

Annual Report & Accounts 2014



"Delivering excellence for our customers,
our people and our environment"



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HIGHLIGHTS

Our Mission

“To supply high quality drinking water whilst providing excellent levels of service for our customers at the lowest price in the country”

During the past year, Portsmouth Water has again maintained its reputation for supplying high quality drinking water, providing excellent levels of customer service and carrying out its functions in a low cost, efficient manner:

- Lowest charges in England and Wales with an average bill of £94
- Leakage reduced to 29.5 MI/d
- Fewest written complaints with only 7.6 complaints per 10,000 connected properties, compared with an industry average for last year of 49
- RoSPA Gold Medal for health and safety
- Submission of Business Plan to Ofwat proposing no price rises beyond inflation for the period 2015 - 2020
- Exceeded water efficiency target set by Ofwat

Operating profits down by 7.0% due to additional costs connected with our leakage recovery programme and costs incurred in submitting the Company's Business Plan to Ofwat.

Values

Our values underpin how we behave in delivering all aspects of our work. These are:

“Excellence, Respect and Integrity”

Turnover £m

£37.11m

2011	35.52
2012	36.67
2013	36.28
2014	37.11

Operating profit £m

£5.89m

2011	6.11
2012	6.51
2013	6.33
2014	5.89

Operating profit before depreciation £m

£14.83m

2011	14.37
2012	15.09
2013	15.25
2014	14.83

Operating cashflow £m

£15.14m

2011	17.56
2012	15.72
2013	15.67
2014	15.14

Capital expenditure £m

£10.67m

2011	9.55
2012	8.13
2013	15.36
2014	10.67

BOARD OF DIRECTORS

Executive



Neville Smith

B.A., F.C.M.A.³

Managing Director

Joined and appointed to the Board in February 1998. Appointed Managing Director in December 2011.



Nicholas John Sheeran

B.Sc. (Hons), A.C.M.A., C.G.M.A.

Finance and Regulation Director

Joined and appointed to the Board in December 2011. Previously with Invensys plc and Caradon plc.



Roderic Colquhoun Porteous

B.Sc., C.Eng., M.I.C.E.

Engineering Director

Joined in 1999. Previously with South East Water. Appointed to the Board in May 2012.

Non-Executive



Terence Michael Lazenby MBE

FR.Eng.¹²³

**Independent Non-Executive Chairman
Chairman of the Nomination Committee**

Joined in June 2002 and appointed Chairman in January 2003. Previously Chairman of the Engineering Construction Industry Training Board, Non-Executive director of MTL Instruments Group plc and Expro International plc, before which he held a number of Senior Executive positions with British Petroleum. Trustee of ITB Pension Fund.



Michael Peter Kirk

MBA, C.Eng., M.I.Cheme, M.Sc., B.Sc. (Hons)¹²³

**Senior Independent Non-Executive Director
Chairman of the Audit Committee**

Joined in November 2012. Chairman of Thackray Medical Museum, Deputy Chairman of Performance Audit and Risk Committee, The Conservation Volunteers. Previously partner at Cazenove and Co. and Managing Director of Weber Shandwick.



Heather Virginia Benjamin

B.A., C.M.I.P.D., I.A.C.C.M., C.I.P.S.¹²³

**Independent Non-Executive Director
Chair of the Remuneration Committee**

Joined in November 2012. Previously held senior positions with Centrica plc. Current Chair of Trustees, Walsingham organisation, Non-Executive Board member of Academy of St. Martins in the Fields Orchestra and Advisory Board for 4C Consultancy.

¹ Member of the Audit Committee

² Member of the Remuneration Committee

³ Member of the Nomination Committee

CHAIRMAN'S STATEMENT

I have the great pleasure to introduce the Annual Report and results for the year ending March 2014. It has been an eventful year with the Periodic Review, development of market reform and greater interaction with our customers being major matters addressed by the management and the Board. At the same time we have delivered an excellent operational and financial performance.

Much of the focus over the past year has been around the Company's submission to Ofwat of its Business Plan for the next price review period (2015 - 2020). Ofwat sets price limits for Portsmouth Water every five years. The Company submitted its Business Plan to Ofwat in December 2013. In March 2014 Ofwat announced which Companies had achieved "enhanced" status i.e. the Companies which had produced the best all round plans. Whilst not achieving "enhanced" status, it is clear from subsequent correspondence from Ofwat, that Portsmouth Water's Business Plan was well received. The Company regards this as a significant achievement, and is testimony to the excellent work undertaken by our staff. It is particularly pleasing that the Company's investment proposals were accepted by Ofwat. The Company is currently in the process of revising its Business Plan to be in line with Ofwat's guidance on Risk and Reward. The revised Plan will be submitted to Ofwat in June 2014 with a Draft Determination expected in August 2014. Ofwat expects all Final Determinations to be issued in December 2014.

I would like to thank all the members of our Customer Challenge Group (CCG) for their help and support in producing our Business Plan.

In May the Water Bill was given Royal Assent which will allow all non-household customers to choose their water supplier from April 2017. The 'Open Water' programme has been established to ensure that the industry is prepared for the changes to the market. The Company is currently working to ensure that it meets the necessary compliance requirements in time for market opening in October 2016. The Company is also assessing what its strategy should be in the new retail market and how best to serve its customers under the new regime.

In the last year Ofwat has published the principles of Corporate Governance which it expects companies to follow. In response the Board has established a Governance Code which is published on the Company website. Details of our compliance with the Ofwat principles is shown in the Corporate Governance section on pages 26 to 28 of this Report.

Exceptional winter rainfall in 2014 saw groundwater levels rise to near record levels, being the second highest levels experienced since records commenced in 1932. Many of our sites experienced extensive flooding. The resilience improvements undertaken on a number of our sites which were completed in 2012 were subjected to significant testing and proved successful in avoiding any loss of production as a result of flood damage.

As a result of the wettest winter for 230 years, groundwater levels moved to the second highest levels we have recorded. Accordingly there are unlikely to be any restrictions this summer.

As reported in last year's report the Company had carried out a full, independent review of its leakage calculation and methodology. The review had confirmed that there was an error in the calculation of the leakage figure and we determined that our leakage level was higher

than we had been reporting by approximately 6.6 Ml per day for 2011/12. This was reported immediately to Ofwat and the Company immediately put in place a programme to reduce leakage which began in November 2012, which was funded by shareholders.

The leakage recovery programme has made excellent progress and for the full year 2013/14 average leakage was recorded at 29.5 Ml/d (2012/13 - 34 Ml/d) although with a mild winter. This is within the leakage target agreed with Ofwat and was achieved well ahead of our intended schedule. We continue to improve our data and review our methodology.

Pleasingly this year the Company has again exceeded its target for water efficiency, claiming overall savings of 0.32 Ml/d. In the four years of the current regulation period the Company has achieved a cumulative surplus of 0.12 Ml/d against the Ofwat target.

In October 2012 the Company successfully implemented a new billing and customer relationship management system (CRM). During 2013/14 the Company has really started to see the benefits of this new system. For 2013/14 the Company was ranked 7th out of 21 companies in a survey of customers conducted by Ofwat to assess how well the Company handled all types of contact. The Company was ranked 3rd overall (and 1st among water only companies) in terms of its handling of customer contacts for billing matters. In addition the Company maintained the lowest level of complaints in the industry and the overall level of complaints fell by 26%.

The health and safety of employees has the highest priority for the business and the effort and commitment of everyone at the Company was once again rewarded by the award of a Gold Medal from RoSPA for 2014. This will be the ninth consecutive year that the Company has received this accolade and demonstrates all the hard work that has been done in making the Company a safer place to work.

After consultation, the Company published its latest Water Resource Management Plan in November 2013. The WRMP examines the factors which will impact upon the demand for water from its customers such as population change and climate change and identifies whether the Company will have sufficient water resources over the next 25 years to meet this demand. In its plan the Company is projecting a water resource surplus in the period to 2040. As a result, the Company does not need to invest in new water resources to meet the needs of its own customers during this period. However, the Company has been approached by two neighbouring water companies to provide bulk supplies of water to meet the needs of their customers and these have been included in the Plan.

Defra requested further information in March 2014 and will now consider if Portsmouth Water should be instructed to publish its Plan. We await this decision which we expect to receive in the very near future.

The results for 2013/14 reflect the 2009 Price Determination, made by Ofwat which included a real reduction in charges for customers in the year of 1.4%. Turnover for the year increased by 2% to £37.1m. The increase in turnover is largely due to higher consumption from non-household customers with summer demand being much higher than the previous year which had very high rainfall.

Operating costs, excluding depreciation, increased by £1.2m in the year mainly due to the additional costs connected with the leakage

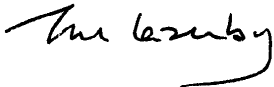
CHAIRMAN'S STATEMENT

recovery programme (£0.5m) and costs incurred in submitting the Company's Business Plan to Ofwat for the period 2015 - 2020 (£0.3m). As a result of the above factors the operating profit was reduced to £5.9m (2013 - £6.3m).

There was an exceptional charge during the year of £0.6m. This relates to the Havant Thicket Winter Storage Reservoir. In our most recent Water Resource Management Plan the Company has a water surplus until 2040 and no requirement therefore to build the reservoir unless more significant bulk supplies are required from our neighbouring water companies. We have, therefore, decided to write off the remaining expenditure on this from the balance sheet.

Gross capital investment during the year was £10.7m (2013 - £15.4m) and included £5.4m (2013 - £5.2m) on infrastructure renewals. After receiving capital contributions and infrastructure charges of £1.1m, net capital expenditure was £9.6m (2013 - £14.5m).

This will be my last report as Chairman of the Company. After 12 years I will be retiring this year. It has been a privilege to work with so many talented people dedicated to providing excellent service to customers. I offer my deepest thanks to the support that individual staff members have given me during my term of office that has made it so special. It is an exciting time for the Industry with changes to the regulatory framework and market reform, but I am confident that my successor, Mike Kirk and the management team will rise to these challenges.



T. M. Lazenby MBE
Chairman

STRATEGIC REPORT

Strategy and Business Model

Principal Activity

The Company is a water supplier operating under an Instrument of Appointment granted by the Secretary of State for the Environment under the Water Industry Act 1991.

Water is supplied to 310,000 domestic and commercial customers in an area of 868 square kilometres in Hampshire and West Sussex through a mains network of 3,293 kilometres.

The Company's area of supply is shown on page 23 of this report.

Mission Statement

'To supply high quality drinking water whilst providing excellent levels of service for our customers at the lowest price in the country'

Vision

'Delivering excellence for our customers, our people and our environment'

Values Our values underpin how we behave in delivering all aspects of our work. These are:

'Excellence, Respect and Integrity'

Strategy

The Company continuously reviews its strategic approach both internally and by engagement with its customers and stakeholders. Over the past couple of years the Company has undertaken extensive research and engagement with stakeholders and customers. After consulting with our Customers and Stakeholders we have developed a number of Outcomes that summarise our proposed business goals and set out our aspirations over the coming years. These outcomes were used as the basis for the Business Plan which the Company submitted to Ofwat in December 2013. These Outcomes are outlined below:

- Safe secure, sustainable and reliable supply of drinking water
- Less water lost through leakage
- A high quality service and value for money
- An improved environment supporting biodiversity, public amenities and recreation.
- Supporting the community we serve by taking opportunities to support the local economy
- Proving attractive to investors, long term sustainable business
- Recognised by stakeholders as having a culture of health and safety through all our activities

In its Business Plan for the period 2015 - 2020 the Company has proposed that prices to the customer only increase by the normal rate of inflation.

Employee Benefit Trust

The ownership structure of the business is unique within the industry, with the majority of the shares being owned by an Employee Benefit Trust (EBT) on behalf of the employees. The Board believes that this structure ensures that we are able to take a long-term view on the business. We believe that this structure also helps to align the interests of employees and customers in the long-term – with the vast majority of our employees also being customers.

Governance

The Board of Portsmouth Water Limited comprises three Executive Directors and three independent Non-Executive Directors. Portsmouth Water is part of the South Downs Capital Group whose ultimate controlling shareholder is an Employee Benefit Trust. A majority of the Directors of the Employee Benefit Trust are independent and are not represented on the Board of Portsmouth Water. This ensures the independence of the Board of the Appointed Water Company. Full details of the Corporate Governance of the Company are published on pages 26 to 28 of this Report.

Financial Structure

Since 2001 the Company has largely been a debt financed entity. An index linked fixed interest loan with a base value of £66.5m was drawn in 2002, with inflation risks on the cost of the loan being effectively hedged against regulated revenues which are also linked to the Retail Prices Index (RPI). Interest is charged at a fixed rate of 3.635% on the indexed amount of the loan. The indexed value of the loan at 31 March 2014 was £95.3m (2013 - £92.4m).

Short term liquidity is achieved through a £10m working capital facility and an overdraft arrangement. At the end of the year, £5.0m of this facility had been drawn (2013 - £5.0m), while the overdraft arrangement remained unutilised. The £10m facility terminates in September 2015 and will be renegotiated again during the current year.

Any short term cash balances are deposited with the Company's bankers, the Royal Bank of Scotland. It should be noted that the Company is currently looking to move its day to day banking facilities to a new bank, during the coming twelve months.

STRATEGIC REPORT

Regulation

The water industry is subject to a range of UK and EU legislation. Standards, particularly those relating to the environment, are being tightened on a regular basis and require increasing levels of investment. The standards of service provided by Portsmouth Water are monitored by three main regulators - the Water Services Regulation Authority (Ofwat) for setting prices and to ensure value for customers, the Environment Agency (EA) for environmental protection and the Drinking Water Inspectorate (DWI) for drinking water quality. Customers are represented by the Consumer Council for Water (CCW), which monitors the quality of service provided by the Company. Portsmouth Water works closely with these and other organisations interested in the services it provides.

Ofwat is the water industry's economic regulator, and its principal duties are exercised through the price-setting process. Ofwat sets price limits for Portsmouth Water every five years. The last determination of prices was in November 2009 for the period 2010 to 2015. The price setting process is known as the Periodic Review and involves a series of consultations between water companies, Ofwat and the other regulators over a two year period. The review examines all aspects of the business and requires the Company to submit a detailed Business Plan to Ofwat. Water companies are allowed to increase prices to customers annually by inflation (RPI) plus or minus the price limit set by Ofwat. The price limits reflect the revenue, which the regulator believes an efficient company needs in order to finance its operations and capital programme, after making an assessment of potential future efficiency gains.

The Company submitted its Business Plan for the next review period (2015 - 2020) to Ofwat in December 2013. The Plan included separate plans for its Retail and Wholesale Businesses, as well as the overall Appointed Business, in preparation for the market opening to competition in 2017. In January 2014, Ofwat issued new guidelines to the water industry on Risk and Reward and in March 2014 announced which companies had achieved "enhanced" status i.e. the companies which Ofwat believed had produced the best all round plans. Whilst not achieving "enhanced" status, it is clear from subsequent correspondence from Ofwat, that Portsmouth Water's Business Plan was the only one which Ofwat regarded as "marginal" i.e. having almost achieved enhanced status. All other Plans submitted by other water companies were classed as "standard" by Ofwat. The Company regards this as a significant achievement, especially due to the fact that the Company's investment proposals were accepted by Ofwat.

The Company is currently in the process of revising its Business Plan to be in line with Ofwat's guidance on Risk and Reward. The revised Plan will be submitted to Ofwat in June with a Draft Determination expected in August 2014. Ofwat expects all Final Determinations to be issued in December 2014.

