



Annual Performance Report

Regulatory reporting 2022–23

from
**Southern
Water** 

The Southern Water logo graphic consists of three stylized, wavy lines in shades of blue, representing water waves.

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Regulatory information and annual performance report

Introduction

This report sets out the performance in 2022–23 of Southern Water's regulated business, as defined under our Licence¹, in financial terms and against our outcome and performance commitments.

This Annual Performance Report comprises four sections:

1. Regulatory financial reporting
2. Price control and additional segmental reporting
3. Performance summary
4. Additional regulatory information – service level.

The additional information required under RAG 3.14, including a copy of all the data tables, has been published alongside this document as an appendix and can be found at: southernwater.co.uk/our-reports.

This Annual Performance Report also includes:

- a Board Statement of Company Direction and Performance
- a statement in relation to our compliance with relevant statutory, licence and regulatory obligations and how we are taking appropriate steps to manage and/or mitigate any risks we face
- a Board assurance statement on the accuracy and completeness of data and information
- a Board assurance statement on Condition P (ring fence certificate).

These are supported by the publication of a data assurance summary, available at: southernwater.co.uk/our-reports. This sets out the results of the data assurance undertaken on our reporting and other key activities for 2022–23.

Board Statement of Company Direction and Performance

In the sections below we, as the Board of Southern Water, describe how we set the direction of the company and ensure it is delivering performance that meets customers' and stakeholders' expectations. In particular, we describe how the company developed the longer-term vision and Business Plan 2020–25 and how it has continued to engage with customers in the delivery phase of the plan. We describe our initial planning for the next regulatory period, 2025–30 and beyond. We also describe how we, the Board, monitor

performance and risk, how we have performed against our business plan objectives during 2022–23 and how performance affects returns to shareholders and the pay of our executive team.

Our vision and Business Plan 2020–25

Our purpose is to provide water for life to:

- enhance health and wellbeing,
- protect and improve the environment,
- sustain the economy.

To deliver on this we have set out an ambitious vision to create a resilient water future for customers in the South East.

Our vision and purpose reflect careful consideration and analysis of the key influences on our sector and within our region including:

- future challenges facing our sector, our region and society
- the future direction of regulation and Government policy
- the views of our stakeholders and customers.

Our stakeholders and customers played a key role in shaping our vision and our Business Plan 2020–25. We carried out over 42,000 direct interviews with customers and other stakeholders to inform our strategy and develop our plan. Our customers told us that as well as thinking about the challenges of the future, they have an expectation that we will continue to deliver on the basics – clean, high-quality drinking water and effective wastewater systems. These twin goals are reflected in our plan, which is built around five service-based outcomes and five transformational programmes.

As we deliver our plan we continue to engage with and capture insight from our customers every day, through our Water Futures 2050 and Water Futures 2030 customer panels, focused research on specific issues and our normal customer contact channels, social media and stakeholder discussions. For more details of how we engage with our customers, see section on Customer Expectations on page 5.

¹ We operate in accordance with an Instrument of Appointment (our 'Licence') issued, by the Secretary of State, to us as a water and sewerage undertaker under the Water Industry Act 1991. The Water Services Regulation Authority (Ofwat) has a duty under the Water Industry Act 1991 to ensure compliance with the conditions of this Licence.

Planning for the future

The next five-year regulatory period, from 2025–30, begins in less than two years' time. We are making good progress in developing our delivery strategy, which will be strongly embedded in a long-term, adaptive plan extending to 2050. As a first step in this process, in June 2022 we published a consultation document setting out our long-term priorities.

Based on our analysis of the long-term challenges we face and opportunities available to us, alongside our understanding of what our customers and stakeholders want from us, we identified four key priorities which will allow us to deliver our ambitions. These priorities include three direct outcomes where stakeholders will be able to see direct benefits for them and the region and one 'enabling' priority that will ensure the successful delivery of our vision.

Over the past year we also published our draft Water Resources Management Plan (dWRMP), which sets out how we will balance supply and demand for water over the next 80 years, and our first ever Drainage and Wastewater Management Plan (DWMP), which analyses the key wastewater

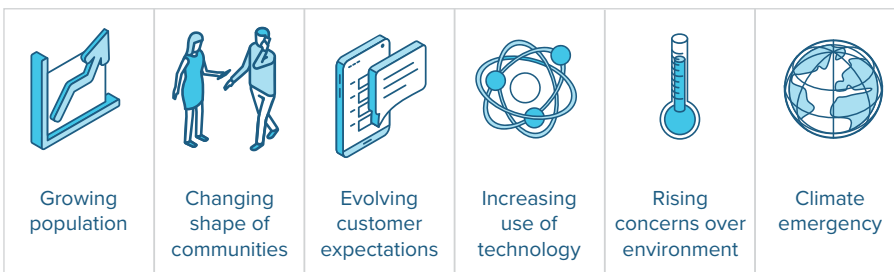
challenges and solutions in each of our drainage catchments over the next 25 years. These detailed technical plans set out how we will deliver our long-term priorities and ambitions.

Our dWRMP was developed in conjunction with the six other water suppliers operating in the South East of England, via the Water Resource South East group, ensuring it provides the best value for customers and the best outcomes for the environment. The plan was published for consultation in November 2022, with comments from customers, stakeholders and other interested parties being received by February 2023. The level of engagement with our draft plan is greater than ever, with 3,000 customers and stakeholders consulted during the preparation of the plan and 591 responses to the consultation received. This engagement ensures that our plan genuinely reflects the priorities of our customers and stakeholders.

Our Statement of Response to the feedback received and our updated revised draft plan will be submitted to Defra on 31 August 2023. We are planning a further consultation on our revised draft plan in the Autumn of 2023.

Figure 1 Our priorities for 2050

Trends



Challenges



Priorities



Enablers



Our DWMP was published in March 2023 following extensive engagement with customers and stakeholders. We held 33 stakeholder workshops (three in each of our 11 river basin catchments), five sets of regional webinars including one on water company funding, run jointly with the Environment Agency, and 41 wastewater system-based meetings to discuss specific risks and agree potential solutions. In developing the plan, we worked with over 75 other organisations across the South East who also have responsibilities for water management, planning and the environment, ensuring the plan was fully integrated.

In addition to these published long-term plans, over the past 12 months we also worked with the Environment Agency to develop the programme of environmental improvements, known as the WINEP (Water Industry National Environment Programme). The WINEP sets out the specific steps we must take to ensure that we meet the statutory and non-statutory environmental requirements that apply to water companies in England. The WINEP is closely aligned with the Government's 25-year Environment Plan as well as river basin management plans, the WRMP and DWMP.

What is very clear as we look across the WINEP, WRMP and DWMP, as well as the requirements of the Drinking Water Inspectorate, is that a very significant increase in the level of investment in our infrastructure is required to meet the expectations of our customers, stakeholders and regulators. Our current five-year plan includes an investment of £3.9 billion in the operation, maintenance and improvement of our assets. To meet all the requirements of our long-term plans it is likely that we will require 50-100% more investment during the next five-year period.

This level of investment will require significant increases in customer bills up to 2030. We are working closely with our customers and regulators to ensure that investment is appropriately prioritised between the 2025–30 regulatory period and subsequent periods. We are also exploring innovative ways in which we can work with third parties to deliver some of the investment in a way that provides greater value and reduces the immediate impact on bills.

To ensure bills remain affordable for all of our customers we will also need to enhance the level of support that we provide. We are looking at how more sophisticated pricing might help ensure bills remain affordable for all.

We will submit our five-year plan to Ofwat in October 2023, with final decisions coming from Ofwat in December 2024. As we develop the 2025–30 plan we continue to work closely with our customers and stakeholders, as well as our independent Customer and Communities Challenge Group. More details on how we work with customers to ensure we are meeting their needs, both in our plans and through the delivery of our services are provided in the section on Customer Expectations below.

Delivering for our customers

We are now three years into the delivery of our Business Plan 2020–25. These three years have been extraordinarily challenging for us and our customers. Having emerged from the COVID-19 pandemic, which dominated all our lives for the first two years, we have subsequently been faced with a cost-of-living crisis, caused by the rapidly escalating cost of energy, food and other household goods.

We know how tough things have been for many of our customers during this period. In recognition of this our Board took the decision to limit our price rises for 2023–24 to no more than the rate of inflation, below the level allowed for by the Ofwat price controls. Nonetheless, this still meant a rise in bills that was larger than in recent years. As a result, we took the decision in December 2022 to significantly increase the level of support provided to those struggling the most. As part of a £98 million package of measures, we increased the minimum level of discount we provide to customers on our Essentials tariff from an average of 20% to at least 45% (with up to a 90% reduction for those most in need) and committed to increasing the number of customers we support via the discounted tariff from 104,000 to 125,000.

Our Business Plan 2020–25 includes some ambitious targets to improve the service that we provide to customers by 2025. These include:

- a 15% reduction in leakage and a 23% reduction in water supply interruptions
- a 20% reduction in both internal and external sewer flooding incidents and an 80% reduction in the number of pollution incidents
- generating 24% of our energy from renewable sources
- further increasing the number of beaches achieving Good and Excellent water quality status
- improving the health of the rivers in our region.

Details of our performance against our targets for 2022–23, are provided in the Strategic Report section of our Annual Report and Financial Statements. In addition, details of our performance against our commitments are set out in Tables 3A-E on pages 55 to 60.

The past year has seen small improvements in performance across a large number of areas including internal sewer flooding, which reduced by 19% over the year; water and wastewater treatment works compliance, where the number of works not meeting their discharge permit requirements reduced from seven to six; pollution incidents, which reduced by 4%, on top of the 7.5% reduction delivered last year; and unplanned water outage, which fell from 7.2% to 6.4% over the year. However, there were setbacks, for example, leakage increased by 5%, and the duration of supply interruptions increased from nine minutes to over an hour. This was predominantly due to several very large one-off incidents at the Isle of Sheppey (which contributed more than 30 minutes to the total), Rumfields in Kent, and in Yew Hill, Hampshire.

Overall, our performance has fallen short of the very challenging performance targets that Ofwat set within its Final Determination (the basis on which our plan for 2020–25 was approved). As a result we have incurred significant penalties under Ofwat’s Outcome Delivery Incentive (ODI) regime. Penalties for missing performance targets in this third year totalled £44 million^{1,2}, which will be reflected in reductions in customer bills in 2023–24. This is higher than the 2021–22 total of £42 million, partly reflecting the progressive tightening of performance targets.

We know that despite the improvements seen in a number of areas, our performance and the rate of improvement is not fast enough. This is why, in April 2023 we published our Turnaround Plan for the last two years of this regulatory period 2023–25³. This plan is based on detailed analysis of the root cause of our performance challenges and sets out four clear outcomes that we are promising to deliver, each with a set of associated performance measures. Publication of the plan underlines our commitment to doing better for our customers and the environment and means that stakeholders and customers can hold us to account for delivery against our promises.

We are currently in discussions with all the company’s shareholders with respect to additional funding in the near term; see page 7 for further information regarding this funding and its effect on going concern, including the related material uncertainty.

The Board closely monitors the delivery of operational improvements and tracks the performance against our regulatory commitments. It does this through a performance dashboard which is focused on those performance measures that have the greatest customer, stakeholder and environmental impact. The Board is supported by the Executive Committee, which focuses on tracking performance through leading indicators, identifying corrective actions where necessary and driving our focused performance improvement plans.

Aligning performance and rewards

Ofwat has put in place mechanisms that provide financial and reputational incentives for us to deliver more of what our customers want, for less.

We have 47 performance commitments, agreed as part of the price review process, that we report on annually (see Section 3 of this report). Reporting our performance in this way to stakeholders provides a reputational incentive to meet our commitments.

In addition, 31 of our performance commitments include financial penalties and rewards associated with delivering for our customers. If we beat our targets, delivering more of what customers want, we can earn rewards, which means shareholders enjoy higher returns. If we fail to meet our performance targets we can incur penalties, meaning shareholders receive a return below market rates. These incentive mechanisms provide a strong alignment between the interests of our shareholders and our customers. As noted, for the 2022–23 reporting year we have incurred total penalties of £44 million.

We are also strongly incentivised to deliver efficiently. At each price review Ofwat assesses the efficient costs for delivering our business plan. If we are able to beat these, we share the benefits of that outperformance with our customers. Between 2020–25, for every pound that we save, around 64 pence is returned to customers via lower bills, while 36 pence is retained by the company. If we overspend, we must bear 64 per cent of the cost, while customers share 36 per cent.

¹ Including estimated penalties for C-MeX and D-MeX comparative measures

² All ODI penalties are expressed in 2017–18 prices, consistent with the basis of Ofwat’s final determination

³ www.southernwater.co.uk/media/8235/6579_ofwat_company_turnaround_plan.pdf

During the year our employees were incentivised to deliver for customers through a company-wide bonus scheme, 'yourBonus'. The bonus scheme is based on company performance against seven metrics, five of which related to delivering excellent service to our customers and improving our environmental performance. The remaining two measures are based on the efficient delivery of our services and the delivery of our Health and Safety Transformation Plan. The bonus earned by each employee was dependent on the delivery of these company-wide objectives as well as their individual performance rating. The scheme aims to align the incentives for all employees with the interests of our customers.

We are committed to fully complying with Ofwat's code of practice for executive remuneration. Our executive remuneration policy closely links with overall company performance for customers, stakeholders and communities. For 2022–23, 50% of the measures used to determine variable annual pay were directly linked to customer outcomes, based on performance against four of our ODIs – pollution, leakage, internal sewer flooding and C-MeX. The remaining four measures focus on health, safety and wellbeing (lost time accident rate and progress on our Health & Safety Action Plan), efficient operating expenditure and personal objectives.

Long-term incentive plan objectives also focus on delivery for our customers and the environment, being based on ODI performance, delivery of capital schemes (two measures), environmental performance (two measures) and outcomes related to the next price review, PR24.

Full details of our executive remuneration policy and details of its application in respect of 2022–23 are set out in our annual report southernwater.co.uk/our-performance/reports/annual-reporting.

As well as ensuring the right incentives are in place, it is important that we strike the right balance between providing a fair return to shareholders and investing for customers. Our dividend policy for the 2020–25 period incorporates a wide range of financial and customer performance measures. It also explicitly considers the financial resilience of the company and whether any financial outperformance should be re-invested to benefit our customers.

To assist in the financing of planned expenditure the company expects to receive £375 million of new equity, with cash expected to be received by the end of October 2023.

In addition, following the announcement by Fitch on 7 July 2023 to downgrade the Class A Unwrapped Debt of the company to BBB (negative outlook) which resulted in a credit ratings Trigger Event the company is unable to make dividend payments until it comes out of Trigger. We expect to remain in Trigger until the end of this regulatory period at March 2025.

Ofwat board leadership, governance and transparency principles

In 2019 Ofwat published its Board leadership, transparency and governance principles ('Ofwat Principles'), which represented a major update of the principles published in 2014 and these incorporate many of the principles and provisions of the UK Corporate Governance Code published by the Financial Reporting Council (FRC) in July 2018. In addition, since July 2019, meeting the objectives of the Ofwat Principles has been a requirement under Southern Water's licence. Accordingly, we seek to apply both the Ofwat Principles and the relevant principles and provisions of the UK Corporate Governance Code.

In addition, we continue the work we do to satisfy Condition P of our Licence. This requires us to demonstrate that the Board has made appropriate diligent enquiry into the activities of the business and can evidence that the company will have sufficient financial resources and facilities, management resources and methods of planning and control in place to meet our statutory duties. The Condition P requirements are also a key part of our Section 19 Undertakings to Ofwat in connection with our historic misreporting (see below) and was subject to external assurance from our external auditors (Deloitte LLP).

Annual risk and compliance statement

The annual risk and compliance statement describes the steps we have taken to understand and meet our customers' expectations and to ensure we meet our statutory and regulatory obligations, as well as the expectations of our key regulators, Ofwat, the Environment Agency and the Drinking Water Inspectorate. It also sets out how we manage and mitigate any compliance risks identified.

Customer expectations

Our Business Plan 2020–25 was based on the results of engagement with more customers than ever before (over 42,000 direct interviews). To drive a deeper understanding of customers we used innovative techniques such as ethnographic mobile apps and integrated 'willingness to pay' surveys to provide a single triangulated view of our customers' preferences.

We continue to engage extensively with customers to ensure that our plans and approach to delivery meet their needs and expectations. Through 2022–23 a key focus of our insight has been working with customers for the next Business Plan 2025–30, ensuring we have robust insight for understanding what our customers want from us now, and in the future.

Our Water Futures 2030 (household customers) and 2050 (young people) consumer groups continued to be central to our engagement with customers over the past year. We introduced additional panels to include businesses, customers in vulnerable circumstances and diverse culture leaders to represent communities where English is not their first language. The groups follow best practice guidance, as set out by the Consumer Council for Water (CCW), to provide a continuous dialogue on both our current delivery and future planning.

We also continue to collaborate closely with other water companies, especially in the South East, running joint projects and sharing the learning from our insight. Our work with leaders where English is not their first language is then helping with a joint Ofwat Innovation project. It is exploring how to help faith communities reduce their water consumption. This joint project then runs through 2023 in partnership with a number of other water companies.

A lot of our engagement now happens through online platforms, as customers have become more comfortable with the technology. We continue to use this opportunity to run joint engagement events, where customers and decision makers come together in joint online workshops. Over the past year, these sessions have included our Chief Customer Officer, Regulatory Director, Asset Strategy Director and heads of departments from our planning teams. These events have been crucial in bringing the voice of the customer to life for leaders within Southern Water.

As we enter 2023–24, customers are concerned about the impact of increases in the 'cost-of-living', and a real need for improvements in terms of how we protect the environment. With such a breadth and depth of insight and continuous channels of engagement, our focus is now on making insight more accessible across the organisation as well as to our partners.

Statutory and regulatory obligations

Our purpose is to deliver water for life to enhance health and wellbeing, protect and improve the environment and sustain the economy. In order to achieve this, we must deliver on our customers' expectations. As a regulated service provider, our primary obligations and duties are set out in the Water Industry Act 1991, the Drinking Water Regulations and our Instrument of Appointment (the Licence). These set the standards under which we must provide our services.

We are committed to driving structural and cultural change to support the development of a transparent and ethical compliance framework. We operate our Modern Compliance Framework (MCF), introduced six years ago, which has become our 'Business as Usual' approach to managing compliance. The framework brings together key elements of risk and compliance (see Figure 1), in terms of our regulatory obligations, our policy framework, ethical business practice and our work to manage the quality and transparency of our regulatory reporting. This is supported by strong governance in key areas of our operations (most notably in our monitoring and reporting programmes) and is backed up with strong training programmes to ensure good practice is embedded in all areas of the company.

Our dedicated risk and assurance, water quality and environment quality teams have a clear role and responsibility to provide a separation of duties in monitoring key performance metrics of drinking water quality and wastewater performance. These teams also provide 'second-line' internal assurance of our front-line teams and also manage key 'third-line' external assurance of key aspects of our front-line performance.

In the past, the company has not met its own high expectations, and our performance has not been as good as our peers in the industry or as good as our customers might expect. We continue to work with our regulators, Ofwat, the Drinking Water Inspectorate (DWI) and the Environment Agency (EA) to implement improvements to our performance and reporting, and to fully embed these changes.

Figure 1 – Performance Improvement under our Modern Compliance Framework



As explained below, Ofwat and the EA continue to scrutinise our response to their joint sector-wide investigation into the management and operation of wastewater treatment works.

Ofwat’s investigation

As reported previously, Ofwat undertook an investigation into our wastewater reporting that led to a decision to impose a financial penalty of £3 million. In addition, we agreed to make significant customer bill rebates, totalling £122.9 million (in 2017–18 prices), between 2020–25. On 8 October 2019, we signed formal Undertakings pursuant to Section 19 of the Water Industry Act 1991 relating to the numerous changes we have put in place, and are putting in place, to ensure that the issues identified in the investigation have been stopped and cannot be repeated.

The Undertakings contain a wide range of corrective actions and interventions across seven themes:

- A. Customer redress measures;
- B. Technical review of Wastewater Treatment Works;
- C. Organisational compliance process measures;
- D. Organisational cultural change measures;

- E. Ensuring Transparency;
- F. Condition P Certificate Assurance Undertaking; and
- G. Reporting on Compliance with the Undertakings.

We continue to make progress on all the Undertakings, with most now substantially complete. Our focus has moved to embedding the improvements and monitoring effectiveness of changes made.

Compliance with the Section 19 Undertakings is subject to a formal assurance regime which is reported to our Board and then to Ofwat on a regular basis. In our February 2023 update to Ofwat we were able to report that the actions arising to ensure compliance have either been completed or are on track to be fulfilled within the five-year period of the undertakings.

In addition, the Section 19 Undertakings require us to provide additional assurance on Board compliance with Condition P of our Ofwat licence (please refer to page 16 for more detail).

The Environment Agency (EA)

Like other wastewater operators, in the normal course of operations we occasionally face investigations by the EA following incidents. In addition to those, the company was subject to a detailed investigation regarding permit breaches at some of our wastewater treatment works during the period 2010–15. It resulted in us being fined £90 million in July 2021. We continue to deliver change programmes to address these historic failures.

The EA continues to investigate the failures covered by the Ofwat investigation referred to above and is conducting a sector-wide investigation into flow compliance.

The EA recently released the Environmental Performance Assessment (EPA) for 2022 in its annual report on the environmental performance of the nine English water and sewerage companies. The end-of-year performance report outlines that we have improved our environmental performance rating from one star in 2021 to two star in 2022. As a company committed to protecting the environment and serving our customers, we were pleased with the improvement in the assessment and we will continue to drive through the changes necessary to positively impact our performance.

The assessment of the Supply Demand Balance Index (SDBI) water supply resilience measure increased from 'red' in 2021 to 'green' in 2022. In addition, our discharge compliance measure also increased from 'red' to 'amber'. The improvement in both these measures moved our assessment from one star to two star.

The two star rating includes the EA's assessment on the number of total pollution incidents and the number of serious (category 1 and 2) pollution incidents, both of which have been assessed as a 'red' rating. We are disappointed with the level of significant pollution incidents within 2022 (albeit an improvement on 2021) and continue to respond with extensive improvements in the way we operate. This includes changes to our operational control centre to identify more swiftly those incidents with the potential to become significant, enabling a more rapid response. The reported number of 358 total (category 1-3 pollution incidents) in the EPA assessment include a number of 'retrospective pollutions' which we understand other companies may not have reported as part of this process. We are keen to ensure that the figures being assessed in the EPA exercise are comparable to those from other companies.

We are committed to reducing pollutions, and in our recent Turnaround Plan, we outline how we want to reduce pollution incidents by 79% in the next two years. While we have made some improvement in

reducing pollutions, we are not where we need to be. Our Pollution Incident Reduction Plan (PIRP) shows how and where we will focus our attention to achieve our goal. In 2020 we announced our PIRP, working in partnership with the EA.

We are now in the fourth year of the plan. We are aiming to improve our pollution performance by focusing on asset resilience and escape prevention, while ensuring that we enable learning and sharing of best practices. The root cause analysis we carried out in the third year has shown us which activities will work best to reduce pollutions and flooding in key areas of our region. This work will reduce the effects of pollution and help protect our 700 miles of coastline and the precious chalk streams of the Rivers Test and Itchen.

The digitalisation of our sewer network is a key part of our plan to reduce pollutions. The installation of industry-leading sewer level monitors has already begun, with 23,000 monitors being installed by the end of 2022 in an ongoing programme. These smart monitors can predict where bursts may occur, and we will start to see the benefits during 2023.

To increase pumping station resilience, as part of our root cause analysis we carried out Platinum Health Checks of the assets linked to most of the pollution incidents. A total of 280 pumping stations were checked, leading to remedial works being carried out on 52 and the remainder being effectively dealt with by our new in-house team implementing the wastewater pumping station (WPS) resilience workstream.

The fourth iteration of the plan will be published shortly.

We remain industry leading in our approach to self-reporting of pollution incidents and that is helping improve the transparency of how we identify and act when things go wrong. The EA has recognised this, in particular of discharges, spills and pollutions during storm conditions. This is underpinned by detailed analysis of all pollutions and spills as part of improvements implemented. This continued good performance and EA feedback is evidence of how embedded our pollution reporting improvements have become. The EA also recognised improvements in pollutions and treatment and overall reduction in risk across the assets. Continuation of work in these areas will support improved future performance.

The Environment Act 2021, which was passed into law in November 2021, sets out the requirement for all water companies to 'secure a progressive reduction in the adverse impacts of discharges from storm overflows'. At the same time, the law also requires the government to publish a plan to reduce

sewage discharges from storm overflows by September 2022 and report to Parliament on the progress towards implementing the plan. We welcome the strengthening of the Act's requirement and are actively participating within the industry and proceeding with action and investment with an objective, subject to funding, of an 80% reduction in storm releases by 2030.

We are fully aligned with the ambition set out by the Government and Ofwat, over the past year; that our impact on the environment requires sustained focus and that the reduction in the use of storm overflows is at the heart of that ambition. We remain fully supportive of the expectations set out in the Environment Act, the Strategic Policy Statement, and the Storm Overflow Discharge Reduction Plan.

Our overall strategy to reduce our environmental impact is to deliver interventions that: improve wastewater processing and capacity within our systems; increase investment in our infrastructure; and continue work to improve water quality monitoring.

We continue to focus our effort on reducing the impact our operations might have on the environment. The Clean Rivers and Seas Task Force, established in November 2021, remains a dedicated team responsible for driving our ambitious targets, and is the delivery vehicle for a number of Pathfinder projects that are piloting initiatives across the region. To date, it has worked with a number of partners including action groups and local councils.

We have already invested £5 million to implement these projects, which included a series of targeted regional trials aimed at helping to 'slow the flow' of rainwater and groundwater entering the network. We are one year into our two-year programme of Pathfinders, that we committed to in our update in April 2022, and with the acceleration of funding this work is being expanded to March 2025.

Subject to Ofwat's approval, we are planning to invest up to £50 million between now and 2025 to reduce up to 600 spills. This will help us learn more over the next two years so that we invest, as part of the Water Industry National Environment Plan.

Increased monitoring is essential to improve our wider environmental performance and to achieve a significant reduction in the use of storm overflows. We continue to invest in improvements to the timeliness and accuracy of our data.

Event Duration Monitors (EDMs) remain an important part of monitoring the quality of our waters and providing accurate information on sewage discharges. We fully support the

Government's aim of having EDMs installed at 100% of storm overflow sites and are continuing to make progress with EDMs installed at 98% of our sites. This has translated to 88% availability with effective monitoring – in line with Ofwat reporting methodology. We are working actively to update our coverage on the final 14 overflows not currently covered by an EDM; each of these are proving difficult due to their location but are being worked through in due course. We are also planning to expand our EDM coverage on Beachbuoy to include all storm overflows by the end of March 2024.

Our Beachbuoy tool provides near real-time information about storm release activity near coastal bathing waters through an interactive map, pop ups and release table. This 24/7 reporting provides information about any release and its frequency. We regularly listen to feedback from our Beachbuoy User Group which includes councils, campaign groups and bathing water users. Following feedback, we released an upgrade to Beachbuoy in September 2022 to account for tidal conditions. The system now uses extensive tidal modelling to work out whether a bathing water will be impacted by a storm release. Bathing waters will now only show a red flag on the online tool, if the modelling determines that it will be impacted.

To ensure transparency, all storm releases are still recorded in the data table on Beachbuoy and when the bathing water icon is clicked, all associated outfalls will indicate if any have released. To speed up our notification to the public, we have improved our processes to confirm whether a release is genuine/not genuine. We are planning to include all storm overflows in Beachbuoy by the end of March 2024.

We are also committed to assisting the EA with its investigation into sampling compliance and reporting issues between 2013 and 2017 (inclusive). As the investigation is ongoing, we are not able to say any more about it at this time.

On 18 November 2021 the EA and Ofwat announced that they had launched a joint investigation into the operation of wastewater treatment works across the industry. We will continue to be open and transparent and are committed to working with the EA and Ofwat constructively throughout the course of the investigation.

The Drinking Water Inspectorate (DWI)

We continue to progress the transformation of our drinking water quality performance. Our Compliance Risk Index (CRI) improved slightly in 2022 but was above the industry average score. We remain in the bottom quartile for this metric compared with the rest of the sector and further improvement is still required.

Our provisional Event Risk Index (ERI) metric is significantly worse than last year. The score is dominated by two events which represented more than 85% of the score which both related to long duration issues with assets. Excluding these two events ERI would have been on a par with the 2021 score. In December and February we had two significant loss of supply events in Hampshire which were both the subject of internal investigations and the results of these investigations were shared with the DWI.

We continue to work closely with the DWI on our transformation programme, holding regular liaison meetings to review progress on improvement schemes as well as ad hoc communications.

The Public Health and Culture Notice closure report was submitted to the DWI in October 2022 although improvement work in this area is still to be undertaken voluntarily by the company.

During 2022 we undertook reviews of the capital works plans at our four largest strategic water treatment works: Hardham; Burham; Testwood and Otterbourne. The reviews took a bottom-up approach to understanding potential water quality risks within the wider context of the supply system and then programming the improvements to reduce risk. These reviews resulted in the 'Supply Resilience Enhancement Programme' which the DWI incorporated into four Final Enforcement Orders (FEO) issued in February 2023.

