ANNUAL PERFORMANCE REPORT 2019

Company Number: 2536455

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INTRODUCTION

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

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

162

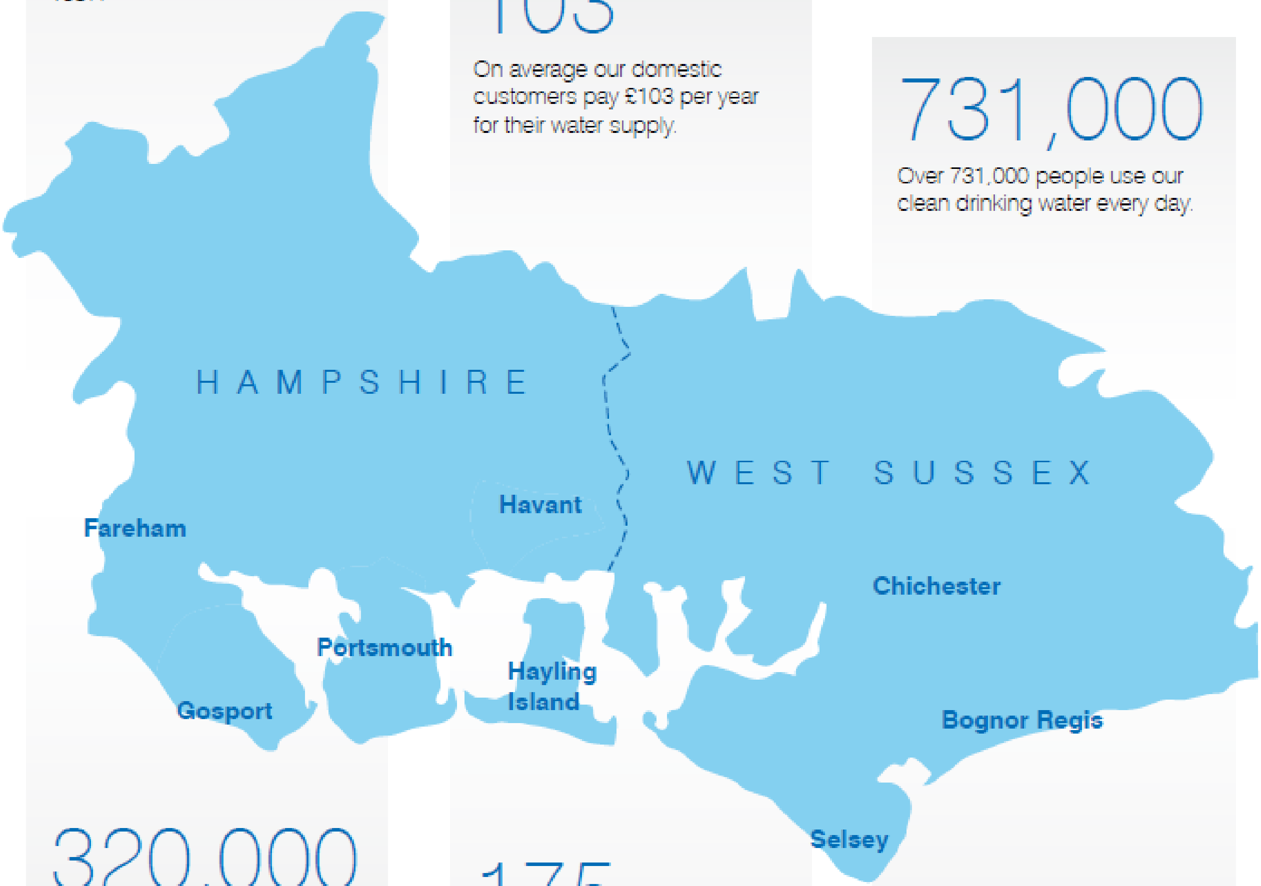
We are proud to have served the local community since 1857.

103

On average our domestic customers pay £103 per year for their water supply.

731,000

Over 731,000 people use our clean drinking water every day.



320,000

We provide clean drinking water to 320,000 homes and businesses in our area.

175

We serve the cities and towns of Portsmouth, Chichester, Fareham, Gosport, Havant and Bognor Regis. On average, each day we supply approximately 175 million litres of water.

3,337

Our area of supply has a network of over 3,337 kilometres of underground mains.

We provide drinking water only. We do not provide sewerage services; this is normally provided by Southern Water

CORPORATE GOVERNANCE

The Board of Portsmouth Water Limited, at 31 March 2019, comprised of two Executive Directors, three independent Non-Executive Directors and one Investor Director. The Executive Directors are Bob Taylor, who has replaced Neville Smith as the new CEO, and Helen Orton who is the Finance and Regulation Director. The independent Non-Executive Directors are Mike Kirk (Chairman), Mike Coffin and Martin Johnson. In addition, there is one Investor Director, David Owens.

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

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

Detailed information in connection with the Company's Corporate Governance processes and compliance, including operation of the Board, Risk Management and Internal Control is set out on pages 38-55 of the Company's ARA.

Compliance

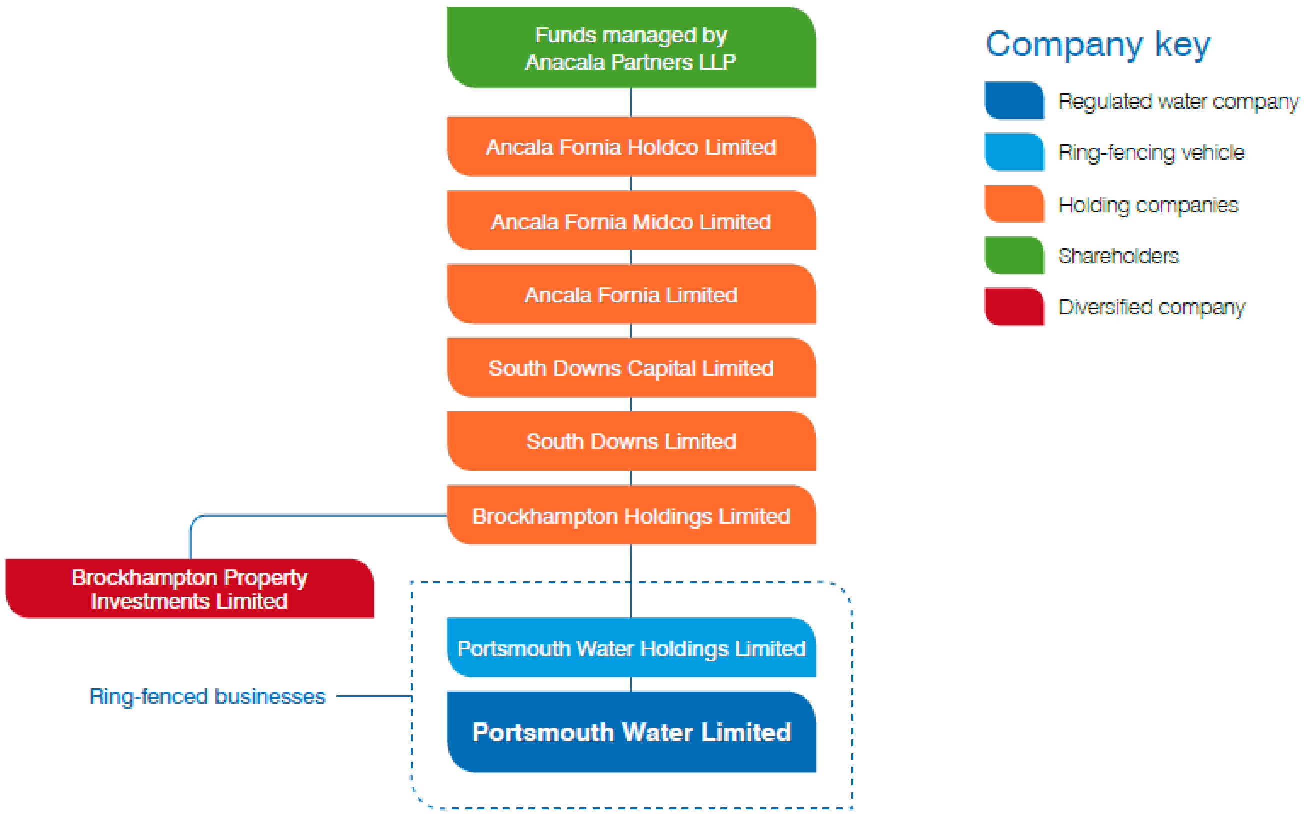
In 2014 Ofwat published the principles by which water companies should deal with Board leadership, transparency and governance. In March 2014 the Company adopted its own Governance Code which can be found on the Portsmouth Water website. The Board complies with the Ofwat principles in all areas.

Auditors

KPMG LLP were appointed as Auditors of the Portsmouth Water Group in 2017.

OWNERSHIP STRUCTURE

The following chart shows the ownership of the Company and the Group Structure. All companies are wholly owned by the parent company shown and all companies are domiciled in the UK for tax purposes.



Explanation of Ownership Structure

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

Ancala Partners LLP (“Ancala”) is a UK based infrastructure fund manager. Its investors are primarily UK corporate and local authority pension plans. The acquisition of South Downs Capital Limited in March 2018 was implemented by a new company, Ancala Fornia Limited, which is incorporated in the UK. The ultimate parent undertaking is Ancala Fornia Holdco Limited (“AFHL”) which is incorporated in the UK. The investors in AFHL comprise a number of investment vehicles, all focused primarily on UK and European pension plans and institutional investors with a long-term infrastructure investment horizon.

We consider AFHL to be the ultimate holding company and ultimate controlling entity. Consolidated group financial statements for the 54 weeks ending 31 March 2019 will be prepared at the level of Ancala Fornia Holdco Ltd and this will be the largest Group for which consolidated financial statements are prepared. Consolidated group financial statements were previously prepared at the level of South Downs Capital Limited (year ended 31 March 2018).

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

As part of development of the PR14 Business Plan the Company established six "outcomes" which are aligned to our Outcome Delivery Incentives ("ODIs") and many of which are established as Company Key Performance Indicators (KPIs). We also include metrics supporting our financial resilience. We have set out on pages 8 and 9 of our Annual Report and Accounts a summary of how our strategy aligns our Outcomes to KPIs and related risks, together with a summary of how these are delivered. Our measurement and trend of KPI performance is summarised on pages 10 and 11 of the ARA together with a clear indication of our performance.

During the year we have committed significant resource to preparation and submission of the PR19 Business Plan. This included significant activity at the Board level in setting the strategy and challenging the level of ambition. This was informed by ongoing engagement with customers across a wide range of topics and customer demographics. It was also informed by other stakeholders such as Ofwat, DEFRA, the EA, the DWI and local environmental groups.

The broad PR19 strategy leverages the Company's strong water resources position with plans to deliver increasing volumes of bulk water supply to our neighbouring water company, Southern Water. This will be delivered through an ambitious combination of reduced leakage, lower demand and the development (over 10 years) of the new water resource: Havant Thicket Winter Storage Reservoir. We have committed to a range of stretching service levels to customers including a 20% reduction in leakage, increasing support for vulnerable customers and lower interruptions to water supplies. We will deliver this for a lower bills at £97 in today's prices. Customer acceptance levels of our Business Plan, at 84%, was extremely high.

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

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

This drive to be an industry leader in customer service requires the Board to have a dynamic approach to managing the business and in setting ongoing strategy and making key business decisions. It also requires a close alignment between company objectives and executive remuneration. Company out-performance has generally been used to invest in service or asset improvement rather than payment to investors. The dividend policy has been reviewed and revised during the year in order to bring this in line with the policy to be applied in PR19. Further information on the dividend policy is set out in page 36.

As set out in the Annual Report and Accounts the Company has performed well against its KPIs in the majority of areas during the first four years of the Business Plan.

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

Levels of customer satisfaction remain high with continued upper quartile SIM performance (and having been the industry leader in the overall measure for 15/16 & 16/17 and joint second in 17/18) and high (95%) levels of developer satisfaction. Results for 2018/19 are yet to be finalised but initial scores indicate a continuing strong performance. As a member of the Institute of Customer Service we were also proud to hold the prestigious "Service Mark". However, we strive to achieve the levels of net promoter scores seen for top performing UK business such as John Lewis Partnership and Amazon. We continue to develop our Customer Service offering and are developing further services to enhance this.

In the majority of areas the Company performs consistently well and benchmarks in the upper quartile of the industry. This includes bursts, interruptions, SIM and water quality contacts. Although for the latter measure, whilst in 2018/19 we remained top industry performer, we fell below our target KPI.

We achieved all but three of our Outcome Delivery Incentives (ODI's). As noted above water quality contacts for colour, taste and appearance was over our target, but at a level which is the lowest in the Industry. Per capita consumption at 153l/h/d has, unfortunately, continued to increase and was adversely impacted by the long, dry summer in 2018. With a low level of meter penetration at 32% and an inability to compulsory meter customers, we have an increasing challenge to influence customer behaviours in relation to water usage. This will be an area where we will face challenges in the next regulatory review period and we are currently developing an innovative strategy to influence a reduction in water use by customers. Finally it was disappointing that in the early part of the year we had three accidents causing an individual to be off work for over 7 days. We reinforced health and safety messages and procedures as a consequence and had no further such events in the year.

Finally, performance in relation to key financial metrics is satisfactory and stable. In the Board's view this supports a business which continues to be financially resilient. The Company maintains a stable and transparent dividend policy in line with levels of expected notional equity returns.

On balance the Board's view is that the Company's overall performance is delivering for customers and stakeholders and that levels of executive remuneration and investor return are both appropriate and consistent with this level of company performance. Further detailed information on executive remuneration is set out on pages 15 and 16 of the APR and pages 46 to 51 of the ARA.

Financial Viability

The Company's financial position is set out in the ARA on pages 58 to 78, including cash flows, liquidity position, borrowing facilities and loan maturities. The Strategic Report, on pages 7 to 31 of the ARA, also covers aspects such as the overall financial performance and financial risks. Finally the Viability Statement on pages 32 to 34 of the ARA (and repeated on pages 9-11 below) sets out the factors considered and the conclusions reached by the Board in assessing both the going concern of the business over the period of 12 months from the balance sheet date and the prospects over a longer period of just under 7 years to the end of the next PR19 Business Plan.

Company's Assurance Process and Outcomes

The Company set out its approach to data assurance, including assurance over the APR, in its Final Audit Plan which was published on 24 April 2019. We have completed our data assurance in accordance with that plan and will publish a summary of the relevant results in the Data Assurance Summary which will be published in July 2019. The Board and the Audit Committee have considered the results of data assurance processes, together with the Company's proposed response to relevant findings, and are satisfied with the overall outcome.

1. Assessment of prospects
The Board has assessed the prospects of the Company over a period of 6 years.

Background information
The Company's business model and strategy are central to an understanding of its prospects, and further explanation can be found on page 7 of the ARA. As a regulated, capital intensive, utility provider the nature of the Company's activities are long-term and, although subject to some regulatory changes, the business model is generally stable. The Company's current overall strategy, budget and cash flow projections are intrinsically linked to the Ofwat 5 year regulatory review cycle. Consequently, the 5 year regulatory Business Plan (which runs from 1 April 2015 to 31 March 2020) and the related Ofwat Final Determination are the primary drivers for the Company's future prospects. The Final Determination sets out the allowed revenue, operating expenditure, capital expenditure and agreed business Outcomes for this 5 year period. More information in respect of the regulatory regime is set out in pages 26 to 29 of the ARA.

The Company is currently in the 2020-2025 regulatory Business Plan cycle with the plan being submitted in September 2018 together with further information submitted on 1 April 2019. Whilst this Draft Business Plan has not been approved, it does capture the Company's current business strategy into the next regulatory period together with detailed financial projections. The Company considers that this represents the best current indication of future operating activity and financial results at this time. This Draft Business Plan includes the development of a new water resource, Havant Thicket Winter Storage Reservoir ("HTWSR"), which will result in significant capital activity throughout the next 6 years and beyond to 2029.

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

The assessment process of the Company prospects

Budget process
The Company's prospects are routinely assessed, primarily, through its budget process and performance against regulatory Outcomes.

These are both closely linked to the 5 year financial position set out in the Ofwat Final Determination for the period 2015/16 to 2019/20 which drives the key budget assumptions.

The budget prepared included;
- Detailed budget analysis by department for the forthcoming (2019/20) financial period.
- Five year analysis to 2019/20 comprising 4 year actuals and 1 year detailed budget. These are compared against the Final Determination.
- Cash flow projections to 2019/20.
- Projection of key financial ratios including those required for banking covenants and to maintain an investment grade credit rating.