Prices

The price limits set for the five year period to 2015 are as follows:

	2010/11	2011/12	2012/13	2013/14	2014/15
% (reduction) in bills before inflation	(4.8)	(2.1)	(1.7)	(1.4)	(0.6)

The Company is currently in the final year of the current price review period (2010 – 2015). In 2014/15 prices will be RPI less the "K" factor from the table above (0.6%). Therefore prices for the 2014/15 period have increased by 2.05%. For the next price review period (2015 – 2020) the Company has committed itself to not increasing prices beyond the rate of RPI. Therefore prices for the next five year review period will remain flat in real terms.

Competition and Market Reform

In 2011, the UK Government published the Water White Paper 'Water for Life', which set out its plans to:

- increase choice and improve service for water customers.
- stimulate innovation and drive more sustainable approaches to managing our water resources.

The Water Bill, which received Royal Assent in May 2014, includes the legislative changes required to deliver these ambitions for the water sector. The Bill will enable the creation of a new market for retail water and sewerage services to all non-domestic customers in England. The intention is to open the new retail market in April 2017.

The Company will ensure that it is compliant in time for the market opening in October 2016. This includes compliance in terms of:

- Systems and how these systems interface with the Market Operator. The objective of the Market Operator is to provide services that help enable and facilitate the effective operation of the competitive market arrangements.
- Structure and processes – the business will need to have a structure and processes which allow the retail and wholesale functions to operate separately and on an "arms length" basis, both internally and with other external companies and retailers.

The Company is currently working to ensure that it meets the necessary compliance requirements in good time. The Company is also assessing what its strategy should be in the new retail market and how best to serve its customers under the new regime.

STRATEGIC REPORT

Water Resources

Portsmouth Water provides water to 310,000 homes and businesses in an area covering 868 square kilometres from the River Meon in Hampshire to the River Arun in West Sussex. The Company serves the cities and towns of Portsmouth, Chichester, Fareham, Gosport, Havant and Bognor Regis. On average, each day it supplies approximately 172 million litres of water through a network of 3,293 kilometres of underground mains. The water supplied is derived from the chalk of the South Downs and is abstracted from wells, boreholes, springs and the River Itchen. The table below shows the major sources used by the Company during the year. The springs at Havant and Bedhampton, which provide 28% of the total supply, are thought to be the largest group of springs used for public supplies in Europe.

Source	Actual 2013/14 Abstraction (Million Litres)	% of Supply 2013/14	% of Supply 2012/13
Springs at Havant & Bedhampton	18,005	28	26
River Itchen	6,521	10	9
Boreholes, Wells & Adits	40,481	62	65
Totals	65,007	100	100

A map showing the Company's area of supply and the location of its sources and treatment works is shown on page 23.

Water from the springs at Havant and Bedhampton is treated at the Farlington treatment works and there are also complex treatment works at the River Itchen, Lovedean, Soberton and Fishbourne. The last three works accounted for approximately 4% of supplies in 2013/14. Water from the remaining sources requires less sophisticated treatment.



Flooding at Westergate Pumping Station caused by one of the wettest winters on record in 2014

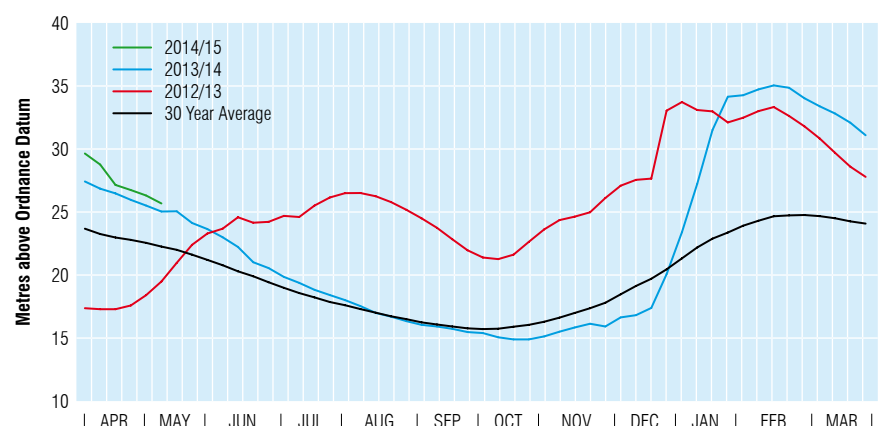
Water Resources - Outlook for 2014

As detailed above, 90% of water supplied to customers is from groundwater springs, boreholes and wells which abstract from the underground chalk of the South Downs. Groundwater levels are therefore critical to maintaining supplies to customers. The Company has for many years monitored the groundwater level at Idsworth Well, Rowlands Castle, which is unaffected by abstraction and is representative of groundwater conditions in the South Downs chalk.

Following a much drier and warmer summer in 2013 than that experienced in the previous year the winter of 2013/14 turned out to be the one of the wettest ever recorded across the Company's region. This produced near record levels of groundwater for the time of year although these have now receded back to more normal levels. The Company has not had to impose restrictions on our customers since 1976 and, as a result of the current groundwater level, it is unlikely to do so this year.

At the end of April 2014, groundwater levels were above the long term average as outlined on the graph below, which includes the thirty year long term average.

Idsworth Well



STRATEGIC REPORT

Water Resources



The River Meon at Morestead

Long Term Resource Planning

In May 2013 the Company published its latest Water Resource Management Plan 2014 (WRMP) for consultation. The WRMP examines the factors which will impact upon the demand for water from its customers such as population change and climate change and identifies whether the Company will have sufficient water resources over the next 25 years to meet this demand.

In its plan the Company is projecting a water resource surplus in the period to 2040. As a result, the Company does not need to invest in new water resources to meet the needs of its own customers during this period. However, the Company has been approached by two neighbouring water companies to provide bulk supplies of water to meet the needs of their customers and these have been included in the Plan.

The Water Resources in the South East (WRSE) group, comprising seven water companies in South East England and led by the Environment Agency, has been investigating the potential for regional solutions to meeting the water needs of South East England. This may require further schemes to be commissioned in the Portsmouth Water area in order to provide water to other communities in the South East.

The Company published its Statement of Response in November 2013 which set out how the Company had responded to the representations received and the changes made to the Draft Water Resources Management Plan as a result. A revised draft Final Water Resources Management Plan was therefore published in November 2013. Defra wrote to the Company in March 2014 requesting further information in support of the Company's Statement of Response. Following the submission of this further information to Defra, the Secretary of State will now consider if Portsmouth Water should be instructed to publish its Plan. We await this decision which we expect to receive in the very near future.

STRATEGIC REPORT

Financial Performance



Scrub clearance at Lavant

The results for 2013/14 reflect the 2009 Price Determination, made by Ofwat which included a real reduction in charges for customers in the year of 1.4% and the increased costs connected with the leakage recovery programme and the submission of the Business Plan to Ofwat. Turnover for the year increased by 2% to £37.1m. The increase in turnover is largely due to income from measured supplies which was £1.0m higher than the previous year. This was due to higher water volumes sold to commercial customers with summer demand being much higher than the previous year, most likely the result of it being a much drier summer in 2013 compared to the previous year. There was also an increase in volumes sold to household customers due to the effect of the increasing customer base as a result of the continued switch from unmeasured charging. However this was partially offset by unmeasured supplies being £0.3m lower than the previous year as a result of a declining customer base as previously unmeasured customers have switched to a measured supply. A small amount of additional income (£0.1m) was earned by the Company through providing additional bulk supplies to Southern Water. The headline results are shown in the table below:

	2013/14 £m	2012/13 £m
Turnover	37.1	36.3
Operating costs excluding depreciation charge	22.3	21.1
Operating profit before depreciation charge	14.8	15.2
Depreciation (including renewals)	8.9	8.9
Total Operating Profit	5.9	6.3

Operating costs, excluding depreciation, increased by £1.2m in the year mainly due to the additional costs connected with the leakage recovery programme (£0.5m) and costs incurred in submitting the Company's Business Plan to Ofwat for the period 2015 – 2020 (£0.3m). Electricity costs were £0.2m higher than the previous year due to additional pumping requirements. However business rates were £0.2m lower due to the Company's transition to a lower rates cost by 2015. As a result of the above factors the operating profit was reduced to £5.9m (2013 - £6.3m).

There was an exceptional non cash charge during the year of £0.6m. This relates to the Havant Thicket Winter Storage Reservoir. In the Company's previous Water Resource Management Plan (WRMP) we were planning to build the reservoir by 2033. However, in our most recent WRMP, which has been developed over the last year, the Company has a water surplus until 2040 and no requirement therefore to build the reservoir unless more significant bulk supplies are required from our neighbouring water companies. Under the work done by Water Resources in the South East (WRSE) we are anticipating making further bulk supplies to these companies but not at a volume sufficient to require the building of Havant Thicket. We have, therefore, decided to write off the remaining expenditure on this from the balance sheet.

Interest receivable at £0.96m (2013 - £1.26m) relates mainly to interest received from another Group company and is based on Libor plus 1%. Other finance income has reduced by £0.3m to £1.64m as a result of a decrease in the expected return on assets in the pension scheme.

Interest payable at £6.5m (2013 - £6.5m) includes £2.9m for indexation of the loan provided by Artesian Finance plc (2013 - £2.8m). The indexation of the loan for 2014 was based on RPI for July 2013 of 3.1%, whereas, RPI for July 2012 was 3.2%. Interest on the capital sum amounted to £3.4m (2013 - £3.4m).

As a result of the above, the profit before tax decreased to £1.3m (2013 - £3.1m).

Taxation

The taxation credit of £2.3m was £1.8m higher than the previous year. The current tax credit for the year was £0.005m (2013 – charge of £0.4m). This was the result of lower taxable profits and higher reliefs, in particular capital allowances claims. The deferred tax credit in the year amounted to £2.3m (2013 – credit of £0.9m). This arose from the Government's proposed reductions to corporate tax rates to 20% from 2015 onwards. This has meant that a large credit has resulted from the recalculation of the deferred tax balances on both the capital allowance pools and the pension asset.

STRATEGIC REPORT

Financial Performance

Dividends

The dividends paid during the year amounted to £1.107m (2013 - £1.449m). Dividends are paid up to the parent company, part of which are ultimately paid to shareholders with the remainder used to service interest payments on an inter-company loan.

The breakdown of the dividend in the year is as follows:

Dividend to the shareholders - £0.367m

Inter company dividend - £0.740m

Cash Flow and Balance Sheet

Net cash inflow from operating activities of £15.1m was lower than the previous year (2013 - £15.7m) reflecting the impact of the lower operating profit and movements in working capital.

At the year end, no new borrowings had been drawn down and £0.1m of the inter company loan with South Downs Limited had been paid back. The expenditure on tangible fixed assets was less than the previous year at £11.7m (2013 - £15.3m). The cash expenditure (after contributions) was £10.6m in the year (2013 - £14.3m).

Net debt (excluding deferred arrangement costs) at £96.0m (2013 - £93.6m) includes an index linked loan with a value of £95.3m (2013 - £92.4m). The value is indexed each year by the previous July's recorded RPI. The increase in debt for the year is a result of this indexation. The level of gearing is an important ratio in the Company's loan covenants and is measured by the ratio of net debt to the Company's Regulatory Capital Value (RCV) which was determined by Ofwat at the 2009 Price Determination. The RCV is also indexed by RPI but at the March (year end) figure. The ratio is known as the Regulatory Asset Ratio (RAR). At the year end, the ratio was 81.4% (2013 - 77.9%). However the Regulatory Asset Ratio will reduce significantly at the beginning of the next review period (starting in 2015) as a result of the "Midnight Adjustment". The Midnight Adjustment allows the Company's RCV to be amended to reflect actual expenditure in 2009/10 which was higher than allowed in the Determination. The Midnight Adjustment has been calculated in accordance with Ofwat's methodology and the resulting adjustment to the Company's RCV for PR14 is plus £5.6m. This adjustment contributes to the fact that the RAR is forecast to fall below 75% in 2015.

Capital Investment

Gross capital investment during the year was £10.7m (2013 - £15.4m) and included £5.4m (2013 - £5.2m) on infrastructure renewals. After receiving capital contributions and infrastructure charges of £1.1m, net capital expenditure was £9.6m (2013 - £14.5m).

During the year the Company renewed 24.7km of mains at a cost of £5.4m. The out turn rates for mains renewals have improved from £260/metre during 2012/13 to £214/metre for 2013/14. This improvement is in part due to the use of prechlorinated pipe which has reduced installation time and an increase in the use of no dig techniques. We renewed 26.2% of the mains using no dig techniques.

Gross expenditure on above ground assets at £4.2m included £0.4m on the construction of roofs over the Highwood raw water reservoir to reduce the risk of Trihalomethanes and over the clarifiers at the River Itchen and Farlington treatment works in order to provide security for the open water at these sites. These schemes which were a major part of the AMP 5 programme have now been completed at a total cost of £6.2m. There was also expenditure of £0.3m connected with leakage improvements and £0.3m on refurbishment of pumps and motors at Havant pumping station. A further £1.0m resulted from investment in small plant, vehicles and office equipment, including £0.4m for payments made in respect of the implementation of a new Work and Asset Management system. In the Final Determination the Company was given an allowance of 5,000 domestic meter options per year, and in 2013/14, 4,873 customers chose to switch to a measured supply. This resulted in a further £1.5m of capital expenditure. At March 2014, meter penetration for the Company was 23% of household customers.

Comparison with the Final Determination in 2009

In the four years to date of this review period the turnover is £10.7m below that allowed in the Determination, indexed by RPI. The Company has largely offset this by lower taxation, savings in operating costs and lower dividends than assumed in the Determination.



Many of the Company's domestic customers have chosen to switch to a measured supply over the last few years. There were over 70,000 measured household customers at the year end.

STRATEGIC REPORT

Financial Performance



New pumps at Havant Pumping Station

In addition over the same period the Company has invested in I.T. infrastructure which was not allowed for in the Determination. This is to ensure that services to customers are maintained at a high level in the future.

Accounting Policies

The accounts have been prepared in accordance with the accounting policies described in note 1 to the accounts on pages 40 to 42 and with UK GAAP.

Under its licence of appointment, Portsmouth Water Limited, a private company, is required to publish information about its annual results as if it were a company covered by the Listing Rules of the Financial Conduct Authority. From April 2005, listed groups were required to prepare accounts in accordance with International Financial Reporting Standards (IFRS). It is the Company's view that these standards are not appropriate for a regulated water business and it has been granted exemption, by Ofwat, such that it need only adopt IFRS when non-listed companies are required by statute to do so. The Company has now decided to adopt FRS102 as its reporting basis going forward and the year 2015/16 will be the first year of reporting under this new standard.

Pensions

The Company takes account of the Brockhampton Pension Scheme, in which it is the principal employer, under the principles of FRS17. The latest actuarial valuation carried out for the purposes of FRS17 as at 31 March 2014 showed a surplus after deferred tax of £16.1m (2013 - £15.3m). The actuarial loss in the year before deferred tax of £0.9m (£2013 - £1.2m), which is shown in the Statement of Total Recognised Gains and Losses (STRGL) on page 37, results mostly from lower than expected returns on scheme assets over the year.

In the most recent triennial actuarial valuation conducted at March 2013, the Scheme had a surplus of £20.1m. Until March 2010, the Company had not made contributions for a number of years. For the year ended 31 March 2014, the Company made contributions of £0.7m, these being at a rate of 12.4% of earnings.

Going Concern

Pages 10 to 12 and page 19 of this Report along with note 18 to the accounts sets out the Company's financial position; cash flows; liquidity position; borrowing facilities; objectives, policies and processes for managing capital; financial risk management objectives; exposures to credit and liquidity risk.

