Severn Trent Water Limited

Report and financial statements
For the year ended 31 March 2019

Company number 2366686

Severn Trent Water Limited

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Welcome to the Severn Trent Water Annual Report 2019

OUR PURPOSE IS TO SERVE OUR COMMUNITIES AND BUILD A LASTING WATER LEGACY. THIS DRIVES OUR VISION TO BE THE MOST TRUSTED WATER COMPANY BY 2020, DELIVERING AN OUTSTANDING CUSTOMER EXPERIENCE, BEST VALUE SERVICE AND ENVIRONMENTAL LEADERSHIP.

This report highlights the progress we have made over the past year in achieving that vision through our strategic objectives and absolute focus on listening to and delivering value for all of our stakeholders.

We're committed to keeping your water flowing clearly and making your waste water clean again, so you can carry on enjoying this precious resource, for generations to come.

What we do

We provide clean water and waste water services to more than 4.5 million households and businesses through Severn Trent Water Limited and its subsidiary Hafren Dyfrdwy Cyfyngedig.

The primary activities we focus on

- Wholesale operations and engineering
- Household customer services

Where we operate

Our region stretches across the heart of the UK, from the Bristol Channel to the Humber, and from North and mid-Wales to the East Midlands.

Turnover

£1,673.1 million

Profit before interest and tax

£557.7 million

Underlying profit before interest and tax[1]

£567.3 million

Households and businesses served

4.5 million

Litres of drinking water supplied each day

2.0 billion

Litres of waste water treated per day

2.9 billion

Employees

6,305

[1.] Alternative Performance Measures are defined in note 43 to the financial statements

Our business model

Running an efficient water business

We provide clean water every time our customers turn on the tap and remove their waste water in an affordable, sustainable and reliable way.

We do so through our regulated subsidiaries and draw upon our skills in water and waste treatment to provide similar services to other organisations through the our Business Services division.

RESOURCES & RELATIONSHIPS WE RELY ON

Resources

Physical assets
A resilient, well maintained network of clean water pipes and reservoirs, sewers and pumping stations.
We maintain over 49,000 km of clean water pipes and over 92,000 km of sewer pipes.

Natural resources
Water from reservoirs, rivers and underground aquifers are essential to support Severn Trent's operations and value creation.
We look after some of the UK's most impressive natural resources.

Financial capital
We have a strong balance sheet, with gearing close to the regulatory model. We are able to access a range of capital markets to fund future operations.
Our gearing is 62%, one of the lowest in the sector. We have committed undrawn facilities of £885 million.

Relationships

Our customers and communities
Our customers and communities are at the heart of everything we do. We aim to anticipate and meet changing customers' and wider societal needs.
We serve over 4.5 million customers.

Our people
We look to attract, develop and retain talented people from all backgrounds, and bring the next generation of water experts into the industry.
We directly employ over 6,300 people. Glassdoor reports that 74% of our people would recommend us to a friend.

Our suppliers and partners
Strong supplier relationships support our business operations in line with our Modern Slavery commitments.

Our regulators
Our industry is regulated by Ofwat and several other regulators and public bodies.
We work with our regulators to shape our industry. Our Severn Trent Plan was fast-tracked by Ofwat.

THE WATER CYCLE

Water is collected
We pay the Environment Agency and Natural Resources Wales for the water we collect from reservoirs, rivers and underground aquifers across our region.

Water is cleaned
Our groundwater and surface water treatment works clean raw water to the highest standards, making it safe to drink.

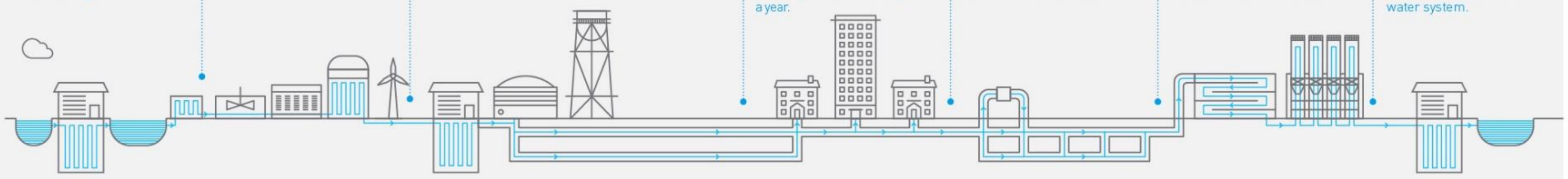
Clean water is distributed
Our network of pipes and our enclosed storage reservoirs bring a continuous supply of clean water right to our customers' taps.

Customers enjoy our services
We serve 4.5 million businesses and households with a safe, reliable supply of water and collect waste water seven days a week, 365 days a year.

Waste water is collected
Our network of sewers and pumping stations collect waste water from homes and businesses and take it to our treatment works.

Waste water is cleaned
Waste water is carefully screened, filtered and treated in our sewage treatment works to meet stringent environmental standards.

Water is recycled to the environment
We pay the Environment Agency and Natural Resources Wales annual consent fees to return the treated water to the water system.



GENERATING & PRESERVING LONG TERM VALUE

Physical assets
Our biggest year of capital investment in over a decade.
Good progress on our Birmingham Resilience Project.
Replaced 230 km of our water network in 2018/19.

Natural resources
We've improved biodiversity of six hectares of Sites of Special Scientific Interest ('SSSIs') in 2018/19.
We are on track to reach our target of 75 hectares by 2020.

Financial capital
Average debt maturity 14 years.
Investment grade credit rating.

Our customers and communities
Lowest bills in England for a decade (Severn Trent) and Wales (Hafren Dyfrdwy).
We helped over 52,800 customers through social tariffs and assistance schemes (2018: 51,700).

Our people
Developing people from all backgrounds in line with our Social Mobility Programme.
31% of our graduates are from a BAME background (2018: 27%).

Our suppliers and partners
Building sustainable relationships that provide mutual benefit.

Our regulators
We stimulate regulatory debates to improve services for customers across the industry.
Launched the World Water Innovation Fund.

Chairman's statement

FULFILLING OUR ROLE IN SOCIETY

"It has never been more important that we focus on our purpose in society. This underpins everything that we do. Not only in the context of our shareholders but also in full consideration of our employees, communities and other stakeholders. This isn't only a focus for us because we are a good Company, but because it is synonymous with the long-term success of Severn Trent."

Andrew Duff
Chairman

This year has seen our Company successfully achieve a series of important milestones, culminating in our business plan for the five years from 2020 being fast-tracked by Ofwat. Our operational performance is discussed in detail in our Chief Executive's statement. Here, I want take the opportunity to look at the bigger picture by highlighting the positive difference we have made for our customers and underline our commitment to being a force for good in the communities we serve.

Our purpose is to serve our communities, build a lasting legacy and be recognised as the most trusted water company – and during the year we were delighted to see this commitment recognised when we were named as a pathfinder with the Purposeful Company Task Force, an initiative that seeks to transform British business with purposeful companies that are committed to creating long-term value through serving the needs of society. We were the only utility to receive this honour, and we're continuing our work with Will Hutton, Clare Chapman and likeminded companies to explore how we can best use social purpose as a tool to promote trust between business and society.

This understanding and recognition of social purpose has never been more important – our purpose connects us with our customers and our communities, inspires our people and reinforces that in the long term, we all share the same interests. We believe that transforming our services and driving growth will lead to mutual benefit for all, with performance that delivers benefits to one group also delivering for others. The interests of our stakeholders such as our customers, employees and pensioners, are often interlinked.

I am pleased to see that in its emerging strategy, Ofwat sees the importance of encouraging companies to deliver public value and how they can, for example, give recognition to companies to own their public purpose.

Long-term achievements

Water services in England and Wales have been transformed for the better over the last 25 years – and we have played a major role in this change, investing £22 billion in today's money in infrastructure improvements over the last quarter of a century. We are proud of the part that our continuous investment has played in providing better services to our customers, greater opportunities for communities and our people and a cleaner environment for all.

The future of the water industry continues to be the subject of significant debate. At Severn Trent, our policy is to only comment on political issues that materially affect our customers. We believe that renationalisation is one such issue, and that the interests of all stakeholders – including UK taxpayers – are best served by the industry remaining privatised whilst operating within a clear and robust regulatory framework.

Our people make the difference
Our people take very seriously the responsibility that comes with providing an essential service that touches the lives of millions. Their passion and commitment shines through in everything they do – meeting customers, solving problems and working tirelessly to keep our product flowing at the turn of a tap, 24 hours a day, seven days a week – and on behalf of the Board I thank them unreservedly.

It is important that the makeup of our workforce is representative of the communities we serve. I am pleased to report that in respect of ethnic diversity, 8.7% of our workforce come from Black, Asian and Minority Ethnic ('BAME') backgrounds. Additionally, 31% of our graduates and 12% of our apprentices come from BAME backgrounds, significantly above industry averages. We've also invested in initiatives to help provide employment opportunities to people from disadvantaged backgrounds in our region. And we are also the highest ranked utility in the Hampton-Alexander report, which measures gender equality.

Sharing the rewards
Under our industry's regulatory framework, high levels of customer service create financial rewards through ODI outperformance. This means that we are able to share the benefits of our work with all stakeholders when we perform well. Over the course of the AMP we will reinvest £220m generated by our outperformance back into our business. Additionally, our new community dividend will set aside 1% of company profits for the benefit of community schemes.

Your Board
There were no changes to Board membership during the year. We continued to work well together as a team, with the appropriate balance of Executive and Non-Executive Directors. The Board was fully engaged throughout the PR19 process; and worked tirelessly with our senior team to create a plan that will bring real improvements to customer service while also keeping bills the lowest in England and Wales.

It is a real privilege to serve as Chairman of Severn Trent and it has been a pleasure to oversee the Company's progress over the last nine years. As we prepare to implement our new business plan, following selection as one of only three companies awarded Fast Track status by Ofwat, I believe this is the right moment to step down and allow a new Chair to lead the Board into this important next phase for Severn Trent. These plans are in the early stages and it is planned to formally announce my successor in due course. You can read more on this process on page 91.

Outlook
Ofwat's fast-tracking of our business plan has, in many ways, endorsed our strategy, structure and business model, and further fuelled our commitment to customer service. I look forward to the year ahead with confidence, knowing that the talent of our people, the financial strengths of our business, and our commitment to good governance will help us to fulfil our potential as a socially responsible business providing a high quality, essential public service.

Andrew Duff
Chairman

Market and industry overview

Our context and peers

A total of 17 regional businesses supply water services to over 50 million household and non-household customers in England and Wales. Eleven of these, including Severn Trent Water Limited and Hafren Dyfrdwy Cyfyngedig, provide waste water services, the remaining six provide water only.

The history of the water sector

Water services in England and Wales have been transformed since the early 1900s. Since privatisation in 1989, the sector has invested £130 billion to deliver improvements in reliability and quality of service and it is estimated that our sector has improved efficiency by around 67%. Drinking water is cleaner, supply is more reliable, sewer flooding is much less frequent and rivers are in a better state of health than at any point since the industrial revolution.

We're very proud of our industry's achievements. The water sector in England and Wales was recently ranked joint first for providing better outcomes for customers compared to other European nations. In five of the six key measures of performance - including water quality, customer service and costs - it is either the top performer or the most improved. Analysis by Water UK states that around 90% of customers are satisfied with their water service and that 86% trust their water company.

The future of the water sector

Our planning horizon goes beyond 25 years plus and we believe that a business that wants to be financially sustainable over the long-term first needs to be socially and environmentally sustainable. It also needs regulators and customers to share our long term vision for a brighter future for the sector. Despite our sector's significant achievements to date there remains much to do. Some of the key challenges facing the water sector include climate change, population growth and developing the trust of stakeholders through continuing to behave responsibly. We continue to respond to these challenges and believe the actions we are taking now can have a significant impact on our ability to be successful in these areas in the long-term.

In April 2019 we were delighted to launch the World Water Innovation fund, bringing together the most forward thinking water companies across Europe, the Americas and Australia. The fund aims to find, develop and accelerate the ground-breaking technologies that will make a real difference across the world. The first area of focus will be leakage – reflecting the importance we place on this sector-wide issue.

We're also taking a national perspective by working with other water companies and partners in the UK to explore ways in which water can be traded across water company boundaries. Currently only 4% of water supplies are transferred between water companies. We are working hard on planning an interconnector to move water from the wettest parts of England and Wales to the driest, for the benefit of customers across the sector. Plans for our new interconnector are described on page 33.

This has been a pivotal year in our regulatory cycle. Our regulatory framework continues to evolve and in the next 5 year period we will see the opening of the Bioresources market, enhanced Outcome Delivery Incentives ('ODIs') and a new measure of customer satisfaction, C-Mex. We welcome this change, as C-MeX will ensure that the totality of the experience of all our customers is represented.

Our regulatory framework

As a provider of an essential public service we work within a wide ranging regulatory framework, with strategic and policy direction provided by the Department for the Environment, Food and Rural Affairs ('Defra') in England and the Welsh Government in Wales. Ofwat is the industry's economic regulator and sets limits on the prices we can charge our customers over five-year Asset Management Plan ('AMP') cycles. This financial year was the fourth of AMP6, which runs from April 2015 to March 2020.

We also work closely with a variety of other regulators and public bodies, including:

• The Drinking Water Inspectorate ('DWI') independently checks that water supplies in England and Wales are safe and that drinking water quality is acceptable to consumers. Its work includes assuring water quality, ensuring companies make the changes necessary to improve, and developing new regulations to further improve water quality.

• The Consumer Council for Water ('CCW') speaks on behalf of water consumers in England and Wales. It provides advice to consumers and takes up complaints on their behalf.

• The Environment Agency ('EA') allows us to collect water from reservoirs, rivers and aquifers and return it to the environment after it's been used by our customers and treated by us.

• Natural Resources Wales is the environmental regulator in Wales. It oversees how the country's natural resources are maintained, improved and used, both now and in the future.

• Natural England advises the Government on the natural environment in England and helps to protect nature and the landscape, especially for plant and animal life in both fresh water and the sea.

• The Health and Safety Executive helps us to manage risk to ensure the health and safety of our employees, customers and visitors is preserved.

A key year in the regulatory cycle

Every five years, Ofwat reviews the prices we charge for the forthcoming five year period. They also review our plan setting out how we intend to deliver for customers and the environment. In September 2018, we submitted our Severn Trent Water and Hafren Dyfrdwy business plans for AMP7, which run from 2020-2025. These plans were the outcome of over 24 months of development.

Severn Trent Water's Plan

Our Severn Trent Water plan was shaped by the largest engagement exercise we have ever coordinated, consulting with 32,000 customers and considering a further 1.9 million customer views. As part of this we established new methods of listening to our customers, such as our online "Tap Chat", which enabled customers to give us rapid feedback on our proposals.

We are committed to continued improvements in core areas of our service. Our plan includes a series of service innovations to reflect our customers' changing needs, and a package of new commitments that aim to make a bigger contribution to the communities we serve, supported by our new community dividend. We will also invest over £6 billion over the next five years, ensuring we continue to build a lasting water legacy for future generations.

At the same time we'll deliver our largest bill reductions in a decade. By challenging ourselves to be 13% more efficient in the way we invest, we will be able to invest more to improve our services to customers whilst delivering a bill reduction for customers of 5% in real terms over the next AMP, maintaining the lowest bills in England over AMP7.

We are proud of our work as a pathfinder purposeful company and are pleased this was recognised by Ofwat who commended us on our 'pathfinding social purpose company' thinking and for our initiative with the Purposeful Company Task Force. We believe that if we're united by a clear social purpose, we'll deliver better outcomes for all our stakeholders – our customers, our colleagues, the society we live in, and the environment that we depend on.

We were delighted that Severn Trent Water was one of only three companies to be awarded fast-track status by Ofwat. We see this as a firm endorsement of our high standards of governance and focus on the sustainability of our business and our customer and community focused approach.

Ofwat has recently published its emerging strategy which sets out three main aspirations that are emerging for the sector - delivering every day excellence, stewardship for the future and value for individuals and society. We are very supportive of Ofwat's emerging thoughts and in particular its thoughts around encouraging companies to deliver public value.

Achieving fast-track status means we have clarity on the challenges and opportunities ahead. With our plan now agreed and commitments set a full 14 months before the start of the next AMP, we are accelerating our preparations. In March 2019, we announced details of the first key contractors we intend to use to deliver our circa £2 billion investment in construction projects for AMP7.

We received our Severn Trent Water draft determination in April 2019 and we're continuing to work constructively with Ofwat on our response.

<u>And in Hafren Dyfrdwy</u>...

In July 2018 we launched Hafren Dyfrdwy – our new water Company dedicated solely to customers in Wales, bringing together all the Welsh customers previously served by Severn Trent Water and Dee Valley Water.

Our Hafren Dyfrdwy business plan was classified as significant scrutiny by Ofwat. This was not unexpected, given that Hafren Dyfrdwy was a new Company and had a lack of historical data. We were pleased that Ofwat's initial assessment recognised the progress made on our cost base over the last two years and the certainty provided by our Totex plan being approved. We have continued to work constructively with Ofwat on the resubmission of the Hafren Dyfrdwy plan to deliver the right outcome for our Welsh customers. The Hafren Dyfrdwy plan was resubmitted in March 2019.

<u>What's next?</u>

Hafren Dyfrdwy draft determination – July 2019

Final determinations for all companies – December 2019

<u>Working in a changing macro environment</u>

The macro environment is changing rapidly and there are three areas which we are particularly focussed on. The Chairman comments on the debate around the future of the water industry in his statement on pages 5 to 6. The current uncertainty around Brexit has had implications for water companies that extend beyond financial matters. An area of focus over the last 12 months has been to put plans in place to ensure that we can maintain access to sufficient quantities of imported chemicals for our treatment works in the event of a 'no-deal' Brexit. Additional detail can be found on page 64. Population growth, driving increased water demand, and climate change, are two of the biggest challenges facing our industry. We have recently committed to the five pledges made by all companies in our sector which respond to these challenges.

Chief Executive's Review

DELIVERING VALUE FOR STAKEHOLDERS

"We are the custodians of a precious resource – water is vital to everyone across the world. As we build the next phase of our journey to deliver for our customers, employees and the environment we pledge to be a force for good in the communities we serve and, in doing so, create value for all our stakeholders."

Liv Garfield
Chief Executive

This has been a pivotal year for Severn Trent and one I'm incredibly proud of. We put together the most ambitious business plan in our history and I'm personally delighted we were given Fast-Track status for the first time, showing Ofwat shares our belief that customers will get the best possible outcome from our plans for the next AMP. It's a great testament to everyone who was involved in pulling the plan together, especially to our customers who helped us create the proposals.

We're proud of our financial and operational performance. We demonstrated resilience and flexibility in our network throughout the prolonged hot, dry weather over the summer - which saw a 22% increase in demand for water from our customers at peak times. This intense activity would not have been possible without the hard work and dedication of our people across the business. And I could not be more proud of the way they responded, without us having to impose hosepipe bans or other restrictions. You can read more about our operational performance in the performance review and our financial performance in James' financial report.

I'm also delighted that Ofwat commended us for our 'pathfinding social purpose company' thinking and our initiative with the Purposeful Company Task Force. In being united by a clear social purpose, we'll deliver better outcomes and build trust between all of our stakeholders.

So, in this year's CEO review, I want to share how our plan will deliver for our customers, the environment and wider society, our people and those supporting us on our long-term journey.

Our customers: at the heart of our plan

32,000 customers had a direct say in development of our plans and a further 1.9 million views helped shape its creation. Our absolute priority is to improve services for all of our customers in areas that matter most to them. We work night and day to create a service that's so good that our customers would still choose us, if they had the choice. So, our plan aims to deliver just that.

Affordability is right at the top of our agenda and we'll be reducing bills by five per cent in real terms. And we already have the lowest bills in England and Wales. We'll be investing £6.6 billion over the next five years and helping nearly 50% more of our customers who are genuinely struggling to pay their bills.

Improving our environment is a key area of focus for us and our plan is not just to protect the environment, it's to significantly improve it. We already work hard to make sure that the impact we have is as positive as possible and we'll be partnering with an extra 2,000 farmers to improve the quality of our raw water supplies. You'll find more on our great performance in this area within our performance review section.

As I've already mentioned, our social purpose ethos aims to build trust between our stakeholders. Three of the things I'm personally most proud of are:

- Our new community dividend through which we will invest 1% of our profits in community projects - a really exciting opportunity to make a positive impact in our region.
- Our commitment to the Social Mobility Pledge - helping people from disadvantaged backgrounds across our region become part of the Severn Trent family and succeed within our business.
- We're getting even more involved in the communities in which we live and work, for example through our Wonderful Water Tour - an innovative educational roadshow that every primary school in the Midlands will have the chance to take part in.

We're committed to creating a more resilient water sector in England and Wales. Key to this is ensuring that water can be traded across water company boundaries. So, we are working hard on feasibility planning for an interconnector to move water from the wettest parts of England and Wales to the driest, for the benefit of customers across the entire sector. Collaborating with other water companies is a great example of how the sector is focused on customers in all parts of the country, not just in their own regions.

Major projects such as this require significant investment. And the last year has seen the largest capital spend in our history. These schemes will deliver a better service and Totex efficiencies for our customers - ensuring a reliable supply of water for generations to come. We've made excellent progress on the Birmingham Resilience Programme which is the biggest water enhancement project in the sector in AMP6, with 25 km of the pipeline already installed. This is on track for completion by the end of the year.

Our AMP7 investment plans are well underway, and we've announced the first contractors we intend to use to deliver our circa £2 billion investment in construction projects over the next AMP. And we're also creating a new specialist design team. By investing in the professional expertise of our people we will further improve the reliability and availability of our assets.

Following year end, we launched our World Water Innovation Fund in April. Joining forces with like-minded companies across the globe to find new ways of working – pooling resources and ideas to develop and accelerate new technologies. Our £5 million investment in the Fund will make a real difference to people's lives across the world and I'm really excited about what we can achieve by working together. The initial focus will be on leakage and we have already invested ourselves in innovative ways of finding leaks faster, and fixing them more efficiently, and I'm pleased that we have started to see some encouraging results.

Our people: delivering our plan for customers, every day of the year

Our people work around the clock to keep wonderful water flowing and treating waste for our customers all year round, day and night. So they can be their best, we work hard to be the best employer we can be. We're constantly looking for new and better ways to help our people do their job more effectively, fulfil their potential and make them feel valued. In doing so, we improve the service we deliver to our customers. So, we're continuing our investment in training – through our new Severn Trent Academy – when completed this will train our engineers and leaders of the future, giving our people growth, development and more rewarding careers.

Over 90% of our people took part in our annual employee survey this year, giving us great feedback on what we're doing well and where they expect us to do better. We're pleased that we were rated among the Best 100 Companies to Work For again, and that 74% of our workforce would recommend us to a friend.

I'd like to thank our people for their amazing contribution to the communities they work and live in. Over 1,900 days were dedicated to our volunteering scheme, Community Champions. We worked alongside partners such as the Canal and River Trust to improve 34km of riverside environment, and in AMP7, we're expanding the volunteering programme to include working with Heart of England Forest to create and protect a huge broadleaf forest across the Midlands.

Our environment: investing for the benefit of all

We're look after some of the UK's most impressive natural resources. We've improved the biodiversity of a further six hectares of Sites of Special Scientific Interest and we're on track to reach our target of 75 hectares by 2020. We're proud of our environmental performance, with rivers in the UK, including the rivers Severn, Trent and Dee in our region, being cleaner than at any time since the industrial revolution.

Water scarcity remains a huge challenge for the water industry across the world – so it's vital that our customers know how to use water wisely. Our Wonderful Water Tour aims to inspire a generation to stay hydrated while reducing water consumption and being more careful about what they put down the loo and sink. And the World Water Innovation Fund will be exploring innovative ways to reduce water scarcity on a global scale.

Long term sustainability for long term investors

We believe that a business driven by social purpose and sustainability aligns with the interests of investors over the long term. Delivering against the customer, social, environmental and financial commitments we have made for the next five years will yield financial outperformance that can be shared with all stakeholders.

Looking to the longer term, we will continue to invest in our asset base to meet the emerging environmental and societal needs of the region we serve. Working with like-minded organisations to tackle the big issues the industry faces will ultimately deliver a more sustainable long-term investment proposition with attractive returns for those that choose to come with us on our journey.

Looking forward

We are driven by our social purpose. To be a financially sustainable business we first need to be socially and environmentally sustainable.

With our plan agreed and performance commitments set well before the start of the next AMP. Our teams now have to deliver everything we've promised, to set us up for continued success in AMP7. Whether that's keeping bills low, improving our services, or having a really positive societal impact on our communities. It's going to be a real challenge and it's one we're confident we can meet.

Liv Garfield
Chief Executive

How we are doing against our strategic objectives

1. Embed customers at the heart of all we do

We'll improve the way in which customers engage with us through improved insight and understanding of what's important to them

What we said we would do in 2018/19

- Build greater capability in incident management focusing on continuous improvement.
- Develop the use of the 'Wonderful on Tap' brand to increase the focus of all colleagues on enhancing the quality of our products and customer service, and increase engagement on the things that matter most to them.
- Deliver on the things that matter most to our customers as measured in Customer ODIs.
- Provide a service that is affordable for all and support our financially vulnerable customers by assisting 50,000 customers with their bills.

Our progress in 2018/19

- We've continued to offer a range of support schemes to help our customers struggling to pay their bills. Our aim is to support at least 50,000 customers each year while continuing to evolve our offers of support and our priority services register. We're already significantly expanding the scope and offers of support available. Alongside this, our Big Difference scheme continues to offer up to 90% discounts for customers that are struggling to pay their bills.
- We've maintained our position delivering the lowest bills in England (Severn Trent) and Wales (Hafren Dyfrdwy). Based on our PR19 Business Plans, we are set to continue this position to 2025.
- We've delivered another good year on Customer ODIs, delivering outperformance equivalent to £91 million. And we agreed with Ofwat to uncap ODIs on our waste water measures. This will help us deliver even more progress this AMP on the areas that matter most to our customers.
- We've made a number of changes to our operating model, including to the design and operation of our Network Control room and increasing availability of real-time data. For example, we've used 100 high pressure loggers across our network to identify pressure transients and modify the systme control on booster pumps to mimise them.
- We applied the learnings from the Freeze Thaw event in March 2018 during the prolonged hot, dry weather this year– which saw a 22% increase in demand for water from our customers at peak times. We demonstrated resilience and flexibility in our network during this time and focussed on prioritising resources to meet the additional demand and minimising the impact on our customers.
- We've increased our customer engagement including running our first ever TV ad to promote water efficiency.

Areas of focus for 2019/20

- Providing a service that is affordable for all and support our financially vulnerable customers.
- Maintaining the lowest bills in England (Severn Trent) and Wales (Hafren Dyfrdwy).
- Delivering on the things that matter most to our customers as measured by Customer ODIs.
- Further improving our incident management capability to ensure we can maintain an uninterrupted supply of clean water to our customers.

2. Drive operational excellence and continuous innovation

We'll build a smarter water and waste water network and develop our business intelligence and simplify our cross business processes.

What we said we would do in 2018/19

- Deliver our plans to be Upper Quartile for Retail, Water and Waste.
- Continue to provide environmental leadership.
- Make further progress on the quality of our water as measured by the DWI's Compliance Risk Index.
- Regain self-assured status for our English business.

Our progress in 2018/19

- Our performance across Waste – service and cost efficiency – remains sector leading. And our PR19 plan placed us in the upper quartile for Waste. In fact, Ofwat have asked us to share best practice with other companies so that customers across England and Wales can benefit from improvements on external sewer flooding performance. In water, we've delivered substantial second half improvements, giving us confidence for 2019/20 and beyond. We are continuing to make improvements in Retail.
- We've successfully delivered two key environmental commitments – overall environmental performance and catchment management, enhancing the quality of our raw product and reducing the level of treatment. We've also made good progress on our Water Framework Directive and biodiversity commitments. Unfortunately we've seen an increase in serious pollution incidents this year and we're putting extra resources in place to make improvements in this area.
- We remain in the targeted assurance category this year, with Ofwat assessing over 80% of measures as 'meets expectations'. All measures were assessed as 'minor amends' or above meaning that Ofwat has no major concerns with the way in which we report our performance to customers and stakeholders.
- We've continued to make strong progress, as a result of our additional investment made earlier in AMP6. We are working really hard on further improvements in this key area.

Areas of focus for 2019/20

- Retaining our strong performance on Waste, while making improvements or Retail and Water service;
- Delivering our environmental commitments including on the Water Framework Directive and Biodiversity;
- Retain a minimum of targeted assurance and all measures assessed as 'minor amends' or above.
- Sharing best practice with other companies so all customers across England and Wales can benefit from the improvements we've delivered in our region on external sewer flooding.