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

This assessment process involves an annual review of the budget (including financial projections through to the end of the current regulatory period) and related objectives, led by the CEO and Finance Director, through the Management Board. All Company departmental heads are involved in this review. A key part of this review is a comparison of the projected total operating and capital expenditure ("Totex") against that set out in the Ofwat Final Determination for the 5 year period. The Board participates fully in the annual process by means of the budget review and approval process, setting annual business objectives and strategy. The annual budget process was completed and approved by the Board during February 2019.

The key business assumptions in the budget related to;
- Increase in RPI (which drives tariffs and costs)
- Levels of capital and renewals spend and related efficiency and cost savings
- Headcount and salary increases
- Interest rates and loan indexation rates
- Levels of targeted cost savings
- Levels of activity and cost related to leakage
- Levels of activity relating to the HTWSR programme

5 year Business Plan process
In addition, the Company's prospects are also considered in relation to the financial modelling and overall Draft Business Plan submission to Ofwat supporting the determination for the Period 2020-2025.

The Development of the Draft Business Plan for submission is a detailed and complex process including the following activities;
- Customer research
- Capital assessment and planning
- Optimization of schemes & activities
- Detailed financial modelling
- Design of rewards & penalties
- Assessment of resilience
- Financeability testing
- Assurance
- Governance & Board approval

These activities culminated in the development of a detailed business plan in line with Ofwat's guidance & methodology.

The critical assumptions underpinning the business plan include;
- A WACC of 2.48% (RPI) /3.48% (CPI) including a company specific premium of 30 bps
- Totex benchmarking and efficiencies
- The inclusion of the HTWSR programme (and related income and costs)
- Capex and mains renewals levels and profile
- Projected RPI & CPI
- Levels of rewards & penalties
- Any historic true up required
- Distribution levels
- Inclusion of £5.4m of 'transition expenditure'
- Bill level & profile
- Availability of financing and access to additional equity and debt

In addition the Company has produced financial modelling of the business performance for a further 10 year period beyond the Business Plan. This is based, primarily, on a roll forwards of the Draft Business Plan, modified by key assumptions such as expected Weighted Average Cost of Capital (WACC), efficiency levels and longer term assumptions such as RPI and CPI levels. It also reflects the impact of HTWSR construction and operating costs.

The further assumptions in the additional 10 year projections relate to;
- A WACC of 3.1% and 3.3% real for successive 5 year periods plus a company specific premium of 30 bps.
- Projected RPI and CPI (which will be used to drive tariffs in future periods)
- Levels of efficiency projected
- Levels of capital and renewals spend together with assessment of the need for any significant new capital schemes.

Risk assessment
Alongside these activities, the Company also updates the analysis of significant risks that could prevent the budget and Outcomes from being delivered. The Board performs regular reviews of the principal risks and uncertainties and a formal annual review and a robust assessment was completed and approved in April 2019. As part of the Business Plan preparation the Company has performed an assessment of "resilience in the round" building from an understanding of operational risks through financial resilience and with regard to overall company resilience including Governance and management effectiveness. Board review and approval in relation to this assessment took place in April 2019. The overall summary of the principal risks and uncertainties (set out on pages 30 to 31 of the ARA) reflects this consideration of "resilience in the round".

Details of the Board risk assessment process are set out on page 43 of the ARA. The purpose of the principal risks table is, primarily, to summarise those matters that could prevent the Company from delivering on its strategy. A number of other aspects of the principal risks – because of their nature or potential impact – could also threaten the Company's ability to continue in business in its current form if they were to occur. This was considered as part of the assessment of the Company's viability, as explained further below.

In setting out specific scenarios for the Viability Statement we have reviewed the risk register together with resilience modelling prepared as part of the PR19 Business Plan together with Board analysis prepared to support "resilience in the round". Using this information we have developed a range of relevant severe, plausible and reasonable business scenarios which have been linked to the relevant business risks. These were reviewed and approved by the Board and are summarized in section 2 below.

The period of assessment
The Board conducted the assessment for a period of 6 years to 31 March 2025. The Board considers that this period of 6 years to be most appropriate given the current stage of the regulatory review cycle. This period covers the 1 year remaining of the current regulatory period and the period to the end of the next Price Review. This is consistent with the fact that, at this point, Ofwat's methodology for the next regulatory review cycle has been finalised and Company's Business Plan (for the 5 years to March 2025) has been submitted.

The Board feels that this is an appropriate length of time to permit a reasonable assessment of likely business performance and to make reasonable estimates of key assumptions. As set out above, the Ofwat Final Determination, the Business Plan and the related Outcomes are significant drivers of the business strategy & performance. This is a key driver to the end of the next regulatory period of 2025. Whilst the Board considers 6 years to be an appropriate horizon to consider the continuing viability of the Company, they do also consider the viability over a longer term beyond this period as indicated above.

2. Assessment of viability
The Assessment of Viability therefore uses a period of 1 year of budgeted information to the end of the current regulatory period and the 5 years of financial performance modelled in the Draft Business Plan to 31 March 2025.

Although the budget and Business Plan financial model reflect the Directors' best estimate of the future prospects of the business, they have also stress tested the potential impact on the Company of a number of scenarios. This has been performed by quantifying their financial impact and overlaying this on the financial forecasts. The potential impact has been considered in relation to operating profit, cash flow, liquidity and the key financial ratios needed for banking covenants and the retention of an investment grade credit rating (such as gearing, net debt:RCV and interest cover).

These scenarios (which are summarised below), which have been driven from the Boards assessment of "resilience in the round" as part of the Draft Business plan (and are reflected in the principal risks and uncertainties set out in pages 30 to 31 of the ARA) represent 'severe, plausible and reasonable' circumstances that the Company could experience.

In addition the Directors also tested a number of broad sensitivities including increase in interest rates, increase in costs and adverse movements in Retail Price Index/Consumer Price Index.

In each case the availability and effectiveness of mitigating actions that could reasonably be taken to reduce the impact was taken into account. The primary mitigating actions relate to the use of available credit facilities, levels of insurance cover, the ability to defer capital and renewals spend and the discretion not to pay dividends.

It has also been assumed that adverse impacts, set out on page 12, which may have an adverse but short lived (1 year) effect on financial ratios, could be managed by careful discussion with key stakeholders such as bond holders and the rating agencies.

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

3. Viability statement
Based on their assessment of prospects and viability above, the Directors confirm that they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the six year period ending 31 March 2025.

4. Going concern
The directors also considered it appropriate to prepare the financial statements on the going concern basis, as explained in the Basis of preparation paragraph in note 1 in the APR.

Summary of Viability Scenarios Tested			
Scenario	**Link to Risk**	**Outcome**	**Mitigation**
The loss of a significant Water Treatment Works	Operational, Financial, Business continuity	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.
A combination of 2 risk events (driven by operational risk scenario modelling)	Operational, Financial, Business continuity	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.
A £12m pension deficit arising	Financial	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by managing costs and additional debt finance.
A maximum one year ODI penalty	Regulatory, Financial	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.
A regulatory fine 3% turnover	Operational, Regulatory	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.
Loss of a critical IT system for one month in combination with two different scenarios;	Business continuity	Cash flow deficit and minor deterioration of interest cover ratios.	No mitigation needed on a stand-alone basis.
i) loss of a significant treatment works (see assumption above);	Operational, Financial, Business continuity	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.
ii) a £12m pension deficit arising.	Financial	Cash flow deficit and minor deterioration of interest cover ratios over the period of recovery.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.
An upper limit capital expenditure test of £20m	Financial, Operational	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by increasing RFF and raising additional debt.
Development of Havant Thicket Winter Storage Reservoir - Cost overrun	Financial, Operational	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.
Sensitivity testing of key assumptions - inflation -1% - WAAC to 2%	Financial	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Both mitigated by raising additional debt in the near term. In the longer term dividends may need to be restricted or equity injected to manage gearing (after 7+ years).
Development of Havant Thicket Winter Storage Reservoir - Delay	Financial, Operational	Cash flow deficit and deterioration of interest cover ratios below covenants & rating agency thresholds for one year.	Mitigated by short term restriction of infrastructure renewals activity and draw down on RCF.

Corporate Structure
The Group structure in which the Company resides, has recently changed and is set out on page 5. The Group is wholly owned by funds managed by Ancala Partners LLP ("Ancala") through a UK holding company Ancala Fornia Holdco Limited. Ancala is a UK based and domiciled independent infrastructure fund manager.

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

Governance in relation to UK taxation

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

Risk Management
Attitude towards tax planning and level of risk
Portsmouth Water Limited manages risks to ensure compliance with legal requirements in a manner which ensures payment of the correct amount of tax.

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

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

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

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

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

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

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

Corporate Criminal Offences Code of Conduct
Tax evasion, tax fraud and attempts to facilitate such actions are unethical and inconsistent with the ethos of Portsmouth Water. Portsmouth Water is committed to complying in full with the UK tax laws, and we expect everyone working with the Company to fully comply with their tax obligations. We believe in paying our fair share, and that everyone working with us should too.

Accountability & Governance
The board of our Company has approved a code of conduct policy and supports our commitment to no tolerance of tax evasion or its facilitation. The Finance and Regulation director is responsible for monitoring compliance with the policy and is supported by the Board and the management team in doing so.

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

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

Our commitment
Portsmouth Water is committed to the following principles:

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

Remuneration Committee

Role of Committee

The primary objective of the Committee is to set a policy to ensure that competitive reward packages are offered that will attract, retain and motivate talented senior executives to run the business effectively and to promote the success of the Company. Within these arrangements, a proportion of reward is based on performance against demanding targets. These targets are set by the Committee based on key strategic priorities benefiting customers, investors and other stakeholders and consistent with a Board approved level of risk.

Activities during the Year

During the year the Committee dealt with the following matters:

• Annual executive salary review and achievement of performance targets
• Determining performance targets in respect of 2018/19 annual incentive bonus plan
• Assisting with the appointment and remuneration of the new CEO taking into account the changing structure of the Executive Directorship and the additional responsibilities of both the new CEO and the Finance Director.

Remuneration Report

<u>Remuneration Policy</u>

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

<u>Service Contracts</u>

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

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

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

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

For full details of the Remuneration Report, including details of actual performance and amounts paid, see pages 46-51 of the ARA.

Link between Directors' Remuneration and Standards of Performance

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

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

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

By implementing the short and long-term elements of discretionary Executive remuneration the Board and the Remuneration Committee believes that there is appropriate balance between delivering the Outcomes for the AMP together with the flexibility to deliver any particular areas of business strategic focus. This permits a dynamic element of the approach to discretionary remuneration.

The executive incentive plan has been in operation in the business since 2010 and the overall objectives are reviewed on a quinquennial basis in line with the business planning cycle. The elements of the bonus structure are summarised below.

Annual Incentive Scheme – maximum 20% award

Maximum Percentage Award	Measure
Up to 5%	**Key customer service measures** (0.5% for each measure); MZC, interruptions, hosepipe restrictions, written complaints, abandoned calls, customer experience survey, PCC, bursts, leakage, water quality contacts.
Up to 5%	**Personal objectives**. These are linked to the Directors' own areas of responsibility and reflect strategic objectives of the Business. This includes a number of service measures and key programmes for the development and implementation of systems and processes to improve future performance.
Up to10 %	**Business objectives** (2% for each measure); TOTEX performance, financial resilience (gearing, interest cover ratio, & credit rating), overall ODI performance, zero reportable accidents, top SIM performer

Long term Incentive Scheme (5 years aligned to AMP)

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

Analysis of incentive award by nature

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

	Annual	Long term
Customer service related	9%	3.5%
Personal (including development and implementation of new systems and processes)	5%	
Other		
• Totex performance	2%	
• Financial resilience	2%	2%
• Health & Safety	2%	
• Overall ODI performance		4.5%
Total	**20%**	**10%**

Determination of performance

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

When personal objectives are set these follow the SMART approach for objective setting (Specific, Measureable, Achievable, Realistic and Time limited). As part of the Remuneration Committee's review these are challenged and agreed at the start of the objective setting process and supporting evidence is sought at the end of the assessment period before an award is made.

In this way the Board has confidence that the performance can be objectively assessed.

Summary of Directors' remuneration

A detailed report on Director's remuneration, including the operation of the incentive bonus scheme is set out in detail on pages 48 to 50 of the ARA.

Statement of Directors' Responsibilities

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

The Directors responsibilities are in accordance with the requirements;

Further to the requirements of Company Law the Directors are required to prepare accounting statements which comply with the requirements of Condition F of the Instrument of Appointment by the Secretary of State for the Environment, Food and Rural Affairs (Defra) and as a water undertaker under the Water Industry Act 1991; Regulatory Accounting Guidelines issued by Ofwat.

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

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business

The Directors are also responsible for:

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

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

Confirmation of disclosure of information to auditors

In so far as the Directors are aware:

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

Statement of Compliance with Licence Condition P – ring-fencing

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

(a) Portsmouth Water Limited will have available to it sufficient financial resources and facilities to enable it to carry out the Regulated Activities, for at least the next twelve months

(b) Portsmouth Water Limited will have available to it sufficient management resources and systems of planning and internal control to enable it to carry out the Regulated Activities, for at least the next twelve months; and

(c) all contracts entered into between Portsmouth Water and any Associated Company include the necessary provisions and requirements in respect of the standard of service to be supplied to the Appointee, to ensure that it is able to carry out the Regulated Activities.

In providing this Ring-fencing Certificate, the Board of Portsmouth Water has taken into account the following main factors.

- the Company's Final Determination at PR14 and the submitted Business Plan for PR19;
- the latest financial position as set out in the Company's Annual Report and Accounts and the most recent management accounts;
- the results of analysis carried out in relation to the Company Viability Statement;
- the approved budget and capital expenditure programme for the year ended 31 March 2020;
- cash balances of £27.2m and available unused term facilities of £5m as at 31 March 2019;
- the current level of gearing together with the projected level of headroom on key covenant ratios through to 31 March 2020;

- a stable and experienced senior management team, with a wide knowledge of the water industry together with a skilled and motivated workforce; and
- appropriate risk management and governance arrangements.

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

Statement of Compliance of Licence Requirement Condition K

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

Statement of Compliance with Regulatory Accounting Guideline 5

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

Statement on Risk & Compliance

The Directors confirm that the Company, in their opinion:

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

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

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

The risk management, monitoring and control systems and processes upon which the Directors rely in making this statement are described in the Company's Annual Report and Accounts within the Strategic Report on pages 30 and 31 and the Corporate Governance Report on page 38.