As highlighted on page 6 the Company meets its day-to-day working capital requirements through a £10m working capital facility that was arranged in 2012, and terminates in September 2015. The Company will be looking to renew this facility in the coming year.

The Company is also intending to move its banking facilities in the coming year and it is currently in discussion with a number of banks in order to facilitate this.

The Company's financial projections, taking into account expected changes in trading performance show that the Company is forecast to operate within the level of its current facility.

Therefore the Directors report that, following the above review, they have a reasonable expectation that the Company has adequate resources to continue in operation for the foreseeable future. Accordingly they continue to adopt the going concern basis of accounting in preparing the accounts.

STRATEGIC REPORT

Current Performance

Gearing (net debt/regulatory capital value) and cash interest cover are recognised as key indicators for the Company. Performance in 2013/14 against the target ratios is shown in the table below.

KPI - ¹	Performance 2013/14	Performance 2012/13
Gearing - Debt/RCV ²	81.4%	77.9%
Cash interest cover ²	1.58	1.80
Return on regulatory equity ²	5.8%	5.2%

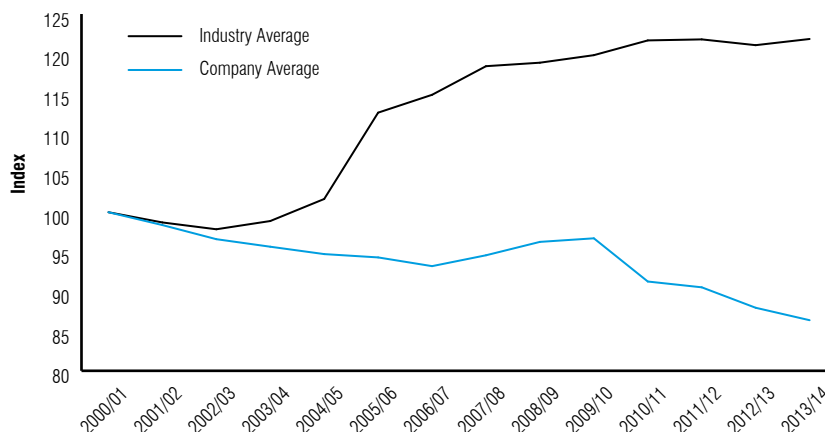
¹ Each KPI is defined in the Appendix on page 54

² Definition of terms is contained in the Appendix on page 54

Water Charges

Portsmouth Water’s charges are the lowest in England and Wales, the average annual bill for water being £94 per household, the equivalent of 26p per day. In real terms, the price of water for household customers has fallen by 13.6% over the last 13 years. This compares with a real increase of 22% for the industry as a whole, as illustrated in the chart below, where the 2000/01 prices are indexed at 100:

Comparison of Average Household Bills with Average Industry Tariffs



The Company is proud of its high levels of customer service

Customer Service

In October 2012 the Company successfully implemented a new billing and customer relationship management system (CRM). During 2013/14 the Company has started to see the benefits of its new CRM system. For 2013/14 the Company was ranked 7th out of 21 companies in a survey of customers conducted by Ofwat to assess how well the Company handled all types of contact. The Company was ranked 3rd overall (and 1st among water only companies) in terms of its Billing score. In addition the Company still achieved the lowest level of complaints in the industry.

Ofwat are now using the Service incentive Mechanism (SIM) to measure the performance of companies in relation to customer service. This places greater emphasis on the quality of service received rather than the speed of response. Part of this is a qualitative assessment survey and the results of this are shown below.

STRATEGIC REPORT

Current Performance



Relining of the well at Eastergate Pumping Station

KPI - 2 Customer Service Measures

	Target	Performance 2013/14	Performance 2012/13
Number of properties at risk of inadequate pressure	≤120	69	66
Properties affected by unplanned interruptions to supply >12 hours	Nil	Nil	Nil
Population subject to hosepipe bans	Nil	Nil	Nil
Written complaints - answered within 10 days*	100%	99.58%	99.96%
Bills for metered customers - number receiving bill based on meter reading	100%	99.99%	100%
Telephone contact - number of calls abandoned - unwanted calls**	≤2.5%	5.77% 26,227	7.21% 75,818
Service Incentive Mechanism - qualitative survey element - position relates to 21 companies	<6th	7th	5th
Number of written complaints per 10,000 connections***	<10	7.6	10.5

* The Company had 236 written complaints. This equates to 7.6 complaints per 10,000 connections, compared with the industry average of 49. Only one written complaint was not answered within 10 days.

** The unwanted call performance reflects significant improvement in our ability to robustly classify calls as either wanted or unwanted. This is as a result of a customer relationship management system which went live in late 2012.

*** For 2012/13, the Industry average was 49 complaints per 10,000 connections.

KPI - 3 Water Quality

The Company carries out an exhaustive programme of testing to ensure that water of the highest quality is supplied to customers. The table below shows the percentage number of samples which pass the strict standards set out in the Water Supply (Water Quality) Regulations.

Water Quality	Target	Performance 2013	Performance 2012
Compliance samples passing standards (mean zonal compliance)	99.96%	99.97%	99.96%

The water quality performance indicator relates to the calendar year.

Operating Efficiency

For many years Ofwat have published a report which included its assessment of the comparative operating efficiency of all water companies in England and Wales using econometric modelling. Portsmouth Water has always been ranked in Band A (mostly the highest or 2nd highest performing company). This benefited customers through relatively lower prices. Ofwat do not intend to publish this assessment in future, however they did use this relative performance to set efficiency targets for the 5 year period to 2015. As a result, Ofwat set an efficiency target of 0.25% per annum. The table below shows the outcome against this target.

KPI - 4 Efficiency

Target	Performance 2013/14
To achieve the Ofwat efficiency target of 0.25% per annum	5.19%

STRATEGIC REPORT

Current Performance



Early purple orchid at Shedfield Service Reservoir site

Leakage

As reported in last year’s report the Company had carried out a full, independent review of its leakage calculation and methodology. The review had confirmed that there was an error in the leakage calculation (although not in the methodology) used for a number of years. By not adapting the leakage calculation to take into account operational changes that had been made in day and night time water pressures, we determined that our leakage level was higher than we had been reporting by approximately 6.6 MI per day for 2011/12. The leakage target, therefore, was missed as a result of a calculation error, rather than as a result of a failure to undertake leakage prevention activity. This was reported immediately to Ofwat and the Company immediately put in place a programme to reduce leakage which began in November 2012.

The leakage recovery programme is ahead of schedule and leakage for the full year 2013/14 was recorded at an average of 29.5 MI/d (2012/13 - 34 MI/d), which is at the target level agreed with Ofwat at the Final Determination in 2009. The Company had set itself an internal target of 32 MI/d for 2013/14 as part of its leakage recovery programme and so the actual reported for the year is well ahead of target. The Company continues to work hard to ensure its leakage targets are achieved, and will continue to improve its data and review its leakage methodology against best practice.

The cost of the recovery programme is being met by the shareholders and not by our customers. The cost during 2013/14 amounted to £0.5m. of operating cost and £0.3m. of capital expenditure. Despite the expenditure the Company will remain comfortably within its covenants for interest cover and gearing.

Portsmouth Water is committed to reducing leakage and, in addition to the work outlined above, invests £5m annually on renewing our pipe network. Over the past ten years Portsmouth Water has reduced the number of burst mains from 900 to 226 in 2013/14.

KPI - 5 Leakage

Target	Performance 2013/14
Average leakage of less than 30 MI/d	Average leakage of 29.5 MI/d

STRATEGIC REPORT

Human Resources



Construction of artificial badger sett at one of the Company's operational sites

The Company employs 244 people and believes it recruits and retains the right people key to the successful performance of the business.

Gender Diversity

The Company is committed to the principle of gender equality on all employment issues such as recruitment, retention, promotion and pay. The Company has recently signed up to the Government's initiative called "Think Act Report" which aims to promote equality for women in the workplace. The numbers of male and female employees as at the end of the financial year are shown in the table below.

	2014 Male	2014 Female	2013 Male	2013 Female
Directors	5	1	5	1
Senior Managers	11	-	11	1
Other Employees	154	73	152	69
Total	170	74	169	70

Ethics Policy

The Company operates a Business Ethics and Anti Bribery Policy which provides a set of principles upon which the Company conducts its business defining what is, and what is not acceptable practice. The Company will endeavour to ensure that a high standard of ethical behaviour is maintained by its employees and that our business, in all operations, allow the rights, freedom and dignity of individuals to be recognised and upheld.

We recognise the UN Universal Declaration of Human Rights and note that the Charter sets out obligations to promote respect and observe human rights and fundamental freedoms for all, without distinction as to race, gender, language or religion.

Disability

The Company has adopted a policy which complies with the Disability Discrimination Act 1995. Every consideration is given to applications for employment from disabled persons, where the job requirements may be adequately covered by a person with a disability. Employees who become disabled during employment are given continued employment where possible and opportunities for training and career development are provided for all disabled employees.

Life Assurance and Pensions

All Company employees are provided with life assurance cover and are entitled to join a Company pension scheme.

Employee Development

The Company is firmly committed to the development of its employees and that they should all have opportunities to reach their full potential and, as a result, a number during the year have undertaken Degrees, HNC's, NVQ's along with associated professional qualifications.

In line with this objective the Company fully supports the principle of Modern Apprenticeships; for example, all new employees within the Customer Services department aged under 25 are employed through the Modern Apprenticeship scheme which leads to a minimum NVQ level 2 qualification with many going on to achieve level 3.

A key part of staff development is the Company involvement with the Institute of Water. The Institute of Water is a professional body whose purpose is to promote the advancement of knowledge within the water industry. To this end, Area and National Committees organise meetings, seminars, technical visits and conferences, as well as a variety of social events. These activities provide a shop window for the latest technological developments in the industry and a forum for the discussion of major topics. The Company encourages its staff to belong to the IoW and gain the benefit for both their personal and professional development by attending these events.

STRATEGIC REPORT

Human Resources

Absence

Total absence for 2013/14 (days per employee per year) was 5.1 (2013 – 5.5). This figure still compares favourably with the average for private sector employers, which stands at 7.6 (Source: CIPD: Absence Survey Report 2013).

Total Accidents and Reportable Accidents



Health and Safety

Health and safety is considered fundamental to the success of the business and the Company is committed to achieving high standards across the organisation. The Company has put health and safety at the top of the agenda and from the Board down has made it a high priority.

Considerable time and resources have continued to be directed into raising the awareness of Health and Safety and the statistical results for the year 2013 show very positive results from these efforts, with only one reportable accident (accident causing more than three days' absence) being recorded.

RoSPA Health and Safety Awards

It is pleasing to report that our efforts have again been recognised externally through the RoSPA Health and Safety Awards, by the Company being awarded the Gold Medal. This is in recognition of our Health and Safety record over the last nine years where we have received eight Gold awards and an Industry sector award. This award is again recognition of the efforts of all employees who should feel proud of their achievements in making the Company a safer place.

STRATEGIC REPORT

Corporate Responsibility

Water Efficiency

In 2010 Ofwat set the Company an annual target of achieving water savings, through water efficiency, of 0.29 mega litres per day (ML/d). This equated to an overall five year target of 1.45 ML/d.

Pleasingly this year the Company has again exceeded the target by achieving overall savings of 0.32 ML/d. In the four years of the current regulation period the Company has achieved a cumulative surplus of 0.12 ML/d against the Ofwat target.

This excellent result was achieved by initiatives such as supplying free water saving packs and subsidised water efficient devices such as shower heads to customers. This was in conjunction with a number of proactive water saving campaigns in the local media such as the "Water Saving Challenge" which is designed to encourage customers to change their behaviour when it comes to water use. The Water Saving Challenge has seen customers save over 1.3 million litres of water every day.

Catchment Management

Portsmouth Water have established 'The Downs and Harbours Clean Water Partnership' with Natural England and the Environment Agency. The partnership's objective is to protect and improve drinking water quality and both river and coastal water quality.

A key issue for the Partnership is to try and ensure that there is no deterioration in the quality of our drinking water supplies which are taken from underground aquifers. This is achieved by advising land owners and farmers on the best practice for use of fertilisers and overall land management. If successful this will prevent us in the future having to use expensive treatment processes to remove chemicals such as nitrate (found in fertilisers) from drinking water.

Work in the community

2013/14 has seen the Company continue to play a valuable role in supporting the local community such as supporting the Hampshire Water Festival held in Havant and the continued sponsorship of the Portsmouth in Bloom competition.

As part of our 'Water for Health' initiative, which promotes the benefits to children of drinking water, we again made available drinking water bottles at the subsidised cost of 30p per bottle to every child in a local primary, infant and junior school. This initiative remains very popular with 30,000 bottles delivered last year and which has seen nearly 380,000 water bottles delivered to local school children over a number of years.

The Company continues to offer community talks to local schools, colleges, clubs and groups such as Age Concern, Rotary and the Women's Institute as well as supporting local schools in activities such as Science Days.

WaterAid

The Company continues to support and promote the charity WaterAid to customers and staff. Over the last 30 years donations from our customers, together with fundraising efforts of our employees have raised a staggering £460,000 for WaterAid. It is estimated the average cost is only £15 per person for supplying a safe water supply to a village, combined with sanitation and hygiene education for life.

Environmental Performance

The Company recognises its impact on the environment and seeks to carry out its activities in a sustainable manner, which is highlighted by the initiatives shown below.

Conservation

The Company's total licensed area of supply covers an attractive part of Southern England between the South Downs and the coastal areas of Hampshire and West Sussex. It includes the historic cities of Portsmouth and Chichester, and the popular holiday resorts of Bognor Regis, Selsey and Hayling Island. The harbours of Portsmouth, Langstone, Chichester and Pagham have a number of important environmental designations under the EU Habitats Directive and are popular water activity venues.

Following the implementation of abstraction licence reductions at Havant and Bedhampton Springs and several sources in Sussex in order to protect habitats, the Company has also included in its Business Plan two schemes associated with the Water Framework Directive. These schemes will provide benefits to both the River Hamble and River Ems.

Biodiversity Action Plan

The Company's policy is to conserve and enhance the natural environment of its land and to preserve historic buildings and equipment, so far as is consistent with the primary duty of providing a sufficient supply of wholesome water at reasonable cost. In our latest Business Plan, submitted to Ofwat in December 2013, the Company is proposing to increase threefold the funds it spends on Biodiversity.

Sustainable Procurement

In procuring goods and services, the Company has a policy which seeks to ensure that its impact on the environment is minimised. This includes the use of low sulphur content diesel fuel, timber from replanted forests and predominantly recycled material for reinstatement.

STRATEGIC REPORT

Risks and Uncertainties

Risk Management

The Company identifies risks under ten main headings - Operational, Water Quality, Financial, Environmental, Regulatory, Information Technology, Human Resources, Legal (including whistleblowing and fraud), Business Continuity and Health and Safety of Employees. Individual risks facing the Company are identified and recorded in a risk register. For each risk the consequences, impact and likelihood of failure are identified, together with the management controls in place. The register also clearly allocates management responsibility and whether any further actions are required to control the risks.

The Board reviews the risk register and the controls established to mitigate these risks on an annual basis. It also receives regular reports on operational matters, including a monthly review of water quality matters directly with the Water Quality Manager and a quarterly review of health and safety matters with the HR Manager. The Directors also receive reports from independent regulatory bodies, which comment on the performance of the core water business.

During the year, the Board has reviewed its tolerance for risk in addition to assessing risk identification and mitigation techniques as they continue with a programme, the objective of which is to ensure risk management is embedded in the business.