The DWI also issued FEOs for work at Timsbury and Twyford works in February 2023 due to delays in the delivery of the improvement programmes.

Our treated water reservoir programme has continued to work towards a maximum 10-year inspection frequency by the end of the AMP. A number of specific sites have been identified as needing to have capital works completed in order for the reservoir to be drained and inspected without interrupting supply and site-specific notices have been issued.

On 9 January 2023, we accepted a caution from the DWI following the supply of water to consumers which was unfit for human consumption relating to an incorrect network connection which resulted in taste and odour complaints at two properties in 2021. We have since changed our policies, procedures and training to prevent a recurrence.

Reporting our performance

We provide a significant amount of data to the EA and Ofwat about the performance of our assets, and any wastewater or sewage discharges we make into the 'water environment' such as rivers, streams and coastal waters. We are committed to transparent reporting of high-quality data that can be trusted by our customers, stakeholders and regulators.

Following historic failings in the quality of our reporting to our regulators, we continue to embed our programme of improvements to ensure our regulators and other stakeholders can trust the data that we report. These improvements have been led by our Risk and Assurance, Water Quality and Environment teams ensure compliance reporting to our regulators is subject to sustained internal review and assurance. Further information on this programme can be found in our Data Assurance Summary 2022–23, available at: southernwater.co.uk/our-reports.

We regularly review performance information against a wide range of measures. Reporting to the Board and the Executive Committee (ExCom) focuses on delivery of our regulatory and statutory obligations. For the business plan period 2020–25, this information is provided to the Board by way of a detailed performance dashboard, including a selection of our business plan performance commitments and additional regulatory targets.

The Audit Committee has monitored the completion of a risk-based programme of assurance activities during the year, as part of a three-year rolling programme, covering the practices, procedures and systems used to secure compliance with our statutory obligations. This included a review of our compliance with our Instrument of Appointment, which was presented to the Audit Committee in March 2023.

In response to new guidance from Ofwat in November 2020 we published, as part of our Annual Performance Report, a Board assurance statement, stating that the data and information provided is accurate and complete and setting out any exceptions to this. This continues to be embedded in our approach and our latest statement is included on page 17.

Each year we engage with our customers, employees and stakeholders to help us identify any risks, strengths and weaknesses associated with our reporting. We published the findings of this exercise in November 2022, with an invitation to stakeholders to comment on the findings. The publication sets out how we would respond to stakeholders' feedback and detailed how our corporate assurance practices would meet our reporting compliance obligations. Our Final Assurance Plan was published on 31 March 2023. It set out how we planned to assure the financial and non-financial information that we publish in our Annual Performance Report.

In line with the Final Assurance Plan, KPMG LLP, as our independent non-financial data assurer, completed the limited assurance under ISAE (UK) 3000 of selected Performance Commitments and Outcome Delivery Incentives (ODIs). KPMG LLP provided Southern Water with an unqualified

ISAE (UK) 3000 opinion for 2022–23 over the selected Performance Commitments reported in Section 3 of the Annual Performance Report marked with the symbol Δ for the calendar year ended 31 December 2022 and the information marked with the symbol * for the financial year ended 31 March 2023. This is the third year that KPMG LLP has issued an unqualified ISAE (UK) 3000 opinion over certain Performance Commitments and ODIs, reflecting their third year as our non-financial assurance partner.

A programme of process and control improvements has been worked through over the past six years and continues into the current year. These have been focused on key data returns to Ofwat, DWI and the EA and include improvements in our reporting control environment. Our work over the past two years has focused on the maturity of first-line controls; this reflects the embedment and maturing of our reporting capability.

The outputs and recommendations from the KPMG LLP technical assurance have demonstrated continued improvements being made across the board, with increased stakeholder engagement, continued focus on the quality of internal documentation and increased focus on first-line controls. Areas of further improvement have been identified, including to the first-line control. For more detail see our Data Assurance Summary 2022–23.

Senior managers and ELT members are accountable for the provision and sign-off of non-financial information from their business areas. This includes ensuring adequate procedures and processes are in place for data collection and reporting. Data providers are accountable for submitting accurate data to set timescales. Subject matter experts within the relevant business areas are accountable for ensuring that this data, and the processes and procedures used in collating it, comply with Ofwat's reporting requirements. This process is managed through our Ofwat Compliance Framework (OCF), which is a system of controls that has been rolled out for data capture, collation and reporting within the business to make sure information used to measure compliance is complete, accurate and reliable. The OCF is in its third year of existence and is in place for business plan period 2020–25. Details of the assurance undertaken on our non-financial regulatory reporting by KPMG LLP are provided in their assurance opinion on page 68.

We have seen improvements in quality of our reporting to the DWI, the EA and Ofwat. These improvements are part of an ongoing programme that will continue through the current business plan period and beyond.

All members of the ELT are required, every six months, to provide a declaration that they and their teams are fully compliant with our procedures and controls for areas of the business for which they are accountable. An action plan is required to address any areas of non-compliance. We have made improvements to this 'Statement of Compliance' process during the year. The updated process includes additional internal assurance and co-ordination of resulting action plans, and provides a compliance maturity assessment of each directorate. The Statement of Compliance is now in its ninth edition and is a key input into our reporting and control improvement plans.

As required by Ofwat, an audit was also performed on sections 1 and 2 of the Annual Performance Report, (excluding elements of table 1F as set out in the audit opinion on page 50) by our auditor, Deloitte LLP together with agreed upon procedures in relation to sections 4 to 9.

In approving the Annual Report and Financial Statements, each director has confirmed that he or she has taken all steps that he or she ought to have taken as a director in order to be aware of any relevant audit information and to establish that our auditor is aware of the information. So far as the directors are aware, there is no relevant audit information of which the company's auditor is unaware.

Managing risks

The Board confirms that the company has appropriate systems and processes in place to identify, manage and mitigate its material risks.

Risk management is a core component of our wider governance and internal control framework, which provides the overarching structure through which the company conducts its business.

Risk is inherent in our business and we face a diverse range of risks and uncertainties that cannot be completely eliminated. The purpose of our approach to risk management is to support better decisions through an improved understanding of risk. Those risks that have the potential to have a material impact on our company and our ability to deliver on our strategic objectives are our principal risks. Our risk governance model ensures that we can manage, monitor and report on our principal risks to maintain a resilient business.

Southern Water's approach to risk management is designed to provide a clear and consistent framework for managing and reporting risks associated with our operations, to executive management and to the Southern Water Board.

The framework seeks to promote better decision making, avoid incidents and encourage the best outcome for the company and our customers by allowing us to:

1. understand the risk environment, identify the specific risks we face and assess the potential exposure for Southern Water.
2. determine how best to manage identified risks to balance overall potential exposure.
3. take action to manage the risks we do not want to be exposed to, ensuring our resources are effectively and efficiently prioritised and used.
4. report to the Audit Committee and to the Board on a periodic basis on how significant risks are being managed, monitored, assured and the improvements that are being made.
5. use our analysis to help the Board to define the company's appetite for the range of risks and monitor and report risks against the desired risk appetite.

Across the company our risk management approach is embedded within the business units and their business processes. We have established a risk management approach that provides a consistent basis for measuring risk to:

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

All areas of the company review significant risks and business processes to help inform and enable risk-based decision making. As part of Southern Water's annual planning process, the Executive and Board review the business' principal risks.

Southern Water's approach to risk management adopts the 'three lines of defence' model in which risk ownership responsibilities are functionally independent from oversight and assurance.

- Primary responsibility for risk management lies with the business. The risk owner is the first line of defence. An important part of the role of all staff throughout Southern Water is to ensure they manage risks appropriately.
- The Risk Management function forms the second line of defence and provides independent and objective review and challenge, oversight, monitoring and reporting in relation to Southern Water's material risks.
- Independent external assurance and the Internal Audit function act as the third line and provide independent assurance on the business control environment and the effectiveness of the wider system of internal control.

Risk oversight and governance

To successfully embed risk management across Southern Water, the risk management process is supported by a governance structure that defines roles and responsibilities at each level of the company. The Board has overall accountability risk management but discharges this role through the Audit Committee, who oversee and advise on enterprise and corporate risks, and the newly formed Health and Safety and Operational Risk Committee who oversee and advise on operational risk.

Role of the Board

The role of the Board is to promote the long-term sustainability of Southern Water and its responsibilities to its shareholders, customers, employees, and the communities in which it operates and it has overall responsibility for risk management within the company.

The Board is responsible for maintaining an effective risk culture and is committed to:

- reviewing, endorsing and monitoring Southern Water's approach to risk culture and conduct
- forming a view on Southern Water's risk culture and the extent to which it supports the ability of Southern Water to operate consistently within its risk appetite.

The Board defines our Risk Appetite, enabling us, in both quantitative and qualitative terms, to judge the level of risk we are prepared to take in achieving our overall objectives.

Our Risk Appetite is directly aligned to our principal risks. The Risk Appetite for each of our principal risks, underpins our governance and reporting framework and is subject to regular review by the Board. The alignment of principal risks with Risk Appetite allows for an informed analysis and discussion of our risk position and has provided the Board risk insight to key decisions.

The Board ensures the oversight and monitoring of our risk culture, risk appetite and risk management activities through the Audit Committee.

The Audit Committee is responsible for the review of our internal financial control systems that identify, assess, manage and monitor financial risks, and other internal control and risk management systems. They advise the Board on the company's overall risk appetite, tolerance culture and strategy, taking into account the current and prospective regulatory, legal, political, macroeconomic and financial environment with the Board retaining overall ownership and approval.

The Audit Committee oversees and advises the Board on the current risk exposure of the company and longer-term strategic risks to determine our future risk strategy. The Audit Committee has a key role in risk assessment, including:

- reviewing the company's overall risk assessment processes for the company's enterprise and corporate risks that inform the Board's decision making, ensuring both qualitative and quantitative metrics are used;
- reviewing regularly and approving the parameters used in these measures and the methodology adopted; and
- setting a standard for the accurate and timely monitoring of large exposures and corporate risk types of critical importance.

In addition, the Audit Committee reviews the company's capability to identify and manage new and emerging risk types and reviews reports on any material breaches of risk limits and the adequacy of proposed corrective actions.

The Health and Safety and Operational Risk Committee is responsible for the oversight and assessment of the overall adequacy and effectiveness, of the health, safety and wellbeing policies, strategies, processes and controls, operational risk management, and compliance with relevant legal and regulatory requirements. The Board retains overall ownership and approval.

The Health and Safety and Operational Risk Committee has a key role in:

- reviewing the areas of significant corporate and individual health, safety, wellbeing and operational risk and whether the executive is managing these risks effectively, including via the supply chain;
- reviewing the company's health, safety and wellbeing performance;
- reviewing operational risk and risk management of information security, information governance, water, wastewater and customer services;
- reviewing the scope, and results of any health, safety, wellbeing, information security, information governance, water, wastewater and customer operational risk audits; and
- considering the findings of internal and external investigations and executives' response.

Board risk and compliance statement

In making the risk and compliance statement, the Board confirms that the company:

- considers that it has 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 fully meet its obligations; and
- has appropriate systems and processes in place to allow it to identify, manage, mitigate, and review its risks.

Signed on behalf of the Board



Stuart Ledger
Chief Financial Officer

14 July 2023

Regulatory matters

The following regulatory accounting statements and required regulatory information are provided to comply with Condition F of our Licence, which requires that regulatory accounts are prepared in accordance with the Regulatory Accounting Guidelines issued by Ofwat.

There are differences between statutory accounting reporting frameworks, International Financial Reporting Standards and the Regulatory Accounting Guidelines. Where different treatments are specified under each, the Regulatory Accounting Guidelines take precedence.

A particular point of definition is worth noting. Southern Water Services Limited is appointed by the Secretary of State to be a water and wastewater undertaker – the activities covered by the appointment are the ‘Appointed Business’. Southern Water Services Limited has other functions and activities which are not covered by the appointment as a water and wastewater undertaker. These activities are termed the ‘Non-Appointed Business’.

Assets, rights and resources (Condition P14)

Under paragraph 14 of Condition P of the Licence, the company is at all times required to ensure, so far as is reasonably practicable, that if a special administration order were made, the company would have available to it sufficient rights and resources (other than financial resources) to enable the special administrator to manage the affairs, business and property of the company. In the opinion of the directors, the company was in compliance with that requirement as at 31 March 2023.

Ring-fencing Certificate and statement (Condition P30)

In order to meet the Licence Condition P Certificate requirements as supplemented by the Ofwat Section 19 Undertakings, the Board needs to be able to clearly evidence the level of diligent enquiry that it has undertaken. To support this process the Southern Water Board signs off Condition P Assurance Statements demonstrating it has discharged its responsibilities and takes accountability for its diligent enquiry into the principal risks facing the business, and most importantly in the context of the Section 19 Undertakings, the wastewater business.

These statements were assured in June and July 2023 and were signed off by the Board as part of approvals for the Annual Performance Report to Ofwat.

To provide the Ring-fencing Certificate required by Licence Condition P30 and meet the Ofwat Section 19 undertakings the Southern Water Board needs to be able to clearly evidence the level of diligent enquiry that the Board has undertaken. This is outlined in detail in the Board Assurance statement (see Appendix 4).

In the Board Assurance Statement, the directors declare that, in their opinion, subject to the successful completion of the equity raise of £375 million as detailed on page 7.

i) The company will have available to it sufficient financial resources and facilities to enable it to carry out its regulated activities (including the investment programme necessary to fulfil its obligations under its appointments)

ii) The company will have available to it:

- a) financial resources and facilities
- b) management resources; and
- c) methods of planning and internal control

which are sufficient to enable it to carry out those functions for a period of at least twelve months.

A specific paper on the Condition P statement is presented for sign off by the Southern Water Board and includes the finalised Board Assurance Statements as detailed in Appendix 4. The Board Assurance Statement is subject to external assurance from our auditor, Deloitte. As part of our Section 19 commitments, their report will be provided separately to Ofwat. This sign-off process happens in parallel with the Board sign-off of an assurance statement on the accuracy and completeness of the data and information (financial and non-financial) submitted to Ofwat as part of our Annual Report and Annual Performance Report submission (see Appendix 3).

Directors' responsibilities for the preparation of the supplementary regulatory accounting statements and disclosure of information to auditors

In addition to their responsibilities to prepare accounts in accordance with the Companies Act 2006 and to disclose all relevant information to the auditor, described in the Corporate Governance section of the statutory accounts, the directors are also responsible under Condition F of the Licence for:

- a) ensuring that proper accounting records are maintained by the company to enable compliance with the requirements of Condition F
- b) preparing as set of regulatory accounting statements, in respect of the twelve- month period ending on 31 March in each year, which are in accordance with the Regulatory Accounting Guidelines published by Ofwat
- c) complying with all other requirements that are set out in the Regulatory Accounting Guidelines published by Ofwat.

The directors approved the regulatory accounting statements (on pages 19 to 82) on 14 July 2023.

Board statement on accuracy and completeness of data and information

The Board confirms that the data and information provided to Ofwat during the reporting year, or published by the company in its role as a water and sewerage undertaker, was accurate and complete and is reflected in our Board Assurance Statement (see appendix 3).

The assurance statement includes a description of the activities which the Board has carried out to allow it to make the statement. The Board believe that our stakeholders deserve to have trust and confidence in the integrity of the information we provide in our annual reports. In order to achieve this, our performance reporting is subject to a system of checks to ensure that we meet the highest quality of reported information.

The Board has been fully aware of previous issues with the non-financial control environment of the company and has over the last six years worked with the executive management team to rebuild capability in this area. This work continues to be embedded and is becoming part of our Business-as-Usual way of working.

The Board has actively engaged and challenged the assurance processes that have been adopted by the company. This covers assurance on both the financial and non-financial reporting. The Board has, over recent years, taken action to ensure that exceptions and weaknesses identified in the non-financial assurance have been addressed. The Board is satisfied that the assurance approaches have appropriately identified and addressed the risks to the provision of accurate and complete data and information. This has been discharged through the Southern Water Services Board and its relevant committees (most notably the Audit Committee).

The Board Assurance Statement does not identify any specific exceptions.

Section 35A of the Water Industry Act 1991

The company is required under section 35A of the Water Industry Act 1991 to provide a statement that the remuneration paid to executive directors is linked to standards of performance. This statement is provided within the Directors' Remuneration Report section of the Annual Report and Financial Statements.

Long-term viability statement

In accordance with provision 31 of the UK Corporate Governance Code, the Board has assessed the prospects of the business over a longer period than the 12 months required by the 'Going Concern' provision.

The Board has elected to conduct this review to 31 March 2030 and full details of the assessment and the viability statement are set out within the Strategic Report section on page 133 of the Annual Report and Financial Statements.

This included the company's liquidity position, headroom against the financial covenants, credit ratings and financial risk assessment against a number of downside scenarios. In addition, the Board have considered the material uncertainty outlined in the going concern as referenced in our Annual Report and Financial Statements.

Statement of disclosure of information to auditor

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

- 1) so far as the director is aware, there is no relevant audit information of which the company's auditor is unaware
- 2) he/she has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

Board statement

Save for those matters mentioned above where the company has identified shortcomings or potential shortcomings and where the company has set out the steps it is taking or will take to manage, mitigate and/or improve those), the Board confirms, that having taken all the steps that they ought to have taken as directors to make themselves aware of any relevant information, the company has:

- 1) a full understanding of, and is meeting, its obligations and has taken steps to understand and meet customer expectations
- 2) sufficient processes and internal systems of control to fully meet its obligations
- 3) appropriate systems and processes in place to allow it to identify, manage and review its risks.



Stuart Ledger
Chief Financial Officer



Keith Lough
Chair

14 July 2023

Regulatory financial reporting

1A – Income statement for the 12 months ended 31 March 2023

	Note	Adjustments			Total adjustments £m	Total appointed activities £m
		Statutory £m	Differences between statutory and RAG definitions £m	Non-appointed £m		
Revenue		815.758	(48.684)	10.467	(59.151)	756.607
Operating costs		(835.925)	28.085	(8.779)	36.864	(799.061)
Other operating income		1.720	23.229	–	23.229	24.949
Operating profit		(18.447)	2.630	1.688	0.942	(17.505)
Other income		6.630	17.931	–	17.931	24.561
Interest income	3	4.283	–	–	–	4.283
Interest expense	3	(281.346)	(32.868)	–	(32.868)	(314.214)
Other interest expense	3	(1.600)	–	–	–	(1.600)
(Loss)/profit before tax and fair value movements		(290.480)	(12.307)	1.688	(13.995)	(304.475)
Fair value losses on derivative financial instruments		659.120	–	–	–	659.120
Profit/(loss) before tax		368.640	(12.307)	1.688	(13.995)	354.645
UK Corporation tax	4	–	–	–	–	–
Deferred tax		(83.689)	3.077	–	3.077	(80.612)
Profit/(loss) for the year		284.951	(9.230)	1.688	(10.918)	274.033
Dividends		–	–	–	–	–
Tax analysis						
Current year		–	–	–	–	–
Adjustments in respect of prior years		–	–	–	–	–
UK Corporation Tax		–	–	–	–	–

Analysis of non-appointed revenue

Imported sludge	–
Tankered waste	7.053
Other non-appointed revenue	3.414
Revenue	10.467

Details of the differences between the statutory and regulatory definitions are shown in note 2.

Note: The signage convention for presentation of this table follows Ofwat guidance. Total adjustments comprise the difference between statutory and regulatory accounting definitions less the non-appointed activity.

1B – Statement of comprehensive income for the 12 months ended 31 March 2023

	Adjustments			Total adjustments £m	Total appointed activities £m
	Statutory £m	Differences between statutory and RAG definitions £m	Non-appointed £m		
Profit/(loss) for the year	284.951	(9.230)	1.688	(10.918)	274.033
Actuarial losses on post-employment plans	(11.500)	–	–	–	(11.500)
Other comprehensive income	2.185	–	–	–	2.185
Total comprehensive income/(loss) for the year	275.636	(9.230)	1.688	(10.918)	264.718

1C – Statement of financial position for the 12 months ended 31 March 2023

	Adjustments			Total adjustments £m	Total appointed activities £m
	Statutory £m	Differences between statutory and RAG definitions £m	Non-appointed £m		
Non-current assets					
Fixed assets	7,092.803	(259.058)	0.409	(259.467)	6,833.336
Intangible assets	109.987	(3.200)	–	(3.200)	106.787
Investments – loans to group companies	10.872	–	–	–	10.872
Investments – other	0.174	–	–	–	0.174
Financial Instruments	83.931	–	–	–	83.931
Total non-current assets	7,297.767	(262.258)	0.409	(262.667)	7,035.100
Current assets					
Inventories	10.447	–	–	–	10.447
Trade and other receivables	253.400	–	3.285	(3.285)	250.115
Cash and cash equivalents	115.846	–	–	–	115.846
Total current assets	379.693	–	3.285	(3.285)	376.408
Current liabilities					
Trade and other payables	(264.787)	(0.824)	–	(0.824)	(265.611)
Capex creditor	(197.954)	–	–	–	(197.954)
Borrowings	(23.235)	–	–	–	(23.235)
Current tax liabilities	(14.856)	–	–	–	(14.856)
Provisions	(29.565)	–	–	–	(29.565)
Total current liabilities	(530.397)	(0.824)	–	(0.824)	(531.221)
Net current liabilities	(150.704)	(0.824)	3.285	(4.109)	(154.813)
Non-current liabilities					
Trade and other payables	(11.969)	–	–	–	(11.969)
Borrowings	(4,133.076)	–	–	–	(4,133.076)
Financial instruments	(1,655.331)	–	–	–	(1,655.331)
Retirement benefit obligations	(73.000)	–	–	–	(73.000)
Provisions	(31.581)	–	–	–	(31.581)
Deferred income – grants and contributions	(28.316)	(3.742)	–	(3.742)	(32.058)
Preference share capital	(64.665)	–	–	–	(64.665)
Deferred tax	(284.517)	66.706	–	66.706	(217.811)
Total non-current liabilities	(6,282.455)	62.964	–	62.964	(6,219.491)
Net assets	864.608	(200.118)	3.694	(203.812)	660.796
Equity					
Called up share capital	0.112	–	–	–	0.112
Retained earnings and other reserves	864.496	(200.118)	3.694	(203.812)	660.684
Total equity	864.608	(200.118)	3.694	(203.812)	660.796

Details of the differences between the statutory and regulatory definitions are shown in note 2.

1D – Statement of cash flows for the 12 months ended 31 March 2023

	Adjustments			Total adjustments £m	Total appointed activities £m
	Statutory £m	Differences between statutory and RAG definitions £m	Non-appointed £m		
Operating profit	(18.447)	2.630	1.688	0.942	(17.505)
Other income	6.630	17.931	–	17.931	24.561
Depreciation	347.120	(15.995)	0.001	(15.996)	331.124
Amortisation – grants and contributions	1.366	(3.089)	–	(3.089)	(1.723)
Changes in working capital	53.777	(4.566)	(1.797)	(2.769)	51.008
Pension contributions	–	–	–	–	–
Movement in provisions	(35.566)	–	–	–	(35.566)
Profit on sale of fixed assets	(1.720)	–	–	–	(1.720)
Cash generated from operations	353.160	(3.089)	(0.108)	(2.981)	350.179
Net interest paid	(178.406)	–	–	–	(178.406)
Tax paid	–	–	–	–	–
Net cash generated from operating activities	174.754	(3.089)	(0.108)	(2.981)	171.773
Investing activities					
Capital expenditure	(676.925)	–	0.108	(0.108)	(677.033)
Grants and contributions	–	3.089	–	3.089	3.089
Disposal of fixed assets	1.381	–	–	–	1.381
Other	319.013	(285.000)	–	(285.000)	34.013
Net cash used in investing activities	(356.531)	(281.911)	0.108	(282.019)	(638.550)
Net cash generated before financing activities	(181.777)	(285.000)	0.000	(285.000)	(466.777)
Cash flows from financing activities					
Equity dividends paid	–	–	–	–	–
Net loans paid	140.186	–	–	–	140.186
Cash inflow from equity financing	–	–	–	–	–
Net cash used in financing activities	140.186	–	–	–	140.186
Decrease in net cash	(41.591)	(285.000)	0.000	(285.000)	(326.591)

Details of the differences between the statutory and regulatory definitions are shown in note 2.

1E – Net debt analysis at 31 March 2023

	Interest rate risk profile			Total £m
	Fixed rate £m	Floating rate £m	Index linked RPI £m	
Borrowings (excluding preference shares)	1,416.885	400.000	2,728.522	4,545.407
Preference share capital	64.665			64.665
Total borrowings	1,481.550	400.000	2,728.522	4,610.072
Cash				(115.846)
Short term deposits				–
Net debt				4,494.226
Gearing				69.85%
Adjusted gearing				68.30%
Full year equivalent nominal interest cost	(12.599)	19.511	440.925	447.837
Full year equivalent cash interest payment	(12.599)	19.511	72.343	79.255
Indicative interest rates				
Indicative weighted average nominal interest rate	(0.850%)	4.878%	16.160%	9.714%
Indicative weighted average cash interest rate	(0.850%)	4.878%	2.651%	1.719%
Weighted average years to maturity	12.117	2.000	9.633	10.533

Adjusted gearing excludes preference shares and includes debt at nominal values along with any unpaid accretion and the accrued accretion on our financial instruments.

The borrowings and full year equivalent interest cost reflect the impact of our financial derivatives, excluding fair value movements.

The calculation of the weighted average years to maturity is based on the designation of the underlying debt instruments and excludes the impact of swaps that we have in place.

A reconciliation between the borrowings reported in tables 1C and 1E is shown below, along with a reconciliation to the principal sum outstanding reported in table 4B, which is published separately alongside this report.

Reconciliation of borrowings between table 1C and tables 1E and 4B

	£m
1C – Current liabilities borrowings	423.235
1C – Non-current liabilities borrowings	3,733.076
Total Borrowings (table 1C)	4,156.311
Debt issue costs	6.902
Bond premium deferred	(6.231)
Deferred gilt lock proceeds	(4.265)
Accrued swap accretion	392.691
Borrowings (table 1E)	4,545.407
Preference shares	64.665
Difference between amortised cost and nominal value	28.058
Principal sum outstanding (table 4B)	4,638.130

The debt issue costs, bond premium, deferred gilt lock proceeds and deferred proceeds are amortised to the income statement and details are presented in note 20 to our statutory accounts.

The accrued swap accretion is an increase in the liability of the swap financial instruments which is presented within the financial instruments balance for statutory accounting purposes but included in borrowings as per table 1E guidance. This figure is also shown in table 4I.

1F – Financial Flows for the 12 months ended 31 March 2023 and for the price review to date (2017–18 financial year average CPIH)

	12 months ended 31 March 2023					
	%			£m		
	Notional returns and notional regulatory equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity	Notional returns and notional equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity
Regulatory equity						
Regulatory equity	2,082.487	2,082.487	1,682.676	–	–	–
Return on regulatory equity						
Return on regulatory equity	3.87%	3.13%	3.87%	80.592	65.120	65.120
Financing						
Impact of movement from notional gearing	–	0.74%	0.40%	–	15.473	6.813
Cost of debt	–	9.52%	12.91%	–	198.171	217.277
Hedging instruments	–	(2.35%)	(2.91%)	–	(48.899)	(48.899)
Return on regulatory equity including Financing adjustments	3.87%	11.04%	14.28%	80.592	229.864	240.311
Operational performance						
Totex out/(under) performance	–	(10.15%)	(12.56%)	–	(211.343)	(211.343)
ODI out/(under) performance	–	(1.80%)	(2.22%)	–	(37.429)	(37.429)
C-MeX out/(under) performance	–	(0.20%)	(0.25%)	–	(4.154)	(4.154)
D-MeX out/(under) performance	–	(0.04%)	(0.06%)	–	(0.936)	(0.936)
Retail out/(under) performance	–	(0.26%)	(0.32%)	–	(5.313)	(5.313)
Other exceptional items	–	0.02%	0.03%	–	0.422	0.422
Operational performance total	–	(12.43%)	(15.38%)	–	(258.753)	(258.753)
RoRE (return on regulatory equity)	3.87%	(1.39%)	(1.10%)	80.592	(28.889)	(18.442)
RCV growth	10.64%	10.64%	10.64%	221.577	221.577	179.037
Total shareholder return	14.51%	9.25%	9.54%	302.169	192.688	160.594
Dividends						
Gross dividend	1.41%	–	–	29.363	–	–
Interest received on intercompany loans	–	–	–	–	–	–
Retained value	13.10%	9.25%	9.54%	272.806	192.688	160.594
Cash impact of 2015–20 performance adjustments						
Totex out/(under) performance	–	(0.04%)	(0.04%)	–	(0.730)	(0.730)
ODI out/(under) performance	–	0.02%	0.03%	–	0.459	0.459
Total out/(under) performance	–	(0.01%)	(0.02%)	–	(0.271)	(0.271)

The figures presented above may not cast due to rounding issues.

