	Unit	Standardising data indicator	Standardising data numerical value	Total minutes lost	Number of properties supply interrupted	Calculated performance level
Water supply interruptions	Average number of minutes lost per property per year	Number of properties	955.09	30,041,563	51,513	00:31:27

Unplanned or planned outage	Current company level peak week production capacity (PWPC) MI/d	Reduction in company level PWPC MI/d	Outage proportion of PWPC %
Unplanned outage	723.46	22.38	3.09

Priority services for customers in vulnerable circumstances	Total residential properties	Total number of households on the PSR (as at 31 March)	PSR reach	Total number of households on the PSR over a 2 year period	Number of attempted contacts over a 2 year period	Attempted contacts %	Number of actual contacts over a 2 year period	Actual contacts %
Priority services for customers in vulnerable circumstances	887.07	29,210	3.3	7,094	5,367	75.7	4,104	57.9

3H. Summary information on outcome delivery incentive payments

	Initial calculation of performance payments (excluding C-MeX and D-MeX) £m (2017/18 prices)
Initial calculation of in period revenue adjustment by price control	
Water resources	(0.14)
Water network+	(4.57)
Residential retail	(1.11)
Business retail	-
Dummy control	-
Initial calculation of end of period revenue adjustment by price control	
Water resources	-
Water network+	-
Residential retail	-
Business retail	-
Dummy control	-
Initial calculation of end of period RCV adjustment by price control	
Water resources	-
Water network+	-
Residential retail	-
Business retail	-
Dummy control	-

3I. Supplementary outcomes information

Unplanned or planned outage	Current company level peak week production capacity (PWPC) MI/d	Reduction in company level PWPC MI/d	Outage proportion of PWPC %
Planned outage	723.46	14.19	1.96

Risk of severe restrictions in drought	Deployable output	Outage allowance	Dry year demand	Target headroom	Total population supplied	Customers at risk
Risk of severe restrictions in drought	646.29	18.37	543.21	48.99	2,281.91	-

4A. Water bulk supply information

for the 12 months ended 31 March 2021

	Volume Ml	Operating costs £000	Revenue £000
Bulk supply exports			
Kingston to Affinity	-	-	-
Total bulk supply exports	-	-	-
Bulk supply imports			
Belmont Scheme	1,597.401	748	
River Medway Scheme	7,702.476	1,020	
Weirwood	1,043.650	749	
Affinity (Egham)	7,343.996	2,717	
Darwell	347.030	1,001	
Total bulk supply imports	18,034.553	6,235	

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4B. Analysis of debt

	Fixed rate instruments						
	Fixed rate listed bond	Fixed rate debenture	Fixed rate debenture	Fixed rate debenture	Fixed rate debenture	Fixed rate debenture	Fixed rate debenture
Instrument identifier	-	-	-	-	-	-	-
Credit rating	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2
Currency	GBP	GBP	GBP	GBP	GBP	GBP	GBP
Class/subordination	A	A	A	A	A	A	A
Further information	-	-	-	-	-	-	-
Instrument start date (if after 31/07/21)	-	-	-	-	-	-	-
Years till maturity	7	-	-	-	-	-	-
Principal sum outstanding as at 31 March 2021 (excluding unamortised debt issue costs) (£m (nominal))	166.000	0.025	0.384	0.178	0.365	0.001	0.037
Amount used to calculate nominal interest cost and cash interest payment (£m (nominal))	166.000	0.025	0.384	0.178	0.365	0.001	0.037
Years to maturity x principal sum (£m (nominal))	1,162.000	-	-	-	-	-	-
Real RPI coupon (%)	4.15	1.61	2.10	2.59	3.58	4.07	4.57
Real CPI coupon (%)	5.58	3.00	3.50	4.00	5.00	5.50	6.00
Nominal interest rate (%)	5.58	3.00	3.50	4.00	5.00	5.50	6.00
Nominal interest cost (full year equivalent) (£m (nominal))	9.263	0.001	0.013	0.007	0.018	-	0.002
Cash interest payment (full year equivalent) (£m (nominal))	9.263	0.001	0.013	0.007	0.018	-	0.002
Unamortised debt issue costs as at 31 March 2021 (£m (nominal))	0.885	-	-	-	-	-	-
Value per balance sheet at 31 March 2021 (£m (nominal))	165.115	0.025	0.384	0.178	0.365	0.001	0.037
Fair value of debt at 31 March 2021 (£m (nominal))	208.745	0.015	0.277	0.147	0.376	0.001	0.045

4B. Analysis of debt continued

Fixed rate instruments (continued)								
	Loan notes (series 1)	Loan notes (series 2)	Lease liability – Laboratory	Lease liability – Brooke House	Lease liability – Blackhill WT	Lease liability – Leithrim House	Lease liability – Lenham Depot	Total
Instrument identifier	-	-	-	-	-	-	-	-
Credit rating	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	
Currency	GBP	GBP	GBP	GBP	GBP	GBP	GBP	
Class/subordination	A	A	A	A	A	A	A	
Further information	-	-	Operating lease	Operating lease	Operating lease	Operating lease	Operating lease	
Instrument start date (if after 31/07/21)	-	-	-	-	-	-	-	
Years till maturity	9	20	13	-	1	7	8	
Principal sum outstanding as at 31 March 2021 (excluding unamortised debt issue costs) (£m (nominal))	75.000	100.000	2.230	0.007	0.007	0.432	1.233	345.898
Amount used to calculate nominal interest cost and cash interest payment (£m (nominal))	75.000	100.000	2.230	0.007	0.007	0.432	1.233	345.898
Years to maturity x principal sum (£m (nominal))	675.000	2,000.000	28.990	-	0.007	3.024	9.864	3,878.885
Real RPI coupon (%)	1.55	1.82	1.82	1.55	1.55	1.55	1.55	
Real CPI coupon (%)	2.94	3.22	3.22	2.94	2.94	2.94	2.94	
Nominal interest rate (%)	2.94	3.22	3.22	2.94	2.94	2.94	2.94	
Nominal interest cost (full year equivalent) (£m (nominal))	2.205	3.220	0.072	-	-	0.013	0.036	14.851
Cash interest payment (full year equivalent) (£m (nominal))	2.205	3.220	0.072	-	-	0.013	0.036	14.851
Unamortised debt issue costs as at 31 March 2021 (£m (nominal))	0.475	0.634	-	-	-	-	-	1.994
Value per balance sheet at 31 March 2021 (£m (nominal))	74.525	99.366	2.230	0.007	0.007	0.432	1.233	343.905
Fair value of debt at 31 March 2021 (£m (nominal))	74.525	99.366	2.230	0.007	0.007	0.432	1.233	387.406