The Audit Committee meets at least three times a year, monitors the effectiveness of the systems which are in place and reports to the Board as a whole.

Operational Risk

The key operational risks facing the Company are the loss of a treatment works or part of the mains network, which would result in a failure to supply water to customers. To mitigate this risk, the supply network has been enhanced over several years to connect different supply areas, such that in most situations water can be transferred to compensate for a failure at a treatment works. The Company also has a fully documented Emergency Plan which is initiated in the event of an incident, impacting either its ability to supply water to the public or resulting in a water quality issue.

Water Quality Risk

To ensure water quality standards are maintained, the Company has a fully documented Drinking Water Safety Plan which identifies the potential risks throughout the supply process. Water quality is also monitored by a comprehensive sampling regime in accordance with statutory legislation. Furthermore, a telemetry system linked to all treatment works provides an alarm to our 24 hour Operations Centre if there is a failure of equipment. The Company also maintains two days storage of treated water in service reservoirs to provide sufficient time for any water quality issues at treatment works to be rectified before supply to customers. In addition, it has membrane filtration at five treatment works considered most at risk from cryptosporidium being present in the raw water. The Business Plan for the period 2015 – 2020 includes a plan to build two ultra violet (UV) treatment plants at two of our sites which face an increasing risk of cryptosporidium being present in the raw water.

Financial Risk

Interest Rate, Liquidity, Capital and Credit Risk

The major financial risks faced by the Company are interest rate, liquidity, capital and credit risks. The Company assesses these risks on an ongoing basis and its policies for managing them remain unchanged from previous periods.

The Company's exposure to interest rate fluctuations is now limited by the fixed interest rate applicable to the index-linked loan drawn in 2002, with inflation risks on the cost of the loan being effectively hedged against regulated revenues which are also linked to the RPI. Interest is charged at a fixed rate of 3.635% on the indexed amount of the loan. The indexed value of the loan at 31 March 2014 was £95.3 (2013 - £92.4m).

The Company seeks to manage financial risk, to ensure sufficient liquidity is available to meet foreseeable needs through an appropriate borrowing structure and to invest cash assets safely and profitably on the short term market. In 2013/14 all of the short term cash was deposited with the Company's Bankers, RBS. Short term liquidity is achieved through a £10m working capital facility and an overdraft arrangement. At the end of the year, £5.0m of this facility had been drawn (2013 - £5.0m), while the overdraft arrangement remained unutilised. The £10m facility was rearranged in 2012 and terminates in September 2015. The Company will be seeking to refinance this loan during the coming year. It should also be noted that the Company will be looking to move its day to day banking facilities to another bank, during the coming year.

The Company's objectives when managing capital are to safeguard the entity's ability to continue as a going concern, so it can provide returns for shareholders and benefit to customers.

The Company's exposure to credit risk results from the continuing impact of bad debt on its ability to collect water revenues. It seeks to minimise this risk by utilising all available means, including the use of a dedicated debt recovery section, agencies for collecting outstanding debt and the following of best practice guidelines.

Financial Loss

The risk of financial loss is addressed through comprehensive insurance cover for a range of risks, including damage to property, public and employee liability, fraud and terrorism. A system of internal controls is in place to manage the risks, the details of which are included in the Statement on Corporate Governance on pages 26 to 28. In early 2007, the Auditors conducted a special review of the Company's internal control systems. The review did not reveal any significant weaknesses and it has recently been updated to reflect system changes. Following the implementation of the Company's new billing system last year, the Auditors undertook a specific review of the new system. This review did not reveal any material weaknesses. A disaster recovery plan is also in place to enable the Company to operate in the event of an incident disrupting its computer systems. At a remote site ten miles from its Head Office, the Company has an additional mainframe computer, which is 'backed up' every evening, and several workstations for employees to operate.

Energy now represents around 9% of total operating costs and fluctuating prices can have a material impact on profitability. In order to provide mitigation against the impact of price movements we fixed the wholesale price of energy in October 2011 until December 2014 at a price considerably lower than we paid in 2010/11. The Company has now signed a contract with a firm of energy brokers who will look to negotiate and manage a new supply contract, which is currently at the tendering stage. A flexible type has been selected in order to take advantage of market pricing and to mitigate against the risk premiums inherent in a fixed type of contract.

STRATEGIC REPORT

Risks and Uncertainties

Environmental Risk

The major environmental risk faced by the Company at the present time is a potential loss of abstraction licence resulting from measures that may be required by the EA to allow the UK to comply with the Water Framework Directive. The Company has carried out studies in order to identify the impacts of its abstraction at certain sites and solutions have been identified.

The flooding in various parts of the UK in 2012 and 2014 has prompted several national reports. Whilst the Company was not affected in those years, it has conducted an assessment of the risks at each of its sites and included a small amount of expenditure which was allowed in the Final Determination of prices to remedy those sites where there is a risk of damage as a result of flooding.

Regulatory Risk

Regulatory risk relates to decisions taken by Ofwat at the five yearly price review and the potential failure to meet the level of service and capital programme agreed with Ofwat for the AMP 5 period, which could result in Ofwat taking action, including financial penalties. The price review is conducted in an open and transparent manner and the Company actively participates in the process. The performance against the regulatory targets is reviewed on a monthly basis by the Board or the Executive Directors. The annual performance against the targets is discussed on pages 14 to 15.

The Company is currently well progressed in agreeing its Business Plan for the next price review period (2015 – 2020). The Company submitted its Plan to Ofwat in December 2013. Although the Company did not achieve “enhanced” status (as only two companies in the industry did) our Plan was considered by the Ofwat team to be “marginal” i.e. having almost achieving enhanced status; the only Company in the industry to be considered in this way. The Company regards the submission of its Business Plan as a real success, not only because of this but also the fact that Ofwat has accepted our proposed investment plans. There are no material financial penalties for the Company relating to AMP 5, identified by Ofwat as part of this process.

Competition in the Water Industry

In 2011, the UK Government published the Water White Paper ‘Water for Life’, which set out its plans to:

- increase choice and improve service for water customers.
- stimulate innovation and drive more sustainable approaches to managing our water resources.

The Water Bill 2014, which received Royal Assent in May 2014, includes the legislative changes required to deliver these ambitions for the water sector. The Bill will enable the creation of a new market for retail water and sewerage services to non-domestic customers in England. The intention is to open the new retail market in April 2017.

The Company will ensure that it is compliant in time for market opening in October 2016. This includes compliance in terms of:

- Systems and how these systems interface with the Market Operator
- Structure and processes – the business will need to have a structure and processes which allow the retail and wholesale functions to operate separately and on an “arms length” basis, both internally and with other external companies / retailers.

The Company is currently working to ensure that it meets the necessary compliance requirements in good time. The Company is also assessing what its strategy should be in the new retail market and how best to serve its customers under the new regime.

Information Technology Risk

The Company’s computer systems are crucial to the smooth running of the business. Should these systems fail it could have important implications for the business. Therefore the Company seeks to minimise these risks by having a Disaster Recovery (DR) programme in place to enable us to continue working should the systems fail, ensuring all software and hardware is compliant and supported by the manufacturer and that a succession plan is in place for key staff. It is also crucial to manage any change in the business by assessing the IT implications of any such change.

Human Resources Risk

The Company could face risks from a Human Resource perspective. This could be the result of losing key staff for long or short term periods, industrial unrest or breaches of employment or other staff related legislation. The Company mitigates against these risks through its programme of employee development, cross training, succession reviews, working and consulting with the unions and having control procedures and policies in place to ensure that all legislation is complied with.

Governance/Legal Risk

The Company considers that the main legal risks that would be likely to arise would be if it failed to fulfil its responsibilities regarding its licence conditions, legal responsibilities, data protection requirements or failure to demonstrate an appropriate level of governance. The consequence could be prosecution, fines, compensation claims or bad publicity and loss of reputation. The Company mitigates against these risks by continually reviewing and updating policies and procedures, including governance procedures and regularly reviewing the performance of the Company’s Reporter and Auditors.

Business Continuity Risk

The risks to business continuity relate primarily to the loss of computer systems (as covered under Information Technology risks above) or water supplies. To mitigate the risk of losing water supplies the Company has a defined Emergency Plan in place which utilises Drinking Water Safety Plan (DWSP) risk assessments.

Health and Safety

The health and safety of employees is taken very seriously and a number of initiatives have been introduced over several years to reduce the number of accidents and the impact of injury. These include:

- A Health and Safety Committee comprising Management and the Trade Unions
- A risk assessment programme that has seen over 500 assessments produced, including guidance on lone working
- A system of workplace inspection ensuring that all manned premises are inspected at least twice per year
- Specific training for those at high risk of injury
- A limited free physiotherapy service for employees to deal with injuries

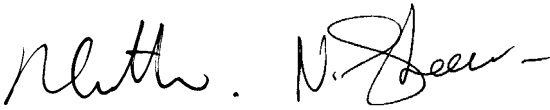
STRATEGIC REPORT

Responsibility Statement

We confirm that to the best of our knowledge:

- the accounts, prepared in accordance with the applicable set of accounting standards give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company; and
- the report and accounts, taken as a whole, provides the information necessary to assess the Company's performance, business model and strategy and is fair, balanced and understandable; and
- the Strategic Report includes a fair review of the development and performance of the business, together with a description of the principal risks and uncertainties.

For and on behalf of the Board



N. Smith
Managing Director

N. J. Sheeran
Finance and Regulation Director

30 May 2014

COMPANY INFORMATION

Registered Office

PO Box 8
West Street
Havant
Hampshire
PO9 1LG

Telephone: 023 9249 9888
Facsimile: 023 9245 3632
Website: www.portsmouthwater.co.uk

Company Number: 2536455
Company Secretary: Christopher Hardyman ACIS

Facts and Figures

Area of Supply	868 km ²
Population	707,000
Number of Properties Served	310,000
Length of Mains	3,293 km
Average Daily Output	172 MI

Auditors

Saffery Champness
Lion House
Red Lion Street
London WC1R 4GB

Bankers

National Westminster Bank plc
PO Box 34
15 Bishopsgate
London EC2P 2AP

Insurance Brokers

Willis UK
International House
Southampton International Business Park
George Curl Way
Southampton SO18 2RZ

AREA OF SUPPLY



Portsmouth Water has been supplying water to Portsmouth and the surrounding area since 1857. The area supplied by the Company extends through South East Hampshire and West Sussex from the River Meon in the West to the River Arun in the East encompassing 868 square kilometres.

The Company provides high quality public water supplies to a domestic population of 693,000, as well as many important industries, large defence establishments and varied commercial businesses.

DIRECTORS' REPORT

The Directors have pleasure in presenting their Report and Accounts for the year ended 31 March 2014.

Principal Activity and Business Review

The principal activity of the Company and a detailed review of its operations, strategy and business model is provided in the Chairman's Statement on pages 4 to 5 and the Strategic Report on pages 6 to 21.

The Company's Area of Supply is shown on page 23 of this report.

Financial Risk Management Objectives and Policies

A detailed review of the Company's financial risk management objectives and the policies employed are set out in the Strategic Report on page 19 and in note 18 to the accounts on page 48.

Financial Results and Dividends

The Company's profit before taxation amounts to £1.329m (2013 - £3.117m). After adding the tax benefit of £2.331m which mainly arises from reductions to tax rates (2013 - tax benefit of £0.527m), a profit of £3.660m has been transferred to reserves (2013 - £3.644m).

The Directors are recommending the payment of a final dividend of £0.195m.

Fixed Assets

Capital expenditure on tangible fixed assets was £10.667m (2013 - £15.357m), including £5.415m on infrastructure renewals (2013 - £5.202m). Information relating to these and other changes in fixed assets is shown in note 10 to the accounts on page 45.

The Directors are of the opinion that the current market value of the land and buildings included in tangible fixed assets is in excess of the value shown in the balance sheet.

As they are held for operational purposes, no professional valuation has been obtained and the excess has not, therefore, been quantified.

Board of Directors

The Directors who held office at 30 May 2014 are shown on page 3.

Mr. N. Smith and Mr. R. C. Porteous who retire by rotation, offer themselves for re-election.

The interests of the Directors in Group shares are detailed in the Report on Remuneration on page 32.

The Company maintains appropriate Directors' indemnity insurance.

Substantial Shareholder

At 31 March 2014, Portsmouth Water Holdings Limited owned the entire voting capital of the Company.

Regulatory Accounts

A set of accounts for regulatory purposes is required by the Water Services Regulation Authority. These accounts relate solely to the regulated water supply business and copies may be obtained on request from the Registered Office.

Employees

Direct communication with employees is maintained through the Company in-house newsletter. In addition, the Joint Information

and Consultative Committee met regularly and ensured effective communication with employee representatives.

The Directors consider health and safety to be an important issue within the Company, with the active participation of employee safety representatives taking place through the Health and Safety Committee. During the year, a number of initiatives were undertaken, which ensured that health and safety continues to maintain its high profile throughout the organisation.

The Company has, for the last nine years, been awarded eight Gold Awards in the RoSPA Occupational Health and Safety Awards and was also awarded an Industry Sector Award in 2009.

Environment

The Company is aware of its obligations to both customers and the environment. In recent years, it has adopted an active approach to environmental issues and further information is set out in the Strategic Report on page 18. The total amount of Greenhouse Gas Emissions that resulted from the Company's operations in the financial year was 10,018 tonnes of carbon.

Licence Requirement

In accordance with its Instrument of Appointment under the Water Industry Act 1991, the Directors are of the opinion that the Company is in compliance with paragraph 3.1 of Condition 'K' of that Instrument.

Auditors

The Auditors, Saffery Champness, have expressed their willingness to continue in office and a resolution providing for their reappointment will be proposed at the Annual General Meeting.

In so far as the Directors are aware:

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

Statement of Directors' Responsibilities

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and the profit and loss of the Company for that period. In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the

DIRECTORS' REPORT

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

The Directors are responsible for:

- keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 2006;
- safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities; and
- under applicable law and regulations, including the Disclosure and Transparency Rules, the Directors are also responsible for preparing a Directors' Report, Strategic Report, Directors' Remuneration Report and Corporate Governance Statement that comply with the requirements of that law and those regulations. In relation to the latter, the Directors represent that, to the best of their knowledge and belief:
 - the financial statements give a true and fair view of the assets, liabilities, financial position and financial result for the year ended 31 March 2014; and
 - the Directors' Report, Strategic Report and information referenced therein, taken together, includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that they face.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board

C. Hardyman ACIS

Secretary

Havant

30 May 2014

CORPORATE GOVERNANCE

The Directors are committed to high standards of corporate governance and take the lead from those set out in the UK Corporate Governance Code and guidance issued by Ofwat. This report and the Report on Remuneration details the Company's approach to governance.

COMPLIANCE

In 2014 Ofwat published the principles by which Water Companies should deal with Board leadership, transparency and governance. In March 2014 the Company adopted its own Governance Code which can be found on the Portsmouth Water website. The Board believes that it complies with the principles although the structure of the Board does not strictly comply, in accordance with the Ofwat guidelines. The Ofwat principles suggest that independent Non-Executives should constitute the largest faction of Directors. The Board of Portsmouth Water consists of three independent Non-Executive Directors (including the Chairman) and three Executive Directors. The Chairman has the casting vote and therefore in principle the independent Non-Executives have the effective majority. We believe that this ensures that the independent Directors have a significantly strong voice in all discussions.

The Board have carefully considered this issue and believe the structure is appropriate. To increase the number of Non-Executives would be an unnecessary expense and the Board believe it is important to have an engineering and finance executive responsibility on the Board. The Board will continue to ensure that compliance with its own Governance Code is maintained in future years.