3. Invest responsibly for sustainable growth

We'll develop an effective strategy which optimises our regulated asset base whilst creating new growth opportunities for the future.

What we said we would do in 2018/19

- Deliver fully on our PR14 (AMP6) investment commitments, being confident that we are able to deliver against our current plans and make appropriate investments for the future.
- Achieve material improvements in some of our key ERM risks.
- Drive a focus on efficiency across all business areas including central functions to support frontline investment.
- Continue to embed innovation across the Company, making it part of every team's way of working.

Our progress in 2018/19

- We've invested over £1 billion this year to ensure we have a resilient network and asset base capable of delivering our services now and into the future. This includes two key investment commitments where customers are protected by customer ODIs – Birmingham Resilience and the Water Framework Directive.
- We've made significant progress on addressing property compliance risks, and continue to make improvements to achieve our target position by the end of the AMP. However our underperformance on key risks means our performance on ERM risks has remained static, see Principal Risks section
- Over AMP6, we have locked in £450 million of efficiency. We've achieved this through a range of initiatives including the roll out of standardised products, embracing 'plug and play' construction, and using smart programming to best utilise assets and resources. We have chosen to reinvest £120 million of this efficiency saving into security, water quality and vulnerable customers, and a further £100 million in smart data.
- We proved financially resilient, during the prolonged hot, dry summer - and were able to absorb the increased costs associated with pumping up to an extra 400 million litres per day and 24/7 use of a fleet of water tankers to top up service reservoirs.
- We launched our World Water Innovation Fund in April 2019, joining with like-minded companies from the UK, the Americas and Australia, to find new ways of working, and make a huge difference to our sector.
- Our cross-team communities of practice continue to develop novel approaches and share best practice with the aim of delivering targets in 2019/20 and meeting the 15% leakage challenge in AMP7.

Areas of focus for 2019/20

- Promoting a more sustainable way of working which looks beyond traditional end-of-pipe solutions (including our partnership working and sustainable sewage treatment commitments);
- Developing the World Water Innovation Fund to help find new ways of working and to leave a lasting water legacy for future generations; and
- Continuing to progress our understanding of the impact of climate change on our long-term service delivery, using the UK Climate Projections 2018 published by the Met Office.

4. Change the market for the better

We'll embrace market opening in the UK and explore opportunities for growth in new water markets.

What we said we would do in 2018/19

- Produce compelling cases for investment at PR19 that enable strong RCV growth over AMP7 and AMP8.
- Deliver phase two of the energy and renewables strategy to achieve 50% self-generation.
- Build a sector leading approach to bioresources.
- Finalise the creation of Hafren Dyfrdwy and deliver a great first year.

Our progress in 2018/19

- We've received fast-track approval for our PR19 business plan for Severn Trent Water. The Totex allowance drives strong RCV growth, with Ofwat's modelled cost allowance having reflecting many of the areas we had highlighted for improvement in AMP7.
- We're on-track to exceed our 50% self-generation target by the end of AMP6
- Ofwat's assessment of our PR19 business plan recognised our leading approach for bioresources.
- The Hafren Dyfrdwy licence came into effect on 1 July – we've invested in improvements in both the technology platform and asset base. There is more to do to improve performance on the measures that matter most to customers at a cost that is affordable, and we are putting extra resources in place to do this.

Areas of focus for 2019/20

- Working progressively with Ofwat to finalise the PR19 outcome.
- Delivering our ambition of 50% self-generation.
- Progressing the development of regional water trading solutions, including the North to South interconnector.

5. Create an awesome place to work

We'll create a culture of empowerment and accountability, with a focus on skills, talent and career development.

What we said we would do in 2018/19

- Deliver a further step change in our safety performance and support the wellbeing of our colleagues.
- Continue to build on our strong volunteering performance and drive the Corporate Responsibility agenda.
- Continue our focus on improving overall QUEST engagement scores.
- Deliver the foundations of the new Training Academy, to make a positive contribution to technical development.

Our progress 2018/19

- We were awarded silver in the Mind Workplace Wellbeing Index 2017/18. Our health and safety performance is upper quartile within the sector and we experienced no major safety incidents and no fatalities in the last 12 months. We did see an increase in Lost Time Incidents ('LTIs'), mainly due to slips, trips and falls. We have detailed plans in place to address this, with new data analytics being used to identify specific areas for improvement. Progress against these areas is considered at the Employee Forum, Executive Committee and Board. In April 2019 we revamped our Goal Zero Strategy, with dedicated quarterly awareness campaigns.
- Over the last year, Community Champions, our volunteering programme, has supported over 1,900 colleagues to make a difference by helping to make our region's waterways even healthier and supporting our local communities.
- We're are also pleased to maintain our strong engagement scores following our QUEST survey – completed by over 90% of our workforce – placing us five points above the average benchmark for UK and Ireland. This is great news, especially given the extra commitment of our people this year in the difficult circumstances during the prolonged hot weather over the summer.
- We're on-track to deliver our Training Academy by Spring 2020. Ensuring our people have the right mindset, technical competence and leadership skills for now and in the future. We've repurposed an existing building to provide a greener solution, and are developing an exciting syllabus that uses state-of-the-art training techniques including virtual reality and network simulation.

Areas of focus for 2019/20

- Delivering an improvement in our safety performance through focused interventions.
- Maintaining our commitment to the wellbeing of our colleagues.
- Continuing to implement improvements identified by our QUEST engagement.
- Developing an exciting and innovative syllabus for our new Training Academy.

ODIs and KPIs

We continue to make progress against our customer ODIs and financial KPIs.

Progress against our Outcome Delivery Incentives[1,2,3]

1. Embed customers at the heart of all we do

1.1 Internal sewer flooding[4]

Actual

729

Reward/Penalty

873

Rate of Reward/Penalty (per incident)

£42,820[1]

Why we measure it

To ensure we do everything we can to prevent flooding of customers' homes or businesses. It is one of our customers' most important priorities.

Progress in the year

We agreed with Ofwat to strengthen our performance commitment on internal sewer flooding from 1 January 2019, see page 27 for further details. We are reporting a performance of 729 incidents, ahead of our adjusted performance commitment of 873.

1.2 External sewer flooding[4]

Actual

3,795

Reward/Penalty

6,499

Rate of Reward/Penalty (per incident)

£2,967[1,5]

Why we measure it

To ensure we do everything we can to prevent flooding of customers' homes or businesses. It is one of our customers' most important priorities.

Progress in the year

We agreed with Ofwat to strengthen our performance commitments on external sewer flooding, from 1 January 2019, see page 27 for further details. We also agreed to reduce our incentive rate from £19,779 to £2,967 at this time. We are reporting a performance of 3,795 incidents ahead of our adjusted performance commitment of 6,499.

*footnotes are included on page 22

1.3 Minutes without supply

Actual

19.7

Penalty

12.0

Reward

9.4

Rate of Reward/Penalty (per minute)

£1.10m[1]

Why we measure it

Our customers value water being there when they need it. This performance commitment ensures we are driving down the impact of any interruptions to supply across our network to minimise the impact on customers.

Progress in the year

We have interrupted customers' supply for an average of 19.7 minutes, higher than our committed performance level of 9.4 minutes.

1.4 SIM – Customer experience

Not yet defined by Ofwat

81.45 SIM score

Why we measure it

Providing good quality service to our customers is key and the Service Incentive Mechanism ('SIM') provides us with a regular opportunity to understand our performance and implement initiatives to improve the quality of service we provide, but also deliver value for money.

Progress in the year

We have reported a SIM score of 81.45 for 2018/19, which is below our target of upper quartile.

1.5 Complaints about water quality

Actual

11,923

Reward/Penalty

9,992

Rate of Reward/Penalty (per complaint)

£900[1]

Why we measure it

Customers value the aesthetic quality of their water. This performance commitment is designed to ensure we manage our network to minimise the number of events that cause discolouration, taste or odour problems.

Progress in the year

During the year the number of drinking water complaints reduced from 12,687 to 11,923, higher than our committed performance level of 9,992.

*footnotes are included on page 22

2. Drive operational excellence and continuous innovation

2.1 Improvements to river water quality

Actual

87

Penalty/Reward

233

Rate of Penalty/Reward (per qualifying point)

£750,000[1]

Why we measure it

We have statutory obligations to deliver, but our customers told us that we should do more where we can. This performance commitment ensures we meet our obligations and drives us to make faster progress more where it is possible.

Progress in the year

We have delivered 53 qualifying Water Framework Directive points during the year and our cumulative total is 87. We are on track for our end of AMP target of 233.

2.2 Number of category 3 pollution incidents

Actual

329

Reward/Penalty

374

Rate of Reward/Penalty (per incident)

£53,900[1]

Why we measure it

Minimising the impact our activity has on the environment is a key concern for our customers. This performance commitment ensures we drive to improve performance in this area.

Progress in the year

We are reporting 329 Category 3 pollution incidents against an adjusted performance commitment of 369 incidents.

2.3 Successful catchment management schemes

Actual

26

Penalty/Reward

12

Reward Cap

21

Rate of Penalty/Reward (per scheme)

£1.03m[1]

*footnotes are included on page 22

Why we measure it

Our customers want us to look for new and innovative ways to improve water quality, whilst working in partnership with other stakeholders to deliver wider benefits. This performance commitment focuses on how our approaches are encouraging farmers and land owners to change their behaviour and practices.

Progress in the year

We have delivered 26 catchment management schemes, well ahead of our performance commitment.

2.4 Asset Stewardship – coliform failures

Actual

13

Penalty

5

Rate of Penalty

£463,000[1]

Why we measure it

The presence of coliforms in our drinking water is unacceptable as it is an indicator of poor quality so we continually monitor our works to ensure we are producing high quality water.

Progress in the year

During the year we detected coliforms at 13 of our water treatment sites, which is higher than our committed performance level of five.

2.5 Leakage

Actual

427

Reward/Penalty

429

Rate of Reward/Penalty (per mega litre per day)

£123,000[1]

Why we measure it

Customers see leakage as a waste of a key resource; our customers want us to reduce our level of leakage as a priority.

Progress in the year

We are reporting an outturn of 427 Ml/d which is marginally ahead of our performance commitment of 429 Ml/d.

*footnotes are included on page 22

3. Invest responsibly for sustainable growth
See our performance review on pages 23 to 38.

4. Create an awesome place to work

4.1 Lost time incidents per 100,000 hrs worked
0.3

2017/18: 0.17

4.2 Employee engagement score improvement[6]
No change

2017/18: 6 percentage points

Progress against our financial KPIs[7]

Turnover	Group PBIT	Group Underlying PBIT[8]
£1,673.1m	£557.7 million	£567.3 million
(2017/18: £1,606.9m)	(2017/18: £525.1 million)	(2017/18: £537.7 million)

Notes

1 In 2012/13 prices after tax.

2 These are also key measurements used to assess our Corporate Responsibility performance.

3 We have reported performance on our customer ODIs on a comparable basis by reporting the current year performance for the Severn Trent Water region that was in place during 2017/18.

4 Targets have strengthened from 1 January 2019, see page 27 for more information.

5 Incentive rate reduced from 1 January 2019, see page 27 for more information.

6 Engagement index used since 2015/16 to support benchmarking and gain better insight about us as an employer.

7 See Financial Review on pages 39 to 46.

8 Alternative Performance Measures are defined in note 43 to the financial statements.

Performance Review

The Severn Trent Water group includes Severn Trent Water Limited and Hafren Dyfrdwy Cyfyngedig. Unless stated otherwise the information in this section relates to Severn Trent Water which makes up 98% of our total customer base.

Embedding customers at the heart of all we do

From the Bristol Channel to the Humber and from Rutland to North Wales, we play an essential role in the lives of 4.5 million households and businesses. We provide them with around 2.0 billion litres of high quality drinking water daily, and treat around 2.9 billion litres of waste water every day.

As part of the development of our Severn Trent Water PR19 plan, we focussed on customer insight gleaned from our most intensive customer engagement activity in our history. This gave us a solid foundation on which to create a comprehensive, detailed business plan – one that was co-created with customers and put their wishes right at its heart. As we developed the plan we asked our Customer Challenge Group, the Water Forum, to rigorously challenge every aspect of our customer engagement to make sure we'd addressed the issues most important to them. The Forum gave us really constructive feedback that led to us making further changes and reassured us that we really were putting our customers first.

<u>The issues that matter</u>

Our engagement programme confirmed that the issue that matters most for our customers continues to be affordability – keeping bills low for our essential service is their top priority, as well as making sure that our most vulnerable customers have the support they and their families need.

Their next most important issue is something that's fundamental for us as a business – providing a reliable supply of clean water and taking away waste water without customers having to worry about it.

Customers also want us to continue to invest in infrastructure, not just for today but for future generations, in the same way that the Victorians did for us. They also want us to have a positive impact on our local environment and in the communities we serve. And they want to be able to talk to us if, when and how they want to, whilst also keeping them informed about what we're doing.

This detailed engagement means we truly understand what matters to our customers – and that gives us a huge amount of clarity around what we have to do for them in the months and years ahead.

So, if those are the issues on customers' minds for the future, how are we doing on those today?

<u>Reducing customer bills</u>

This was the ninth consecutive year that Severn Trent Water customers have enjoyed the lowest bills in England. Our average combined bill for the year was £348 - less than £1 a day - which was more than £59 lower than the average bill and £152 lower than the highest. Similarly our Hafren Dyfrdwy customers enjoyed the lowest bills in Wales at £311. Over the next five years, we're going to be reducing bills by a further 5% in real terms, whilst at the same time investing more and making further improvements to the services we offer customers. In Hafren Dyfrdwy we're increasing investment by 4% per customer to improve services, whilst limiting the increase in customer bills to 1.9% in real terms over the five year period.

We understand that even though our bills are low, some customers have difficulty paying - so we do everything we can to help those who are genuinely struggling to pay their bills. We do this through a range of measures, such as water saving devices and fitting meters for smaller and low occupancy households. We also offer our Big Difference Scheme which has helped over 37,000 customers who are genuinely struggling to pay their bills, access discounts of up to 90% over the last 12 months.

Looking ahead, we intend to help even more of our customers. For example, our PR19 plan includes a commitment to support almost 50% more people between 2020 and 2025, through schemes such as our social tariff and through other options, such as payment breaks.

<u>Working hard to provide the quality service that customers expect</u>

Our waste water performance continues to be sector leading both in terms of performance and efficiency. We have continued to reduce the number of sewer flooding incidents that occur on our network, that we know can lead to the worst possible experience for our customers. We will never be complacent about our performance and will continue to push for year-on-year improvement through further investment.

After demonstrating strong customer support for our proposal, we were pleased that, in December, Ofwat agreed to lift the customer ODI cap on our waste water measures for the remainder of the AMP. This supports customers and the environment even earlier than previously agreed with Ofwat.

This year, we have made continued progress on key clean water metrics such as water quality complaints, with a further 6% improvement, delivering complaint numbers which are the lowest for [six years]. We've also worked well with our supply partners to resolve issues on 35 properties which were at risk of low pressure. We're continuing our multi-year journey to improve our coliform performance in our distribution service reservoirs, surface water works and groundwater works – for which coliforms are a key measure of asset health. The ODI measure focuses on coliform detections at surface and groundwater sites, which have increased slightly this year. Our investment in distribution service reservoirs has delivered significant performance improvements, and we are confident that the next phase of our plan will deliver similar improvements in the ODI measure next year.

The resilience of our water supply was tested through one of the hottest, driest summers on record – which saw a 22% increase in demand for water from our customers at peak times. We worked tirelessly to give our customers the level of service they expect and deserve, without the need for a hosepipe ban or other restrictions.

Supply interruption events were impacted during this period and this has affected our full year performance. We have increased our efforts in this area, our focus being on 'prevent, restore, repair'. And during the last quarter of the year we saw some encouraging improvements in supply interruptions performance. Additional information can be found on page 28.

We are particularly pleased with the progress we are making in partnership with landowners and farmers across our region to improve the ecology of rivers in our region. Our industry leading Catchment Management Programme has yielded great results over the past year and demonstrates the power of strong collaborative working. We talk more about this on page 30.

<u>Investing for future generations</u>

This year has seen our biggest single year of capital investment in the last decade, demonstrating our commitment to continued investment in long-term infrastructure. All of our current major capital schemes made good progress during the year including our Birmingham Resilience Project, which is the biggest water enhancement capital project in the sector to be completed within AMP6. This will ensure security of supply to Birmingham for generations. Please see page 30 for more details on this and other key capital projects.

Listening, every moment of every day

We’ve made it easier for our customers to contact us through whichever mode they prefer, whatever the time of day. People can phone us, talk to us on webchat on the website, through various social media platforms, or write to us.

We also launched Tap Chat during the year. This new online community panel gives us feedback about how we’re doing and, more importantly, how we can do even better. With 15,000 active participants, representing all walks of life and areas across our region, Tap Chat played an important role in shaping our PR19 business plan and provides ongoing engagement with our customers.

Serving local communities

We’re very aware of the central role we play in our community – this is not only where we work, but where most of our employees live. We know that our customers want us to do more - to help improve the environment, to support education, and give something back.

We carry out an enormous number of projects to enhance rivers and other natural resources – many of them supported by our employees who dedicated over 2,000 days to volunteering during the year. Our supply chain also supports us in our environmental ambitions, undertaking a variety of charitable environmental projects such as the Water Walkway Project at Draycote Reservoir.

Looking ahead, through our new community dividend we will invest 1% of our profits in community projects – a really exciting opportunity to make a positive impact in our region. Our hope is that the community dividend will benefit thousands of our customers, together with their communities, to make a positive difference to their everyday lives. We are also doing more to engage with our customers of the future through the Wonderful Water Tour, see case on page 26.

Customers trust our performance

We are proud to have been acclaimed the most trusted water company in England, by the most recent independent customer satisfaction tracker. We feel that this reflects the huge progress we’ve made in delivering on the issues which matter most to customers: investing in the resilience of our network and renewable energy, as well as doing more for our most vulnerable customers.

We know we’ve still got more to do on SIM, Ofwat’s current customer service measure and we were disappointed to finish the year in fourteenth place. However, we were pleased to again be in the top quartile of utility companies in the UK Customer Service Index, which will be relevant in AMP7 when Ofwat’s new customer satisfaction measure (C-MeX) is set to be introduced. C-MeX will be partly based on customer contact, as with SIM, and partly on customer perception which is a much wider measure. We welcome this change as C-MeX will ensure the totality of the experience of all our customers is represented.

Helping customers to help us

Extra demand for water as a result of increasing population and climate change means it’s vital that our customers know how to use water wisely. First, we need to give them the right advice to help them save water. And second, we need to provide them with the tools they need to achieve that. Last year, we carried out 26,000 home water efficiency checks to help customers manage their consumption, save money and protect future supplies.

Here when you need us

We can't deliver great service to our customers unless we're aware of the issues that matter to them. So it's important that they can contact us at a time that's convenient to them. We offer a wide range of contact channels – they can ring us, talk to us through our livechat on our website or via social media. They can even write us a letter if they prefer. Whatever method they choose, they will be certain of a response. More than 1.9 million customers are now signed up to our online offerings and, during the last year, our web self-serve platform handled more than 1.6 million customer contacts. And the hard work of our customer communication team was recognised by a Silver Award at the European Contact Centre and Customer Service Awards.

Engaging with the customers of the future

We're getting even more involved in the communities in which we live and work, for example through our Wonderful Water Tour – an innovative educational roadshow that every primary school in the Midlands will have the chance to take advantage of. The Wonderful Water Tour is targeted at children aged between seven and 11, to inspire them about water. Comprising two buses and a whole host of gadgets and hands-on activities, the Tour educates children on three key messages: the importance of using water wisely; helping them understand what they can, and can't, put down the toilet and sink; and the health benefits of staying hydrated. During the last 12 months, our tour has engaged with over 130,000 young people, and will be available across our region from 2020-2025. The Severn Trent Wonderful Water Tour helped launch our Wild Water topic with a splash! It inspires and educates the children, catering for all children's interests and abilities. "The knowledgeable, friendly and helpful staff engaged the children at all times and helped bring our water topic to life." Tracey Gillin, St Anne's Catholic Primary School, Nuneaton

Driving operational excellence and continued innovation

Our customers expect us to improve our core services every year. That means providing them with clean drinking water which is there when they need it – and taking waste water away efficiently before recycling it safely to the environment.

We're committed and long-term supporters of Ofwat's Outcome Delivery Incentives, which reward companies when they exceed targets for measures that customers feel are the most important, and also penalise companies for poorer performance. In our view, this is the best way to ensure high quality performance for the benefit of all stakeholders – our customers and communities, our investors and the environment. We've agreed with Ofwat to share our expertise with the rest of the industry so that all customers in England and Wales may benefit.

We've continued to deliver on our track record in the waste water measures that customers have told us are the most important. Overall, 2018/19 was also an encouraging year for our water performance as we continue to make progress on our multi-year improvement journey on water quality and provided a high quality product to our customers, whilst protecting public health.

Another strong year for waste water performance

Removing waste water safely and efficiently is hugely important for customers - so we're very pleased to report that our track record continued during 2018/19 with significant outperformance against internal and external sewer flooding, Category 3 pollution targets and a whole host of other environmental measures.

On a like-for-like basis, we earned £103.1 million from waste water ODIs in the year which was reduced to £7.1 million by the impact of the regulatory cap imposed by Ofwat and changes to our ODI incentives and targets for the remainder of the AMP. After providing evidence of support from our customers, in December 2018, Ofwat agreed to raise the cap and we accepted even more challenging measures. This will allow us to deliver an even better service for customers earlier than previously planned and to continue to drive improvements in the industry.

Sewer flooding

We've continued our focus on sewer flooding and during 2018/19 we outperformed our internal and external sewer flooding targets by 16% and 41% respectively. We're continuing to drive performance through targeting proactive work on sewer flooding hotspots across our waste network.

Alongside investment in infrastructure we have used innovative chemical treatments to help reduce the build-up of fats, oils and greases ('FOG'). We're also working with communities and industries to reduce the amount of FOG that ends up in our sewers. Our programmes to educate customers and their children on sewer misuse are an important element of our approach, see case study on page 30 for more information. Additionally, we're identifying and taking legal action against businesses that clog our sewers with FOG and recovering operational costs in cases where prosecution is not possible. These are important factors in our goal to create a calm network and ensure an enhanced and sustained service provision into AMP7 and beyond.

Pollutions

We work hard to manage our impact on the environment. We were pleased to have continued to outperform against the challenging targets we set ourselves for Category 3 pollutions incidents. Our performance was flat year on year due to a challenging start to 2018. By re-doubling our efforts we've delivered significantly better performance in the second half of 2018 which we have sustained through the beginning of 2019.

We have more work to do on serious and Category 4 pollution incidents and are disappointed that we missed our targets on these measures. During the year we continued our programme to roll out more monitors which will significantly improve our ability to detect issues and prevent pollution incidents occurring in future. We are focussing our efforts on the highest risk areas to ensure we get the best possible outcome as quickly as possible.

Focussing on water quality and supply

Good progress on water quality

Following our renewed focus on water quality in recent years, complaints fell again by 6% during 2018/19 in line with the target agreed with the DWI. This builds on our achievements of the previous year when complaints were down by 12%. Water catchment initiatives have played a major part in this improvement and we're continuing to work with farmers and other stakeholders to raise the quality of the water that enters our rivers.

We have introduced new technology to drive further improvements in water quality in years to come by ensuring we proactively intervene to address risks to water quality. For example, bacterial analysis can take 30 hours from taking a sample to receiving a result. Our innovation team analysed technology across a range of different sectors and created a bespoke solution that is acknowledged as the world’s first online bacterial monitoring system. This gives us high quality analysis in real time, allowing us to identify issues quickly and take action to prevent bacteriological failures at our treatment works and distribution service reservoirs. By the summer of 2019, we will have 20 units available, most as fixed installations, as well as others that we can use on a mobile basis.

Meeting Water Demand

The summer of 2018 saw a period of prolonged hot, dry weather and we saw a 22% increase in demand for water from our customers at peak times.

We demonstrated resilience and flexibility in our network during this time – and focused on prioritising resources to meet the additional demand and minimising the impact on our customers. We proved financially resilient, and were able to absorb the increased costs associated with pumping up to an extra 400 million litres of water per day at peak times and the 24/7 use of a fleet of water tankers to top up service reservoirs. Our operations were largely resilient and we came through the heatwave without imposing any restrictions on usage such as a hosepipe ban. However, some of our water network measures, including supply interruptions, were adversely impacted during the period as outlined below. Our focus during this time was on prioritising resources to meet the additional demand and minimising the impact on our customers.

Supply interruptions

Supply interruptions ended the year at 19.7 minutes against our target of 10.8 minutes. We have increased our focus on this area and are starting to see definite improvements through our 'Prevent, Restore, Repair' strategy, which focuses on preventing asset failure where possible, and restoring supply at speed if it happens. Performance in the second half of the year improved by 64% and we delivered our best ever performance in February and March.

Over the last year we've achieved a dramatic improvement in the speed at which we arrive on site, which has significantly reduced – supported by our new video calling service which enables us to assess an issue remotely, deploy the right resources to site quickly and support us in fixing the issue, first time.

At the same time we’ve continued to invest in technology that provides us with valuable insight into how the network is operating. Technological innovations such as low point loggers, acoustic loggers and advance analytics are all now hard at work across our network. We now have 19,500 additional ‘eyes and ears’ on network and are on track to have 35,000 by the end of March 2020. Furthermore, we are focusing on understanding the true causes of failure which lead to supply interruptions and addressing them at source – investing in operating a calmer network to reduce the failure rate across our network.

Driving improvement in leakage

The first half of the year was operationally challenging, with the tail end of freeze-thaw followed by the hot, dry summer putting pressure on some of our key water measures. Our significant focus in the second half means we have hit our performance commitment for leakage and delivered a reduction year-on-year of 16ML/d by:

- maintaining our strong operational focus on leakage recovery and improving processes to reduce known network leaks - including a 67% increase in leakage fix teams;
- introducing innovative ways of finding leaks faster, and fixing them more efficiently – including accelerated installation of acoustic loggers, targeted WIP reduction and the use of more innovative solutions such as satellite technology; and
- spending time to better understand our leakage component data – giving us more clarity on how we can best target leakage and providing more accurate reporting going forward.

As in prior years, we base our customer ODI on 'unaccounted water'. The weather events earlier in the year, which led to an increase in pipe bursts and an increase in demand, also led to an increase in unaccounted water. The considerable momentum we generated has reduced this impact, though has still resulted in a penalty. Our key focus is now on retaining that energy to reduce leakage and hit our target in 2019/20, keeping us on the right track to meet the 15% challenge in AMP7.

As outlined on page 7 we have recently launched the World Water Innovation Fund – joining forces with like-minded companies across the globe to find new ways of working – pooling resources and ideas to develop and accelerate new technologies. Our £5 million investment in the Fund will make a real difference to peoples' lives across the world. The Fund's initial focus will be on leakage, which is a key issue for all companies.

Improving our environment

The way a company interacts with the environment it operates in has risen to the top of the agenda for all of our stakeholders. Increasingly, these groups expect utility companies to demonstrate performance beyond financial return. We take great care to understand and control the impact we have on the environment and in everything we do - when taking water from our rivers and reservoirs, and when safely returning it back to the river in a clean state.

We're committed to creating thriving bird, insect and plant habitats in our region. We improved biodiversity on six hectares of Sites of Special Scientific Interest ('SSSIs') during the year, and we're on track to reach our target of 75 hectares by 2020. By 2025, we're aiming to work with organisations such as the Wildlife Trust to improve biodiversity on a further 1,015 hectares. That's an area equivalent to 1,400 football pitches and represents more than a tenfold increase over our current target.

Managing our catchments

When it comes to improving water quality, prevention is always better than cure - so over the last year we've continued to make investments to ensure that the water that enters our rivers is as clean as possible in the first place. Known as catchment management, this approach reduces the significant cost of treatment at our works. Cleaner rivers mean that we have to use fewer chemicals - and that's far better for the environment. We've already established an excellent record in this area, particularly through the success of our Farm to Tap scheme. This innovative and industry-leading scheme has seen over 820 farmers sign up to protect raw water sources from pesticides and other chemicals - and resulted in peak concentrations of metaldehyde - an anti-slug pesticide which is expensive and difficult to remove at water treatment works – reducing by 64%. This is good news for the environment because it enhances biodiversity, good news for customers because it reduces treatment costs and enables us to invest elsewhere in the network, and good news for investors because it's generated some £11.4 million in customer ODI outperformance payments. We aim to expand our catchment schemes to include biodiversity options in our farmer grants and to increase grant uptake by 42% by 2025.