Signed by:

M P Kirk

C R Taylor

H M G Orton

M P Johnson

M R Coffin

D W Owens

SECTION 1 REGULATORY FINANCIAL REPORTING

1A INCOME STATEMENT

For the 12 months ended 31 March 2019

		Current year				
			Adjustments			
	Note	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
		£'000	£'000	£'000	£'000	£'000
Revenue	2	42,161	(1,796)	175	(1,971)	40,190
Operating costs	3	(34,235)	0	117	(117)	(34,352)
Other operating income	4	(494)	0	0	0	(494)
Exceptional items:						
National Insurance cost relating to exercise of share options	24	(2,422)	0	0	0	(2,422)
Operating profit/(loss)		5,010	(1,796)	292	(2,088)	2,922
Other income	5	0	1,796	0	1,796	1,796
Interest income	6	957	0	0	0	957
Interest expense	7	(7,444)	0	0	0	(7,444)
Other interest income	6	762	0	0	0	762
(Loss)/Profit before tax and fair value movements		(715)	0	292	(292)	(1,007)
Fair value gains/(losses) on financial instruments		0	0	0	0	0
(Loss)/Profit before tax		(715)	0	292	(292)	(1,007)
UK Corporation tax	8	140	0	0	0	140
Deferred tax	8	(147)	0	0	0	(147)
(Loss)/Profit for the year		(722)	0	292	(292)	(1,014)
Dividends	9	3,076		292	(292)	2,784

Tax Analysis

	Note	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
Current Year	8	0	0	0	0	0
Adjustments in respect of prior years	8	140	0	0	0	140
UK Corporation Tax		140	0	0	0	140

1B STATEMENT OF COMPREHENSIVE INCOME

For the 12 months ended 31 March 2019

Current year

	Note	Statutory	Adjustments: Differences between statutory and RAG definitions	Adjustments: Non-appointed	Adjustments: Total adjustments	Total appointed activities
		£'000	£'000	£'000	£'000	£'000
(Loss)/Profit for the year		(722)	0	292	(292)	(1,014)
Actuarial gains/(losses) on post-employment plans	22	(1,170)	0	0	0	(1,170)
Other comprehensive income	20	199	0	0	0	199
Total Comprehensive income for the year		(1,693)	0	292	(292)	(1,985)

1C STATEMENT OF FINANCIAL POSITION

As at 31 March 2019

		Current year				
			Adjustments			
	Note	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
		£'000	£'000	£'000	£'000	£'000
Non-current assets						
Fixed assets	10	136,136	0	0	0	136,136
Intangible assets	11	1,116	0	0	0	1,116
Investments - loans to group companies	12	55,484	0	0	0	55,484
Investment Properties		325	0	0	0	325
Retirement benefit assets	22	23,782	0	0	0	23,782
Total non-current assets		216,843	0	0	0	216,843
Current assets						
Inventories		419	0	0	0	419
Trade & other receivables	13	8,933	0	458	(458)	8,475
Investments - other	14	2	0	0	0	2
Cash & cash equivalents	15	27,210	0	0	0	27,210
Total current assets		36,564	0	458	(458)	36,106
Current liabilities						
*Trade & other payables	17	(13,440)	0	(458)	458	(12,982)
Capex creditor	17	(2,356)	0	0	0	(2,356)
Borrowings	16	(10,284)	0	0	0	(10,284)
Current tax liabilities	17	(9,281)	0	0	0	(9,281)
Provisions	17	(1,412)	0	0	0	(1,412)
Total current liabilities		(36,773)	0	(458)	458	(36,315)
Net Current assets/(liabilities)		(209)	0	0	0	(209)
Non-current liabilities						
Borrowings	18	(106,709)	0	0	0	(106,709)
Deferred income - G&C's	19	(27,138)	0	0	0	(27,138)
Deferred tax	20	(6,919)	0	0	0	(6,919)
Total non-current liabilities		(140,766)	0	0	0	(140,766)
Net assets/(liabilities)		75,868	0	0	0	75,868
Equity						
Called up share capital	21	1,078	0	0	0	1,078
Retained earnings & other reserves	21	74,790	0	0	0	74,790
Total Equity		75,868	0	0	0	75,868

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

For the 12 months ended 31 March 2019

		Current year				
			Adjustments			
	Note	Statutory	Differences between statutory and RAG definitions	Non-appointed	Total adjustments	Total appointed activities
		£'000	£'000	£'000	£'000	£'000
Operating profit		5,010	(1,796)	292	(2,088)	2,922
Other income		0	1,796	0	1,796	1,796
Depreciation		5,866	0	0	0	5,866
Amortisation - G&C's		(646)	0	0	0	(646)
Changes in working capital		(1,564)	0	0	0	(1,564)
Notional Pension Costs		811	0	0	0	811
Movement in provisions		(174)	0	0	0	(174)
Loss on sale of fixed assets		494	0	0	0	494
Cash generated from operations		9,797	0	292	(292)	9,505
Net interest paid		(3,073)	0	0	0	(3,073)
Tax paid		0	0	0	0	0
Net cash generated from operating activities		6,724	0	292	(292)	6,432
Investing activities						
Capital expenditure		(14,008)	0	0	0	(14,008)
Grants & Contributions		1,404	0	0	0	1,404
Disposal of fixed assets		0	0	0	0	0
Other		0	0	0	0	0
Net cash used in investing activities		(12,604)	0	0	0	(12,604)
Net cash generated before financing activities		(5,880)	0	292	(292)	(6,172)
Cashflows from financing activities						
Equity dividends paid		(3,076)	0	(292)	292	(2,784)
Equity payment received		2,422	0	0	0	2,422
Net loans received		7,000	0	0	0	7,000
Net cash generated from financing activities		6,346	0	(292)	292	6,638
Increase in net cash		466	0	0	0	466

1E NET DEBT ANALYSIS (Appointed activities)

As at 31 March 2019

	Interest rate risk profile			
	*Fixed rate	Floating rate	Index linked	Total
	£'000	£'000	£'000	£'000
Borrowings (excluding preference shares)	284	10,000	107,476	117,760
Preference share capital				0
Total borrowings	284	10,000	107,476	117,760
**Cash				(18,190)
Short term deposits				0
Net Debt	284	10,000	107,476	99,570
Gearing				66.34%
Adjusted Gearing				n/a
Full year equivalent nominal interest cost (£m)	0.010	0.240	6.631	6.881
Full year equivalent cash interest payment (£m)	0.010	0.240	3.867	4.117
Indicative interest rates				
Indicative weighted average nominal interest rate	3.52%	2.40%	6.17%	5.84%
Indicative weighted average cash interest rate	3.52%	2.40%	3.60%	3.50%
Weighted average years to maturity	25	< 1	13	13

* Perpetual Debt

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

Total Borrowings difference between 1C and 1E is the deferred arrangement costs of £0.767m on the index linked debt.

For the 12 months ended 31 March 2019
(2012/13 financial year average RPI)

	Units	% Notional returns and notional regulatory equity	% Actual returns and notional regulatory equity	% Actual returns and actual regulatory equity	£ Notional returns and notional regulatory equity	£ Actual returns and notional regulatory equity	£ Actual returns and actual regulatory equity
*Return on regulatory Equity	%	5.70%	5.41%	5.70%	2,732,124	2,593,690	2,593,690
Actual performance adjust. 2010/15	%	1.82%	1.73%	1.82%	872,362	828,161	828,161
Adjusted return on regulatory equity	%	7.52%	7.14%	7.52%	3,604,486	3,421,851	3,421,851
Regulatory Equity Base	£	47,932,000	47,932,000	45,503,341			
Financing							
Gearing	%	0.00%	0.19%	0.20%	0	90,211	90,211
Variance in corporation tax	%	0.00%	0.91%	0.95%	0	434,000	434,000
Group relief	%	0.00%	0.00%	0.00%	0	0	0
Cost of debt	%	0.00%	-2.36%	-2.58%	0	(1,130,989)	(1,175,710)
Hedging instruments	%	0.00%	0.00%	0.00%	0	0	0
Sub total	%	7.52%	5.87%	6.09%	3,604,486	2,815,073	2,770,352
Operational Performance							
Totex out / (under) performance	%	0.00%	-1.17%	-1.23%	0	(560,000)	(560,000)
ODI out / (under) performance	%	0.00%	0.00%	0.00%	0	0	0
Retail out / (under) performance	%	0.00%	-0.13%	-0.14%	0	(62,000)	(62,000)
Other exceptional items	%	0.00%	0.00%	0.00%	0	0	0
Sub Total	%	0.00%	-1.30%	-1.37%	0	(622,000)	(622,000)
Total earnings	%	7.52%	4.58%	4.72%	3,604,486	2,193,073	2,148,352
RCV growth from RPI inflation	%	3.06%	3.06%	3.06%	1,466,034	1,466,034	1,391,752
Total shareholder return	%	10.58%	7.63%	7.78%	5,070,520	3,659,107	3,540,104
Net dividend	%	4.00%	3.30%	3.48%	1,917,280	1,581,479	1,581,479
Retained Value	%	6.58%	4.33%	4.30%	3,153,240	2,077,628	1,958,625
Dividends reconciliation							
Gross Dividend	%	4.00%	5.02%	5.28%	1,917,280	2,404,608	2,404,608
Interest Receivable on Intercompany loans	%	0.00%	1.72%	1.81%	0	823,129	823,129
Net dividend	%	4.00%	3.30%	3.48%	1,917,280	1,581,479	1,581,479

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

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

	Units	%			£		
		Notional returns and notional regulatory equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity	Notional returns and notional regulatory equity	Actual returns and notional regulatory equity	Actual returns and actual regulatory equity
*Return on regulatory Equity	%	5.79%	5.09%	5.79%	2,683,535	2,360,747	2,360,747
Actual performance adjust. 2010/15	%	1.00%	0.88%	1.00%	463,478	407,728	407,728
Adjusted return on regulatory equity	%	6.79%	5.97%	6.79%	3,147,012	2,768,475	2,768,475
Regulatory Equity Base	£	46,347,750	46,347,750	40,772,835			
Financing							
Gearing	%	0.00%	0.35%	0.40%	0	162,065	162,065
Variance in corporation tax	%	0.00%	0.07%	0.08%	0	31,178	31,178
Group relief	%	0.00%	0.12%	0.14%	0	57,070	57,070
Cost of debt	%	0.00%	-2.05%	-2.50%	0	(951,375)	(1,018,537)
Hedging instruments	%	0.00%	0.00%	0.00%	0	0	0
Sub total	%	6.79%	4.46%	4.91%	3,147,012	2,067,413	2,000,251
Operational Performance							
Totex out / (under) performance	%	0.00%	0.31%	0.36%	0	145,250	145,250
ODI out / (under) performance	%	0.00%	-0.01%	-0.01%	0	(4,250)	(4,250)
Retail out / (under) performance	%	0.00%	-0.99%	-1.13%	0	(460,500)	(460,500)
Other exceptional items	%	0.00%	0.00%	0.00%	0	0	0
Sub Total	%	0.00%	-0.69%	-0.78%	0	(319,500)	(319,500)
Total earnings	%	6.79%	3.77%	4.12%	3,147,012	1,747,913	1,680,751
RCV growth from RPI inflation	%	2.50%	2.50%	2.50%	1,159,278	1,159,278	1,019,835
Total shareholder return	%	9.29%	6.27%	6.62%	4,306,290	2,907,191	2,700,586
Net dividend	%	4.00%	2.64%	3.00%	1,853,910	1,222,466	1,222,466
Retained Value	%	5.29%	3.63%	3.63%	2,452,380	1,684,725	1,478,120
Dividends reconciliation							
Gross Dividend	%	4.00%	4.43%	5.03%	1,853,910	2,052,444	2,052,444
Interest Receivable on Intercompany loans	%	0.00%	1.79%	2.04%	0	829,978	829,978
Net dividend	%	4.00%	2.64%	3.00%	1,853,910	1,222,466	1,222,466

COMMENTARY

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

- The notional returns on Regulatory Equity are taken from the Ofwat FD Risk Assessment Tool, adjusted from 2017/18 to exclude the return for the Non-Household Retail business.
- The notional regulatory equity values are taken from Ofwat's documents "Appointee Regulatory Equity", for each year. These documents also include the actual regulatory equity values up to 2017/18.
- The gearing and cost of debt calculations use the RCV numbers published by Ofwat in 'Regulatory Capital Values', in each year. The gearing calculation adjusts the actual return on net debt by the July RPI movement, in line with the actual loan arrangements.
- Actual returns exclude exceptional items relating to the sale of the non-household business operations (note 25) and exceptional costs relating to the disposal of the business (note 24).

Variances between the Final Determination and the results for 2018/19
We have considered the significant variances arising between the return assumed in the Final Determination and the actual return for 2018/19. In overall terms the ***actual*** total shareholder return of £3.5m and net dividend paid of £1.6m both fall below the notional total shareholder return of £5.1m and notional net dividend paid of £1.9m based upon the Final Determination.

The material differences are driven by;
- higher gearing than the notional company
- lower corporation tax charges than assumed in the Final Determination
- higher cost of debt than allowed in the Final Determination
- operational under performance
- lower net dividend levels than assumed in the Final Determination

Gearing
Actual gearing of 66.3% is above the notional gearing of 62.5% by 3.8 percentage points. This has two implications. Firstly it results in a lower regulatory Equity Base as regulatory equity % (the reciprocal of gearing) is lower in the actual structure (actual equity 33.7% versus notional equity of 37.5%). Secondly it results in a benefit of £0.09m due to a higher allowed cost of debt.

Corporation Tax
(Amounts in 2012/13 prices)

	£'000
Allowed corporation tax charge in FD	148
Actual Corporation tax credit on appointed activities	(165)
Variance	(313)
Minus variance arising from prior year adjustment	(121)
Total variance (favourable)	(434)

There is a favourable tax difference to the FD in the year as a result of an actual loss before tax in 2018/19 and claims for R&D tax credits together with a tax adjustment relating to prior years. Further analysis of tax is set out in note 8.

Cost of debt
The Company's actual cost of debt of 3.64% (index linked) exceeds the allowed cost of debt, together with the slightly higher gearing levels (noted above) this results in a £1.2m reduction in financial returns.

Totex under performance
See commentary relating to Table 4B on page 63.
The 2018/19 variance on capital expenditure is shown as -£3,559k, on page 62, but is virtually eliminated in this analysis as it is a result of timing differences. The remaining adverse variance relates to operating costs and is mainly the increase in leakage recovery expenditure in the year.

Retail out/under performance
The 2018/19 Household Retail expenditure is broadly in line (but slightly above) the FD.

Cumulative variances for the price review to date
The material elements of the cumulative variances are also consistent with the significant factors explained above.

In relation to Totex, in the AMP to date, there is a favourable variance mainly due to the efficiency in renewals expenditure. However, this variance will be eliminated in the final year of the AMP as the Company plans to reinvest this saving in additional schemes.

The retail variance for the AMP to date is adverse by £460k. This is partly due to an increase in the provision for doubtful debts overall of around £200k. Also, there is an adverse impact from the change in the allocation method for General rates, which is partially offset by a decrease in other shared services costs.

For the year ended 31 March 2019

	Statutory £'000	Regulatory £'000	Commentaries
INCOME STATEMENT			
Revenue	42,161	40,190	See a) below
Operating profit	5,010	2,922	See b) below
STATEMENT OF FINANCIAL POSITION			
Tangible fixed assets (net book value)	136,136	136,136	See c) below

a) The difference relates to the way these figures have been presented in both sets of accounts. In the ARA, this figure includes amortisation of Developer Contributions and income from Connection Charges. In addition, there is non-appointed revenue of £0.001m, which relates to Commercial Water Efficiency, and £0.174m, which is income from the sale of the Non-Household business, and relates to meter reading services. All of these amounts are excluded from the Regulatory revenue.

	£'000
Statutory revenue	42,161
Amortisation of Developer Contributions	(646)
Income from Connection Charges	(1,150)
Non-appointed revenue	(1)
Non-appointed meter reading revenue	(174)
Regulatory revenue	40,190

b) The difference relates to the way these figures have been presented in both sets of accounts, as well as the inclusion of non-appointed business in the ARA. In the ARA, this figure includes other income of £1.796m, but this is reported after operating profit in the APR. The breakdown of this income is shown below.

There is a non-appointed operating profit of £0.001m, which relates to Water Efficiency, as well as a number of other non-appointed items relating to rental properties and the sold Non-Household Retail Business. These are excluded from Regulatory operating profit.

	£'000
Statutory operating profit	5,010
Amortisation of Developer Contributions	(646)
Income from Connection Charges	(1,150)
Non-appointed operating profit	(1)
Non-appointed meter reading revenue	(174)
Non-appointed Rental Income	(145)
Non-appointed Home Assistance	(1)
Non-Household meter reading costs	29
Regulatory operating profit	2,922

c) N/A

1 ACCOUNTING POLICIES

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

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

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

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

(a) Revenue

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

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

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

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

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

Differences between Statutory and Regulatory accounts
Non-appointed income is included within turnover in the statutory accounts but is excluded from turnover in the APR.

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

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

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

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

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

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

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

(b) Fixed assets

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

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

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

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

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

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

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

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

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

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

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

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

(c) Investment properties

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

(d) Capital contributions

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

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

(e) Stocks

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

(f) Taxation

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

Deferred tax is recognised on all timing differences where the transactions or events that give the company an obligation to pay more tax in the future, or the right to pay less tax in the future, have occurred by the statement of financial position date. Deferred tax assets are recognised when it is 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 statement of financial position date.

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

(g) Leases

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

(h) Pension costs and other post-retirement benefits

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

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

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

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

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

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

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

(i) Financial instruments

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

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

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

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

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

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

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

The Company subsequently categorises financial instruments as follows:

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

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

Investments
Investments consist of non-current and current investments.