4B. Analysis of debt continued

	Floating rate instruments							Total
	Bank loan via committed facility	Bank loan via committed facility	Bank loan via committed facility	Bank loan	Undrawn committed facilities	Undrawn committed DSR liquidity facility	Undrawn committed O&M reserve facility	
Instrument identifier	-	-	-	-	-	-	-	-
Credit rating	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	-	-	-	-
Currency	GBP	GBP	GBP	GBP	-	-	-	-
Class/subordination	A	B	C	A	-	-	-	-
Further information	-	-	-	-	-	-	-	-
Instrument start date (if after 31/07/21)	-	-	-	-	-	-	-	-
Years till maturity	4	4	4	4	4	-	-	-
Principal sum outstanding as at 31 March 2021 (excluding unamortised debt issue costs) (£m (nominal))	40.000	10.000	30.000	120.000	-	-	-	200.000
Amount used to calculate nominal interest cost and cash interest payment (£m (nominal))	40.000	10.000	30.000	120.000	10.000	38.000	20.000	268.000
Years to maturity x principal sum (£m (nominal))	160.000	40.000	120.000	480.000	-	-	-	800.000
Real RPI coupon (%)	(0.83)	(0.88)	(0.86)	(0.08)	(0.83)	(0.29)	(0.29)	
Real CPI coupon (%)	0.53	0.48	0.50	1.29	0.53	1.08	1.08	
Reference interest rate (%)	0.08	0.03	0.05	0.09	0.08	0.08	0.08	
Margin over market index (%)	0.45	0.45	0.45	1.20	0.45	1.00	1.00	
Nominal interest rate (%)	0.53	0.48	0.50	1.29	0.53	1.08	1.08	
Nominal interest cost (full year equivalent) (£m (nominal))	0.212	0.048	0.150	1.548	0.053	0.410	0.216	2.637
Cash interest payment (full year equivalent) (£m (nominal))	0.212	0.048	0.150	1.548	0.053	0.410	0.216	2.637
Unamortised debt issue costs as at 31 March 2021 (£m (nominal))	-	-	-	1.275	-	-	-	1.275
Value per balance sheet at 31 March 2021 (£m (nominal))	40.000	10.000	30.000	118.725	-	-	-	198.725
Fair value of debt at 31 March 2021 (£m (nominal))	40.000	10.000	30.00	118.725	-	-	-	198.725

4B. Analysis of debt continued

	RPI linked instrument				Total
	Index linked listed bond	Index linked listed loan	Index linked listed loan	Index linked listed loan	
Instrument identifier	-	-	-	-	
Credit rating	BBB/Baa2	BBB/Baa2	BBB/Baa2	BBB/Baa2	
Currency	GBP	GBP	GBP	GBP	
Class/subordination	A	A	A	A	
Further information	-	-	-	-	
Instrument start date (if after 31/07/21)	-	-	-	-	
Years till maturity	20	16	11	12	
Principal sum outstanding as at 31 March 2021 (excluding unamortised debt issue costs) (£m (nominal))	177.369	121.870	227.159	53.064	579.462
Amount used to calculate nominal interest cost and cash interest payment (£m (nominal))	177.369	121.870	227.159	53.064	579.462
Years to maturity x principal sum (£m (nominal))	3,547.380	1,949.920	2,498.749	636.768	8,632.817
Real RPI coupon (%)	2.54	2.43	3.69	2.80	
Nominal interest rate (%)	3.94	3.83	5.11	4.21	
Nominal interest cost (full year equivalent) (£m (nominal))	6.997	4.672	11.609	2.233	25.511
Cash interest payment (full year equivalent) (£m (nominal))	4.505	2.961	8.382	1.486	17.335
Unamortised debt issue costs as at 31 March 2021 (£m (nominal))	1.014	1.252	0.953	0.184	3.403
Value per balance sheet at 31 March 2021 (£m (nominal))	176.355	120.618	226.206	52.880	576.059
Fair value of debt at 31 March 2021 (£m (nominal))	221.624	152.885	287.822	63.144	725.475

4B. Analysis of debt continued

	Totals for all instruments £m (nominal)
Principal sum outstanding as at 31 March 2021 (excluding unamortised debt issue costs)	1,125.361
Amount used to calculate nominal interest cost and cash interest payment	1,193.361
Years to maturity x principal sum	13,311.702
Nominal interest cost (full year equivalent)	42.999
Cash interest payment (full year equivalent)	34.823
Unamortised debt issue costs as at 31 March 2021	6.672
Value per balance sheet at 31 March 2021	1,118.689
Fair value of debt at 31 March 2021	1,311.606
	%
Inflation assumptions	
RPI	1.37
CPI	-
Indicative interest rates	
Indicative weighted average nominal interest rate	3.82
Indicative weighted average cash interest rate	3.09
Indicative debt portfolio breakdown	
Floating rate debt as percentage of total debt (gross)	17.77
Fixed rate debt as percentage of total debt (gross)	30.74
RPI linked debt as percentage of total debt (gross)	51.49
CPI linked debt as percentage of total debt (gross)	-
All index (CPI and RPI) linked debt as percentage of total debt (gross)	51.49
Fixed rate debt and index linked debt as percentage of total debt (gross)	82.23
Weighted average years to maturity (number)	11.8

Variances exist between tables 4B and 1E in relation to the nominal interest cost and cash interest payments. Within table 4B, in line with the regulatory requirements, the debt amounts used to calculate the nominal interest cost and cash interest payments have been reported in millions to three decimal places. This differs from the approach taken in calculating the nominal interest cost and cash interest payment within table 1E where the unrounded values of debt are used. Similarly, within table 4B, the interest rates have been rounded to two decimal places whereas for table 1E the true rates have been used. The coupling of these differing treatments have, in some instances, caused differences in the calculated values of interest charges and cash interest payments between the two tables.

In relation to fixed rate debt in particular, the total nominal interest cost and cash interest payment reported within table 4B is £14.851 million compared to £14.856 million within table 1E. The cause of this variance is the differing rounding principles used for the nominal interest rate between the two tables. In line with the regulatory guidelines, the interest rate on our fixed rate listed bond in table 4B has been rounded to 5.58 per cent whereas for table 1E the true interest rate of 5.5834 per cent has been used resulting in an increased interest value within table 1E.

Within table 4B, on floating interest rate debt, the total nominal interest cost and cash interest payment amounts to £2.637 million versus £1.957 million within table 1E. This variance has been driven in totality by the inclusion within table 4B of the company's undrawn committed facilities which are otherwise not reported within table 1E.

4B. Analysis of debt continued

Variances also exist between the nominal interest cost and cash interest payments on RPI linked debt reported in tables 4B and 1E. Where a nominal interest cost value of £25.511 million is reported in table 4B, the value in table 1E is £26.831 million resulting in a difference of £1.320 million. The cash interest payment calculated in table 4B equates to £17.335 million compared to the reported value within table 1E of £17.342 million resulting in a variance of £0.007 million. The drivers of these variances are illustrated within the below tables.