In addition, the Company will continue to have regard to the UK Corporate Governance Code. There were a number of changes made to this Code during 2013 and the Directors have taken the view that the Company should take a pragmatic approach to the new requirements and comply with those that are deemed consistent with the Ofwat principles.

DIRECTORS

The Board

The Board of Directors retains full and effective control of the Company and is collectively responsible for setting its strategy, ensuring appropriate resources are in place to meet objectives and monitoring performance.

The Non-Executive Directors play a full part by constructively challenging and contributing to the development of strategy. They are responsible for determining appropriate levels of remuneration for the Executive Directors and for recommending new appointments to the Board.

The members of the Board and the roles of each Director are shown on page 3, together with biographical notes. The Chairman is Mr. T. M. Lazenby MBE and the Managing Director is Mr. N. Smith. The Board Senior Independent Non-Executive Director is Mr. M. P. Kirk.

The Board meets monthly and has a schedule of matters specifically reserved to it for decision making. It has control of the Company, but delegates the day to day conduct of business to the Executive Directors and their senior management colleagues. However, there are a number of matters which must only be decided by the Board as a whole, including strategy, authorisation of all contracts over £150,000, dividend policy and certain regulatory matters.

Committee membership, number of formal meetings held during the year and attendance are shown in the following table:

	Number of meetings held	Number of meetings attended
Audit		
M. P. Kirk (Chairman)	3	3
H. V. Benjamin	3	3
T. M. Lazenby MBE	3	3
Nomination		
T. M. Lazenby MBE (Chairman)	2	2
H. V. Benjamin	2	2
M. P. Kirk	2	2
N. Smith	2	2
Remuneration		
H. V. Benjamin (Chair)	3	3
M. P. Kirk	3	3
T. M. Lazenby MBE	3	3
Full Board		
T. M. Lazenby MBE (Chairman)	14	14
H. V. Benjamin	14	14
M. P. Kirk	14	13
R. C. Porteous	14	14
N. J. Sheeran	14	14
N. Smith	14	14

The Chairman talks with and holds meetings on an informal basis with the other Non-Executive Directors without the Executives present. The Non-Executive Directors meet without the Chairman present annually to appraise his performance.

There were no circumstances arising during the year where it was necessary to record unresolved concerns in the Board minutes.

Chairman and Managing Director

The roles of Chairman and Managing Director are separate with a clear division of responsibilities between them.

The Chairman is responsible for leading the Board and ensuring its effectiveness. He facilitates the contribution of the Non-Executive Directors and the relationship between them and the Executive Directors.

Board Balance and Independence

The Board comprises a Non-Executive Chairman, three Executive Directors and two other Non-Executive Directors. The Non-Executive Directors bring a wide range of experience and knowledge to the Board, which complements the expertise of their Executive Director colleagues. They are all considered to be independent of management and the ultimate shareholder.

The Board considers that its structure achieves an appropriate balance of authority at the head of the Company, such that no one individual has an unfettered power of decision.

Appointments to the Board

The Nomination Committee comprises the Managing Director, Mr. N. Smith, and the three independent Non-Executive Directors, Mr. T. M. Lazenby MBE (Chairman), Mr. M. P. Kirk and Mrs. H. V. Benjamin. It is responsible for recommending new appointments to the Board.

CORPORATE GOVERNANCE

Decisions regarding the appointment of Directors are taken by the Board as a whole. The Nomination Committee met twice during the year.

The terms and conditions of appointment of Non-Executive Directors are available for inspection.

Information and Professional Development

Information is circulated to the Board in a timely fashion to ensure that all Directors are fully briefed on all issues arising at Board meetings. They are free to seek any further information considered necessary.

All Directors have access to the services of the Company Secretary and may take independent professional advice at the Company's expense in the furtherance of their duties.

Performance Evaluation

During the year, a formal performance evaluation of the Board, its committees and its Directors was undertaken. Each Director was required to complete a questionnaire, the responses to which were reviewed by the Board as a whole. The Non-Executive Directors also met without the Executives to consider the performance of the Board and its committees, and without the Chairman to appraise his performance. The Executive Directors are subject to a formal appraisal of performance which is reviewed by the Chairman. The Chairman also meets with each Non-Executive Director to review individual performance. The evaluation concluded that the Board and its committees operated effectively, and that each Director demonstrated commitment to the role and performed effectively.

Re-Election

In accordance with the Company's Articles of Association, all Directors are required to retire by rotation and one third of the Board must seek re-election each year. All Directors are subject to election at the first Annual General Meeting after their appointment.

REMUNERATION

Policy and practice in relation to Directors' remuneration is dealt with in full in the Report on Remuneration on pages 29 to 35.

ACCOUNTABILITY AND AUDIT

Financial Reporting

The Board believes that the Annual Report and Accounts play an important part in presenting a clear, balanced and understandable assessment of the Company's position and prospects. This is supported by the Chairman's Statement, together with a more detailed analysis of operations and financial matters in the Strategic Report.

Internal Control

The Directors are responsible for the Company's system of internal control and for reviewing its effectiveness. Such a system is designed to minimise the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. There has been no significant changes in the system of internal control during the year.

The Board is of the view that there is an ongoing process for identifying, evaluating and managing the Company's significant risks, that it has been in place for the year ended 31 March 2014 and up to the date of approval of the Annual Report and Accounts, that it is regularly reviewed by the Directors. The Board have also set the Risk Appetite for the business and it is reviewed annually.

The key procedures, which have been established with a view to providing effective internal control, are as follows:

Organisation

The Company's activities are operated through a Board of Directors with clearly defined reporting lines and delegation of authority. The Directors meet at least monthly to consider a schedule of matters required to be brought to them for decision making. A standing sub-committee of the Board meets fortnightly for the purpose of ensuring that full and effective control is maintained over appropriate financial, regulatory and operational issues.

Budgetary Control

Each year the Directors approve an annual plan produced from a comprehensive budgeting system. Actual results are reported against the approved plan on a monthly basis to provide a timely and regular monitoring of performance.

Investment Appraisal

The Company has a clearly defined framework for assessing capital expenditure needs and options, while post project appraisal looks at relevant improvement in the internal control procedures. Board approval is required for any project exceeding a quantified expenditure level.

Business, Operational and Compliance Risks

The Company assesses the risks facing its business on an ongoing basis and has identified them under ten main headings - operational, water quality, financial, environmental, regulatory, information technology, health and safety of employees, human resources, legal (including whistleblowing and fraud) and business continuity. They are subject to regular reporting to the Directors. The Board reviews the controls established to mitigate these risks and its insurance requirement on an annual basis. The Directors also receive reports from independent regulatory bodies, which comment on the performance of the core water business. Any issues raised in these reports are identified and dealt with in an appropriate manner.

At the April 2014 Board meeting, the Directors carried out their annual assessment for the year to 31 March 2014, including consideration of events since the year end.

Audit Committee and Auditors

The Audit Committee comprises the three Non-Executive Directors Mr. M. P. Kirk (Chairman), Mr. T. M. Lazenby MBE and Mrs. H. V. Benjamin.

It meets at least three times during the year. The purpose of the Committee is to ensure the preservation of good financial practices throughout the Company, to ensure that controls are in force to ensure the integrity of those practices and to monitor them, to review the interim and annual financial statements and to provide, by way of timely meetings, a line of communication between the Board and the external auditors. During these meetings with the external auditors the Audit Committee have asked to be made aware of significant issues, discovered by the Auditors on the financial statements. No issues have been identified which would have had a material impact on the financial statements.

The Committee has formal Terms of Reference, which deal with its authorities and duties. It has primary responsibility for making a recommendation on the appointment, reappointment and removal

CORPORATE GOVERNANCE

of the external auditors. It also reviews annually arrangements by which staff of the Company may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters.

The Committee reviews the independence and objectivity of the external auditors. This includes reviewing the nature and extent of non-audit services supplied by the external auditors to the Company, seeking to balance objectivity and value for money. The non-audit services provided during the year were for advice given on taxation matters and for advice on dealing with statutory reporting, including new accounting standards. These services would be those expected to be provided by the Company's external auditor.

The Committee does not consider that an internal audit function is required for the Company due to the size and nature of the business. This recommendation is reviewed annually.

REPORT ON REMUNERATION

The report sets out information on directors' remuneration for the year ended 31 March 2014. The Company is not required to comply with the rules for quoted companies contained within Schedule 8 of The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 but sets out certain additional information which the Directors consider to be relevant and in line with best practice.

Remuneration Committee

The Remuneration Committee met three times during the year to consider and approve, on behalf of the Board, the conditions of service of the Executive Directors of the Company. It comprises the three independent Non-Executive Directors, Mrs. H. V. Benjamin (Chair of the Remuneration Committee), Mr. T. M. Lazenby MBE and Mr. M. P. Kirk.

Statement of the Chairman of the Remuneration Committee

The principles of our remuneration policy remain unchanged from previous years. During the current financial, year the Remuneration Committee have not taken any major decisions to make changes to the directors' remuneration.

Directors' Remuneration Policy

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

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

The Executive Directors have one year service contracts with the Company. None of the Executive Directors serves as a Non-Executive Director for another company. The Non-Executive Directors do not have service contracts.

The service contracts of the Executive Directors include notice periods of one year, both by the Company and by the Director. There are no provisions for termination payments, other than payments for the period of notice. Fees payable to the Non-Executive Directors are determined by the Board as a whole and reflect the time, commitment and responsibilities of the role.

No Director is involved in deciding their own remuneration.

Revisions to Directors' Remuneration Policy

The Company is not proposing any changes to the current Policy.

REPORT ON REMUNERATION

FUTURE POLICY TABLE

ELEMENT, PURPOSE AND LINK TO STRATEGY	OPERATION, PERFORMANCE MEASURES, DEFERRAL	MAXIMUM OPPORTUNITY
<p>Base Salary (Fixed Pay) To pay a fair salary, commensurate with the individual's role, responsibilities and experience, and having regard to the market rates for similar roles in the water/utility sector and other comparable companies</p>	<p>Reviewed annually, taking account of market salary levels, Company performance, individual performance, changes in responsibility and levels of increase for the broader employee population.</p> <p>The remuneration committee considers the impact of any base salary increase on the total remuneration package.</p>	<p>There is no prescribed maximum salary or maximum rate of increase. The remuneration committee is guided by the general increase for the broader employee population but on occasions may need to recognise, for example, development in role, change in responsibility, specific retention issues, market practice or changes in regulatory requirements.</p> <p>Details of the outcome of the most recent salary review are provided in the annual report on remuneration.</p>
<p>Benefits (Fixed Pay) To provide cost-effective taxable benefits and to support the wellbeing of employees.</p>	<p>The Company currently provides a range of taxable benefits such as medical insurance; life insurance and paid holiday.</p> <p>Specific benefits provision may be subject to minor change from time to time, within this policy.</p>	<p>Taxable benefits are not subject to a specific cap, but represent only a small element of total remuneration. The costs associated with benefits provision are closely monitored and controlled.</p>
<p>Pension (Fixed Pay) To provide market competitive defined contribution pension arrangements, to assist with recruitment and retention.</p>	<p>Employer contributions are made to appropriate defined contribution pension arrangements.</p>	
<p>Annual bonus (Variable Pay) To reward performance and align Executives' interests to those of shareholders.</p>	<p>Bonus awards to Executive Directors are made each year and are approved by the remuneration committee. Executive bonus awards take account of the Company's key financial and service performance indicators for the relevant financial year.</p> <p>Details of the performance indicators for the most recent financial year and performance against them are provided in the annual report on remuneration. Similar indicators have been applied for the forthcoming year and we will report on the outcomes against the measures in the 2015 report.</p>	
<p>Employment contracts, and loss of office To facilitate recruitment and retention, and support pay for performance, by providing fair but not excessive contract features.</p>	<p>Notice periods from the Company are limited to 12 months.</p>	
<p>New Executive Director appointments To facilitate recruitment of necessary talent.</p>	<p>Remuneration for new appointments will be set in accordance with the policy detailed in this table.</p>	

REPORT ON REMUNERATION

Approach to Recruitment Remuneration

The remuneration package for a newly appointed Executive Director is set in accordance with the terms of the Company’s approved remuneration policy in force at the time of appointment. The variable remuneration for a new Executive Director is determined in the same way as for existing Executive Directors.

Service Contracts

The Executive Directors have one year service contracts with the Company. None of the Executive Directors serves as a Non-Executive Director for another company. The Non-Executive Directors do not have service contracts.

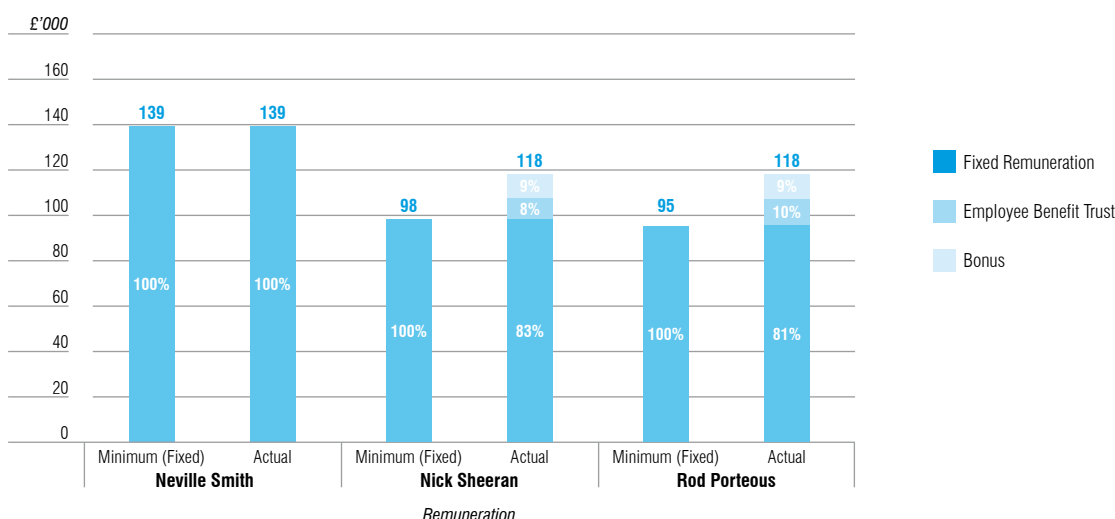
The service contracts of the Executive Directors include notice periods of one year, both by the Company and by the Director. There are no provisions for termination payments, other than payments for the period of notice.

The remuneration committee periodically reviews the contractual terms for new Executive Directors to ensure that these reflect best practice.

Illustration of Application of Remuneration Policy

The table below illustrates the minimum (fixed) remuneration, and provides an indication of the total remuneration for a year using the annual bonus and Employee Benefit Trust payment figures for the year ended 31 March 2014 and the base salaries effective 1 April 2013.

Relative Sizes of Remuneration Components



Policy on Payment for Loss of Office

There are no provisions for termination payments, other than payments for the period of notice.

Statement of Consideration of Employment Conditions Elsewhere in the Company

The remuneration approach for the Executive Directors is broadly consistent with that for employees across the Company as a whole. However, the exception is that general employees do not receive an annual performance related bonus. However all employees, apart from the Managing Director, do receive their twice annual payment from the Employment Benefit Trust (EBT). The EBT owns a controlling interest in the Company’s shares on behalf of the employees. Payments are made to all employees in June and November each year.