1F – Financial Flows for the 12 months ended 31 March 2023 and for the price review to date (2017–18 financial year average CPIH)

	Average 2020–23					
	%			£m		
	Notional returns and notional regulatory equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity	Notional returns and notional equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity
Regulatory equity						
Regulatory equity	2,001.201	2,001.201	1,538.331	–	–	–
Return on regulatory equity						
Return on regulatory equity	3.90%	3.00%	3.90%	78.047	59.995	59.995
Financing						
Impact of movement from notional gearing	–	0.90%	0.47%	–	18.052	7.239
Cost of debt	–	2.88%	4.36%	–	57.585	67.103
Hedging instruments	–	0.63%	0.82%	–	12.660	12.660
Return on regulatory equity including Financing adjustments	3.90%	7.41%	9.56%	78.047	148.292	146.997
Operational performance						
Totex out/(under) performance	–	(5.17%)	(6.73%)	–	(103.549)	(103.549)
ODI out/(under) performance	–	(1.89%)	(2.46%)	–	(37.811)	(37.811)
C-MeX out/(under) performance		(0.15%)	(0.20%)		(3.020)	(3.020)
D-MeX out/(under) performance		(0.03%)	(0.04%)		(0.656)	(0.656)
Retail out/(under) performance		(0.97%)	(1.26%)		(19.342)	(19.342)
Other exceptional items	–	(1.42%)	(1.85%)	–	(28.474)	(28.474)
Operational performance total	–	(9.64%)	(12.54%)	–	(192.852)	(192.852)
RoRE (return on regulatory equity)	3.90%	(2.23%)	(2.98%)	78.047	(44.560)	(45.855)
RCV growth	6.30%	6.30%	6.30%	126.076	126.076	96.915
Total shareholder return	10.20%	4.07%	3.32%	204.123	81.516	51.060
Dividends						
Gross dividend	1.40%	0.06%	0.08%	28.017	1.263	1.263
Interest received on intercompany loans	–	(0.06%)	(0.08%)	–	(1.263)	(1.263)
Retained value	8.80%	4.07%	3.32%	176.106	81.516	51.060
Cash impact of 2015–20 performance adjustments						
Totex out/(under) performance	–	(0.04%)	(0.05%)	–	(0.730)	(0.730)
ODI out/(under) performance	–	0.02%	0.03%	–	0.459	0.459
Total out/(under) performance	–	(0.01%)	(0.02%)	–	(0.271)	(0.271)

The figures presented above may not cast due to rounding issues.

Commentary regarding table 1F – Financial Flows

Table 1F Financial Flows aims to improve transparency and explain the elements that have the most significance on the financial flows to investors. As the analysis is designed to estimate the impact on equity return due to actual performance and capital structure, it includes some high-level approaches to estimate the impact of regulatory mechanisms. This results in regulatory rewards and penalties, earned in the current price review period 2020–25 but not realised by shareholders until the next price review period 2025–30, being included in the table. A simplified approach is also adopted for the cost of debt and replicated in hedging instruments in order to ensure consistency of approach.

The above table provides information in a three-column format:

- ‘notional returns and notional regulatory equity’ (column 1) – equivalent to our allowance in the Final Determination for 2020–25.
- ‘actual returns and notional regulatory equity’ (column 2 – provides a representation of the variance in financial performance between the return allowed in the PR19 Final Determination and actual results.
- ‘actual returns and actual regulatory equity’ (column 3) – an extension of column 2, designed to show the impact on shareholder returns where their investment in the company is smaller or larger than the regulatory assumption (with debt being correspondingly larger or smaller, respectively).

Base return:

The base return on regulatory equity of 3.87%, plus inflation of 10.64% on the regulated equity, results in a total shareholder return of 14.51%. This is based on Ofwat’s price review approach to determining returns, reflecting an efficient company with the regulatory notional gearing of 60.00%. The equivalent actual total shareholder return, reflecting our average gearing in 2022–23 of 67.68% and actual performance, was 9.54%.

Our actual return of 9.54% differed from the notional return of 14.51% due to financing out-performance of 10.41% and operational under-performance of 15.38%.

Financing performance:

Our average actual gearing of 67.68% is higher than the regulatory assumption of 60.00%, and has the effect of amplifying percentage returns to shareholders. This is partly because the same value of return is applied to a smaller shareholder equity base, representing a greater proportion. This increases the volatility of returns, in both out-performance and under-performance scenarios, with the risk being borne entirely by shareholders.

The price setting process also allows us a return on equity between the notional gearing of 60.00% and our actual gearing of 67.68%, rather than the lower cost of debt. The impact of this relative cost of debt versus equity is estimated in the ‘Impact of movement from notional gearing’ returns adjustment of 0.40%.

Our ‘Comparison between tax charge and allowance in price limits’ (see page 36) provides a detailed narrative on our corporation tax charge. In summary, our PR19 determination includes no funding from customers for corporation tax and we incurred no current tax charge in 2022–23. The net impact on shareholder returns of corporation tax and group relief is 0.0%.

Our cost of debt (excluding the impact of swap instruments), measured by reference to an implied real rate of interest, was lower than the amount allowed in our PR19 determination (updated for the cost of debt reconciliation mechanism) increasing returns by 12.91%. This is driven by the high inflation experienced this year, and the impact it has when deflating to the implied real rate of interest. The 5.93% actual cost of debt, when deflated by inflation of 8.77%, gives an implied real rate of -2.61% – comparing favourably with the 2.16% allowed real cost of debt.

We have a portfolio of inflation linked swaps that match the cost we pay under our debt instruments to the cash flow we receive from customer bills. We have calculated the impact of these hedging instruments in a manner consistent with the prescribed calculation for cost of debt, by deflating to an implied real rate of net interest. This creates a negative impact for the year of 2.91%, driven by the impact of the high inflation when converting the swap interest receivable to an implied real rate, in a similar manner as outlined above for the cost of debt adjustment. This is offset by benefits to our interest cashflows from the capital restructuring carried out in 2018.

Operational performance:

For AMP7 we will retain approximately 64% of wholesale totex overspends, but only 36% of wholesale totex cost savings, with the remainder being returned to customers. Some types of wholesale totex are not subject to customer sharing, with any out-performance or under-performance remaining entirely with the company. To account for any timing differences in our totex delivery, such as slippage or acceleration in our capital programme, we adjust for this in Table 4C. In 2022–23, we experienced a retained overspend of £211.3 million, equivalent to a decrease of 12.56% in returns.

The company share of retail cost under-performance represents the amount by which we are overspending against the PR19 price determination. There is no sharing with customers

of the retail expenditure variance, with the result that the £5.3 million over-spend for 2022–23 reduces returns by 0.32%.

The impact of our performance on Outcome Delivery Incentives (ODIs) is £37.4 million for 2022–23, decreasing returns by 2.22%. Penalties or rewards are included even if they are not payable or receivable until later in the current AMP or the next AMP. Tables 3A and 3B provide further details.

For 2022–23 we report a £4.2 million penalty for the Customer Measure of Experience (C-MeX) ODI in our Retail business, and a £0.9 million penalty for the Developer Measure of Experience (D-MeX) ODI in Developer Services. These are equivalent to a 0.25% and 0.06% reduction to returns, respectively.

The exceptional item entry of £0.4 million, equivalent to a 0.03% increase in returns, relates to the company share of land sales, which we include under the 'exceptional items' to ensure consistency with Ofwat guidance for this table. The values for the land sales are immaterial, and not reported as exceptional items elsewhere in the financial statements.

Other:

The inflationary RCV return of 10.64% is long-term in nature and cannot be immediately realised.

No ordinary dividends were paid in 2022–23.

AMP7 annual average returns

We have restated the opening gearing for 2020–21, from 70.40% to 71.28%, to align with the updated RCV models published by Ofwat. This reduces the 2020–21 average actual regulatory equity, concentrating the impact of under-performance, and reducing the total shareholder return in that year from -0.98% to -1.04%. The impact reported this year is reflected in the 'Average 2020–23' table, decreasing the average shareholder return from 4.52% to 4.50%. We have also updated our calculation for the impact of our hedging instruments for all three years of the AMP to include the annual inflation charge for those swap instruments which are index-linked to RPI, matching the treatment of the index-linked bonds in the cost of debt. The impact reported this year due to the changed treatment in 2020–21 and 2021–22 is reflected in the 'Average 2020–23' table, decreasing the average shareholder return by 0.84%. No adjustment was required to align our previously-reported ODI performance for 2020–21 and 2021–22 with Ofwat's in-period ODI determinations, and consequently there is no impact on average shareholder returns.

Over the first three years of the AMP7 regulatory period, and including the 6.30% average annual inflationary growth of the RCV, the total shareholder

return averages 3.32%. Excluding the inflationary RCV return, which is long-term in nature and cannot be immediately realised, the average annual return potentially available to shareholders is -2.98%, 6.88% lower than the 3.90% return allowed by Ofwat in the price determination.

The main driver of the shortfall on returns is our operational performance, which reduces returns by 12.54%. Our wholesale business comprises 11.04% of this difference, with 6.73% relating to cost overruns, 2.46% to our performance against Performance Commitments and resulting ODI penalties, and 1.85% to the exceptional item – almost entirely comprising the fine and costs of the Environment Agency prosecution. It should be noted that the EA prosecution, while being recognised in 2021–22, related to historical performance over a number of years between 2010 and 2015. The remaining 1.50% of our operational performance mainly relates to cost overruns and C-MeX performance in the Retail business.

The 5.66% increase to returns due to our financing performance partially offsets the impact of our operational performance.

During AMP7 we have retained shareholder value in the business and made no dividends.

Cash impact of 2015–20 performance adjustments

The impact of 2015–20 performance adjustments has been removed from the main calculation of shareholder return. The cash impact is now reported as a memo note at the foot of the table and, consistent with Ofwat table guidance, we show the impact for wholesale totex and wholesale ODIs.

Other adjustments relating to 2015–20 performance are no longer reported. The most material of these are the regulatory settlement following the Ofwat investigation into our wastewater treatment compliance (discussed on page 9) and the Service Incentive Mechanism (SIM) in the Retail business, which was the AMP6 equivalent of C-MeX. For 2022–23 these penalties reduce returns by £24.2 million (1.44%) and £6.0 million (0.30%) respectively.

Note:

We believe that our RCV for 2022–23 published by Ofwat is understated by approximately £38.3 million, due to the approach taken to convert from year-average prices to March 2023 prices for the proportion of our RCV which remains linked to RPI. For our reporting we have used the value published by Ofwat, which translates to a lower regulatory equity value, amplifying the impact of out-performance and under-performance in the Financial Flows table. We are engaging with Ofwat to determine the correct treatment.

Notes to the regulatory financial statements

For the year ended 31 March 2023

1 Accounting policies

a) Basis of preparation

The regulatory accounting statements have been prepared in accordance with Condition F of the Appointment and the Regulatory Accounting Guidelines (RAGs) published by Ofwat, the accounting policies set out in the statement of accounting policies and under the historical cost convention. They have been prepared on a going concern basis, notwithstanding the material uncertainty discussed on page 205 of the Southern Water Services Limited Annual Report and Accounts 2022–23.

The company has a significant level of planned expenditure, over at least the next twelve months and will continue to March 2025 to improve operational performance, the resilience of its assets, and reduce the impact on the environment from the treatment and processing of water and wastewater. The company is also facing the effect of high inflation, particularly on costs such as energy, chemicals, and materials.

To assist in financing the planned expenditure the company expects to receive £375 million of new equity in the coming months. The ultimate shareholders of the company have indicated their support for the company and are believed to be at an advanced stage of the equity process, but the receipt has not been committed at the date of signing these financial statements.

The directors are of the opinion that the equity will be received but given it has not been committed at the date of the financial statements and its commitment is not within the directors' control, believe that the risk that the equity is not received constitutes a material uncertainty that may cast significant doubt about the company's ability to continue as a going concern such that it may be unable to realise its assets and discharge its liabilities in the normal course of business.

The accounting policies used in the regulatory accounting statements are the same as those adopted in the statutory financial statements, except as set out below.

The regulatory accounting statements are separate from the statutory financial statements of the company. The statutory financial statements are prepared under FRS 101 'Reduced Disclosure Framework'. There are differences between International Financial Reporting Standards under FRS 101 and the basis of preparation of information provided in the regulatory accounts because the Regulatory Accounting Guidelines specify alternative treatment or disclosure in respect of:

- revenue recognition
- capitalisation of borrowing costs.

Where the Regulatory Accounting Guidelines do not specifically address an accounting issue, then they require the company's statutory accounting framework to be followed. Financial information other than that prepared wholly on the basis of IFRS, FRS 101 or FRS 102 may not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 2006.

b) Fixed assets

Interest – To meet the requirements of RAG 1.09 the interest capitalised within the statutory accounts under IAS 23 'Borrowing Costs' has been reversed and charged through the income statement.

Capitalisation policy – Costs that are either directly attributable to bringing an asset into working condition or subsequent expenditure that provides an enhancement of the economic benefits of a fixed asset are treated as capital expenditure. In order to aid classification of expenditure the following rules are applied:

Non-infrastructure assets

- Expenditure on a single item of equipment, including installation costs, exceeding £3,000 is treated as capital expenditure. Individual items purchased for less than £3,000 are charged to operating costs unless they form part of a capital scheme.
- All repairs, replacements and improvements to non-infrastructure fixed assets costing in excess of £3,000 and which extend the life of the asset are charged to capital.

Infrastructure assets

- All repairs and maintenance to infrastructure assets will generally be treated as operating expenditure.
- Large repairs, involving the replacement of a significant length of pipe, are treated as capital expenditure after review with the Finance Team.
- Planned renewals to replace significant lengths of pipe in relation to a specific asset are treated as capital expenditure.

Private sewers – The ownership of and responsibility for private sewers in Southern Water's region were transferred to the company on 1 October 2011.

Following the adoption of FRS 101, expenditure in relation to private sewers has been treated as an expense and charged to the income statement.

c) Revenue recognition

Revenue represents the income receivable in the ordinary course of business (excluding value added tax) for goods and services provided in the year by the regulated activities of the business.

Revenue relates to charges due in the year and includes charges billed to customers for water and sewerage services, which are recognised in the period in which they are earned, and an accrual in respect of unbilled charges. Revenue excludes payments received in advance which are recorded as deferred revenue.

Unmetered bills for water and wastewater services are based on either the rateable value of the property, an assessed volume of water supplied or on a Fixed Licence Fee.

Metered bills for water and wastewater services are based on actual or estimated water consumption. Metered revenue is dependent upon the volumes supplied and includes an estimate of the consumption between the date of the last meter reading and the period end. Meters are read on a cyclical basis and the company recognises revenue for unbilled amounts based on estimated usage from the last meter reading date through to the end of the reporting period. The accrual is estimated using a defined methodology based upon historical billing and consumption information and the applicable tariff. Where there is insufficient historical information, estimation is based on average consumption for defined levels of occupancy.

Within the accrual, adjustments to billing are made for changes to occupancy dates and where consumption levels are in excess of certain tolerances. No other amendments are made between revenue and billing.

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

In the statutory accounts, reported under IFRS 15 – ‘Revenue from Contracts with Customers’, revenue is only recognised when it is probable that economic benefits will result to the company. RAG 1.09 requires that no judgment is applied to the probability of collection. Following a review of the collectability of revenue for the bad debt provision charge for 2019–20, revenue has been recognised in full in the statutory accounts and therefore there is no difference this year between the revenues reported for statutory and regulatory purposes.

Charging policy

Water and sewerage charges fall into the following three categories:

- 1) Charges which are payable in full
- 2) Charges which are payable in part
- 3) Not chargeable (void properties).

The circumstances in which each of the above applies are set out below. All of the charges covered in categories 1) and 2) are included in revenue.

Charges payable in full

Charges are payable in full in the following circumstances:

i) Occupied and furnished

Water (and sewerage) charges are payable in full from the date of connection or change of customer on all properties which are recorded as occupied and furnished.

ii) Unoccupied and furnished

Water (and sewerage) charges are payable in full on unoccupied, furnished premises. These include properties:

- left with bedding, a desk or other furniture
- used for multiple occupation with shared facilities
- used as holiday, student, hostel or other accommodation
- used for short-term occupation or letting where the occupation or terms of tenancy is less than six months.

Exceptions to this, where water (and sewerage) charges are not payable, include where the customer is:

- in a care home
- in long-term hospitalisation
- in prison
- overseas long term
- deceased.

iii) Unoccupied and unfurnished

Water (and sewerage) charges are payable in full on unoccupied, unfurnished premises where water is being consumed. This includes:

- premises where renovation, redecoration or building work is being undertaken
- premises being used as storage
- premises not normally regarded as being occupied such as cattle troughs and car parks
- non-household agricultural properties.

Charges payable in part

The following charges only are payable in certain circumstances:

- Metered standing charges – Payable on unoccupied, metered properties which are still connected.
- Surface water charge – Payable on unmeasured properties which are temporarily disconnected.
- Sewerage unmeasured tariff – Payable on unmeasured, occupied properties where the water supply is disconnected but sewerage is still provided.
- Surface water and highway drainage – Payable on furnished properties where the water supply is disconnected.

Not chargeable

Properties which are unoccupied, unfurnished and disconnected are not chargeable for water and sewerage therefore no billing is raised, and no revenue recognised in respect of these properties.

Definition and treatment of properties

Occupied properties

The occupier is any person who owns a premises or who has agreed with us to pay water and sewerage services in respect of the premises.

The property management process is followed to identify whether the property is occupied or not and, if occupied, to identify the chargeable person and raise a bill.

The property management process may comprise some or all the following:

- Physical inspection
- Mailings
- Customer contacts
- Meter readings for metered properties
- Checks with third parties, e.g. credit agencies.

When a new customer is identified, the company process aims to establish the date that they became responsible for water and sewerage charges at the property. This is normally the date at which they moved into the property. The new customer will be charged retrospectively from the date at which they became responsible for water and sewerage charges of the premises.

Where evidence exists that a property is occupied the property management process is followed until occupancy details are obtained. Bills are not issued in the name of 'The Occupier' to try to generate confirmation of occupancy and therefore there is no billing in the name of 'The Occupier' within revenue.

Unoccupied properties

A property is deemed to be unoccupied when the company has completed the property management process and not identified the property as occupied. To be classified as unoccupied a property must meet at least one of the following criteria:

- A new property has been connected but is empty and unfurnished.
- The company has been informed that the customer has left the property, it is unfurnished and not expected to be reoccupied immediately.
- It has been disconnected following a customer request.
- The identity of the customer is unknown.
- The company has been informed that the customer is in a care home, long-term hospitalisation, prison, overseas long term or deceased.

If the property management process confirms that the property is unoccupied, the property may be declared void and the supply turned off.

New properties

All new properties are metered. Charges accrue from the date at which the new connection is assessed as being made and/or when the meter is installed. The developer is billed between the date of connection and first occupancy and this is recognised as revenue.

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

d) Revenue disclosures

In accordance with RAG 3.14 we highlight the following comments in respect of turnover for the year:

- (i) The value of household billings raised in the year ended 31 March 2023 for consumption in prior years was £225.6 million. The value of these billings was lower than the metered income accrual made at 31 March 2022. The estimation difference was £7.9 million and this has been recognised in the current year's turnover. This difference is larger than we would normally expect, with customer usage patterns much remaining more difficult to predict since COVID-19.
- (ii) No changes have been made to the overall accrual methodology in the year although we have taken into consideration the experience from March 2022.

e) Social tariffs

We provide a number of schemes and tariffs to improve affordability and accessibility for vulnerable customers. These include:

- **Essentials** – for customers whose household income is less than £21,000, or for those in receipt of pension credit.
- **WaterSure** – for those who are in receipt of means tested benefits and use a large amount of water either as a result of large families, or because of a particular medical condition.
- **Water Direct** – where bills may be paid from a customer's existing benefit schemes directly to us.
- **NewStart** – for those who owe us money but have not been able to make a payment for a while.

In response to the COVID-19 pandemic, we took a number of immediate steps to help our customers. We introduced a three-month payment break for many of those impacted by the pandemic and took steps to streamline the application process for our social and capped tariffs. This included moving to an automatic renewal process (to relieve the administration burden on those in need).

Further details can be found in our Annual Report and on our website at: southernwater.co.uk/account/what-if-i-can-t-pay-my-bill

f) Bad and doubtful debts

The bad debt provision is calculated by applying estimated recovery rates, based on the past collection experience of other customers who share similar characteristics.

Higher provisioning percentages are applied to customers which are, based on their characteristics, considered to be of greater risk. These include those with a poor payment history as well as to those with older debts. Bad debt provisioning rates are updated annually to reflect the latest collection performance data from the company's billing system. Actual amounts recovered may differ from the estimated levels of recovery, which could impact on operating results.

The company operates a comprehensive debt recovery process and bad debt is only written off when the recovery of such debt has been exhausted through routine collection, debt recovery or litigation processes or where it would be uneconomical to undertake further recovery action.

Situations where this may arise and where debt may be written off are as follows:

- Where the customer has absconded without paying and strategies to trace their whereabouts and collect outstanding monies have been fully exhausted,
- Where the customer has died without leaving an estate or has left an insufficient estate from which to recover the debt,
- Where the age and/or value of the debt makes it uneconomical to pursue,
- Where county court proceedings and attempts to recover the debt using debt collection agencies have proved unsuccessful,
- Where the customer has been declared bankrupt, is in liquidation or is subject to insolvency proceedings or a debt relief order and no dividend has been or is likely to be received.

Write-off rules apply primarily to customers to whom the company has ceased to supply a service. Only in exceptional circumstance or as part of specific debt recovery assistance programmes is debt relating to continuing customers considered for write-off.

For debt to be written off there must be a legitimate charge against the debtor. If it is considered that part or all of the debt is incorrect or unsubstantiated, then such elements are dealt with through the issue of a credit note.

The company's bad debt provisioning and write-off policies have remained unchanged and have been consistently applied during the year. The value of debt written off over the past year has remained low due to the continuation of projects aimed at reducing bad debt before the point of write-off.

The value of trade and other receivables of the appointed business increased to £250.1 million (2022: £242.5 million). This increase largely relates to prepayments for interest and IT contracts which grew by £9.2 million in the year.

g) Price control units

The notes to the regulatory accounting statements analysing revenues, operating costs and fixed assets by price control segment have been drawn up in accordance with the guidance provided by Ofwat in RAG 2.09 and our accounting separation methodology statement which is published separately on our website.

The methods for undertaking cost allocations to produce this information are summarised below:

Operating expenditure

Most direct costs are specific either to water, wastewater or retail services. Where costs cannot be directly attributed to a sub-function an apportionment has been made on an appropriate basis, using the most accurate allocation method available. Examples of allocation methods include the use of time recording devices, headcount, operational site data and management estimates.

The allocation methods adopted have been agreed following review meetings held across the business with management and technical experts.

The information relating to non-appointed business, including an allocation of overhead cost, has been excluded in line with the guidance.

Fixed assets

The fixed asset data has predominantly been directly attributed to the price control segments based on an assessment of the overall nature of each scheme.

Where a scheme relates to more than one price control segment it has been allocated to the price control unit where the principal use occurs. For corporate assets, the price control of principal use is wholesale wastewater as this is our largest price control and recharges to the other price control units are made for the use of these assets.

New expenditure incurred during the year is allocated to business units within each price control based on an analysis of the scheme design.

Revenues

Revenue streams have been directly attributed to price control segments where they have been recorded as such in our systems. Classification of household and non-household revenues has been made in line with the classifications in place when the business plan was completed in accordance with the guidance from Ofwat.

Revenues that could not be directly attributed to a price control segment have been assessed and allocated to the appropriate price control segment based on the nature of the income.

h) Provisions and contingencies

Environment Agency – wastewater sites

The company is seeking to work proactively with the Environment Agency to resolve its investigation into sampling compliance and reporting issues 2013 and 2017 (inclusive). The Board has concluded that it is not yet possible to make a reliable estimate of the financial obligation that will arise from this investigation and further details are provided within the contingent liability disclosures in our Annual Report.

i) Havant Thicket

In February 2021 the company entered into a contractual arrangement with Portsmouth Water, under which Portsmouth Water will obtain planning permission, design, build, finance, and operate a reservoir in Havant. Once the construction is complete, Portsmouth Water will supply, on the request of Southern Water up to 21 million litres of treated water per day from 1 April 2029.

Following a detailed review of the complex contractual arrangement which require both parties to complete certain activities to enable the water to be provided, we have formed the judgment that this contract should be accounted for as an executory contract until such time that both parties have fulfilled their obligations and the right to water can be met.

As a result, payments made during 2020–21 of £6.5 million, and included within the totex reported in that year, are classified within prepayments in the Statement of Financial Position.

2 Differences between statutory and regulatory reporting

Statutory reporting reflects the financial performance of Southern Water Services which comprises appointed and non-appointed activities. The appointed business relates to those activities which are necessary for the company to fulfil its function and duties as a water and sewerage undertaker. The non-appointed business relates to activities we undertake that are not covered by our Licence but are related to our business. For regulatory reporting the activities of the non-appointed business have been separated from those of the appointed business.

In addition, there are differences between regulatory accounting definitions and those applied for statutory reporting under FRS 101. These are summarised below:

Income statement – differences between statutory and RAG definitions

	Revenue £m	Operating costs £m	Other operating income £m	Other income £m	Interest expense £m
i) CHP income	(3.5)	3.5	–	–	–
ii) Grants and contributions	(22.0)	–	–	22.0	–
iii) Regulatory settlement amortisation	(23.2)	–	23.2	–	–
iv) Borrowing costs	–	16.0	–	–	(32.9)
v) Innovation costs	–	8.6	–	(4.1)	–
Total	(48.7)	28.1	23.2	17.9	(32.9)

- i) Income generated from Combined Heat and Power (CHP) processes, which convert methane into electricity, is recorded as revenue within the statutory accounts. For regulatory reporting this income is reported as a negative operating cost. As a result, £3.5 million of revenue has been reclassified as a negative operating cost.
- ii) As required by RAG 1.09 section 4.11, grants and contributions received and recognised in the income statement are reported under other income in the Annual Performance Report financial tables. As a result, £22.0 million has been transferred from revenue to other income in the income statement. See table 2E for further information.
- iii) In 2018–19 we made a provision for rebates to be made to customers during the period from 2020–25 as a result of the investigation undertaken by Ofwat into wastewater reporting as set out on page 9. For regulatory purposes, the amortisation of this provision is reclassified from revenue to other operating income.
- iv) For statutory reporting, borrowing costs associated with capital expenditure are capitalised. Regulatory reporting does not permit interest to be capitalised. As a result, operating costs are reduced by £16.0 million, reflecting the removal of depreciation on interest capitalised and the interest charge has been increased by £32.9 million reversing the element of interest capitalised in the year.
- v) As required by Ofwat we have removed the costs paid and accrued in relation to the innovation fund from our operating costs. The value paid into the fund and for administration of the fund of £4.1 million has been reclassified within other income in order to reflect this transaction through reserves and the accrual of £4.5 million has been reversed in accordance with IN-2201 Expectations for monopoly company annual performance reporting 2021–22 as published by Ofwat.

Statement of financial position – differences between statutory and RAG definitions

	Fixed Assets £m	Intangible Assets £m	Current trade and other payables £m	Deferred income – grants and contributions £m
i) Borrowing costs	(259.1)	(3.2)	–	–
ii) Grants and contributions	–	–	3.7	(3.7)
iii) Innovation costs	–	–	(4.5)	–
Total	(259.1)	(3.2)	(0.8)	(3.7)

- i) As borrowing costs cannot be capitalised under regulatory reporting, fixed and intangible assets have been reduced by £259.1 million and £3.2 million respectively, reflecting the removal of cumulative borrowing costs capitalised. There is a corresponding reduction to retained earnings.
- ii) Grants and contributions relating to requisitions of £3.7 million classified within current trade and other payables in the statutory accounts have been transferred to deferred income for regulatory reporting.
- iii) Removal of the innovation cost accrual as mentioned in note (v) to the income statement above.

Statement of cash flows – differences between statutory and RAG definitions

	Operating profit £m	Other income £m	Depreciation £m	Amortisation – grants and contributions £m	Changes in working capital £m	Grants and contributions £m	Investing activities – other £m
i) Grants and contributions – income statement	(22.0)	22.0	–	–	–	–	–
ii) Depreciation	16.0	–	(16.0)	–	–	–	–
iii) Grants and contributions – cash	–	–	–	(3.1)	–	3.1	–
iv) Innovation fund	8.6	(4.1)	–	–	(4.5)	–	–
v) Short-term deposits	–	–	–	–	–	–	(285.0)
Total	2.6	17.9	(16.0)	(3.1)	(4.5)	3.1	(285.0)

- i) The re-classification of grants and contributions received in the income statement of £22.0 million from operating profit to other income.
- ii) There is a £16.0 million adjustment made to both operating profit and depreciation relating to the removal of capitalised borrowing costs.
- iii) In the statutory accounts for 2022–23, cash contributions received and held on the Balance Sheet have been presented as operating cashflows. These have been included within the statutory amortisation of grants and contributions row of table 1D. For regulatory purposes £3.1 million, reflecting the cash received for specific capital assets, has been reclassified to grants and contributions within investing activities.
- iv) Innovation fund – reclassification of payments made from operating costs to other income of £4.1 million and removal of the accrual made in the statutory accounts of £4.5 million.
- v) Short-term deposits – reclassification of the movement of short-term deposits from current investments to cash and cash equivalents

3 Interest

Further details of the interest income and expenses charged to the income statement are provided below:

	£m
Interest income	
Deposit income on short-term bank deposits	4.3
	4.3
Interest expense	
Interest payable on other loans	(4.6)
Interest paid to group companies	(163.5)
Indexation	(139.8)
Amortisation of issue costs	(1.5)
Amortisation of gilt lock proceeds	0.1
Amortisation of bond premium	0.7
Finance lease interest	(1.0)
Dividends on preference shares	(4.6)
	(314.2)
Other interest expense	
Pension financing charge	(1.6)
	(1.6)

4 Corporation tax reconciliation

The tax assessed for the year is different to the standard rate of corporation tax in the UK and the reconciliation is shown in the table below.