	Nominal interest cost (full year equivalent)							
	Index linked listed bond		Index linked listed loan		Index linked listed loan		Index linked listed loan	
	APR table 4B	APR table 1E	APR table 4B	APR table 1E	APR table 4B	APR table 1E	APR table 4B	APR table 1E
Amount used to calculate nominal interest cost and cash interest payment (£)	177,369,000	177,369,193	121,870,000	121,869,451	227,159,000	227,159,365	53,064,000	53,063,634
Real RPI coupon rate (%)	2.5400	2.5429	2.4300	2.4280	3.6900	3.6920	2.8000	2.8010
Increase in RPI (%)	1.3700	1.3581	1.3700	1.8499	1.3700	1.6235	1.3700	1.6235
Nominal interest rate (%)	3.9448	3.9355	3.8333	4.3229	5.1106	5.3754	4.2084	4.4700
Nominal interest cost (£m)	6.997	6.980	4.672	5.268	11.609	12.211	2.233	2.372
Variance (£m)		0.017		(0.596)		(0.602)		(0.139)

	Cash interest payment (full year equivalent)							
	Index linked listed bond		Index linked listed loan		Index linked listed loan		Index linked listed loan	
	APR table 4B	APR table 1E	APR table 4B	APR table 1E	APR table 4B	APR table 1E	APR table 4B	APR table 1E
Amount used to calculate nominal interest cost and cash interest payment (£)	177,369,000	177,369,193	121,870,000	121,869,451	227,159,000	227,159,365	53,064,000	53,063,634
Real RPI coupon rate (%)	2.5400	2.5429	2.4300	2.4280	3.6900	3.6920	2.8000	2.8010
Nominal interest cost (£m)	4.505	4.510	2.961	2.959	8.382	8.387	1.486	1.486
Variance (£m)		(0.005)		0.002		(0.005)		

As a result of these variances there are minor differences on the weighted average nominal interest and average cash interest rates reported within tables 4B and 1E of 0.06 per cent and 0.05 per cent respectively.

4C. Impact of price control performance to date on RCV

	12 months ended 31 March 2021		Price control period to date	
	Water resources £000	Water network+ £000	Water resources £000	Water network+ £000
Totex				
Final determination allowed totex (net of business rates, abstraction licence fees and grants and contributions)	22,780	112,075	22,780	112,075
Actual totex (net of business rates, abstraction licence fees and grants and contributions)	17,572	146,278	17,572	146,278
Transition expenditure	-	-	-	-
Disallowable costs	(352)	(735)	(352)	(735)
Total actual totex (net of business rates, abstraction licence fees and grants and contributions)	17,220	145,543	17,220	145,543
Variance	(5,560)	33,468	(5,560)	33,468
Variance due to timing of expenditure	6,000	(22,616)	6,000	(22,616)
Variance due to efficiency	440	10,852	440	10,852
Customer cost sharing rate (%)	38.09	38.09	38.09	38.09
Customer share of totex over/underspend	168	4,133	168	4,133
Company share of totex over/underspend	272	6,719	272	6,719
Final determination allowed totex – business rates and abstraction licence fees	3,856	16,304	3,856	16,304
Actual totex – business rates and abstraction licence fees	3,886	17,280	3,886	17,280
Variance – business rates and abstraction licence fees	30	976	30	976
Customer cost sharing rate – business rates and abstraction licence fees (%)	75.00	75.00	75.00	75.00
Customer share of totex over/underspend – business rates and abstraction licence fees	23	732	23	732
Company share of totex over/underspend – business rates and abstraction licence fees	8	244	8	244
Final determination allowed totex – not subject to cost sharing	-	545	-	545
Actual totex – not subject to cost sharing	-	1,618	-	1,618
Variance – 100% company allocation	-	1,073	-	1,073
Total company share of totex over/underspend	280	8,036	280	8,036

4C. Impact of price control performance to date on RCV continued

	12 months ended 31 March 2021		Price control period to date	
	Water resources £000	Water network+ £000	Water resources £000	Water network+ £000
RCV				
Total company share of totex over/underspend	190	4,865	190	4,865
PAYG rate (%)	52.86	74.25	52.86	74.25
RCV element of totex over/underspend	90	1,253	90	1,253
Adjustment for ODI outperformance payment or underperformance payment			-	-
RCV determined at FD at 31 March			79,467	1,302,544
Projected 'shadow' RCV			79,557	1,303,797

TABLE CONTENT SUMMARY

This table tracks year on year changes to the RCV and reports a 'shadow' RCV as a result of actual totex and any ODI adjustments.

BACKGROUND AND PURPOSE

This information is intended to show the rolling impact on the RCV of changes in investment activity relative to the determination and ODI performance over the year.

4C. Impact of price control performance to date on RCV continued

TABLE COMPLETION METHODOLOGY

Key inputs to the table and their sources are summarised in the table below:

Line	Description	Source data and analysis
4C.1	Final determination allowed totex (net of business rates, abstraction licence fees and grants and contributions)	The company's allowed totex in the final determination, net of allowed totex for business rates, Environment Agency / Natural Resources Wales abstraction licence fees, grants and contributions and other items not subject to cost sharing, as published in Ofwat's Financial Flows data reference document on our website alongside the annual publication of the Regulatory Capital Values. Values should be inflated using the average CPIH figure for the reporting year./ price control period.
4C.2	Actual totex (net of business rates, abstraction licence fees and grants and contributions)	The company's actual totex, excluding business rates and Environment Agency abstraction licence fees and income offset grants and contributions and other items not subject to cost sharing, as reported in: Actual totex – 2B.26 Less the sum of costs excluded from cost sharing or with separate sharing rates: · Income offset payments – 2E.15/~~2E.27~~ · Non price control grants and contributions (negative number) – sum of 2E.4-6/2E.17-19/~~2E.29-31~~ · Third party services (opex) – 2B.13 · Third party services (capex) – 2B.20 · Other cash items – 2B.25 · Pension deficit recovery costs – 2B.24 · Actual expenditure on innovation projects funded through the innovation competition – 9A.20 · Non-section 185 diversions – 4P.3 · Abstraction charges (water only) – 2B.3 · Local authority and cumulo rates – 2B.8 ~~· Strategic scheme development costs – 4L.37~~
4C.3	Transition expenditure	Expenditure incurred in 2019/20 for the delivery of outcomes in the price control period 2020 to 2025 and that was included in the totex allowance at PR19.
4C.4	Disallowable costs	In setting price controls, we have used an overarching principle that costs should only feature in our totex for cost sharing for activities where it is appropriate for a company to share an over (or under) spend with their customers. We define disallowable items as costs that do not conform to this overarching principle. These include: · Costs associated with impairment of other businesses · Costs related to financing (bond issuance fees, refinancing, takeover costs) · Fines and investigation costs · Compensation claims · Any other costs where the activity driving it does not, ex ante, have a reasonable expectation of customer benefit
4C.7	Variance due to timing of expenditure	The value due to a variation in the timing of the planned expenditure (i.e. accelerated or deferred).