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

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

(j) Provisions

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

(k) Cost allocation policies

Accounting Separation

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

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

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

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

ANNUAL PERFORMANCE REPORT - BUSINESS UNIT TABLES
2018/19

	BASIS OF ALLOCATION
DIRECT COSTS	
Employment Costs	Direct and management estimate
Power	Pumping Head
Hired & Contracted Services	Direct
Materials & Consumables	Direct
Service Charges	Direct
Other Direct Costs	Direct
GENERAL & SUPPORT ACTIVITIES	
Land & Property	Direct and prorata on direct
Mechanical & Electrical	Direct and prorata on direct
Supply Engineer	M&E basis
Supply General	Direct
Distribution General & Admin	Direct
Personnel Services	FTE's
Legal & Property	FTE's
Financial Services	FTE's
Directors	Time on activities and Board Agenda
Data processing	No. of computers & mobile devices
Operational / Technical Support	GMEAV of asset additions
Vehicles & Plant	No of vehicles
Stores	Direct material costs
GENERAL ADMIN	
Directly identifiable items	Direct
Other General Admin	Direct/Floor space/FTE's
Other Business Activities	Direct/1/5 per Business Unit
Scientific Services	Quality samples
Doubtful Debts	Direct
General Rates	Floor space
Bulk Supply	Direct
Third Party Costs (RCW)	Direct
Renewals Expensed	Direct

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

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

Information on critical accounting judgements and key sources of estimation uncertainty can be found on page 69 of the Annual Report and Accounts.

2. REVENUE

	Appointed 2019 £000	Non Appointed 2019 £000	Total 2019 £000	Appointed 2018 £000	Non Appointed 2018 £000	Total 2018 £000
Unmeasured household supplies	21,148	-	21,148	21,017	-	21,017
Measured household supplies	9,678	-	9,678	8,861	-	8,861
Non-household supplies	8,757	-	8,757	8,671	-	8,671
Third party services	556	175	731	294	343	637
Other sources	51	-	51	94	-	94
	40,190	175	40,365	38,937	343	39,280

Measured Income Accrual

For the year 2017/18 the measured income accrual was £2,207,453, and the corresponding actual billed revenue was £2,303,819. This is a difference of £96,366.

3. ANALYSIS OF OPERATING COSTS

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

	Appointed 2019 £000	Non Appointed 2019 £000	Total 2019 £000	Appointed 2018 £000	Non Appointed 2018 £000	Total 2018 £000
Manpower costs	10,272	29	10,301	10,644	29	10,673
Other costs of employment	438	-	438	297	-	297
Power	2,659	-	2,659	2,323	-	2,323
Rates	2,487	-	2,487	2,316	-	2,316
Hired and contracted services	5,669	-	5,669	3,950	-	3,950
Materials and consumables	2,220	-	2,220	1,397	-	1,397
Service charges	1,319	-	1,319	1,322	-	1,322
Renewals expensed	2,580	-	2,580	2,851	-	2,851
Provision for bad and doubtful debts	544	-	544	795	316	1,111
Other operating costs	299	(146)	153	214	22	236
Depreciation and Amortisation	5,865	-	5,865	6,409	-	6,409
	34,352	(117)	34,235	32,518	367	32,885

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

	2019 £000	2018 £000
Manpower as reported	10,272	10,644
Notional Pension Cost	(811)	(866)
Manpower Cost for Efficiency and Price Determination purposes	9,461	9,778

4. OTHER OPERATING INCOME

	Appointed 2019 £000	Non Appointed 2019 £000	Total 2019 £000	Appointed 2018 £000	Non Appointed 2018 £000	Total 2018 £000
Loss arising on disposal of fixed assets	(494)	-	(494)	(16)	-	(16)

5. OTHER INCOME	Appointed 2019 £000	Non Appointed 2019 £000	Total 2019 £000	Appointed 2018 £000	Non Appointed 2018 £000	Total 2018 £000
Amortisation of Developer Contributions	646	-	646	638	-	638
S45 Connection Charges	1,150	-	1,150	571	-	571
	1,796	-	1,796	1,209	-	1,209

6. INTEREST INCOME	2019 £000	2018 £000
Loan to Group Company	953	832
Interest on short term deposits	4	9
	957	841
Other Interest Income (see note 22)	762	346

7. INTEREST EXPENSE		2019 £000	2018 £000
£66.5m loan	- interest	3,867	3,733
	- indexation	3,357	3,624
	- amortisation of fees	57	57
	- administration expenses	131	92
		7,412	7,506
Other bank loans and overdraft		10	84
Debenture stocks		10	10
Other interest payable		12	3
		7,444	7,603

8. TAXATION (APPOINTED BUSINESS ONLY)	2019 £000	2018 £000
Current tax		
United Kingdom corporation tax at 19% (2018 - 19%)	-	50
Group relief	-	-
Adjustment in respect of prior periods	(140)	-
	(140)	50
Deferred tax		
Origination and reversal of timing differences	302	(89)
Effect of change to corporation tax rate	-	-
Difference between pension cost charge and pension cost relief	-	-
Adjustment in respect of prior periods	(155)	61
	147	(28)
Tax on loss on ordinary activities	7	22

8. TAXATION (APPOINTED BUSINESS ONLY) (continued)

	2019 £000	2018 £000
The tax charge for the year is lower (2018 - higher) than the standard rate of Corporation tax in the UK of 19% (2018 - 19%), explained as follows:		
Loss on ordinary activities before tax	(1,007)	51
*Less EBT payment (RAG differences) (deductible)	-	(1,267)
Loss before tax (taxable)	(1,007)	(1,216)
Loss on ordinary activities multiplied by standard rate of corporation tax in the UK of 19% (2018 - 19%)	(191)	(231)
Effect of:		
Depreciation on assets not qualifying for capital allowances	64	173
Other tax adjustments (including effect of change in tax rate)	20	9
Difference between pension cost charged and relieved	-	99
Prior year adjustments	(140)	-
Expenses not deductible for tax purposes	107	-
Current tax charge/(credit) for the year	(140)	50

*There are no further payments to employees as beneficiaries under the EOT since the sale of the Company in March 2018.

RECONCILIATION BETWEEN CURRENT TAX CHARGE AND CURRENT TAX IN PRICE LIMITS

	Note	Statutory Accounts £'000	Non-Appointed £'000	Appointed £'000	Final Determination £'000	Tax Difference @19% £'000
Profit before tax	1	(715)	292	(1,007)	3,251	809
Ofwat adjustments gearing	1				(1,452)	(276)
PBT adjusted for gearing	1	(715)	292	(1,007)	1,799	533
Add depreciation	2	5,865		5,865	3,976	(359)
Less Capital allowances		(6,372)		(6,372)	(5,830)	103
Pensions difference		359		359	161	(38)
Other adjustments	3	259		259	300	8
Tax losses utilised in the period	4		(292)	292		(55)
Tax losses carried forward	5	604		604		(115)
Adjusted profit chargeable to CT		0	0	0	406	77
@ tax rate 19%						
Current Tax charge		0	0	0	77	
Prior year adjustment	6	(140)		(140)		
		(140)	0	(140)		

We have analysed the differences between the current tax charge of -£0.140m for the appointed business against the tax charge calculated in the Final Determination of £0.077m. The significant movements are as follows:

1. Loss before tax of -£1.007m is lower than the FD profit of £3.2m. However, this should be further adjusted for by a charge of £1.5m which relates to the Ofwat net tax adjustment for gearing. This reflects the higher actual finance cost when compared to the notional finance cost included in the FD.
2. Actual depreciation outturn is higher than estimated in the Business Plan submission.
3. Some differences in disallowable expenses.
4. Non-trading losses utilised against non-trading, non-regulated profits.
5. Trading tax losses carried forward for use in future periods
6. Prior year current tax adjustment – tax credit arising from R&D tax claim.

9. DIVIDENDS

Equity: Ordinary/'A' Ordinary

	2019 £000	2018 £000
Interim paid	3,076	544
Final paid	-	546
Total Dividends	3,076	1,090

The Directors are proposing the payment of a final dividend of £1.975m for the year ended 31 March 2019. This dividend has not been accounted for within the current year financial statements, as it has yet to be approved.

Dividend Policy
The Company's dividend policy covers two elements. The first element is a dividend which is paid to shareholders. The second part of the dividend is the payment to cover the servicing of intercompany debt; interest due from South Downs Limited on a loan from Portsmouth Water. This element of the dividend is effectively recirculated.

Revision of the dividend policy
Following the change in ownership of the group and concurrent with the guidance set out in the "putting the sector into balance" consultation and the development of the PR19 Business Plan the Board took the decision to amend the dividend policy. The policy adopted is consistent with that proposed for the PR19 Business Plan and further details in this regard are set out below.

The Board has committed to maintaining a fair, sustainable and transparent dividend policy, which is reflective of the business performance and of delivery for customers. The revised dividend policy is entirely consistent with that proposed for PR19 and was developed by considering all relevant factors – particularly performance against Company promises to customers, long-term resilience, financeability, wider obligations and responsibilities to stakeholders.

The dividend policy is based upon the following relevant factors;

- For the appointed business a base level of dividend, calculated using a 5% dividend yield on regulatory equity value.
- At the Board's discretion, and transparently communicated to stakeholders, the base dividend will be adjusted to reflect wider performance factors such as performance in relation to service levels and ODI measures. Any such adjustments will be clearly set out in the Annual Performance Report in the form of a table reconciling between base dividend and actual dividend and explaining each material adjustment (including its linkage the relevant service levels and ODI performance). Consideration will be given as to whether any outperformance should be shared with customers. Should the business underperform, consideration and challenge will be given as to whether further investment is required to achieve Outcomes for customers and to improve long-term resilience. This may in turn necessitate a reduction in dividend and/or further external investment.
- The dividend may be increased to reflect any amounts which are paid solely to allow the servicing of intercompany debt and to the extent that such dividend will be recycled to the company as interest income.
- The financial performance of the non-appointed parts of the Portsmouth Water Limited may also be considered in determining the overall dividend at the level of the statutory entity.

The Board is committed to considering these factors in declaring a dividend and in transparently reporting, the dividend policy, the factors that have been considered in determining the dividend and how these relate to the dividend declared.

In calculating the dividend paid and proposed for the financial year the Company has taken account of the following elements;

- a 5% base dividend yield on regulatory equity value
- a payment to allow for the servicing of intercompany debt
- no element of adjustment has been made to the based dividend to reflect company performance levels or out-performance

There are no payments to employees, as they are no longer beneficiaries under the Employee Ownership Trust.

	2019 £000	2018 £000
Dividend ultimately for group shareholders	2,626	422
Employee Ownership Trust	-	1,267
Servicing of intercompany debt net of tax	450	668
Total Dividends	3,076	2,357

10. TANGIBLE FIXED ASSETS

	Freehold land, buildings & reservoirs Restated £'000	Mains Restated £'000	Pumping Plant £'000	Vehicles, mobile plant & office equipment £'000	Total Restated £'000
COST					
At 1st April 2018	55,300	60,639	52,001	20,358	188,298
Additions	3,264	3,718	4,220	3,571	14,773
Impairment	(253)	-	-	-	(253)
Disposals	-	(184)	-	(462)	(646)
At 31st March 2019	**58,311**	**64,173**	**56,221**	**23,467**	**202,172**
DEPRECIATION					
At 1st April 2018	13,532	4,861	28,254	14,715	61,362
Charge for year	529	1,114	1,901	1,655	5,199
Disposals during year	-	(80)	-	(445)	(525)
At 31st March 2019	**14,061**	**5,895**	**30,155**	**15,925**	**66,036**
NET BOOK VALUE					
At 31st March 2019	**44,250**	**58,278**	**26,066**	**7,542**	**136,136**
At 1st April 2018	41,768	55,778	23,747	5,643	126,936

ASSETS IN THE COURSE OF CONSTRUCTION
Included in the above table are assets in the course of construction as follows:

	Freehold land, buildings & reservoirs £'000	Mains £'000	Pumping Plant £'000	Vehicles, mobile plant & office equipment £'000	Total £'000
COST					
At 1st April 2018	803	2,257	(184)	55	2,931
Additions	3,339	4,225	4,205	2,646	14,415
Transferred into fixed assets	(260)	(3,541)	(4,843)	(2,670)	(11,314)
At 31st March 2019	**3,882**	**2,941**	**(822)**	**31**	**6,032**
DEPRECIATION					
At 1st April 2018	-	-	-	-	-
Charge for year	-	-	-	-	-
At 31st March 2019	-	-	-	-	-
NET BOOK VALUE					
At 31st March 2019	**3,882**	**2,941**	**(822)**	**31**	**6,032**
At 1st April 2018	803	2,257	(184)	55	2,931

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

11. INTANGIBLE FIXED ASSETS

	Software, Consultancy and Internal Costs £'000
COST	
At 1st April 2018	2,923
Additions (WIP completed assets)	112
Disposals	(5)
At 31st March 2019	**3,030**
AMORTISATION	
At 1st April 2018	1,249
Disposals	(2)
Charge for year	667
At 31st March 2019	**1,914**
NET BOOK VALUE	
At 31st March 2019	**1,116**
At 1st April 2018	1,674

Intangible fixed assets primarily comprise software costs and the in house development of bespoke software and related IT solutions. Included in the numbers above is £0.112m of assets in the course of construction, which relates to the development of new software for the Drinking Water Safety Plan.

12. FIXED ASSET INVESTMENT

	Loan to Group Undertakings £000
At 1 April 2018	55,484
	-
At 31 March 2019	55,484

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

13. DEBTORS

	2019 £000	2018 £000
Trade debtors	3,070	3,510
*Amounts owed by Group companies	960	143
Prepayments and accrued income	3,714	3,343
Other debtors	731	537
	8,475	7,533

* Amounts owed by Group companies excludes the notional intercompany payable relating to the deferred income for Non-household meter reading, which is non-appointed. 2018 has been restated to include this adjustment of £0.631m.

All of the above amounts fall due within one year. Included within other debtors is corporation tax recoverable of £0.271m. (2018 - £0.200m)

As at 31 March 2019, trade debtors had a carrying value of £7.706m (2018 - £8.090m) before provision for bad debt. Trade debtors in arrears are provided for on a sliding scale depending on age of debt. The amount of the provision was £4.636m as at 31 March 2019 (2018 - £4.580m).

The ageing of these debtors was as follows:

	2019 £000	2018 £000
Up to 12 months	3,690	4,304
Over 12 months	4,016	3,786
	7,706	8,090

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.

Movement on the provision for bad debt are as follows:

	2019 £000	2018 £000
As at 1 April 2018	4,580	3,883
Provision for bad debt required in the year	544	1,111
Debt written off in the year as uncollectable	(488)	(414)
As at 31 March 2019	4,636	4,580

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

	2019 £000	2018 £000
Total Debtors Outstanding > 30 days		
- Household	5,564	5,471

Write Off Policy
Our bad debt write off policy has not changed within the period under review. However, we no longer report on Non-household customers, since the sale of the Retail business on 1 April 2017.

Customers who remain within our area of supply;

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

Customers who have moved outside of our area of supply;

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

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

Provisioning policy
The provisioning policy has been consistently applied as follows:-

Unmeasured Customers: All debt
Provide for 100% of the outstanding balances over four years old
Provide for 80% of the outstanding balances that are one to four years old
Provide for 60% of the outstanding balances that are up to one year old

Measured Customers: Household debt
Provide for 80% of the outstanding balances relating to current occupiers that are over one year old
Provide for 60% of the outstanding balances relating to current occupiers that are up to one year old
Provide for 100% of the outstanding balances relating to former occupiers

14. INVESTMENTS

	2019 £000	2018 £000
Unlisted investments	2	2

15. CASH AT BANK AND IN HAND

Of the total amount shown of £27.210m (2018 - £26.744m), £1.968m (2018 - £1.909m) is held specifically for the payment of the next half yearly loan interest charges.

£9.020m (2018 - £11.037m) of the increase in cash is due to proceeds of sale and share options being transferred from Ancala. This is to settle future incremental employment related social security liabilities brought about by the transaction (See note 24 of the APR)

16. BORROWINGS: DUE WITHIN ONE YEAR

	2019 £000	2018 £000
3% Perpetual debenture stock	60	60
3½% Perpetual debenture stock	185	185
4% Perpetual debenture stock	39	39
Balance outstanding on revolving credit facility	10,000	3,000
	10,284	3,284

The Revolver Credit Facility 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.