	Appointed £m	Non- appointed £m
Profit before tax and fair value movement	(304.5)	1.7
Tax at the UK corporation tax rate of 19%	(57.8)	0.3
Permanent differences	1.2	–
Fixed asset timing differences	39.0	(0.3)
Other short-term timing differences	20.1	–
Pension cost relief in excess of pension charge	(2.5)	–
Group relief received for nil payment	–	–
Adjustment in respect of prior years – current tax	–	–
Tax charge for year	–	–

Details of factors affecting future tax charges:

The Spring Finance Bill 2023 confirmed increase in the main rate of UK corporation tax from 19% to 25%, effective 1 April 2023. All our deferred assets and liabilities will reverse after 1 April 2023 and therefore deferred tax has been calculated at the 25% rate.

Based on current capital investment plans, the company expects to continue to be able to claim capital allowances in excess of depreciation in future years at a similar level to the current year.

Comparison between tax charge and allowance in final determination

A comparison of the current appointed tax charge with the allowance in price limits is shown in the table and associated notes below:

	Current tax charge
	£m
i) Final determination allowance	–
ii) Price determination – tax not charged on forecast tax losses	(7.6)
iii) Earnings before interest and tax	(41.7)
iv) Regulatory settlement	3.9
v) Net finance costs, including taxable fair value movements	(54.9)
vi) Depreciation and capital allowances claimed	24.9
vii) Pensions	(4.4)
viii) Group relief claimed	–
ix) Change in tax rate	–
x) Other	76.0
Current tax before payments for group relief and prior year adjustments	–
xi) Payments for group relief	–
Appointed current tax charge	–

- i) In the price review process for the current regulatory period, 2020–25, there was no corporation tax forecast to be paid in the wholesale business and therefore there is no allowance for corporation tax in customer bills.
- ii) For 2022–23 the price determination included tax losses of £7.6 million and no allowance was provided for these in price limits.
- iii) Actual earnings before interest and tax are lower than those in the Final Determination. This is mainly driven by additional operating expenditure in both the wholesale and retail businesses.
- iv) In 2018–19 we made a provision for the regulatory settlement on revenues and did not reflect a reduction to our tax charge due to the reduced revenues in that year. During AMP7 this provision is released to the income statement, increasing revenues. We do not reverse this for tax purposes, instead recognising an increased tax charge due to the regulatory settlement.
- v) Net finance costs increased, reducing our tax charge, due to higher interest costs, higher inflation on index-linked debt instruments, and taxable fair value losses relating to debt indexation. This is partially offset by the interest receivable on our derivative financial instruments.
- vi) Lower capital allowances were claimed compared to the final determination as in 2022–23 we recorded a taxable loss.
- vii) We are making pension contributions in excess of those in the price determination. These additional contributions reduce our tax charge.
In 2021–22, a lump sum payment of £59.6 million, covering agreed contribution payments to March 2025, was made and has been subject to pension spreading rules for tax.
- viii) Historically we have used losses from other companies within the Greensands group to reduce the current tax charge for Southern Water. Capital allowances not claimed, in favour of group losses, were then available to Southern Water as a deduction against future taxable profits.
In 2022–23 we claimed no group losses.
- ix) The Final Determination assumed that corporation tax would be payable at a rate of 17%. The actual tax rate of 19% would, all other things being equal, increase/decrease our current tax charge/credit. Historically we have shown a small value in this reconciliation for the impact of the change in tax rate, applied to the current tax charge prior to the use of group relief. For 2022–23 the rate change impact is nil.
- x) In 2022–23 we incurred a tax loss of £84.3 million, this has been recorded within the deferred tax balance for the year, reducing the overall deferred tax liability.
- xi) As described above at (ix), we claimed no group relief in the year and have therefore made no payments.

Taxation policy and strategy

We manage our tax affairs in an open and transparent way and contribute materially to the Exchequer each year.

Our tax policy is consistent with the overall values and strategy of the company and will consider financial risk, reputational risk, and social responsibilities. Our approach to tax planning is to align to business decisions made in the best interests of customers and stakeholders rather than using tax planning to drive or determine business decisions. Our focus is therefore on compliance, and our tax planning is always aligned with our commercial and economic activity. The very nature of our business means we take a long-term view on all the activities we undertake and as a result we also ensure our tax strategy is sustainable.

Our approach to tax management is compliant with tax laws, rules, regulations and reporting requirements in all of its operations. A culture of doing the right thing is embedded in our core values and our approach to tax embodies this by ensuring we pay the right amount of tax, in the right place at the right time. Management of our tax affairs is carried out by an experienced internal tax team with the support of professional tax advisers and specialist tax support. Professional tax advisers are used in circumstances when additional advice is deemed appropriate (for example, to ensure compliance with new legislation and tax planning). We use specialist tax support in the preparation of our capital allowances.

Risk is managed by ensuring there are sufficient processes, systems, governance and appropriate controls in place. Internal assurance for the company is carried out by our Internal Audit team and we have also used the services of professional tax advisers to assist us with our tax compliance. Our tax policy extends to the wider group and ensures all companies within the Southern Water and Greensands groups are subject to UK tax, and all companies are UK tax resident irrespective of their place of incorporation.

A key factor in managing tax is our relationship with HMRC. We meet all statutory and legislative requirements and we manage our tax affairs in an open and transparent way. This extends to us sharing information with HMRC, such as internal audit findings. HMRC share our view of our low-risk approach to the management of our tax affairs with an assessment of us as a 'low-risk' company and this was reaffirmed in an Annual Conversation with HMRC in December 2022.

Further information is available in our Annual Report and Financial Statements on page 110.

5 Innovation Fund

For the period from 2020–25 Ofwat has introduced a series of innovation competitions. We are collecting monies from customers through our revenue across this regulatory period to fund these innovation competition activities. Several awards were made during 2022–23 for which we have paid the administration fees and contributions totalling £4.1 million. As disclosed above this payment has been re-classified through other income in the regulatory financial statements to exclude it from operating costs, as required by Ofwat, and ensure that it is reflected in retained earnings.

An accrual of £4.5 million, made for the liability associated with innovation fund income collected from customers but not yet paid out in awards, has been removed from the regulatory accounting statements in accordance with IN-2201 Expectations for monopoly company annual performance reporting 2021–22 as published by Ofwat.

Price control and other segmental reporting

2A – Segmental income statement for the 12 months ended 31 March 2023

	Retail		Wholesale				Total £m
	Retail household £m	Retail non-household £m	Water resources £m	Water network + £m	Wastewater network + £m	Bioresources £m	
Revenue – price control	45.400	–	25.268	184.669	445.124	47.573	748.034
Revenue – non price control	–	–	5.553	0.317	2.649	0.054	8.573
Operating expenditure – excluding PU recharge impact	(52.688)	–	(15.204)	(137.910)	(233.897)	(28.238)	(467.937)
PU opex recharge	(1.624)	–	(2.017)	(15.315)	21.904	(2.948)	–
Operating expenditure – including PU recharge impact	(54.312)	–	(17.221)	(153.225)	(211.993)	(31.186)	(467.937)
Depreciation – tangible fixed assets	(2.587)	–	(10.462)	(69.673)	(207.377)	(21.740)	(311.839)
Amortisation – intangible fixed assets	(1.740)	–	(0.131)	(0.494)	(16.920)	–	(19.285)
Other operating income	0.002	–	0.001	0.223	24.701	0.022	24.949
Operating profit/(loss)	(13.237)	–	3.008	(38.183)	36.184	(5.277)	(17.505)
Surface water drainage rebates							(0.427)

PU = Principal Use

2B – Totex analysis for the 12 months ended 31 March 2023 – Wholesale

	Water resources £m	Water network + £m	Wastewater network + £m	Bioresources £m	Total £m
Base operating expenditure					
Power	4.539	13.504	38.136	(1.830)	54.349
Income treated as negative expenditure	–	(0.041)	0.001	(3.406)	(3.446)
Abstraction charges/discharge consents	4.144	0.100	4.041	–	8.285
Bulk supply/bulk discharge	–	1.167	–	–	1.167
Renewals expensed in year (Infrastructure)	–	21.743	40.218	–	61.961
Renewals expensed in year (Non-Infrastructure)	–	–	–	–	–
Other operating expenditure	6.478	94.258	114.447	34.672	249.855
Local authority and Cumulo rates	0.999	11.296	13.355	1.750	27.400
Total base operating expenditure	16.160	142.027	210.198	31.186	399.571
Other operating expenditure					
Enhancement operating expenditure	0.088	6.582	–	–	6.670
Developer Services operating expenditure	–	1.510	1.795	–	3.305
Total operating expenditure excluding third party services	16.248	150.119	211.993	31.186	409.546
Third party services	0.973	3.106	–	–	4.079
Total operating expenditure	17.221	153.225	211.993	31.186	413.625
Grants and contributions					
Grants and contributions – operating expenditure	–	–	–	–	–
Capital expenditure					
Base capital expenditure	3.734	157.264	303.986	25.139	490.123
Enhancement capital expenditure	23.243	29.306	114.513	(0.026)	167.036
Developer Services capital expenditure	–	10.172	17.156	–	27.328
Total gross capital expenditure excluding third party services	26.977	196.742	435.655	25.113	684.487
Third party services	0.866	3.438	–	–	4.304
Total gross capital expenditure	27.843	200.180	435.655	25.113	688.791
Grants and contributions					
Grants and contributions – capital expenditure	0.868	5.477	8.307	–	14.652
Net totex	44.196	347.928	639.341	56.299	1,087.764
Cash expenditure					
Pension deficit recovery payments	–	–	–	–	–
Totex including cash items	44.196	347.928	639.341	56.299	1,087.764

2C – Cost analysis for the 12 months ended 31 March 2023 – Retail

	Household £m	Total £m
Operating expenditure		
Customer services	23.536	23.536
Debt management	8.213	8.213
Doubtful debts	12.012	12.012
Meter reading	3.948	3.948
Other operating expenditure	4.955	4.955
Local authority and Cumulo rates	0.024	0.024
Total operating expenditure excluding third party services	52.688	52.688
Depreciation		
Depreciation on tangible fixed assets existing at 31 March 2015	0.980	0.980
Depreciation on tangible fixed assets acquired after 1 April 2015	1.607	1.607
Amortisation on intangible fixed assets existing at 31 March 2015	1.030	1.030
Amortisation on intangible fixed assets acquired after 1 April 2015	0.710	0.710
Recharges		
Recharge from wholesale for legacy assets principally used by wholesale (assets existing at 31 March 2015)	0.082	0.082
Income from wholesale for legacy assets principally used by retail (assets existing at 31 March 2015)	–	–
Recharge from wholesale assets acquired after 1 April 2015 principally used by wholesale	1.542	1.542
Income from wholesale assets acquired after 1 April 2015 principally used by retail	–	–
Net recharges costs	1.624	1.624
Total retail costs excluding third party and pension deficit repair costs	58.639	58.639
Third party services operating expenditure	–	–
Pension deficit repair costs	–	–
Total retail costs including third party and pension deficit repair costs	58.639	58.639
Debt written off		
Debt written off	41.675	41.675
Capital expenditure		
Capital expenditure	4.524	4.524
Other operating expenditure includes the net retail expenditure for the following household retail activities which are part funded by wholesale		
Demand-side water efficiency – gross expenditure	–	
Demand-side water efficiency – expenditure funded by wholesale	–	
Demand-side water efficiency – net retail expenditure	–	
Customer-side leak repairs – gross expenditure	–	
Customer-side leak repairs – expenditure funded by wholesale	–	
Customer-side leak repairs – net retail expenditure	–	
Comparison of actual and allowed expenditure		
Cumulative actual retail expenditure to reporting year end	210.418	
Cumulative allowed expenditure to reporting year end	154.775	
Total allowed expenditure 2020–25	261.689	

Movement in costs from 2021–22

Household retail operating expenditure has decreased by £12.5 million to £52.7 million (2022: £65.2 million).

This is principally due to a reduction in the bad debt charge by £18.0 million to £12.0 million (2022 £30.0 million). The prior year bad debt charge included an additional one-off charge of £10.3 million to reflect the impact of high inflation on the cost-of-living and on customers' ability to pay. In addition, there was a reduction of £7.7 million reflecting the resumption of debt collection activities over the past 18 months following the pandemic.

Debt management costs have increased by £1.9 million to £8.2 million (2022 £6.2 million) due to the full resumption of debt collection activities that had been suspended during the period of the first national COVID-19 lockdown during 2021 and partially resumed in the prior year.

There have been increases in other costs with customer services costs rising by £2.8 million, meter reading costs increasing by £0.7 million due to increased activity levels and inflation.

Comparison to the final determination

Household

Total household retail costs totalling £58.6 million are £6.2 million higher than allowed in the Final Determination (£52.3 million). The increase is due to the following factors:

Debt management costs are £2.2 million higher than the business plan due to increased activity to optimise litigation, this is reflected in the year-on-year reduction in the under lying bad debt charge which is lower than the business plan by £0.5 million. Customer services costs are £5.5 million higher than the business plan, both due to transformational activities taking longer than planned. This is offset by £5.3 million lower allocated overheads due to the outsourcing of customer services.

Meter reading costs are £1.3 million over the business plan due to additional costs incurred as a result of increasing volumes of failing automatic reads.

The charge for depreciation and amortisation of tangible and intangible assets for the household retail business is £3.0 million higher than the allowance in the Final Determination. This all relates to the charge for depreciation and amortisation on assets acquired after March 2015.

Recharges from wholesale assets was not in the business plan and is therefore a variance of £1.6 million, this is offset by £1.5 million lower pension deficit repair costs which were prepaid in the prior year.

Non-household

On 1 April 2017 we exited the non-household retail business and our customers transferred to a specialist retail company, Business Stream.

2D – Historic cost analysis of tangible fixed assets – Wholesale and retail

	Wholesale				Retail	Total £m
	Water resources £m	Water network + £m	Wastewater network + £m	Bioresources £m	Household £m	
Cost						
At 1 April 2022	257.329	2,160.282	6,791.567	648.331	34.995	9,892.504
Disposals	(0.833)	(10.997)	(12.680)	(0.199)	–	(24.709)
Additions	27.988	200.968	405.569	25.315	3.821	663.661
Adjustments	–	–	–	–	–	–
Assets adopted at nil cost	–	–	11.404	–	–	11.404
At 31 March 2023	284.484	2,350.253	7,195.860	673.447	38.816	10,542.860
Depreciation						
At 1 April 2022	(77.512)	(694.689)	(2,311.469)	(310.471)	(28.222)	(3,422.363)
Disposals	0.833	10.995	12.651	0.199	–	24.678
Adjustments	–	–	–	–	–	–
Charge for year	(10.462)	(69.673)	(207.377)	(21.740)	(2.587)	(311.839)
At 31 March 2023	(87.141)	(753.367)	(2,506.195)	(332.012)	(30.809)	(3,709.524)
Net book amount at 31 March 2023	197.343	1,596.886	4,689.665	341.435	8.007	6,833.336
Net book amount at 1 April 2022	179.817	1,465.593	4,480.098	337.860	6.773	6,470.141
Depreciation charge for year						
Principal services	(8.773)	(67.706)	(207.027)	(21.739)	(2.587)	(307.832)
Third party services	(1.689)	(1.967)	(0.350)	(0.001)	–	(4.007)
Total	(10.462)	(69.673)	(207.377)	(21.740)	(2.587)	(311.839)

The net book value of tangible assets includes £733.0 million in respect of assets in the course of construction.

In order to present the intangible asset information alongside the fixed asset information Table 2O is presented below.

20 – Historic cost analysis of intangible assets – Wholesale and retail

	Wholesale				Retail	Total £m
	Water resources £m	Water network + £m	Wastewater network + £m	Bioresources £m	Household £m	
Cost						
At 1 April 2022	14.509	5.070	163.441	0.296	40.005	223.321
Disposals	–	–	(0.940)	–	–	(0.940)
Additions	(0.145)	(0.788)	30.086	(0.202)	0.703	29.654
At 31 March 2023	14.364	4.282	192.587	(0.094)	40.708	252.035
Amortisation						
At 1 April 2022	(8.693)	(2.927)	(98.573)	(0.094)	(16.616)	(126.903)
Disposals	–	–	0.940	–	–	0.940
Charge for year	(0.131)	(0.494)	(16.920)	–	(1.740)	(19.285)
At 31 March 2023	(8.824)	(3.421)	(114.553)	(0.094)	(18.356)	(145.248)
Net book amount at 31 March 2023	5.540	0.861	78.034	–	22.352	106.787
Net book amount at 1 April 2022	5.816	2.143	64.868	0.202	23.389	96.418
Amortisation charge for year						
Principal services	(0.130)	(0.486)	(16.920)	–	(1.740)	(19.276)
Third party services	(0.001)	(0.008)	–	–	–	(0.009)
Total	(0.131)	(0.494)	(16.920)	–	(1.740)	(19.285)

The net book value of intangible assets includes £39.1 million in respect of assets in the course of construction.

Additions for the year include items re-classified between business units from the prior year.

2E – Analysis of ‘grants and contributions’ for the 12 months ended 31 March 2023
– water resources, water network+ and wastewater network+

	Fully recognised in income statement £m	Capitalised and amortised (in the income statement) £m	Total £m
Grants and contributions – water resources			
Diversions – s185	–	–	–
Other contributions (price control)	–	0.868	0.868
Price control grants and contributions	–	0.868	0.868
Diversions – NRSWA	–	–	–
Diversions – other non-price control	–	–	–
Other contributions (non-price control)	–	–	–
Total	–	0.868	0.868
Value of adopted assets	–	–	–
Grants and contributions – water network+			
Connection charges	4.493	–	4.493
Infrastructure charge receipts	0.007	–	0.007
Requisitioned mains	0.628	0.572	1.200
Diversions – s185	(0.130)	–	(0.130)
Other contributions (price control)	–	1.443	1.443
Price control grants and contributions before deduction of income offset	4.998	2.015	7.013
Income offset	1.704	–	1.704
Price control grants and contributions after deduction of income offset	3.294	2.015	5.309
Diversions – NRSWA	0.168	–	0.168
Diversions – other non-price control	–	–	–
Other contributions (non-price control)	–	–	–
Total	3.462	2.015	5.477
Value of adopted assets	–	–	–
Grants and contributions – wastewater network+			
Receipts for on-site work	0.032	0.386	0.418
Infrastructure charge receipts	8.681	–	8.681
Diversions – s185	0.606	–	0.606
Other contributions (price control)	0.521	–	0.521
Price control grants and contributions before deduction of income offset	9.840	0.386	10.226
Income offset	2.585	–	2.585
Price control grants and contributions after deduction of income offset	7.255	0.386	7.641
Diversions – NRSWA	(0.111)	–	(0.111)
Diversions – other non-price control	–	–	–
Other contributions (non-price control)	–	0.777	0.777
Total	7.144	1.163	8.307
Value of adopted assets	11.404	–	11.404

2E – Analysis of ‘grants and contributions’ for the 12 months ended 31 March 2023 – water resources, water network+ and wastewater network+ – continued

IFRS 15 ‘Revenue from Contracts with Customers’ became effective for financial period commencing on or after 1 January 2018.

The effect of applying IFRS 15 results in the immediate recognition, on completion of the performance obligation, of developer related revenue relating to diversions, requisitions and adoptions, previously treated as deferred revenue. Until the performance obligation is completed the revenue for these activities will be deferred on the Balance Sheet.

Grants and contributions recognised in the statutory income statement as revenue have been reclassified to other income for regulatory purposes in table 1A. These include the amounts of £3.5 million and £7.1 million disclosed above for water and wastewater respectively together with £11.4 million of adopted assets.

	Water resources £m	Water network+ £m	Wastewater network+ £m	Total £m
Movements in capitalised grants and contributions				
Brought forward	5.347	10.750	13.638	29.735
Capitalised in year	0.868	2.015	1.163	4.046
Amortisation (in income statement)	(0.157)	(0.966)	(0.600)	(1.723)
Carried forward	6.058	11.799	14.201	32.058

2F – Residential retail for the year ended 31 March 2023

	Revenue £m	Number of customers 000's	Average residential revenues £
Residential revenue			
Wholesale charges	557.134		
Retail revenue	45.400		
Total residential revenue	602.534		
Retail revenue			
Revenue Recovered ('RR')	45.400		
Revenue sacrifice	–		
Actual revenue (net)	45.400		
Customer information			
Actual customers ('AC')		1,984.665	
Reforecast customers		1,999.237	
Adjustment			
Allowed revenue ('R')	43.179		
Net adjustment	(2.221)		
Other residential information			
Average residential retail revenue per customer			22.88

As we have exited the retail market and in accordance with the guidance in RAG 4.11, we are not required to report tables 2G and 2H.

2I – Revenue analysis for the 12 months ended 31 March 2023

	Household £m	Non- household £m	Total £m	Water resources £m	Water network+ £m	Total £m
Wholesale charge – water						
Unmeasured	17.949	1.236	19.185	2.305	16.880	19.185
Measured	140.891	48.531	189.422	22.756	166.666	189.422
Third party revenue	–	1.330	1.330	0.207	1.123	1.330
Total wholesale water revenue	158.840	51.097	209.937	25.268	184.669	209.937

	Household £m	Non- household £m	Total £m	Wastewater network+ £m	Bioresources £m	Total £m
Wholesale charge – wastewater						
Unmeasured – foul charges	83.512	2.849	86.361	77.179	9.182	86.361
Unmeasured – surface water charges	1.583	0.129	1.712	1.712	–	1.712
Unmeasured – highway drainage charges	0.955	0.068	1.023	1.023	–	1.023
Measured – foul charges	274.121	86.954	361.075	322.684	38.391	361.075
Measured – surface water charges	22.591	2.279	24.870	24.870	–	24.870
Measured – highway drainage charges	15.532	0.727	16.259	16.259	–	16.259
Third party revenue	–	1.397	1.397	1.397	–	1.397
Total wholesale wastewater revenue	398.294	94.403	492.697	445.124	47.573	492.697

Wholesale total	557.134	145.500	702.634			
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Retail revenue

Unmeasured	5.908	–	5.908			
Measured	39.492	–	39.492			
Other third party revenue	–	–	–			
Retail total	45.400	–	45.400			

Third party revenue – non-price control

Bulk supplies – water			4.529			
Bulk supplies – wastewater			1.796			
Other third party revenue			2.225			

Principal services – non-price control

Other appointed revenue			0.023			
Total appointed revenue			756.607			

2J – Infrastructure network reinforcement costs for the 12 months ended 31 March 2023

	Network reinforcement capex £m	On site / site specific capex (memo only) £m
Wholesale water network+ (treated water distribution)		
Distribution and trunk mains	(0.001)	4.092
Pumping and storage facilities	0.656	–
Total	0.655	4.092
Wholesale wastewater network+ (sewage collection)		
Foul and combined systems	10.369	2.560
Pumping and storage facilities	0.182	1.113
Total	10.551	3.673

2K – New connections – infrastructure charges reconciliation for the 12 months ended 31 March 2023

	Water £m	Wastewater £m	Total £m
Impact of infrastructure charge discounts			
Infrastructure charges	0.007	8.681	8.688
Discounts applied to infrastructure charges	0.072	–	0.072
Gross infrastructure charges	0.079	8.681	8.760
Comparison of revenue and costs			
Variance brought forward	3.435	(10.334)	(6.899)
Revenue	0.007	8.681	8.688
Costs	(0.655)	(10.551)	(11.206)
Variance carried forward	2.787	(12.204)	(9.417)

Infrastructure charges are received when new connections are made to the network and represent a contribution to the incremental impact additional connections have on the overall network. Network reinforcement costs represent the capital expenditure undertaken generally on our network to allow for the increased flows as a consequence of new connections/developments.

In order to be in a position to accept the flows as new connections are made it is necessary to complete the infrastructure enhancement in advance of the new connections meaning construction normally precedes income. For example, a further £3.9 million (2022: £8.4 million) has been expended in the year on providing a new 6.5km rising main to support an ongoing development at Chilmington Green near Ashford. This is a development of up to 7,500 new properties to be built over the coming years. We continue to increase capacity in several areas of our region, to support substantial long-term population growth, including Chichester £1.8 million, Bishops Waltham, £1.4 million and Bexhill £0.7 million.

The table above compares infrastructure charges received in the year with the level of general network reinforcement work. The variance in the year relates to the timing difference of completing these activities and is expected to even out over time.

2L – Analysis of land sales for the 12 months ended 31 March 2023

	Water resources £m	Water Network+ £m	Wastewater Network+ £m	Total £m
Proceeds from disposals of protected land	–	–	0.996	0.996

2M – Revenue reconciliation for the 12 months ended 31 March 2023 – wholesale

	Water resources £m	Water network+ £m	Wastewater network+ £m	Bioresources £m	Total £m
Revenue recognised					
Wholesale revenue governed by price control	25.268	184.669	445.124	47.573	702.634
Grants and contributions (price control)	0.868	5.309	7.641	–	13.818
Total revenue governed by wholesale price control	26.136	189.978	452.765	47.573	716.452
Calculation of the revenue cap					
Allowed wholesale revenue before adjustments (or modified by CMA)	29.632	187.364	454.131	49.965	721.092
Allowed grants and contributions before adjustments (or modified by CMA)	0.305	21.150	20.001	–	41.456
Revenue cap	29.937	208.514	474.132	49.965	762.548
Calculation of the revenue imbalance					
Revenue cap	29.937	208.514	474.132	49.965	762.548
Revenue recovered	26.136	189.978	452.765	47.573	716.452
Revenue imbalance	3.801	18.536	21.367	2.392	46.096

Overall wholesale price control revenue was £46.1 million (6.0%) lower than allowed in the final determination.

We under-recovered by £3.8 million (12.7%) in Water Resources and in Water Network+ we under-recovered by £18.5 million (8.9%). This under-recovery reflects both consumption being 2% lower than forecast and the decision of the Board to purposefully defer some revenues to later years to ensure that the increase in water supply bills faced by our customers was not excessive.

In Wastewater Network+ we under-recovered by £21.4 million (4.5%). In Bioresources the allowed wholesale revenue is as set out in Ofwat's final determination; the revenue imbalance of £2.4 million (4.8%) is due to the actual volume of sludge being lower than forecast in our business plan and reflected in the Final Determination from Ofwat. The revenue imbalance will be reconciled through a revenue adjustment to bills in year five of the AMP.

In total Grants and Contributions were £27.6 million below the allowed level. Contributions received for water resources were £0.6 million higher than our allowance, but this was offset by Water and Wastewater Network+, which were £15.8 million and £12.4 million lower than the Ofwat assumption respectively. Under Ofwat's 'single till' approach Grants and Contributions and wholesale revenues are treated as a single allowance; due to the forecast shortfall in Grants and Contributions we will recover more of the allowed revenues from wholesale water and wastewater charges than forecast in the Final Determination.

The shortfall in Grants and Contributions results primarily from reduced developer related activities in relation to requisitions, diversions and new connections. In addition, we have experienced increasing numbers of New Appointment Variations and water self-lay activity, resulting in much lower requisition volumes.

2N – Residential retail – social tariffs

	Revenue £m	Number of customers 000s	Average amount of customers £
Number of residential customers on social tariffs			
Residential water only social tariffs		2.100	
Residential wastewater only social tariffs		63.308	
Residential dual service social tariffs		47.731	
Number of residential customers not on social tariffs			
Residential water only no social tariffs		93.194	
Residential wastewater only no social tariffs		865.274	
Residential dual service no social tariffs		913.059	
Social tariff discount			
Average discount per water only social tariffs customer			47.143
Average discount per wastewater only social tariffs customer			64.099
Average discount per dual service social tariffs customer			88.580
Social tariff cross-subsidy – residential customers			
Total customer funded cross-subsidies for water only social tariffs customers	0.099		
Total customer funded cross-subsidies for wastewater only social tariffs customers	4.058		
Total customer funded cross-subsidies for dual service social tariffs customers	4.228		
Average customer funded cross-subsidy per water only social tariffs customer			1.039
Average customer funded cross-subsidy per wastewater only social tariffs customers			4.370
Average customer funded cross-subsidy per dual service social tariffs customer			4.401
Social tariff cross-subsidy – company			
Total revenue forgone by company to fund cross-subsidies for water only social tariffs customers	–		
Total revenue forgone by company to fund cross-subsidies for wastewater only social tariffs customers	–		
Total revenue forgone by company to fund cross-subsidies for dual service social tariffs customers	–		
Average revenue forgone by company to fund cross-subsidy per water only social tariffs customer			–
Average revenue forgone by company to fund cross-subsidy per wastewater only social tariffs customer			–
Average revenue forgone by company to fund cross-subsidy per dual service social tariffs customer			–
Social tariff support – willingness to pay			
Level of support for social tariff customers reflected in business plan			6
Maximum contribution to social tariffs supported by customer engagement			13

We have updated the maximum contribution to social tariffs supported by customer engagement to reflect the level above which most of the customers surveyed confirmed an increase would be unacceptable. We consulted with our regulators in July 2022 for their approval to increase the support we provide to those customers most in need.