REPORT ON REMUNERATION

Annual Report on Remuneration

Directors Remuneration as a Single Figure (Audited Information)

Remuneration is analysed by director below:

	Salary/Fees £000	Benefits £000	Bonus Scheme £000	EBT £000	Pension £000	Total 2014 £000	Total 2013 £000
Executive:							
A. R. Neve (retired 30 April 2012)	-	-	-	-	-	-	24
R. C. Porteous (appointed 1 May 2012)	95	12	11	12	72	202	233
N. J. Sheeran	98	11	11	9	-	129	123
N. Smith	139	18	-	-	68	225	230
Non-Executive:							
H. V. Benjamin (appointed 1 November 2012)	23	-	-	-	-	23	9
M. P. Kirk (appointed 1 November 2012)	23	-	-	-	-	23	9
T. M. Lazenby MBE (Chairman)	36	-	-	-	-	36	35
R. L. Sullivan (resigned 1 November 2012)	-	-	-	-	-	-	16
R. J. Tennant (resigned 1 November 2012)	-	-	-	-	-	-	16
	414	41	22	21	140	638	695

Fees paid in respect of Mr. T. M. Lazenby MBE are paid to Seamab Consultancy Limited, in respect of Mr. M. P. Kirk to Mike Kirk Photography Limited, and in respect of Mrs. H. V. Benjamin to Benjamin and Rodgers Limited.

Long-term bonus schemes

The Company operates a long-term performance linked bonus scheme. This element of bonus is linked to five year targets and is based upon achievements at the end of that five year period.

Share options

The Company does not operate an Executive Share Option Scheme.

Directors' interests (Audited information)

The Directors' beneficial holdings of shares in South Downs Capital Limited, the ultimate parent undertaking, are detailed below and, in total, represent 8% of the issued share capital of this holding Company. They have no direct interests in the shares of Portsmouth Water Limited.

	'C' Ordinary Shares
N. Smith	450

There have been no changes to this shareholding between the 31 March 2014 and the date of this report.

Directors' emoluments waived during the year

There were no Directors' emoluments waived during the year.

Taxable benefits

Benefits comprise company cars and medical insurance.

The table below provides a breakdown of taxable benefits provided to directors in the period.

	2014 £000	2013 £000
Car and Fuel benefit	37	35
Medical insurance	4	6
Total	41	41

Variable pay/performance measured pay for Executive Directors

Short term annual bonus scheme

The remuneration package of the Executive Directors, as reported in the accounts, includes a performance related element. The performance related element is based upon the achievement of agreed financial, customer service and personal targets and is paid in the form of a payment at the end of the year.

REPORT ON REMUNERATION

The Executive Directors can earn up to 30% of basic salary for the performance related element, with a third of this being for long term performance and is held until the end of the current price control period. The assessment of this element is based upon:

- 27% based on Customer Service performance including meeting the outputs agreed at the Final Determination 2009 and being a top performer in the Service Incentive Mechanism.
- 17% Personal Objectives
- 23% Financial and Business Objectives
- 33% Long-term objectives. Paid in 2015 if achieved

The achievements were:

	% of salary (out of possible 20%)	Bonus £000
R. C. Porteous	10.5%	10
N. J. Sheeran	9.5%	9

The Managing Director does not receive a performance related element. This has been waived due to his shareholding in the holding company, South Downs Capital Limited.

Mr. R. C. Porteous and Mr. N. J. Sheeran also received payment from the Employee Benefit Trust on the same basis as other employees. Mr. N. Smith, as a shareholder of the Parent Company, is not entitled to payments from the Employee Benefit Trust.

Relative weighting of performance measures as described above for variable pay.

	Customer Service Measure 1 %	Personal Objectives Measure 2 %	Financial/ Business Objectives Measure 3 %	Long-Term Objectives Measure 4 %	Total %
R. C. Porteous	27	17	23	33	100
N. J. Sheeran	27	17	23	33	100
N. Smith	N/A	N/A	N/A	N/A	100

The above weightings convert into maximum percentages of salary payable as follows:

	Customer Service Measure 1 %	Personal Objectives Measure 2 %	Financial/ Business Objectives Measure 3 %	Long-Term Objectives Measure 4 %	Total %
R. C. Porteous	8.1%	5.1%	6.8%	10.0%	30%
N. J. Sheeran	8.1%	5.1%	6.8%	10.0%	30%
N. Smith	N/A	N/A	N/A	N/A	N/A

Summary of directors' performance targets and maximum variable pay achievable.

	Customer Service Measure 1		Personal Objectives Measure 2		Financial/Business Objectives Measure 3		Long-Term Objectives Measure 4		Maximum Variable Pay Achievable	
	Target %	Value £	Target %	Value £	Target %	Value £	Target %	Value £	2014	2013
R. C. Porteous	8.1	7,695	5.1	4,845	6.8	6,460	10	9,500	19,000	18,000
N. J. Sheeran	8.1	7,938	5.1	4,998	6.8	6,664	10	9,800	19,600	19,000
N. Smith	N/A	-	N/A	-	N/A	-	N/A	-	-	-

Summary of directors' performance against measures set for the period.

	Customer Service Measure 1		Personal Objectives Measure 2		Financial/Business Objectives Measure 3		Long-Term Objectives Measure 4		Variable Pay Achieved	
	Achieved	Value £	Achieved	Value £	Achieved	Value £	Achieved	Value £	2014	2013
R. C. Porteous	3.5	3,325	4.0	3,800	3.0	2,850	-	-	9,975	10,538
N. J. Sheeran	3.5	3,430	3.0	2,940	3.0	2,940	-	-	9,310	10,925
N. Smith	N/A	-	N/A	-	N/A	-	N/A	-	-	-

All variable pay has been awarded in accordance with the remuneration policy and criteria outlined at the commencement of the period. No discretion has been exercised over any variable pay awarded.

REPORT ON REMUNERATION

Pension Entitlements (Audited Information)

The Company participates in the Brockhampton Pension Scheme to provide pension benefits for its employees, including the Executive Directors.

Benefits in kind relating to company cars are considered to be part of pensionable pay for all employees under the Scheme.

The Executive Directors have accrued pension benefits under the Brockhampton Pension Scheme, which is a defined benefit scheme, during the year as detailed below:

	Value of increase in scheme benefit 2013/14 £000	Directors Contributions 2013/14 £000	Total included in single figure remuneration table 2013/14 £000	Value of increase in scheme benefit 2012/13 £000	Directors Contributions 2012/13 £000	Total included in single figure remuneration table 2012/13 £000	Accrued Pension 31/03/14 £000pa	Accrued Pension 31/03/13 £000pa
R. C. Porteous ¹	76	4	72	117	4	113	46	41
N. Smith ²	76	8	68	84	7	77	83	77

The value of the increase in accrued pension in excess of inflation, less each Directors' own contributions is included in the Directors' single figure remuneration table on page 32 of this report.

The accumulated accrued pension is the leaving service benefit to which the Director would be entitled to if he were to leave service at the end of the year. It includes any benefits earned as an employee prior to becoming a Director, as well as those earned for qualifying services after becoming a Director.

¹The pensionable salary used to calculate Mr. R. C. Porteous' accrued pension excludes £21,000 (2012/13 - £22,000) of non-pensionable salary.

²The pensionable salary used to calculate Mr. N. Smith's accrued pension excludes £4,000 (2012/13 - £6,000) of non-pensionable salary.

No additional benefits will become available to directors who retire early. For further details regarding each of the pension schemes, please refer to note 28 in the financial statements.

Mr. N. J. Sheeran is a member of the defined contribution scheme, although no contributions were made on his behalf by the Company in the year. The Non-Executive Directors are not members of either of the pension schemes.

Payments to Past Directors

No payments requiring disclosure were made to past directors during the period.

Payments for Loss of Office

No payments for loss of office were made during the period.

Remuneration of the Managing Director

The table below summarises the remuneration of the Managing Director for each of the last five financial years. The Managing Director does not receive a performance related element of remuneration. These figures do not include amounts accruing under defined benefit pension arrangements as the figures for historic years are not readily available.

Year ending 31 March:	2010	2011	2012	2013	2014
Total remuneration excluding pension (£000)	162	166	137	153	157

Percentage Change in Remuneration of the Managing Director

The following table shows the percentage change in the base salary, benefits and annual bonus of the Managing Director between the current and previous financial year compared to the average for all employees of the Company.

% change in:	Managing Director	Average for all employees
Base salary ¹	3.0%	2.9%
Benefits ²	0%	0%
Annual bonus ³	N/A	N/A

¹This increase represents the annual pay award to cover cost of living increases.

²There were no changes made to the underlying value of benefit payments provided during the year.

³This does not include payments made to employees from the Employee Benefit Trust.

REPORT ON REMUNERATION

Statement of Implementation of Remuneration Policy in the Following Financial Year

The Remuneration Committee intends to continue to apply broadly the same key performance metrics as in the previous year and to assess performance taking account of strategic and annual expectations for the Company.

Approval

This report was approved by the Board on 30 May 2014 and will be subject to shareholder approval at the Annual General Meeting to be held on 25 July 2014.

H. V. Benjamin

Chair of the Remuneration Committee

AUDIT REPORT

Independent Auditors' report to the members of Portsmouth Water Limited

We have audited the financial statements of Portsmouth Water Limited for the year ended 31 March 2014, which comprise the profit and loss account, the statement of total recognised gains and losses, the balance sheet, the cash flow statement and the related notes on pages 40 to 52 and the part of the report on remuneration to be audited. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

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

Respective Responsibilities of Directors and Auditors

As explained more fully in the Statement of Directors' Responsibilities, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements, and the part of the Report on Remuneration to be audited, in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all of the financial and non-financial information in the Report and Accounts to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of affairs of the company as at 31 March 2014 and its profit for the year then ended; and
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

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

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements and the part of the Report on Remuneration to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Nicholas Kelsey

Senior Statutory Auditor

For and on behalf of

Saffery Champness

Chartered Accountants

Statutory Auditors

Lion House

Red Lion Street

London

WC1R 4GB

4 July 2014

PROFIT AND LOSS ACCOUNT

For the year ended 31 March 2014

	Notes	2014 £000	2013 £000
Turnover	2	37,109	36,282
Cost of sales		(20,225)	(19,454)
Gross profit		16,884	16,828
Net operating expenses	3	(10,998)	(10,497)
Operating profit		5,886	6,331
(Loss)/profit on sale of fixed assets		(10)	1
Profit on ordinary activities before exceptional item		5,876	6,332
Exceptional item	10	(611)	-
Profit on ordinary activities before interest		5,265	6,332
Interest receivable	5	961	1,264
Other finance income	28	1,636	1,984
		7,862	9,580
Interest payable and similar charges	6	(6,533)	(6,463)
Profit on ordinary activities before taxation	7	1,329	3,117
Taxation on profit on ordinary activities	8	2,331	527
Profit for the financial year	20	3,660	3,644

The profit and loss account has been prepared on the basis that all operations are continuing operations.

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31 March 2014

	Notes	2014 £000	2013 £000
Profit for the financial year		3,660	3,644
Actuarial (loss) on pension scheme	28	(932)	(1,215)
Deferred tax relating to actuarial loss on pension scheme	17	186	280
Effect of change to corporation tax rate on pension asset	17	(576)	(360)
Total recognised gains and losses relating to the year		2,338	2,349

The accompanying notes form an integral part of these accounts.

BALANCE SHEET

As at 31 March 2014

	Note	2014 £000	2014 £000	2013 £000	2013 £000
Fixed assets					
Tangible assets	10	100,043		100,003	
Investments	11	59,384	159,427	59,468	159,471
Current assets					
Stocks		544		589	
Debtors	12	6,760		5,077	
Investments	13	2		4	
Cash at bank and in hand	14	4,503		4,059	
		11,809		9,729	
Creditors: amounts falling due within one year	15	(19,118)		(18,945)	
Net current liabilities			(7,309)		(9,216)
Total assets less current liabilities			152,118		150,255
Creditors: amounts falling due after more than one year	16		(94,216)		(91,369)
Provisions for liabilities	17		(8,021)		(9,414)
Net assets excluding pension asset			49,881		49,472
Pension asset	28		16,130		15,308
Net assets including pension asset			66,011		64,780
Capital and reserves					
Called up share capital	19		1,078		1,078
Share premium account	20		1,539		1,539
Capital redemption reserve	20		3,250		3,250
Profit and loss account	20		60,144		58,913
Shareholders' funds	21		66,011		64,780

The accompanying notes form an integral part of these accounts.

The accounts were authorised for issue and approved by the Board on 30 May 2014, and signed on its behalf by;

T. M. Lazenby MBE
Chairman

Company Number: 2536455

CASH FLOW STATEMENT

For the year ended 31 March 2014

	Notes	2014 £000	2014 £000	2013 £000	2013 £000
Net cash inflow from operating activities	22		15,140		15,672
Returns on investments and servicing of finance					
Interest received		964		1,263	
Interest paid		(3,602)	(2,638)	(3,550)	(2,287)
Taxation					
UK corporation tax paid		(110)		-	
Payments for group relief		(302)	(412)	(96)	(96)
Capital expenditure and financial investment					
Purchase of tangible fixed assets		(11,684)		(15,237)	
Sale of tangible fixed assets		3		6	
Capital contributions received		1,056	(10,625)	887	(14,344)
Equity dividends paid			(1,107)		(1,449)
Cash inflow/(outflow) before management of liquid resources and financing			358		(2,504)
Management of liquid resources					
(Purchase) of short term deposits		(44)		(58)	
Sale of investments		2	(42)	-	(58)
Financing					
New loans		-		4,000	
Loan repayment from Group company		84	84	-	4,000
Increase in cash in the year	23		400		1,438

The accompanying notes form an integral part of these accounts.

NOTES TO THE ACCOUNTS

1 Accounting Policies

The accounts have been prepared under the historical cost convention and in accordance with applicable United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) and with the provisions of the Companies Act 2006, except for the treatment of capital contributions as detailed in note 1.(c).

In view of the licence conditions under which the Company operates as a water supplier, it has to publish information about its annual results as if it were a company covered by the Listing Rules of the Financial Conduct Authority, except where it is considered inappropriate to do so. Earnings per share disclosures required by FRS 22 are not presented as the Company is a wholly owned subsidiary.

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

(a) Turnover

Turnover, which excludes value added tax, represents the income receivable for goods and services provided to external customers in the ordinary course of business. It comprises the value of water supplied and other related charges. Turnover from the regulated water business includes amounts billed for the year, together with an estimation of amounts unbilled at the year end, for measured water customers. Unmeasured income bills are based on the rateable value of properties. Measured income arises from customers who have meters fitted at their premises and amounts billed, therefore, are based on actual water consumption. The estimation of the amounts unbilled at the year end uses a defined methodology based upon a measure of unbilled water consumed, which is calculated from historical customer data.

(b) Fixed assets

(i) Infrastructure assets - mains

Infrastructure assets comprise a network of systems. Expenditure on infrastructure assets relating to increases in capacity or enhancement of the network and on maintaining the operating capability of the network in accordance with defined standards of service is treated as an addition and included in tangible fixed assets at cost. The cost of infrastructure assets is their purchase cost together with incidental expenses of acquisition and directly attributable labour costs which are incremental to the Company.

The depreciation charge on infrastructure assets is the estimated level of annual expenditure required to maintain the operating capability of the network, based on an independently certified asset management plan.