As well as putting significant new effort behind our Catchment Management initiatives, we've also been working with other partners to improve raw water. Rivers in the UK, including the rivers Severn, Trent and Dee in our region, are now cleaner than at any time since the industrial revolution.

Fighting the fat(berg)

A major cause of sewer flooding are blockages which can be caused by fatbergs, the industry's name for the build-up of wet wipes, fats, oils and grease into a solid mass which has potential to block pipework.

Our fight against fatbergs is based on education and prevention. For example, while cleaning the sewers of Stratford-upon-Avon in December 2018, we found and removed several build-ups that could have developed into major blockages. Working with 24 food service outlets and officers from Environmental Compliance and Services, we launched a programme aimed at educating catering outlets about the right - and wrong - ways to dispose of fats, oils and greases.

Making more informed decisions

Our continued investment in monitoring technology such as sensors and loggers has further informed our teams' decision making. In fact we have more data points than any other water company in England or Wales. Armed with real time awareness of supply and demand across our region, we're able to forecast stresses and strains on the network and proactively take action to ensure that customers are provided with an excellent service.

Proud to hold the Carbon Trust Standard

We've been proud to hold the Carbon Trust Standard since 2009. This certification recognises that we take a best practice approach to measuring and managing our environmental impacts. In the last 12 months, our Group net GHG emissions fell by 27%.

Improving raw water

We are working with our partner Moors for the Future on a project that's transforming a moorland area around Ladybower Reservoir. We've invested over £1 million during the current AMP to help re-vegetate 114 acres of peat, protect 16 hectares of blanket bog and dwarf shrub, and plant new trees across 170 hectares. This has cut peat erosion and protected one of our region's most diverse habitats, while also improving the quality of the raw water which will further reduce our treatment costs.

Investing responsibly for sustainable growth

Since privatisation, we've invested £22 billion in today's money and the pace and scale of our ambition continues to grow. In 2018/19, we invested over £750 million in our asset base as well as a further £141 million in renewing our infrastructure network. And we're on track with our commitment to invest £1,300 for every household we serve over AMP6.

We've worked hard to maximise the value we get from this investment and continue to forecast AMP6 Totex efficiencies of £870 million. These efficiencies have enabled us to re-invest £220 million to improve our water networks, making them more resilient and reliable through utilising the latest technology available. This investment will benefit customers today and also for generations to come.

Investing for today… and for future generations

Our mission is to create a lasting legacy for future generations. We do this by investing in new infrastructure, by exploring and investing in ways to provide additional capacity, and by taking our Wonderful Water Tour around schools to inspire the next generation to use water wisely.

We've replaced 230km of our water network, enabling us to make further progress on water quality and again meet the low pressure customer ODI target. We've also completed 28 capital projects to improve our waste network, helping us to maintain upper quartile on cost and performance.

All of our major schemes made good progress during the year, including the Birmingham Resilience project ('BRP'). This will secure a second source of water supply for Britain's second city and safeguard of one of our oldest, but most strategic and efficient, water resources for years to come. The BRP is the biggest AMP6 water enhancement capital programme in the sector and will be ready to deliver anticipated benefits to customers in 2020. Thanks to the way we have delivered the project it is on track to deliver supply resilience benefits - in the event of both water resource and treatment failures - and to enable effective proactive maintenance of some of our most important assets for the long term. This is the result of considerable hard work and effort from our people and supply partners, as well as some bold decisions, such as our decision in spring 2017 to replace our original supply partner. Progress in the year included completion of the 25km raw water pipeline that will transport water from the River Severn to our Frankley water treatment site.

In Nottinghamshire, we made great progress on a scheme to improve our services in Newark, where a £60 million programme will benefit 400 local homes and businesses. We're installing 4km of high volume sewers to reduce flooding risk, as well as 10km of new water network to improve water supply. We achieved a major milestone this year, with the completion of a 3km tunnel which encircles the town 15 metres below ground. This hugely complex project was carried out through the town centre and under a major railway line - and our efforts to limit disruption were acknowledged by the 'Community Engagement' Award at the New Civil Engineer awards for high-quality community engagement.

As part of our commitment to invest £1,300 for every home and business we serve in the five years to 2020, this year we started work on a new £11 million investment to improve the resilience and reliability of the clean water supplied to around 55,000 people in Stroud, Gloucestershire. The upgrade project will see 16km of new pipeline stretching from Minchinhampton reservoir to Whaddon.

<u>Seizing opportunities to improve our environment</u>

We have a duty - and a great opportunity - to use our experience, expertise and resources to protect local environments across our estate.

Environmental sustainability is hugely important to our capital programme, and we're constantly looking for ways to reduce our environmental impact. We're working on the development of innovative solutions at our sewage treatment works which will enable us to meet the needs of a growing population in a sustainable manner. We're on track to deliver a number of schemes in the final year of the AMP under our sustainable sewage treatment works ODI, including our site at Rugby.

We also remain committed to creating and sustaining cleaner rivers. We've invested significant time and resource to fulfil our obligations under the Water Framework Directive ('WFD') to achieve 'good' status for all watercourses. This year we have completed an additional 27 sewage treatment upgrades which are helping us improve over 430 km of river. We're on track to improve at least 1,600 km of our rivers in AMP6 - and a further 2,100 km in AMP7.

<u>New partnership model with our supply chain</u>

We revised our capital project operating model during the year in order to boost our internal capabilities and deliver better value, both for us and all our stakeholders.

Implementation of the new model began early in 2019 and, when complete, we will have a skilled and capable in-house team able to provide design and feasibility study services that have historically been outsourced. The design team will take full responsibility for some projects, while also providing support and expertise to existing suppliers where appropriate.

In AMP7 we also plan to work with a larger number of contractors than previously, contracting directly with our Tier 2 suppliers as well as our network of larger suppliers – known as our One Supply Chain ('OSC').

Receiving fast-track status has allowed us to make an early start on our £2 billion capital programme for 2020-25 and in March we announced the contractors we will be working with for the first two lots of our AMP7 capital deliver framework Lot 1 (Capital Delivery Design and Build Framework) and Lot 2 (Capital Delivery Build Framework). Over the next twelve months we will start to work with our new construction partners to define the key projects which we will deliver for our customers.

<u>Our suppliers and partners</u>

A core principle of our supplier contracts is that they sign up to our Sustainability Supply Chain Charter and support our corporate social responsibility agenda, including commitments on safety, sustainability and human rights. Targets for individual suppliers are tailored to their circumstances and role, but as a minimum we expect them to adopt our values, comply with national laws, demonstrate alignment with the United Nations Global Compact initiative and take proactive measures to avoid environmental and social harm.

Investing to keep water flowing

Every year, we invest significant capital to improve water supplies to communities with a history of poor supply in times of high demand, such as through the summer months. In 2018/19 we carried out works that are now providing an improved service to farmers and other residents in the uplands around Breamfield in Derbyshire. These works included commissioning a borehole, installing new valves to reduce airlocks and connecting existing pipework to other parts of the network so that water can be quickly pumped into the area when necessary.

Making the right connections

With an increasing population and hotter, drier summers continuing to drive up demand for water, we're working with our peers and regulators to identify solutions that deliver for the whole of the UK – not just for our region. And we were pleased that our collaboration with United Utilities and Thames Water on a potential Severn-Thames interconnector took another important step forwards during the year. The proposed interconnector is expected to be a large bore pipe that will move water quickly from the wetter north and west of England and Wales to the drier south and south-east. In our PR19 business plan, we've committed to completing all planning and design activity to get the scheme 'shovel ready' by 2025. Ofwat has endorsed the concept of the interconnector and is expected to set up a regulatory alliance with the DWI and the EA. This will help manage the project through the legislative and licensing stages, and ensure it delivers the anticipated benefits.

Changing the market for the better

England and Wales have seen a transformation in water services over the last 30 years. Drinking water is cleaner, supply is more reliable, sewer flooding is much less frequent and rivers are in a better state of health than at any point since the 18th century. All this has been achieved while keeping bills affordable, with Severn Trent leading the way with the lowest bills of all.

At Severn Trent, we're committed to changing the water market for the better - by playing our part and doing even more for our customers, the environment and wider society. We work with companies and other organisations both within and outside our industry, combining our joint expertise and resources to make a difference for our people, customers and broader society.

Many of our corporate social responsibility commitments echo the United Nations' Social Development Goals, and during the year we explored how best to express our support for these, as part of the creation of our PR19 business plan. Looking ahead, we'll continue to refine our reporting and better align our internal policies with these goals.

Our latest business plan sets out our ambitious programme, with four key elements:

- To provide our customers with world class services – this sits at the heart of everything we do.
- To treat our customers as individuals, with their own unique needs and preferences. In our view, service should be personal.
- Do more for society as a whole. For example, by investing in educating future generations to preserve water and reduce the quantity of unwanted items into the sewer network.
- Do everything we can to build trust. Among many examples, this means ensuring that our decisions are guided by feedback from our 15,000 strong customer panel, and also establishing our new community dividend.

At the same time, we're also working hard to lead the way in how local services are delivered. Having already integrated Dee Valley Water into the business, we were pleased to officially launch our Welsh business Hafren Dyfrdwy in July 2018. This has aligned our operations with the England-Wales border, with all customers in Wales now being served by the new business – bringing clarity to the water market in the area.

Driving innovation in waste water

A new test-bed facility under construction at Redditch in the West Midlands is set to transform the way we evaluate and commercialise a wide range of new technologies. It is the result of our £6 million investment, plus further significant capital support from European and UK research organisations. The testbed will enable us to identify how the best ideas from academia can be applied in a practical way to benefit the water sector as a whole. These ideas include exploring how we can turn phosphorus, proteins, cellulose and bioplastics extracted from our waste streams into marketable products.

Creating an awesome place to work

Our people are fundamental to the success of our business. We're fortunate to have a team of dedicated, skilled individuals that serve our customers 24 hours a day, 365 days a year. We're a team that's not only passionate about what we do - but also brilliant at making things happen. We work very hard to keep it that way, by ensuring that Severn Trent is an awesome place to work.

We employ around 6,000 people, most of them at locations across the East and West Midlands and in North and mid-Wales. Each member of our team plays an important role in helping us provide excellent services to customers and build a lasting water legacy - and they deserve our wholehearted support at all times. We work hard to create a workplace that's welcoming and safe, where good work is well-rewarded and people are treated with respect.

We engage with our employees at every opportunity, helping them progress and enjoy satisfying, rewarding careers. We look after their health, safety and wellbeing and forge strong links with the communities that most of our people call home.

Employee engagement

We believe in open and honest communication between our management team and our employees at all times, and continually engage with them via formal and informal routes.

For the last two years, our employee survey (‘QUEST’) has achieved a participation rate of over 90%, which is five points ahead of the UK and Ireland benchmark. This feedback informs our engagement strategy and acts as a catalyst for continued improvement and positive change. Recent developments that have been shaped by the survey include greater visibility of pay structures, helping our employees understand how their pay is set and how they can progress their careers to increase their earning potential.

We’re are also pleased to maintain our strong engagement scores following our QUEST survey – placing us seven points above the average benchmark for UK and Ireland. In a year of intense activity this underlines the positive relationship that exists between the Group and our people. Our employees want to engage with us and shape our business, they know that their concerns are listened to and acted upon – and they’re proud to work with us to improve every aspect of our performance.

This approach is yielding positive results. We’ve been honoured with a Glassdoor Employee’s Choice Award, recognising the Best Places to Work in 2019, and Glassdoor reports that 74% of our people would recommend us to a friend. Our average retention rate over the year was 90% and QUEST results reported that 92% of our people say they’re proud to work for us and 93% feel we trust them to do their job.

Our Employee Forum brings together around 20 employee representatives in quarterly meetings and is co-chaired by a member of the Executive Team and a member of the trade unions. Our Chairman and Chief Executive rotate attendance and in 2019/20 Non-Executive Directors will be invited to attend. These sessions cover a range of topics. Discussions over the last year included health and safety, the content of our PR19 plan and our social purpose. These discussions have led to practical changes in how we work - such as a full refresh of our induction experience, the education of our workforce on modern slavery and installation of gender neutral changing rooms at all locations - including operational sites - to support our commitment to greater diversity.

Promoting diverse talent

We're dedicated to providing opportunities for all - and that starts by giving people the chance to enjoy a great career regardless of their postcode, education, gender, ethnicity or whether they join as apprentices, graduates or from other organisations.

With around 30% of the UK's social mobility coldspots in our region, we've refined our recruitment process to remove some of the barriers that traditionally prevent people from those areas applying to companies like Severn Trent. For example, we've removed some of the qualification requirements for applicants. We've also sent some of our younger employees into schools to demonstrate that people from all walks of life can succeed. These actions help to ensure that the make-up of our workforce reflects the diversity of our region – and brings employment and money into the areas that need it most. Details of some of the outcomes of our Social Mobility Programme can be seen in the case study below.

8.7% of our employees consider themselves to be Black, Asian and Minority Ethnic (‘BAME’). The number of BAME graduates rose by 4.6% during the year. We're equally proud of our track record in gender diversity and we’re ranked fourth among all FTSE100 companies and the first utility once again in the Hampton Alexander report. We've continued our focus on providing a more inclusive working environment for our LGBT+ employees, and during the year it was great to see Severn Trent represented prominently at both the Coventry and Birmingham Pride events. We also launched our LGBT+Ally Programme this year, an opportunity for all employees to challenge behaviour and actively support their LGBT+ colleagues.

Our employability initiative with Hereward College in Coventry - a college for young people with disabilities and additional needs - is another example of how we're making a real difference to people's lives. We offer one-year placements to Hereward students, with the aim of turning these short-term posts into real, long-term jobs - and we were delighted to offer full-time jobs to individuals in the most recent cohort.

The year also saw us continue to perform well on gender diversity, with the gender pay gap now standing at 2.8%, a small increase on last year's 2.4%.

<u>Providing careers not just jobs</u>

We strive to create careers with purpose and meaning. Our aim is to attract and retain talented, hard-working people who want to progress in their careers and provide great customer service. We support the development of all colleagues at all stages of their career and want every employee to feel competent and confident in their everyday work. During the year, we provided our teams with over 16,000 training days and delivered more than 25,000 e-learning hours.

As part of our preparations for AMP7, we're creating the Severn Trent Academy, which will be a step change in the way we provide training and development to our colleagues. This will ensure that our people have the right mindset, technical competence and leadership skills for now and in the future. By offering foundation apprenticeships and graduate entrants, through to higher and degree level apprenticeships and Masters degrees, we will ensure that our workforce is resilient for the future.

Our graduate and apprentice schemes are always in demand, as we strive to offer people a way into the Company regardless of their educational, social or cultural background. In 2018, we launched three new apprenticeship programmes within our HR, Legal and Vehicle Technician populations. We now have 11 active apprenticeship programmes, and expect this to increase to 13 in 2019, which includes Degree Level Quantity Surveying and Level 2 Tanker Driver Apprenticeships.

<u>Rewarding our employees</u>

As part of being an awesome place to work it is important that our people are properly rewarded. During the year, in response to feedback raised through the Employee Forum and QUEST, we communicated with our teams to make sure that they understand how their pay is set and how they can earn more by progressing through the business.

We also ensure we help all employees keep an eye on the future. We offer a market-leading defined contribution pension scheme and double contributions that our employees make (up to a maximum of 15% of salary), regardless of their level or seniority. As our people approach retirement we provide education and support to help them plan for the next stage of their lives.

It's an indication of our employees' pride in Severn Trent and their appreciation of the advantages of the pension arrangements that, during the year, 98% were members of the pension scheme and 57% paid contributions above the statutory minimum of 3% with 36% contributing the maximum.

Many of our colleagues are Severn Trent Plc shareholders as well, either directly through its share plans, such as Sharesave – which nearly 70% of our employees participate in - or indirectly through private pensions, FTSE index trackers or other investments.

<u>Promoting health, safety and wellbeing</u>

We believe passionately that no-one should be hurt or become unwell by what we do. With this in mind we provide extensive training on all aspects of health and safety. We are pleased that over the last two years we have been consistently upper quartile in Water UK benchmarking on Lost Time Incidents ('LTIs'). However, whilst we experienced no major safety incidents and no fatalities in the last twelve months, unfortunately we did see an increase in LTI's, mainly due to slips, trips and falls. This is the subject of regular discussion at the Employee Forum, Executive Committee and Board and in April 2019 we revamped our Goal Zero Strategy, with dedicated quarterly awareness campaigns.

We continued to campaign to remove the stigma associated with mental health and have trained a further 28 mental health first aiders. More than 70% of our line managers have now been trained on mental health awareness. We have 400 mental health first aiders in place to help those who need support. We continued our work to help people understand how menopause affects individuals and families and we've shared our approach with other organisations, including Ofwat and the DWI.

Supporting our communities

The vast majority of our employees are also customers and members of the communities in our region. Our people don't just serve our local communities, they are an integral part of them. The case study below demonstrates the passionate support our people have for their friends, family, neighbours and the local environment in volunteering to make a difference.

Turning up the heat on social mobility coldspots

Our region includes 30% of the nation's social mobility coldspots. We're working hard to redress the balance, and the evidence suggests that we're already making a difference.

- We were placed 20th in the Social Mobility Index, up 18 places on the previous year.
- Several members of our Executive Team grew up in coldspots, and over 50% studied at non-Russell Group universities.

Playing our part

Our volunteering programme continues to prove popular, with all employees being given two fully paid days to volunteer in local communities. In 2018/19, this amounted to a total over 2,000 days, much of it dedicated to our Community Champions programme where we worked alongside partners such as the Canal and River Trust to improve 34.4km of riverside environment. In AMP7, we're expanding the volunteering programme to work with Heart of England Forest, planting trees to create and protect a huge broadleaf forest across the Midlands. We look forward to providing further detail on these plans over the coming months.

Our teams again supported a wide range of charities during the year, raising over £390,000 for our long-term partner WaterAid as well as providing facilities and people to operate call centres for Comic Relief and Children in Need. We have recently agreed our new Partnership agreement with WaterAid for the period 1 April 2019 to 31 March 2024 and will be raising money to fund a climate change resilience project in Bangladesh.

Helping our customers to reduce plastic

We're delighted to support Refill across our region – a fantastic scheme that promotes the health benefits of tap water, while helping to protect the environment. There are now over 16,000 refill stations in the UK where you can fill up a water bottle for free, including shops, cafes, restaurants and museums – simply look for the blue sticker in the window. This year, we organised ten volunteered action days in some of our key towns and cities, encouraging local businesses to sign up to Refill. The reception was overwhelmingly positive. With the help of over 150 enthusiastic Severn Trent volunteers, and the support of local councils and environmental groups, we're helping to make it as easy as possible for our customers to refill when they're out and about. All our visitor experience sites have signed up as refill stations too. In our region there are now 20,000 refill stations. If each of these are used twice a day instead of a customer buying a new plastic bottle, then this would save 1.2 million plastic bottles in a year.

Raising awareness of modern slavery

Modern slavery is a growing global and local issue, impacting an estimated 40.3 million people worldwide. We're committed to eradicating forced labour and using our influence within our supply chain and wider stakeholders to help them do the same. To date, no instances of modern slavery have been raised.

This year, our focus has been on training and raising awareness. Working with our expert charity partners, Hope for Justice, we delivered six half-day workshops for our contract managers, procurement and construction project managers. We selected these employees because they have frequent and direct engagement with our highest risk area, our supply chain. Attendees gave us very positive feedback, with 98% reporting that they now felt confident in identifying modern slavery indicators and reporting it. Our senior management team have all received a dedicated briefing.

We were pleased that our Severn Trent Group 2018 Modern Slavery statement was ranked 16th among FTSE100 companies by the Business Human Rights Resource Centre - an improvement for the second consecutive year. This is a complex issue, and we're committed to continually reviewing and improving our approach as our understanding evolves. A key focus for next year is to roll out a bespoke e-learning module. Our full statement is available on the Severn Trent website.

Financial Review

We have delivered good financial performance in 2018/19, delivering good growth in PBIT, even after an additional £22 million of operating costs due to the hot, dry summer and our recovery after it. And we continue to outperform on Return on Regulated Equity (‘RoRE') which was 8.1% for the year end 2018/19. While this year’s return was partly held back by reaching our Waste ODI cap, our strong financial performance helped us to an AMP6 cumulative RoRE of 9.1%, putting us amongst the very best in the sector, with outperformance on all three levers.

Our funding position continues to be strong, with all our projected investment and cash flow needs covered by cash or committed facilities through to September 2021 and we continue to actively monitor and manage our interest rate exposure.

We are committed to paying the right amount of tax at the right time. We pay a range of taxes, including business rates, employers’ national insurance and environmental taxes such as Climate Change Levy and the Carbon Reduction Commitment as well as corporation tax which is included in our tax charge in the income statement. This year the Severn Trent Group published a Tax Report that sets out details of all of the taxes we incur and pay out on our website. Our corporation tax charge was 16.7%, reflecting a revaluation gain on financial instruments that is not subject to tax. Our cash tax payments were reduced by the benefit of tax allowances on our capital programme, contributions to our pension schemes and the timing of instalment payments to HMRC under the current rules.

A brief overview of our financial performance for the year is as follows:

- Group turnover from continuing operations was £1,673.1 million (2017/18: £1,606.9 million), an increase of 4.1% mainly due to RPI-linked tariff increases.

- Underlying PBIT grew by 5.5% to £567.3 million (2017/18: £537.7 million).

- We recorded net exceptional costs of £9.6 million (2017/18: £12.6 million). On 25 October 2018 the High Court issued a judgment in the Lloyds Bank case in relation to gender equality in Guaranteed Minimum Pension rights that has an impact on the Group’s defined benefit pension liabilities.

- Net finance costs were £188.8 million (2017/18: £215.9 million). Our effective interest rate of 3.8% was significantly lower than 2017/18 (4.4%). The reduction was a result of low interest rates on new and refinanced debt and lower RPI inflation on our index-linked debt which more than offset the impact of higher average net debt.

Turnover and underlying PBIT

Turnover for the Group was £1,673.1 million (2017/18: £1,606.9 million) and underlying PBIT was £567.3 million (2017/18: £537.7 million).

	2019	2018	Better/(worse)	
	£m	£m	£m	%
Turnover	**1,673.1**	1,606.9	66.2	4.1
Net labour costs	**(142.4)**	(162.4)	20.0	12.3
Net hired and contracted costs	**(182.2)**	(151.5)	(30.7)	(20.3)
Power	**(90.2)**	(79.2)	(11.0)	(13.9)
Bad debts	**(25.5)**	(25.7)	0.2	0.8
Other costs	**(185.8)**	(191.4)	5.6	2.9
	(626.1)	(610.2)	(15.9)	(2.6)
Infrastructure maintenance	**(141.4)**	(135.2)	(6.2)	(4.6)
Depreciation	**(338.3)**	(323.8)	(14.5)	(4.4)
Underlying PBIT	**567.3**	537.7	29.6	5.5

Turnover increased by 4.1%, the components of this were:

- RPI and the K factor increased revenue by £55.7 million;
- Customer ODI rewards taken in the current year were £9.6 million lower than the previous year;
- The reduction from the Wholesale Revenue Forecasting Incentive Mechanism was £13.9 million more favourable than the previous year;
- Additional revenue from higher consumption during the hot weather was around £5 million; and
- Other small factors increased revenue by £1.2 million.

Net labour costs were £20.0 million (12.3%) lower. Gross employee costs increased by 7.8%, due to the annual pay award and the continuation of our strategy to bring more work in-house (including the new design team). The growth in activity on capital projects increased the level of own labour capitals, up 22.3% on the previous year.

Net hired and contracted costs were up £30.7 million (20.3%), primarily in relation to costs incurred over the hot, dry summer and resulting operational recovery activities in the second half of the year.

Power costs were £11.0 million higher year on year. This was driven by forecasted higher unit prices from increased pass through costs and greater consumption from the higher volume of water produced to meet the demand over the summer months.

Our bad debt charge from household customers decreased by £0.2 million this year, and represented 2.0% of household revenues (2017/18: 2.2%). We continued to improve the pace of collection for new debt but also experienced slightly slower recoveries of older debt on which we are actively targeting our efforts this year.

Other costs decreased by £5.6 million, following increased profit on the disposal of tangible assets (mainly property) during the year.

Infrastructure maintenance expenditure of £141.1 million was £6.2 million higher in the year. The increase was driven by additional activity to reduce leakage and an acceleration of our trunk mains renewal programme.

Depreciation of £338.3 million was £14.5 million higher than the prior year, partly driven by the shift towards more investment in technology assets with shorter lives. There was also an increase in abandonment charges of £5.4 million as we upgraded some of our ageing assets.

Return on Regulatory Equity ('RoRE')

RoRE is a key performance indicator for our business and reflects the combined performance on totex, customer ODIs and financing against the base return allowed in the Final Determination.

RoRE for the year ended 31 March 2019 and for the four years ended on that date is set out in the following table:

	2018/19 %	AMP6 to Date %
Base return	5.6	5.6
Totex outperformance	-	1.2
ODI outperformance	(0.1)	1.0
Financing outperformance	2.6	1.3
Regulatory return for the year[1]	8.1	9.1

1 Calculated in accordance with Ofwat guidance set out in RAG 4.07

We have delivered RoRE of 8.1% in the year thanks to our significant outperformance on financing. ODIs were broadly neutral, impacted by hitting the Waste cap of 2% of RoRE. We reinvested totex savings for the benefit of our customers resulting in flat year-on-year performance. Our cumulative AMP 6 RoRE remains strong at 9.1% with four-year outperformance broadly based from sustained customer service delivery on ODIs, early delivery of totex efficiencies and strong performance on financing.

Exceptional items before tax

We recorded a net exceptional charge of £9.6 million (2017/18: charge of £12.6 million).

On 25 October 2018 the High Court issued a judgment in the Lloyds Bank case in relation to gender equality in Guaranteed Minimum Pension rights that has an impact on the Group's defined benefit pension liabilities. We have obtained independent advice from the Group's actuaries to determine the amount of the additional liability and have made provision for our best estimate in this year's financial statements.

In 2017/18 the charge of £12.6 million comprised exceptional restructuring costs of £20.9 million preparing our Bioresources business for AMP7 and an exceptional gain of £8.3 million from the net benefit of a Pension Increase Exchange arrangement.

Net finance costs

Our net finance costs for the year were £188.8 million, £27.1 million lower than the prior year. The reduction was driven by a lower effective interest rate, as a result of recent low cost debt issues and lower RPI inflation on our index-linked debt, which more than offset the impact of higher average net debt.

Our effective cash cost of interest (excluding the RPI uplift on index linked debt and pensions-related charges) was 3.1% (2017/18: 3.4%). Our effective interest rate of 3.8% was also down (2017/18: 4.4%) as a result of lower RPI inflation on our index-linked debt (down £30.8 million). Net pension finance costs were broadly in line with the previous year.

Capitalised interest of £31.6 million increased by £7.0 million year-on-year due to the higher level of capital activity in the year.

Our earnings before interest, tax depreciation and amortisation (EBITDA) interest cover was 5.2 times (2017/18: 4.3 times) and PBIT interest cover was 3.2 times (2017/18: 2.7 times). See note 43 for further details.

Gains/losses on financial instruments

We use financial derivatives solely to hedge risks associated with our normal business activities including:

- Exchange rate exposure on foreign currency borrowings;
- Interest rate exposures on floating rate borrowings; and
- Exposures to increases in electricity prices; and
- The phased switch in our regulatory model from RPI to CPIH.

Note 12 to the financial statements gives an analysis of the amounts charged to the income statement in relation to financial instruments.

As part of our power cost management strategy, we have fixed around 75.5% of our estimated wholesale energy usage for 2019/20.

Taxation

The total tax charge from continuing operations for the year was £71.2 million (2017/18: £59.6 million).

Note 13 in the financial statements sets out the tax charges and credits in the year, which are described in more detail below.

The current tax charge from continuing operations for the year was £34.2 million (2017/18: £32.5 million) and the deferred tax charge was £37.0 million (2017/18: £27.1 million).

In common with other utilities, we have a significant deferred tax provision that mainly relates to the benefits received in the past from tax allowances on capital expenditure before the depreciation on those assets was charged to our profits. This provision does not represent a liability for tax payable but is released to the income statement as the depreciation catches up with the tax allowances received. The provision is calculated at the rate of tax applicable when the provision is expected to reverse.

Pensions

We have three defined benefit pensions arrangements, two from Severn Trent and one from Dee Valley Water. The Severn Trent schemes are closed to future accrual.