Independent Auditor's report

Independent auditor's report to the Water Services Regulation Authority (the WSRA) and Directors of Southern Water Services Limited

Opinion

We have audited the sections of Southern Water Services Limited's ("the Company") Annual Performance Report for the year ended 31 March 2023 ("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.8, 1F.12 to 1F.14, 1F.21 to 1F.22 and 1F.24 to 1F.26 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 – wholesale (table 2B), the cost analysis – retail (table 2C), the historical cost analysis of fixed assets (table 2D), the analysis of grants and contributions (table 2E), the residential retail (table 2F), the non-household water revenues by tariff type (table 2G), the non-household wastewater revenues by tariff type (table 2H), the revenue analysis (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.9 to 1F.11, 1F.15 to 1F.20 and 1F.23 of the statement of financial flows (table 1F), the Outcome performance table (tables 3A to 3I) or the additional regulatory information in tables 4A to 4W, 5A to 5B, 6A to 6F, 7A to 7F, 8A to 8D, 9A, 10A to 10E and 11A.

In our opinion, Southern Water Services 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 2.09, RAG 3.14, RAG 4.11 and RAG 5.07) and the accounting policies (including the Company's published accounting methodology statement(s), as defined in RAG 3.14, appendix 2), set out on page 28.

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.

Material uncertainty relating to going concern

We draw attention to note 1a to the Regulatory Accounting Statements, which indicates that the planned equity raise of £375 million required to have sufficient liquidity over the going concern period has not been committed at the date of signing the financial statements. As stated in note 1a to the Regulatory Accounting Statements, these events or conditions, along with the other matters as set forth, indicate that a material uncertainty exists that may cast significant doubt on the company’s ability to continue as a going concern. Our opinion is not modified in respect of this matter.

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 3.14, 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. As a result, the Regulatory Accounting Statements may not be suitable for another purpose. 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 (“UK 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 19 to 82 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.

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 17, the directors are responsible for the preparation of the Annual Performance Report in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the Company's accounting policies (including the Company's published accounting methodology statement(s), as defined in RAG 3.14, 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 the 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 WSRA, 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 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, in-house and external 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, the audit committee, reviewing internal audit reports and reviewing correspondence with Ofwat and other regulatory authorities; 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.

A further description of our responsibilities for the audit of the Regulatory Accounting Statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/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 WSRA in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewage undertaker under the Water Industry Act 1991 (“Condition F”). Our audit work has been undertaken so that we might state to the Company and the WSRA those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under Condition F to procure such a report and (b) to facilitate the carrying out by the WSRA of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the WSRA, for our audit work, for this report or for the opinions we have formed.

Our opinion on the Regulatory Accounting Statements is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2023 on which we reported on 7 July 2023, 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 2023

Performance Summary

Assurance

KPMG LLP were engaged to provide independent limited assurance over the selected annual performance data highlighted in this section marked with the symbol Δ for the calendar year ended 31 December 2022 and the information marked with the symbol * for the financial year ended 31 March 2023 using the assurance standard ISAE (UK) 3000. KPMG LLP has provided assurance only over the performance level reported for 2022–23. KPMG LLP has issued an unqualified opinion over the selected annual performance data which is available on page 68.

3A – Outcome performance – Water common performance commitments

Common performance commitments – Water (Financial)	Status	Unit	Performance level – actual	PCL met?	Outperformance or underperformance payment	Forecast of total 2020–25 outperformance or underperformance payment
Water quality compliance (CRI) Δ		number	6.38	No	(2.751)	(10.243)
Water supply interruptions*		hh:mm:ss	1:28:10	No	(4.148)	(11.273)
Leakage*		%	0.2	No	(2.332)	(8.918)
Per capita consumption*		%	(4.5)	No	–	(9.790)
Mains repairs*		number per 1,000 km of main	152.8	No	(3.788)	(14.305)
Unplanned outage*		%	6.44	Yes	–	–
Bespoke performance commitments – Water and Retail (Financial)						
Drinking water appearance Δ		nr	0.93	No	(1.294)	(4.020)
Drinking water taste and odour Δ		nr	0.24	No	(0.046)	(0.277)
Abstraction Incentive Mechanism*		nr	-14	No	(0.634)	0.899
Access to daily water consumption data		nr	–	No	–	–
Void properties*		%	2.82	No	(0.600)	(2.760)
Replace lead customer pipes		nr	–	No	–	–
Properties at risk of receiving low pressure*		nr	207	Yes	–	(0.341)
Long term supply demand schemes		months	50	No	–	(27.323)
Impounding reservoirs		%	–	No	(0.324)	(2.267)
Financial water performance commitments achieved	%	–		13		
Overall performance commitments achieved (excluding C-MeX and D-MeX)	%	–		33		

Notes:

Each performance commitment is shown with the assessed performance status (red, amber or green) which indicates performance against expectations. An explanation of each performance commitment, the definitions and the criteria for assessment is given in appendix 2.

3B – Outcome performance – Wastewater common performance commitments

Common performance commitments – Wastewater (Financial)	Status	Unit	Performance level – actual		Outperformance or underperformance payment	Forecast of total 2020–25 outperformance or underperformance payment
			Current reporting year	PCL met?		
Internal sewer flooding*	⊖	Number of incidents per 10,000 sewer connections	2.25	No	(3.723)	(13.837)
Pollution incidents ^Δ	⊖	Number of incidents per 10,000 km of sewer	90.11	No	(8.193)	(41.256)
Sewer collapses*	⊖	Number of sewer collapses per 1,000 km of all sewers	6.18	No	(1.087)	(11.776)
Treatment works compliance ^Δ	⊖	%	98.22	No	(7.800)	(37.800)
Bespoke performance commitments – Wastewater (Financial)						
Effluent re-use	✓	nr	82	Yes	0.000	0.001
Renewable generation	✗	%	13.03	No	(1.326)	(6.630)
Satisfactory bioresources recycling ^Δ	✓	%	100.00	Yes	–	–
River water quality*	✓	nr	102.70	Yes	–	–
Maintain bathing waters at 'Excellent' ^Δ	✓	nr	57	Yes	–	–
Improve the number of bathing waters to at least 'Good' (Cost Adjustment Claim) ^Δ	✓	nr	–	–	–	(3.704)
Improve the bathing waters at 'Excellent' quality (Cost Adjustment Claim) ^Δ	✓	nr	–	–	–	(1.700)
Surface water management	⊖	m ³	–	No	(0.052)	(0.239)
External sewer flooding*	✓	nr	3,748	Yes	0.669	1.631
Thanet sewers	✓	months	–	Yes	–	–
Financial wastewater performance commitments achieved	%	–		50		

Key

- ✓ Ofwat target met or exceeded
- ⊖ Ofwat target missed but performance improved in relation to prior year outcome
- ✗ Ofwat target missed and performance worse than prior year outcome
- Not applicable

3C – Customer measure of experience (C-MeX) table

Item	Unit	Value
Annual customer satisfaction score for the customer service survey	Number	66.69
Annual customer satisfaction score for the customer experience survey	Number	72.85
Annual C-MeX score*	Number	69.77
Annual net promoter score	Number	(7.50)
Total household complaints	Number	46,605
Total connected household properties	Number	2,048,390
Total household complaints per 10,000 connections	Number	227.520
Confirmation of communication channels offered	True or False	True

Notes:

Each performance commitment is shown with the assessed performance status (red, amber or green) which indicates performance against expectations. An explanation of each performance commitment, the definitions and the criteria for assessment is given in appendix 2.

3D – Developer services measure of experience (D-MeX) table

Item	Unit	Value
Qualitative component annual results	Number	62.85
Quantitative component annual results	Number	98.26
D-MeX score*	Number	80.56
Developer services revenue (water)	£m	7.953
Developer services revenue (wastewater)	£m	10.226

Calculating the D-MeX quantitative component

Water UK performance metric	Unit	Reporting period (1 April to 31 March)	Quantitative score (annual)
W1.1 Pre-development enquiry – reports issued within target	%	100.00%	
W3.1 s45 quotations – within target	%	99.43%	
W4.1 s45 service pipe connections – within target	%	95.04%	
W6.1 Mains design	%	95.56%	
W7.1 Mains design >500 plots – quotations within target	%	–	
W8.1 Mains construction within target	%	100.00%	
W17.1 Mains diversions (without constraints) – quotations within target	%	86.67%	
W17.2 Mains diversions (with constraints) – quotations within target	%	100.00%	
W18.1 Mains diversions – construction/commissioning within target	%	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 reports >500 plots etc – reports issued within target	%	100.00%	
W23.1 Self lay design and terms request	%	100.00%	
W24.1 Self lay design and terms request >500 plots etc – quotations within target	%	100.00%	
W26.1 Self lay water for pressure/bacteriological testing – provided within target	%	100.00%	
W27.1 Self lay permanent water supply– provided within target	%	100.00%	
W30.1 Self lay plot references and costing details – issued within target	%	–	

Calculating the D-MeX quantitative component (continued)

Water UK performance metric	Unit	Reporting period (1 April to 31 March)	Quantitative score (annual)
S1.1 Pre-development enquiry – reports issued within target	%	100.00%	
S3.1 Sewer requisition design – offers issued within target	%	100.00%	
S4.1 Sewer requisition – constructed and commissioned within agreed extension	%	–	
S7.1 Adoption legal agreement – draft agreements issued within target	%	100.00%	
SN2.2 % Bulk discharge offer letters issued to the applicant within target period	%	100.00%	
SN4.1 % of main laying schemes constructed and commissioned within the target period	%	–	
WN1.1 % of 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%	
WN4.1 % of main laying schemes constructed and commissioned within the target period	%	100.00%	
WN4.2 % of testing supplies provided within target period	%	–	
WN4.3 % of permanent supplies made available within the target period	%	–	
SAM – 3/1 Update draft agreement	%	100.00%	
SAM – 4/1 Inspections and construction period	%	100.00%	
D-MeX quantitative score (for the relevant reporting period)	%	98.26%	
D-MeX quantitative score (annual)	Number		–

3E – Outcome performance – Non financial performance commitments

Common	Status	Unit	Performance level – actual	
			Current reporting year	PCL met?
Risk of severe restrictions in a drought*		%	–	Yes
Priority services for customers in vulnerable circumstances – PSR reach*		%	8.3	No
Priority services for customers in vulnerable circumstances – Attempted contacts*		%	112.0	Yes
Priority services for customers in vulnerable circumstances – Actual contacts*		%	22.0	No
Risk of sewer flooding in a storm		%	11.55	Yes
Bespoke performance commitments				
Target 100*		%	37	No
Water saved from water efficiency visits		m ³ /day	534	No
Effectiveness of financial assistance		%	71	No
Customer satisfaction with vulnerability support*		%	73	No
Community engagement		rank	–	No
Schools visited and engagement with children		%	98.00	No
Water supply resilience*		nr	129,111	Yes
Combined Sewer Overflows (CSO) monitoring		%	87.93	No
Natural capital		nr	3	Yes
Gap sites*		nr	37	No
Distribution input*		MI/day	566	No
Value for money		%	67	No
WINEP delivery*		text	Not met	No
Non-financial water performance commitments achieved		%		39

3F – Underlying calculations for common performance commitments – water and retail

Performance commitments set in standardised units – Water	Status	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 1000 km	Mains length in km	13,919.00	1,397	100.37
Mains repairs – Proactive	✘	Mains repairs per 1000 km	Mains length in km	13,919.00	730	52.45
Mains repairs	✘	Mains repairs per 1000 km	Mains length in km	13,919.00	2,127	152.81
Per capita consumption (PCC)	⊖	l/p/d	Total household population (000s) and household consumption (Ml/d)	2,612.80	336	128.40

Performance commitments measured against a calculated baseline	Status	Unit	Performance level – actual				Performance level – actual			Performance level 3 year average	Calculated performance level to compare against PCLs
			(2017 –18)	(2018 –19)	(2019 –20)	Baseline	(2020 –21)	(2021 –22)	(2022 –23)		
Leakage	✘	Ml/d	102.6	102.9	94.1	99.9	93.8	96.8	108.5	99.7	0.2
Per capita consumption (PCC)	⊖	l/p/d	126.0	129.6	128.1	127.9	139.0	133.6	128.4	133.7	-4.5

Water supply interruptions	Status	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	1,143.3	100809915	85,894	1:28:10

Unplanned or planned outage	Status	Current company level peak week production capacity (PWPC) Ml/d	Reduction in company level PWPC Ml/d	Outage proportion of PWPC %
Unplanned outage	✔	867.67	55.89	6.44%

Priority services for customers in vulnerable circumstances	Status	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	✔	1,993	166,384	8.3%	30,231.0	33,863	112.0%	6,657.0	22.0%

3G – Underlying calculations for common performance commitments – wastewater

Performance commitments set in standardised units	Status	Units	Standardising data indicator	Standardising data numerical value	Performance level – actual current reporting year	Calculated performance level
Internal sewer flooding – customer proactively reported	⊖	Number of incidents per 10,000 sewer connections	Number of sewer connections	2,030.28	393	1.94
Internal sewer flooding – company reactively identified (i.e. neighbouring properties)	⊖	Number of incidents per 10,000 sewer connections	Number of sewer connections	2,030.28	63	0.31
Internal sewer flooding	⊖	Number of incidents per 10,000 sewer connections	Number of sewer connections	2,030.28	456	2.25
Pollution incidents	⊖	Number of incidents per 10,000 km of sewer	Sewer length in km	39,729.00	358	90.11
Sewer collapses	⊖	Number of sewer collapses per 1,000 km of all sewers	Sewer length in km	39,973.00	247	6.18

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	(0.958)
Water network+	(14.399)
Wastewater network+	(20.521)
Bioresources (sludge)	(1.286)
Residential retail	(0.600)
Business retail	–
Dummy control	–

Initial calculation of end of period revenue adjustment by price control

Water resources	(2.011)
Water network+	(35.215)
Wastewater network+	–
Bioresources (sludge)	–
Residential retail	–
Business retail	–
Dummy control	–

Initial calculation of end of period RCV adjustment by price control

Water resources	–
Water network+	–
Wastewater network+	–
Bioresources (sludge)	–
Residential retail	–
Business retail	–
Dummy control	–


3I – Supplementary outcomes information

Unplanned or planned outage	Status	Current company level peak week production capacity (PWPC) MI/d	Reduction in company level PWPC MI/d	Outage proportion of PWPC %
Unplanned outage		867.67	10.78	1.24%

Risk of severe restrictions in drought	Status	Deployable output MI/d	Outage allowance MI/d	Dry year demand MI/d	Target headroom MI/d	Total population supplied	Customers at risk
Risk of severe restrictions in drought		757.59	94.28	566.00	24.84	2,665,515.00	No

Risk of sewer flooding in a storm	Status	Total pe served	Total pe in excluded catchments	Percentage of total pe in excluded catchments
Risk of sewer flooding in a storm		4,809,665.85	0.00	0.00%

Risk of sewer flooding in a storm	Status	Total pe Option 1a	Percentage of total pe Option 1a	Total pe Option 1b	Percentage of total pe Option 1b	Vulnerability risk grade Percentage of total population served		
						Low	Medium	High
Risk of sewer flooding in a storm		239,326.78	4.87%	4,575,339.07	95.13%	88.45%	3.82%	7.73%

Sewer collapses	Status	Number of patch repairs or relining undertaken on sewer and not included in reported sewer collapses
Sewer collapses		912

2022–23 performance against performance commitments

In 2022–23 we met or exceeded 15 of our 47 performance commitments compared to 18 in 2021–22. However we did see improved performance in some areas, outperforming on external sewer flooding, unplanned outage, and priority services measures, including a ODI reward of £0.7 million for reducing external flooding below the target set.

We incurred a net ODI underperformance payment for wholesale services of £37.8 million, compared to £34.4 million in 2021–22. The overall level of penalties incurred reflect the continued significant level of performance challenge in Ofwat’s PR19 final determination.

For Ofwat’s C-MeX and D-MeX measures of customer experience, which are based on comparative performance, we also forecast higher penalties than for 2021–22 at £4.8 million and £1.0 million respectively (2021–22: £4.2 million and £0.9 million).

The impact of these penalties and rewards will be reflected in customers’ bills from 2024–25.

We comment here on the wholesale performance commitments associated with the largest underperformance payments⁴. A full description of performance against all our performance commitments is provided in our Annual Report and Financial Statements.

Pollution incidents (penalty: £8.2 million)

Whilst we continue to reduce the number of pollutions each year, with a marginal improvement in 2022 compared to 2021, we remain well above our Ofwat target. We are working hard to make significant improvements in this area and understand the priority that protecting the environment has for all our customers and stakeholders and know that our performance needs to reflect this.

We have made further changes to the Pollution Incident Reduction Plan, which sets out how we will aim to reduce the annual number of pollutions to between 77 – 98 by the end of 2024 and aims for zero by 2040. The PIRP strategy has already laid the foundations for a continued steady improvement in our performance, informing future plans by showing the trends in pollutions from all sources, including electrical and mechanical (MEICA), blockages and bursts, as well as pollutions from sewer blockages. Our 2023 Improvement Plans are focused into three main categories containing 18 separate initiatives delivering a benefit reduction of between 126–212 pollutions.

Wastewater treatment works compliance (underperformance payment: £7.8 million)

The number of our treatment works that were classified as failed works by the Environment Agency fell from seven to six in the 2022 calendar year, continuing the improvement seen in 2021.

As mentioned in our turnaround plan and Annual Report and Financial Statements, we are making significant investments to make sure our assets work to capacity. We are continuing to update our maintenance standards and proactive control to stop assets failing and developing an improved emergency response to further reduce the number of failing works. Our plans moving forward are focused on the root cause of technical failures so we can prevent them in the future, building capacity and resilience at our wastewater treatment works to reach 99%+ compliance with treatment and permit standards.

Water supply interruptions (underperformance payment: £4.2 million)

Several significant incidents during 2022–23 left our customers without supply for a longer than average time. This has taken the average number of minutes that our customers were without water to 01:28:10 exceeding target of 00:05:45 by a significant margin.

Up until June 2022, we saw a decrease in water supply interruptions compared to 2021–22 and a reduction in mains bursts in the same period. Since June, we had a number of atypical bursts which affected large numbers of customers.

In July, a single event on the Isle of Sheppey contributed 35 minutes to the overall year total. In November, another significant event at our Rumfields site in Broadstairs Kent contributed almost 23 minutes, this was followed by two events in December at our Yew Hill WSR in Hampshire adding 32 minutes, and a second event at Rumfields in January adding another two minutes to the total. Excluding these exceptional events would have seen an outcome of 00:07:23 in line with our 2022–23 execution plan.

Since these incidents, we have improved our response by ensuring better communication with customers, such as using text messages to keep customers updated during an incident. We now provide more frequent incident updates on social media and the website, including the incident map. By increasing resources, we have been able to respond more quickly to social media messages and posts.

We have also made sure that bottled water availability and deliveries have been improved, so we can open bottled water stations more quickly when required, as well as providing more effective delivery of bottled water to our vulnerable customers.

⁴ Comment is provided for all performance commitments with an underperformance penalty of greater than £1 million for 2022–23. In addition, we provide a brief commentary on per capita consumption performance, due to the level of stakeholder interest in this area and on long term supply demand schemes

Our turnaround plan to improve performance over the next two years includes upgrades to our logistics capability so we can move people and materials around faster. This includes a new tanker fleet, storage of critical spares and an overhaul of our work management processes.

**Main repairs
(underperformance payment £3.8 million)**

A focused effort on reducing leakage through proactive detection coupled with weather conditions exhibiting both a high and low temperature variations included the drought conditions over the summer period and a cold harsh weather winter event in December has seen both an increase in demand and resultant mains failures resulting in us exceeding this year's performance commitment and generating an associated penalty. As part of our action plan to reduce leakage has delivered a programme of Advanced Pressure management schemes within this reporting period which will continue over the two next years to improve performance in this area.

**Internal sewer flooding
(underperformance payment: £3.7 million)**

As in 2020–21 and 2021–22, we beat our target for external sewer flooding, but we fell short of our target for internal sewer flooding, although the number of internal flooding incidents decreased significantly from 614 in 2021–22 to 456 in 2022–23. We know this is an area that we must do better in, and are continuing to have improving our performance in this area as a key focus for us.

Digitalising our wastewater network will make a significant difference to our ability to detect and even predict flooding incidents as well as sewer blockages. We have installed 23,000 sewer level monitors to send water level data back to a powerful machine-learning tool, focusing on hotspot areas. Our dedicated Pollution and Flooding Resilience team and our Zero Flooding project aims to eliminate sewer flooding incidents in key hotspots across our regions. We are also continuing our fat, oil and grease (FOG) and Unflushables campaign to explain to customers what can go down the toilet or the sink, as well as improving our incident response.

In line with our turnaround plan, we have set an ambitious target to outperform our internal flooding targets for the remainder of the AMP in the absence of further severe weather events.

**Compliance Risk Index
(underperformance payment: £2.8 million)**

We have seen a marginal decrease in CRI score for 2022 to 6.38 (2021: 6.69). Whilst we are disappointed in this performance, we recognise that the main causes of CRI at our works (70%) were damp and unused sections of pipe, which are being addressed through improved regular maintenance of water tanks. A further quarter was due to issues at our sampling facilities, which are regularly inspected. The remainder of this was an increase in CRI at customer taps due to sediment build up in the mains, which will be addressed by our wider replacement programme in the next seven years.

Despite this, we maintain our performance in water quality, with 99.97% of water quality samples met all of the required DWI standards and are targeting to have reduced CRI to below our year 1 score of 4.53 by the end of the AMP.

**Leakage
(underperformance payment: £2.3 million)**

Despite additional investment during the year, our leakage level for the 2022–23 year was 108.5 megalitres per day (MI/d), resulting in an increase to the overall measure on a three-year rolling average basis to 99.7MI/d, (2021–22: 94.9 MI/d). This is higher than forecast, with unprecedented weather conditions over the drought in the summer and rapid changes in temperatures during the winter resulted in high leakage levels.

In order to reduce leakage levels to an acceptable level, we have already increased find and fix activity, and understanding the opportunities that new technologies present us with to improve the management of our network, and we're installing monitors and sensors on our network. We'll continue to invest in systems and tools that help us to maximise the data available, so we can find and fix more leaks faster and make our networks more efficient. We are aware that we may not reach the end of AMP target of a 15% reduction in leakage, and as part of our turnaround plan have committed to maintaining a leakage level below 100 MI/d by 2025.

**Renewable generation
(underperformance payment: £1.3 million)**

We saw a continued fall in the level renewable energy generated to 13.30% (2021–22: 15.85%), falling below our target of 24%. As mentioned in our Annual Report and Financial Statements, the percentage of energy produced is affected by the amount of Combined Heat and Power (CHP) generation as well as the amount of overall electricity we use. Our CHP generation reduced due to a number of CHP failures, making the equipment unavailable, and we had to import more electricity than normal due to increased use of pumps during periods of wet weather. We remain committed to using renewable sources of energy where we can, and continue to have 100% of the energy we use being green.

**Drinking water appearance
(underperformance payment: £1.3 million)**

We saw a drop in performance in 2022, impacted by high proportion of contacts related to Rownhams, Harham, Twyford and Yew Hill water supply zones. The score was also impacted by network incidents (mains bursts and mains repairs) in the summer and a resulting spike in contacts in July and August. Benefits have been seen from flushing programmes covering the following water supply zones (Fairlight; Borstal; Wigmore; Colewood; Cobham; Darland) achieving contact reduction between 39% and 82% by area. Proactive flushing continues in the Rowhams area, alongside network activities including identification of key risk areas, proactive air valve maintenance, development of a system health check and an increase in network inspector resources to increase the overall level of proactive maintenance.

**Sewer collapses
(underperformance payment: £1.1 million)**

Despite having successfully reduced the number of incidents for the third year running, with a 21% reduction compared with 2021–22, we have not met our target. As part of our turnaround plan we will continue to reduce the number of collapses each year; performance will, however, remain above target to the end of AMP7.

**Per capita consumption – PCC
(underperformance payment: n/a)**

Whilst customer consumption has been impacted across the industry by the COVID-19 pandemic, we continue to see a reduction in year of PCC, with consumption levels having come down gradually from their pandemic peak of 138.5 l/p/d to an average of 128.4 l/p/d over 2022–23, resulting in a three-year rolling average of 133.7 l/p/d.

Our water efficiency plan is evolving post-pandemic to manage and reduce consumption, and our aim is for this to be a blueprint for long-term behaviour change rooted in behavioural science principles with the single aim of creating a consciously water-efficient culture. We want to create a future where all our customers, stakeholders and employees are water stewards: fully aware of their water environment, feel connected to it, and willing to play their part in protecting and preserving it to support our mission statement of Water for life.

Over the last year, we have worked with customers across our region and gained vital intelligence from ethnographic studies to inform our design of water-saving options. We have identified seven catalysts that will accelerate behaviour change among householders: home audits, smart meter technology, tariffs, communications and marketing, education, water-efficiency solutions, and government interventions. Further information on which can be found both in our Annual Report and Financial Statements and in our APR supporting commentary 2022–23.

We recognise that despite our considerable efforts around our T100 performance commitment, the success of home audits and drought campaigns, we're still above forecast and are likely to end the AMP above our baseline of 128 l/p/d.

Long term supply demand schemes

Within our PR19 final determination, we have an ODI to ensure that we remain on track to deliver a number of supply demand schemes by no later than 31 March 2027. ODI penalties are incurred for every month of delay to the schemes.

Delivery of these schemes is now underway, including replacement schemes where we have not been able to progress existing schemes. A number have experienced unavoidable delays which has meant progress is currently behind the original delivery schedule, which is reflected in the table above.

We are in the process of procuring an appropriately qualified external third party to carry out a formal review to inform the PR24 price review that will determine the progress of the schemes and be submitted alongside our business plan. Whilst we hope these are significantly reduced in the formal review, we are currently forecasting a 50-month delay and a shortfall of 45.8Ml/d.

Forecasts of future years' performance

As required by Ofwat, we have provided a forecast of total 2020–25 outperformance or underperformance payments for all performance commitments. These represent a current best estimate based on our turnaround plan. This plan will be updated over the next two years to reflect ongoing performance and thus forecasts of outperformance or underperformance payments. We will continue to strive to meet the targets set in the final determination and reduce the level of underperformance payments incurred.

Reporting to customers

Ofwat requires us to describe how the information reported in the Section 3 of this Annual Performance Report relates to the information on outcome performance we have published and reported to our customer challenge group or similar body and customers more generally. We can confirm that the performance commitment information reported here is fully consistent with the information we have reported to our customers in our Annual Report and Financial Statements. We have been updating our Customer and community challenge panel throughout the year on our level of performance and they will be informed of our 2022–23 results here.

Independent Limited Assurance Report of KPMG LLP to Southern Water Services Limited

KPMG LLP ('KPMG' or 'we') were engaged by Southern Water Services Limited ('Southern Water') to provide limited assurance over the Selected Information described below for the year ended 31 March 2023 and the calendar year ended 31 December 2022.

Our conclusion

Based on the work we have performed and the evidence we have obtained, nothing has come to our attention that causes us to believe that the Selected Information has not been properly prepared, in all material respects, in accordance with the Reporting Criteria.

This conclusion is to be read in the context of the remainder of this report, in particular the inherent limitations explained below and this report's intended use.

Selected Information

The scope of our work includes only the information included within the Southern Water Annual Performance Report ('the Report') in respect of the year ended 31 March 2023 marked with the symbol * and in respect of the calendar year ended 31 December 2022 marked with the symbol Δ (together 'the Selected Information').

We have not performed any work, and do not express any conclusion, over any other information that may be included in the Report or displayed elsewhere on Southern Water's website for the current year or for previous periods unless otherwise indicated.

Reporting Criteria

The Reporting Criteria we used to form our judgements are the Southern Water Reporting Criteria 2022–23 as set out at [southernwater.co.uk/our-performance/reports/annual-reporting](https://www.southernwater.co.uk/our-performance/reports/annual-reporting) ('the Reporting Criteria').

The Selected Information needs to be read together with the Reporting Criteria.

Inherent limitations

The nature of non-financial information; the absence of a significant body of established practice on which to draw; and the methods and precision used to determine non-financial information, allow for different, but acceptable evaluation and measurement techniques and can result in materially different measurements, affecting comparability between entities and over time.

The Reporting Criteria has been developed to assist Southern Water in detailing the methodology applied in their reporting obligations under the 2019 Price Review as prescribed by Ofwat. As a result, the Selected Information may not be suitable for another purpose.

Directors' responsibilities

The Directors of Southern Water are responsible for:

- designing, operating and maintaining internal controls relevant to the preparation and presentation of the Selected Information that is free from material misstatement, whether due to fraud or error;
- selecting and/or developing objective Reporting Criteria;
- measuring and reporting the Selected Information in accordance with the Reporting Criteria; and
- the contents and statements contained within the Report and the Reporting Criteria.