(ii) Other assets

Other assets comprise buildings and reservoirs, pumping plant, vehicles, mobile plant and office equipment. The cost of other assets is their purchase cost together with incidental expenses of acquisition and directly attributable labour costs which are incremental to the Company. Depreciation is provided on all other fixed assets with the exception of freehold land. It is calculated to write off the cost of assets less estimated residual values over their estimated useful economic lives using the straight line method. Those lives are estimated as follows:

Buildings and Reservoirs	100 years
Pumping Plant	15-25 years
Vehicles and Mobile Plant	5-7 years
Office Equipment	5-10 years

(iii) Impairment

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

(iv) Assets in the course of construction

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

(c) Capital contributions

(i) Mains contributions

In certain circumstances third parties make non-returnable contributions towards the cost of specific infrastructure assets. They are treated as capital contributions and the Directors consider it appropriate that, in order to present a true and fair view, they should be deducted from fixed assets, as shown in note 10 to the accounts on page 45. In accordance with the Companies Act 2006 requirement to include fixed assets at cost, such contributions would normally be treated as deferred income and released to the profit and loss account over the useful life of the corresponding assets. However, the assets to which they relate do not have determinable finite lives and, accordingly, no basis exists on which to recognise those contributions as deferred income.

(ii) Infrastructure charges

Infrastructure charges are made in respect of new connections in accordance with Condition 'C' of the Instrument of Appointment. These charges are treated as capital contributions and deducted from fixed assets, as more fully explained in note 1.(c)(i) above.

NOTES TO THE ACCOUNTS

(d) Investments

Investments are stated at the lower of cost or net realisable value.

(e) Stocks

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

(f) Taxation

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

Deferred tax is recognised on all timing differences where the transactions or events that give the Company an obligation to pay more tax in the future, or the right to pay less tax in the future, have occurred by the balance sheet date. Deferred tax assets are recognised when it is more likely than not that they will be recovered. Deferred tax is measured using rates of tax that have been enacted or substantively enacted by the balance sheet date.

The deferred tax balances have been discounted using a post-tax yield to maturity that could be obtained at the balance sheet date on government bonds with maturity dates similar to when the timing differences are expected to reverse.

(g) Leases

All leases are regarded as operating leases. Operating lease payments are charged to the profit and loss account on a straight line basis over the period of the lease.

(h) Pension costs and other post retirement benefits

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

The current service costs are charged to the profit and loss account and included as staff employment costs. The interest cost and expected return on assets are shown as a net amount within other finance income. Actuarial gains and losses are recognised immediately in the Statement of Recognised Gains and Losses.

Pension scheme liabilities are measured on an actuarial basis using the projected unit method and are discounted to their present value using the AA corporate bond rate. Pension scheme assets are valued at market value at the balance sheet date. The pension scheme surplus is recognised in full on the balance sheet.

The deferred tax relating to a defined benefit asset is offset against the defined benefit asset and not included with other deferred tax liabilities. Detailed information regarding the surplus and actuarial position of the scheme is given in note 28 to the accounts on pages 51 and 52.

The Company also operates a defined contribution pension scheme. The charge to the profit and loss account amounts to the contributions payable to the scheme in respect of the accounting period.

(i) Financial instruments

When a financial asset or liability is recognised initially it is measured at its fair value plus or minus transaction costs. The Company subsequently categorises financial instruments as follows:

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

The Company's financial liabilities consist of fixed rate borrowings in the form of perpetual debentures and an index linked loan. These instruments are classified as other liabilities and are measured at amortised cost.

NOTES TO THE ACCOUNTS

(j) Provisions

A provision is recognised when the Company has a legal or constructive obligation as a result of past events and it is probable that an outflow of economic benefits will be required to settle the obligation. The effect of the time value of money, except in the case of deferred tax as mentioned in note (f) above, is not material and therefore the provisions are not discounted.

2 Turnover	2014	2013
	£000	£000
Unmeasured supplies	21,396	21,681
Measured supplies	14,294	13,332
Bulk supply to Southern Water Services	631	513
Chargeable work	788	756
	37,109	36,282

Turnover is wholly attributable to water supply and related activities in the United Kingdom.

3 Net operating expenses	2014	2013
	£000	£000
Administrative expenses	11,359	10,866
Other operating income	(361)	(369)
	10,998	10,497

4 Directors and employees

Employment costs:	2014	2013
	£000	£000
Wages and salaries	7,755	7,349
Social security costs	662	618
	8,417	7,967
Defined benefit pension costs (note 28)	1,392	1,412
Defined contribution pension costs (note 28)	53	26
	9,862	9,405
Transferred to capital schemes	(496)	(465)
Net employment costs charged to the profit and loss account	9,366	8,940

Average numbers employed during year:	2014	2013
	Number	Number
Operations	151	147
Administration	87	85
	238	232

Directors' remuneration:	Highest Paid	Highest Paid	Total	Total
	Director	Director		
	2014	2013		
	£000	£000	£000	£000
Total remuneration	157	153	498	505
Pension scheme benefit	68	77	140	190
	225	230	638	695

The number of directors for whom retirement benefits are accruing under defined contribution schemes amounted to 1 (2013 - nil). The number of directors for whom retirement benefits are accruing under defined benefit schemes amounted to 2 (2013 - 2).

Further details relating to Directors' remuneration are set out in the Report on Remuneration on pages 29 to 35. The information set out in that Report which is subject to audit forms part of these financial statements.

5 Interest receivable	2014	2013
	£000	£000
Loan to Group company	948	1,244
Interest on short term deposits	8	19
Other interest receivable	5	1
	961	1,264

NOTES TO THE ACCOUNTS

6 Interest payable and similar charges	2014	2013
	£000	£000
£66.5m. loan		
- interest	3,409	3,357
- indexation	2,900	2,826
- amortisation of fees	57	57
- administration expenses	25	25
	6,391	6,265
Other bank loans and overdraft	129	185
Debenture stocks	10	10
Other interest payable	3	3
	6,533	6,463

7 Profit on ordinary activities before taxation	2014	2013
	£000	£000
Profit on ordinary activities is after charging:		
Depreciation		
- infrastructure assets	5,177	5,059
- non infrastructure assets	3,770	3,862
Rates	2,018	2,254
Water abstraction charges	1,327	1,327
Hire of plant and machinery	6	8
Other operating leases	339	339
Auditors' remuneration:		
Fees payable to the Company's auditor for the audit of the annual accounts	31	31
Fees payable to the Company's auditor for other services:		
- audit-related assurance services	7	11
- taxation compliance services	6	3
- taxation advisory services	-	1
- other assurance services	-	5
- other non audit services	20	-
Fees in respect of the Brockhampton Pension Scheme		
- audit*	2	3

* These fees are not paid by Portsmouth Water Limited.

NOTES TO THE ACCOUNTS

8 Taxation	2014	2013
	£000	£000
Current tax		
United Kingdom corporation tax at 23% (2013 - 24%)	(5)	403
Adjustment in respect of prior periods	(4)	(5)
	(9)	398
Deferred tax		
Origination and reversal of timing differences	276	202
(Increase)/decrease in discount	(461)	75
Effect of change to corporation tax rate	(1,208)	(803)
Difference between pension cost charge and pension cost relief	243	352
Effect of change to corporation tax rate on pension asset	(1,172)	(751)
	(2,322)	(925)
Tax on profit on ordinary activities	(2,331)	(527)

The tax charge for the year is lower (2013 - lower) than the standard rate of corporation tax in the UK of 23% (2013 - 24%). The difference is explained as follows:

	2014	2013
	£000	£000
Profit on ordinary activities before tax	1,329	3,117
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 23% (2013 - 24%)	306	748
Effect of:		
Expenses not deductible for tax purposes	148	8
Capital allowances for the period in excess of depreciation	(200)	(3)
Revenue items charged to capital	20	17
Difference between pension cost charge and pension cost relief	(279)	(367)
Adjustments to tax charge in respect of prior periods	(4)	(5)
Current tax charge for year	(9)	398

9 Dividends	2014	2013
	£000	£000
Equity: Ordinary/'A' Ordinary		
First interim paid	556	848
Second interim paid	551	601
	1,107	1,449

The Directors are proposing the payment of a final dividend of £0.195m for the year ended 31 March 2014. This dividend has not been accounted for within the current year financial statements, as it has yet to be approved.

NOTES TO THE ACCOUNTS

10 Tangible fixed assets	Freehold land, buildings & reservoirs £000	Mains £000	Pumping plant £000	Vehicles, mobile plant & office equipment £000	Total £000
Cost					
At 1 April 2013	51,903	134,609	39,874	17,368	243,754
Additions	788	6,463	962	2,454	10,667
Disposals	-	(846)	-	(154)	(1,000)
At 31 March 2014	52,691	140,226	40,836	19,668	253,421
Depreciation					
At 1 April 2013	10,158	81,224	18,666	11,692	121,740
Charge for year	524	5,177	1,725	1,521	8,947
Impairment loss	611	-	-	-	611
Disposals during year	-	(846)	-	(141)	(987)
At 31 March 2014	11,293	85,555	20,391	13,072	130,311
Net book value					
At 31 March 2014	41,398	54,671	20,445	6,596	123,110
At 31 March 2013	41,745	53,385	21,208	5,676	122,014
Capital contributions					
At 1 April 2013	-	22,011	-	-	22,011
Received during year	-	1,056	-	-	1,056
At 31 March 2014	-	23,067	-	-	23,067
Net book value after deducting capital contributions					
At 31 March 2014	41,398	31,604	20,445	6,596	100,043
At 31 March 2013	41,745	31,374	21,208	5,676	100,003

Included within vehicles, mobile plant and office equipment is an asset in the course of construction amounting to £0.764m (2013 - £0.331m), and within freehold land, buildings and reservoirs is a further asset in the course of construction amounting to £0.045m (2013 - nil). Both have thus far not been depreciated.

Included within freehold land, buildings and reservoirs at cost was an amount of £0.611m relating to a capital project involving the design and construction of a winter storage reservoir at Havant Thicket. Costs incurred to date were in respect of initial design, planning application and environmental impact studies. This project is now unlikely to start in the foreseeable future and therefore the expenditure is considered to have no economic benefit. An impairment provision has therefore been made for the above amount and has been shown as an exceptional item in the profit and loss account on page 37. An earlier impairment provision of £1.086m had been made as at the 31 March 2011, therefore the total costs to date relating to this project of £1.697m have now been taken as impaired and provided for.

11 Fixed asset investments

	Loans to Group undertakings £000
At 1 April 2013	59,468
Repayment	(84)
At 31 March 2014	59,384

NOTES TO THE ACCOUNTS

12 Debtors	2014	2013
	£000	£000
Trade debtors	3,137	1,671
Amounts owed by Group companies	28	29
Prepayments and accrued income	3,083	2,985
Other debtors	512	392
	6,760	5,077

All of the above amounts fall due within one year.

As at 31 March 2014, trade debtors had a carrying value of £5.916m (2013 - £4.270m) before provision for bad debt. Trade debtors in arrears are provided for in full, but only an element of current debt is provided for. The amount of the provision was £2.779m as at 31 March 2014 (2013 - £2.599m).

The ageing of these debtors was as follows:

	2014	2013
	£000	£000
Up to 12 months	3,426	1,940
Over 12 months	2,490	2,330
	5,916	4,270

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

Movements on the provision for bad debt are as follows:

	2014	2013
	£000	£000
At 1 April 2013	2,599	2,478
Provision for bad debt required in the year	665	467
Debt written off in the year as uncollectable	(485)	(346)
At 31 March 2014	2,779	2,599

The other classes within debtors do not contain balances that may be irrecoverable. The maximum exposure to credit risk at the reporting date is the fair value of each class of debtor mentioned above. The Company does not hold any collateral as security.

13 Current asset investments

	Unlisted investments
	£000
At 1 April 2013	4
Sold during year	(2)
At 31 March 2014	2

14 Cash at bank and in hand

Of the total amount shown of £4.503m, £1.757m (2013 - £1.713m) is held specifically for the payment of the next half yearly loan interest charges.

15 Creditors: amounts falling due within one year

	2014	2013
	£000	£000
3% Perpetual debenture stock	60	60
3½% Perpetual debenture stock	185	185
4% Perpetual debenture stock	39	39
Bank loan	5,000	5,000
Payments received on account	2,320	2,156
Trade creditors	752	1,635
Amounts owed to Group companies	1,506	1,765
Corporation tax	-	95
Social security and other taxation	235	230
Other creditors	1,941	2,478
Accruals	654	613
Water rates in advance	6,426	4,689
	19,118	18,945

The £5.0m bank loan is part of a three year £10m working capital facility, which is secured upon the assets of the Company and bears interest at London Interbank rates.

NOTES TO THE ACCOUNTS

16 Creditors: amounts falling due after more than one year	2014	2013
	£000	£000
Due within one to two years:		
Payments received on account	-	110
In five years or more:		
Bank loan	95,268	92,368
Less: deferred arrangement costs	1,052	1,109
	94,216	91,259
	94,216	91,369

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

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

17 Provisions for liabilities	2014	2013
	£000	£000
Deferred taxation:		
At 1 April 2013	9,414	9,940
Provided during the year in profit and loss account	(1,393)	(526)
At 31 March 2014	8,021	9,414

The total deferred tax balance before the effect of discounting is £8.989m (2013 - £9.997m). The amount provided for deferred taxation represents timing differences caused by the excess of tax allowances over depreciation.

	2014	2013
	£000	£000
Deferred tax excluding that relating to pension asset:		
Accelerated capital allowances	8,021	9,414
Pension asset (note 28)	4,033	4,572
Total provision for deferred tax	12,054	13,986
At 1 April 2013	13,986	14,831
Deferred tax charge in profit and loss account (note 8)	(2,322)	(925)
Deferred tax charged to the statement of total recognised gains and losses	390	80
At 31 March 2014	12,054	13,986

A reduction in the UK corporation tax rate from 23% to 21% with effect from 1 April 2014 and from 21% to 20% with effect from 1 April 2015 was enacted during the period. As a consequence the deferred tax charge includes a decrease in the deferred tax liability of £1.208m.

No provision has been made for deferred tax on gains recognised on the sale of properties where potentially taxable gains have been rolled over into replacement assets. Such tax would become payable only if the property were sold without it being possible to claim rollover relief. The total amount unprovided for is £0.495m (2013 - £0.570m). At present it is not envisaged that any tax will become payable in the foreseeable future.

NOTES TO THE ACCOUNTS

18 Financial instruments

Page 19 of the Strategic Report provides an explanation of the objectives and policies for holding financial instruments. The numerical disclosures in this note deal with financial assets and liabilities. Short term debtors and creditors have been excluded from all disclosures. The fair value of all financial instruments is not materially different to the book value.

Financial assets

The financial assets of the Company are detailed below. The fixed asset investment earns interest based on London Interbank rates. Cash at bank and in hand includes a sterling cash deposit of £1.757m, which is placed on the money market at a six monthly rate and is held specifically for the payment of the next half yearly loan interest charges. The remaining cash balances on bank accounts receive interest at commercial rates.

Financial liabilities

The Company has no foreign currency contracts. The interest rate profile of its financial liabilities at 31 March 2014 is detailed below:

Sterling	2014 £000	2013 £000
Assets		
Fixed asset investment	59,384	59,468
Current asset investments	2	4
Cash at bank and in hand	4,503	4,059
	63,889	63,531

Sterling	Fixed Rate 2014 £000	Fixed Rate 2013 £000	Floating Rate 2014 £000	Floating Rate 2013 £000	Total 2014 £000	Total 2013 £000
Liabilities						
Bank loans and overdraft	94,216	91,259	5,000	5,000	99,216	96,259
Debenture stock	284	284	-	-	284	284
	94,500	91,543	5,000	5,000	99,500	96,543

Fixed rate	Weighted Average Interest Rate %	Weighted Average Interest Rate %	Weighted Average Period for which Rate is Fixed Years	Weighted Average Period for which Rate is Fixed Years
Sterling	2014	2013	2014	2013
	3.6	3.6	18	19

Interest on the floating rate financial liability is based on London Interbank rates.