The most recent formal actuarial valuations for the Severn Trent schemes (‘the Schemes’) were completed as at 31 March 2016. The agreement reached with the Trustee for the STPS, which is by far the largest of the schemes, included:

- Inflation-linked payments of £15 million per annum through an asset-backed funding arrangement, potentially continuing to 31 March 2031, although these contributions will cease earlier should a subsequent valuation of the STPS show that these contributions are no longer needed;

- Payments under another asset-backed funding arrangement which provides £8.2 million per annum to 31 March 2032; and

- A deficit reduction payment of £10 million for each of the three financial years ended 31 March 2019;

- In addition to these payments, the Company will directly pay the annual PPF levy incurred by the STPS (£1.4 million in 2018/19).

The next formal actuarial valuations of the Schemes are currently underway.

The Schemes have entered into additional hedging arrangements to reduce the impact of fluctuations in interest rates and inflation on the Schemes’ liabilities without adversely impacting the expected return from the Schemes’ assets.

Hafren Dyfrdwy participates in the Dee Valley Water Limited Section of the Water Companies Pension Scheme (“the Section”). The Section funds are administered by trustees and are held separately from the assets of the Group. The Section is closed to new entrants. The last formal actuarial valuation of the Section was completed as at 31 March 2017 and as a result deficit reduction contributions to the Section ceased.

On an IAS 19 basis, the net position (before deferred tax) of all of the Group's defined benefit pension schemes was a deficit of £444.3 million (2018: £511.1 million). To calculate the pension deficit for accounting purposes, we are required to use corporate bond yields as the basis for the discount rate of our long-term liabilities, irrespective of the nature of the scheme’s assets or their expected returns.

The movements in the net deficit during the year were:

	Fair value of plan assets £m	Defined benefit obligations £m	Net deficit £m
At start of the year	2,339.8	(2,850.9)	(511.1)
Amounts charged to income statement	58.7	(84.4)	(25.7)
Actuarial gains/(losses) taken to reserves	95.9	(37.9)	58.0
Cash received/paid by the schemes	(75.5)	110.0	34.5
At end of the year	2,418.9	(2,863.2)	(444.3)

On an IAS 19 basis, the funding level was 84.0% (31 March 2018: 82.0%).

Treasury management

Our principal treasury management objectives are:

- To access a broad range of sources of finance to obtain both the quantum and lowest cost compatible with the need for continued availability
- To manage our exposure to movements in interest rates to provide an appropriate degree of certainty as to our cost of funds
- To minimise our exposure to counterparty credit risk
- To provide an appropriate degree of certainty as to our foreign exchange exposure
- To maintain an investment grade credit rating
- To maintain a flexible and sustainable balance sheet structure

We invest cash in deposits with highly rated banks and liquidity funds. We regularly review the list of counterparties and report to the Treasury Committee.

Our policy for the management of interest rates is that at least 40% of our borrowings in AMP6 should be at fixed interest rates, or hedged through the use of interest rate swaps or forward rate agreements. At 31 March 2019, interest rates for 53% (2018: 48%) of our net debt of £5,700.2 million were fixed.

Our long term credit ratings are:

Agency	Rating	Outlook
Moody’s	A3	Negative
Standard and Poor’s	BBB+	Stable

Group cash flow

	2019 **£m**	2018 £m
Cash generated from operations	**808.9**	788.0
Net capital expenditure	**(752.4)**	(582.8)
Purchase of subsidiaries	**–**	(0.2)
Net interest paid	**(161.9)**	(177.4)
Tax paid	**(20.9)**	(14.9)
Swap termination payment	**–**	(40.0)
Free cash flow	**(126.3)**	(27.3)
Dividends	**(225.1)**	(204.0)
Change in net debt from cash flows	**(351.4)**	(231.3)
Non cash movements	**(33.3)**	(57.0)
Change in net debt	**(384.7)**	(288.3)
Net debt 1 April	**(5,315.5)**	(5,027.2)
Net debt at 31 March	**(5,700.2)**	(5,315.5)

	2019 **£m**	2018 £m
Cash and cash equivalents	**12.9**	12.1
Bank overdraft	**(0.8)**	(8.4)
Net cash and cash equivalents	**12.1**	3.7
Loans due from/(to) parent company	**80.6**	(9.3)
Bank loans	**(1,086.0)**	(1,182.1)
Other loans	**(4,732.3)**	(4,138.2)
Finance leases	**(111.7)**	(113.9)
Cross currency swaps	**37.1**	24.5
Loans due from joint ventures	**100.0**	99.8
Net debt	**(5,700.2)**	(5,315.5)

We generated £808.9 million cash from operations (2017/18: £788.0 million). Operating cash flows were higher mainly due to higher PBIT, depreciation and amortisation and our increase in working capital was lower than the previous year.

Our biggest year of capital investment in a decade led to net capital expenditure of £752.4 million (2017/18: £582.8 million).

Our net interest payments were lower at £161.9 million (2017/18: £177.4 million). Our tax payments were £20.9 million, £6.0 million higher than the previous year.

These cash flows, resulted in an increase of £351.4 million in net debt (2017/18: £231.3 million).

At 31 March 2019 we held £12.1 million in cash and cash equivalents (2018: £3.7 million). Average debt maturity was around 14 years (2017/18: 14 years). Including committed facilities, our cash flow requirements are funded until September 2021.

Net debt at 31 March 2019 was £5,700.2 million (2018: £5,315.5 million) and balance sheet gearing (net debt/net debt plus equity) was 69.4% (2018: 69.5%). Net debt, expressed as a percentage of estimated Regulatory Capital Value at 31 March 2019 was 62.2% (2018: 60.8%).

The estimated fair value of debt at 31 March 2019 was £1,212.1 million higher than book value (2018: £1,177.8 million higher). The increase in the difference to book value is largely due to lower prevailing market interest rates.

Accounting policies

Our consolidated financial statements are prepared in accordance with International Financial Reporting Standards that have been endorsed by the European Union. The Company financial statements are prepared in accordance with FRS 101.

Risk management

Our approach to risk

Risk is all about uncertainty. We recognise that uncertainty can manifest itself as both negative and positive impacts. Our goal is to minimise the threats and maximise the opportunities for the benefit of our customers, employees, supply partners and the environment.

The Board has overall accountability for ensuring that risk is effectively managed across the Severn Trent Water Group. The Board's mandate includes defining risk appetite and monitoring risk exposure to ensure significant risks are aligned with the overall strategy of the Severn Trent Water Group.

On behalf of the Board, the Severn Trent Plc Audit Committee assesses the effectiveness of the Group's Enterprise Risk Management ('ERM') process and internal controls to identify, assess, mitigate and manage risk. Additional information is set out in the Severn Trent Plc Audit Committee's report in the Severn Trent Plc Annual Report and Accounts 2018/19 on page 85.

The Executive Committee reviews strategic objectives and assesses the level of risk taken in achieving these objectives. This 'top down' risk process helps to ensure the 'bottom up' ERM process, described below, is aligned to current strategy and objectives.

The management of risk is embedded in our everyday business activities. Risks are managed within the overall Governance Framework which includes clear accountabilities, delegated authority limits and reward policies. These are designed to provide employees with a holistic view of effective risk management.

Our approach to risk reflects our status as a regulated utility providing essential services and operating as part of the Critical National Infrastructure for the UK. The nature of this business is such that there are some significant inherent risks. We have a strong control framework in place to enable us to understand and manage these risks in accordance with our risk tolerance and appetite.

The principal risks facing the Severn Trent Water Group are illustrated on pages 50 to 63.

Our Enterprise Risk Management process

We use an established ERM process to assess and manage our significant risks. The process is controlled by the central ERM team and underpinned by standardised tools and methodology to ensure consistency.

ERM Champions and Co-ordinators operate throughout the business, with support and challenge from the ERM team, continually identify and assess risks in their business units on a quarterly basis. Criteria are used to consider the likelihood of occurrence and potential financial and reputational impacts. The potential causes and subsequent impact of the risks are documented to enable mitigating controls to be assessed. This assessment allows us to put in place effective strategies to remediate defective controls or implement additional controls.

Business units' information is combined to form a consolidated view of risk and allows the risks to be prioritised. Our significant risks form our risk profile which is reported to the Executive Committee for review and challenge. This is reported to the Severn Trent Plc Audit Committee and Board on a six monthly basis. The report provides an assessment of the effectiveness of controls over each of those risks and an action plan to improve controls where this has been deemed necessary.

To further enhance our ERM information, we report ‘risk flightpaths’. These demonstrate the level of risk the Group faces and the timeline for the key risk mitigation steps to manage the risk to the target position. The flightpaths help to facilitate a more thorough review of the target risk positions, consider risk appetite and assess whether actions are on target with the correct prioritisation in place.

Risk appetite

The Board keeps the relationship between our strategic ambitions and the management of risk under continual review. The ERM process establishes target risk positions for each of our significant risks. The Board formally discusses the progress towards this position and the mitigating actions being undertaken every six months.

Financial risks

Like all businesses, we plan future funding in line with business need. This is part of our normal business planning process.

The Board receives regular updates relating to funding, solvency and liquidity matters through the Treasury Committee so we can respond quickly to any changes in our ability to secure financing (see Principal Risk 10). The pension fund Trustees and Company regularly monitor our pension deficit, with advice from investment managers and actuarial advisers. An annual pension fund review paper is tabled for the Board updating them on fund performance and proposed initiatives to manage down pension liabilities and further balance pension risks (see Principal Risk 9).

The ERM process and relevant risk assessments are factored into the ‘stress testing’ to assess the Company’s prospects as part of our Long-Term Viability Statement.

Sustainability risks

Sustainability risks are treated in the same way as all our other Company risks, captured at a local level by responsible teams and managed centrally through our established ERM process. By the nature of what we do, several of our principal risks have a Sustainability focus, and we monitor our social and environmental impacts with the same rigour as our broader performance.

Emerging risks

We defined emerging risks as upcoming events which present uncertainty but are difficult to assess at the current stage.

Emerging risks have the potential to increase in significance and affect the performance of the Severn Trent Water Group and, as such, are continually monitored through our existing ERM processes comprising: ERM coordinators, ERM champions and risk owners and cross functional workshops that operate at all levels of the organisation. We use tools such as horizon scanning and PESTLE analysis. The outputs of this process are reported to the Audit Committee and Board through our emerging risk horizon map.

Our ERM process ensures emerging risks are identified and aids the Severn Trent Plc Audit Committee and Board’s assessment of whether the Group is adequately prepared for the potential opportunities and threats they present. The process enables new and changing risks to be identified at an early stage – so we can analyse them thoroughly and assess potential exposure.

We closely monitor emerging risks and with time they may become fully fledged ERM risks or be incorporated into existing ERM risks (as potential causes) as we learn more. Emerging risks may also be superseded by other risks or cease to be relevant as the internal and external environment in which we operate evolves. A non-exhaustive list of some current emerging risks of relevance to the Severn Trent Water Group are set out below.

Title	Detail	Area / Factor	Time Horizon
Water industry structure	Increasing social and political scrutiny on the structure of the water industry.	Political & Social	Medium
Micro plastics	Understanding and addressing the impact of micro plastics – including on natural resources and customers.	Health, Safety & Environmental	Medium
Macroeconomics	Increased macroeconomic uncertainty post Brexit.	Economic	Short
Compliance	The challenge of compliance in a more complex, disaggregated regulatory framework for AMP7 and beyond.	Legal & Regulatory	Short - Medium
HS2	Direct impact on operational sites along the proposed route and the indirect impact on labour availability in the area.	Operational	Medium - Long
Skills gap and labour shortage	Shortage of STEM expertise within the labour market and future talent pipelines. We are addressing this through our new Severn Trent Academy. Read more on page 36.	Operational	Medium - Long
Automation, robotics & AI	Opportunity for increased efficiency through use of automation, robotics and artificial intelligence.	Technological	Short - Medium
Rising energy costs	Opportunity to increase renewable energy generation and efficiency as technology develops.	Technological	Medium - Long

Principal risks

The directors have carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity. These have been categorised across:

- Customer perception;
- Legal, regulatory and political environment;
- Operations, assets and people; and
- Financial risks.

For each risk we state what it means for us and what we are doing to manage it.

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
1	We may be unable to improve and maintain our levels of customer service sufficiently to deliver what our customers tell us they want.	ODIs 24-27	We are a regulated utility providing essential services to our customers. We recognise that our customers increasingly expect more from us and demand an improved and more consistent experience. As other industries improve their levels of service, the bar continues to be raised. Failure to deliver the service that customers expect will lead to customer dissatisfaction. This may result in financial penalties under Ofwat's Service Incentive Mechanism (SIM) in AMP6, and C-MeX in AMP7, and	Understanding what our customers want is key to managing this risk. Our PR19 Severn Trent plan was shaped by consulting with 32,000 customers, evaluating 24,000 complaints and analysing 1.9 million contacts on social media. As one of only three companies to be fast-tracked we see this as a firm endorsement of our customer focused approach. We recognise that our performance on SIM has not been where we would have wanted. Work is now underway to prepare for Ofwat's new AMP7 customer measure of performance (C-MeX), which will be partly based on customer contact, as with SIM, and partly on customer perception which is a much wider measure. We are pleased to again be in the top quartile of water companies in England in the UK Customer Service Index,	⇔ No change

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
			associated ODI outturn.	especially as this is an element of the forthcoming C-Mex measure. The Retail Upper Quartile (UQ) programme continues to deliver a number of initiatives focussed on customer experience. Future initiatives include ‘Customer First’ interventions and Robotics Process Automation. Customers continue to tell us they are delighted when we are able to complete issues for them at Point of Contact and we will continue the work improve our Point of Contact resolution further (with a large focus in Metering) to improve the overall experience. We set up Tap Chat during the year. This new online community panel gives us feedback about how we’re doing and, more importantly, how we can do even better. With 15,000 active participants, representing all walks of life and areas across our region, Tap Chat played an important role in refining our PR19 business plan and provides ongoing engagement with our customers. More than 1.9 million customers are now signed up to our online offerings	

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
				and, during the last year, our web self-serve platform handled more than 1.6 million transactions. And the hard work of our customer communication team was recognised by a Silver Award at the European Contact Centre and Customer Service Awards.	
2	We may be unable to effectively anticipate and/or influence future developments in the UK water industry resulting in our business plans becoming unsustainable.	n/a	The regulated business operates in a highly regulated environment. Whilst we are broadly content with the direction of changes proposed for our industry, there remains a risk that additional future changes could have a significant impact on Severn Trent. The renationalisation of the water industry continues to be a central policy of the Opposition and therefore remains a possibility in the event of a change of Government. In the event of Renationalisation, there is a possibility that the Group's regulated businesses (Severn	With the successful submission of our PR19 Severn Trent Plan we now have more certainty about the next five year AMP period running from 2020-25. Severn Trent has always contributed to the debate about our industry's future We will continue to be an active participant in these conversations, so we can help shape thinking about how to best serve our customers in the future. We specifically continue to engage with the Government, MPs, the Welsh Government, regulators and other stakeholders about the future shape and direction of the water sector. The renationalisation of the water industry remains a possibility in the event of a change of Government, and any associated changes in Government policy may	Decrease

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
			Trent Water and Hafren Dyfrdwy) are acquired at below the value currently implied in Severn Trent Plc's share price.	fundamentally impact our ability to deliver the Group's strategic objectives, impacting shareholder value. Our aim is to ensure the water sector in England and Wales continues to deliver a world class service for customers, is able to invest for the future and maximises the benefits to wider society all stakeholders through the social and environmental benefits the current model allows us to deliver. We seek to minimise potential risk and maximise opportunities through regular communication and robust scenario planning as Government policy evolves. Creating our Welsh business Hafren Dyfrdwy has aligned our interests around the England-Wales border along national boundaries, with all customers in Wales now being served by the new business - bringing clarity to the water market in the region.	
3	The regulatory landscape is complex and subject to on-going change. There is a risk that processes may fail or that our processes	ODIs 1-4 ODIs 19-23 30-43	Our policies and processes must reflect the current legal and regulatory environment and all relevant employees must be kept aware of new requirements. The	We have established governance and control frameworks that we openly publish to provide transparency. Our engagement with customers and stakeholders, policies, internal controls, guidance and training ensure our	No change

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
	may not effectively keep pace with changes in legislation leading to the risk of non-compliance.		group as a whole may face censure for non-compliance in an individual group company or a specific region in which we operate.	ongoing compliance with all applicable laws and regulations including Competition Law for the operation of separate Wholesale and Retail business and between our group businesses. We regularly review our control frameworks to take account of changes to legislation, regulation and our business. This year we have updated to include the new boundaries of Seven Trent and Hafren Dyfrdwy. Ensuring compliance with the General Data Protection Guidelines (GDPR) has also been a key area of focus since they came into effect on 25 May 2018. Changes to the legal and regulatory environment are captured as 'emerging risks' through our ERM process with the necessary owners and actions identified to ensure compliance when the changes come into effect. Our external legal advisers also provide us with horizon scanning reviews of upcoming legislation that may affect the Group. This is considered by our internal legal team, and any applicable upcoming changes are reported to the Executive Committee and	

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
				communicated across the business as required.	
4	We may experience loss of data or interruptions to our key business systems as a result of cyber threats.	ODIs 1-4 ODIs 5-18 ODIs 19-23 ODIs 24-17	The risks arising from loss of one or more of our major systems or corruption of data held in those systems could have far reaching effects on our business. We have recognised the increasing threats posed by the possibility of cyber-attacks on our systems and data. Whilst this threat can never be eliminated and will continue to evolve, we are focussed on the need to maintain effective mitigation.	We continue to commit significant resources and financial investment to maintain the integrity and security of our assets and data. We follow guidance from the National Cyber Security Centre and have defence through multiple layers of software and processes including web gateways, filtering, firewalls, intrusion and advanced threat detection. We have strengthened our security and network operations capability this year and have improved the controls around third party access to our systems and data. We have reviewed our cyber risk methodology and are using this to prioritise future investment to ensure that we protect ourselves in-line with GDPR, Network and Information Systems Regulation and Payment Card Industry Data Security Standard (PCI DSS) best practices. We have also participated in a number of internal cyber security incident exercises to test our response capability to cyber-attacks. Despite the enhancement of our defence during the year,	Increase

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
				considering the current cyber threat levels we have recognised an overall increase in the net risk exposure.	
5	We may fail to meet our regulatory targets including targets from Ofwat in relation to operational performance of our assets resulting in regulatory penalties.	ODIs 1-45	If we are unable to meet operational performance targets, we may be subjected to significant regulatory penalties either within the current price review period, or applied to the next price review. Regulatory targets apply to all of our water treatment, distribution, sewerage and sewage treatment assets. Measures are in place in relation to water quality, continuous supplies, sewer flooding, sewer collapses and pollution events.	Our strong wastewater performance has continued and we have made good progress in water quality, but further work is required to improve over performance on supply interruptions and leakage. We are starting to see improvement in supply interruptions through our 'Prevent, Restore, Repair' strategy which focusses on preventing asset failure where possible, and restoring supply at speed it this happens. On leakage, we have introduced innovative ways of finding leaks faster and fixing them more efficiently, and we are pleased that we have started to see some encouraging results. We use leading measures on our comm cells and performance meetings to track delivery against customer ODIs and performance commitments so that we can intervene in a timely fashion if performance is drifting.	No change
6	Failure of certain key assets or processes may	ODIs 1-4	Some of our assets are critical to the provision of water to	Our business plan for 2015-2020 includes considerable investment in our assets to improve the resilience of our	No change

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
	result in inability to provide a continuous supply of clean water and safely take waste water away within our area.	ODIs 5-18 ODIs 19-23	large populations for which we require alternative means of supply. Examples of risk include the failure of one of our reservoirs or water treatment works. These assets are regularly inspected and maintained and our assessment of the overall condition of these assets is good. Other examples are our IT, telephony systems and remote monitoring systems which are also key to our operations.	networks, reduce interruptions and improve the service that our customers receive. We recognise there are areas where our performance is not as consistent as we would like and are committed to improving these. We are continuing our Cleanest Water Plan which drives the delivery of our inspection, cleaning and repair of storage tanks, increasing our capital maintenance interventions, optimising our operation and maintenance tasks and formalising our processes, standards and operating procedures involved in delivering clean water. We learned from the experience of the “freeze/thaw” in March 2018 and this helped us prepare and respond well to a particularly challenging summer where very high water demands were experienced for a sustained period due to prolonged hot weather. Several rural areas experienced intermittent supply interruptions and we are investing across the network to avoid such issues in the future. Our response to failures in supply such as burst mains has been greatly	

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
				enhanced and we are now able to reach the site and initiate recovery plans much quicker than in previous years. We have a programme of work to improve the reliability of our major Water Treatment Works and to return them to their design output capacity where they have not been in a condition to meet it. In Nottinghamshire, we made great progress on a scheme to improve ou1r service in Newark, where a £60m programme will benefit 400 local homes and businesses. We're installing 4km of high volume sewers to reduce flooding risk, as well as 10km of new water network to improve water supply. In addition to investing in resilience improvements to our network we also have assurance plans in place to monitor, inspect and maintain our most critical assets and to ensure clean water is always available to our customers and we will always be able to safely take their waste water away.	
7	Due to the nature of our operations we	ODIs 30-41	The nature of our assets, operations and business are	We have a well-established Health, Safety & Wellbeing framework to ensure all of	⇔ No change

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
	could endanger the health and safety of our people, contractors and members of the public as well as negatively impact our local and wider environment.	ODIs 42&43	such that threats to the safety of our employees, contractors, customers and the wider public exist. Operational failures or negligence could result in damage to the environment. We are responsible for a large estate of assets and have to secure these from unauthorised access to ensure our operations are not impacted nor the safety of the public compromised.	operations and processes are conducted in compliance with Health and Safety legislation and in the interests of the safety of our people and contractors. Our Goal Zero initiative clearly establishes our target that no one should be injured or made unwell as a result of what we do. We are disappointed that in the second half of the year we have seen an increase in accidents and lost time incidents. As a result we have refreshed our strategy and focussed in on four key building blocks to deliver enhanced resilience, and targeted interventions in the four main hazard areas causing us harm. There are a number of ODI commitments we have made to protect our local environment, including river water quality, pollution incidents, biodiversity improvements and environmental compliance. In AMP6 we will be delivering our largest ever environment programme, a programme which is supported by our customers who wanted to see us do more to improve river water quality. As part of the Water Framework Directive, we're on track to improve at least	

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
				1,600 km of our rivers in AMP6 - and a further 2,100 km in AMP7 This year we expect to achieve a 3* Environmental Performance Assessment status from the Environment Agency. We recognise the impact our operations have on the wider environment and we want to reduce our carbon footprint by seeking lower carbon ways of operating our business, driving energy efficiency and generating renewable energy. We've made excellent progress against our target of generating 50% of our own energy requirements, with the completion of a Thermal Hydrolysis Plant at our Minworth wastewater site during the year. During the year we were re-certified by the Carbon Trust - the tenth consecutive year we've achieved its standard. This verifies that we have sound carbon management processes in place and are reducing absolute carbon emissions year-on-year. More details can be found in the Severn Trent Plc Annual Report and Accounts Corporate Responsibility report on pages 94 to 96.	

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
8	We are unable to deal with the impact of extreme and unpredictable weather events on our assets and infrastructure and/or are unable to successfully plan for future water resource supply and demand due to climate change.	ODIs 1-4 ODIs 5-18 ODIs 19-23 ODIs 42-43	Climate change (hotter and drier summers, wetter winters and increased storminess) could result in an inability to meet customer demand, lower river levels, decreased raw water quality, flooding of our water or waste works, sewer capacity being exceeded and increased land movement. Climate change could also be a contributing factor for principal risks 1,5,6 and 7 detailed above. There are also some potential opportunities that climate change presents for us, including aquifer recharge and increased biological treatment. It is important that we understand these opportunities to maximise the benefits.	*Extreme Weather* We have applied the learnings from the Freeze Thaw event in March 2018 and the prolonged hot, dry summer. See Principal Risk 6 above for further detail of our resilience improvements. Our analysis for the National Flood Resilience Review (NFRR), that was instigated by Defra / the Cabinet Office after the flooding of winter 2015/16, identified those non-infrastructure (overground) sites that could be at risk from river or surface water flooding using a new higher standard called the 'Extreme Flood Outline'. This has informed our contingency plans and future investment plans. *Climate Change* Our climate change adaption report sets out our strategy for coping with future changes to our climate. Our draft water resources management plan for the next 25yrs was consulted on through 2018. The plan includes a detailed assessment of climate change impact for our region and our demand management and proposed new sources are designed to	⇔ No change

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
				offset any supply risk resulting from climate change. The final plan will be published in 2019. We're also taking a national perspective by working with other water companies to develop an interconnector that can move water quickly from the wetter north to the drier south, enhancing water resilience across the UK. Our own impact and contribution to climate change cannot be ignored and, as outlined in principal risk 7 above, there are a number of ways in which we are addressing our impact on the environment.	
9	Lower interest rates, higher inflation or underperforming equity markets may require us to provide more funding for our pension schemes.		We already provide significant funding but could be called upon to provide more money to reduce pension deficits in our defined benefits schemes.	Our IAS19 deficit has reduced from £520m as at 31st March 2018 by £67m to £453m as at 31st March 2019. The main pension scheme benefits from significant levels of interest rate, inflation and equity hedging to reduce materially the impact on the scheme deficit from these risks. We are currently in discussion with the scheme Trustees to agree the triennial actuarial valuation as at 31st March 2019 and resulting deficit repair payments. These negotiations may in due course also involve the	Increase

Ref	What is the risk?	ODIs	What does it mean for us?	What are we doing to manage the risk?	Movement in Net Risk Exposure
				Pension Regulator. Due to changes in market conditions between March 31 2016 (the date of the last triennial valuation) and March 31 2019 these negotiations may result in increased annual deficit repair payments for the next three years.	
10	We are unable to fund the business sufficiently in order to meet our liabilities as they fall due.		We must ensure sufficient liquidity is available to meet our near term financial commitments. We have a significant funding requirement in AMP6, to fund our investment programme and refinance maturing debt. This is a well-controlled risk, but it is important that we maintain these high standards to mitigate this risk.	We have a marked improvement against this risk exposure as our liquidity position has increased materially. Due to current political and economic landscape we have increased our available liquidity to a total of 29 months. We have been active in the EMTN (Euro Medium Term Note) private placement market, increased our committed bank facilities and have accessed further the US Private Placement market and GBP public bond market this year. This demonstrates we are able to replace the European Investment Bank as a source of financing caused by the UK's planned departure from the European Union. See our Viability Statement on page 64.	Decrease

Brexit Statement

At the time of writing, the terms of the UK's departure from the EU ('Brexit') remain uncertain. Brexit does not give rise to a new principal risk for the Group. However, it does have the potential to impact risks in other areas of our operations, such as supply chain, interest rates, availability of funding, regulatory changes and uncertainty for the domestic economy.

Our preparations for a no-deal Brexit are well advanced and include a Brexit Steering Committee to oversee the contingency and scenario planning necessary to operate effectively if the UK leaves the EU without transition arrangements. The Committee covers; Incident Management, People, Procurement, Security and Resilience, Logistics, Communications, Finance and Capital Delivery. We have been actively engaged with a Water UK coordinated group called the Operations Strategy Group (OSG) at an executive level, focussing on industry preparedness and industry wide testing of response plans for a 'No Deal' scenario. We're also working with a number of Local Resilience Forums to test our approach and plans. We are confident that we are well prepared for the UK's departure from the EU and specifically the risks associated with 'No Deal'. The most significant risk identified is associated with the availability of chemicals imported into the UK. We identified this at an early stage and have ensured we have a robust process for maintaining stock levels. This has also been a key focus for the OSG which accordingly has worked with suppliers to increase stock levels chemicals across the UK. The Government, Defra and other industry regulators have been kept informed of preparations throughout. We have also increased stock for critical spare parts where a potential risk has been highlighted, by working with our supply chain.

Progress in the Brexit negotiations will continue to be monitored and the risks and uncertainties will be managed through our existing ERM process.

Viability statement

Assessment of current position and long-term prospects

The directors' assessment of the Group's current financial position is set out in the Financial review on pages 39 to 46.

The Group's principal operating subsidiary is Severn Trent Water, which is a regulated long-term business characterised by multi-year investment programmes and stable revenues. The water industry in England and Wales is currently subject to economic regulation rather than market competition and Ofwat, the economic regulator, has a statutory obligation to secure that water companies can (in particular through securing reasonable returns on their capital) finance the proper carrying out of their statutory functions. Ofwat meets this obligation by setting price controls for five year Asset Management Periods (AMPs). This mechanism reduces the potential for variability in revenues from the regulated business. The current AMP runs until March 2020 and Ofwat has published its draft determination of price controls for Severn Trent Water for the AMP period 2020 – 2025 (AMP7) and Severn Trent Water has made significant progress in developing its plans to deliver the operational and financial performance set out in the draft determination. Ofwat will publish its final determination for AMP7 in December 2019. We do not this expect to be materially different from the draft determination.