4C. Impact of price control performance to date on RCV continued

Line	Description	Source data and analysis
4C.9	Customer cost sharing rate	The customer cost sharing rate as published in Ofwat's Financial Flows data reference document on our website alongside the annual publication of the Regulatory Capital Values.
4C.12	Final determination allowed totex -business rates and abstraction licence fees	The company's allowed totex in the final determination for business rates and Environment Agency / Natural Resources Wales abstraction licence fees as published in Ofwat's Financial Flows data reference document on our website alongside the annual publication of the Regulatory Capital Values. Values should be inflated using the average CPIH figure for the reporting year/ price control period.
4C.13	Actual totex – business rates and abstraction licence fees	The company's actual totex for business rates and Environment Agency / Natural Resources Wales abstraction licence fees as reported in: · Business rates – line 2B.8 · Abstraction charges – line 2B.3
4C.15	Customer cost sharing rate – business rates and abstraction licence fees	The customer cost sharing rate as published in Ofwat's Financial Flows data reference document on our website alongside the annual publication of the Regulatory Capital Values.
4C.18	Final determination allowed totex not subject to cost sharing	The company's allowed totex in the final determination for third party services, strategic regional water resource development schemes, other cash items and non-s185 diversions as published in Ofwat's Financial Flows data reference document on our website alongside the annual publication of the Regulatory Capital Values.
4C.19	Actual totex not subject to cost sharing	The company's actual totex for items not subject to cost sharing – · Non-s185 diversions – line 4P.3 · Innovation fund – line 9A.20 · ~~Strategic water resource development schemes – line 4L.37~~ · Other cash items – line 2B.25
4C.23	PAYG rate	The appropriate PAYG rate as published in Ofwat's Financial Flows data reference document on our website alongside the annual publication of the Regulatory Capital Values.
4C.25	Adjustment for ODI outperformance payment or underperformance payment	RCV impact of the outperformance payment or underperformance payment from the ODI.
4C.26	RCV determined at FD at 31 March	RCV at 31 March per the 2019 price determination inflated using the appropriate CPIH and RPI values – these are published on the OFWAT website annually in April.

4C. Impact of price control performance to date on RCV continued**TABLE COMPLETION METHODOLOGY DISCUSSION****Applying the appropriate cost sharing amount to the RCV**

The following query is listed in the Ofwat log (#14) for queries companies have submitted regarding the APR21 tables and the RAG guidance.

Line	Description	Source data and analysis
Table 4C	Lines 21-27	As raised in the 2020/21 RAGs consultation, reported shadow RCV should be calculated by applying customer share of totex under/overspend but table build-up using company share of totex under/overspend. The way the definition is currently drafted would result in totex items excluded from the customer sharing mechanism, eg. fines, being erroneously included in shadow RCV.

The corresponding response has been given by Ofwat:

We agree the reported shadow RCV should be calculated by applying customer share of totex under/overspend, we will propose a change for 2021/22.

From the Ofwat response it is unclear if we are to make this change for 2020/21. For the purposes of correctly reporting the shadow RCV we believe it is correct to make this change. We confirm that we have made the change by modifying the calculation for line 4C.22 as follows:

Ref	Heading	Calculation
Original 4C.22	Total Company share of totex over/under spend	4C.11 + 4C.17 + 4C.20
Revised 4C.22	Total Customer share of totex over/under spend	4C.10 + 4C.16

4C. Impact of price control performance to date on RCV continued

SOUTH EAST WATER FINANCIAL FLOWS DATA CLARIFICATIONS

When preparing our APR table 4C we checked the original published version of financial flows (v1g, c10 May 21) against our expectation of numbers and in particular to the numbers reported in our financial model and company specific final determination report – particularly tables 3.2 and 3.7 available at www.ofwat.gov.uk/publication/pr19-final-determinations-south-east-water-final-determination

Table 3.2 Totex by wholesale price control and type of cost, 2020 to 2025 (2017/18 prices) and table 3.7 Cost sharing rates for 2020 to 2025 and totex for end of period reconciliation (2017/18 prices) are set out below:

Table 3.2: Totex by wholesale price control and type of cost, 2020 to 2025 (2017/18 prices)	Water resources	Water Network+	Total
Base expenditure	75.0	661.2	736.2
Enhancement expenditure	40.8	121.7	162.4
Operating lease adjustment	(0.2)	(0.7)	(0.9)
Gross allowed totex used to calculate cost sharing rates	115.6	782.2	897.7
Strategic regional water resources solutions and other cash items	-	-	-
Third party costs	-	2.2	2.2
Non-section 185 diversions	-	0.4	0.4
Ex-ante cost sharing adjustment	-	-	-
Gross totex	115.6	784.8	900.3
Grants and contributions after adjustment for income offset ¹	-	87.7	87.7
Net allowed totex used in PAYG calculation	115.6	697.1	812.6
Pensions deficit recovery costs ²	2.5	15.0	17.5
Total	118.1	712.1	830.1

¹ Includes price control and non-price control grants and contributions.

² We are displaying pension deficit recovery costs separately as they are not included in the calculation for PAYG (see section 4).

4C. Impact of price control performance to date on RCV continued**Table 3.7: Cost sharing rates for 2020 to 2025 and totex for end-of-period reconciliation**

	Water resources	Water Network+	Total
Totex for cost sharing rates – September 2018 business plan	127.6	877.0	
Totex for cost sharing rates – August 2019	127.6	877.0	
Weighted company view of totex for cost sharing rates	127.6	877.0	
Gross allowed totex for cost sharing rates	115.6	782.2	897.7
Cost sharing ratio		1.12	
Cost sharing rate – outperformance		38%	
Cost sharing rate – underperformance		62%	
Grants and contributions	-	109.0	
Abstraction charges and business rates	18.4	77.9	
Net allowed totex subject to cost sharing reconciliation with standard cost sharing rates in this table	97.1	595.3	692.4

GRANTS AND CONTRIBUTIONS

The financial flows for South East Water grants and contributions gives the following.

G&Cs	Unit	20/21	21/22	22/23	23/24	24/25	Comments
WN – G&Cs – capital expenditure – price control – real	£m	21.49	21.80	21.85	21.81	21.73	
WN – G&Cs – operational expenditure – price control – real	£m	-	-	-	-	-	Excludes WN Opex G&Cs
WR – G&Cs – capital expenditure – price control – real	£m	-	-	-	-	-	
WR – G&Cs – operational expenditure – price control – real	£m	-	-	-	-	-	
WWN – G&Cs – capital expenditure – price control – real	£m	-	-	-	-	-	
WWN – G&Cs – operational expenditure – price control – real	£m	-	-	-	-	-	

We note that the total grants and contributions does not correspond with the grants and contributions shown in table 3.7 of £109 million with a difference of £0.365 million.