17. OTHER CURRENT LIABILITIES	**Appointed 2019 £000**	**Non Appointed 2019 £000**	**Total 2019 £000**	**Appointed 2018 £000**	**Non Appointed 2018 £000**	**Total 2018 £000**
Payments received on account	1,845	-	1,845	2,820	-	2,820
Trade creditors	3,118	-	3,118	2,772	-	2,772
Amounts owed to Group companies	1,531	-	1,531	1,619	-	1,619
Other creditors	(33)	458	425	702	-	702
Accruals	818	-	818	837	-	837
Water rates in advance	7,115	-	7,115	7,025	-	7,025
Trade and other payables	14,394	458	14,852	15,775	-	15,775
Capex creditor	2,356	-	2,356	575	-	575
Other taxation and social security	9,281	-	9,281	11,446	-	11,446
	26,031	458	26,489	27,796	-	27,796

18. NON-CURRENT LIABILITIES	**2019 £000**	**2018 £000**
In five years or more:		
Bank loan	107,476	104,118
Less: deferred arrangement costs	(767)	(824)
	106,709	103,294

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

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

19. DEFERRED INCOME: CAPITAL CONTRIBUTIONS

	2019 £000	**2018 £000**
Capital Contributions	27,783	26,131
Release of Capital Contribution to Turnover	(645)	(638)
	27,138	25,493

20. PROVISIONS FOR LIABILITIES	**2019 £000**	**2018 £000**
DEFERRED TAXATION:		
At 1 April 2018	6,764	6,703
Charged during the year in profit and loss account	155	61
At 31 March 2019	6,919	6,764

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

	2019 £000	2018 £000
Deferred tax including that relating to pension asset:		
Accelerated capital allowances	8,088	7,697
Other timing differences	(1,169)	(933)
Pension asset (note 22)	4,871	5,078
Total provision for deferred tax	11,790	11,842
At 1 April 2018	11,842	9,047
Deferred tax charge in profit and loss account (note 8)	147	(28)
Deferred tax charged to the statement of comprehensive income	(199)	2,822
At 31 March 2019	11,790	11,842

21. RESERVES

	Called up Share Capital £'000	Share Premium £'000	Capital Redemption £'000	Profit and Loss £'000	Total £'000
Balance at 1st April 2018	1,078	4,527	3,250	69,360	78,215
Loss for Financial Year	-	-	-	(1,014)	(1,014)
Remeasurement of net defined benefit asset	-	-	-	(1,170)	(1,170)
Movement on deferred tax relating to pension scheme	-	-	-	199	199
Total comprehensive profit for the year	-	-	-	(1,985)	(1,985)
New share capital/share premium issued	-	2,422	-	-	2,422
Dividends	-	-	-	(2,784)	(2,784)
Balance at 31st March 2018	**1,078**	**6,949**	**3,250**	**64,591**	**75,868**

The retained earnings balance represents accumulated profits and losses, including unrealised profits on the remeasurement of investment properties, net of dividends paid and other adjustments. As at 31 March 2019 £64.418m (2018 - £69.072m) was distributable in accordance with company law and £0.173m (2018 - £0.288m) was not distributable.

The share premium reserve contains the premium arising on the issue of equity shares, net of issue costs. On 28 March 2019 ten new Ordinary Shares at 10p each were issued at a premium of £242,216.88 per share which was fully paid up in cash for £2,422,169.76. This resulted in an increase in share capital of £1 and created a share premium of £2,422,168.76.

22. PENSIONS

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

The formal actuarial valuation as at 31 March 2018 was updated to the 31 March 2019 accounting date by an independent qualified actuary in accordance with FRS 102. As required by FRS 102, the value of the defined benefit liabilities has been measured using the projected unit method.

The estimated Company contributions expected to be paid to the Scheme by Portsmouth Water Ltd for the year commencing 1 April 2019 is £1.1m (2018 actual: £1.2m). Of this amount, £0.9m is contributed directly by the Company and £0.2m is contributed by employees by salary sacrifice under the SMART arrangement. The key FRS 102 assumptions used for the scheme were as follows:

	2019 % per annum	2018 % per annum	2017 % per annum
RPI inflation	3.3	3.2	3.3
CPI inflation	2.4	2.3	2.4
Discount rate	2.3	2.5	2.4
Pension increases	2.4	2.3	2.4
Salary growth	4.4	4.3	4.4

Life expectancy of a male aged 65 at the accounting date is 21.9 years and for a female is 24.2 years. Allowances for future improvements in life expectancy mean that life expectancy of a male aged 65 at the accounting date plus 20 years is 23.5 years and for a female is 25.9 years.

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

	%	2019 Fair Value £000	%	2018 Fair Value £000	%	2017 Fair Value £000
Equities	34	56,452	32	52,727	35	56,931
Absolute Return Fund	24	40,922	25	41,111	24	38,439
LDI	22	37,610	23	38,205	22	36,552
Property	10	17,312	11	17,525	9	14,653
Cash and other	10	15,851	9	15,480	10	16,733
	100	168,147	100	165,048	100	163,308

	2019 £000	2018 £000
Total fair value of scheme assets	168,147	165,048
FRS 17 value of scheme liabilities	(133,273)	(135,176)
Impact of asset ceiling	(6,221)	-
Gross pension asset	28,653	29,872
Related deferred tax liability	(4,871)	(5,078)
Net pension asset	23,782	24,794

Under FRS 102, the scheme is represented on the statement of financial position at 31 March 2019 by an asset of £28.653m (2018 - £29.872m), which amounts to £23.782m net of deferred tax (2018 - £24.794m).

The Company paid contributions at a rate of 20.6% of earnings. Members pay contributions at a rate of 5% of earnings via salary sacrifice. The Company also operates a defined contribution pension scheme. The contributions payable by the Company for the year in respect of the defined contribution scheme amounted to £240,016 (2018 - £205,772).

Movement in the net balance sheet position

<u>The FRS 102 value of scheme assets moved over the period as follows:</u>

	2019 £000	2018 £000
Opening asset	29,872	13,790
Expense charged to profit and loss	(1,231)	(1,749)
Gain recognised outside of profit and loss	(1,170)	16,602
Employer contributions	1,182	1,229
Closing asset	28,653	29,872

Movement in present value of defined benefit obligation

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

	2019 £000	2018 £000
Opening scheme liabilities	135,176	149,518
Employer's part of current service cost	1,993	2,095
Interest on scheme liabilities	3,312	3,546
Benefits paid	(5,452)	(3,537)
Actuarial (gain)/loss	(1,756)	(16,446)
Closing scheme defined benefit obligation	133,273	135,176

Movement in fair value of scheme assets

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

	2019 £000	2018 £000
Opening fair value of scheme assets	165,048	163,308
Interest on scheme assets	4,074	3,892
Contributions by the Company, including employee contributions under the SMART arrangement	1,182	1,229
Benefits paid	(5,452)	(3,537)
Actuarial (loss)/gain	3,295	156
Closing fair value of scheme assets	168,147	165,048

Expense recognised in Income Statement

The following amounts have been included within operating profit:

	2019 £000	2018 £000
Current service cost (employer's part only)	(1,993)	(2,095)
Total operating charge	(1,993)	(2,095)

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

	2019 £000	2018 £000
Interest on pension scheme assets	4,074	3,892
Interest on pension scheme defined benefit obligation	(3,312)	(3,546)
Net return	762	346
Total return recognised in the Income Statement	(1,231)	(1,749)

Amounts recognised outside Income Statement

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

	2019 £000	2018 £000
Actual return less interest	(3,295)	(156)
Experience gains arising on scheme defined benefit obligation	(3,083)	(1,226)
Loss/(gain) due to changes in assumptions	1,327	(15,220)
Change in asset limit other than interest	6,221	
Remeasurement loss/(gain) of net defined benefit asset	1,170	(16,602)

The actual return on plan assets was £7.369m in the year to 31 March 2019 (2018 - £4.048m).

23. ULTIMATE CONTROLLING PARTY

On 16 March 2018 the entire share capital of the Company's ultimate parent Undertaking, South Down's Capital Ltd, was acquired by funds managed by Ancala Partners LLP ("Ancala") an independent infrastructure investment fund. The new group structure is set out on page 5 in the APR.

The Ultimate controlling party is Ancala Fornia Holdco Ltd. For the period ended 31 March 2019 Ancala Holdco Ltd is the parent of both the smallest and largest group of which the Company is a member. Consolidated accounts can be obtained on request from the Registered Office. For the period ended 31 March 2018 South Downs Capital Ltd was the smallest group of which the company was a member.

24. DISPOSAL OF THE SOUTH DOWNS CAPITAL GROUP

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

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

External tax advice and HMRC clearance indicated that the sales proceeds, due to employees, were deemed to have arisen "by virtue of their employment" by the Group. As such these distributions were subject to PAYE and NI contributions. In order to tax effect these sale proceeds due to employees the gross consideration was paid to the Company and processed through payroll with payments being made net to employees. As such, additional employee PAYE and NIC contributions were settled out of the gross proceeds and were payable during April 2018 and 2019. This resulted in a beneficial cash flow position of £9.02m (2018 - £11.037m) as at 31 March 2019 due to the timing of the receipt of proceeds for distribution and the settlement of PAYE and NIC liabilities.

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

It should be noted that approximately 66% of the sales proceeds payable have been deferred for future payment to employees in March 2019 and March 2020.

A further impact of the transaction and its manner of distribution was the liability arising in respect of employers NIC and apprenticeship levy. As these are payable on payroll costs, a total additional charge of £2,422,000 (2018 - £2,988,000) arose in relation to the sale proceeds paid to employees. As this could not be deducted from the employees' distribution it results in a charge to the income statement which has been treated as an exceptional cost. However, this has been compensated for by the injection of additional share capital and share premium of £2,422,000 (2018 - £2,988,000) (note 23 in ARA). This reflects part of the total purchase consideration.

25. DISPOSAL OF THE NON-HOUSEHOLD BUSINESS

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

SECTION 2 PRICE REVIEW AND OTHER SEGMENTAL REPORTING

2A SEGMENTAL INCOME STATEMENT

For the 12 months ended 31 March 2019

Current year

	Retail		Wholesale			
	Household	Non-Household	Water Resources	Water Network+	Water Total	Total
	£'000	£'000	£'000	£'000	£'000	£'000
Revenue - price control	4,747	0		34,836	34,836	39,583
Revenue - non-price control	0	0		607	607	607
Operating expenditure	(4,469)	0	(4,597)	(19,421)	(24,018)	(28,487)
Depreciation - tangible fixed assets	(87)	0	(258)	(4,854)	(5,112)	(5,199)
Amortisation - intangible fixed assets	0	0	(8)	(658)	(666)	(666)
Other operating income	0	0	0	(2,916)	(2,916)	(2,916)
Operating profit before recharges	191	0			2,731	2,922
Recharges in respect of 'principal use assets'	(82)	0	0	82	82	0
Recharges from other segments	0	0	0	0	0	0
Recharges to other segments	0	0	0	0	0	0
Operating profit	109	0			2,813	2,922

For the 12 months ended 31 March 2019

£'000	Water Resources	Water Network+	Water Total
Operating expenditure			
Power	1,025	1,549	2,574
Abstraction charges/ discharge consents	1,319	0	1,319
Bulk supply/ Bulk discharge	0	0	0
Other operating expenditure			
- Renewals expensed in year (Infrastructure)	0	2,580	2,580
- Renewals expensed in year (Non-infrastructure)	0	0	0
- Other operating expenditure excluding renewals	1,775	12,732	14,507
Local authority and Cumulo rates	478	1,740	2,218
Total operating expenditure excluding third party services	4,597	18,601	23,198
Third party services	0	820	820
Total operating expenditure	4,597	19,421	24,018
Capital expenditure			
Maintaining the long term capability of the assets - infra	20	2,659	2,679
Maintaining the long term capability of the assets - non-infra	698	5,493	6,191
Other capital expenditure - infra	0	972	972
Other capital expenditure - non-infra	2,514	2,431	4,945
Infrastructure network reinforcement	0	67	67
Total gross capital expenditure (excluding third party)	3,232	11,622	14,854
Third party services	0	(60)	(60)
Total gross capital expenditure	3,232	11,562	14,794
Grants and contributions	0	1,370	1,370
Totex	7,829	29,613	37,442

For the 12 months ended 31 March 2019

£'000	Household	Non-Household	Total
Operating expenditure			
Customer services	2,035	0	2,035
Debt management	66	0	66
Doubtful debts	544	0	544
Meter reading	176	0	176
Services to developers	0	0	0
Other operating expenditure	1,648	0	1,648
Total operating expenditure excluding third party services	4,469	0	4,469
Third party services operating expenditure	0	0	0
Total operating expenditure	4,469	0	4,469
Depreciation - tangible fixed assets	87	0	87
Amortisation - intangible fixed assets	0	0	0
Total operating costs	4,556	0	4,556
Debt written off	488	0	488

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

£'000	Wholesale		Retail		Total
	Water Resources	Water Network+	Household	Non-Household	
Cost					
At 1 April 2018	13,613	173,503	1,182	0	188,298
Impairment	0	(253)	0	0	(253)
Disposals	0	(646)	0	0	(646)
Additions	3,082	11,632	59	0	14,773
At 31 March 2019	16,695	184,236	1,241	0	202,172
Depreciation					
At 1 April 2018	3,616	56,905	841	0	61,362
Adjustments	0	0	0	0	0
Disposals	0	(525)	0	0	(525)
Charge for year	258	4,854	87	0	5,199
At 31 March 2019	3,874	61,234	928	0	66,036
Net book amount at 31 March 2019	12,821	123,002	313	0	136,136
Net book amount at 1 April 2018	9,997	116,598	341	-	126,936
Depreciation charge for year					
Principal Services	258	4,854	87	0	5,199
Third Party Services	0	0	0	0	0
Total	258	4,854	87	0	5,199

The net book value includes £7.1m in respect of assets in the course of construction.

For the 12 months ended 31 March 2019

£'000	Current year			
	Fully recognised in income statement	Capitalised and amortised against depreciation	Fully netted off capex	Total
Grants and contributions - water				
Connection charges [1]	1,150	0	0	1,150
Infrastructure charge receipts	0	1,136	0	1,136
Requisitioned mains	0	234	0	234
Other Contributions (price control)	0	0	0	0
Diversions	0	0	0	0
Other Contributions (non-price control) [2]	0	1,044	0	1,044
Total	1,150	2,414	0	3,564

Movements in capitalised grants and contributions	Current year	
	Water	Total
Balance sheet		
Brought forward [3]	25,370	25,370
Capitalised in year	2,414	2,414
Amortisation (in income statement)	(646)	(646)
Carried forward	27,138	27,138

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

[1] Connection Charges (s45) were included in Revenue in the Business Plan, and not Grants and Contributions.
[2] Contribution from Southern Water for bulk supply pipeline.
[3] Includes a prior year pricing adjustment of £0.123m.

For the 12 months ended 31 March 2019

HOUSEHOLD

	Wholesale charges revenue	Retail revenue	Total revenue	Number of customers	Average household retail revenue per customer
	£m	£m	£m	000s	£
Unmeasured water only customer	18.209	2.939	21.148	201.669	15
Measured water only customer	7.870	1.808	9.678	92.945	19
Total	26.079	4.747	30.826	294.614	16

NON-HOUSEHOLD

Portsmouth Water has exited the non-household retail business, so Table 2G has been excluded, as per the Ofwat guidance. The Wholesale revenue for the non-household business in 2018/19 is £8,757k.

For the 12 months ended 31 March 2019

£'000	Current year Household	Non-Household	Total
Wholesale charge - water			
Unmeasured	18,209	246	18,455
Measured	7,870	8,511	16,381
Third party revenue	0	0	0
Water Total	26,079	8,757	34,836
Wholesale Total	26,079	8,757	34,836
Retail revenue			
Unmeasured	2,939	0	2,939
Measured	1,808	0	1,808
Other third party revenue	0	0	0
Retail Total	4,747	0	4,747
Third party revenue - non-price control			
Bulk supplies			321
Other third party revenue			235
Principal Services - non-price control			
Other appointed revenue			51
Total appointee revenue	30,826	8,757	40,190

	Current year Water	Total
Wholesale revenue governed by price control	34,836	34,836
Grants and Contributions[1]	1,370	1,370
Total revenue governed by wholesale price control	36,206	36,206
Amount assumed in wholesale determination	36,623	36,623
Adjustment for WRFIM	(877)	(877)
Total assumed revenue	35,746	35,746
Difference[2]	460	460

[1] Relevant capital contributions as defined in FD

[2] Narrative explanation on page 55

For the 12 months ended 31 March 2019

£'000	Current year: Network reinforcement capex	Current year: On site/site specific capex (memo only)
Wholesale water network+ (treated water distribution)		
Distribution and trunk mains	67	0
Pumping and storage facilities	0	0
Other	0	0
Water Total	67	0
Wholesale Total	67	0

For the 12 months ended 31 March 2019

	Current year	
£'000	Water	Total
Impact of infrastructure charge discounts		
Infrastructure charges	1,136	1,136
Discounts applied to infrastructure charges	0	0
Gross Infrastructure charges	1,136	1,136
Comparison of revenue and costs		
Variance brought forward	0	0
Revenue	1,136	1,136
Costs	(67)	(67)
Variance carried forward	1,069	1,069

The cost of £67k for water mains network reinforcement works in 2018/19 was associated with two schemes at Clay Lane, Fishbourne and Coppice Hill, Bishops Waltham.