The maturity profile of the Company's financial liabilities at 31 March 2014 is detailed below:

	2014 £000	2013 £000
In one year or less	5,284	5,284
In more than five years	94,216	91,259
	99,500	96,543

The Company had undrawn committed borrowing facilities at 31 March 2014, in respect of which all conditions precedent had been met, as follows:

	2014 £000	2013 £000
Expiring between one and two years	9,000	-
Expiring in more than two years	-	9,000

The carrying amounts of the financial assets and liabilities shown above approximate their fair value.

NOTES TO THE ACCOUNTS

19 Called up share capital	2014	2013
	£000	£000
Authorised:		
Equity:		
6,000,000 Ordinary Shares of 10p each	600	600
10,500,000 'A' Ordinary Shares of 10p each	1,050	1,050
	1,650	1,650
Non-equity:		
3,250,000 Redeemable Preference Shares of £1 each	3,250	3,250
	4,900	4,900
Allotted, called up and fully paid:		
Equity:		
4,265,177 Ordinary Shares of 10p each	427	427
6,509,162 'A' Ordinary Shares of 10p each	651	651
	1,078	1,078

The Ordinary and 'A' Ordinary Shareholders are entitled to receive dividends pari passu according to the amount paid up or credited as paid up on their shares. The Ordinary Shares are the only class of share to carry voting rights.

In a distribution on the winding up of the Company, the Ordinary and 'A' Ordinary Shareholders are entitled to share the balance of any surplus assets pari passu according to the amount paid up or credited as paid up on their shares.

20 Reserves	Share Premium £000	Capital Redemption £000	Profit and Loss £000
At 1 April 2013	1,539	3,250	58,913
Profit for the financial year	-	-	3,660
Dividends	-	-	(1,107)
Actuarial (loss) on pension scheme	-	-	(932)
Movement on deferred tax relating to pension scheme	-	-	186
Effect of change to corporation tax rate on pension asset	-	-	(576)
At 31 March 2014	1,539	3,250	60,144

21 Reconciliation of movements in shareholders' funds	2014	2013
	£000	£000
Profit for the financial year	3,660	3,644
Dividends	(1,107)	(1,449)
	2,553	2,195
Actuarial (loss) on pension scheme	(932)	(1,215)
Movement on deferred tax relating to pension scheme	186	280
Effect of change to corporation tax rate on pension asset	(576)	(360)
Net addition to shareholders' funds	1,231	900
Opening shareholders' funds	64,780	63,880
Closing shareholders' funds	66,011	64,780

22 Reconciliation of operating profit to net cash inflow from operating activities	2014	2013
	£000	£000
Operating profit	5,886	6,331
Notional pension costs	421	454
Depreciation charge	8,947	8,921
Loss on disposal of asset	-	10
Decrease in stocks	45	7
(Increase)/decrease in debtors	(1,662)	1,440
Increase/(decrease) in creditors	1,503	(1,491)
Net cash inflow from operating activities	15,140	15,672

NOTES TO THE ACCOUNTS

23 Reconciliation of net cash flow to movement in net debt	2014	2013
	£000	£000
Increase in cash in the year	400	1,438
Cash outflow from increase in liquid resources	42	58
Cash (inflow) from (increase) in debt	-	(4,000)
Change in net debt resulting from cash flows	442	(2,504)
Non cash movement	(2,957)	(2,883)
Movement in net debt in the year	(2,515)	(5,387)
Net debt at 1 April 2013	(92,480)	(87,093)
Net debt at 31 March 2014	(94,995)	(92,480)

The Company includes as liquid resources term deposits of less than one year and current asset equity investments.

24 Analysis of changes in net debt	At 1 April 2013	Cash Flow	Non cash Movements	At 31 March 2014
	£000	£000	£000	£000
Cash at bank and in hand	2,346	400	-	2,746
Debt falling due within one year	(5,284)	-	-	(5,284)
Debt falling due after one year	(91,259)	-	(2,957)	(94,216)
	(96,543)	-	(2,957)	(99,500)
Short term deposits	1,713	44	-	1,757
Current asset equity investments	4	(2)	-	2
	1,717	42	-	1,759
	(92,480)	442	(2,957)	(94,995)

The non cash movement relates to the annual indexation of the loan and the amortisation of the issue fees.

25 Capital commitments	2014	2013
	£000	£000
Contracted for but not provided in these financial statements	2,649	2,520

The Company has a further commitment under operating leases relating to computer hardware and associated software of £0.192m per annum (2013 - £0.339m) which expire as set out below:

	2014	2013
	£000	£000
Within one year	-	339
Within two to five years	192	-

26 Contingent liabilities

There were no reportable contingent liabilities at 31 March 2014 or at 31 March 2013.

27 Ultimate parent undertaking

At 31 March 2014 the Company's ultimate parent undertaking was South Downs Capital Limited, which is the parent of both the smallest and largest groups of which the Company is a member. There is no ultimate controlling party but South Downs Capital Limited is controlled by the Directors of the Employee Benefit Trust which is the ultimate controlling shareholder. Copies of the consolidated accounts can be obtained on request from the Registered Office.

NOTES TO THE ACCOUNTS

28 Pensions

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

The formal actuarial valuation as at 31 March 2013 was updated to the accounting date by an independent qualified actuary in accordance with FRS 17. As required by FRS 17, the value of the defined benefit liabilities has been measured using the projected unit method.

The estimated Company contributions expected to be paid to the Scheme for the year commencing 1 April 2014 is £1.0m (2013 actual - £1.0m). Of this amount, £0.7m is contributed directly by the Company and £0.3m is contributed by employees by salary sacrifice under the SMART arrangement.

The key FRS 17 assumptions used for the scheme were as follows:

	2014	2013	2012
	% per annum	% per annum	% per annum
RPI inflation	3.5	3.5	3.4
CPI inflation	2.6	2.6	2.5
Discount rate	4.3	4.3	4.6
Pension increases	2.6	2.6	2.5
Salary growth	5.75	5.75	5.65

On the basis of the assumptions used for life expectancy, a male pensioner currently aged 65 would be expected to live for a further 23.6 years (2013 - 23.6 years). Allowance is made for future improvements in life expectancy.

The fair value of assets in the scheme, a breakdown of the assets into the main asset classes, the present value of the FRS 17 liabilities and the surplus of assets over the FRS 17 liabilities (which equals the gross pension asset) are set out below:

	2014	2014	2013	2013	2012	2012
	Expected	Fair	Expected	Fair	Expected	Fair
	Return %	Value	Return %	Value	Return %	Value
	per annum	£000	per annum	£000	per annum	£000
Equities	7.4	65,741	6.9	63,599	7.2	74,294
Absolute return fund	5.2	9,004	6.2	8,420	-	-
Bonds	3.4	48,819	2.9	50,361	3.2	44,154
Property	5.5	4,422	4.9	3,611	-	-
Cash	1.3	6,625	0.4	6,930	0.7	5,214
	5.4	134,611	4.9	132,921	5.5	123,662

The total expected return on assets is derived by taking the weighted average of the long-term expected return on each of the asset classes.

	2014	2013
	£000	£000
Total fair value of scheme assets	134,611	132,921
FRS 17 value of scheme liabilities	114,448	113,041
Gross pension asset	20,163	19,880
Related deferred tax liability	4,033	4,572
Net pension asset	16,130	15,308

Under FRS 17, the scheme is represented on the balance sheet at 31 March 2014 as an asset of £20.163m (2013 - £19.880m), which amounts to £16.130m net of deferred tax (2013 - £15.308m).

The Company paid contributions at a rate of 12.4% of earnings. Members pay contributions at a rate of 5% of earnings via salary sacrifice.

The Company also operates a defined contribution pension scheme. The contributions payable by the Company for the year in respect of the defined contribution scheme amounted to £52,778 (2013 - £25,538).

NOTES TO THE ACCOUNTS

The FRS 17 value of scheme liabilities moved over the period as follows:

	2014 £000	2013 £000
Opening scheme liabilities	113,041	104,097
Employer's part of current service cost	1,392	1,412
Interest cost	4,814	4,705
Contributions by scheme participants	-	-
Benefits paid	(3,579)	(5,102)
Actuarial (gain)/loss	(1,220)	7,929
Closing scheme liabilities	114,448	113,041

The FRS 17 value of scheme assets moved over the period as follows:

	2014 £000	2013 £000
Opening fair value of scheme assets	132,921	123,662
Expected return on assets	6,450	6,689
Contributions by scheme participants	-	-
Contributions by the Company, including employee contributions under the SMART arrangement	971	958
Benefits paid	(3,579)	(5,102)
Actuarial (loss)/gain	(2,152)	6,714
Closing fair value of scheme assets	134,611	132,921

The following amounts have been included within operating profit under FRS 17:

	2014 £000	2013 £000
Current service cost (employer's part only)	1,392	1,412
Past service cost	-	-
Total operating charge	1,392	1,412

The following amounts have been included as other finance income under FRS 17:

	2014 £000	2013 £000
Expected return on pension scheme assets	6,450	6,689
Interest on pension scheme liabilities	(4,814)	(4,705)
Net return	1,636	1,984
Total return recognised in the profit and loss account	244	572

The following amounts have been recognised within the statement of total recognised gains and losses (STRGL) under FRS 17:

	2014 £000	2013 £000
Actual return less expected return on scheme assets	(2,152)	6,714
Experience gains arising on scheme liabilities	1,003	-
Gain/(loss) due to changes in assumptions underlying the FRS 17 value of scheme liabilities	217	(7,929)
Actuarial (loss) recognised in the STRGL	(932)	(1,215)

The actual return on plan assets was an increase of £4.298m in the year to 31 March 2014 (2013 - increase of £13.403m).

The history of experience gains and losses is:

	2014	2013	2012	2011	2010
Present value of scheme liabilities (£000)	(114,448)	(113,041)	(104,097)	(91,313)	(100,268)
Total fair value of scheme assets (£000)	134,611	132,921	123,662	120,037	113,843
Gross pension asset (£000)	20,163	19,880	19,565	28,724	13,575
Actual return less expected return on scheme assets (£000)	(2,152)	6,714	(1,326)	1,181	24,665
Percentage of scheme's assets	(2%)	5%	(1%)	1%	22%
Experience gains arising on scheme's liabilities (£000)	1,003	-	1,783	-	-
Percentage of the FRS 17 value of the scheme's liabilities	1%	0%	1%	0%	0%
Total amount recognised in the STRGL (£000)	(932)	(1,215)	(10,245)	14,904	(2,636)
Percentage of the FRS 17 value of the scheme's liabilities	(1%)	(1%)	(10%)	16%	(3%)

The cumulative amount of actuarial gains and losses recognised in the STRGL as at 31 March 2014 was a loss of £20.121m (2013 - loss of £19.189m).

The Accounting Standards Board have published guidance relating to best practice for disclosure of pensions information. The Company have decided not to follow the guidance at this time.

NOTICE OF MEETING

Notice is hereby given that the Annual General Meeting of Portsmouth Water Limited will be held at the Company's Registered Office, PO Box 8, West Street, Havant, Hants, at 11.00 am on Thursday, the 25th day of July 2014, on the following business:

1. To receive and consider the Directors' Report and Accounts for the year ended 31 March 2014 and the Auditors' Report thereon.
2. To approve the Report on Remuneration.
3. To re-elect Mr. N. Smith a Director of the Company.
4. To re-elect Mr. R. C. Porteous a Director of the Company.
5. To approve a total final dividend of £195,000 to be made to the holders of Ordinary and 'A' Ordinary Shares.
6. To reappoint Saffery Champness as Company Auditors and to authorise the Directors to fix their remuneration.

Registered Office

PO Box 8
West Street Havant
Hants PO9 1LG
30 May 2014

By order of the Board
C. Hardyman ACIS
Secretary

Notes:

- i) Debenture holders are reminded that the holding of debenture stock does not entitle them to attend or vote at the meeting.
- ii) Shareholders are reminded that no voting rights attach to the 'A' Ordinary Shares. 'A' Ordinary Shareholders are not entitled to attend the meeting.
- iii) A proxy form is enclosed for Shareholders entitled to vote at the meeting.
- iv) To be valid proxies must reach the Company's Registered Office not later than forty-eight hours before the time fixed for the meeting.

APPENDIX - KEY PERFORMANCE INDICATORS

KPI - 1	2014	2013
a) Gearing - Debt/RCV	£000	£000
(i) Debt		
Bank loan (note 16)	95,268	92,368
Bank loan (note 15)	5,000	5,000
Debenture stock (note 15)	284	284
Cash at bank and in hand	(4,503)	(4,059)
	96,049	93,593

For the purposes of this ratio, debt excludes the deferred arrangement costs of £1.052m (note 16) and the current asset investment of £0.002m (note 13).

(ii) Regulatory Capital Value (RCV)

Value established by Ofwat in Final Determination in 2009

One of the elements considered by Ofwat in assessing revenues required by the Company is a return on the capital investment in the business. The value of the capital base of each company for the purposes of setting price limits is the RCV. The RCV is widely used by the investment community as a proxy for the market value of the regulated business. For Portsmouth Water the RCV is a key element of its bond covenants.

	2014	2013
	£000	£000
Regulatory capital value indexed to 31 March	117,938	120,071
(iii) Gearing - Debt/RCV ratio (i) ÷ (ii)	81.4%	77.9%

b) Cash interest cover

This ratio represents the number of times cashflow of the business covers interest payments.

(i) Cashflow before interest paid is derived from the cashflow statement on page 39 and is calculated as follows:

	2014	2013
	£000	£000
Operating profit, after adding back Employee Benefit Trust payments	6,972	7,316
Notional pension costs	421	454
Depreciation charges	8,947	8,921
Other items	-	10
Interest received, excluding amounts for inter-company loan	13	20
Taxation, excluding payments for group relief	(110)	-
Capital expenditure	(10,625)	(14,344)
Loan repayment from Group company	84	-
New loans	-	4,000
	5,702	6,377
(ii) Interest paid	3,602	3,550
(iii) Cash interest cover ratio (i) ÷ (ii)	1.58	1.80

c) Return on regulatory equity

This ratio represents the return on regulatory equity in terms of the equity element of the regulatory capital value.

	2014	2013
	£000	£000
Revenue	37,109	36,282
Operating costs, excluding Employee Benefit Trust payments	21,190	20,045
Current cost depreciation	5,893	5,856
Infrastructure renewals charge	5,177	5,059
Earnings before interest and tax	4,849	5,322
Current tax charge/(credit)	(9)	398
Interest payable, excluding indexation and amortisation	3,576	3,580
(i) Return	1,282	1,344
(ii) Average Regulatory Capital Value, equity element only	22,135	26,062
(iii) Return on regulatory equity (i) ÷ (ii)	5.8%	5.2%

APPENDIX - KEY PERFORMANCE INDICATORS

KPI - 2 Customer Service Measures

Indicators are based on information supplied to Ofwat and confirmed in the Ofwat publication 'Levels of Service for the Water Industry in England and Wales Report'.

KPI - 3 Water Quality

This indicator is based on figures reported to the DWI.

KPI - 4 Efficiency

The results for this indicator are provided by Ofwat in its publication 'Water and Sewerage Unit Costs and Efficiency'.

KPI - 5 Leakage

This indicator is based on figures supplied to Ofwat and confirmed in its report 'Security of Supply, Leakage and the Efficient Use of Water'. The figures for 2013/14 have been supplied to Ofwat, but will not be confirmed in the Ofwat document until later in 2014.