4C. Impact of price control performance to date on RCV continued

Our understanding of grants and contributions allowed in totex from the published South East Water financial model available at www.ofwat.gov.uk/wp-content/uploads/2019/12/Financial-model_SEW_FD.xlsb is as follows:

Water Network	Notionalised	No sensi case				
Model period ending	-	Checks – 5 year period	31 Mar 19	31 Mar 20	31 Mar 21	
Timeline label	-	Track chgs	Pre-Fcst	Pre-Fcst	Forecast	
Financial year ending	2	Alerts – 5 year period	2019	2020	2021	
Model column counter	Constant	Unit	Total	1	2	3
Opex						
Operating expenditure						
<i>Water network: Totex</i>						
Water network operating expenditure (amount for totex CR) (post override) – real	[Enter positive]	£m	394.219	-	-	76.286
WN – Total gross capital expenditure – real – including cost sharing	[Enter positive]	£m	390.545	-	-	68.422
Water network+ capex grants and contributions	-	£m	87.347	-	-	17.744
Water network+ opex grants and contributions	-	£m	0.365	-	-	0.075

The income offset is not available directly from the financial model. However we have derived this from the South East Water Grants and Contributions model published at www.ofwat.gov.uk/wp-content/uploads/2019/12/Grants-and-Contributions-model_SEW_FD.xlsm in the calculation as set out below. This ties in the numbers from table 3.2 and table 3.7. (Note that the numbers from the Grants and Contributions model are slightly different to the numbers used in the financial model. We have used the numbers from the financial model with priority.)

4C. Impact of price control performance to date on RCV continued

Grants and Contributions – workings	Constant	Unit	Total					
<i>FD – Grants and contributions (2017/18 prices)</i>				2020/21	2021/22	2022/23	2023/24	2024/25
FD G&C net (real)		£m	87.347	17.744	17.590	17.498	17.325	17.190
Opex diversions contributions – NRSWA		£m	0.365	0.075	0.074	0.072	0.072	0.071
FD Total G&C net (real)		£m	87.712	17.820	17.664	17.570	17.398	17.261
SEW BP App28 Income Offset Water efficiency challenge – (post override)	10.27%	£m	23.771	4.173	4.695	4.851	4.997	5.055
FD Income offset net (real)		£m	21.310	3.740	4.210	4.350	4.480	4.530
FD G&C gross (real)		£m	109.022	21.560	21.874	21.920	21.878	21.791
FD Income offset		£m	(21.310)	(3.740)	(4.210)	(4.350)	(4.480)	(4.530)
FD Total G&C net (real)		£m	87.712	17.820	17.664	17.570	17.398	17.261

These figures match those for grants and contributions in table 3.2 (after income offset) £87.7 million and table 3.7 (before income offset) £109 million.

4C. Impact of price control performance to date on RCV continued

COSTS NOT SUBJECT TO SHARING

Initially Ofwat issued Version 1g of the financial flows data with the following data for costs not subject to cost sharing. We agree with this data and it ties in to the exclusions itemised in table 3.2 above.

Costs not subject to cost sharing WN G&Cs	Unit	20/21	21/22	22/23	23/24	24/25	Comments
WN – Opex third party services for financial flows – Real	£m	0.43	0.43	0.43	0.43	0.43	2.16
WN – Capex third party services for financial flows – Real	£m	-	-	-	-	-	
WN – Opex strategic water resources development scheme for financial flows – Real	£m	-	-	-	-	-	
WN – Capex strategic water resources development scheme for financial flows – Real	£m	-	-	-	-	-	
WN – Opex other cash items for financial flows – Real	£m	-	-	-	-	-	
WN – Capex other cash items for financial flows – Real	£m	-	-	-	-	-	
WN – Opex Non-s185 diversions for financial flows – Real	£m	0.09	0.09	0.09	0.09	0.08	0.43
WN – Capex Non-s185 diversions for financial flows – Real	£m	-	-	-	-	-	
WN Conditional Allowance	£m	-	-	-	-	-	
Total costs not subject to cost sharing – WN – Real	£m	0.52	0.52	0.52	0.52	0.52	2.59

4C. Impact of price control performance to date on RCV continued

Ofwat subsequently issued version 1i (and 1k) of the financial flows data which gives the following data for costs not subject to cost sharing WN:

Costs not subject to cost sharing WN G&Cs	Unit	20/21	21/22	22/23	23/24	24/25	Comments
WN – Opex third party services for financial flows – Real	£m	0.43	0.43	0.43	0.43	0.43	2.16
WN – Capex third party services for financial flows – Real	£m	-	-	-	-	-	
WN – Opex strategic water resources development scheme for financial flows – Real	£m	-	-	-	-	-	
WN – Capex strategic water resources development scheme for financial flows – Real	£m	-	-	-	-	-	
WN – Opex other cash items for financial flows – Real	£m	-	-	-	-	-	
WN – Capex other cash items for financial flows – Real	£m	-	-	-	-	-	
WN – Opex Non-s185 diversions for financial flows – Real	£m	0.09	0.09	0.09	0.09	0.08	0.43
WN – Capex Non-s185 diversions for financial flows – Real	£m	-	-	-	-	-	
WN Conditional Allowance	£m	-	-	-	-	-	
WN – Income Offset	£m	4.17	4.70	4.85	5.00	5.06	23.77
WN – Grants and Contributions – capital expenditure – non price control – real	£m	-	-	-	-	-	
WN – Grants and Contributions – operational expenditure – non price control – real	£m	(0.08)	(0.07)	(0.07)	(0.07)	(0.07)	(0.37)
Total Costs not subject to cost sharing – WN – Real	£m	4.62	5.14	5.30	5.44	5.50	

4C. Impact of price control performance to date on RCV continued

We have the following concerns regarding the highlighted numbers:

We are concerned to find that the income offset is being included in 'costs not subject to cost sharing'. This contradicts table 3.7 of our FD document which clearly shows grants and contributions (gross of income offset) as being included in cost sharing at standard rates.

Also we find that the opex grants and contributions which are included in our totex (see reconciliation above) are shown in table 3.7 to be allocated to 'standard cost sharing rates' (i.e. included in the £109 million) but here are being allocated to 'costs not subject to cost sharing'.

In order to be consistent with our final determination financial model for allowed revenue and the FD reported tables we have made the following changes to our financial flows for table 4C and submitted our views to Ofwat.

- the items highlighted in yellow have been removed from the 'costs not subject to cost sharing WN' table;
- the opex grants and contributions have been added to the grants and contributions table.

SOUTH EAST WATER CLOSING RCV AT MARCH 2021

Ofwat has published its view of companies RCV taking into account the 2020/21 year average and year end inflation figures for RPI and CPIH at www.ofwat.gov.uk/publication/regulatory-capital-values-2021/. By populating our published FD financial model with actual CPIH and RPI values we are able to replicate the published opening and closing RCVs on a nominal year average basis. We are able to replicate the nominal year end RCV for the CPIH component of the existing RCV and the new assets component of the RCV by uplifting the year average position using March 2020 CPIH/2020/21 average CPIH. It appears that the RPI component of the existing RCV has also been uplifted to year end using CPIH. We would expect the year end position for the RPI component of the existing RCV to be calculated using RPI i.e. by uplifting the nominal year average position using March 2020 RPI/2020/21 average RPI.