When considering the Group's prospects beyond 2025, it is necessary to make assumptions about the price review process for the period 2025 – 2030 (PR24), which will take place in 2024, and has not yet been specified. In making this assessment we have taken account of:

- Ofwat's statutory duty to secure that companies can finance the proper carrying out of their functions;

- Severn Trent Water's financial structure, which is close to the Ofwat notional capital structure and our plan to retain this; and
- Severn Trent Water's progress in developing plans for AMP7, the successful execution of which would deliver benefits to all stakeholders and financial incentives that would help to improve our financial resilience in the period beyond 2025.

The Group has significant investment programmes that are largely funded through access to debt markets. The Group's strategic funding objectives reflect the long term nature of the Severn Trent Water business and the Group seeks to obtain a balance of secure long term funding at the best possible economic cost. The Group's Treasury Policy requires that it maintains sufficient liquidity to cover cash flow requirements for a rolling period of at least 18 months in order to mitigate the risk of restricted access to capital markets. The Group's debt maturity profile is actively managed by the Group Treasury department to spread the timing of refinancing requirements and to enable such requirements to be met under most market conditions. The weighted average maturity of debt at the balance sheet date was 14 years.

The Group has an established process to assess its prospects. The Board undertakes a detailed assessment of the Group's strategy on an annual basis and the output from this assessment sets the framework for the Group's medium term plan, which is updated annually.

The Group's medium term plan assesses its prospects and considers the potential impacts of the principal risks and uncertainties. Stress tests are performed to assess the potential impact of combinations of those risks and uncertainties. The plan also considers mitigating actions that the Group might take to reduce the impact of such risks and uncertainties, and the likely effectiveness of those mitigating actions.

Period of assessment

The directors considered a number of factors in determining the period to be covered by the assessment. The long-term nature of the Group's principal business, together with relatively stable revenues and a model of economic regulation that places a duty on the regulator to secure that water companies can finance the proper carrying out of their functions, support a longer period of assessment.

However, the changing nature of regulation of the water industry increases the uncertainty that is inherent in the Group's financial projections. The Group has an established planning and forecasting process and the directors consider that the assessment of the Group's prospects is more reliable if it is based on an established process. The Group's latest medium term plan extends in detail to the end of the next AMP period in 2025 with less detailed projections looking beyond this.

A longer period of assessment introduces greater uncertainty because the variability of potential outcomes increases as the period considered extends.

Bearing in mind the long term nature of the Group's business; the enduring demand for its services; the nature of the Group's established planning process and the changing nature of the regulation of the water industry in England and Wales, the directors have determined that seven years is an appropriate period over which to assess the Group's prospects and make its viability statement this year.

Assessment of viability

In assessing its future prospects, the Group has considered the potential effect of risks and uncertainties that could have a significant financial impact under severe but plausible scenarios. The risks and uncertainties considered were identified in the Group's ERM process, which is described on pages 47 to 48, and from the key assumptions in the financial model. The scenarios tested are described below.

Scenario tested	Related principal risk	Mitigating actions
1. *An increase in the funding deficit of the Group's defined benefit pension schemes* The planned funding for the Group's defined benefit pension arrangements is based on current assumptions for future inflation, asset returns and members' longevity. Outcomes different from these might result in additional cash contributions being required during the period under consideration. Contributions are reviewed and agreed with the Scheme trustee on a triennial basis with the next valuation of the main scheme based on the funding position at 31 March 2019.	Risk 9: Increased funding for pension schemes	Discuss impact on debt covenants with lenders and seek a temporary waiver if necessary. Consider use of hybrid debt instruments to protect credit ratings. Consider a temporary reduction in dividends. Identify and implement sustainable cost savings and efficiencies. Reduce working capital to support cash flow.
2. *STW experiences a severe climate event, operational failure or other exceptional event with a very significant financial impact* The Group's Enterprise Risk Management process has identified a number of risks including extreme weather events, failure of key assets and cyber-attacks that might have a significant impact on the Group's operational and financial performance.	Risk 4: Cyber security Risk 6: Failure of key assets Risk 7: Health and safety and environmental impact Risk 8: Impact of extreme weather/climate change	Reduce discretionary expenditure to cover any extra costs resulting from the event Consider use of hybrid debt instruments to protect credit ratings. Consider a temporary reduction in dividends.
3. *A reduction in inflation or increase in interest rates for part of the period under consideration* Severn Trent Water's revenues are linked to inflation. Low or	N/A – key assumption in financial model	Reduce discretionary expenditure in the short term. Reduce working capital to support cash flow.

negative inflation tends to adversely impact profits and cash flows if increases in costs exceed increases in revenue. Higher costs of debt would adversely impact the Group's profits, cash flows and credit metrics.		Consider a temporary reduction in dividends
4. *STW underperforms against its performance commitments* Severn Trent Water operates under a regulatory model which encourages companies to deliver what customers want using performance related rewards and penalties. Failure to deliver performance at the committed level can lead to significant penalties.	Risk 1: Failure to deliver what our customers want	Reduce discretionary expenditure to cover any extra costs resulting from penalties. Discuss the impact on debt covenants with lenders and seek a temporary waiver if necessary.
5. *STW incurs higher costs than planned that are not funded* Significant overspending could result in a deterioration in financial metrics and performance, which might adversely impact the Group's solvency.	Risk 2: changes in the regulatory environment for the UK water industry	Reduce discretionary expenditure in the short term. In the medium term implement a cost reduction programme to deliver sustainable cost savings and efficiencies to bring costs back in line with regulated allowances. Discuss impact on debt covenants with lenders and seek a temporary waiver if necessary. Consider a temporary reduction in dividends.
6. *A combination of scenarios 2,3 & 4*	See above	Reduce discretionary expenditure in the short term. Reduce working capital to support cash flow. Discuss impact on debt covenants with lenders and seek a temporary waiver if necessary. Consider a temporary reduction in dividends.

The combined scenario represents a situation where several of the severe but plausible scenarios occur simultaneously. In this situation the same mitigating actions would be available to the Group but their application would be deeper.

The Group has significant funding requirements to refinance existing debt that falls due for repayment during the period under review and to fund the Group's capital programme. Under all scenarios considered the Group would remain solvent and have access to sufficient funds in normal market conditions. The Group's Treasury Policy requires that it retains sufficient liquidity to meet its forecast obligations, including debt repayments for the next 18 months.

The Group's business plans are based on the current regulatory framework and do not take into account any changes that might arise if a future Government implemented a policy of renationalisation of the water sector.

In making its assessment the Board has made the following key assumption:

- Any period in which the Group is unable to access capital markets to raise finance during the period under review will be shorter than 18 months.
- There is no renationalisation of the water sector in the period under consideration.

On this basis, the stress tests indicated that none of these scenarios, including the combined scenario, would result in an impact to the Group's expected liquidity, solvency or debt covenants that could not be addressed by mitigating actions and are therefore not considered threats to the Group's viability.

Governance and assurance

The Board reviews and approves the medium term plan on which this viability statement is based. The Board also considers the period over which the assessment of prospects and viability statement should be made. The Audit Committee supports the Board in performing this review. This statement is subject to review by Deloitte, our external auditor. Their audit report is set out on page 107.

Assessment of viability

The directors have assessed the viability of the Company over a seven year period to March 2026, taking into account the Company's current position and principal risks. Based on that assessment, the directors have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to 31 March 2026.

Going concern

In preparing the financial statement the Directors considered the Company's ability to meet its debts as they fall due for a period of one year from the date of this report. This was carried out in conjunction with the consideration of the Long-Term Viability Statement above. On this basis the Directors considered it appropriate to adopt the going concern basis in preparing the financial statements.

The strategic report, as set out from page 3 through to page 68, has been approved by the Board.

By order of the Board

Bronagh Kennedy
General Counsel and Company Secretary
20 May 2019

Chairman's Introduction to Governance

I am pleased to introduce our Governance report for 2019, on behalf of your Board. This report outlines how we have ensured that best practice and effective corporate governance procedures are in place to help support the creation of long-term value for the mutual benefit of all of our stakeholders. To ensure the long-term success of your business, directors and the companies they lead need to build and maintain successful relationships with a wide range of stakeholders, taking account of and responding to their views. These relationships will only be successful and enduring if they are based on respect, trust and mutual benefit. Accordingly, we want to promote a culture of integrity and openness, which values diversity and is responsive to the views of stakeholders. The Board has also embraced Ofwat's principles for board leadership, transparency and governance with its emphasis on the importance of strong board leadership and the special responsibilities attached to regulated monopoly companies providing an essential public service.

Company purpose and culture
The Board recognises the importance of its role in setting the tone for Severn Trent's culture and making sure that it is embedded throughout the Group. Our Code of Conduct, 'Doing the Right Thing', sets out clearly defined values and standards of behaviour that we expect from everyone who works for, and with, Severn Trent.

As discussed on page 89, we are committed to diversity and inclusion in all its forms, and during the year we were pleased to see the Company's progress continue to receive external recognition.

Workforce engagement
Engaged people are the key to the success of Severn Trent, which is why one of our five key strategic goals is to create an awesome place to work. Your Board recognises the importance of understanding the views of the workforce and considers that our Employee Forum is an excellent means of making sure that views from across the organisation are considered in Board discussions and decision making.

Engagement with our other stakeholders
Severn Trent's success also depends on your Board taking decisions that deliver mutual benefit to our customers and communities. Further details on how we have engaged with all of our stakeholders over the year can be found on pages 80 to 82.

Board effectiveness
This year the Board undertook an internal evaluation. The results of this review can be found on pages 85 to 86. I am pleased to report that your Board, its Committees, and individual Directors continue to operate effectively.

Looking ahead

Maintaining the highest standards of corporate governance is integral to the delivery of our strategy, and we remain focused on creating sustainable long-term value for the mutual benefit of our customers and communities. In July 2018 the FRC published the 2018 UK Corporate Governance Code (the "Code"), which we will voluntarily apply to our financial year ending 31 March 2020. We consider that this approach compliments the important matters within Ofwat's principles of leadership, transparency and governance and ensures the highest standards of governance are applied. As you will see within this report, the Board has carefully considered the 2018 Code and implemented many of the new principles earlier than required. This will allow new processes and procedures to fully embed ahead of our 2020 Annual Report and Accounts.

Board succession

The Board and the Severn Trent Plc Nominations Committee have fully considered Board succession during the course of the year to ensure that the Board has the right mix of skills and experience, as well as the capability to provide constructive challenge and to promote diversity. Additional details can be found within the Severn Trent Plc Nominations Committee report on page 81 to 84 of the Severn Trent Plc Annual Report and Accounts 2018/19.

As mentioned in my Chairman's Statement on page 5, I believe this is the right moment to step down and allow a new Chair to lead the Board into the next phase for Severn Trent. The Severn Trent Plc Nominations Committee, led by Senior Independent Director Kevin Beeston, is overseeing the process ahead of making a formal recommendation to the Board.
The Nominations Committee is in the initial stages of succession planning and further detail can be found on page 91. Kevin Beeston chaired the Committee when it met to discuss this matter. I hope you find this report useful.

Andrew Duff
Chairman
20 May 2019

UK Corporate Governance Code Compliance Statement

The membership of the Board of Severn Trent Water Limited is the same as that as the listed Company, Severn Trent Plc. This structure was implemented in 2007 to make sure that the highest standards of corporate governance are applied at the regulated subsidiary level and to foster greater visibility and supervision by the Severn Trent Plc Board.

As Severn Trent Water Limited is not a listed company it is not required to comply with the UK Corporate Governance Code (the "Code"). Severn Trent Water Limited complies with the 2016 Code. Severn Trent Water Limited also complies with Ofwat's Principles of board leadership, transparency and governance, to ensure the highest standards of governance.

The Code is available on the Financial Reporting Council's (FRC) website (www.frc.org.uk). The Board is pleased to confirm that Severn Trent Water Limited applied the principles and complied with all of the provisions of the 2016 Code throughout the year.

LEADERSHIP AND EFFECTIVENESS
Board of Directors

1. **Andrew Duff** BSc FEI
Appointed: Non-Executive Director on 10 May 2010, Chairman on 20 July 2010

Andrew’s extensive experience of international and regulated business, strategic management and customer service in high profile, dynamic environments has equipped him well for the role of Chairman of the Severn Trent Group. Andrew spent 16 years at BP Plc in marketing, strategy and oil trading. He joined National Power in 1998 and the Board of Innogy Plc upon its demerger from National Power in 2000. He played a leading role in its restructuring and transformation through the opening of competition in energy markets culminating in its subsequent sale to RWE in 2003. He became Chief Executive Officer of the successor Company and a member of the RWE Group Executive Committee until his retirement in 2010. He was a Non-Executive Director of Wolseley Plc from July 2004 until November 2013. Andrew was appointed Non-Executive Deputy Chairman of Elementis Plc on 1 April 2014 and became Non-Executive Chairman of Elementis Plc on 24 April 2014. He is the Senior Trustee of Macmillan Cancer Support.

2. **Olivia Garfield** BA (Hons)
Appointed: Chief Executive on 11 April 2014

Olivia (Liv) brings to the Board a wealth of experience managing customer service delivery and complex infrastructure and organisations in a regulated environment. Before joining Severn Trent, Liv was Chief Executive Officer of Openreach, part of the BT Group, where she spearheaded and oversaw the commercial roll-out of fibre broadband to two-thirds of the country. She joined BT in 2002 and held the pivotal roles of Group Director of Strategy and Regulation, Managing Director Commercial and Brands, Global Services and UK Customer Services Director. From 1998 to 2002, Liv worked for Accenture as a consultant in the Communications and High Tech Market Unit, designing and implementing business change solutions across a number of industry sectors.

3. **James Bowling** BA (Hons) Econ, ACA
Appointed: Chief Financial Officer on 1 April 2015

James is a chartered accountant, who started his career with Touche Ross and brings significant financial management, M&A and business transformation expertise to the Board. Prior to joining Severn Trent, James was interim Chief Financial Officer of Shire Plc, where he had been since 2005, first as

Head of Group Reporting and from 2008 as Group Financial Controller. Prior to joining Shire, James spent nine years at Ford Motor Company in various finance roles of increasing responsibility.

4. **John Coghlan** BCom, ACA
Appointed: Independent Non-Executive Director on 23 May 2014

John has a wealth of experience in financial and general management. He spent 11 years at Exel PLC as Chief Financial Officer and ultimately as Deputy Chief Executive Officer until retiring in 2006. Since then, he has been a Director of publicly-quoted and private companies across several sectors. Currently, John is also Non-Executive Director and Audit Committee Chairman of Associated British Ports Holdings Limited and Clarion Housing Group, and is Non-Executive Director of O.C.S. Group Limited.

John has recent and relevant financial experience as a member of the Institute of Chartered Accountants in England and Wales.

5. **Dame Angela Strank** DBE, FRS, FREng, CEng, FIChemE, DSc, PhD
Appointed: Independent Non-Executive Director on 24 January 2014

Angela brings a wealth of strategic, technical and commercial experience to the Board. Angela is Head of Downstream Technology and Group Chief Scientist at BP Plc. She is a member of the Downstream Executive Leadership Team. Angela is responsible for enabling delivery of the Downstream strategic agenda through the development of differentiated technology advantage across the refining, fuels, lubricants and petrochemicals businesses. Since joining BP in 1982, she has held many senior leadership roles around the world in business development, commercial and technology, including in 2012, as Vice President and Head of the Chief Executive's Office. In 2010, Angela was the winner of the UK First Woman's Award in Science and Technology recognising pioneering UK women in business and industry. Her track record and experience in strategy, operations, technology and transformational change are a complementary addition to the Board's skill set. In June 2017, Angela was recognised in the Queen's Birthday Honours List with the title Dame Commander of the Most Excellent Order of the British Empire ('DBE') for services to the Oil and Gas Industry and encouraging women into STEM careers.

6. **The Hon. Philip Remnant** CBE FCA MA
Appointed: Independent Non-Executive Director on 31 March 2014

Philip is a senior investment banker and brings substantial advisory and regulatory experience to the Board. A chartered accountant, he is Senior Independent Director of Prudential Plc, Deputy Chairman of the Takeover Panel and Chairman of City of London Investment Trust Plc. Previously, Philip was Vice Chairman of Credit Suisse First Boston Europe and Head of the UK Investment Banking Department. Philip was Director General of the Takeover Panel for two years between 2001 and 2003, and again in 2010. He served on the Board of Northern Rock Plc from 2008 to 2010 and from 2007 to 2012 was Chairman of the Shareholder Executive.

Philip has recent and relevant financial experience as a fellow of the Institute of Chartered Accountants in England and Wales.

7. **Dominique Reiniche** MBA
Appointed: Independent Non-Executive Director on 20 July 2016

Dominique has a wealth of operational experience in Europe and has international consumer marketing and innovation experience. Dominique is Independent Chair of CHR Hansen Holdings A/S and also a Non-Executive Director of Mondi Plc and PayPal (Europe). Dominique started her career with Procter & Gamble AG before moving to Kraft Jacobs Suchard AG as Director of Marketing and Strategy where she was also a member of the Executive Committee. Dominique previously held a number of senior roles at Coca-Cola Enterprises and at Coca-Cola Company, including President – Western Europe, President – Europe and Chairman – Europe, Dominique was a Non-Executive Director of Peugeot-Citroen SA until December 2015 and was a Non-Executive Director of AXA SA until April 2017.

8. **Kevin Beeston** FCMA
Appointed: Senior Independent Non-Executive Director on 1 June 2016

Kevin has a wealth of commercial, financial and high level management experience. Kevin is Chairman of Taylor Wimpey Plc and Elysium Healthcare and also a Non–Executive Director of the Football Association Premier League Limited and Marston Corporate Limited. Previously, Kevin spent 25 years at Serco Plc, where he held the roles of Finance Director, Chief Executive and finally Chairman until 2010. Kevin was previously Chairman of Domestic & General Limited, Partnerships in Care Limited and Equiniti Group Plc, and was a Non-Executive Director of IMI Plc.

Kevin has recent and relevant financial experience as a fellow of the Chartered Institute of Management Accountants and was previously Finance Director at Serco Plc.

Board and Committee meeting attendance 2018/19

The following table shows the attendance of Directors at scheduled Board and Committee meetings during the year:

Director	Position	Board	Audit Committee	Nominations Committee	Remuneration Committee	Treasury Committee	CR Committee
				Attended/scheduled			
Andrew Duff	Chairman	7/7	–	4/4	4/4	–	4/4
Kevin Beeston	Senior Independent Director	7/7	4/4	4/4	4/4	–	–
James Bowling	Chief Financial Officer	7/7	–	–	–	5/5	–
John Coghlan	Non-Executive Director	7/7	4/4	4/4	–	5/5	–
Liv Garfield	Chief Executive	7/7	–	–	–	–	4/4
Dominique Reiniche	Non-Executive Director	7/7	–	4/4	–	–	4/4
Philip Remnant	Non-Executive Director	7/7	4/4	4/4	4/4	5/5	–
Dame Angela Strank	Non-Executive Director	7/7	–	4/4	4/4	–	4/4

Executive Committee

1. **Olivia Garfield** BA (Hons)
Appointed: Chief Executive on 11 April 2014
Please see full biography on page 71

2. **James Bowling** BA (Hons) Econ, ACA
Appointed: Chief Financial Officer on 1 April 2015
Please see full biography on page 71

3. **Dr. Tony Ballance** BSc (Hons), MA (Econ), PhD
Director of Strategy and Regulation
Tony's extensive experience in utility policy, regulation and stakeholder engagement leaves him ideally placed to lead the Company's strategic, regulatory and external affairs work. Prior to joining Severn Trent, he held the posts of Chief Economist for Ofwat, Director of London Economics and Director of Stone and Webster Consultants.

Other roles
- Member of Water UK Council
- Senior Independent Director of the National Forest Company

• Chairman of the Corporate Advisory Panel of the Regulatory Policy Institute

4. **Sarah Bentley** BSc (Hons), Management Science with Computing
Chief Customer Officer Sarah is responsible for Customer Retail and Network operations, Group Technology and Transformation. Previously Sarah worked for Accenture as Managing Director of their £3 billion global digital business focused on digital marketing, mobility and analytics for customers, employees and the enterprise. Prior to Accenture, Sarah was CEO of Datapoint, an Alchemy backed company delivering CRM services, and Senior Vice President of eLoyalty, a global CRM and marketing consultancy. She was SVP of the European Business, led the sales and operations activity in North America and ran eLoyalty Ventures L.L.C. working in Silicon Valley, Austin and New York.

Other roles
• Non-Executive Director of Lloyds Bank Plc and Bank of Scotland Plc
• Director and secretary of Twizzletwig Limited

5. **Martin Kane** BSc, CEng, CEnv, MICE, MIWEM, FIW
Special Advisor
He has held various senior roles giving him an extensive and unique understanding of the design, construction and operation of water and waste water treatment plants, water distribution networks and sewerage systems. Martin was Director of Customer Relations, Severn Trent Plc, from May 2006 until January 2012, and Chief Executive Officer of Severn Trent Services until July 2014.

Other roles
• Chairman of the Board of Trustee's of International Society for Trenchless Technology
• Chairman of the Panton McLeod Limited
• Chairman of the Coventry and Warwickshire Growth Hub

6. **Bronagh Kennedy** BA (Hons)
Bronagh joined Severn Trent in 2011 as Group Company Secretary and General Counsel. She is also responsible for compliance and assurance and the Group's Corporate Social Responsibility programme. During her career she has worked across several sectors including finance, leisure and hospitality and she has a broad range of corporate experience, having led FTSE100 Company HR, communications, insurance, risk and health, safety and wellbeing functions. She has also been a Non-Executive Director on industry bodies such as the British Hospitality Association. Prior to moving in house she was a senior associate solicitor in Allen & Overy's banking and insolvency group.

Other roles
• Chairman, HR and Remuneration Committee and Non-Executive Director of British Canoeing
• Member of the GC100 Group

7. **Helen Miles** CIMA
Capital Delivery and Commercial Director
Helen joined Severn Trent in November 2014 as the Chief Commercial Officer. Helen brings with her a breadth of commercial experience having worked within regulated businesses and sectors across Telecoms, Leisure and Banking. As a member of the UK Board, Helen was instrumental in delivering HomeServe's future growth strategy and ensuring a sustainable, customer-focused business. Helen is Non- Executive Director of the Royal Navy and as an experienced finance professional, Helen was previously Chief Financial Officer for Openreach, part of BT Group Plc, and has extensive experience of delivering major business transformation across the Group. Prior to BT Group, Helen worked in a variety of sectors and organisations such as Bass Taverns, Barclays Bank, Compass Group and HSBC.

Other roles

• Non-Executive Director of the Royal Navy

8. **Andy Smith** BTech (Hons)
Managing Director, Business Services
Andy was appointed to the role of MD, Business Services on its creation in 2014 having previously been responsible for the drinking water business within Severn Trent Water. Andy brings to the role a broad range of executive and operational expertise gained from diverse sectors. Currently, Andy is also a Non-Executive Director of Diploma plc. He has worked in the UK and overseas with global businesses such as BP, Mars and Pepsi in both engineering, HR and operational management roles. Previously, he has served as a member of the Board at Severn Trent Plc and at Boots Group Plc.

Other roles
• Non-Executive Director, Chairman of the Remuneration Committee and member of the Audit and Nominations Committees of Diploma Plc
• Director of Water Plus Limited – joint venture with United Utilities

9. **Neil Morrison** Bsc (Hons), FCIPD
Director of Human Resources
Neil joined Severn Trent in August 2017 as a Director of Human Resources. Neil started a career in HR management in 1996 and for the subsequent 12 years he worked in a variety of HR roles within FTSE 100 companies, including Rentokil Initial and GUS (which latterly became Home Retail Group). Before joining Severn Trent, Neil worked at Penguin Random House taking responsibility for strategic people issues across their publishing and distribution offices in the UK, APAC, India and South Africa. He was one of the main leads in helping to steer and finalise the global merger between Random House and Penguin.

10. **Dr. James Jesic** BEng (Hons), PhD, MIChemE, CEng
Managing Director of Production
James is a chartered chemical engineer who joined Severn Trent on its graduate programme in 2003 and was appointed as Managing Director of Production in 2017. During his time with the business, James has had full accountability for the management of the operational multi-billion pound asset base, being responsible for producing and supplying drinking water and collecting and treating waste water for millions of customers across the Midlands. As part of that role, he has delivered industry-leading customer service performance, as well as driving sector leading environmental results. He has a PhD in Chemical Engineering from the University of Birmingham and has attended Harvard Business School.

11. **Dr. Bob Stear** MEng (Hons), PhD, MCIWEM, CWEM, FIWater
Chief Engineer
Bob was appointed Chief Engineer in November 2018 and is a chartered Environmental Engineer who joined Severn Trent in 1997 as a process technician. He has worked his way up through the company via operational, engineering, strategic and innovation roles. In particular Bob played a key role in the transformation of the wastewater business and successfully governed a c£1.2bn capital programme. In 2013, Bob worked alongside the Government on the implementation of the 2014 Water Act. He has a PhD in wastewater treatment.

Governance – Board Composition and Roles

As at 31 March 2019, our Board comprised the Chairman, five Non-Executive Directors and two Executive Directors.

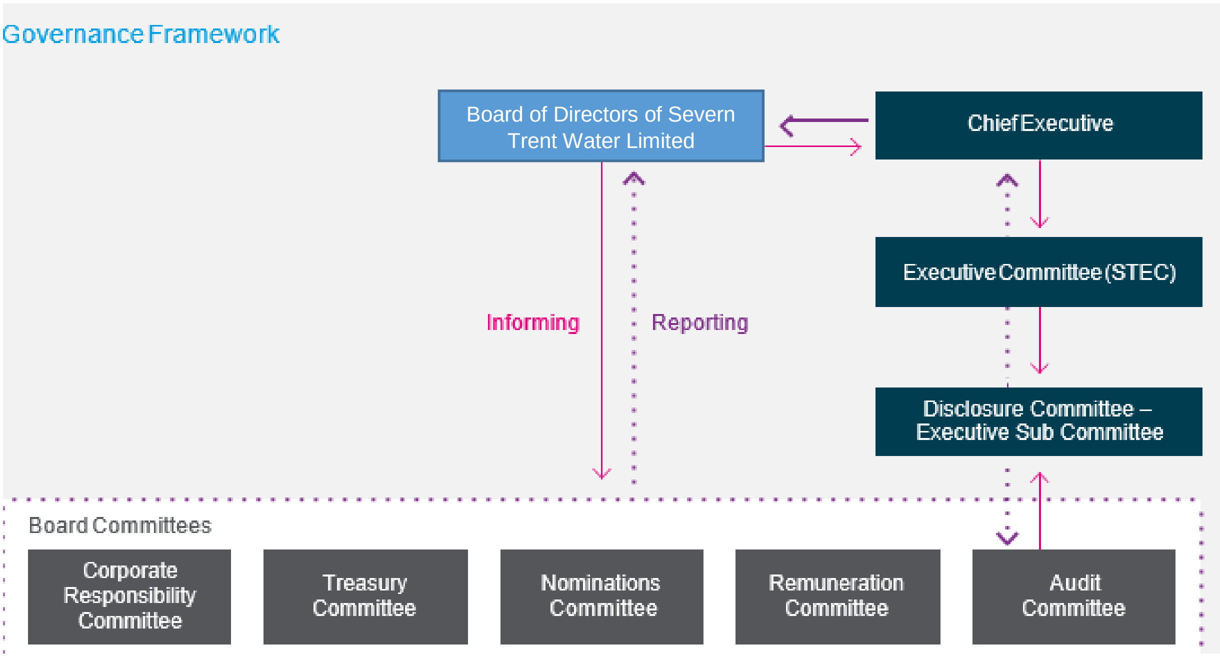
The details of their career background, relevant skills, Committee membership, tenure and external appointments can be found within the individual Biographies on pages 71 to 73.

The composition and effectiveness of the Board is subject to regular review by the Severn Trent Plc Nominations Committee which, in particular, considers the balance of skills, experience and independence of the Board, in accordance with the Board Diversity Policy. The Board Diversity Policy statement is available on the Severn Trent Plc website. Any new appointments to the Board result from a formal, rigorous and transparent procedure, responsibility for which is delegated to the Severn Trent Plc Nominations Committee (although decisions on appointments are a matter reserved to the Severn Trent Water Limited Board).