Our responsibilities

Our responsibility is to plan and perform our work to obtain limited assurance about whether the Selected Information has been properly prepared, in all material respects, in accordance with the Reporting Criteria and to report to Southern Water in the form of an independent limited assurance conclusion based on the work performed and the evidence obtained.

Assurance standards applied

We conducted our work in accordance with International Standard on Assurance Engagements (UK) 3000 *Assurance Engagements other than Audits or Reviews of Historical Financial Information* ('ISAE (UK) 3000') issued by the Financial Reporting Council. That Standard requires that we obtain sufficient, appropriate evidence on which to base our conclusion.

Independence, professional standards and quality control

We comply with the Institute of Chartered Accountants in England and Wales ('ICAEW') Code of Ethics which includes independence, and other requirements founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour, that are at least as demanding as the applicable provisions of the IESBA Code of Ethics. The firm applies International Standard on Quality Management 1 Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements which requires the firm to design, implement and operate a system of quality management including policies or procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

Summary of work performed

A limited assurance engagement involves planning and performing procedures to obtain sufficient appropriate evidence to obtain a meaningful level of assurance over the Selected Information as a basis for our limited assurance conclusion. Planning the engagement involves assessing whether the Reporting Criteria are suitable for the purposes of our limited assurance engagement. The procedures selected depend on our judgement, on our understanding of the Selected Information and other engagement circumstances, and our consideration of areas where material misstatements are likely to arise.

The procedures performed included:

- assessing on a sample basis whether the Selected Information has been collected and reported in accordance with the applicable criteria;
- conducting interviews with Southern Water's management to obtain an understanding of the key processes, systems and controls in place over the preparation of the Selected Information;
- selected limited substantive testing, including agreeing a selection of the Selected Information to corresponding supporting information, including to independent databases and monitoring systems such as Waternet, Prism, SAP BI, Qlikview, CSM and to regulatory returns from Water UK, the Drinking Water Inspectorate (DWI) and the Environment Agency (EA);
- performing analytical procedures over the aggregated Selected Information, including a comparison to the prior period's amounts having due regard to changes in business volume; and

- reading the Report and narrative accompanying the Selected Information in the Report with regard to the Reporting Criteria, and for consistency with our findings.

The work performed in a limited assurance engagement varies in nature and timing from, and is less in extent than for, a reasonable assurance engagement. Consequently, the level of assurance obtained in a limited assurance engagement is substantially lower than the assurance that would have been obtained had a reasonable assurance engagement been performed.

This report's intended use

Our report has been prepared for Southern Water solely in accordance with the terms of our engagement. We have consented to the publication of our report in the Report for the purpose of Southern Water showing that it has obtained an independent assurance report in connection with the Selected Information.

Our report was designed to meet the agreed requirements of Southern Water determined by Southern Water's needs at the time. Our report should not therefore be regarded as suitable to be used or relied on by any party wishing to acquire rights against us other than Southern Water for any purpose or in any context. Any party other than Southern Water who obtains access to our report or a copy and chooses to rely on our report (or any part of it) will do so at its own risk. To the fullest extent permitted by law, KPMG LLP will accept no responsibility or liability in respect of our report to any other party.



KPMG LLP

Chartered Accountants
London,
14 July 2023

The maintenance and integrity of Southern Water's website is the responsibility of the Directors of Southern Water; the work carried out by us does not involve consideration of these matters and, accordingly, we accept no responsibility for any changes that may have occurred to the reported Selected Information, Reporting Criteria or Report presented on Southern Water's website since the date of our report

Additional regulatory information

4A – Water bulk supply information for the 12 months ended 31 March 2023

	Volume MI	Operating costs £m	Revenue £m
Bulk supply exports			
Affinity	4.000	–	0.009
South East Water	11,556.280	6.691	3.927
Total bulk supply exports	11,560.280	6.691	3.936
	Volume MI	Operating costs £m	
Bulk supply imports			
Sutton and East Surrey Water	370.364	0.406	
Portsmouth Water	4,158.395	0.761	
Total bulk supply imports	4,528.759	1.167	

Bulk exports to NAV customers are not included in the table.

We do not show cost information for the bulk exports to Affinity Water and Wessex Water. These supplies are made via our distribution network and the costs are therefore not separately identifiable. Operating costs are included for the exports to South East Water. These agreements are based on a sharing of specific operating costs.

4B – Analysis of debt

As permitted by RAG 3.14 section 2.7, table 4B is excluded from this APR document and is published alongside this document and can be found at southernwater.co.uk/our-reports.

4C – Impact of price control performance to date on RCV

	12 months ended 31 March 2023			
	Water resources £m	Water network+ £m	Wastewater network+ £m	Bioresources £m
Totex (net of business rates, abstraction licence fees and grants and contributions)				
Final determination allowed totex (net of business rates, abstraction licence fees and grants and contributions)	18.154	176.156	499.127	65.697
Actual totex (net of business rates, abstraction licence fees and grants and contributions)	22.855	320.009	623.239	54.549
Transition expenditure	–	–	–	–
Disallowable costs	0.116	1.039	1.982	0.155
Total actual totex (net of business rates, abstraction licence fees and grants and contributions)	22.739	318.970	621.257	54.394
Variance	4.585	142.814	122.130	(11.303)
Variance due to timing of expenditure	(11.643)	(41.823)	(138.529)	(2.842)
Variance due to efficiency	16.228	184.637	260.659	(8.461)
Customer cost sharing rate – outperformance	63.55%	63.55%	63.92%	–
Customer cost sharing rate – underperformance	36.45%	36.45%	36.08%	–
Customer share of totex overspend	5.915	67.300	94.046	–
Company share of totex overspend	10.313	117.337	166.613	–
Company share of totex underspend	–	–	–	(8.461)
Totex – business rates and abstraction licence fees				
Final determination allowed totex – business rates and abstraction licence fees	6.366	12.198	13.909	1.448
Actual totex – business rates and abstraction licence fees	5.143	11.396	13.355	1.750
Variance – business rates and abstraction licence	(1.223)	(0.802)	(0.554)	0.302
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	(0.917)	(0.602)	(0.416)	0.227
Company share of totex over/underspend – business rates and abstraction licence fees	(0.306)	(0.201)	(0.139)	0.076
Totex not subject to cost sharing				
Final determination allowed totex – not subject to cost sharing	22.351	39.102	9.729	–
Actual totex – not subject to cost sharing	16.198	16.523	2.747	–
Variance – 100% company allocation	(6.153)	(22.579)	(6.982)	–
Total customer share of totex over/underspend	4.998	66.699	93.630	0.227
RCV				
Total customer share of totex over/underspend	4.998	66.699	93.630	0.227
PAYG rate	42.49%	49.27%	35.87%	37.14%
RCV element of totex over/underspend	2.874	33.836	60.045	0.142

4C – Impact of price control performance to date on RCV – continued

	Price control period to date			
	Water resources £m	Water network+ £m	Wastewater network+ £m	Bioresources £m
Totex (net of business rates, abstraction licence fees and grants and contributions)				
Final determination allowed totex (net of business rates, abstraction licence fees and grants and contributions)	51.500	530.634	1,277.912	143.214
Actual totex (net of business rates, abstraction licence fees and grants and contributions)	79.621	739.096	1,609.523	135.429
Transition expenditure	1.721	0.980	–	–
Disallowable costs	0.116	1.039	98.429	0.155
Total actual totex (net of business rates, abstraction licence fees and grants and contributions)	81.226	739.037	1,511.094	135.274
Variance	29.726	208.403	233.182	(7.940)
Variance due to timing of expenditure	(12.112)	(42.390)	(150.280)	(0.904)
Variance due to efficiency	41.838	250.793	383.462	(7.036)
Customer cost sharing rate – outperformance	63.55%	63.55%	63.92%	–
Customer cost sharing rate – underperformance	36.45%	36.45%	36.08%	–
Customer share of totex overspend	15.250	91.414	138.353	–
Company share of totex overspend	26.588	159.379	245.109	–
Company share of totex underspend	–	–	–	(7.036)
Totex – business rates and abstraction licence fees				
Final determination allowed totex – business rates and abstraction licence fees	17.864	34.229	39.030	4.064
Actual totex – business rates and abstraction licence fees	14.500	31.944	39.993	5.245
Variance – business rates and abstraction licence	(3.364)	(2.285)	0.963	1.181
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	(2.523)	(1.714)	0.722	0.886
Company share of totex over/underspend – business rates and abstraction licence fees	(0.841)	(0.571)	0.241	0.295
Totex not subject to cost sharing				
Final determination allowed totex – not subject to cost sharing	44.479	81.326	27.851	–
Actual totex – not subject to cost sharing	42.449	49.807	6.549	–
Variance – 100% company allocation	(2.030)	(31.519)	(21.302)	–
Total company share of totex over/underspend	12.727	89.700	139.075	0.886
RCV				
Total customer share of totex over/underspend	12.727	89.700	139.075	0.886
PAYG rate	42.49%	49.27%	35.87%	37.14%
RCV element of totex over/underspend	7.319	45.505	89.189	0.557
Adjustment for ODI outperformance payment or underperformance payment	–	–	–	–
RCV determined at FD at 31 March	144.384	1,421.574	4,608.081	260.193
Projected 'shadow' RCV	151.703	1,467.079	4,697.270	260.750

Wholesale totex analysis

Our total expenditure (totex) for 2022–23 was higher than the allowance in the PR19 final determination for both water and wastewater. We set out below the principal reasons for the variances within each wholesale price control and each cost category shown above. It is important to note that the final determination from Ofwat does not explicitly show the totex allowance at a granular level. The variances described therefore represent a best estimate of the reasons for the variances.

The principal totex variances to the final determination have been allocated between timing and efficiency within the table above. The following rules have been applied in making these allocations:

- All operating expenditure variances are allocated to efficiency on the basis that these

are recurring costs that cannot typically be shifted between years.

- Variances related to renewals and capital maintenance expenditure have been allocated to efficiency given that the Board has committed to a significant level of investment in excess of the final determination.
- Enhancement costs have been compared with a notional allocation of each category of expenditure to each year of the AMP using Ofwat's final determination profiling assumptions. All identified variances have been allocated to timing.
- Any enhancement costs incurred in relation to schemes which were not funded within the final determination (for example carryover of AMP6 expenditure) has been allocated to the efficiency category.

Totex variance to final determination

Water totex variance over/(under) £m	12 months ended 31 March 2023		Price control period to date	
	Water resources	Water network+	Water resources	Water network+
Net totex	4.6	142.8	29.7	208.7
Business rates and abstraction licences	(1.2)	(0.8)	(3.3)	(2.3)
Not subject to cost sharing	(6.2)	(22.6)	(2.0)	(31.5)
Total totex variance	(2.8)	119.4	24.4	174.6

Water

Water resources totex is £4.6 million higher than the final determination allowance for 2022–23 and is £29.7 million over the final determination for the AMP to date.

The variance of £4.6 million in 2022–23 reflects an overspend of £16.2 million, offset by timing variances of £11.6 million, of these variances £8.2 million results from the reversal of timing variances from prior years, now shown as overspends.

The principal reasons for the overspend are the completion of some Eels Regulations schemes from the previous regulatory period (AMP6), representing £2.5 million in the year and £25.4 million cumulatively, expenditure relating to supply and demand side enhancements of £2.7 million in the year and £10.3 million cumulatively, additional asset maintenance capital expenditure to help improve operational performance and compliance of £1.8 million in the year and cumulatively, together with an increase in the provision made for ecological work associated with the section 20 agreement in relation to the Rivers Test and Itchen and the Candover Stream of £0.3 million in 2022–23 and £2.8 million cumulatively. These

variances have been included within the (in) efficiency category.

The favourable timing variance is a combination of a slower start than assumed in the theoretical profile provided by Ofwat on enhancement projects, including schemes related to raw water deterioration (£2.1 million in year and £7.1 million cumulatively) and WINEP investigations (£2.0 million in year and £6.2 million cumulatively).

Water network+ expenditure is £142.8 million above the final determination in 2022–23. This variance consists of timing variances of £42.1 million offset by an overspend of £184.9 million, of these variances £21.6 million results from the reversal of timing variances from prior years, now shown as overspends.

In addition to the reversal from prior years, the timing variance mainly relates to an underspend in the year of £22.4 million on supply demand balance schemes during the year and £79.0 million cumulatively. These schemes are expected to be delivered later in the AMP.

As set out in our Annual Report, we have experienced some significant additional operating costs during 2022–23.

- Significant incidents on the Isle of Sheppey and at Otterbourne impacted large numbers of customers and resulted in additional costs of £12.8 million being incurred.
- At our Testwood Water Supply Works we have improved water quality performance through capital investment to replace the chemical dosing on site, however as a consequence, and to maintain compliance on site, this increased the amount of tankering and treatment required for the waste produced, adding £10.3 million.
- Following the dry winter in 2021 and the hot summer water companies across the country faced the first nationwide drought for a decade, introducing a temporary usage ban for our customers in Hampshire. We incurred additional £4.5 million of operating costs in preparation for the drought and replenishing our reservoir at Bewl, along with additional leakage activity and water repairs to mitigate the effect on our overall water resources.
- We experienced hyper-inflation rates ranging from 14% to 200% for certain chemicals and fuel and these increased our operating costs by £3.7 million.
- Our transformation programme to improve operational performance included the creation of a new logistics team, managing our own small fleet of water tankers as well as stores of spares for plant and equipment repairs and made improvements to our control centre and alarm handling. This programme added £1.6 million to our water cost base.

The remaining efficiency variance results from additional capital maintenance to address water quality risks at our supply works and general operating expenditure which is significantly higher than the final determination assumption. This overspend largely reflects additional contract costs and efficiencies not delivered in line with expectations, and this is also the main driver for the cumulative variance to date.

Business rates for water resources and water network+ are £2.0 million lower than the final determination allowance overall, mainly reflecting lower abstraction charges for water resources. Cumulatively the total variance is £5.6 million

lower than the determination, this variance also includes the impact of a one-off business rates rebate in 2020–21 of £2.4 million.

Within the 'costs not subject to sharing' category water resources expenditure is £6.1 million lower than the final determination allowance while water network+ is £22.6 million below the allowance in 2022–23. The largest element of expenditure within this category is related to the strategic water resources development schemes which form our Water for Life Hampshire programme.

Overall expenditure on these schemes is £22.4 million below the final determination allowance, with an underspend of £16.0 million within the water network+ price control and an underspend of £6.4 million within the water resources control.

The remaining variance is principally associated with the income offset (relating to developer-led schemes) which is £4.5 million lower than allowed reflecting a lower level of development activity during the year.

Pension deficit repair costs, which are not subject to cost sharing, are excluded from both the final determination allowed totex and the actual totex.

Wastewater

Bioresources totex is £11.3 million lower than the final determination allowance for 2022–23 and £7.9 million lower over the final determination for the AMP to date.

The variance of £11.3 million in 2022–23 reflects an underspend of £8.5 million and a favourable timing variance of £2.8 million.

The timing element of this variance results from the sludge quality and growth schemes for which an allowance of £2.6 million was made in the notional final determination allocation for the year. We did not incur any expenditure against this in the year offsetting the expenditure that was incurred in prior years. Cumulative expenditure is now £1.3 million lower than the notional determination allowance. The efficiency variance is driven by higher operating expenditure in relation to sludge transport costs and materials and chemicals offset by lower capital maintenance costs.

Wastewater network+ totex is £122.1 million higher than the final determination representing

Totex variance to final determination

Wastewater totex variance over/(under) £m	12 months ended 31 March 2023		Price control period to date	
	Wastewater network+	Bioresources	Wastewater network+	Bioresources
Net totex	122.1	(11.3)	233.2	(7.9)
Business rates and abstraction licences	(0.6)	0.3	0.9	0.9
Not subject to cost sharing	(7.0)	–	(21.3)	–
Total totex variance	114.5	(11.0)	212.8	(6.7)

favourable timing differences of £138.5 million offset by an overspend of £260.6 million of these variances £54.8 million results from the reversal of timing variances from prior years, now shown as overspends.

The remainder of the favourable timing variance relates to an underspend in the year of £83.7 million on enhancement schemes, £246.1 million cumulatively. Within the enhancement schemes the largest areas of underspend to date, compared with the implied final determination profile, are in relation to Flows to Full Treatment schemes £32.3 million in year and £93.0 million cumulatively, storage schemes at treatment works £14.9 million in year and £50.4 million cumulatively and phosphorous removal schemes £15.3 million in year and £42.7 million cumulatively.

The efficiency variance relates principally to higher expenditure on capital maintenance and renewals during the year, £160.5 million, and this is largely driven by significant schemes to improve our wastewater treatment works compliance and pumping station performance.

In addition, as set out in our Annual Report, we have experienced some significant additional operating costs during 2022–23, for example:

- Since October 2022 we have experienced a prolonged period of extremely wet weather, with our region receiving 181% of the long-term average rainfall. Dealing with the high-ground water levels and infiltration cost a further £10.8 million as well as increasing power consumption by £2.0 million.
- We have increased proactive maintenance of our sewerage network by £5.3 million as part of our pollution reduction programme.
- We experienced hyper-inflation rates ranging from 14% to 200% for certain chemicals and fuel and these increased our operating costs by £4.5 million.
- Our transformation programme to improve operational performance included the creation of a new logistics team, managing our own small fleet of water tankers as well as stores of spares for plant and equipment repairs and made improvements to our control centre and alarm handling. This programme added £3.1 million to our wastewater cost base.

These costs, together with cost reductions anticipated as part of the final determination not being achieved in line with expectations are the main reasons for the variances experienced to date.

Business rates for bioresources and wastewater network+ are £0.3 million lower than the final determination allowance for the year.

Within the ‘costs not subject to sharing’ category actual expenditure is £7.6 million less than the final determination allowance for the year and £21.3 million lower for the AMP to date. This

variance is largely driven by the income offset (relating to developer-led schemes) which is £5.0 million lower than the determination in 2022–23, £14.8 million cumulatively reflecting a lower level of developer activity than anticipated together with lower expenditure on third party services of £2.6 million in the year, £71 million cumulatively, offset by expenditure of £0.6 million in relation to the innovation fund.

Pension deficit repair costs, which are not subject to cost sharing, are excluded from both the final determination allowed totex and the actual totex.

Atypicals/Exceptionals

The atypical costs shown in table 4D relate to a court fine and costs associated with a prosecution by the DWI for an event in May 2018 when high chlorate levels were detected at the reservoir. These have been classified as disallowable costs in table 4C and do not form part of the variances that are highlighted above.

Link to the final determination outcomes

With the exception of performance commitments that relate to specific capital delivery schemes it is generally not possible to directly associate expenditure with the delivery of the final determination outcomes. This is because the vast majority of outcomes are delivered through base operating and capital maintenance expenditure rather than specific funded schemes. We note that despite both water and wastewater totex being significantly higher than the final determination allowance we have nonetheless incurred significant Outcome Delivery Incentive underperformance payments, in particular in relation to internal drinking water quality, water supply interruptions, leakage, mains repairs, sewer flooding and pollution incidents. These remain key areas of focus and investment for the business.

Disallowable costs

When comparing our actual totex to that allowed in the Final Determination we are required to make adjustments for certain disallowable costs, including fines and investigation costs. The disallowable costs disclosed for 2022–23 of £3.3 million, include the court fine and costs mentioned as atypical above and costs incurred in 2021–22 in relation to a one-off transaction incentive, awarded to certain individuals in the company linked to the successful delivery of the transaction which saw a fund managed by Macquarie Asset Management invest more than £500 million into the company.

Recharges between business units

Details of our process for allocating costs between business units can be found in our Methodology Statement.

4D – Totex analysis for the 12 months ended 31 March 2023 – water resources and water network+

	Network+					Total £m
	Water resources £m	Raw water transport £m	Raw water storage £m	Water treatment £m	Treated water distribution £m	
Operating expenditure						
Base operating expenditure	16.160	0.381	0.288	69.892	71.466	158.187
Enhancement operating expenditure	0.088	0.004	0.004	5.686	0.888	6.670
Developer services operating expenditure	–	–	–	–	1.510	1.510
Total operating expenditure excluding third party services	16.248	0.385	0.292	75.578	73.864	166.367
Third party services	0.973	–	–	2.444	0.662	4.079
Total operating expenditure	17.221	0.385	0.292	78.022	74.526	170.446
Grants and contributions						
Grants and contributions – operating expenditure	–	–	–	–	–	–
Capital expenditure						
Base capital expenditure	3.734	0.146	–	89.549	67.569	160.998
Enhancement capital expenditure	23.243	0.399	–	20.430	8.477	52.549
Developer services capital expenditure	–	–	–	–	10.172	10.172
Total gross capital expenditure (excluding third party)	26.977	0.545	–	109.979	86.218	223.719
Third party services	0.866	–	–	3.447	(0.009)	4.304
Total gross capital expenditure	27.843	0.545	–	113.426	86.209	228.023
Grants and contributions						
Grants and contributions – capital expenditure	0.868	–	–	1.443	4.034	6.345
Net totex	44.196	0.930	0.292	190.005	156.701	392.124
Cash expenditure						
Pension deficit recovery payments	–	–	–	–	–	–
Totex including cash items	44.196	0.930	0.292	190.005	156.701	392.124
Atypical expenditure						
High Park DWI prosecution	0.066	–	–	–	–	0.066
Total atypical expenditure	0.066	–	–	–	–	0.066

4E – Totex analysis for the 12 months ended 31 March 2023 – wastewater network+ and bioresources

	Network+ Sewage collection			Network+ Sewage treatment		Bioresources			Total £m
	Foul £m	Surface water drainage £m	Highway drainage £m	Sewage treatment and disposal £m	Imported sludge liquor treatment £m	Sludge transport £m	Sludge treatment £m	Sludge disposal £m	
Operating expenditure									
Base operating expenditure	74.125	13.647	13.647	105.419	3.360	5.526	17.964	7.696	241.384
Developer services operating expenditure	1.249	0.273	0.273	–	–	–	–	–	1.795
Total operating expenditure excluding third party services	75.374	13.920	13.920	105.419	3.360	5.526	17.964	7.696	243.179
Third party services	–	–	–	–	–	–	–	–	–
Total operating expenditure	75.374	13.920	13.920	105.419	3.360	5.526	17.964	7.696	243.179
Grants and contributions									
Grants and contributions – operating expenditure	–	–	–	–	–	–	–	–	–
Capital expenditure									
Base capital expenditure	86.336	18.820	18.820	180.010	–	–	25.139	–	329.125
Enhancement capital expenditure	8.676	1.890	1.890	102.057	–	–	(0.026)	–	114.487
Developer services capital expenditure	11.946	2.605	2.605	–	–	–	–	–	17.156
Total gross capital expenditure (excluding third party)	106.958	23.315	23.315	282.067	–	–	25.113	–	460.768
Third party services	–	–	–	–	–	–	–	–	–
Total gross capital expenditure	106.958	23.315	23.315	282.067	–	–	25.113	–	460.768
Grants and contributions									
Grants and contributions – capital expenditure	5.263	1.147	1.147	0.750	–	–	–	–	8.307
Net totex	177.069	36.088	36.088	386.736	3.360	5.526	43.077	7.696	695.640
Cash expenditure									
Pension deficit recovery	–	–	–	–	–	–	–	–	–
Totex including cash items	177.069	36.088	36.088	386.736	3.360	5.526	43.077	7.696	695.640
Atypical expenditure									
N/A	–	–	–	–	–	–	–	–	–
Total atypical expenditure	–	–	–	–	–	–	–	–	–

4F – Major project expenditure for wholesale water by purpose for the 12 months ended 31 March 2023

	Expenditure in report year					Total £m
	Water network+					
	Water resources £m	Raw water transport £m	Raw water storage £m	Water treatment £m	Treated water distribution £m	
Major project capital expenditure by purpose						
Western Grid SRO Common costs	9.586	–	–	–	–	9.586
West Country Sources South	0.168	–	–	–	–	0.168
River Itchen effluent re-use	–	–	–	7.123	–	7.123
West Country Sources North	0.197	–	–	–	–	0.197
Thames – Southern Transfer	–	1.091	–	–	–	1.091
Havant Thicket – Pipeline	3.471	–	–	–	–	3.471
Total major project capital expenditure	13.422	1.091	–	7.123	–	21.636

	Cumulative expenditure on schemes completed in the report year					Total £m
	Water network+					
	Water resources £m	Raw water transport £m	Raw water storage £m	Water treatment £m	Treated water distribution £m	
Major project capital expenditure by purpose						
West Country Sources South	0.333	–	–	–	–	0.333
Fawley Desalination	–	–	–	4.249	–	4.249
West Country Sources North	0.593	–	–	–	–	0.593
West Country – Southern Transfer	0.179	–	–	–	–	0.179
Total major project capital expenditure	1.105	–	–	4.249	–	5.354

As part of the RAPID gate 2 final decision, it was agreed that funding would be allowed for the Thames (Water) to Southern (Water) Transfer (T2ST) to continue to be developed to gate three.

We have formally stopped all work on Fawley desalination development due to potential adverse environmental impacts and have agreed with RAPID and Ofwat to pursue the best alternative option that emerged via a comprehensive option selection process. The current Strategic Resource Option (SRO) in the Water for Life Hampshire programme, is referred to as the Hampshire Water Transfer and Water Recycling Project (HWTWRP). This is currently (June 2023) mid- RAPID Gate 3 and is projected to deliver water resource benefit comparable to Fawley desalination, with lower environmental risk, lower carbon emissions and at lower whole life financial cost.

In May 2022 it was also confirmed that, due to a projected shortfall in available water for bulk transfer to Southern Water, we would no longer be part of the West Country Sources projects and have therefore reported our cumulative cost for this scheme as complete.

4G – Major project expenditure for wholesale wastewater by purpose for the 12 months ended 31 March 2023

We have no projects classed as major projects to report within wholesale wastewater.

4H – Financial metrics for the 12 months ended 31 March 2023

	Units	Metric	AMP to date
Financial Indicators			
Net debt	£m	4,494.226	
Regulatory equity	£m	1,940.006	
Regulatory gearing	%	69.85%	
Post tax return on regulatory equity	%	(15.68%)	
RORE (return on regulatory equity)	%	(1.39%)	(2.23%)
Dividend yield	%	–	
Retail profit margin – Household	%	(2.15%)	
Retail profit margin – Non Household	%	–	
Credit rating – Fitch	n/a	BBB (Negative)	
Credit rating – Moody's	n/a	Baa3 (Stable)	
Credit rating – Standard & Poor's	n/a	BBB+ (Negative)	
Return on RCV	%	0.11%	
Dividend cover	dec	–	
Funds from operations (FFO)	£m	120.765	
Interest cover (cash)	dec	1.76	
Adjusted interest cover (cash)	dec	(0.19)	
FFO/Debt	dec	0.03	
Effective tax rate	%	–	
Retained cash flow (RCF)	£m	120.765	
RCF/Net debt	dec	0.03	
Borrowings			
Proportion of borrowings which are fixed rate	%	32.14%	
Proportion of borrowings which are floating rate	%	8.68%	
Proportion of borrowings which are index linked	%	59.19%	
Proportion of borrowings due within 1 year or less	%	0.00%	
Proportion of borrowings due in more than 1 year but no more than 2 years	%	0.10%	
Proportion of borrowings due in more than 2 years but no more than 5 years	%	26.84%	
Proportion of borrowings due in more than 5 years but no more than 20 years	%	61.25%	
Proportion of borrowings due in more than 20 years	%	11.81%	

The interest cover and adjusted interest cover ratios quoted above are based on the cash interest payable for the financial year rather than the cash interest paid in the financial year.

Interest Cover Ratios reconciliation

	ICR (cash) £m	Adj ICR (cash) £m
Funds from operations	120.765	120.765
Add back cash interest paid in year	181.775	181.775
Less regulatory depreciation	–	(335.701)
	302.540	(33.161)
Cash interest paid in year	181.775	181.775
Less interest paid in prior year	(44.032)	(44.032)
Add interest payable re current year	40.950	40.950
Less interest prepaid	(7.258)	(7.258)
Interest payable for 2022–23	171.434	171.434
Ratio (dec)	1.765	(0.193)

4I – Financial derivatives for the 12 months ended 31 March 2023

Interest rate swap (sterling)	Nominal value by maturity (net) at 31 March				Total value at 31 March		Total accretion at 31 March £m	Interest rate (weighted average for 12 months to 31 March)	
	0 to 1 year	1 to 2 years	2 to 5 years	Over 5 years	Nominal value (net)	Mark to Market		Payable	Receivable
	£m	£m	£m	£m	£m	£m			
Fixed to index-linked									
Super-senior swaps with breaks or accretion paydowns	–	–	–	1,265.262	1,265.262	1,481.149	392.691	2.09%	9.34%
Pari-passu swaps with breaks or accretion paydowns	–	–	–	51.346	51.346	90.252	–	0.00%	0.00%
Fixed to index-linked Total	–	–	–	1,316.608	1,316.608	1,571.401	392.691		

The pari-passu derivatives have accretion payments in 2050 and 2055 relating to a £250 million inflation-linked swap against a £300 million fixed rate bond. The remaining inflation-linked cashflows associated with this inflation-linked swap are super senior.

Floating to index-linked derivatives are intended to expose interest cash flows, and the nominal value of debt outstanding, to short-term movement in RPI inflation. This ensures a proportion of our interest cost is a match against the nature of our inflation-linked cash flows and our inflation-linked RCV. Our inflation-linked financial instruments have a long maturity in order to finance the long life of our assets and the long-term nature of our investment decisions.