4C. Impact of price control performance to date on RCV continued

The table below sets out our view of the correct calculation.

Ofwat published RCV – South East Water			WR	WN	Total
Closing RCV – CPI(H) at 31 March	£m Mar-21 YE prices		33.729	636.675	670.404
Closing RCV – CPI(H) + RPI wedge at 31 March	£m Mar-21 YE prices		33.491	632.039	665.530
Closing RCV – Additions at 31 March	£m Mar-21 YE prices		12.247	33.830	46.077
Closing RCV at 31 March	£m Mar-21 YE prices		79.467	1,302.544	1,382.011
South East Water calculated RCV			WR	WN	Total
Closing RCV – CPI(H) at 31 March	£m 2020/21 av		33.547	633.241	666.788
Closing RCV – CPI(H) + RPI wedge at 31 March	£m 2020/21 av		33.311	628.635	661.946
Closing RCV – Additions at 31 March	£m 2020/21 av		12.181	33.647	45.828
Closing RCV at 31 March	£m 2020-21 av		79.039	1,295.523	1,374.562
CPIH 2020/21 FYA	Index	109.108			
CPIH Mar-21	Index	109.700			
CPI(H): Fin year average – inflate from base year 2017/18 average calc	%	100.54			
RPI 2020/21 FYA	Index	294.167			
RPI Mar-21	Index	296.900			
CPI(H): Fin year average – inflate from base year 2017/18 average calc	%	100.93			
Correct RCV values			WR	WN	Total
Closing RCV – CPI(H) at 31 March	£m 2020/21 YE		33.729	636.675	670.404
Closing RCV – CPI(H) + RPI wedge at 31 March	£m 2020/21 YE		33.620	634.476	668.096
Closing RCV – Additions at 31 March	£m 2020/21 YE		12.247	33.830	46.077
Closing RCV at 31 March	£m 2020/21 YE		79.596	1,304.981	1,384.577
Difference	£m 2020/21 YE		0.129	2.437	2.566

Ofwat has responded to this query by publishing their calculation methodology. We have used the Ofwat published RCV in our table 4C however, as set out above we do not believe that the movement from average RCV to year end RCV has been applied correctly to the RPI component of the existing RCV.

4C. Impact of price control performance to date on RCV continued

TABLE CALCULATIONS

4C.1 FD indexation to outturn 'Final determination allowed totex (net of business rates, abstraction licence fees and grants and contributions).'

Totex (net of business rates, abstraction licence fees and grants and contributions) (£m 2017/18 prices)	WR	WN	Total
Operating expenditure (amount for totex CR) (post override) – real			
Total gross capital expenditure – real (incl g&c) – incl cost sharing	-	-	-
Final determination allowed gross totex (See Note 1)	25.442	144.707	170.149
· Less FD Third Party costs (opex)	-	0.431	0.431
· Less FD Third Party costs (capex)	-	-	-
· Less FD Non-sect 185 diversions	-	0.089	0.089
Final determination allowed gross totex – for cost sharing	25.442	144.186	169.629
· Less FD grants and contributions (totex)	-	17.744	17.744
· Less FD grants and contributions (income offset)	-	3.744	3.744
· Less FD grants and contributions WN Opex (Financial Flows correction) (See Note 2)	-	0.075	0.075
· Less FD business rates and abstraction licence fees	3.683	15.573	19.256
Final determination allowed totex (net of business rates, abstraction licence fees and grants and contributions)	21.759	107.050	128.809
CPI(H): Fin year average – inflate from base year 2017/18 average 104.69%			
FD allowed totex (net of business rates, abstraction licence fees and G&Cs) (£m 2020/21 prices)	22.780	112.075	134.856

1. This ties in to the five year total in South East Water Specific FD report table 3.2 of £900.3 million.
2. See discussion above regarding allowed grants and contributions in our financial model totex calculations and South East Water Specific FD report.

CPIH – Convert base year to outturn

CPIH 2017/18 FYA – Base Year	Index	104.217
CPIH 2020/21 FYA – Outturn	Index	109.108
CPI(H): Fin year average – inflate from base year 2017/18 average	%	104.69%

4C. Impact of price control performance to date on RCV continued

4C.2 Detail for calculation of 'Less the sum of costs excluded from cost sharing or with separate sharing rates'.

Actual totex for sharing at standard rates (£m 2020/21 prices)	WR	WN	Total
Actual totex (net)	22.149	170.939	193.088
· Less Actual grants and contributions (income offset)	-	1.586	1.586
· Less Actual Non price control grants and contributions	-	-	-
· Less Actual Third party services (opex)	-	0.403	0.403
· Less Actual Third party services (capex)	-	-	-
· Less Actual Other cash items	-	-	-
· Less Actual Pension deficit recovery costs	0.691	4.177	4.868
· Less Actual expenditure on innovation	-	0.830	0.830
· Less Actual Non section 185 diversions	-	0.385	0.385
· Less Actual abstraction licence fees	2.934	0.172	3.106
· Less Actual business rates	0.952	17.108	18.060
· Less Actual Strategic scheme development costs	-	-	-
Actual totex (net of business rates, abstraction licence fees and G&Cs)	17.572	146.278	163.850

4C.4 Detail for calculation of 'Disallowable costs'

Disallowable costs (£m 2020/21 prices)	WR	WN	Total
Costs associated with impairment	-	-	-
· Costs relating to financing (bond issue etc)	-	-	-
· Fines and investigation costs	-	-	-
· Compensation claims	0.352	0.735	1.086
· Other disallowables	-	-	-
Total	0.352	0.735	1.086

4C.7 Detail for calculation of 'Variance due to timing of expenditure'

Variance due to timing (£m 2020/21 prices)	WR	WN	Total
WR Opex	-	-	-
· WN Opex (See Note 1)	-	4.188	4.188
· WR Schemes (See Note 2)	(6.000)	-	(6.000)
· WN Schemes (See Note 3)	-	18.428	18.428
Variance due to timing of expenditure (£m 2020/21 prices)	(6.000)	22.616	16.616

1 South East Water has reprofiled the FD allowance for enhancement opex allowed for leakage (c£4 million).

2 WR has underspent on the following projects which are still expected to be delivered over the five year period.

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4C. Impact of price control performance to date on RCV continued

	£m 2020/21 prices
WINEP (National Environment Programme)	(3.4)
ANP (Butler – SOSI Scheme)	(1.2)
River Medway Scheme (Bulk Supply from Southern Water)	(0.9)
Abstraction Meters	(0.1)
Bewl to Darwell (INNs Project)	(0.2)
Flooding (Investigations)	(0.2)
Total	(6.0)

3. WN has overspent on the following projects. These costs are as a result of reprofiling expenditure from the FD allowance.