Director	Responsibility
Chairman Andrew Duff	• Leads our unified Board and is responsible for its effectiveness. • Sets agendas and ensures timely dissemination of information to the Board, to support sound decision making and allow for constructive discussion, challenge and debate, in consultation with CEO, CFO and Company Secretary. • Responsible for scrutinising the performance of the Executive Committee and overseeing the annual Board effectiveness evaluation process. • Facilitates contribution from all Directors and ensures that effective relationships exist between them. • Ensures that the views of all stakeholders are understood and considered appropriately in Board discussion and decision-making.
CEO Liv Garfield	• Represents Severn Trent externally to all stakeholders, including our employees, the Government and regulators, customers, suppliers and the communities we serve. • Develops and implements the Group's strategy, as approved by the Board. • Sets the cultural tone of the organisation. • Facilitates an effective link between the business and the Board to support effective communication. • Responsible for overall delivery of commercial objectives of the Group. • Promotes and conducts Group affairs with the highest standards of integrity, probity and corporate governance, in line with our strategic framework and values.
CFO James Bowling	• Manages the Group's financial affairs. • Supports the CEO in the implementation and achievement of the Group's strategic objectives. • Oversees Severn Trent's relationships with the investment community. • Represents Severn Trent externally to all stakeholders, including our employees, the Government and regulators, customers, Pension Trustees for the company's Defined Benefit Pension Scheme, suppliers and the communities we serve.
SID Kevin Beeston	In addition to his responsibilities as a Non-Executive Director, Kevin also: • Supports the Chairman in the delivery of his objectives. • Acts as an alternative contact for shareholders should they have a concern that is unresolved by the Chairman, CEO or CFO. • Leads the appraisal of the Chairman's performance with the Non-Executive Directors. • Undertakes a key role in succession planning for the Board, together with the Board Committees, Chairman and NEDs.
NEDs John Coghlan Dominique Reiniche Dame Angela Strank Philip Remnant	• Monitor the delivery of strategy by the Executive Committee within the risk and control framework set by the Board. • Satisfy themselves that internal controls are robust and that the External Audit is undertaken properly. • Engage with internal and external stakeholders and feedback insights to the Board, including in relation to employees and the culture of the Company. • Constructively challenge and assist in the development of strategy. • Have a key role in succession planning for the Board, together with the Board Committees, Chairman and SID. • Serve on various Committees of the Board.
Company Secretary Bronagh Kennedy	• Ensures sound information flows to the Board in order for the Board to function effectively and efficiently. • Advises and keeps the Board updated on Listing and Transparency Rule requirements and on best-practice corporate governance developments. • Facilitates a comprehensive induction for newly appointed Directors, tailored to their individual requirements. • Ensures compliance with Board procedures and provides support to the Chairman. • Co-ordinates the performance evaluation of the Board in conjunction with the Chairman. • Provides advice and services to the Board.

Our Board

The Board's role is to ensure the long-term success of Severn Trent Water Limited. Maintaining the highest standards of governance is integral to the effective delivery of our strategy and ensuring that the Board take decisions that create sustainable long-term value for the mutual benefit of our stakeholders, customers, employees and the communities we serve. The operation of our Board is supported by the collective experience of the Directors and the diverse skills and experience they possess. This enables the Board to reach decisions in a focused and balanced way, supported by independent thought and constructive debate between the Directors. Trust and mutual respect are the cornerstones of relationships between our Directors, with a Board dynamic that supports open and honest conversations to ensure decisions are taken for the benefit of the Company in full consideration of the impact on all stakeholders. Responsibility to all of our stakeholders for the approval and delivery of the Company's strategy and for creating and overseeing the framework to support its delivery sits with the Board. The requirements of the Board are clearly documented in the Severn Trent Water Limited Articles of Association, Schedule of Matters Reserved to the Severn Trent Water Limited Board and Charter of Expectations. These are available on the Severn Trent Plc website. As outlined on page 77, there is a clear division of responsibilities between the roles of Chairman and CEO. To allow these responsibilities to be discharged effectively, the Chairman and CEO maintain regular dialogue outside of the Boardroom, to ensure an effective flow of information. The Non-Executive Directors have direct access to senior management at all times. Informal as well as formal contact with the wider business is encouraged to develop a deeper understanding of Severn Trent's operations and requests for further information are welcomed. This broadens the Non-Executive Directors' sources of information and enables them to consider the wider impact of any Board decisions on stakeholders more broadly.



Governance Framework

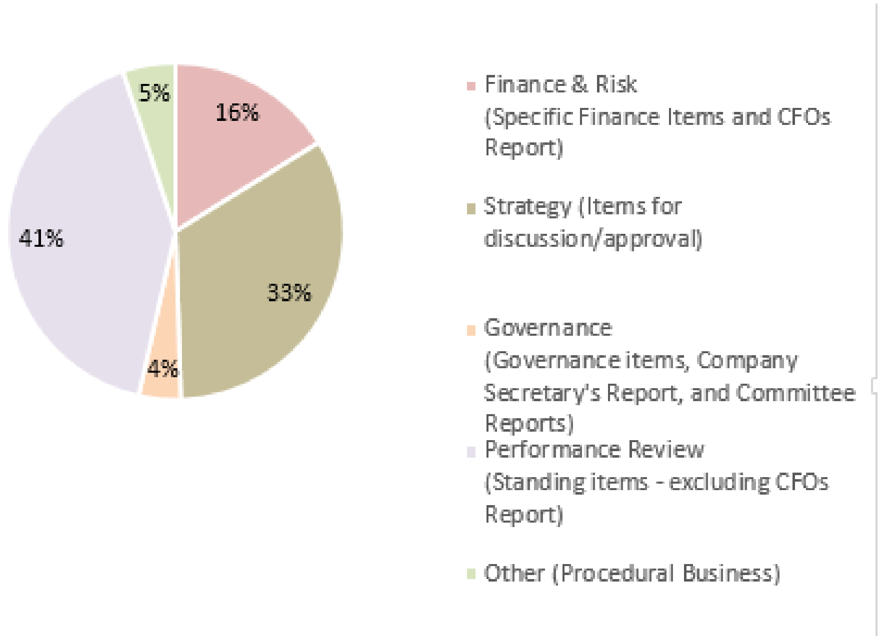
The Board is supported by the Severn Trent Governance Framework, which is set out above. The Governance Framework comprises the Board, STEC and their respective Committees. In line with the Code, the Board delegates certain roles and responsibilities to its various Committees. The Committees assist the Board by fulfilling their roles and responsibilities, focusing on their specific activities, reporting to the Board on decisions and actions taken, and making any necessary recommendations to the Board in line with their Terms of Reference. The Board regularly reviews the Terms of Reference of each

Committee, which are available on the Severn Trent Plc website. The Governance Framework is also subject to periodic review to ensure that it continues to remain fit for purpose.

Severn Trent Executive Committee ('STEC')

Responsibility for the development and implementation of the Company's strategy and overall commercial objectives rests with the Chief Executive who is supported by STEC. More information on our STEC members can be found on pages 74 to 76.

Board Focus 2018/19



Main topics discussed by the Board during the year

Regular Updates

- CEO Performance Review
- CFO Performance Review
- Operational Performance Review
- Reports from Employee Forum
- Corporate Governance developments and Legal Affairs report

Financing Strategy

- Budget
- Severn Trent Water Dividend
- Pension Scheme Update
- Annual Report and Accounts for Severn Trent Water Limited
- Annual Performance Report for Severn Trent Water Limited

Governance and Stakeholders

- Board Effectiveness Evaluation

- Preparations for the 2018 UK Corporate Governance Code
- Presentations from DWI, CCW, Chair of Customer Forum

Regulatory

- PR19
- Annual Report and Accounts
- Annual Performance Reports
- Water Resources Management Plan
- Scheme of Charges
- New connections charging
- Renationalisation update
- Modern Slavery Act
- GDPR

Strategy

- People strategy
- Property strategy
- Talent development and succession planning
- Technology strategy
- Innovation update
- Tax strategy
- Board Strategy day

Culture and Values

- Company purpose and culture
- Board Diversity
- Health, Safety and Wellbeing
- Annual employee survey results – QUEST
- Review and approval of various Group policies to support Severn Trent's culture of Doing the Right Thing

Risk Management

- Cyber risk
- Whistleblowing updates
- Regulatory updates
- Enterprise Risk Management reports
- Brexit
- Review of Effectiveness of Internal Controls and Risk Management
- Defense update
- Review of Effectiveness of Risk Management and Internal Controls

Stakeholder Engagement

The Board recognises the importance of considering all stakeholders in their decision making, as set out in Section 172 of the Companies Act, and the positive impact this has in promoting the success of the Company as a whole. The table below sets out details of key stakeholder engagement undertaken by the Board during the year.

Customers

- Customer Delivery Performance Report tabled at every Board meeting.
- Extensive customer research considered regularly by the Board in relation to the PR19 plan and submission.
- Board attended some of our PR19 customer research sessions.

Employees

- Board attended a Company Purpose and Culture session with employee representation and discussion of the QUEST survey results.
- CEO attended employee roadshows and senior leader event.
- Board meetings held at a variety of sites, including operational sites. Directors met a number of employees at these events.
- Board site visits outside of the Board meeting calendar, where Directors met employees and discussed matters with them.
- Chairman, Non-Executive Director and Executive Director attendance at the Employee Forum, including an opportunity to meet employees across the Group. Individual Directors provide feedback to the Board following Forum attendance.
- Internal blogs by Executive Directors.
- Regular senior leader calls with Executive Directors.
- Talent development considered by the Board.
- Dedicated People Strategy discussion at Board Strategy day

Communities

- Employees who live and work in our communities meet the Board at the Employee Forum and site/ operational visits.
- Corporate Responsibility reports regularly discussed at Board meetings, including an update on community activities.
- Board received updates on the Group's volunteering programme during the year.
- Immersive Board session on the 'Wonderful Water Tour' - our new innovative educational tour to inspire and educate children in our communities.
- Volunteering update considered by the Board.
- Board site visit to Lake Vyrnwy Reservoir and Visitor Experience Site.

Regulators / Government

- Renationalisation Reports considered by the Board.
- Regulatory matters regularly considered at Board meetings, including PR19, Water Resources Management Plan and Scheme of Wholesale Charges.
- Regulatory stakeholder attendance at Board meetings during the year.
- Chairman met with Jonson Cox, Ofwat.
- Engagement with the DWI Lead Inspector, EA, CCW and Pension Trustees for the Company's Defined Benefit Pension Scheme.
- Regulatory consultation updates provide to the Board, including Severn Trent's proposed response

Suppliers / Contractors

- Commercial Performance Report tabled at every Board meeting, including an update on relationships with suppliers and associated performance.
- Chairman and Executive Director attendance at the Employee Forum, including attendance by suppliers.

The Board in Action

The Board sets the strategy, oversees its delivery and maintains the highest standards of governance which are integral to its delivery. The Board also ensures that, in making its decisions, these create sustainable, long-term value for the mutual benefit of stakeholders. In order for the Company to manage risk effectively, the Board monitors financial performance and reporting and also ensures that appropriate and effective succession planning arrangements and remuneration policies are in place. The main topics discussed by the Board during the year are set out on pages 79 and 80.

Board Strategy Days

In addition to formal meetings at which strategic matters are regularly considered, in June 2018 the Board held a dedicated strategy meeting with the Executive Committee to focus on PR19, being a key matter for the Company during the year. The day also focussed on the Company's people strategy, including culture, talent acquisition, talent development, talent management and organisational performance. The Strategy Day also covered the potential for artificial intelligence, data analytics and robotic process automation to improve efficiency and performance across the business. The Board was immersed in Strategy Day topics through use of real examples and simulation to demonstrate current and planned interventions. For 2019, a portion of the strategy meeting will focus on AMP7 delivery plans, following Severn Trent Water's plan for the five years from 2020 being fast-tracked by Ofwat. The Board will also consider the Company's carbon and energy strategies, with discussion on key priority areas.

Our Company purpose and culture
The Board is responsible for establishing Severn Trent's purpose, vision and strategy, and satisfying itself that its culture is aligned. Our purpose – to serve our communities and build a lasting water legacy – reflects 'why' we do what we do. Our strategy provides us with 'what' we do. But the 'how' we deliver our purpose and strategy is what differentiates us and sets us apart and that is driven by our culture, values and behaviours. To support the creation of long-term value for the mutual benefit of our stakeholders, our employees, customers and communities, the Board recognises the importance of building and promoting a culture of integrity and openness, where inclusion and diversity is valued and we are responsive to the views of all our many stakeholders in all that we do.

At the heart of Severn Trent's culture are a closely held set of values – 'Doing the Right Thing'. These values embody the principles by which the Company operates, and provide a consistent framework for responsible business practices. These policies codify how to identify and deal with suspected wrongdoing, fraud or malpractice; how to ensure that the highest standards of safety are maintained; and how to apply good ethics and sound judgment. During the year, the Board has focused on deepening its understanding of the Company's culture even further, through a dedicated Company purpose and culture session in January 2019. The session was centred on the results of the all employee survey 'QUEST' and other relevant data. The Board considered the positive and more challenging aspects revealed by the survey and discussed the Company's approach to addressing areas of employee focus, such as health and safety and gender neutral facilities at operational sites. The Board routinely interacts with employees as part of their site visit programme. This direct interaction with employee representatives specifically in relation to culture has allowed the Board to understand first-hand the key issues identified by our workforce, and provided an opportunity to feedback specific insights to them. The findings from this culture session are being used to inform future areas of focus for the Board moving forward. As part of this activity the Board satisfied itself that the Company's policies, practices and behaviour throughout the business are wholly aligned with Severn Trent's purpose, vision and strategy.

Reinforcing our culture

Severn Trent's values support Doing the Right Thing and drives delivery of the Group's strategy

- We put our **customers first**
- We are **passionate** about what we do
- We act with **integrity**
- We protect our **environment**
- We are inspired to create an **awesome company**

Educating our people, supporting and guiding them to demonstrate positive behaviours in all they do

Doing the Right Thing has supporting policies that apply to everyone who works for Severn Trent.

These policies are the strategic link between our vision and how we manage our day-to-day business, and are underpinned by specific company standards and procedures.

To support understanding of our policies and standards, there is programme of targeted training, including e-learning modules and practical training sessions.

Review mechanisms to further support and assess our culture

Our workforce can raise concerns at work through their line manager, senior management and through our confidential and independent whistleblowing helpline, 'Safecall'. All investigations are carried out independently with findings being reported directly to the Audit and Corporate Responsibility Committees. The Audit Committee monitors and reviews the effectiveness of the Group's whistleblowing arrangements annually and provides feedback to the Board.

Reports from the respective Chairs are provided to the Board at the outset of every meeting, with any serious allegations being directly reported to the Board.

Our annual employee engagement survey, 'QUEST', provides data in a clear and comprehensive form, identifying what's going well and where we can improve across the Group. QUEST is conducted by an independent research company to ensure the results are anonymous and the results are reported to the Board.

Dedicated culture discussions are included at our Employee Forum, hosted by the Company and attended by the Chairman, Non-Executive Directors and Executive Directors. This regular Forum is attended by numerous employee representatives, Unions and other stakeholders to enable the views throughout the organisation to be considered at Board level. Individual Directors provide feedback at the Board meetings following Forum attendance.

Feedback to the Board to deepen its understanding of the Group's culture

Our established reporting mechanisms for company purpose and culture are essential tools in the Board's oversight of cultural matters. All feedback received deepens the Board's understanding of the Group's culture and Board feedback is used to inform future areas of focus and ensure that local plans are consistent with feedback received.

Board Evaluation

The effectiveness of the Board is reviewed at least annually, and conducted according to the guidance set out in the Code and FRC Guidance on Board Effectiveness. An externally facilitated evaluation was last conducted by Manchester Square Partners in 2017/18, with the next externally facilitated session scheduled for 2021.

The 2018/19 evaluation was internally conducted by the Chairman with support from the Company Secretary through a series of one-to-one meetings in January and February 2019. Separate meetings were held to consider the effectiveness of the CEO, led by the Chairman, and of the Chairman, led by the Senior Independent Director. Following completion of the Evaluation process, the Board considered the report's findings and agreed specific actions. It was also agreed that six-monthly reviews on progress against the report's recommendations would be tabled for Board discussion.

Evaluation Process

Step 1. 2018/19 Process Planning

The Company Secretary undertook a detailed review of the Board Effectiveness Evaluation process and made revisions to incorporate recommendations and areas of focus highlighted in the 2018 UK Corporate Governance Code and FRC Guidance on Board Effectiveness.

A process for comprehensive one-to-one meetings was developed for the Board and its Committees, with interview questions structured on the basis of feedback from the 2017/18 evaluation, including areas for improvement and any additional observations.

Step 2. One-to-one meetings

Board and Committee members participated in comprehensive one-to-one meetings with the Company Secretary, with appropriate time provided to allow detailed discussion to take place.

Step 3. Evaluation and reporting

The Company Secretary compiled the individual responses, including analysis of themes and proposed actions. A detailed report, setting out the findings of the Evaluation was provided to the Chairman for consideration. The Company Secretary and Chairman met to discuss the findings, with the resulting report being tabled to the Nominations Committee and Board in March 2019.

Step 4. Agree actions and monitor progress

The findings of the Evaluation exercise were fully considered when making recommendations in respect of the re-election of individual Directors and included an assessment of their independence, time commitment and individual performance.

Evaluation findings

The Evaluation concluded that excellent progress had been made in respect of areas for further focus identified in the 2017/18 review as detailed below. The key theme highlighted in the 2018/19 evaluation was positive Board discussion dynamics. It was noted that all Directors fostered a culture of open, constructive debate, undertaken by a respectful and cohesive, and appropriately challenging Board.

The Evaluation also concluded that the Board was effective and that all Directors were considered to have demonstrated considerable commitment and time to their roles, well in excess of that required by the Charter of Expectations, notwithstanding any other positions held by them outside of Severn Trent. Minor areas for further development of the Board's effectiveness were as detailed below: As part of the Evaluation, full consideration was given to the number of external positions held by the Non- Executive Directors. Directors' other appointments were reviewed, including the time commitment required for each. As a result of this review, the Severn Trent Plc Nominations Committee did not identify any instances of overboarding and confirms that all individual Directors have sufficient time to commit to their appointment as a Director of Severn Trent Water Limited. The full list of external appointments held by our Directors can be found on pages 71 to 73. All of our Non-Executive Directors are considered to be independent.

Evaluation findings

Evaluation Action 2017/18	Progress 2018/19
Balance of Debate – continue to maintain focus on strategic, operational and reputational priorities as well as regulatory matters.	Separate, dedicated PR19 meetings were scheduled outside the normal Board and Committee timetable, to reduce the pressure on the Board agenda and maintain focus on strategic, operational and reputational priorities. During the 2018/19 Evaluation, the Board noted that PR19 approval and submission had been particularly well managed and that the use of additional Board Committee meetings and briefing papers had ensured that this topic had not distracted the Board from considering other strategic issues and operational performance oversight.
Talent Management and Succession Planning – opportunity to apply more structure to succession planning and talent development discussions at the Nominations Committee and the Board.	Talent and succession planning have been added as separate standing Nominations Committee agenda items with a forward Board programme for talent and succession planning also being developed. Existing talent and succession planning elements of the Board induction programme were updated to give new Non-Executive Directors better oversight of the Group's processes.
Board Composition – opportunity to increase the ethnic diversity of the Board in line with the recommendations of the Parker Review and to appoint an additional Director with Treasury/ Engineering experience.	Succession planning was considered by the Nominations Committee, and Board, during the year. This included consideration of the Board's Diversity Policy and its aims to increase the ethnic diversity of the Board in line with the recommendations of the Parker Review. The Board also considered Board succession planning in respect of Directors with more Treasury and Engineering experience.
Financing – opportunity to spend more time on this topic during NED induction given its complexity.	Relevant sections of the Board induction materials have been reviewed during the year. The Board induction programme now includes two additional face-to-face sessions with the finance team to provide the opportunity to clarify and deepen Director knowledge.
Culture – develop a structured plan to enable the views, ideas and constructive challenge throughout the organisation to be considered at Board level.	Company purpose and culture continues to be considered by the Board as a separate Board agenda item. The Chairman and Non-Executive Directors will continue to attend our Employee Forum. This regular forum is attended by numerous employee representatives, Unions and other stakeholders to enable the views throughout the organisation to be considered at Board level. Individual Directors provide feedback at the Board meetings following Forum attendance.

Minor areas for further development of the Board's effectiveness

Evaluation Action 2018/19	
Succession Planning	Opportunity to apply more focus to succession planning, in full consideration of Director tenure.
Balance of Debate	The Board noted the excellent chairing of Board discussions despite challenging agendas during the year. Opportunity to allocate additional time on the Board agenda to engage personally with presenters and discuss matters more informally.
Board Composition	Opportunity to consider broader diversity and inclusion in terms of the Board's composition.
Remit of Board Committees	Opportunity to review the duties within the respective Committee Terms of Reference and ensure that Committee meetings have sufficient time allocated to them.

Board Development and Knowledge

Training and continuing professional development ('CPD')

As well as Board agenda items, training and CPD sessions in relation to specific topics of interest were presented to Directors during the year, as follows:

- Severn Trent Academy;
- Leakage Innovation;
- Birmingham Resilience;
- Customer Bills;
- Wonder Water Tour (our Educational Buses);
- Impact of Renationalisation;
- Robotics and Artificial Intelligence;
- Company Purpose and Culture; and
- Capital Spend.

The aim of the training sessions is to continually refresh and expand the Board's knowledge and skills. In doing so, the Directors can contribute to discussions on technical and regulatory matters more effectively. The sessions also serve as an opportunity for the Board to discuss strategy and risks with management below Executive Committee level and gain further direct insight into our businesses and management capability.

Our Regulators
To deepen Board level understanding of our Regulators, our Chairman and Non-Executive Directors formally met with our Regulator, Ofwat, five times during the year.

Informal Board interactions
The Board regularly meets more informally, in the form of Board dinners, outside of the scheduled Board meeting calendar. These sessions are convened to build and maintain successful relationships and promote a culture of openness in Board discussions. Senior Management and external stakeholders (including Ofwat and the Water Forum) are invited to attend these sessions.

Directors' resources
An online resource library and CPD repository is available for use by the Directors, which is continually reviewed and updated. The library includes a Corporate Governance Manual and details of Board training sessions. It also contains a further reading section which covers updates and guidance on changes to legislation and corporate governance best practice. The Directors also have access to professional development provided by external bodies and our advisers. CPD requirements were considered through individual performance review meetings between the Chairman and each Director, as part of the internally facilitated Board effectiveness review in 2018/19.

Induction programme

Whilst there have been no new appointments to the Board of Severn Trent Water Limited during the year, we have an established induction programme in place which can be tailored to meet the requirements of individual Directors and includes the following elements/details:

- Ofwat pre-appointment process;
- Our business and how we are regulated, including performance;
- Strategy;
- Key operations and processes;
- Key stakeholder relationships including an immersive, practical journey through the water and waste cycle;
- Customer delivery;
- Capital delivery and commercial;
- How the business is financed and financial performance;
- Financial performance;
- Our people and how we work, including health, safety and wellbeing, talent and succession, trade unions and an overview of our Remuneration Policy;
- Risk and audit, including the Company’s risk profile and our approach to risk;
- Face-to-face meetings with key senior colleagues;
- Directors’ duties; and
- Governance matters and Company policies.

We continually enhance the Board’s induction process, in full consideration of feedback from new appointees and the Board effectiveness evaluation.

Operational and Site Visits

The Board, and individual Directors, undertook two key site visits during the year, to deepen their understanding of the Company’s operations and further inform the Board’s decision making in creating sustainable long-term value for the mutual benefit of stakeholders.

Site	Objectives	Key Board Considerations
Minworth – Thermal Hydrolysis Plant ('THP')	• Practical demonstration of Health and Safety considerations on complex operational sites • Employee expertise • Overview and demonstration of the sludge treatment process and operations • Overview of THP process and its importance to the Group, including implementation of technological advances • Process optimisation across the Minworth site • Site sampling and performance record • Environmental	• Health and safety • Employee stakeholders and people strategy • Operational knowledge • Technology • Environment
Lake Vyrnwy Reservoir and Visitor Site	• Practical demonstration of Health and Safety considerations on publicly accessible sites • Tour and briefing on educational programmes provided at the site • Tour of conversation programmes, including RSPB Organic Farm and SSSI site. • Opportunity to interact with employees • Overview of Lake Vyrnwy's infrastructure • Catchment management activities • Biodiversity activities	• Customer and community experience • Environment • Health and safety • Employee stakeholders and people strategy • Operational knowledge • Infrastructure • Environment • Biodiversity

Diversity

As highlighted earlier in the report, the Board continues to drive the agenda of diversity across the Company and is proud of the progress made, especially in respect of female representation on the Board and Executive Committee (now at 37.5% and 36% respectively). A breakdown by gender of the number of persons who were Directors of the Company, strategic leaders and other employees as at 31 March 2019 is set out below.

Employee Population	Male	Female
Board	62.5%	37.5%
Strategic Leader and Director	59.32%	40.68%
Group	69.86%	30.14%
Graduates	60.76%	39.24%
Apprentices	86.15%	13.85%

The Board remains focused on promoting broader diversity, and creating an inclusive culture in line with the recommendations from the Parker and McGregor-Smith reviews. A diverse organisation benefits from differences in skills, regional and industry experience, background, race, gender, sexual orientation, religion, belief and age, as well as culture and personality. The Board Diversity Policy (the ‘Policy’) was updated and approved by the Board in January 2019. As part of Board discussions, recognition was given to the importance and benefits of greater diversity, including gender diversity, social and ethnic background and cognitive and personal strengths throughout the organisation, including on the Board itself. Although no targets have been set at present, the benefits that diversity brings to the Board are wholly recognised and is evidenced through the commitments made in the Board Diversity Policy. The objectives of the Policy, and an update against each of them, are set out below. A copy of the Policy is available on the Severn Trent Plc website.

Policy Objectives	Implementation	Progress against objectives
Ensure the Board comprises an appropriate balance of skills, experience and knowledge required to effectively oversee and support the management of the Company.	Annual review of the Board's composition by the Nominations Committee each year with particular consideration being given to the balance of skills, experience and independence of the Board. Board effectiveness evaluation specifically considers the composition of the Board and the contribution, commitment and independence of individual Directors.	At its March meeting, the Committee formally reviewed the composition of the Board and the performance, contribution and commitment of each of the above retiring Directors in the context of the Board Effectiveness Review. No concerns were raised regards the composition of the Board. Regular updates in respect of succession planning fully consider the Board's Diversity Policy and its aims to increase the ethnic diversity of the Board in line with the recommendations of the Parker Review. The Board also considered Board succession planning in respect of Directors with specific experience in Treasury and Engineering.
Ensure consideration is given to candidates for Non-Executive Director Board appointments from a wide pool, including those with no listed company Board level experience.	The Board and Nominations Committee recognise the importance and benefits of greater diversity including gender diversity, social and ethnic background and cognitive and personal strengths, throughout the organisation, including on the Board itself. On instruction of an executive search firm(s), the specification will ensure that candidates with no listed company Board level experience are fully considered.	No Board appointments were made during the year however all recommendations in respect of future Board appointments will be conducted in full consideration of the Policy, 2018 Code, and additional relevant guidance.
Ensure Board appointment 'long lists' include diverse candidates, including diversity of social and ethnic backgrounds and cognitive and personal strengths.	The Board and Nominations Committee recognise the importance and benefits of greater diversity including gender diversity, social and ethnic background and cognitive and personal strengths, throughout the organisation, including on the Board itself. The Company only engages with executive search firms who have signed up to the voluntary Code of Conduct on gender and BAME diversity and best practice.	No Board appointments were made during the year however all recommendations in respect of future Board appointments will be conducted in full consideration of the Policy, 2018 Code, and additional relevant guidance.
Ensure the Board and Nominations Committee only engage executive search firms who have signed up to the voluntary Code of Conduct on gender diversity and best practice.	The Company only engages with executive search firms who have signed up to the voluntary Code of Conduct on gender and BAME diversity and best practice.	We continue only to engage with executive search firms who have signed up to the voluntary Code of Conduct on gender and BAME diversity and best practice.
Ensure focus is given to the development of a pipeline of diverse high calibre candidates for Board level roles.	Regular Board and Nominations Committee consideration of the importance and benefits of greater diversity including gender diversity, social and ethnic background and cognitive and personal strengths, throughout the organisation, including representation of these cohorts in the Group's talent pipeline and on the Board itself.	At its March meeting, the Nominations Committee considered Diversity and Inclusion within the Group. As part of these discussions, the Board committed to building on existing graduate, apprentice and leadership programmes to embed inclusivity in our succession planning and talent development work to strengthen our talent pipeline, with an enhanced focus on ensuring appropriate representation from minority ethnic candidates, as well as other relevant diverse cohorts. This was also an area of specific focus within the Board Succession Planning discussions that took place during the year.