The variance between revenue and cost is due to the infrastructure charges being related to network reinforcement on a 5 year rolling programme. The cost of network reinforcement is not linear from year to year and is associated with the timing of specific developments. We have significant cost forecast in the next 4 years for network reinforcement works in the Barnham, Yapton and Farlington areas.

RETAIL PRICE CONTROL ANALYSIS

Household Retail
Operating expenditure within the Household Retail price control was broadly in line with the Business Plan assumptions, with operating costs £4,556k, against a final determination of £4,468k.

The principal variations were as follows:-

- Debt Management costs reduced from £304k in 2017/18 to £66k. This was due to a one-off exercise to write off historic uncashed cheques, totalling £269k.
- Doubtful Debts has reduced from £795k in 2017/18 to £544k. There has been no change in provisioning policy during the period.
- Depreciation and Amortisation. This year's charge of £87k was lower than 2017/18, which totalled £283k.

WHOLESALE CONTROL RECONCILIATION

REVENUE £'000	Actual	FD	Difference
Wholesale Charge:			
Household – Unmeasured	18,209	18,136	73
Household - Measured	7,870	7,355	515
Non-Household - Unmeasured	246	275	(29)
Non-Household - Measured	8,511	8,530	(19)
Total revenue from charges	34,836	34,296	540
Grants and Contributions	1,370	1,450	(80)
TOTAL REVENUE	**36,206**	**35,746**	**460**

We have compared actual revenue with that implicit in tariff setting for 2018/19, and this complied with the Final Determination.

The Wholesale revenue variance is £0.460m reflecting additional revenue from standard charges of £0.540m and less capital contributions from developers for mains of £0.080m.

The household measured wholesale revenue reflects higher per property consumption than assumed, due to an exceptionally hot summer. The household unmeasured wholesale revenue reflects a greater number of properties, due to a lower take-up of meter optants than assumed at tariff setting.

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

The variance of wholesale charges relative to the Final Determination is 1.6%.

The total variance of wholesale revenue relative to the Final Determination is 1.3%.

SECTION 3 PERFORMANCE SUMMARY

OUTCOME PERFORMANCE TABLE 3A

For the 12 months ended 31 March 2019

Row	Unique ID	Performance commitment	Unit	Unit description	Decimal places	2017-18 performance level - actual (for information)	2018-19 performance level - actual	2018-19 PCL met?	2018-19 outperformance payment or underperformance payment - ODIs payable at the end of AMP6 (indicator)	2018-19 outperformance payment or underperformance payment - ODIs payable at the end of AMP6 (£m, to 4 dp)	31 March 2020 forecast - total AMP6 outperformance payment or underperformance payment (indicator)	31 March 2020 forecast - total AMP6 outperformance payment or underperformance payment (£m, to 4 dp)
1	PR14PRTWSW_A1	A1: Bursts	nr	No. of burst mains per year	0	347	347	No	Underperformance payment deadband		Underperformance payment deadband	0.0000
2	PR14PRTWSW_A2	A2: Water quality standards	%	Mean zonal compliance (%)	2	99.93	99.96	Yes	Underperformance payment deadband		Underperformance payment	-0.6388
3	PR14PRTWSW_A3	A3: Water quality contacts	nr	No. contacts per 1,000 population served	3	0.549	0.437	No	Underperformance payment	-0.3806	Underperformance payment	-1.9030
4	PR14PRTWSW_A4	A4: Temporary usage bans	nr	No. of temporary usage bans per year	0	0	0	Yes				
5	PR14PRTWSW_B1	B1: Leakage	nr	Megalitres per day (Ml/d)	2	32.87	28.12	Yes	-		-	
6	PR14PRTWSW_C1	C1: Interruptions to supply	time	Mins:secs per property per year	mins:secs	4 min 17 secs	3 mins 54 secs	Yes	Outperformance payment	0.0121	Outperformance payment	0.0604
7	PR14PRTWSW_D1	D1: Biodiversity	%	% (completion of agreed actions)	0	60	80	Yes	-		-	
8	PR14PRTWSW_D2	D2: Water Framework Directive (WFD)	text	Programme completion	na	Completed and signed off by EA	n/a	-	-		-	
9	PR14PRTWSW_D3	D3: Carbon	%	Energy sourced from renewables (% increase)	0	> 95%	> 95%	Yes				
10	PR14PRTWSW_E1	E1: RoSPA Health and Safety accreditation	text	RoSPA Gold award	na	Awarded	Awarded	Yes				
11	PR14PRTHHR_A1	A1: Service incentive mechanism (SIM)	text	Service incentive mechanism (SIM) score ranking	na	87.9	89.1	-				
12	PR14PRTHHR_B1	B1: Reducing per capita consumption (PCC)	nr	Litres per head per day (l/h/d)	2	147.54	152.39	-	-		Underperformance payment	-0.1625
13	PR14PRTHHR_C1	C1: Survey of developers	%	Satisfaction rate (%)	0	91	95	Yes				

Introduction
Table 3A shows the performance of the Company against its 13 Outcome Delivery Incentives. The performance data has been assured by the Board of Portsmouth Water, who have engaged Atkins to undertake an independent third party review of the data reported. This data has also been shared with our Customer Challenge Group and a comprehensive report was discussed with the CCG on 19 June 2019.

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

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

Of our 9 financial ODIs, 5 reflect performance over the 5 year period from 1 April 2015. Therefore, we have used the first four years performance and a forecast for 2019/20 to give an indication of any outperformance or underperformance payments which will apply in 2020. Further, 2 of our ODIs are agreed projects with set deadlines in the monitoring period, and there is no expectation that underperformance payments will apply.

We have one specific ODI that is assessed annually, A2 - Mean Zonal Compliance and thus we can determine whether an underperformance payment should apply.

Finally we have an ODI which only applies in year 5, which cannot be determined with certainty at this stage, given we are only at the end of year four of the five year period.

2018/19 performance
Table 3A shows the performance for each ODI in 2018/19 and quantifies any outperformance / underperformance which are likely to apply in 2020.

Given the structure of our 9 Financial ODIs discussed briefly above, the Company has four entries for 2018/19 which result in two payments being accrued until 2020. The two payments associated with 2018/19 are for water quality contacts and interruptions to supply.

Whilst the number of contacts we receive from customers relating to water quality has been higher than target in each of the four years in this AMP period to date, we have continued to reduce and improve our performance. It is unlikely that we will meet our five year target and thus an underperformance payment is due resulting in a reduction in wholesale revenue of £1.903m in 2020.

Our performance on interruptions to supply remains ahead of target and it is likely that we will exceed our five year target. Thus an outperformance payment is due resulting in an increase in wholesale revenue by £0.060m in 2020.

We have failed our target for bursts in the year. However, not only is this a five year target, it also has a dead band in operation. The value of 347 lies well within the band of 250-435 and the Company considers there is no chance that it will lie outside of this range over the five years resulting any change to wholesale revenue in 2020.

Earlier in this AMP period we have twice failed Mean Zonal Compliance, in 2015 and 2017. These two failures result in a reduction in wholesale revenue of £0.639m in 2020. At 99.96% in 2018 we exceeded the value where underperformance payments apply.

Similarly, we expect to fail our per capita consumption target for 2019/20. We forecast this will reduce retail revenue by £0.163m in 2020.

All other ODIs have met or exceeded expectation in 2018/19. Specifically, for 3 of our ODIs which are measured on an on-going basis namely, leakage, temporary usage bans and our survey of developers we have exceeded our performance commitments. For our 4 project based ODIs, Biodiversity, Water Framework Directive, Carbon and RoSPA, we have completed or are on target to be ahead of target over the five year period. For carbon we buy over 95% of our electricity from a supplier which is totally renewable in nature and thus have met our commitment to increase renewables by 10% over the 5 year period.

The only ODI we cannot currently confirm performance is SIM ranking for 2018/19, given it is a relative measure compared to others in the industry. We note however that for the most important factor in the SIM calculation, our qualitative survey score, was placed 2nd in the industry. We will undertake this exercise when all companies publish their ODIs in July 2019.

Our full ODI report will be published on our website on 15 July 2019.

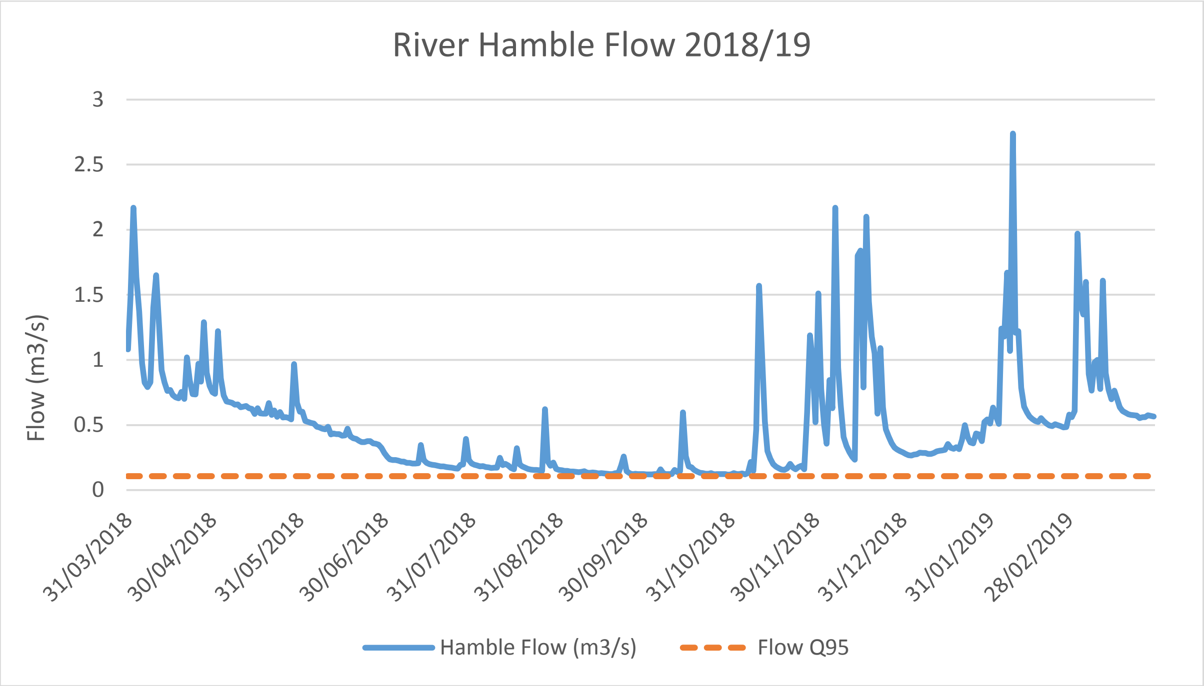
For the 12 months ended 31 March 2019

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

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

Northbrook is the only Portsmouth Water site remaining in the Abstraction Incentive Mechanism (AIM) as it is deemed to impact on flows on the River Hamble. In 2017/18 Portsmouth Water completed an NEP (National Environment Program) scheme designed to improve water quality on the River Hamble.

The AIM minimum flow target for the River Hamble is 0.104 m3/second and is represented by the line in the figure below. This target is based on Q95 flows in the river and recent actual abstraction at our Northbrook site from the period 2007 to 2014. During 2018/19 the low flow trigger was not passed in any day, and therefore, entries for Table 3C of the annual reporting are all zero.



For the 12 months ended 31 March 2019

	Units	Decimal places	Score
Qualitative Performance			
1st Survey Score	nr	2	4.59
2nd Survey Score	nr	2	4.47
3rd Survey Score	nr	2	4.61
4th Survey Score	nr	2	4.57
Qualitative SIM Score (out of 75)	nr	2	66.75
Total Contact Score	nr	2	53.62
Quantitative Performance			
Quantitative SIM Score (out of 25)	nr	2	22.32
Total Annual SIM score (out of 100)	nr	2	89.07

For the 12 months ended 31 March 2019

This schedule has been published alongside the Annual Performance Report.

For the 12 months ended 31 March 2019

Retail - Household	Current year Unmeasured	Current year Measured
Number of void households ('000s)	6.002	1.734
Per capita consumption (excluding supply pipe leakage) l/h/d	161	128

Wholesale	Current year Water
Wholesale Volume (Ml/d)	
Bulk supply export	5.55
Bulk supply import	0.00
Distribution input	174.6

£m	Current year	Cumulative 2015-2020
	Water	Water
Actual Totex	37.442	124.631
Less: Items excluded from the menu		
Third party costs	0.760	3.971
Pension deficit recovery payments	0.000	0.000
*Other 'Rule Book' adjustments	0.612	1.756
Total costs excluded from the menu	1.372	5.727
Adjusted Actual totex	36.070	118.904
Adjusted Actual totex - base year prices	31.155	107.317
Allowed totex based on final menu choice - base year prices	27.380	111.607
Variance - base year prices	(3.775)	4.290

* Wholesale share of FRS102 pension charges

TOTEX MENU VARIANCE ANALYSIS

In the Final Determination, the allowed expenditure from the totex menu is £31.702m, in 2018/19 prices. This menu position gives a variance to actual totex in the year of -£4.368m (-£3.775m in 2012/13 prices). The following table shows this variance for each element of totex.

2018/19 Prices	**Allowed Menu Totex 2018/19**	**Actual 2018/19**	**Variance 2018/19**
Operating Expenditure	18,284	20,006	(1,722)
Renewals	6,043	5,010	1,033
Capital Expenditure	8,825	12,424	(3,599)
Grants and Contributions	(1,450)	(1,370)	(80)
WHOLESALE TOTEX	**31,702**	**36,070**	**(4,368)**

Operating Expenditure

Actual performance is adverse to the Final Determination by £1.722m. In the year, there were a number of one-off items of expenditure including the following:

- Additional costs in relation to leakage recover activity of £1.1m. This is mainly for external contract staff to deliver additional leak detection and to increase the quantity of free repairs for customers.
- One-off costs relating to the Business Plan submission of £0.4m, which were higher than anticipated.
- Higher electricity costs than expected of £0.6m. This was due to an exceptionally hot summer and consequently a much higher demand from Household Measured customers.
  .

Renewals

The renewals expenditure for the year was less than the Business Plan by £1.033m. This was due to the following:

- Activity in the year was less than expected, with 20km of pipe being renewed, compared to 22km in the Business Plan.
- Lower prices from the new contractor and new installation technology. We have achieved 67% no-dig installations, as compared to 23% in AMP5. However this rate is lower than last year due to the completion of a 2.2km trunk main renewal which had to be completed using open cut techniques.
- Increased amount capitalised in the year, due to the nature of the programmes undertaken.

Capital Expenditure

Capital expenditure is higher than the Business Plan by £3.599m. The significant differences are as follows:

- A number of capital schemes were completed earlier than expected and consequently a number of schemes were delayed until the final 2 years of the AMP. In particular, a large programme of work relating to Water Quality Contact Time was started in 2018/19, to be completed in the following year. This amounted to an additional £0.693m in 2018/19. Also, membrane replacement work was less than expected and delayed until 2018/19, amounting to £0.579m.
- Additional leakage capex equipment, not included in the Final Determination, was purchased in 2018/19, amounting to £1.375m.This is one-off expenditure, mainly on noise loggers, to facilitate an increase in leak detection activity.
- Havant Thicket Winter Storage project work, not in the Final Determination, continued in 2018/19 and amounted to £2.514m.
- Optional Metering was less than anticipated, with a reduction in costs of £0.571m.
- There were a number of schemes included in the Final Determination but not completed in 2018/19, including ones relating to Boosters, Pump Stations and Boreholes.

£m	Year to Date
Cumulative totex over/underspend so far in the price control period	(4.579)
Customer share of cumulative totex over/underspend	(2.257)
RCV element of cumulative totex over/underspend (in March 2019 prices)	(1.140)
Adjustment for ODI outperformance payment or underperformance payment	0.000
*RCV determined at FD at 31 March 2019	150.097
Projected 'shadow' RCV	148.957

The Final Determination average PAYG% is 75.27%.
Therefore, the % of Totex underspend that adjusts the RCV is 24.73%.

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

*RCV published by Ofwat, in March 2019 prices.