	£m 2020/21 prices
Aylesford Reservoir (Sinkhole occurred at the end of September, remedial works on-going)	4.5
Renewals – costs brought forward from later in AMP for early environmental/design works	0.5
IT Agile Working – accelerated from later in AMP	0.4
Covid claims from contractor and claim provision	2.0
Developer costs reprofiled	2.5
Summer demand schemes brought forward	0.7
Keleher WTW reprofiled	0.5
Base WQ – reprofiled disinfection treatment projects	3.7
Buildings – reprofiled work at Snodland Head Office and Lenham	1.5
Apparatus Renewals/stop tap replacement reprofiled	2.2
	18.4

A significant component of the water network totex overspend (c£14 million) arises as a result of a shortfall in developer contributions. As part of our final determination an additional £31 million (2017/18 prices) developer contributions was allowed to fund enhancement development expenditure of c£42 million (2017/18 prices). (See page 60 of our South East Water specific FD report). This was to be funded through increasing infrastructure charges and an increasing income offset. We discussed this approach to funding new development with Ofwat at an early stage and identified that we were constrained both by the rules for setting infrastructure charges and practical developer considerations. We identified that the assumptions in the FD would result in us reporting a significant shortfall in collection of developer contributions, particularly in the early years. This conversation took place before the impact of Covid-19 which has further impacted our developer activity and contributions.

4C. Impact of price control performance to date on RCV continued

4C.12 FD indexation to outturn 'Final determination allowed totex – business rates and abstraction licence fees'.

Totex – business rates and abstraction licence fees		WR	WN	Total
FD business rates	£m Mar-21 YE prices	0.886	15.437	16.323
FD abstraction rates	£m Mar-21 YE prices	2.797	0.136	2.933
FD allowed totex – business rates and abstraction licence fees	£m Mar-21 YE prices	3.683	15.573	19.256
CPI(H): Fin year average – inflate from base year 2017/18 average – CALC	% 104.69			
Final determination allowed totex – business rates and abstraction fees	£m Mar-21 YE prices	3.856	16.304	20.160

4C.18 FD indexation to outturn 'Final determination totex not subject to cost sharing'

FD totex not subject to cost sharing (£m 2017/18 prices)		WR	WN	Total
FD Third party services (opex)		-	0.431	0.431
FD Third party services (capex)		-	-	-
FD Non-sect 185 diversions		-	0.089	0.089
FD Strategic scheme development costs		-	-	-
FD totex – not subject to cost sharing		-	0.521	0.521
CPI(H): Fin year average – inflate from base year 2017/18 average – 104.69%				
Final determination allowed totex – not subject to cost sharing (£m 2020/21 prices)		0.000	0.545	0.545

4C.19 Detail for calculation 'Actual' totex not subject to cost sharing

Actual totex not subject to cost sharing (£m 2020/21 prices)		WR	WN	Total
Actual Third party services (opex)		-	0.403	0.403
Actual Third party services (capex)		-	-	-
Actual Other cash items		-	-	-
Actual expenditure on innovation		-	0.830	0.830
Actual Non section 185 diversions		-	0.385	0.385
Actual Strategic scheme development costs		-	-	-
Actual totex not subject to cost sharing (£m 2020/21 prices)		-	1.618	1.618

4C.25 Adjustment for ODI outperformance payment or underperformance payment

None of our ODIs for 2020/21 impact our RCV.

Changes in methodology since last year

This is a new table design and layout which has significantly changed since the table 4C in APR 2019/20.

Risks to data accuracy and robustness

We have some differences in understanding of the financial flows data with Ofwat – particularly when cross referencing to our financial model and South East Water specific final determination report. The data we have used in this table is sourced from and consistent with our South East Water financial model and the South East Water specific financial determination report. We will use the query process with Ofwat to understand any differences.

4D. Totex analysis – water resources and water network+

for the 12 months ended 31 March 2021

	Network+					
	Water resources £000	Raw water transport £000	Raw water storage £000	Water treatment £000	Treated water distribution £000	Total £000
Operating expenditure						
Base operating expenditure	14,890	596	220	24,075	63,410	103,191
Enhancement operating expenditure	-	-	-	-	1,419	1,419
Developer services operating expenditure	-	-	-	-	-	-
Total operating expenditure excluding third party services	14,890	596	220	24,075	64,829	104,610
Third party services	-	-	-	-	403	403
Total operating expenditure	14,890	596	220	24,075	65,232	105,013
Grants and contributions – operating expenditure	-	-	-	-	-	-
Capital expenditure						
Base capital expenditure	988	772	50	26,014	29,949	57,773
Enhancement capital expenditure	5,580	-	-	7,310	2,637	15,527
Developer services capital expenditure	-	-	-	-	16,793	16,793
Total gross capital expenditure (excluding third party)	6,568	772	50	33,324	49,379	90,093
Third party services	-	-	-	-	-	-
Total gross capital expenditure	6,568	772	50	33,324	49,379	90,093
Grants and contributions – capital expenditure	-	-	-	-	(6,886)	(6,886)
Net totex	21,458	1,368	270	57,399	107,725	188,220
Cash expenditure						
Pension deficit recovery payments	691	19	-	1,748	2,410	4,868
Other cash items	-	-	-	-	-	-
Totex including cash items	22,149	1,387	270	59,147	110,135	193,088
Atypical expenditure						
Covid-19 wholesale personnel opex impact	67	5	-	207	402	681
Covid-19 wholesale power & chemicals opex impact	286	16	-	199	799	1,300
Covid-19 wholesale bulk supply opex impact	-	-	-	-	72	72
Covid-19 wholesale contractors opex impact	203	-	-	-	523	726
Covid-19 wholesale reactive maintenance opex impact	-	-	-	-	793	793
Total atypical expenditure	556	21	-	406	2,589	3,572

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4H. Financial metrics

for the 12 months ended 31 March 2021

	Current Year	AMP to date
Financial indicators		
Net debt (£m)	1,083.920	
Regulatory equity (£m)	298.091	
Regulatory gearing (%)	78.43	
Post tax return on regulatory equity (%)	6.50	
RORE (return on regulatory equity) (%)	(0.48)	(0.48)
Dividend yield (%)	(48.17)	
Retail profit margin – household (%)	(8.73)	
Retail profit margin – non household (%)	1,068.18	
Credit rating – Fitch	-	
Credit rating – Moody's	Baa2 (stable)	
Credit rating – Standard and Poor's	BBB (stable)	
Return on RCV (%)	4.64	
Dividend cover (dec)	(0.12)	
Funds from operations (FFO) (£m)	85.856	
Interest cover (cash) (dec)	3.50	
Adjusted interest cover (cash) (dec)	2.00	
FFO/net debt (dec)	0.08	
Effective tax rate (%)	8.84	
RCF (£m)	229.456	
RCF/net debt (dec)	0.21	
Revenue and earnings		
Revenue (actual) (£m)	239.484	
EBITDA (actual) (£m)	116.420	
Borrowings		
Proportion of borrowings which are fixed rate (%)	30.74	
Proportion of borrowings which are floating rate (%)	17.77	
Proportion of borrowings which are index linked (%)	51.49	
Proportion of borrowings due within 1 year or less (%)	7.11	
Proportion of borrowings due in more than 1 year but no more than 2 years (%)	-	
Proportion of borrowings due in more than 2 years but no more than 5 years (%)	10.66	
Proportion of borrowings due in more than 5 years but no more than 20 years (%)	57.49	
Proportion of borrowings due in more than 20 years (%)	24.74	

The company does not currently receive credit ratings from Fitch Rating, therefore no value has been entered in the above table for this.