Talent development

We recognise the importance of developing our people and, as such, talent management remains a key topic of discussion. The Company's five year talent plan focuses on building technical and leadership capability, and creating talent pipelines for the future. We have a total of 78 graduates in training, with 43 places offered in 2018. We currently have five entry programmes for graduates – Business Leadership, Finance, IS, Engineering and Project Management. Our placements programme for undergraduates offers a range of summer and 12 month placements across Engineering, Finance and the Visitor

Experience teams, with 23 opportunities filled in 2018 with a new opportunity in the Quantity Surveying team being offered in 2019. We currently have 133 apprentices in training. In 2018, we launched three new Apprenticeship programmes within our HR, Legal and Vehicle Technician populations. We now have 11 active Apprenticeship programmes, and we expect this to increase to 13 in 2019. We have been a key partner in the development and implementation of the new water industry apprenticeships standards through the Government's Trailblazer initiative. As one of the 13 firms making up the employer group, we have ensured that Severn Trent Water has been at the forefront of its development.

Our innovative delivery model for the water process technician standard has allowed us to design a programme that ensures high quality apprenticeship training delivered in just 24 months – significantly faster than any previous schemes. Elsewhere in the industry this course would take at least 36 – 48 months to complete.

Succession planning

Kevin Beeston led the discussion on the process of succession planning for Andrew Duff, who has been on the Board since May 2010 and has been our Chairman since July 2010, therefore reaching the nine year limit for Chairs specified in the 2018 Code.

The Severn Trent Plc Nominations Committee is in the initial stages of succession planning and it is planned to formally announce Andrew's successor in due course. In line with the provisions of our Board Diversity Policy, any executive search firms involved must be signed up to the voluntary code of conduct on gender and BAME diversity and best practice.

The Committee looks forward to appointing a well-qualified and high calibre Chair in due course, and does not believe that it would be in the interests of shareholders for this to take place immediately, for the following reasons:

- It would be beneficial for the new Chair to be able to join the Board and work alongside Andrew Duff for a period before they step up to become Chair;
- A search for a high quality candidate takes time and the Committee does not want to rush this important search; and
- In the Committee's opinion, Andrew Duff remains a very strong and effective Chairman, who is independent of management and provides robust challenge. The findings of the Board effectiveness evaluation support this view.

In the year ahead, the Committee will focus on ensuring a smooth and orderly handover and induction, in conjunction with the Company Secretary. Kevin Beeston will continue to Chair all meetings of the Committee when it meets to discuss this matter.

Director conflicts and independence
In March 2019, the Committee conducted its annual review of individual Director conflict authorisations as recorded in our Conflicts of Interest Register. Additionally, the Board considers conflicts of interest at every meeting and reviews the authorisation of any potential conflicts of interest every six months. The Conflicts of Interest Register sets out any actual or potential conflict of interest situations which a Director has disclosed to the Board in line with their statutory duties.

When reviewing conflict authorisations, the Nominations Committee considers any other appointments held by the Director as well as the findings of the Board effectiveness evaluation. Following the review, the Committee recommended to the Board that each conflict authorisation remained appropriate. There were no new potential conflict situations during the year.

The independence of our Non-Executive Directors is formally reviewed annually by the Nominations Committee, and as part of the Board evaluation exercise. The Nominations Committee and Board consider that there are no business or other circumstances that are likely to affect the independence of any Non-Executive Director and that all Non-Executive Directors continue to demonstrate independence.

Human Rights and Modern Slavery

We are committed to protecting the human rights of our employees and contractors as we have clearly set out in our Code of Conduct, 'Doing the Right Thing'. We have a responsibility to understand our potential impact on human rights and to mitigate or eliminate any potentially negative impacts. Whilst not having a specific human rights policy, we have Company policies on Human Resources, Anti-Bribery and Anti-Fraud, Whistleblowing ('Speak Up') and Procurement.

We will always treat people in our business and supply chain fairly and have a clear zero tolerance approach to modern slavery. To date we have had no instances of modern slavery raised, but we are not at all complacent and are fully committed to protect against modern slavery in our business and supply chain and have robust mechanisms in place to report any concerns. Our understanding is constantly evolving and we are continually adapting and improving our approach accordingly. We know modern slavery is a growing global issue and know our customers and stakeholders share our concern. Our highest risk is through our supply chain. Therefore we work with our suppliers to ensure they operate to the same standards we set ourselves, and we have also been working closely with our suppliers to ensure they understand the risks involved in their own supply chains.

All suppliers are required to sign up and operate in line with our Code of Conduct, which clearly states our zero tolerance, and is built into our procurement tender process as part of the prequalification questionnaire template. We have been working with Hope For Justice for three years to develop our approach. Our full Anti-Slavery and Human Trafficking Statement can be found on the Severn Trent Water Limited website.

Whistleblowing

Our employees, and wider workforce, can raise concerns at work through their line manager, senior management and through our confidential and independent whistleblowing helpline, 'Safecall'. All investigations are carried out independently and the findings are reported directly through to the Severn Trent Plc Audit and Severn Trent Plc Corporate Responsibility Committees.

Prevention and Detection of Bribery and Corruption

Our Severn Trent Group financial crime policy prohibits bribery, corruption and fraud in all our business dealings, regardless of the country or culture within which we work. This year we have also updated our policy to take into account the new tax evasion offences. Employees identified as high risk, through a risk review for all Group employees, are required to undertake an online training module and test to ensure awareness of, and compliance with, anti-bribery and corruption.

Directors' remuneration report

Remuneration details

The Executive Directors of Severn Trent Water Limited mirror those of Severn Trent Plc and, consequently it is not possible to separate the remuneration received solely for their services to Severn Trent Water Limited. Therefore, the Remuneration Report that follows is a summary of the Remuneration Report found in the Severn Trent Plc Annual Report and Accounts which is available on the Severn Trent Plc website.

The Severn Trent Plc Remuneration Committee (the 'Committee') sets the Remuneration Policy for Executive Directors and other senior executive managers, taking into account the Company's strategic objectives over the short and the long term and the external market.

The Committee addresses the need to balance risk and reward. The Committee monitors the variable pay arrangements to take account of risk levels, ensuring an emphasis on long term and sustainable performance. The Committee believes that the incentive schemes are appropriately managed, and that the choice of performance measures and targets does not encourage undue risk taking by the Executives, so that the long term performance of the business is not compromised by the pursuit of short term value. The schemes incorporate a range of internal and external performance metrics, measuring both operational and financial performance over differing and overlapping performance periods, providing a rounded assessment of overall Company performance.

Directors' remuneration and annual bonus scheme
Remuneration for Executive Directors comprises the following elements:

- base salary and benefits;
- annual bonus;
- long term incentive plan; and
- pension arrangements.

As outlined in the Severn Trent Plc Annual Report and Accounts, the non-executive Chairman, Andrew Duff, and non-executive directors, do not participate in the Company's incentive arrangements, i.e. annual bonus or share plans.

Base salaries and benefits
Base salaries for individual Directors are reviewed annually by the Committee and normally take effect from 1 July. Salaries are set with reference to individual performance, experience and contribution, together with developments in the relevant employment market (having regard to similar roles in publicly quoted companies of a comparable size (currently FTSE 51-150) and practice in other water companies), Company performance, affordability, wider economic environment and internal relativities.

In addition to base salary, Executive Directors receive a benefits package which contractually includes car allowance, membership of a defined contribution pension scheme or cash allowance in lieu, family level private medical insurance, life assurance, personal accident insurance, health screening and incapacity benefits scheme. Executive Directors may also take advantage of the Severn Trent flexible benefit scheme open to all employees.

Annual Bonus 2018/19
The annual bonus is designed to encourage improved financial and operational performance, and to align the interests of Directors with shareholders through the partial deferral of payment in shares. The maximum bonus opportunity is 120% of salary, with 60% of base salary being paid at target.

Bonuses are based on customer, financial, operational and personal performance. Half of the bonus is paid in cash and half in shares which vest after three years (with the value of any dividends to be rolled up and paid on vesting).

Malus and clawback mechanisms also apply to allow the recoupment within three years of the payment of the cash bonus or the grant of deferred shares in the event of financial misstatement, error in the calculation or gross misconduct.

Annual bonus performance is measured over a single financial year. An annual bonus was awarded of 70.2% of salary for both the Chief Executive Officer and the Chief Financial Officer. Please note that the bonuses incorporate amounts in respect of the achievement of Severn Trent Business Services targets and personal performance targets. Annual bonus payments to Executive Directors are not pensionable.

The table below shows a summary of the metrics and targets which were used to determine the annual bonus awards, together with the actual performance achieved (please note that the Business Services PBIT element of the bonus has been omitted as it does not relate to the performance of Severn Trent Water):

Measure	***Weighting*** ***% Total award***	**Threshold (0% payable)**	**Target (50% payable)**	**Stretch (100% payable)**	**Actual Performance**	**Outcome % Total award**
RWWW PBIT	*47%*	£515.1m	£528.1m	£541.1m	£527.0m	21.5%
Customer ODIs	*20%*	£40m	£60m	£80m	£91.1m	20%
Customer Experience (i)	*8%*	5%	10%	15%	-14%	0%
Health and safety (ii)	*8%*	0.17	0.13	0.09	0.30	0%
Personal Performance	*7%*	Detailed overleaf				Chief Executive Officer - 7% Chief Financial Officer - 7%

(i) Measured as percentage reduction is written complaints.
(ii) Measured as number of lost time incidents divided by number of hours worked by multiplied by 100,000.

Further comment on our overall performance during the financial year can be found in the CEO's review on page 10 to 12.

Personal objectives for the Executive Directors are linked to our strategic framework which will move us towards our ambition to be the most trusted water company. Objectives were shared across the team with each Executive Director leading on the areas which best align with their accountabilities and expertise.

The achievement of the personal objectives was 7% for both the CEO and the CFO.

The table below sets out performance outcomes for each Executive Director in relation to their specific personal objectives.

CEO

Objective	Activity	Key achievements in 2018/19	Performance outcome
Embed customers at the heart of all we do	Deliver on customer measures through Customer Outcome Delivery Incentives (ODIs)	• Achieved ODI uncapping enabling benefits of outperformance to be shared with customers. • 40% year on year improvements in Supply Interruptions. • Ofwat approved waste uncapping benefitting the remainder of AMP6. • Supported 52,838 vulnerable customers. • Retained UQ for Customer Service Index for 2018/19.	Fully met
Drive operational excellence and continuous innovation	Deliver UQ plans across Waste, Water and Retail	• Significant improvements have been made in waste networks ODIs during AMP6, including 50% reduction in total flooding incidents (internal and external), and year on year reduction in the number of Cat3 pollutions. • Delivery of 2018 Agrivert acquisition. • Significant improvements in leakage year on year including leakage work in progress down by 65% and a 50% improvement in the median number of days to fix a leak. • New customer first programme rolled out to all Contact Centre staff.	Fully met
Invest responsibly for sustainable growth	Improvement in some key senior management level ERM risks	• Taken actions to reduce risk scores across a range of areas through reviewing and embedding control and assurance frameworks, additional infrastructure investment and identification and implementation of remedial plans.	Fully met
Change the market for the better	Produce compelling case for investment for investment at PR19	• PR19 fast-tracked. • Only utility to be named as a Pathfinder by the Purposeful Task Force Company.	Fully met
Create an awesome place to work	Continue improvement overall Quest engagement scores	• Overall QUEST score held flat in spite of exceptional work effort, and unprecedented external factors affecting normal day to day working. We are 5 points above the UK and Ireland benchmark. • Social Mobility Employer Index ranking increased from 38th to 20th.	Fully met

CFO

Objective	Activity	Key achievements in 2018/19	Performance outcome
Embed customers at the heart of all we do	Support Customer outcome delivery incentives	• Identified and made improvements in reporting and analysis, enabling management to have greater insight when making in-year decisions. • Ofwat approved waste uncapping benefitting the remainder of AMP6.	Fully met
Drive operational excellence and continuous innovation	Continue the evolution of regulatory submissions and building financial resilience	• Produced high quality Annual Performance Reports for both Severn Trent Water and Hafren Dyfrdwy. • Embedded robust financial resilience processes e.g. early adoption of Ofwat's proposed stress testing scenarios for PR19.	Fully met
Invest responsibly for sustainable growth	Support effective decision making in Capital Delivery, delivering efficiencies	• Implemented improved capital governance model, enabling more efficient project resource allocation. • Successful creation of £100m "Spend to Save" capital fund targeted at operational efficiencies for AMP7.	Fully met

	and effective resource allocation		
Change the market for the better	Deliver Finance plan for PR19, and an excellent assurance programme for PR19 submission	• Created cost-effective Assurance plan as part of PR19 submission, and achievement of fast-track status has enabled early implementation.	Fully met
Create an awesome place to work	Develop breadth and depth of experience and expertise across whole Finance team	• Launched Finance for the Future model designed to improve effectiveness, embrace innovation and drive efficiency towards AMP7 Totex challenges, supported by an award winning study program for future talent (graduates and apprentices).	Fully met

Summary of the implementation of the Remuneration Policy in 2019/20

Shareholders approved the Remuneration Policy at the AGM in 2018 (99.18% voted in favour). Full details of the Policy can be found on pages 120 to 128 of the 2018 Group Annual Report and Accounts, and a summary is contained in this year's Report and Accounts as well as on the Severn Trent Plc website. The Committee believes that the fundamental architecture of the Executive Directors' remuneration package is appropriate and the policy remains to attract, retain and motivate its leaders and to ensure they are focused on delivering business priorities within a framework designed to promote the long term success of Severn Trent, aligned with shareholder interests.

Base Salary

Annual Bonus 2019/20

As the Company's strategic priorities evolve, the Committee firmly believes that the operation of the bonus must evolve with it, and as a result the Committee has contacted our 30 largest shareholders representing over 50% of our issued share capital, as well as Glass Lewis, The Investment Association and ISS, to inform them of proposed changes to the operation of our annual bonus for 2019/20. Full details are set out on pages 98 to 106 of this year's Severn Trent Plc Annual Report and Accounts.

In summary, whilst the total bonus opportunity will not change, the annual bonus performance measures and weightings for 2019/20 financial year will be as follows:

- Group Profit Before Interest & Tax – 49%
- Resilient Service ODIs – 35%
  - Customer Outcomes (15%)
  - Asset Health (10%); and
  - Environment and Social Outcomes (10%)
- Customer Service – 8%
- Health and Safety (Lost Time Incidents) – 8%

The Committee considers the forward looking performance targets to be commercially sensitive and has, therefore, determined not to disclose them in advance. Details of the targets used will be disclosed in next year's Remuneration Report.

Long Term Incentive Plan

Executive Directors may also participate in the Severn Trent Plc Long Term Incentive Plan ('LTIP') which is designed to encourage strong and sustained improvements in financial performance, in line with the Company's strategy, and long term shareholder returns. Under this plan conditional awards of performance shares are made to Directors up to an annual maximum limit and vest after three years. The value of dividends paid on the shares comprising the award will be rolled up and paid on vesting.

Malus and clawback mechanisms apply to allow the recoupment of incentive awards within three years of vesting in the event of financial misstatement, an error in calculating the level of vesting or gross negligence, fraud or gross misconduct.

2016 LTIP Awards

The 2016 awards are subject to a RoRE performance condition measured over three financial years. Average RoRE performance is compared with the baseline RoRE figure set by Ofwat in our FD. 25% of the award will vest if average RoRE matches the baseline figure, increasing on a straight-line basis to full vesting for outperforming the baseline by 1.39 times. The 2016 LTIP awards were granted on 21 June 2016. The share price used to calculate the number of shares granted was £21.59 (being the average price over the preceding three days).

The RoRE calculation used for LTIPs differs slightly from that used in the annual performance report, which uses the Ofwat definition. The LTIP measure seeks to better align our LTIP targets to actual cash flows and against a clearly defined target (the FD). In this measure financing outperformance is based on actual gearing rather than the notional capital structure and compares our cost of debt against the allowance in the Ofwat Financial Model. It includes profits/losses associated with land sales, miscellaneous activities and the impact of the wholesale revenue forecasting incentive mechanism.

The three year performance period for the 2016 LTIP award ended on 31 March 2019. Our final RoRE of 8.1% times the Final Determination results in a vesting of 100% of the maximum. Further details can be found in the Severn Trent Plc Annual Report and Accounts.

2017, 2018 & 2019 LTIP Awards

Awards granted from 2015 onwards are subject to a Return on Regulated Equity (RoRE) performance condition measured over three financial years. Average RoRE performance is compared with the baseline RoRE figure set by Ofwat in our Final Determination (FD). For the 2017 award threshold performance is equal to the FD, increasing on a straight line basis to target vesting for out-performing the FD by 1.39 times. For the 2018 and 2019 awards an additional stretch target of upper quartile RoRE has been added. A 2-year post vesting holding period will also apply. Further details can be found in the Severn Trent Plc Annual Report and Accounts.

The grant level for the 2019 LTIP award is 200% of base salary for the Chief Executive Officer and 150% of base salary for the Chief Financial Officer.

Shareholding guidelines

The Company operates shareholding guidelines under which Executive Directors are expected to build and maintain a shareholding in the Company. The Chief Executive Officer is expected to build and maintain a holding of shares to the value of 300% of salary, and the Chief Financial Officer 200% of salary. Executive Directors are expected to retain all of the net of tax number of shares they receive through the LTIP and deferred share bonus until the shareholding guidelines have been met.

The Chief Executive Officer and Chief Financial Officer have exceeded the shareholding requirement of 300% and of 200% respectively of base salary.

Directors' report

The Directors present their report and the audited financial statements, for the year ended 31 March 2019. The performance review of the Company can be found within the Strategic report from the inside cover to page 68. This provides detailed information relating to the Company, its business model and strategy, the operation of its businesses, future developments and financial position for the year ended 31 March 2019. The Governance Report set out on pages 69 to 97 is incorporated by reference into this report and, accordingly, should be read as part of this report.

Details of the Company's policy on addressing the principal risks and uncertainties facing the Group are set out in the risk management section on pages 47 to 64.

Principal activity

The principal activity of the Company is to treat and provide water and remove waste water in the UK. There have not been any significant changes to the Company's principal activities in the year under review. The Directors are not aware, at the date of this report, of any likely major changes in the Company's activities in the next year.

Directors and their interests

Biographies of the Directors currently serving on the Board are set out on pages 71 to 73.

All of the Directors at the year-end are also Directors of Severn Trent Plc. As such, they will all be offering themselves for reappointment at the Severn Trent Plc 2019 AGM. The Chairman, Andrew Duff, will be standing for re-election and in order to facilitate an effective succession plan, it is intended that he remains as Chairman until the announcement and induction of his successor.

Details of Directors' service contracts are set out in the Directors' Remuneration Report. The interests of the Directors in the shares of Severn Trent Plc are disclosed in the Annual Report and Accounts for that Company for the year ended 31 March 2019.

The Board has a documented process in place in respect of conflicts which is described on page 91.

Insurance and indemnities

The Company maintains Directors' and Officers' liability insurance in respect of legal action that might be brought against its Directors and Officers. As permitted by the Company's Articles of Association (the 'Articles'), and to the extent permitted by law, the Company indemnifies each of its Directors and other Officers against certain liabilities that may be incurred as a result of their positions within the Group. The indemnity was in force throughout the tenure of each Director during the last financial year, and is currently in force.

Severn Trent Water Limited does not have in place any indemnities for the benefit of the external Auditor.

Employees

The average number of employees within the Company is shown in note 8 to the financial statements.

Severn Trent Water Limited believes a diverse and inclusive workforce is a key factor in being a successful business. Through our Diversity and Equal Opportunities Policy, the Company seeks to ensure that every employee, without exception, is treated equally and fairly and that all employees are aware of their responsibilities. This means more than ensuring we don't discriminate in any way – we want to create and maintain a culture open to a diverse population. Severn Trent believes that no one should be hurt or made unwell by what we do. We did not experience any major safety incidents and no fatalities during the year.

We are an equal opportunities employer and welcome applications from all individuals, including those with a disability. We are fully committed to supporting applications made by disabled persons, and make reasonable adjustments to their environment where possible (having regard to their particular aptitudes and abilities). We are also responsive to the needs of our employees. As such, should any employee become disabled during their time with us, we will actively re-train that employee and make reasonable adjustments to their environment where possible, in order to keep them in employment with us.

All our training, promotion and career development processes are in place for all our employees to access, regardless of their gender, race, age or disability. The provision of occupational health programmes is of crucial importance to Severn Trent with the aim of keeping our employees fit, healthy and well, including an employee assistance programme.

Additional information on our diversity aims and progress can be found on pages 89 and 90.

Employee engagement

We continuously engage with our employees in a number of ways to accommodate different working patterns. This includes:

- all people briefings, ‘Team Talk’;
- corporate communications events and roadshows held by functions across the Company;
- a dedicated intranet, ‘Streamline’;
- online news portal and weekly roundup, ‘Pipeline News’;
- an active employee social media presence, ‘Yammer’;
- conference calls and email;
- leadership engagement channels – Executive Director blogs, senior management monthly visibility programme and quarterly events;
- Employee forum; and
- regular meetings with Unions.

Details of the financial and economic factors affecting the performance of the Company are shared with all employees at the appropriate time using the methods listed above.

We provide opportunities for employees to give their feedback to the Company in a number of ways, from team or shift meetings, our Employee Forum and our annual employee satisfaction survey (‘QUEST’).

Research and development

Innovative use of existing and emerging technologies will continue to be crucial to the successful development of new products and processes for the Group and our products must continue to deliver value for customers.

Expenditure on research and development is set out in note 6 to the financial statements.

Post balance sheet events

Details of post balance sheet events are set out in note 41 to the financial statements.

Contributions for political and charitable purposes

Donations to charitable organisations during the year amounted to £65,936 (2018: £81,947). Donations are given to charities whose projects align closely with our aim to promote the responsible use of water resources and waste water services which provide the opportunity for longer term partnerships. In addition, we provide donations to employee nominated charities through a matched funding scheme and health and safety reward schemes. We are also committed to supporting WaterAid, the UK's only major charity dedicated to improving access to safe water, hygiene and sanitation in the world's poorest countries.

Severn Trent's policy is not to make any donations for political purposes in the UK, or to donate to EU political parties or incur EU political expenditure. Accordingly neither Severn Trent Plc nor its subsidiaries made any political donations or incurred political expenditure in the financial year under review. Under the provisions of the Political Parties Elections and Referendums Act 2000 (the relevant provisions of which are now contained in Part 14 of the Companies Act 2006), shareholder authority is required for political donations to be made or political expenditure to be incurred by the Company or any of its subsidiaries in the EU and disclosure of any such payment must be made in the Annual Report and Accounts. The legislation gives a wide definition of what constitutes political donations and political expenditure including sponsorship, subscriptions, payment of expenses, paid leave for employees fulfilling public duties and support for bodies representing the business community in policy review or reform. The Company has therefore obtained limited authority from shareholders as a precautionary measure to allow the Company to continue supporting the community and such organisations without inadvertently breaching the legislation.

At the 2018 Severn Trent Plc AGM, shareholders gave the Company authority to make political donations or to incur political expenditure in the EU (which would not ordinarily be regarded as political donations) up to an aggregate annual limit of £150,000 for the Company and its subsidiaries. Pursuant to those authorities, during the year ended 31 March 2019 the Group incurred costs of £nil (2018: £nil). Those authorities will expire at the 2019 AGM and, in line with market practice to renew the authorities on an annual basis, the Board has decided to put forward a resolution to this year's AGM to renew the authorities to make donations to political organisations and to incur political expenditure up to a maximum aggregate of £150,000 p.a. As permitted under the Companies Act 2006, this resolution also covers any political donations made or political expenditure incurred by any subsidiaries of the Company.

Supplier payment policy

Individual operating companies within the Group are responsible for establishing appropriate policies with regard to the payment of their suppliers, in accordance with the Prompt Payment Code ('PPC'). The companies agree terms and conditions under which business transactions with suppliers are conducted. It is Group policy that provided a supplier is complying with the relevant terms and conditions, including the prompt and complete submission of all specified documentation, payment will be made in accordance with agreed terms. It is also Group policy to ensure that suppliers know the terms on which payment will take place when business is agreed.

Internal controls

The Board is responsible for the Company's Internal Control systems and for reviewing their effectiveness. The Severn Trent Plc Audit Committee regularly monitors and reviews the effectiveness of the systems of Internal Control, including Risk Management, financial, operational and compliance aspects, in accordance with the requirements of the Code and the Guidance, and these systems have been in place for the year ending 31 March 2019 and up to the date of the Annual Report. This is described in the Severn Trent Plc Audit Committee report on page 89 of the Severn Trent Plc Annual Report.

The Internal Control system can provide only reasonable and not absolute assurance against material misstatement or loss, as it is designed to manage rather than eliminate the risk of failure to achieve business objectives.

Greenhouse gas emissions

We reduce our carbon footprint

The UK is playing a leading part in reducing carbon emissions. We want to play our part in reducing our impact by reducing our carbon emissions. As the majority of our carbon emissions are driven by our use of energy, managing carbon also means managing costs. We therefore aim to reduce carbon emissions and increase our generation of renewable energy.

We are achieving both of these aims, and this year we have seen another reduction in overall carbon emissions. We've seen a consistent reduction since 2002 when we began publicly reporting on our greenhouse gas emissions. We have held the Carbon Trust Standard since 2009 in recognition of this achievement, which means we've now held the accreditation for a decade.

We have recently committed to becoming Net Carbon Zero by 2030. This is even more ambitious than a science-based target and builds on our long track record of making year-on-year reductions in emissions. We will set out our detailed strategy to deliver this goal as part of our forward plans.
The Carbon Trust Standard recognises our consistent emissions reductions and effective carbon management processes and we scored in the top quartile of companies. We continue to report to the Carbon Disclosure Project ('CDP') each year which means our climate change information is publicly accessible. CDP request information about climate change from companies on behalf of investors and score each company on the quality and completeness of their responses.

We plan to continue to reduce our operational emissions by reducing our energy use and increase our renewable energy generation from sludge. Pursuing these measures will continue to reduce our key sources of emissions, reduce our reliance on the electricity grid and bring financial benefits for our customers and investors.

Report on Greenhouse gas emissions

This is the sixth year Severn Trent has been required to report greenhouse gas (GHG) emissions in the Directors' report. Severn Trent is committed to reducing its GHG emissions. For Severn Trent Water, which accounts for 99% of our total group emissions, we have been publicly reporting on our emissions since 2002. In that time we have reduced our emissions by being more energy efficient and generating more renewable energy.

Our GHG emissions are reported in tonnes of carbon dioxide equivalent (tCO_2e), for the period 1 April 2018 to 31 March 2019. Our total net emissions have fallen again this year, due to the reduction in the emissions-intensity of UK grid electricity and reduced process emissions as we move to more advanced digestion of our sewage sludge. Our net emissions have also fallen as we have now secured a proportion of our electricity supply from accredited renewable energy sources. We have reported this market-based benefit separately in the table below.

The GHG data we report is reported internally during the year to the Corporate Responsibility Committee and to the Board. We have subjected our GHG data and processes to external assurance by Jacobs.

Severn Trent Water Direct Operational Greenhouse Gas Emissions (tonnes CO_2e)	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Emissions from combustion of fuel and operation of facilities (Scope 1)	123,940	122,282	126,009	128,584	130,662	129,379
Emissions from electricity purchased for own use (Scope 2)	333,721	357,701	340,484	298,872	264,290	218,726
Total Annual Gross Operational Emissions	457,661	479,983	466,493	427,456	394,951	348,106
Emissions benefit of the renewable energy we export (including biomethane exported for which we hold green gas certificates).	18,638	24,247	24,887	22,790	27,476	20,432
Emissions reduction from purchase of renewable energy (market-based carbon accounting benefit).						34,818
Total Annual Net Operational Emissions	439,023	455,735	441,606	404,666	367,475	292,856

Annual GHG intensity ratio (t CO_2/unit)	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Net Operational GHG emissions of Severn Trent Water per £m turnover	247	258	243	222	217	178

Our approach to reporting is based on the GHG Protocol Corporate Accounting and Reporting Standard and we have included only emissions from the assets which we own and operate and which we can directly influence and reduce, known as the financial control boundary. In accordance with the reporting regulations, we have not reported on emissions we can influence, but which we are not responsible for, referred to as indirect emissions.

For the appointed UK Water businesses Severn Trent and Dee Valley, we have calculated our emissions using the 'Carbon accounting in the UK Water Industry: methodology for estimating operational emissions, Version 13' (released April 2019). This is a peer-reviewed calculation tool developed and used by all the major water companies in the UK. It is updated each year to include the latest available emissions factors.

Our gross emissions total in the table above shows applies the '**location-based'** accounting methodology for grid emissions, which is consistent with previous years. This year, we have also shown the net benefit of our renewable energy procurement via our suppliers, applying the '**market-based'** accounting methodology, which is included in our net emissions total.