For the 12 months ended 31 March 2019

£'000	Water resources		Network +				Total
	Abstraction licences	Raw water abstraction	Raw water transport	[1]Raw water storage	Water treatment	Treated water distribution	
Operating expenditure							
Power	0	1,025	0	3	148	1,398	2,574
Abstraction charges/ discharge consents	1,319	0	0	0	0	0	1,319
Bulk supply	0	0	0	0	0	0	0
Other operating expenditure							
- Renewals expensed in year (infrastructure)	0	0	0	0	0	2,580	2,580
- Renewals expensed in year (Non-infrastructure)	0	0	0	0	0	0	0
- Other operating expenditure excluding renewals	0	1,775	0	38	3,430	9,264	14,507
Local authority and Cumulo rates	0	478	0	12	1,168	560	2,218
Total operating expenditure excluding third party services	1,319	3,278	0	53	4,746	13,802	23,198
Third party services	0	0	0	0	0	820	820
Total operating expenditure	1,319	3,278	0	53	4,746	14,622	24,018
Capital expenditure							
Maintaining the long term capability of the assets - infra	0	20	0	0	0	2,659	2,679
Maintaining the long term capability of the assets - non-infra	0	698	0	24	3,056	2,413	6,191
Other capital expenditure - infra	0	0	0	0	0	972	972
Other capital expenditure - non-infra	0	2,514	0	0	47	2,384	4,945
Infrastructure network reinforcement	0	0	0	0	0	67	67
Total gross capital expenditure (excluding third party)	0	3,232	0	24	3,103	8,495	14,854
Third party services	0	0	0	0	0	(60)	(60)
Total gross capital expenditure	0	3,232	0	24	3,103	8,435	14,794
Grants and contributions						(1,370)	(1,370)
Totex	1,319	6,510	0	77	7,849	21,687	37,442
Cash expenditure							
Pension deficit recovery payments	0	0	0	0	0	0	0
Other cash items	0	0	0	0	0	0	0
Totex including cash items	1,319	6,510	0	77	7,849	21,687	37,442

Unit cost information (operating expenditure)

	Licenced volume available	Volume abstracted	Volume transported	[1]Average volume stored	Distribution input volume	Distribution input volume
Volume (Ml)	115,705	66,996	63,725	135	63,725	63,725
Unit cost (£/Ml)	11.40	48.93	-	392.59	74.48	229.45
Population	730,710	730,710	730,710	730,710	730,710	730,710
Unit cost (£/pop)	1.81	4.49	-	0.07	6.50	20.01

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

For the 12 months ended 31 March 2019

£'000	Household Unmeasured Water only	Household Measured Water only	Total
Operating expenditure			
Customer services	1,224	811	2,035
Debt management	56	10	66
Doubtful debts	378	166	544
Meter reading	0	176	176
Other operating expenditure	1,128	520	1,648
Total operating expenditure	2,786	1,683	4,469
Depreciation - tangible fixed assets			
- on assets existing at 31 March 2015	59	26	85
- on assets acquired since 1 April 2015	1	1	2
Amortisation - intangible fixed assets			
- on assets existing at 31 March 2015	0	0	0
- on assets acquired since 1 April 2015	0	0	0
Total operating costs	2,846	1,710	4,556
Capital Expenditure	62	29	91

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

Household

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

4G WHOLESALE CURRENT COST FINANCIAL PERFORMANCE
INCOME STATEMENT

For the 12 months ended 31 March 2019

£'000	Note	Water	Total
Revenue		35,443	35,443
Operating expenditure		(24,018)	(24,018)
Capital maintenance charges	1	(8,063)	(8,063)
Other operating income		(2,916)	(2,916)
Current cost operating profit		446	446
Other income		1,796	1,796
Interest income		957	957
Interest expense		(7,444)	(7,444)
Other Interest expense		762	762
Current Cost Profit before tax and fair value movements		(3,483)	(3,483)
Fair value gains/(losses) on financial instruments		0	0
Current Cost Profit before tax		(3,483)	(3,483)

1. CAPITAL MAINTENANCE CHARGES

The Capital Maintenance charges (£8,063) include the Wholesale amount of the Current Cost Depreciation £6.635m and the Infrastructure Renewals Charge £1.428m.

Current Cost Depreciation

	Operational Assets	Infrastructure Assets	Other Tangible Assets	Total
GROSS REPLACEMENT COSTS				
At 1st April 2018	262,493	1,096,196	24,600	1,383,289
RPI Adjustment	6,407	26,802	590	33,799
Disposals		(184)	(467)	(651)
Additions	7,596	3,718	3,571	14,885
Impairment	(253)			(253)
At 31st March 2019	**276,243**	**1,126,532**	**28,294**	**1,431,069**
DEPRECIATION				
At 1st April 2018	128,884	-	17,969	146,853
RPI Adjustment	3,159		426	3,585
Disposals during year			(527)	(527)
Charge for year	4,856		1,887	6,743
At 31st March 2019	**136,899**	**-**	**19,755**	**156,654**
NET BOOK VALUE				
At 31st March 2019	**139,344**	**1,126,532**	**8,539**	**1,274,415**
At 1st April 2018	133,609	1,096,196	6,631	1,236,436
DEPRECIATION				
WHOLESALE	4,856	-	1,779	**6,635**
RETAIL	-	-	108	**108**
	4,856	**-**	**1,887**	**6,743**

Infrastructure Renewals Charge

Estimation of Infrastructure Renewals Charge at 2018/19 prices

	£'000
Actual expenditure 2018/19	2,951
Budget 2019/20	988
Business Plan 2020/21 - 2032/33	1,235
Average Cost over 15 years	**1,428**

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

For the 12 months ended 31 March 2019

Financial Indicators	Units	Current year Metric	AMP to date Metric
Net debt	£m	99.570	
Regulated equity	£m	50.527	
*Regulated gearing	%	66.34	
Post tax return on regulated equity	%	-1.68	
RORE (return on regulated equity)	%	3.37	4.88
Dividend yield	%	3.62	
Retail profit margin - Household	%	0.62	
Retail profit margin - Non-Household	%	0.00	
Credit rating	n/a	BBB	
Return on RCV	%	3.28	
Dividend cover	dec	-0.43	
Funds from operations (FFO)	£m	7.996	
Interest cover (cash)	dec	2.96	
Adjusted interest cover (cash)	dec	1.49	
FFO/Debt	dec	0.08	
Effective tax rate	%	0.00	
Free cash flow (RCF)	£m	5.212	
RCF/capex	dec	0.37	
Revenue and earnings			
Revenue (actual)	£m	39.583	
EBITDA (actual)	£m	11.096	
Movement in RORE			
Base Return	%	5.70	5.79
Totex out/(under) performance	%	-1.16	0.20
Retail cost out/(under) performance	%	-0.13	-0.81
ODI out/(under) performance	%	0	0
Financing out/(under) performance	%	-1.04	-1.02
Other factors (exceptional item)	%	0	0.72
Regulatory return for the year	%	3.37	4.88
Borrowings			
Proportion of borrowings which are fixed rate	%	0.24	
Proportion of borrowings which are floating rate	%	8.49	
Proportion of borrowings which are index linked	%	91.27	
Proportion of borrowings due within 1 year or less	%	8.49	
Proportion of borrowings due in more than 1 year but no more than 2 years	%	0	
Proportion of borrowings due in more than 2 years but no more than 5 years	%	0	
Proportion of borrowings due in more than 5 years but no more than 20 years	%	91.27	
Proportion of borrowings due in more than 20 years	%	0.24	

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

RORE MOVEMENTS COMPARED TO BASE RORE SET AT PR14

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

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

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

2015/16 Adjusted RORE 4.01%
2016/17 Adjusted RORE 3.97%
2017/18 Adjusted RORE 5.30% (8.14% including exceptional gain on disposal) of NHH
2018/19 Adjusted RORE 3.37%

The average RORE for the first 4 years of the AMP is 4.88%. (Using 8.14% in 2017/18)

The adjustments are explained below, and all numbers are in 2012/13 prices.

2012/13 PRICES	2015/16	2016/17	2017/18	2018/19	
NET INCOME – Final Determination	2.644	2.680	2.667	2.713	Used to calculate FD RORE %'s
Operating cost adjustments	(0.492)	(0.512)	0.348	(0.750)	Includes Totex, Retail and ODI variances
Gain on disposal of NHH business			1.641		Exceptional item in the year
Depreciation adjustment	0.005	0.005	0.013	(0.016)	Based on run-off rate of 3.8%
Interest adjustment	(0.569)	(0.578)	(0.592)	(0.603)	Based on real cost of debt of 3.6%
Tax on adjustments	0.211	0.217	(0.267)	0.260	Tax rate of 19%
NET INCOME - Adjusted	**1.799**	**1.812**	**3.808**	**1.604**	Used to calculate adjusted RORE %'s
REGULATED EQUITY	**44.930**	**45.623**	**46.757**	**47.631**	
Adjusted RORE	**4.01%**	**3.97%**	**8.14%**	**3.37%**	

<u>Revenue Adjustment and Gain on Disposal</u>
Due to the sale of the Non-Household Retail business, there is no longer any associated Retail profit. This amounts to £0.090m and has been deducted from the Final Determination net income each year from 2017/18. In addition, there is an exceptional gain on disposal in 2017/18 of £1.641m. The overall impact of this transaction is £1.569m, and this equates to +2.68% on the 2017/18 RORE.

<u>Totex PAYG Adjustments</u>
These reflect favourable Wholesale totex variances, adjusted for timing differences, as follows:

2015/16 £1.093m
2016/17 £0.492m
2017/18 £0.533m
2018/19 (£0.675m)

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

<u>Retail Operating Cost Adjustments</u>
These reflect the adverse Retail operating cost variances as follows:

2015/16 (£0.613m)
2016/17 (£0.701m)
2017/18 (£0.466m)
2018/19 (£0.076m)

See commentary on page 55 for an explanation of these variances.

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

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

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

For the 12 months ended 31 March 2019

£'000	Water resources		Network +				Total
	Abstraction licences	Raw water abstraction	Raw water transport	[1]Raw water storage	Water treatment	Treated water distribution	
Operating expenditure (exclu. atypicals)							
Power	0	1,025	0	3	148	1,398	2,574
Abstraction charges/ discharge consents	1,319	0	0	0	0	0	1,319
Bulk supply	0	0	0	0	0	0	0
Other operating expenditure							
- Renewals expensed in year (infrastructure)	0	0	0	0	0	2,580	2,580
- Renewals expensed in year (Non-infrastructure)	0	0	0	0	0	0	0
- Other operating expenditure excluding renewals	0	1,775	0	38	3,430	9,264	14,507
Local authority and Cumulo rates	0	478	0	12	1,168	560	2,218
Total operating expenditure excluding third party services	1,319	3,278	0	53	4,746	13,802	23,198
Third party services	0	0	0	0	0	820	820
Total operating expenditure	1,319	3,278	0	53	4,746	14,622	24,018
Capital expenditure (excl. atypicals)							
Maintaining the long term capability of the assets - infra	0	20	0	0	0	2,659	2,679
Maintaining the long term capability of the assets - non-infra	0	698	0	24	3,056	2,413	6,191
Other capital expenditure - infra	0	0	0	0	0	972	972
Other capital expenditure - non-infra	0	2,514	0	0	47	2,384	4,945
Infrastructure network reinforcement	0	0	0	0	0	67	67
Total gross capital expenditure (excluding third party)	0	3,232	0	24	3,103	8,495	14,854
Third party services	0	0	0	0	0	(60)	(60)
Total gross capital expenditure	0	3,232	0	24	3,103	8,435	14,794
Grants and contributions						(1,370)	(1,370)
Totex	1,319	6,510	0	77	7,849	21,687	37,442
Cash expenditure (exclu. atypicals)							
Pension deficit recovery payments	0	0	0	0	0	0	0
Other cash items	0	0	0	0	0	0	0
Totex including cash items	1,319	6,510	0	77	7,849	21,687	37,442
Atypical expenditure							
							0
							0
							0
Total atypical expenditure	0	0	0	0	0	0	0
Total expenditure	1,319	6,510	0	77	7,849	21,687	37,442

4L ENHANCEMENT CAPITAL EXPENDITURE BY PURPOSE – WHOLESALE WATER

For the 12 months ended 31 March 2019

£'000	Expenditure in report year						
	Water resources		Network +				Total
	Abstraction licences	Raw water abstraction	Raw water transport	[1]Raw water storage	Water treatment	Treated water distribution	
Enhancement capital expenditure by purpose							
NEP - Making ecological improvements at abstractions (Habitats Directive, SSSI, NERC, BAPs)							0
NEP - Eels Regulations (measures at intakes)							0
NEP - Invasive Non-Native Species							0
Addressing low pressure							0
Improving taste/ odour/ colour							0
Meeting lead standards							0
Supply side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Supply side enhancements to the supply/demand balance (dry year annual average conditions)		2,514					2,514
Demand side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Demand side enhancements to the supply/demand balance (dry year annual average conditions)						1,050	1,050
New developments						1,039	1,039
New connections element of new development (CPs, meters)							0
Investment to address raw water deterioration (THM, nitrates, Crypto, pesticides, others)					32		32
Resiliance							0
SEMD							0
NEP - Drinking Water Protected Areas (schemes)							0
NEP - Water Framework Directive measure							0
NEP - Investigations							0
Improvements to river flows					15		15
Metering (excluding cost of providing metering to new service connections) - meters requested by optants						814	814
Metering (excluding cost of providing metering to new service connections) - meters introduced by companies							0
Metering (excluding cost of providing metering to new service connections) - other							0
Boundary Boxes						520	520
							0
							0
Total enhancement capital expenditure	0	2,514	0	0	47	3,423	5,984

For the 12 months ended 31 March 2019

£'000	Cumulative expenditure on schemes completed in report year						
	Water resources		Network +				Total
	Abstraction licences	Raw water abstraction	Raw water transport	[1]Raw water storage	Water treatment	Treated water distribution	
Enhancement capital expenditure by purpose							
NEP - Making ecological improvements at abstractions (Habitats Directive, SSSI, NERC, BAPs)							0
NEP - Eels Regulations (measures at intakes)							0
NEP - Invasive Non-Native Species							0
Addressing low pressure							0
Improving taste/ odour/ colour							0
Meeting lead standards							0
Supply side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Supply side enhancements to the supply/demand balance (dry year annual average conditions)		2,514					2,514
Demand side enhancements to the supply/demand balance (dry year critical/ peak conditions)							0
Demand side enhancements to the supply/demand balance (dry year annual average conditions)						1,050	1,050
New developments						1,039	1,039
New connections element of new development (CPs, meters)							0
Investment to address raw water deterioration (THM, nitrates, Crypto, pesticides, others)					32		32
Resiliance							0
SEMD							0
NEP - Drinking Water Protected Areas (schemes)							
NEP - Water Framework Directive measure							
NEP - Investigations							0
Improvements to river flows					15		15
Metering (excluding cost of providing metering to new service connections) - meters requested by optants						814	814
Metering (excluding cost of providing metering to new service connections) - meters introduced by companies							0
Metering (excluding cost of providing metering to new service connections) - other							0
Boundary Boxes						520	520
							0
							0
Total enhancement capital expenditure	0	2,514	0	0	47	3,423	5,984