The value of the Mark to Market represents forecast future cash flows for the duration of the derivatives and discounted by prevailing interest rates. This value is extremely volatile given that market interest rates are constantly moving. The liability shown in the table above of £1,571.4 million associated with the Mark to Market valuations of our derivatives is very high at present given the current low interest rate environment. The risk of this Mark to Market value crystallising is extremely remote given that it can only crystallise under certain conditions of a default of our financing covenants, in which case operations of the company are protected and will continue. Further details are available on page 244 of our Annual Report and Financial Statements.

4V – Mark-to-market of financial derivatives analysed based on payment dates

	Derivatives – Analysed by earliest payment date				Derivatives – Analysed by expected maturity date			
	Net settled £m	Gross Settled outflows £m	Gross Settled inflows £m	Total £m	Net settled £m	Gross Settled outflows £m	Gross Settled inflows £m	Total £m
Due within one year	–	–	–	–	–	–	–	–
Between one and two years	–	–	–	–	–	–	–	–
Between two and three years	168.385	–	–	168.385	–	–	–	–
Between three and four years	–	–	–	–	–	–	–	–
Between four and five years	–	–	–	–	–	–	–	–
After five years	1,403.015	–	–	1,403.015	1,571.400	–	–	1,571.400
Total	1,571.400	–	–	1,571.400	1,571.400	–	–	1,571.400

4W – Defined Benefit Pension Scheme – Additional Information

Item	Defined benefit pension schemes Pension scheme 1
Scheme details	
Scheme name	Southern Water Pension Scheme
Scheme status	Closed to new members and future accrual
Scheme validation under IAS/IFRS/FRS	
	£m
Scheme assets	612.800
Scheme liabilities	685.800
Scheme surplus/(deficit) Total	(73.000)
Scheme surplus/(deficit) Appointed business	(73.000)
Pension deficit recovery payments	–
Scheme valuation under part 3 of the Pensions Act 2004	
	£m
Scheme funding valuation date	31 March 2022
Assets	720.200
Technical Provisions	988.000
Scheme surplus/(deficit)	(267.800)
Discount rate assumptions	Fixed interest gilts curve + 65bps

Recovery plan

Under the recovery plan agreed on 15 March 2023, the company will pay the following deficit contributions arising from the latest triennial valuation carried out as at 31 March 2022:

On 31 March 2022 the company made a contribution of £59.6 million. The funding shortfall of £267.8 million above uses an asset valuation that excludes this payment. This was a prepayment of the 1 April 2022 contribution of £20.6 million plus a further prepayment of £39.0 million in relation to contributions due in future years as set out below:

- a) From 2023 to 2029 £20.976 million per annum increased by RPI each year based on December RPI.
- b) An additional £0.5 million per annum from 2023 to 2028 being the continuation of advance payments (made since 2018) of the 2029 deficit contribution which will be reduced by £5.5 million from that calculated in a) above.

The deficit contributions, offset where relevant by the £39.0 million prepayment are payable on 1 April of each relevant year.

Recovery plan end date	1 April 2029
Asset Backed Funding (ABF) arrangements	n/a
Responsibility for ABF arrangements	n/a

Additional regulatory tables

As permitted by RAG 3.14 section 2.9, the remaining regulatory tables which form the Annual Performance Report are excluded from this document and are published as an appendix at [southernwater.co.uk/our-reports](https://www.southernwater.co.uk/our-reports).

Data assurance summary

We take full responsibility for the information we publish on our performance. We seek to provide confidence to customers and stakeholders through a transparent approach to data assurance. This assurance provides confidence in our reported performance and the delivery of performance commitments made in our 2020–25 business plan.

Whilst assurance is rarely able to provide absolute certainty over the quality of reported information, we aim for the assurance that we perform and commission to provide our internal and external stakeholders with sufficient comfort over the robustness and quality of the information that we report.

The assurance activity we undertake around the information that we provide is one of the critical

elements we have put in place to build and secure the trust and confidence of our regulators, stakeholders and customers.

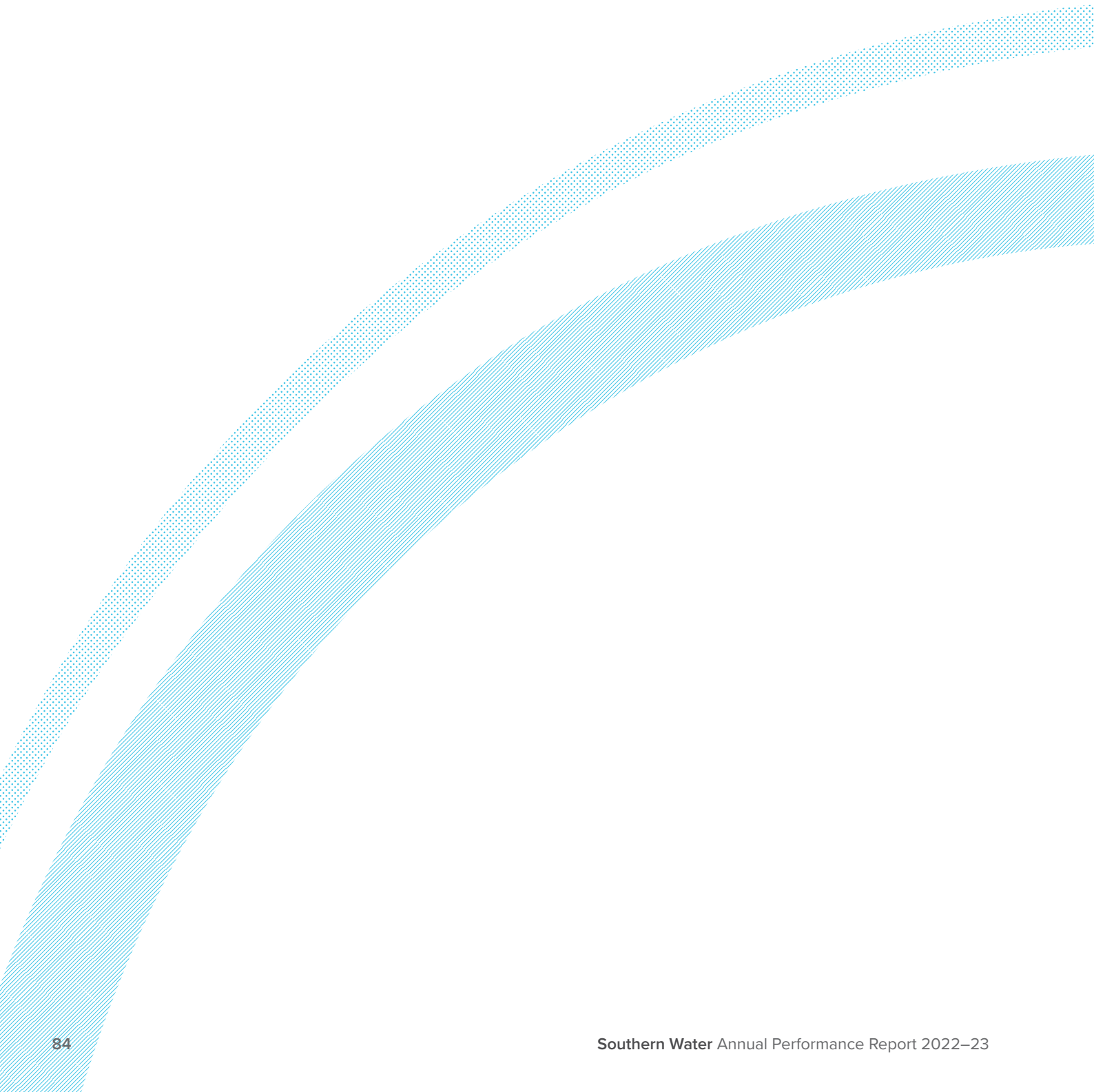
Our technical assurance framework agreement in place for our five-year Business Plan period (AMP7) allows us to appoint the most suitable assurance partners to different technical assurance projects. KPMG LLP and Jacobs are now completing their third year in this role.

We have published a separate document that details the completed assurance work performed on our reported information for the 2022–23 financial year. The results, both positive and improvement areas are published in the document entitled ‘Data Assurance Summary’ which is available on our Southern Water website southernwater.co.uk/our-reports.

The main assurance areas for the annual reports are:

Significant areas for assurance Assurance results for 2022–23

<p>The Annual Report including the Statutory and Regulatory Accounts, cost allocation and segmental reporting</p>	<p>The Annual Report and Financial Statements were audited by Deloitte LLP. Their opinion is included on page 258 of that report.</p> <p>The Annual Performance Report (APR), sections 1 and 2, excluding table 1F, were audited by Deloitte LLP. Their assurance statement is included on page 50.</p> <p>Deloitte LLP also performed assurance activities agreed with us on the financial information presented in table 1F and sections 4 to 9 of the APR and the financial information published in the cost assessment tables alongside this report. No issues were identified.</p>
<p>Additional assurance undertaken</p>	<p>Deloitte LLP also undertook assurance procedures on the following statements made in the Annual Report and APR:</p> <ul style="list-style-type: none"> • Viability statement • Ring-fencing Certificate and statement (Licence Condition P)
<p>Ofwat Performance Commitments and Outcome Delivery Incentives (ODIs)</p>	<p>Our technical assurers KPMG LLP have issued an unqualified limited assurance ISAE (UK) 3000 opinion over the reported performance against selected Performance Commitments for the Business Plan period 2020–25 in Section 3 of the APR.</p>
<p>Specific assurances related to other regulators’ required information (i.e. The Drinking Water Inspectorate and The Environment Agency)</p>	<p>Each specified requirement is detailed in our Data Assurance Summary</p>



Appendices

The information in the appendices has not been audited.

Appendix 1. Transactions with associates and the non-appointed business

Services supplied to associated companies by the appointee

Greensands Holdings Limited (GSH) is the ultimate parent of Greensands Investments Limited (GSI), which is an intermediate parent of Southern Water Services Limited (SWS), the appointee. The purpose of GSH and GSI is to act as holding companies for SWS. As such they do not trade and have no turnover.

During the year, recharges for group-related management services, for example legal, treasury, governance and financial services, supplied by Southern Water Services Limited were as follows:

Service	Company	Turnover of associate	Terms of supply	Value £m
Management charges	Greensands Investments Limited	–	Cost/market price	1.000

Services received by the appointee from associated companies

There were no services supplied by associate companies to SWS.

Group relief received by the appointee

Service	Company	Turnover of associate	Terms of supply	Value £m
Corporation tax group relief	–	–	Cost	–

No group relief was received by the appointee.

Allocation of costs between regulated and non-regulated businesses

Each non-appointed activity is treated separately within the company's financial records. Examples of non-appointed activities include non-monopoly rechargeable works, property searches and services for waste tankering. Revenues, costs, assets and liabilities are generally directly allocated to particular business activities. Administrative overheads have been apportioned from the appointed business to the non-appointed business on an activity cost basis.

Service provided by the non-appointed business	Basis of recharge made by the appointed business	Value £m
Treatment of imported sludge	Not applicable	–
Treatment of tankered waste	The Mogden Formula was used to calculate the income for tankered waste and the costs were derived from this calculation	6.864
Other	Headcount (FTE) was used to calculate administrative overhead for property searches, accommodation rental and Homeserve costs	0.304

Details of intercompany loans

Loans granted to Southern Water Services Limited

Company	Loan type	Interest rate %	Repayment date	Balance at 31 March 2023 £m
SW (Finance) I Plc	Fixed rate	6.192	2029	349.045
	Index linked	3.706	2034	288.889
	Index linked	3.706	2034	61.056
	Fixed rate	6.640	2026	349.429
	Fixed rate	5.000	2041	147.347
	Fixed rate	4.500	2052	197.349
	Fixed rate	5.125	2056	292.903
	Fixed rate	2.375	2028	371.500
	Fixed rate	3.000	2037	444.221
	Fixed rate	1.625	2027	296.245
	Fixed rate	2.780	2031	174.290
	Fixed rate	2.960	2036	74.635
SW (Finance) II Limited	Index linked	4.076	2033	317.938
	Index linked	3.635	2032	294.229
Total				3,659.076

Loans granted by Southern Water Services Limited

Company	Loan type	Interest rate %	Repayment date	Balance at 31 March 2023 £m
SW (Finance) I Plc	Fixed rate	0.000	On demand	30.065
Total				30.065

Dividends paid by Southern Water Services Limited to group companies

Company	2023 £m	2022 £m
SWS Holdings Limited (ordinary dividend)	–	–

No ordinary dividend was declared for payment to SWS Holdings Limited (SWSH) in 2023 (2022: £nil).

Dividend policy

Our dividend policy is formulated to ensure a fair balance of reward between investors and customers. To deliver on our vision for the successful delivery of our Business Plan for 2020–25, all stakeholders must share in success: customers benefitting through enhanced service and lower bills, and shareholders earning a fair return on the near £2 billion of equity invested.

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

1. Determination of a base level of dividend, based on an equity return consistent with our most recent Final Determination and our actual level of gearing. This recognises our management of economic risks and capital employed.
2. In assessing any adjustment to the base level of dividend, we will take into account our financial and non-financial performance. This would reflect our overall financial performance as compared to the final Business Plan for 2020–25 as agreed by Ofwat and would explicitly consider a qualitative assessment of customer service levels and how customers share in our successes.
3. We will consider our financial resilience ahead of any dividend decision, and whether any financial outperformance should be re-invested to benefit our customers. This consideration will also include taking into account the interests of our employees, other stakeholders, and our pension schemes.

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

- a) headroom under debt covenants
- b) the impact on the company's credit rating
- c) the liquidity position and ability to fulfil licence conditions
- d) key areas of business risk.

4. We will be transparent in the payment of dividends and will clearly justify the payment in relation to the factors outlined above.
5. We will publish our Dividend Policy annually (as part of the Annual Report) and highlight any changes

Comparison of dividend to the PR19 Final Determination

The Board has resolved that the company will not pay dividends until it is clear that to do so would not be detrimental to the company's financial position. No ordinary dividends were declared or paid in 2022–23 (2022: £nil).

On 26 July 2022, having undertaken a careful consideration of the company's financial position, progress in delivery for customers, and all other relevant factors, the Board approved the redemption of 5,164 of its Class B preference shares, at nominal value plus the premium on issue, including settlement for fixed value dividends due to that date. The total amount paid was £17.5 million, comprising principal redemption of £5.2 million and dividends of £12.3 million (2022: £nil).

Dividends on the preference shares accrue like interest and from an accounting perspective they are treated as interest, even though they are called dividends. The payment made in July 2022 was our first payment since 2020. These payments are made to a SWS group company and enable the payment of external interest on loans within the group. None of this money is paid to Southern Water shareholders.




An accrual totalling £4.5 million in relation to the cumulative liability of preference share dividends to 31 March is included within the financial statements as an inter-company creditor.

Asset transfers


There were no asset transfers during the year.

Appendix 2. KPI definitions and status assessment rules

Performance Commitment Definitions RAG status

-  Ofwat target met or exceeded
-  Ofwat target missed but performance improved in relation to prior year outcome
-  Ofwat target missed and performance worse than prior year outcome
- Not applicable

Performance Commitment Definitions

 Deliver great service	
Water quality compliance (Compliance Risk Index)	<p>Definition: The definition for this performance commitment is set by the Drinking Water Inspectorate (DWI) in collaboration with the industry. This is published as DWI Compliance Risk Index (CRI), August 2018: ofwat.gov.uk/publication/dwi-compliance-risk-index-cri-definition/.</p>
Drinking water appearance	<p>Definition: The number of times the company is contacted by consumers due to the drinking water not being clear, reported per 1,000 population. Calculation is the number of contacts for appearance multiplied by 1,000 divided by the resident population as reported to the Drinking Water Inspectorate (DWI).</p>
Drinking water taste and odour	<p>Definition: The number of times the company is contacted due to the taste and odour of drinking water, reported per 1,000 population. Calculation is the number of contacts for all taste/ odour contacts multiplied by 1,000 divided by the resident population as reported to the Drinking Water Inspectorate (DWI).</p>
Replace lead customer pipes	<p>Definition: The number of residential properties receiving grants from the company towards removing lead pipes in the home in the 2020–25 period.</p> <p>This is a co-delivery measure with the company’s customers to reduce the amount of lead in customer pipes. The performance commitment will apply only in the company’s Deal, Kent, water supply zone, where it is trialling this approach to eliminating lead pipes and fittings.</p>
Water supply interruptions	<p>Definition: Reducing interruptions to water supply is defined in the reporting guidance for PR19 – Supply Interruptions, published on 27 March 2018: ofwat.gov.uk/publication/reporting-guidance-supply-interruptions/</p> <p>It is calculated as the average number of minutes lost per customer for the whole customer base for interruptions that lasted three hours or more.</p>
C-MeX	<p>Definition: The customer measure of experience (C-MeX) is a measure of customer satisfaction. A company’s C-MeX score is calculated as the weighted average of customer satisfaction (CSAT) scores from customer service (CS) and customer experience (CE) surveys.</p> <p>Standard and higher performance payments under C-MeX depend on a company’s performance relative to those of other companies.</p> <p>Higher performance payments are available if the company passes each of the following three ‘gates’:</p> <ul style="list-style-type: none"> • the company is one of the top three performers by C-MeX score; • the company is at or above a cross-sector threshold of customer satisfaction performance based on the all-sector upper quartile (ASUQ) of the UK Customer Satisfaction Index (UKCSI); and • the company has lower than the industry average number of household complaints (per 10,000 connections).



Deliver great service

Void properties

Definition:

The number of household properties classified as void as a percentage of the total number of household properties served by the company.

Void properties are defined as properties, within the company's supply area, which are connected for either a water service only, a wastewater service only or both services but do not receive a charge, as there are no occupants. Additionally a property connected for both services that is not occupied, only counts as one void property.

Gap sites

Definition:

The number of household gap sites identified by the company and brought into charge annually. A gap site is identified as a property that is not recorded on the company's billing database. To add one more site requires the company to add one property to its billing database.

Internal sewer flooding

Definition:

The internal sewer flooding measure is defined in the reporting guidance for PR19 – Sewer Flooding, published on 27 March 2018: ofwat.gov.uk/publication/reporting-guidance-sewer-flooding/

The measure is calculated as the number of internal sewer flooding incidents normalised per 10,000 sewer connections including sewer flooding due to severe weather events.

External sewer flooding

Definition:

The performance commitment will be reported as the absolute number of the company's external sewer flooding incidents per year including incidents caused by severe weather.

The external sewer flooding measure is defined in the reporting guidance for PR19 – Sewer Flooding, updated on 28 April 2018: ofwat.gov.uk/publication/reporting-guidance-sewer-flooding/

Customer Satisfaction with Vulnerability Support

Definition:

Percentage of customers that have received non-financial support who believe Southern Water's support addresses their specific requirements and needs.

Non-financial support is defined as any support that is provided by the company to a customer with specific requirements or needs which affects the customer for reasons that are not specific to their financial position. This support is provided through the Priority Services Register (PSR) e.g. braille bills or talking bills.

Performance will be measured through a survey of customers that have received PSR support. Customers will be asked whether the support provided addresses their specific requirements and needs in relation to their water and wastewater service. Customers will be provided information about the support the company provides as part of the questionnaire so they clearly understand the premise of the question.

The questionnaire used will be consistent with that used in the company's baseline survey for 2017–18. Customers will be able to respond with a 'Yes' or 'No' answer and provide additional comments to give the company feedback on any improvements that could still be made to improve support.

The performance will be measured as the total number of yes responses divided by the total number of responses. The company will not include in the survey PSR customers who have not received a service from the company in the reporting period.

The survey should be planned and carried out following social research best practice (example any applicable sections of a relevant code such as that published by the Market Research Society).

The sample size should be selected to give a reasonable statistical significance for the purpose of the performance commitment.



Deliver great service

Effectiveness of financial assistance

Definition:

The percentage of customers that pay their bills in the immediate twelve months following the receipt of financial assistance.

The measure includes residential customers who have received support through the Essentials social tariff, WaterSure, Water Direct, NewStart Debt Matching scheme and any new financial assistance schemes the company implements. Any new financial schemes introduced by the company for inclusion in this performance commitment should be subject to assurance from the Customer Challenge Group.

Customers 'paying their bills' is defined as customers either having paid in ten distinct months (of twelve) or having paid 90% of the billed value.

Priority services for customers in vulnerable circumstances

Definition:

This common performance commitment is defined in the reporting guidance: 'Reporting guidance – Common performance commitment for the Priority Service Register'.

This performance commitment consists of the following criteria:

- The PSR reach: percentage of households that the company supplies with water and/or wastewater services that are registered on the company's PSR;
- Attempted contact: percentage of distinct households on the PSR that the company has attempted to contact over a two-year period;
- Actual contact: percentage of distinct households on the PSR that the company has actually contacted over a two-year period.

To achieve compliance with this performance commitment the reach, attempted contact and actual contact targets should be achieved.

Properties at risk of receiving low pressure

Definition:

The number of properties receiving or at risk of receiving pressure below the low pressure reference level. This measure is calculated as the total number of properties receiving pressure below standard, minus the number of those properties that are covered by the predetermined allowable exclusion categories as detailed in the reporting guidance.

Low pressure reference level is defined in the reporting guidance published 11 December, 2017 'Properties at risk of receiving low pressure':

ofwat.gov.uk/publication/properties-at-risk-of-receiving-low-pressure/

Value for money

Definition:

Percentage of customers that state they are satisfied with the value for money of water and sewerage services in their area.

This performance commitment will be measured through an annual survey of customers that is run by CCWater (Water Matters). The measure will take the results for Southern Water customers only.

The proportion of customers that state either 'very' or 'fairly' satisfied on a five-point scale, as measured by CCWater's annual tracking report 'Water Matters'.

It combines a mean average score of the ratings:

- Satisfaction with value for money for water services; and
- Satisfaction with value for money for sewerage services

CCWater will interview 200 of Southern Water's customers each year in this survey.

The measurement of the survey will be conducted in a consistent way over the 2020 to 2025 period.

If, during the period, CCWater cease measurement of the relevant data set, the company will replace the source data and measurement for this performance commitment with an appropriate equivalent confirmed and assured by an appropriately qualified independent third party.



Long term supply demand schemes

Definition:

The expected number of months delay to deliver long term supply-demand capacity benefit of 182.5 MI/d which is expected to be delivered by 31 March 2027.

The capacity benefit (MI/d) target represents the total of the stated average capacities for the individual schemes, both treatment and transfer, identified by the company within the business plan and the revised draft WRMP.

The following schemes are expected to be delivered:

- Ford Wastewater Treatment Works (WwTW) indirect potable water reuse (20 MI/d);
- Utilise full existing transfer capacity (3 MI/d);
- East Woodhay Water Supply Works (WSW) (1 MI/d);
- Bournemouth Water supply from Knapp Mill (20 MI/d);
- Coastal desalination – Shoreham Harbour (10 MI/d);
- Sussex Coast – Lower Greensand (2 MI/d);
- Hardham winter transfer: Stage 2 (2 MI/d);
- Aylesford WwTW indirect potable water reuse – Eccles Lake (18 MI/d);
- Sandown WwTW indirect potable water reuse (8.5 MI/d); and
- Internal interconnections (98 MI/d).

Sewer collapses

Definition:

Sewer collapse: A sewer collapse is considered to be where a structural failure has occurred to the pipe that results in a service impact to a customer or the environment and where action is taken to replace or repair the pipe to reinstate normal service. The measure intentionally does not refer to the magnitude of the collapse. The measure includes rising mains. Collapses on the entire network are to be reported.

Sewer length: Include the length of the entire network, including sewers that transferred to their responsibility under the Transfer of Public Sewers Regs 2011. The company should separately record the length of transferred sewers, the calculation of this measure should be based on the latest measurements of the length.

Surface water management

Definition:

Reduction in volume (m³) of surface water entering the surface or combined sewer network as a result of sustainable urban drainage approaches.

Solutions include sustainable urban drainage approaches to slow down and reduce the volume of water entering the network. These include, but are not limited to:

- Provision of a soakaway, either through providing a grant to the customer or through installation by Southern Water.
- Provision of a sustainable drainage system which does not connect to a combined sewer network or which materially attenuates the flow of surface water to the combined network (e.g. a rain garden).

Community engagement

Definition:

The percentile performance of Southern Water compared to other utility companies in the B4SI annual report

The company has engaged B4SI, a company that measures corporate community investment and philanthropy, to measure the company's performance in line with organisations both within and outside the sector.

The measure will be based on the company's annual ranking of utilities companies in the B4SI annual report, which will be influenced by the company's ongoing commitment to increase hours volunteered, partnering with charities, raising money for charities, community and outreach events and administering community grants.

Each year the company will convert the ranking into a percentile using the excel function 'PERCENTRANK.INC' multiplied by 100 and report this. The data will be organised so that the best company will receive the highest percentile.



Schools visited and engagement with children

Definition:

The measure is the percentage of feedback the company receives, from schools that have been visited in the year, which the schools have rated as ‘good’ or ‘excellent’, based on a survey completed after the visit.

It is measured annually on a reporting year basis.

A ‘visit’ is defined as any activity involving a school, either at the school premises or other venue, which has as its aim the education of pupils in relation to the company’s core activities, including the value of water, water efficiency, ‘unflushables’ and the water cycle.

‘Schools’ includes any establishment involved in the education of children under the age of 18.

The survey should be planned and carried out following social research best practice (e.g. any applicable sections of a relevant code such as that published by the Market Research Society).

The sample size should be selected to give a reasonable statistical significance for the purpose of the performance commitment.

Impounding reservoirs

Definition:

This performance commitment measures the progress that the company makes against its programme of work for enhancing the safety of four named reservoir assets, measured as the percentage completion of the schemes. The company must increase the drawdown rates for four of its largest impounding reservoirs to at least the basic levels as set out in the below table for the purposes of measuring delivery under this performance commitment.

The company must comply with the Reservoirs Act 1975.

Statutory reservoir name	Basic drawdown standard rate (metres per day at 50 percentile inflow)	Latest timing of statutory inspection	% completion allocation	Target completion date of the works
Bewl	1.00	2018	48.8	11 Nov 2022
Darwell	0.83	2024	14.8	11 Nov 2024
Powdermill	0.31	2019	19.9	11 Nov 2024
Weir Wood	0.53	2023	16.5	11 Nov 2024

Mains repairs

Definition:

Mains repairs is defined in the reporting guidance for PR19 – Mains Repairs per 1000 km, published on 27 March 2018. ofwat.gov.uk/publication/reporting-guidance-mains-repairs-per-1000km/

It is reported as the number of mains repairs per thousand kilometres of the entire water main network (excluding communication and supply pipes).

Unplanned water outage

Definition:

Unplanned outage is defined in the reporting guidance for PR19 – Unplanned Outage, published on 4 April 2019. ofwat.gov.uk/publication/reporting-guidance-unplanned-outage/

This measure is reported as the temporary loss of peak week production capacity (PWPC) in the reporting year weighted by the duration of the loss (in days). Unplanned outage for each water production site is calculated separately and then summed over the reporting year to give a total actual unplanned outage for the water resource zone.

The company water resource zone weighted outage should then be summed (MI/d) and normalised based on overall company peak week production capacity to be reported as a percentage.



Risk of sewer flooding in a storm

Definition:

Risk of sewer flooding in a storm is defined within the guidance titled, Reporting guidance – Risk of sewer flooding in a storm, published on 4 April 2019: ofwat.gov.uk/publication/reporting-guidance-risk-of-sewer-flooding-in-a-storm/

This measure will record the percentage of the region’s population at risk from internal hydraulic flooding from a 1 in 50-year storm, based on modelled predictions.

D-MeX

Definition:

D-MeX is a measure of customer satisfaction. A company’s overall D-MeX score is calculated from two components that contribute equally:

- qualitative D-MeX score, based on the ratings provided by developer services customers who transacted with the company throughout the reporting year to a customer satisfaction survey; and
- quantitative D-MeX score, based on the company’s performance against a set of selected Water UK performance metrics throughout the reporting year.

The survey results which are used to calculate the qualitative component of the company’s D-MeX score will be supplied by a survey agent appointed by Ofwat. This is supplied out of 100 to form the score for the qualitative component of D-MeX.

The set of Water UK performance metrics which are used to calculate the quantitative component of the company’s D-MeX score, in place at the time of PR19 final determinations publication, are set out in annex 2 of ‘PR19 final determinations: Customer measure of experience (C-MeX) and developer services measure of experience (D-MeX) policy appendix’. For each metric, a percentage is reported and a simple average of these metrics is taken. This is rescaled to be out of 100 to form the score for the quantitative component of D-MeX.

Water supply resilience

Definition:

Number of residential properties at risk of long term loss of supply (>48 hours) in the company’s Thanet, Brighton and the Isle of Wight water supply zones.

A property is considered at risk of long term loss of supply (>48 hours) if it is likely to experience a long term supply interruption if one of the key hazards identified in the table below were to occur.

The key hazards and assets that are considered in the assessments are summarised in the table below.