4I. Financial Derivatives

This table has not been reproduced in this regulatory report as the company has no financial derivatives to report on under the RAGs.

4j. Base expenditure analysis – water resources and water network+

for the 12 months ended 31 March 2021

	Network+					
	Water resources £000	Raw water transport £000	Raw water storage £000	Water treatment £000	Treated water distribution £000	Total £000
Operating expenditure						
Power	4,998	271	-	392	13,981	19,642
Income treated as negative expenditure	(16)	(1)	-	(1)	(41)	(59)
Bulk supply	1,042	-	-	5,087	-	6,129
Renewals expensed in year (infrastructure)	-	-	-	-	-	-
Renewals expensed in year (non-infrastructure)	-	-	-	-	-	-
Other operating expenditure	4,980	129	5	16,986	33,499	55,599
Local authority and cumulo rates	952	197	215	1,439	15,257	18,060
Service charges						
Canal & river trust abstraction charges/discharge consents	-	-	-	-	-	-
Environment agency/NRW abstraction charges/discharge consents	2,934	-	-	172	-	3,106
Other abstraction charges/discharge consents	-	-	-	-	-	-
Other operating expenditure						
Costs associated with traffic management act	-	-	-	-	643	643
Costs associated with lane rental schemes	-	-	-	-	71	71
Statutory water softening	-	-	-	-	-	-
Total base operating expenditure	14,890	596	220	24,075	63,410	103,191
Capital expenditure						
Maintaining the long term capability of the assets – infra	-	772	-	182	13,775	14,729
Maintaining the long term capability of the assets – non-infra	988	-	50	25,832	16,174	43,044
Total base capital expenditure	988	772	50	26,014	29,949	57,773
Traffic management act						
Projects incurring costs associated with traffic management act (nr)	-	-	-	-	24,470	24,470

4N. Developer services expenditure – water resources and water network+

for the 12 months ended 31 March 2021

	Network+					
	Water resources £000	Raw water transport £000	Raw water storage £000	Water treatment £000	Treated water distribution £000	Total £000
New connections – capital expenditure	-	-	-	-	4,830	4,830
New connections – operating expenditure	-	-	-	-	-	-
Requisition mains – capital expenditure	-	-	-	-	6,653	6,653
Requisition mains – operating expenditure	-	-	-	-	-	-
Infrastructure network reinforcement – capital expenditure	-	-	-	-	4,574	4,574
Infrastructure network reinforcement – operating expenditure	-	-	-	-	-	-
s185 diversions – capital expenditure	-	-	-	-	351	351
s185 diversions – operating expenditure	-	-	-	-	-	-
Other price controlled activities – capital expenditure	-	-	-	-	-	-
Other price controlled activities – operating expenditure	-	-	-	-	-	-
Total developer services capital expenditure	-	-	-	-	16,408	16,408
Total developer services operating expenditure	-	-	-	-	-	-
Total developer services expenditure	-	-	-	-	16,408	16,408

4P. Expenditure on non-price control diversions

for the 12 months ended 31 March 2021

	Water resources £000	Water network+ £000	Total £000
Non-price control diversions			
Diversions – NRSWA	-	385	385
Diversions – other non-price control	-	-	-
Total expenditure on non-price control diversion	-	385	385

9A. Innovation competition

	Current year £000
Allowed	
Allowed innovation competition fund price control revenue	827
Revenue collected for the purposes of the innovation competition	
Price control revenue collected from customers	827
Non-price control revenue (e.g. royalties)	-
Revenue collected from customers and transferred into the innovation competition fund	-

Bids accepted and awarded funding for innovation competition nr	Forecast expenditure on innovation projects funded through the innovation competition £000	Actual expenditure on innovation projects funded through the innovation competition in year £000	Difference between actual and forecast expenditure £000	Cumulative spend on innovation projects £000	Allowed future expenditure on innovation projects funded through the innovation competition £000	Expenditure on innovation projects funded by shareholders £000
-	-	-	-	-	-	-
Total	-	-	-	-	-	-

	Current year £000
Administration	
Administration charge for innovation partner	-

In the year, a total of £0.8 million was included in customer bills by South East Water in respect of the Innovation Fund. These funds were included in water revenue in table 1A and costs equalling this income were accrued, setting up a provision for the expected future distribution of these funds.

The total collected during the year in respect of the Innovation Fund was £0.6 million. No payments were made in the year in respect of the fund, so the full amount collected is held by South East Water awaiting distribution to successful applicants to the fund. Therefore, the closing cash balance for the year represents £39.8 million of general operations funds and £0.6 million in respect of the Innovation Fund.

In April 2021, Ofwat announced the results of the first Innovation in Water Challenge competition. South East Water Limited's project, titled CatchmentLIFE, was successful in the competition. The project will receive £178,000 in funding from the Innovation Fund in the 2021/22 financial year. However, no costs were incurred on this project during the year.

Transactions with associate companies

Loans from associate companies

Associate	Interest	Loan period	2021 £000
South East Water (Finance) Limited	Fixed rate	Repayable in March 2029	166,000
South East Water (Finance) Limited	Index linked plus 0.01% margin fee	Repayable in December 2041	130,000
	Indexation		47,369
South East Water (Finance) Limited	Index linked plus 0.01% margin fee	Repayable in December 2037	100,000
	Indexation		21,869

Interest and related fees payable to associate companies

Associate	Nature of transaction	Terms of supply	2021 £000
South East Water (Finance) Limited	Interest, RPI indexation and margin fees on intercompany loans (see below)	(See above)	21,293
South East Water (Finance) Limited	Ambac fees on £166 million	Monoline fees	340
South East Water (Finance) Limited	Facility fees	Commitment fees on loan facilities	255

Loans to associate companies

Associate	Interest	Loan period	2021 £000
South East Water (Holdings) Limited	LIBOR plus 2%	Repayable in July 2034	-

Interest receivable from associate companies

Associate	Nature of transaction	Terms of supply	2021 £000
South East Water (Holdings) Limited	Interest on intercompany loans of £136 million	LIBOR plus 2%	2,201

The intercompany loan to South East Water (Holdings) Limited, due for repayment in July 2034, was repaid early in December 2020. The repayment was funded by special restructuring dividends paid by South East Water Limited to its parent company, which resulted in a net nil cash impact.

The interest receivable of £2.201 million above constitutes the interest due on the aforementioned loan up to the date of repayment.

To the best of the directors' knowledge, all appropriate transactions with associated companies have been disclosed in compliance with condition I and RAGs 3.12 and 5.07.