For the 12 months ended 31 March 2019

Water Resources	Units	Input
Proportion of distribution input derived from impounding reservoirs	Propn 0 to 1	0
Proportion of distribution input derived from pumped storage reservoirs	Propn 0 to 1	0
Proportion of distribution input derived from river abstractions	Propn 0 to 1	0.164
Proportion of distribution input derived from groundwater works,excluding managed aquifer recharge (MAR) water supply schemes	Propn 0 to 1	0.836
Proportion of distribution input derived from artificial recharge (AR) water supply schemes	Propn 0 to 1	0
Proportion of distribution input derived from aquifer storage and recovery (ASR) water supply schemes	Propn 0 to 1	0
Number of impounding reservoirs	nr	0
Number of pumped storage reservoirs	nr	0
Number of river abstractions	nr	1
Number of groundwater works excluding managed aquifer recharge (MAR) water supply schemes	nr	20
Number of artificial recharge (AR) water supply schemes	nr	0
Number of aquifer storage and recovery (ASR) water supply schemes	nr	0
Total number of sources	nr	21
Total number of water reservoirs	nr	1
Total capacity of water reservoirs	Ml	135
Total number of intake and source pumping stations	nr	21
Total number of raw water transfer stations	nr	0
Total capacity of intake and source pumping stations	kW	6596
Total capacity of raw water transfer pumping stations	kW	0
Total length of raw water mains and conveyors	km	25.39
Average pumping head – resources	m.hd	29.6
Average pumping head – raw water transport	m.hd	0
Total length of raw and pre-treated (non-potable) water transport mains	km	0
Water resources capacity (measured using water resources yield)	Ml/d	226.5
Water Treatment		
Total water treated at all SW simple disinfection works	Ml/d	0
Total water treated at all SW1 works	Ml/d	0
Total water treated at all SW2 works	Ml/d	0
Total water treated at all SW3 works	Ml/d	0
Total water treated at all SW4 works	Ml/d	0
Total water treated at all SW5 works	Ml/d	29.32
Total water treated at all SW6 works	Ml/d	0
Total water treated at all GW simple disinfection works	Ml/d	59.51
Total water treated at all GW1 works	Ml/d	0
Total water treated at all GW2 works	Ml/d	11.50
Total water treated at all GW3 works	Ml/d	0
Total water treated at all GW4 works	Ml/d	78.61
Total water treated at all GW5 works	Ml/d	0
Total water treated at all GW6 works	Ml/d	0
Total water treated at more than one type of works	Ml/d	0
Total number of SW simple disinfection works	nr	0
Total number of SW1 works	nr	0
Total number of SW2 works	nr	0
Total number of SW3 works	nr	0
Total number of SW4 works	nr	0
Total number of SW5 works	nr	1
Total number of SW6 works	nr	0
Total number of GW simple disinfection works	nr	13
Total number of GW1 works	nr	0
Total number of GW2 works	nr	1
Total number of GW3 works	nr	0
Total number of GW4 works	nr	6
Total number of GW5 works	nr	0
Total number of GW6 works	nr	0
Number of treatment works requiring remedial action because of raw water deterioration	nr	0
Zonal population receiving water treated with orthophosphate	000's	646.776
Average pumping head – treatment	m.hd	1.99

For the 12 months ended 31 March 2019

Water Distribution	Units	Input
Total length of potable mains as at 31 March	km	3348.6
Total length of mains relined	km	0
Total length of mains renewed	km	21.9
Total length of new mains	km	33.9
Potable water mains (<320mm)	km	2995.4
Potable water mains 320mm - 450mm	km	184.5
Potable water mains 450mm - 610mm	km	110.4
Potable water mains > 610mm	km	58.1
Capacity of booster pumping stations	kW	2982
Capacity of service reservoirs	Ml	484
Capacity of water towers	Ml	0
Distribution input	Ml/d	174.58
Water delivered (non-potable)	Ml/d	0
Water delivered (potable)	Ml/d	152.02
Water delivered (billed measured residential)	Ml/d	25.98
Water delivered (billed measured business)	Ml/d	34.08
Total Leakage	Ml/d	28.12
Distribution losses	Ml/d	19.6
Water taken unbilled	Ml/d	2.52
Number of lead communication pipes	nr	81447
Number of galvanised iron communication pipes	nr	18037
Number of other communication pipes	nr	208359
Number of booster pumping stations	nr	26
Total number of service reservoirs	nr	30
Number of water towers	nr	0
Total length of mains laid or structurally refurbished pre-1880	km	52.8
Total length of mains laid or structurally refurbished between 1881 and 1900	km	60.7
Total length of mains laid or structurally refurbished between 1901 and 1920	km	173.9
Total length of mains laid or structurally refurbished between 1921 and 1940	km	437.2
Total length of mains laid or structurally refurbished between 1941 and 1960	km	424.2
Total length of mains laid or structurally refurbished between 1961 and 1980	km	847.9
Total length of mains laid or structurally refurbished between 1981 and 2000	km	863.0
Total length of mains laid or structurally refurbished post 2001	km	488.8
Average pumping head – distribution	m.hd	37.96
Band Disclosure (nr)		
WTW's in size band 1	nr	8
WTW's in size band 2	nr	1
WTW's in size band 3	nr	5
WTW's in size band 4	nr	4
WTW's in size band 5	nr	2
WTW's in size band 6	nr	1
Band Disclosure (%)		
Proportion of Total DI band 1	%	2
Proportion of Total DI band 2	%	2
Proportion of Total DI band 3	%	16
Proportion of Total DI band 4	%	25
Proportion of Total DI band 5	%	26
Proportion of Total DI band 6	%	29

For the 12 months ended 31 March 2019

Properties and Population	Units	Input
Residential properties billed for measured water (external meter)	000s	70.303
Residential properties billed for measured water (not external meter)	000s	22.642
Business properties billed measured water	000s	14.018
Residential properties billed for unmeasured water	000s	201.667
Business properties billed unmeasured water	000s	1.942
Total business connected properties at year end	000s	18.384
Total residential connected properties at year end	000s	303.208
Total connected properties at year end	000s	321.148
Number of residential meters renewed	000s	11.47
Number of business meters renewed	000s	0.209
Number of meters installed at request of optants	000s	2.580
Number of selective meters installed	000s	0
Total number of new business connections	000s	0.147
Total number of new residential connections	000s	1.979
Total population served	000s	730.710
Number of business meters (billed properties)	000s	17.020
Number of residential meters (billed properties)	000s	95.618
Company area	km^2	686
Other		
Number of lead communication pipes replaced for water quality	nr	18
Total supply side enhancements to the supply demand balance (dry year critical/ peak conditions)	Ml/d	0
Total supply side enhancements to the supply demand balance (dry year annual average conditions)	Ml/d	0
Total demand side enhancements to the supply demand balance (dry year critical/ peak conditions)	Ml/d	0
Total demand side enhancements to the supply demand balance (dry year annual average conditions)	Ml/d	0
Energy consumption - network plus	MWh	14
Energy consumption - water resources	MWh	11
Energy consumption - wholesale	MWh	25
Mean zonal compliance	%	99.96%
Compliance Risk Index	nr	1.78
Event Risk Index	nr	11.76
*Volume of leakage above or below the substainable economic level	Ml/d	-3.280

*SELL=31.4 Ml/d

4V OPERATING COST ANALYSIS – WATER RESOURCES

For the 12 months ended 31 March 2019

£'000	Impounding Reservoir	Pumped Storage	River Abstractions	Groundwater, exclu. MAR water supply schemes	Artificial Recharge (AR) water supply schemes	Aquifer Storage and Recovery (ASR) water supply schemes	Other	Total
Operating expenditure								
Power	0	0	104	921	0	0	0	1,025
Abstraction charges/discharge consents	0	0	236	1,083	0	0	0	1,319
Bulk supply	0	0	0	0	0	0	0	0
Other operating expenditure	0	0	0	0	0	0	0	0
Renewals expensed in year (Infrastructure)	0	0	0	0	0	0	0	0
Renewals expensed in year (Non-Infrastructure)	0	0	0	0	0	0	0	0
Other direct operating expenditure	0	0	0	97	0	0	0	97
Other indirect operating expenditure	0	0	0	1,678	0	0	0	1,678
Total functional expenditure	0	0	340	3,779	.	0	0	4,119
Local authority and Cumulo rates	0	0	0	478	0	0	0	478
Total operating expenditure (excluding 3rd party)	0	0	340	4,257	0	0	0	4,597
Depreciation	0	0	0	266	0	0	0	266
Total operating costs (excluding 3rd party)	0	0	340	4,523	0	0	0	4,863

OTHER EXPENDITURE – WHOLESALE WATER

For the 12 months ended 31 March 2019

£'000	Water Resources	Raw Water Distribution	Water Treatment	Treated Water Distribution	Total
Other Expenditure					
Employment costs - directly allocated	14	6	554	2,913	3,487
Employment costs - indirectly allocated	648	0	1,350	2,161	4,159
Number FTEs - directly allocated	1	0	14	70	85
Number FTEs - indirectly allocated	12	0	25	40	77
Costs asscociated with Traffic Management Act	0	0	0	116	116
Service Charges					
Canal & River Trust abstraction charges/ discharge consents	0	0	0	0	0
Environment Agency abstraction charges/ discharge consents	1,319	0	0	0	1,319
Other abstraction charges/ discharge consents	0	0	0	0	0
Statutory water softening	0	0	0	0	0

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

Borrowings or Sums Lent

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

Interest Received

A receipt of interest amounting to £449,605 in respect of the inter-company loan made to South Downs Limited in 2002 (as covered above) was received from South Downs Limited.

Dividends paid to Associated Undertakings

The dividends paid to the holding company, Portsmouth Water Holdings Limited, are shown in note 9 on page 36 of this Annual Performance Report. The dividend policy is also covered within this note.

Payments for Tax Losses

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

Supply of Services

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

Service	Associate Company	Turnover of Associate (£000's)	Terms of Supply	Value (£000's)
Rent of operational sites	Brockhampton Holdings Limited	312*	Market Tested	57
Solar power income			Market Tested	19

*Brockhampton Holdings Limited accounts do not include any amounts classified as turnover. Amounts relating to rent and solar power income are included within other operating income which totals £312k of which £168k relates to total rental income and £144k relates to total income from solar power.

Directors Remuneration

There is a recharge of Directors salaries amounting to £43,125 paid to Portsmouth Water Limited by Brockhampton Holdings Limited, which represents the time spent by Portsmouth Water Executive Directors on Group matters. There is also a recharge into the following entities relating to administrative time spent on Group matters:

Brockhampton Pension Scheme	£19,898
Brockhampton Holdings Ltd	£20,187
Brockhampton Property	£20,187
South Downs Ltd	£5,888
South Downs Capital Ltd	£2,676
Ancala Mid Co	£2,498
Ancala Bid Co	£2,498
Ancala Hold Co	£2,498

Statement by Board of Directors

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

Price Control Units

Portsmouth Water has closely followed the Ofwat guidance for the allocation of costs and assets between price control units and therefore believes that there is no cross subsidy between them. Therefore, no market testing has been undertaken in 2018/19.

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

Opinion

We have audited the sections of/tables within Portsmouth Water Limited's Regulatory Accounts for the year ended 31 March 2019 ("the Regulatory Accounts") which comprise:

- the regulatory financial reporting tables comprising the income statement (table 1A), the statement of comprehensive income (table 1B), the statement of financial position (table 1C), the statement of cash flows (table 1D), the net debt analysis (table 1E), the financial flows (table 1F) and the related notes; and
- the regulatory price review and other segmental reporting tables comprising the segmental income statement (table 2A), the totex analysis for wholesale water and wastewater (table 2B), the operating cost analysis for retail (table 2C), the historical cost analysis of tangible fixed assets for wholesale and retail (table 2D), the analysis of grants and contributions and land sales for wholesale (table 2E), the household water revenues by customer type (table 2F), the non-household water revenues by tariff type (table 2G- not completed in line with RAG 4.08), the non-household wastewater revenues by tariff type (table 2H- not completed in line with RAG 4.08)the revenue analysis & wholesale control reconciliation (table 2I), the infrastructure network reinforcement costs (table 2J), the infrastructure charges reconciliation (table 2K) and the related notes.

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

In our opinion, Portsmouth Water Limited's Regulatory Accounts have been prepared, in all material aspects, in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA (RAG 1.08, RAG 2.07, RAG 3.11, RAG 4.08 and RAG 5.07) and the accounting policies (including the company's published accounting methodology statement, as defined in RAG 3.11, appendix 2), set out on pages 28 to 45.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)"), including ISA (UK) 800, and applicable law, except as stated in the section on Auditors' responsibilities for the audit of the Regulatory Accounts below, and having regard to the guidance contained in ICAEW Technical Release Tech 02/16 AAF 'Reporting to Regulators on Regulatory Accounts' issued by the Institute of Chartered Accountants in England & Wales.

Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the Regulatory Accounts section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit, including the Financial Reporting Council's (FRC's) Ethical Standards as applied to public interest entities, and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of matter – special purpose basis of preparation

We draw attention to the fact that the Regulatory Accounts have been prepared in accordance with Condition F, the Regulatory Accounting Guidelines, the accounting policies (including the company's published accounting methodology statement, as defined in RAG 3.11, appendix 2) set out in the statement of accounting policies and under the historical cost convention. The nature, form and content of the Regulatory Accounts are determined by the WSRA. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the WSRA's purposes. Accordingly we make no such assessment.

The Regulatory Accounts are separate from the statutory financial statements of the Company and has not been prepared in compliance with UK Accounting Standards, including Financial Reporting Standard 102 "The Financial Reporting Standard applicable in the United Kingdom and Republic of Ireland" ("FRS 102") and the Companies Act 2006. Financial information other than that prepared on the basis of FRS 102 does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in statutory financial statements prepared in accordance with the Companies Act 2006. The Regulatory Accounts on pages 19 to 23 have been drawn up in accordance with Regulatory Accounting Guidelines with a number of departures from FRS 102. A summary of the effect of these departures from Generally Accepted Accounting Practice in the Company's statutory financial statements is included in the tables within section 1

The Regulatory Accounts are prepared in accordance with a special purpose framework for the specific purpose as described in the Responsibilities for the Regulatory Accounts and the audit section below. As a result, the Regulatory Accounts may not be suitable for another purpose.

Our opinion is not modified in respect of this matter.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which ISAs (UK) require us to report to you when:

- the directors' use of the going concern basis of accounting in the preparation of the Regulatory Accounts is not appropriate; or
- the directors have not disclosed in the Regulatory Accounts any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the Regulatory Accounting Statements are authorised for issue.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the company's ability to continue as a going concern.

Reporting on other information

The other information comprises all of the information in the Regulatory Accounts other than the Regulatory Accounting Statements within the Regulatory Accounts and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the Regulatory Accounting Statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the Regulatory Accounting Statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Regulatory Accounting Statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the Regulatory Accounting Statements within the Regulatory Accounts or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement or inconsistency of this other information, we are required to report that fact.

We have nothing to report based on these responsibilities.

Responsibilities of the Directors for the Annual Performance Report

As explained more fully in the Statement of Directors' Responsibilities set out on pages 17 and 18, the directors are responsible for the preparation of the Regulatory Accounts in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the Company's accounting policies (including the Company's published accounting methodology statement, as defined in RAG 3.11, appendix 2).

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

In preparing the Regulatory Accounts, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the Audit of the Regulatory accounting statements within the Annual Performance Report

Our objectives are to obtain reasonable assurance about whether the Regulatory accounting statements within the Regulatory Accounts are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these Regulatory Accounts.

As part of an audit in accordance with ISAs (UK), we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the company's Regulatory Accounts, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion.

Our conclusions are based on the audit evidence obtained up to the date of our report. However, future events or conditions may cause the company to cease to continue as a going concern.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during the audit.
- Assess the reasonableness of significant accounting estimates and related disclosures made by the directors.

We have not assessed whether the accounting policies are appropriate to the circumstances of the Company where these are laid down by Condition F. Where Condition F does not give specific guidance on the accounting policies to be followed, our audit includes an assessment of whether the accounting policies adopted in respect of the transactions and balances required to be included in the Annual Performance Report are consistent with those used in the preparation of the statutory financial statements of the company.

The Company has presented the allocation of operating costs and assets in accordance with the accounting policy for price control segments set out in note 1k and its accounting methodology statement. We are not required to assess whether the methods of cost allocation set out in the Methodology Statement are appropriate to the circumstances of the Company or whether they meet the requirements of the WSRA, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK).

Opinion on other matters prescribed by Condition F

Under the terms of our contract we have assumed responsibility to provide those additional opinions required by Condition F in relation to the accounting records. In our opinion:

- proper accounting records have been kept by the appointee as required by paragraph 3 of Condition F; and
- the Regulatory Accounting Statements are in agreement with the accounting records and returns retained for the purpose of preparing the Regulatory Accounts.

Use of this report

This report is made, on terms that have been agreed, solely to the Company and the WSRA in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewage undertaker under the Water Industry Act 1991 (“Condition F”). Our audit work has been undertaken so that we might state to the Company and the WSRA those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under Condition F to procure such a report and (b) to facilitate the carrying out by the WSRA of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the WSRA, for our audit work, for this report or for the opinions we have formed.

Our opinion on the Regulatory Accounting Statements within the Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2019 on which we reported on 22 May 2019, which are prepared for a different purpose. Our audit report in relation to the statutory financial statements of the Company (our “Statutory audit”) was made solely to the Company’s members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our Statutory audit work was undertaken so that we might state to the Company’s members those matters we are required to state to them in a statutory audit report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our Statutory audit report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

James Ledward
For and on behalf of KPMG LLP
Chartered Accountants
Gateway House
Tollgate
Chandlers Ford
SO53 3TG

June 2019