Key hazards	Water supply works	Service reservoir	% completion allocation	Target completion date of the works
Flooding	✓	✓	✓	X
Critical Asset Failure	✓	✓	✓	✓
Contamination	X	✓	X	✓
Raw Water Loss	✓	X	X	X
Malicious Damage	✓	✓	✓	X
Cyber Security Incident	✓	✓	✓	X



Protect and improve the environment

Abstraction Incentive Mechanism

Definition:

The abstraction incentive mechanism (AIM) reduces abstraction of water at environmentally sensitive sites when flow or levels are below an agreed point otherwise known as a trigger. The trigger point is usually based on a level or flow, beyond which the AIM is considered to be 'switched on'. This trigger will usually be related to the point at which damage is caused and is intended to prevent this from happening or ameliorate the negative impacts.

The company has included one site for AIM for the period 2020–25, this is Otterbourne and Twyford. The trigger point for this site is the month of September as this is when impacts on the environment are most severe.

The September total abstraction limit for the 2020–25 period is 2280 MI. The company's stated target is to outperform this by 15 MI/d.

The abstraction incentive mechanism is defined in the reporting guidance – Guidelines on the abstraction incentive mechanism, published in 2016: ofwat.gov.uk/wp-content/uploads/2016/02/gud_pro20160226aim.pdf

Pollution incidents

Definition:

Pollution incidents is defined in the following guidance for PR19 – Water & Sewerage Company Environmental Performance Assessment (EPA) Methodology (version 3). Published November 2017 by the Environment Agency.

ofwat.gov.uk/wp-content/uploads/2017/12/WatCoPerfEPAmethodology_v3-Nov-2017-Final.pdf

Thanet sewers

Definition:

The expected number of months delay to deliver an enhancement scheme related to the reduction of exfiltration from sewers located within tunnels in Thanet by 31 March 2025.

The specification of the scheme is set out in the company's April 2019 business plan

Maintain bathing waters at 'excellent'

Definition:

The number of bathing waters maintained at 'Excellent' each year, as designated by the Environment Agency, based on a four-year average.

This measures the number of designated bathing waters within the Southern Water region which are assessed as having Excellent bathing water quality at the end of each bathing season.

This is based on a four-year assessment. If a bathing water is closed for sampling the company will use the most recent classification as reported by the Environment Agency.



Protect and improve the environment

Improve the number of bathing waters to at least 'good'

Definition:

The cumulative number of named bathing waters that are improved and assessed as at least 'Good' water quality classification by the Environment Agency in the 2020-25 period.

The following are the named bathing waters to be taken to 'Good' classification:

- Broadstairs Viking Bay
- Littlestone
- Lancing, Beach Green
- Hastings Pelham Beach
- Felpham

If during investigations an additional bathing water is identified it can be added to this list with the agreement of the Environment Agency.

If a bathing water is de-designated during the period, it will not be counted and will reduce the potential for the company to perform.

For the 2024–25 reporting year, if a season is classed as 'abnormal' as there are at least two samples two standard deviations away from typical wet weather affected samples, an underperformance payment will not apply for the 2024–25 year so far that it relates to an 'abnormal' assessment. The performance assessment would be deferred to the following year. The performance assessment for bathing waters assessed as abnormal will not be deferred again. It is expected that any underperformance or outperformance payments for bathing waters assessed as abnormal for the 2024–25 year will apply instead for the year 2025–26, this will be confirmed at the next price review. The overall amount of underperformance or outperformance payments should be the same as if an assessment takes place in 2025–26, had taken place in 2024–25.

Improve the number of bathing waters at 'excellent' quality

Definition:

The cumulative number of named beaches that are improved and assessed as 'Excellent' bathing water classification by the Environment Agency in the 2024–25 period. At least two from the following four bathing waters will be improved:

- Gurnard;
- Seagrove;
- Ramsgate Sands; and
- Pevensey Bay

If a bathing water is de-designated during the period, it will not be counted and will reduce the potential for the company to perform.

For the 2024–25 reporting year, if a season is classed as 'abnormal' as there are at least two samples two standard deviations away from typical wet weather affected samples, underperformance payments will not apply for the 2024–25 year so far that it relates to an 'abnormal' assessment. The performance assessment would be deferred to the following year. The performance assessment for bathing waters assessed as abnormal will not be deferred again. It is expected that any underperformance or outperformance payments for bathing waters assessed as abnormal for the 2024–25 year will apply instead for the year 2025–26, this will be confirmed at the next price review. The overall amount of underperformance or outperformance payments should be the same as if an assessment that takes place in 2025–26, had taken place in 2024–25.

Effluent re-use

Definition:

Volume of treated effluent in cubic metres (m³) made available annually for direct re-use by customers. The measurement will be m³ of treated effluent utilised by local authorities, businesses, farmers and communities on an annual basis. It measures effluent that the company no longer discharges direct to the environment but instead provide to a third party (at the appropriate quality required) for use. This could be, for example, to a council for watering flower beds or to a grower for crop irrigation.



Protect and improve the environment

Natural capital

Definition:

The cumulative number of river catchments for which the company establishes and publishes baseline natural capital accounts.

The company will establish baseline natural capital accounts for at least three of its ten catchments (the Test, Arun & Western Streams and Medway catchments) supported by natural and social capital metrics that will allow it to monitor and measure changes in natural capital stocks (extent and condition) and the value of water-related ecosystem services over time as a result of its investments/activities.

Distribution input

Definition:

This measure is reported as an annual average in megalitres per day (Ml/d). Distribution input should be reported using the following criteria:

- Distribution input to the system shall be metered with at least daily readings at all locations of water input to the distribution network at treatment works, boreholes and bulk supply locations;
- Meters shall be an appropriate size for the flow to be measured and located at appropriate inputs to the network confirmed by record plans. Any treatment works' take-off downstream of a meter shall be excluded from the distribution input calculations; Data validity checks shall be carried out at least monthly;
- Any missing data shall be infilled using both pre- and post-data for the location over at least one month, extrapolated from pump hours or use of upstream or downstream meters; and
- The data transfer systems from meter output to the central database shall be checked and validated on a risk-based frequency every one to two years.

This measure should be calculated consistently with other water balance components. If any missing data is infilled then the same data should be used in leakage and per capita consumption (PCC) reporting.

Treatment works compliance

Definition:

Treatment works compliance is defined in the reporting guidance for PR19 – Water & Sewerage Company Environmental Performance Assessment (EPA) Methodology (version 8).

[ofwat.gov.uk/publication/environment-agencys-epamethodology/](https://www.ofwat.gov.uk/publication/environment-agencys-epamethodology/)

The discharge permit compliance metric is reported as the number of failing sites (as a percentage of the total number of discharges) and not the number of failing discharges.

Renewable generation

Definition:

Total renewable electricity generated as a percentage of the company's total electricity consumption.

The measure includes all electricity consumed at the company's sites, including both operational sites and offices.

All renewable energy generated on the company's sites will contribute towards this performance measure, irrespective of whether it has been generated using assets owned, operated and maintained by it, or on behalf of it by a third party, non-regulated, or subsidiary business unit. In this way performance against the target will be intrinsically linked to behaviours incentivised by the market for the purpose of value creation and not restricted by a traditional operating model.

The total amount of renewable electricity generated at the company's sites is measured in kilowatt hours (kWh) at the generation source after deducting any power not used (parasitic loads) and including electricity both consumed on site and any surplus exported into the National Grid.



Protect and improve the environment

Satisfactory bioresources recycling

Definition:

The overall percentage of company sludge satisfactorily used or disposed of in line with version 3 of the Environment Agency's Water and Sewerage Company Environmental Performance Assessment (EPA) methodology (published November 2017), which includes compliance with certain environmental laws and industry agreements in effect at the date of final determination, including:

- the Sludge (Use in Agriculture) Regulations 1989;
- Environmental Permitting (England and Wales) Regulations 2010; and
- Water company voluntary compliance with the Safe Sludge Matrix.

The full methodology, published in 2017, can be found here:

ofwat.gov.uk/wp-content/uploads/2017/12/WatCoPerfEPAMethodology_v3-Nov-2017-Final.pdf

River water quality

Definition:

The cumulative length of river improved as a consequence of regulatory and legislative drivers.

The length of river defined as improved will be based on the delivery of specified schemes in the WINEP. The commitment level will be limited to those schemes with Green status as at 1 April 2019 and which are already confirmed.

The length of river water quality improvements will be derived from specified schemes in the WINEP. It is assumed for the purposes of this performance commitment that delivery of the WINEP schemes will deliver the specified improvements to water quality.

Combined Sewer Overflows (CSO) Monitoring

Definition:

Percentage of CSOs with effective monitoring. To count as effective monitoring under this measure, the following criteria will apply:

- The monitor is an 'Event and Duration Monitor', which is a monitor that monitors that a CSO has spilt and the duration of the spill;
- The monitor is in place and available providing at least 10 months valid data in any one year;
- Data from the monitor has been validated, through either internal or external review; and
- Data from the monitor has been made available on the company's website.

WINEP delivery

Has the company 'met' or 'not met' all of its requirements for WINEP, in the reporting year.

This measure tracks the completion of required schemes in each year, as per the latest WINEP programme published by Defra. If any scheme is not delivered by the time specified in the WINEP tracker titled 'Completion Date (DD/MM/YY)', the company will report 'not met'.

All WINEP schemes will be included including those reported under other performance commitments.



Use water wisely

Access to daily water consumption data

Definition:

Number of residential properties provided with a device which can give access to daily water consumption.

The measure includes all residential properties.

Water saved from water efficiency visits

Definition:

Estimated reduction in consumption in cubic meters per days from 1 April 2020.

The estimate is based on the number and type of water saving devices fitted and their estimated usage reduction. This will be calculated by the company's water efficiency visit supplier at the time of the visit.

A water saving device is any physical device designed to save water (for example, a low flow shower head or tap aerator) or other intervention (for example, dripping tap repair).

The estimated saving will be based on the estimated daily saving associated with each device installed and the customer's stated usage. The estimated daily saving associated with each device installed will be published on the company website.

The annual savings will be calculated as the sum of the estimated daily savings at each property.

The measure includes all residential properties.

Leakage

Definition:

The percentage reduction of three year average leakage in megalitres per day (Ml/d) from the 2019–20 baseline. The total level of leakage is defined in the Final reporting guidance for PR19 – Leakage, published on 27 March 2018: ofwat.gov.uk/publication/reporting-guidance-leakage/

Three-year average values are calculated from annual average values for the reporting year and two preceding years and expressed in megalitres per day (Ml/d).

Per capita consumption

Definition:

Per capita consumption is defined in the Final reporting guidance for PR19 – Per Capita Consumption, published on 27 March 2018: ofwat.gov.uk/publication/reporting-guidance-per-capita-consumption/

Three-year average values are calculated from annual average values for the reporting year and two preceding years and expressed in litres/person/day (l/p/d).

Target 100

Definition:

Percentage of household population with estimated per capita consumption (PCC) of less than 100 litres/person/day. PCC is defined as the average amount of water used by each customer that lives in a household property

Appendix 3. Board statement on the accuracy and completeness of the data and information (financial and non-financial)

We, the Board of Southern Water (SWS), have considered carefully the requirements of the Board statement on the accuracy and completeness of the data and information (financial and non-financial). The Board is pleased to provide the following Board Statements.

We believe that our stakeholders deserve to have trust and confidence in the integrity of the information we provide in our annual reports. In order to achieve this, our performance reporting is subject to a system of checks to ensure that we meet the highest quality of reported information.

The Board has been fully aware of previous issues with the control environment of the company and has over the last six years worked with the executive management team to rebuild capability in this area. This work is on-going and is on track and is now supporting our operational turnaround plans.

Subject to this, the Board has actively engaged and challenged the assurance processes that have been adopted by the company. This covers assurance on both the financial and non-financial reporting and assessment of applicable confidence grades. The Board has, over recent years, taken action to ensure that exceptions and weaknesses in the assurance approaches have been addressed. The Board are satisfied that the approaches have appropriately identified and addressed any risks to the provision of accurate and complete data and information. This has been discharged through the SWS Board and its relevant Committees (most notably the Audit Committee).

Detail of this activity is included below:

Financial Reporting

- The Board has reviewed the external auditor assurance outputs from Deloitte relating to the statutory and regulatory accounts.
- The Board have visibility of the high-level financial governance and controls that are in place around our financial reporting, and this is captured as part of the annual external audit, internal audit reports looking at financial controls and updates on the implementation of new accounting standards as reflected in the Schedule of Matters Reserved to the Board.
- The Board reviews the monthly KPI reports, including performance against budgets.

- The Board, via its Committees, monitors the Southern Water internal control framework and if necessary, how weaknesses are being addressed. This applies to both Financial and Non-Financial controls.
- The Board has approved updates in the Annual Report, Interim Accounts, Annual Performance Report and Data Assurance Summary that detail improvements in governance and controls, and has included specific caveats where capability has been improving.

Non-Financial Reporting

- The Board continues to support the company to ensure it maintains the standards required by our regulators and ourselves – for example, data reporting and assurance – work is ongoing to materially improve processes and systems, underpinned by values-based ethical business practice, to ensure the mistakes of the past are not repeated.
- SWS has adopted the ‘three lines of defence’ framework for reporting governance and assurance activity. This has been in place since 2017 and has supported the continued maturity of the internal system of control and helps to assure performance information by applying multiple levels of control. The process continues to be embedded across the business, and the management focus is on the areas of highest risk. The framework is delivered and reviewed as part of the Final Assurance Plan and the Internal Audit Annual plan (both of which are signed off by the Audit Committee).
- Internal controls are applied and improved processes are now in place to mitigate the risk of supplying incorrect or inaccurate information in all the company’s non-financial regulatory reporting. A programme of improvements continues to strengthen first and second-line assurance processes for all regulatory reporting. The next phase of control improvements being supported by the implementation of new technology (including a new Governance Risk and Control system) is systemising some of the manual improvements that have been implemented over the last six years.

- The Board and Audit Committee regularly receives and reviews information and reports on non-financial resources and performance that support the efficient delivery of services to our customers and other stakeholders.
- The Audit Committee review progress of non-financial reporting improvement plans and the Ofwat Section 19 undertakings.
- The Board reviewed the assurance outputs regarding the non-financial performance, reported in the 2022–23 Annual Performance Report from KPMG LLP. KPMG LLP presented their views to the Board Audit Committee at the meeting on 16 June 2023.
- The Board, via its Audit Committee has, received an internal assurance report in March 2022, which reported Southern Water compliance with their Licence of Appointment.
- The Board, via its Committees, monitors the Southern Water internal control framework and if necessary, how weaknesses are being addressed. This applies to both Financial and Non-Financial controls.
- The Audit Committee has monitored the completion of a risk-based programme of internal assurance activities during the year, as part of an Internal Audit programme.

Data Assurance Summary

We have published a separate document that details the completed assurance work performed on our reported information for the 2022–23 financial year. The results, both positive and improvement areas are published in the document entitled 'Data Assurance Summary' which is available on our Southern Water website southernwater.co.uk/our-reports.



Stuart Ledger
Chief Financial Officer

14 July 2023



Keith Lough
Chair

Appendix 4. Condition P – Ring-fencing Certificate – Board assurance statement

The Board is pleased to provide the following Board Statements:

We, the Board of Southern Water, have carefully considered the requirements of the Condition P Certificates and have undertaken reasonable diligent enquiry and challenge to confirm the statements made below. The Board considers that these arrangements are in place for the at least the next 12 months.

NB: For the purposes of this statement “the Board” refers to the Southern Water Board and its key committees including the Audit Committee, the Remuneration Committee, Nominations Committee, Health and Safety and Operational Risk Committee, ESG Committee and the PR24 Committee.

The Board is pleased to provide the following Statements:

Financial resources and facilities:

- In September 2021, funds managed by Macquarie Asset Management invested £1.1 billion of equity into Southern Water and its holding companies. This recapitalisation by a new majority shareholder is facilitating Southern Water’s Turnaround Plan, including the investment of £2 billion in its network during the current regulatory period (2020–25).
- Southern Water has engaged with its shareholders to seek an additional £550 million of equity funding for the Southern Water group of which £375 million will be invested as equity into Southern Water’s regulated entity and £175 million into its holding companies. Southern Water expects this equity raise will successfully conclude by the end of October 2023, with participation by funds managed by Macquarie Asset Management and potentially other existing shareholders, but this has not been committed at the date of the statutory financial statements or at this report, and hence was identified as a material uncertainty with respect to going concern in the Annual Report and Financial Statements.
- The planned £375 million equity injection into Southern Water will maintain a prudent gearing ratio, consistent with the deleveraging of the Group since the equity recapitalisation in 2021. Interest cover ratios are forecast to be lower in this regulatory period due to the additional expenditure. Southern Water expects that the interest cover ratios will normalise in the next regulatory period.

- The Board has reviewed the going concern for at least 12 months from signing the accounts and the long-term viability assessment (LTVA) to March 2030. This included the company’s liquidity position, headroom against the financial covenants, credit ratings and financial risk assessment against a number of downside scenarios. In addition, the Board have considered the material uncertainty outlined in the going concern as referenced in our Annual Report and Financial Statements.
- The Board has considered the implications of the announcement by Fitch on 7 July 2023 to downgrade the Class A Unwrapped Debt of the company to BBB (negative outlook) which resulted in a credit ratings Trigger Event and the fact that the company also expects to be in a debt covenant Trigger Event. Proactive action is being taken regarding this and the Board does not believe that they will materially impact the financial resources and facilities available to the company.
- The Board has reviewed the plans that were presented to them in the updated SWS Business Plan (EP23) for the period up to the end of this business plan period and concluded that they are aligned to meeting the needs of our customers and stakeholders and are in line with the final determination that has been agreed with Ofwat. The Board has approved EP23.
- The Board is confident that EP23 delivers our statutory and regulatory obligations and allows us to demonstrate compliance with Condition P of the Licence of Appointment.
- The Board receives updates on the financial status of the company including cash flow forecast and monitoring. The Board also receives updates on the company’s credit ratings and meetings with the credit rating agencies.
- The Board is aware of potential litigation in relation to investigations by the Environment Agency and has approved related financial disclosures within the financial accounts.

Subject to the successful completion of the equity raise of £375 million as detailed opposite which gave rise to a material uncertainty with respect to going concern, the Board confirms that the company has sufficient financial resources and facilities.

Management resources:

- The Board has acknowledged that, in the past, the company failed to meet its own high expectations. The Board continues to strongly support the executive management, who have continued to work to ensure previous improvements are embedded into the way the company conducts its business (an example of this has been the regular updates the Audit Committee receives on the embedment of the Three Line Defence model, and our compliance activities).
- The company has continued to evolve its management structure in the financial year, bringing in key resource at executive level to support the further development of the company. This includes making a number of key appointments at senior director level including a new Chief Financial Officer in January 2023, a new Chief People Officer in May 2023, and a new Interim Director of Corporate Relations in May 2023.
- The General Counsel and his wider team function as the second line team and provide the check and challenge on the rest of the company. It delivers a risk-based programme (structured around our obligations) to ensure that the company is meeting its regulatory and statutory obligations.
- The Board also conducts reviews of its own capability through Board effectiveness reviews, which are supported by external assessments of their capability. An external assessment was undertaken in 2021–22 as part of an externally-facilitated Board evaluation once every three years. An informal review of effectiveness was conducted in 2022–23.
- The Board also looks to ensure that its membership is diverse to ensure a diversity of perspectives. The Board's Nomination Committee has committed to review this area following the changes of shareholder representatives which has reduced the Board's diversity.

The Board therefore confirms that the company has sufficient management resources.

Systems of planning and internal control:

- The Board continues to support the company to ensure it maintains the standards required by our regulators and ourselves – for example, asset compliance, or data reporting and assurance – work is ongoing to materially improve processes and systems, underpinned by values-based ethical business practice, to ensure the mistakes of the past are not repeated.
- SWS has adopted the 'three lines of defence' framework for reporting governance and assurance activity. In relation to non-financial reporting, this has been in place since 2017 and has supported the continued maturity of the internal system of control and helps to assure performance information by applying multiple levels of control. The framework is delivered and reviewed as part of the Final Assurance Plan and the Internal Audit Annual plan (both of which are signed off by the Audit Committee).
- The Board and Audit Committee regularly receives and reviews information and reports on non-financial performance that support the efficient delivery of services to our customers and other stakeholders.
- The Board have visibility of the high-level financial governance and controls that are in place around our financial reporting, and this is captured as part of the annual external audit, internal audit reports looking at financial controls and updates on the implementation of new accounting standards. There is a Schedule of Matters Reserved to the Board.
- The Board has also commissioned a review of the schedule of delegated authority and financial approvals.
- The Board reviews the monthly KPI reports, including performance against budgets.
- The Audit Committee reviews progress of non-financial reporting improvement plans and the Ofwat Section 19 undertakings.
- The Board reviewed the assurance outputs regarding the non-financial performance, reported in the 2022–23 Annual Performance Report from KPMG. KPMG presented their views to the Audit Committee at the meeting on 16 June 2023.
- The Board are involved in the approval of key milestones on our work on Water For Life Hampshire and our submissions to RAPID.

- The Board is actively involved in supporting the development of the PR24 submission to Ofwat. The Board has a key role in the PR24 process. The PR24 Board Assurance Process includes the development of oversight structures and a detailed programme of board assurance, which has covered all areas of the plan and included specific arrangements for approving and assuring the WRMP, WINEP and DWMP submissions.
- The Board, via its Audit Committee, has received an internal assurance report in March 2023 (produced by the Risk and Assurance Team), which reviewed Southern Water compliance with its Licence of Appointment.
- The Board, via its Audit Committee, is actively involved in reviewing current gaps and the resulting preparations for the UK government proposed changes in relation to Corporate Reform / internal controls over financial reporting.
- The Audit Committee has monitored the completion of a risk-based programme of internal assurance activities during the year, as part of the Internal Audit programme.
- The Board has overall responsibility for risk management and is supported in this role by the Audit Committee (who have recently taken on the responsibility for Enterprise Risk) and the Health and Safety and Operational Risk Committee.
- The Board, via the Audit Committee and the Health and Safety and Operational Risk Committee, reviews key areas of risk for the company in regular 'deep-dive reviews'.
- The Board has approved updates in the Annual Report, Interim Accounts, Annual Performance Report and Data Assurance Summary that detail improvements in governance and controls and has included specific caveats where capability is still improving.

The Board has been fully aware of previous issues with the control environment of the company and has over the last six years worked with the Executive Team to rebuild capability in this area. This work is on-going and is on track but will require further work in coming years. Subject to this, the Board therefore confirms that the company has appropriate governance policies and procedures in place to maintain an effective control environment.

Resources other than financial or management resources:

- The ESG Committee conducted a deep dive on the company's ED&I initiatives and Agreed targets in this area.
- The Board has continued to support the embedment of the Southern Water values. The company values, developed in 2019, continue to be embedded. This has included a recent addition of a fourth value, 'working with care'.
- The Board were presented and approved the Code of Ethics in September 2022. The company's Speak Up procedures have been enhanced, and an annual review of Speak Up was presented to the Audit Committee in March 2023, in addition to regular updates on Speak Up at each Audit Committee.
- The Audit Committee receives regular detailed reports on Speak Up cases and discusses progress on resolution.

The Board therefore confirms that the company has sufficient programmes on culture and employee engagement to support non-financial resources and facilities

Contracting:

- The Board, through its PR24 Committee have reviewed our procurement arrangements as part of our preparations for the next Business Plan Period, and as part of work on deliverability for PR24.
- The company does have active Associated Companies, but these are used for financing purposes and do not have any operational contracts or transactions with the operating company.

The Board confirms that whilst it does have Associated Companies in place these do not have any operational contracts or transactions with the operating company.

Material issues or circumstances:

The Board has considered the following material issues or circumstances that meet our Condition P Certificate in relation to the operation of our wastewater business (as detailed in our S19 undertakings with Ofwat):

- The Board has reviewed the financial resources and facilities related to our wastewater business as part of the Execution Plan (EP23) including the budget and confirms that there are sufficient resources in relation to our wastewater operations over the next twelve months.
- The Board has previously considered the organisational structures and governance within our wastewater business and confirms that we are able to deliver services to our customers and stakeholders and meet our statutory and regulatory requirements in this area – the Board originally approved changes to the company’s organisational structure that took place in 2017, and included work on the separation of duties in the Wastewater Directorate and the establishment of the Risk and Compliance Directorate (now part of our General Counsel Directorate) and the development of a ‘Three Lines of Defence’ model of compliance. The Board is confident that these changes have been embedded in the company and are a key element of improvements and transformation of the company. These arrangements are subject to detailed external assurance as part of our S19 Undertakings to ensure they remain in place and are embedded in the way the company performs its duties.
- The Board acknowledges that whilst we come toward the end of the period of the S19 undertakings, it still requires regular update on these matters.
- The Board confirms that it is aware of the material risks faced by the wastewater business and the company has undertaken appropriate investigations to ensure all significant risks are identified, together with the monitoring of key risk mitigation actions.

- The Board has considered the specific operational plans relating to our wastewater business, as part of our review of the updated draft EP23 including the budget and confirm they are aligned to meeting the needs of our customers and stakeholders and are aligned with the final determination and Undertakings that have been agreed with Ofwat.
- The Board, via its Audit Committee, has been provided regular updates on the progress of the S19 Undertakings and has provided robust check and challenge on the process over the year.

The Board therefore confirms that it has considered the material issues facing the wastewater business (as detailed in our S19 undertakings with Ofwat), and that the company has sufficient financial, non-financial resources and facilities.



Stuart Ledger
Chief Financial Officer



Malcolm Cooper
Chair of the
Audit Committee

14 July 2023

Appendix 5. Glossary of regulatory terms

Appointed business

The appointed business comprises the regulated activities of the company which are necessary for it to fulfil the function and duties of a water and sewerage undertaker under the Water Industry Act 1991.

Arm's-length trading

Where the company treats associate companies on the same basis as external third parties.

Asset Management Plan (AMP)

A plan agreed with Ofwat on a five-yearly basis for the management of water and wastewater assets. The plan runs for a five-year period. AMP7, the seventh plan since privatisation, covers April 2020 to March 2025.

Associated company

Condition A of the Licence defines an associated company to be any group or related company. Condition F of the Licence requires all transactions between the company and its associated companies to be disclosed subject to specified materiality considerations.

C-MeX

C-MeX is Ofwat's measure of customer experience. It comprises two surveys – a survey of customers who have recently contacted their company and a survey of random members of the public in relation to their water company. These are used to calculate a score which can be compared between water companies, with rewards and penalties for the best and worst performers.

Final Determination (FD)

The conclusion of discussions on the scale and content of the Asset Management Plan for the forthcoming five-year period. It includes a determination of the allowable revenues for the period and the performance targets that must be achieved.

K factor

The annual increase, set by Ofwat, in wholesale revenues that companies in the water industry can recover from customers. The amount by which a company can increase (or must decrease) its revenues is controlled by the price limit formula $CPIH + \text{or} - 'K'$. CPIH is expressed as the percentage increase in the Consumer Price Index (including owner occupiers' housing costs) in the year to November before the charging year. 'K' is a number determined by Ofwat for each company, usually at a price review, for each year to reflect the revenues it needs above or below inflation in order to finance the provision of services to customers.

Licence

The Instrument of Appointment dated August 1989 under Sections 11 and 14 of the Water Act 1989 (as in effect on 1 August 1989) under which the Secretary of State for the Environment appointed Southern Water Services Limited as a water and wastewater undertaker under the Act for the areas described in the Instrument of Appointment, as modified or amended from time to time.

Non-appointed business

The non-appointed business activities of the company are activities for which the company as a water and wastewater undertaker is not a monopoly supplier (for example, the sale of laboratory services to an external organisation) or involves the optional use of an asset owned by the company (for example, the use of underground assets for cable television).

Ofwat

The name used to refer to the Water Services Regulation Authority (WSRA). The WSRA is the economic regulator of the water industry.

Outcome Delivery Incentive (ODI)

Performance Commitments with outperformance and/or underperformance payments agreed with customers and Ofwat through the periodic review process.

Performance Commitment (PC)

Performance Commitments are service targets set by Ofwat as part of the Final Determination.

Periodic review

A review conducted by Ofwat each five years for the purpose of determining price controls. Each water and wastewater undertaker submits a business plan covering the five-year period for which Ofwat will set the controls. (PR19 relates to 2020–25; PR24 will cover the period 2025–30).

Price control

A price control determines the limit on the level of charges or revenues that can be recovered from customers. As part of the price control Ofwat also determines performance targets and other related matters.

Regulatory Accounting Guidelines (RAG)

The accounting guidelines for regulatory accounts issued, and amended from time to time, by Ofwat.

Regulatory Capital Value (RCV)

The capital base used in setting price limits. The value of the appointed business that earns a return on investment. It represents the initial market value (200-day average), including debt at privatisation, plus subsequent net new capital expenditure including new obligations imposed since 1989. The capital value is calculated using the Ofwat methodology (i.e. after current cost depreciation and infrastructure renewals accrual).

Consumer Price Index (CPIH)

CPI is a measure of the change in consumer prices based on the prices of a typical basket of goods and services in the United Kingdom. The CPIH measure, includes owner occupier's housing costs. This is the principal measure of inflation used by Ofwat for regulatory purposes, including inflating allowed revenues or prices.

Totex

Total expenditure is the sum of operating expenditure and capital expenditure. It is used by Ofwat to determine the efficient level of costs as part of the periodic review process.

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