External Auditor

Having carried out a review of their effectiveness during the year, described in the Severn Trent Plc Audit Committee report on page 90 of the Severn Trent Plc Annual Report, the Severn Trent Plc Audit Committee has recommended to the Board the reappointment of Deloitte LLP as auditor.

The reappointment and a resolution to that effect will be on the agenda at the Severn Trent Plc AGM. Deloitte LLP indicated their willingness to continue as Auditor. The Severn Trent Plc Audit Committee will also be responsible for determining the audit fee on behalf of the Board.

Severn Trent Relevant audit information

The Directors confirm that:

- so far as each of them is aware, there is no relevant audit information of which the Company's Auditor is unaware; and
- each of them has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's Auditor is aware of that information.

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

Annual Performance Report of Severn Trent Water Limited
The Annual Performance Report for Severn Trent Water Limited is prepared and sent to Ofwat. A copy of this will be available on the website of Severn Trent Water Limited or on request to the Company Secretary. There is no charge for this publication.

By order of the Board
Bronagh Kennedy
Group General Counsel and Company Secretary
20 May 2019

Directors' responsibilities statement

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors are required to prepare the Group financial statements in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the European Union and the Parent Company financial statements in accordance with United Kingdom Generally Accepted Practice (United Kingdom Accounting Standards and applicable law) including FRS101 'Reduced Disclosure Framework'. Under company law the Directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing the parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK 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.

In preparing the Group financial statements, International Accounting Standard 1 requires that Directors:

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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

Responsibility statement

Each of the Directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- the Strategic report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- The Annual Report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

This Responsibility Statement was approved by the Board of Directors on 20 May 2019 and is signed on its behalf by:

Andrew Duff
Chairman

James Bowling
Chief Financial Officer

20 May 2019

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SEVERN TRENT WATER LIMITED

Report on the audit of the financial statements

Opinion

In our opinion:

- **the financial statements of Severn Trent Water Limited (the 'parent company') and its subsidiaries (the 'group') give a true and fair view of the state of the group's and of the parent company's affairs as at 31 March 2019 and of the group's profit for the year then ended;**
- **the group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;**
- **the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 101 "Reduced Disclosure Framework"; and**
- **the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.**

We have audited the financial statements which comprise:

- the consolidated income statement;
- the consolidated statement of comprehensive income;
- the consolidated and parent company balance sheets;
- the consolidated and parent company statements of changes in equity;
- the consolidated cash flow statement; and
- the related notes to the consolidated and company financial statements 1 to 44.

The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards, including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the group and the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Summary of our audit approach

Key audit matters	The key audit matters that we identified in the current year were: • Valuation of the provision for trade receivables in Severn Trent Water Limited; • Valuation of the group's retirement benefit obligation; and • Classification and valuation of capital expenditure in Severn Trent Water Limited.

	Within this report, any new key audit matters are identified with and any key audit matters which are the same as the prior year identified with .
Materiality	The materiality that we used for the group financial statements was £16 million which was determined on the basis of profit before tax, gains/losses on financial instruments and exceptional items.
Scoping	Our audit scoping has resulted in 100% of the group's turnover and over 90% of the group's net operating assets and profit before tax being subject to audit testing
Significant changes in our approach	In the year ended 31 March 2018, we reported the "Accuracy of wholesale revenue for non-household customers in the new water market" as a key audit matter. As the year ended 31 March 2019 represents the second year of the operation of this market, and processes and controls are embedded within the business, we no longer consider this to be a reportable key audit matter.

Conclusions relating to going concern, principal risks and viability statement

Going concern

We have reviewed the directors' statement in note 2a to the financial statements and on page 68 of the Strategic report about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the group's and company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements.

We considered as part of our risk assessment the nature of the group, its business model and related risks including where relevant the impact of Brexit, the requirements of the applicable financial reporting framework and the system of internal control. We evaluated the directors' assessment of the group's ability to continue as a going concern, including challenging the underlying data and key assumptions used to make the assessment, and evaluated the directors' plans for future actions in relation to their going concern assessment.

We state whether we have anything material to add or draw attention to in relation to that statement that would be required by Listing Rule 9.8.6R(3) if the company had a premium listing and report if the statement is materially inconsistent with our knowledge obtained in the audit.

We confirm that we have nothing material to report, add or draw attention to in respect of these matters.

Principal risks and viability statement

Based solely on reading the directors' statements and considering whether they were consistent with the knowledge we obtained in the course of the audit, including the knowledge obtained in the evaluation of the directors' assessment of the group's and the company's ability to continue as a going concern, we are required to state whether we have anything material to add or draw attention to in relation to:

We confirm that we have nothing material to report, add or draw attention to in respect of these matters.

- the disclosures on pages 50 to 63 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation on page 50 that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity; or
- the directors’ explanation on pages 64 to 68 as to how they have assessed the prospects of the group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We also report whether the directors’ statement relating to the prospects of the group that would be required by Listing Rule 9.8.6R(3) if the company had a premium listing is materially inconsistent with our knowledge obtained in the audit.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Valuation of the provision for trade receivables in Severn Trent Water Limited	
Key audit matter description	A portion of household customers do not or cannot pay their bills which results in the need for provisions to be made for non-payment of the customer balance. Management makes estimates regarding the expected future loss rate when calculating the bad debt provision. The bad debt provision as at 31 March 2019 was £115.2 million (31 March 2018: £124.5 million). Changes have been made to the basis of estimation of the bad debt provision for the year ended 31 March 2019 as a result of the adoption of IFRS 9 ‘Financial Instruments’. Provisions are made against Severn Trent Water Limited’s trade receivables based on historical cash collection rates of debt now aged over 7 years, which is considered by management to be representative of the collection risk on the whole population of household debtors. The key audit matter, which is also a potential fraud risk, has been focused on the valuation of the household bad debt provision, specifically cash collection reflected in the model for debt aged greater than 7 years. The bad debt provision is discussed in note 2(o) and 20 to the financial statements.

How the scope of our audit responded to the key audit matter	We have audited and critically reviewed the assumptions used in the calculation of the bad debt provision as follows: • Assessed the design and implementation of key management review controls over the bad debt provision model; • Assessed the allocation of cash collected relating to debt now aged between seven and ten years to ensure that it has not been inappropriately allocated to this ageing bucket to reduce the overall provisioning rate; • Reviewed management's assumptions applied to the bad debt provision and challenged whether they reflect the lifetime expected credit loss applied to the bad debt provision, including a review of cash collection trends, demographic and economic trends; and • Reconciled the debtor ageing for each debt category to source data.
Key observations	We are satisfied that the assumptions applied in assessing the overall bad debt provision are reasonable and we consider changes to the basis of estimation of the bad debt provision to be appropriate.
Valuation of the group's retirement benefit obligation	
Key audit matter description	Valuation of retirement benefit obligations is an area involving significant estimation because the process is complex and requires management (after taking advice from their actuarial advisers) to make a number of assumptions concerning the discount rate, inflation rate, pension increases, and the longevity of current pensioners in order to determine the value of the scheme's liabilities. The key audit matter is focused on the valuation of the pension scheme liabilities and the appropriateness of the actuarial assumptions that are used to calculate it, specifically with reference to the discount rate. The group's retirement benefit obligation as at 31 March 2019 is £444.3 million (31 March 2018: £511.1million) as per note 27 Retired Benefit Schemes. Management has included this as a key source of estimation uncertainty in note 4 to the financial statements.
How the scope of our audit responded to the key audit matter	We have challenged the assumptions applied by performing the following procedures: • Evaluated the design and implementation of management's key control; • With the support of our pension specialists within our audit team, we challenged the assumptions used in the calculation of the pension scheme deficit as detailed in note 27 specifically challenging the discount rate with reference to comparable market and other third party data; and • Assessed whether there had been any changes in the methodology to determine the assumptions since the prior year.

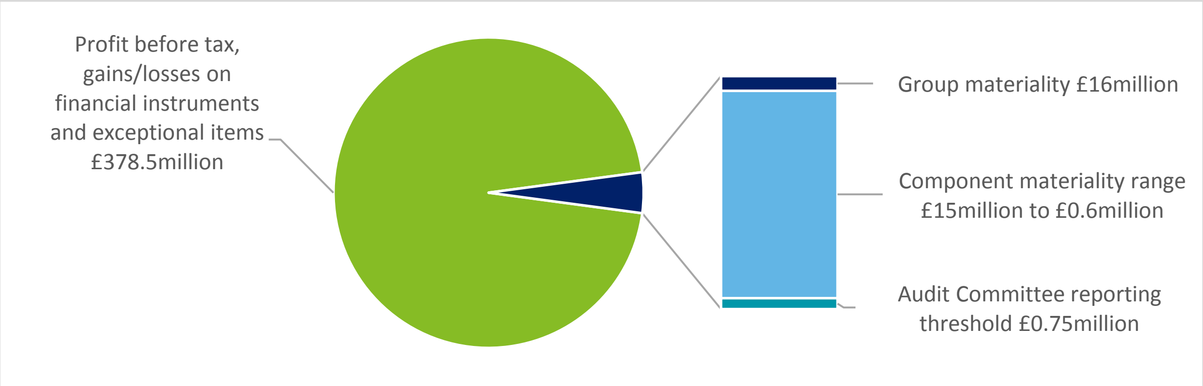
Key observations	We are satisfied that management's assumptions in the valuation of the retirement benefit obligation are appropriate with consistent valuation methodology to previous periods.
Classification and valuation of capital expenditure in Severn Trent Water Limited	
Key audit matter description	Severn Trent Water Limited has a substantial capital programme which has been agreed with the regulator ("Ofwat") and therefore incurs significant expenditure in relation to the development and maintenance of both infrastructure and non-infrastructure assets. Property, plant and equipment ("PPE") additions in the year which were made externally to the Severn Trent Water Limited group were £838.2 million (2018: £663.2 million) of the total additions of £869.1 million (2018: £663.2 million) disclosed in Note 17. As the classification of capital expenditure, operating expenditure and infrastructure renewals expenditure directly affects the group's reported financial performance we identified a key audit matter relating to an overstatement of capital expenditure, whether by changing the Group's capex implementation guidance and/or incorrect application of these guidelines. Due to the level of judgement involved, we have determined that there was a potential for fraud through possible manipulation of this balance. Management has included this as a key source of estimation uncertainty in note 4 to the financial statements.
How the scope of our audit responded to the key audit matter	We performed the following procedures to respond to the key audit matter: • Reviewed Severn Trent Water's capitalisation policy and implementation guidance to understand any changes in the current year and to determine compliance with the relevant accounting standards; • Evaluated the design and implementation and operating effectiveness of controls over the application of the policy to expenditure incurred on projects within the group's capital programme during the year; • Tested whether there have been any changes in the application of the policy; and • For a sample of capital projects, assessed the application of the capitalisation policy to the costs incurred by reviewing the business cases and invoices, and obtaining further explanations and support for significant changes in capital expenditure from budget.
Key observations	We are satisfied that the classification and valuation of assets capitalised in the year is appropriate.

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Parent company financial statements
Materiality	£16 million (2018: £16 million)	£ 15 million (2018: £15 million)
Basis for determining materiality	Approximately 5% (2018: approximately 5%) of profit before tax, exceptional items and fair value movements in derivative financial instruments.	Approximately 5% (2018: approximately 5%) of profit before tax, exceptional items and fair value movements in derivative financial instruments.
Rationale for the benchmark applied	As in 2018, profit before tax, gains/losses on financial instruments and exceptional items has been used in order to focus on the group's underlying trading performance consistent with the group's internal and external reporting.	As in 2018, profit before tax, gains/losses on financial instruments and exceptional items has been used in order to focus on the parent company's underlying trading performance consistent with the parent company's internal and external reporting.



We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £750,000 (2018: £750,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our group audit was scoped by obtaining an understanding of the group and its environment, including group-wide controls, and assessing the risks of material misstatement at the group level.

Based on that assessment, we focused our group audit scope on the consolidation at the parent company level and Severn Trent Water Limited, Severn Trent Utilities Finance plc and Hafren Dyfrdwy Cyfyngedig.

Severn Trent Water Limited, Severn Trent Utilities Finance Plc and Hafren Dyfrdwy Cyfyngedig were subject to full statutory audits using component materiality of £15 million (2018: £15 million), £9 million (2018: £9 million) and £606,000 (2018: £547,000) respectively and together account for 100% of the group's turnover (2018: 100%), and over 90% (2018: 90%) of the group's net assets and profit before tax, gains/losses on financial instruments and exceptional items.

The group audit team performs the audits of Severn Trent Water Limited, Severn Trent Utilities Finance Plc and Hafren Dyfrdwy Cyfyngedig without the involvement of a component audit team.

Parent company and consolidation
At the parent entity level we also tested the consolidation process and carried out analytical procedures to confirm our conclusion that there were no significant risks of material misstatement of the aggregated financial information of the remaining components not subject to audit or audit of specified account balances.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

In this context, matters that we are specifically required to report to you as uncorrected material misstatements of the other information include where we conclude that:

Fair, balanced and understandable – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and

We have nothing to report in respect of these matters.

understandable and provides the information necessary for shareholders to assess the group's position and performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or

Audit committee reporting – the section describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee; or

Directors' statement of compliance with the UK Corporate Governance Code – the parts of the directors' statement that would be required if the company had a premium listing relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code'.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditor's responsibilities for the audit of the financial statements

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

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the group and of the parent company and their environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records

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

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made.

We have nothing to report in respect of this matter.

Use of our report

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

Kate Hadley, FCA (Statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
Birmingham, United Kingdom
20 May 2019

Severn Trent Water Limited
Group and Company income statement
For the year ended 31 March 2019

		Group		Company	
		2019	2018	**2019**	2018
	Note	**£m**	£m (restated, note 2a)	**£m**	£m (restated, note 2a)
Turnover	5	**1,673.1**	1,606.9	**1,643.8**	1,579.0
Operating costs before charge for bad and doubtful debts and exceptional items	6	**(1,080.3)**	(1,043.5)	**(1,050.7)**	(1,022.0)
Charge for bad and doubtful debts		**(25.5)**	(25.7)	**(24.2)**	(25.0)
Exceptional items	7	**(9.6)**	(12.6)	**(9.2)**	(12.6)
Total operating costs	6	**(1,115.4)**	(1,081.8)	**(1,084.1)**	(1,059.6)
Profit before interest, tax and exceptional items		**567.3**	537.7	**568.9**	532.0
Exceptional items	7	**(9.6)**	(12.6)	**(9.2)**	(12.6)
Profit before interest and tax		**557.7**	525.1	**559.7**	519.4
Finance income excluding exceptional items	10	**63.0**	66.5	**85.8**	86.1
Finance costs	11	**(251.8)**	(282.4)	**(275.7)**	(305.1)
Exceptional finance income	7	**–**	**–**	**21.9**	–
Net finance costs		**(188.8)**	(215.9)	**(168.0)**	(219.0)
Net gains on financial instruments	12	**37.7**	11.4	**37.7**	11.4
Profit on ordinary activities before taxation		**406.6**	320.6	**429.4**	311.8
Current tax	13	**(34.2)**	(32.5)	**(40.7)**	(30.4)
Deferred tax	13	**(37.0)**	(27.1)	**(35.8)**	(27.9)
Taxation on profit on ordinary activities		**(71.2)**	(59.6)	**(76.5)**	(58.3)
Profit for the year from continuing operations		**335.4**	261.0	**352.9**	253.5
Loss for the year from discontinued operations	37	**–**	(1.2)	**–**	(1.2)
Profit for the year		**335.4**	259.8	**352.9**	252.3

Severn Trent Water Limited
Group and Company statement of comprehensive income
For the year ended 31 March 2019

	Group		Company	
	2019	2018 (restated)	**2019**	2018 (restated)
	£m	£m	**£m**	£m
Profit for the year	**335.4**	259.8	**352.9**	252.3
Other comprehensive income				
Items that will not be reclassified to the income statement:				
Net actuarial gain	**58.0**	38.9	**57.6**	30.7
Tax on net actuarial gain	**(12.2)**	(9.2)	**(12.2)**	(7.8)
Deferred tax arising on rate change	**–**	–	**–**	–
	45.8	29.7	**45.4**	22.9
Items that may be reclassified to the income statement:				
(Losses)/gains on cash flow hedges	**(8.9)**	4.1	**(8.9)**	4.1
Deferred tax on losses/gains on cash flow hedges	**1.5**	(0.7)	**1.5**	(0.7)
Amounts on cash flow hedges transferred to the income statement	**8.5**	8.5	**8.5**	8.5
Deferred tax on transfer to the income statement	**(1.4)**	(1.4)	**(1.4)**	(1.4)
	(0.3)	10.5	**(0.3)**	10.5
Other comprehensive income for the year	**45.5**	40.2	**45.1**	33.4
Total comprehensive income for the year	**380.9**	300.0	**398.0**	285.7

Severn Trent Water Limited
Group statement of changes in equity
For the year ended 31 March 2019

	Equity attributable to owners of the company					
	Share capital	**Hedging reserve**	**Retained earnings**	**Total**	**Non-controlling interests**	**Total equity**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
At 1 April 2017	1.0	(89.7)	2,329.8	2,241.1	10.6	2,251.7
Profit for the year	–	–	259.8	259.8	–	259.8
Gains on cash flow hedges	–	4.1	–	4.1	–	4.1
Deferred tax on gains on cash flow hedges	–	(0.7)	–	(0.7)	–	(0.7)
Amounts on cash flow hedges transferred to the income statement	–	8.5	–	8.5	–	8.5
Deferred tax on transfer to the income statement	–	(1.4)	–	(1.4)	–	(1.4)
Net actuarial gains	–	–	38.9	38.9	–	38.9
Tax on net actuarial gains	–	–	(9.2)	(9.2)	–	(9.2)
Total comprehensive income for the year	–	10.5	289.5	300.0	–	300.0
Share options and LTIPs						
- value of employees' services	–	–	6.8	6.8	–	6.8
Current tax on share based payments	–	–	0.8	0.8	–	0.8
Deferred tax on share based payments	–	–	(1.3)	(1.3)	–	(1.3)
Dividends paid	–	–	(204.0)	(204.0)	–	(204.0)
At 31 March 2018 restated	1.0	(79.2)	2,421.6	2,343.4	10.6	2,354.0
At 1 April 2018, as previously reported	1.0	(79.2)	2,403.0	2,324.8	10.6	2,335.4
Restatement (see note 2 a)	–	–	18.6	18.6	–	18.6
At 1 April 2018	1.0	(79.2)	2,421.6	2,343.4	10.6	2,354.0
Profit for the year	–	–	335.4	335.4	–	335.4
Losses on cash flow hedges	–	(8.9)	–	(8.9)	–	(8.9)
Deferred tax on losses on cash flow hedges	–	1.5	–	1.5	–	1.5
Amounts on cash flow hedges transferred to the income statement	–	8.5	–	8.5	–	8.5
Deferred tax on transfer to the income statement	–	(1.4)	–	(1.4)	–	(1.4)
Net actuarial gains	–	–	58.0	58.0	–	58.0
Tax on net actuarial gains	–	–	(12.2)	(12.2)	–	(12.2)
Total comprehensive income for the year	–	(0.3)	381.2	380.9	–	380.9
Share options and LTIPs - value of employees' services	–	–	8.0	8.0	–	8.0
Current tax on share based payments	–	–	0.2	0.2	–	0.2
Deferred tax on share based payments	–	–	0.1	0.1	–	0.1
Dividends paid	–	–	(225.1)	(225.1)	–	(225.1)
At 31 March 2019	**1.0**	**(79.5)**	**2,586.0**	**2,507.5**	**10.6**	**2,518.1**

Severn Trent Water Limited
Company statement of changes in equity
For the year ended 31 March 2019

	Equity attributable to owners of the company			
	Share capital	Hedging reserve	Retained earnings	Total
	£m	£m	£m	£m
At 1 April 2017	1.0	(89.7)	2,380.0	2,291.3
Profit for the year	–	–	252.3	252.3
Gains on cash flow hedges	–	4.1	–	4.1
Deferred tax on gains on cash flow hedges	–	(0.7)	–	(0.7)
Amounts on cash flow hedges transferred to the income statement	–	8.5	–	8.5
Deferred tax on transfer to the income statement	–	(1.4)	–	(1.4)
Net actuarial gains	–	–	30.7	30.7
Tax on net actuarial gains	–	–	(7.8)	(7.8)
Total comprehensive income for the year	–	10.5	275.2	285.7
Share options and LTIPs				
- value of employees' services	–	–	6.8	6.8
Current tax on share based payments	–	–	0.8	0.8
Deferred tax on share based payments	–	–	(1.3)	(1.3)
Dividends paid	–	–	(204.0)	(204.0)
At 31 March 2018 restated	1.0	(79.2)	2,457.5	2,379.3
At 1 April 2018, as previously reported	1.0	(79.2)	2,438.9	2,360.7
Restatement (see note 2 a)	–	–	18.6	18.6
At 1 April 2018	1.0	(79.2)	2,457.5	2,379.3
Profit for the year	–	–	352.9	352.9
Losses on cash flow hedges	–	(8.9)	–	(8.9)
Deferred tax on losses on cash flow hedges	–	1.5	–	1.5
Amounts on cash flow hedges transferred to the income statement	–	8.5	–	8.5
Deferred tax on transfer to the income statement	–	(1.4)	–	(1.4)
Net actuarial gains	–	–	57.6	57.6
Tax on net actuarial gains	–	–	(12.2)	(12.2)
Total comprehensive income for the year	–	(0.3)	398.3	398.0
Share options and LTIPs				
- value of employees' services	–	–	7.8	7.8
Current tax on share based payments	–	–	0.2	0.2
Deferred tax on share based payments	–	–	0.1	0.1
Dividends paid	–	–	(225.1)	(225.1)
At 31 March 2019	**1.0**	**(79.5)**	**2,638.8**	**2,560.3**

Severn Trent Water Limited
Group and Company balance sheet
For the year ended 31 March 2019

		Group		Company	
		2019	2018 (restated)	**2019**	2018 (restated)
	Note	**£m**	£m	**£m**	£m
Non-current assets					
Goodwill	15	**63.5**	63.5	**1.3**	1.3
Other intangible assets	16	**89.5**	85.7	**79.7**	81.4
Property, plant and equipment	17	**8,903.3**	8,362.7	**8,682.2**	8,223.8
Investments	18	**1,510.8**	1,488.6	**2,121.6**	1,966.9
Derivative financial instruments	19	**68.4**	36.0	**68.4**	36.0
Trade and other receivables	20	**188.0**	101.9	**334.9**	262.8
Retirement benefit surplus	27	**18.6**	18.2	**–**	–
		10,842.1	10,156.6	**11,288.1**	10,572.2
Current assets					
Inventory		**10.6**	7.6	**10.1**	7.1
Trade and other receivables	20	**472.6**	432.4	**472.8**	422.1
Derivative financial instruments	19	**0.1**	0.2	**0.1**	0.2
Cash and cash equivalents		**12.9**	12.1	**11.4**	9.2
		496.2	452.3	**494.4**	438.6
Current liabilities					
Borrowings	22	**(196.0)**	(304.2)	**(216.4)**	(319.7)
Trade and other payables	25	**(460.8)**	(449.3)	**(458.5)**	(430.3)
Current tax payable		**(11.1)**	(7.9)	**(16.7)**	(4.8)
Provisions for liabilities	28	**(15.3)**	(16.6)	**(15.3)**	(16.6)
		(683.2)	(778.0)	**(706.9)**	(771.4)
Net current liabilities		**(187.0)**	(325.7)	**(212.5)**	(332.8)
Total assets less current liabilities		**10,655.1**	9,830.9	**11,075.6**	10,239.4
Non-current liabilities					
Borrowings	22	**(5,734.8)**	(5,147.7)	**(6,398.3)**	(5,821.0)
Derivative financial instruments	24	**(119.3)**	(108.2)	**(119.3)**	(108.2)
Trade and other payables	25	**(1,075.9)**	(1,008.9)	**(1,063.7)**	(998.7)
Deferred tax	26	**(735.1)**	(676.6)	**(719.6)**	(662.3)
Retirement benefit obligations	27	**(462.9)**	(529.3)	**(205.4)**	(263.7)
Provisions for liabilities	28	**(9.0)**	(6.2)	**(9.0)**	(6.2)
		(8,137.0)	(7,476.9)	**(8,515.3)**	(7,860.1)
Net assets		**2,518.1**	2,354.0	**2,560.3**	2,379.3
Equity					
Called up share capital	29	**1.0**	1.0	**1.0**	1.0
Hedging reserve		**(79.5)**	(79.2)	**(79.5)**	(79.2)
Retained earnings		**2,586.0**	2,421.6	**2,638.8**	2,457.5
Equity attributable to owners of the company		**2,507.5**	2,343.4	**2,560.3**	2,379.3
Non-controlling interests		**10.6**	10.6	**–**	–
Total equity		**2,518.1**	2,354.0	**2,560.3**	2,379.3

Signed on behalf of the Board who approved the accounts on 20 May 2019.

Andrew Duff
Chairman

James Bowling
Chief Financial Officer

Company Number 02366686

Severn Trent Water Limited
Group and Company cash flow statement
For the year ended 31 March 2019

		Group		Company	
	Note	**2019 £m**	2018 £m	**2019 £m**	2018 £m
Cash generated from operations	38	**808.9**	788.0	**820.9**	799.5
Tax paid	38	**(20.9)**	(14.9)	**(19.0)**	(13.0)
Net cash generated from operating activities		**788.0**	773.1	**801.9**	786.5
Cash flows from investing activities					
Purchases of subsidiary, net of cash acquired		**–**	(0.2)	**–**	(0.2)
Purchases of property, plant and equipment		**(771.5)**	(599.9)	**(751.1)**	(582.2)
Purchases of intangible assets and goodwill		**(32.8)**	(25.3)	**(26.6)**	(25.5)
Contributions and grants received		**40.1**	36.7	**38.0**	36.8
Proceeds on disposal of property, plant and equipment		**11.8**	5.7	**5.2**	5.5
Net loans advanced to related parties		**–**	–	**(90.1)**	–
Interest received from intercompany finance leases		**–**	–	**5.7**	5.1
Interest received		**1.8**	5.5	**6.7**	5.1
Net cash from investing activities		**(750.6)**	(577.5)	**(812.2)**	(555.4)
Cash flow from financing activities					
Interest paid		**(159.3)**	(177.8)	**(174.1)**	(197.9)
Interest element of finance lease payments		**(4.4)**	(5.1)	**(5.9)**	(5.3)
Dividends paid to shareholders of the parent		**(225.1)**	(204.0)	**(225.1)**	(204.0)
Repayments of borrowings		**(124.1)**	(552.7)	**(100.0)**	(151.5)
Repayments of obligations under finance leases		**(2.2)**	(1.8)	**(18.9)**	(18.4)
New loans raised		**567.0**	790.0	**322.2**	290.0
New intercompany loans raised		**–**	2.9	**237.0**	106.6
Loans to group undertakings		**(80.9)**	–	**–**	–
Receipts from intercompany finance leases		**–**	–	**–**	0.6
Swap termination payment		**–**	(40.0)	**–**	(40.0)
Interest element of intercompany finance lease payments		**–**	–	**–**	(2.8)
Repayments of obligations under intercompany finance leases		**–**	–	**(13.9)**	(3.1)
Net cash flow from financing activities		**(29.0)**	(188.5)	**21.3**	(225.8)
Net movement in cash and cash equivalents		**8.4**	7.1	**11.0**	5.3
Net cash at the beginning of the year		**3.7**	(3.4)	**0.4**	(4.9)
Net cash and cash equivalents at end of the year		**12.1**	3.7	**11.0**	0.4
Cash and cash equivalents		**12.9**	12.1	**11.4**	9.2
Bank overdrafts		**(0.8)**	(8.4)	–	(8.8)
Net cash and cash equivalents at end of the year		**12.1**	3.7	**11.4**	0.4

1 General information

The Severn Trent Water Group includes Severn Trent Water Limited and its subsidiary companies.

Severn Trent Water Limited is a company incorporated and domiciled in the United Kingdom. The address of its registered office is Severn Trent Centre, 2 St John's Street, Coventry, CV1 2LZ.

2 Accounting policies

a) Basis of preparation

The financial statements have been prepared on the going concern basis (see Strategic' report on page 68) under the historical cost convention as modified by the revaluation of certain financial assets and liabilities (including derivative instruments) at fair value.

i) Group financial statements

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) and IFRIC interpretations issued and effective and ratified by the European Union as at 31 March 2019.

ii) Company financial statements

The Company financial statements have been prepared in accordance with United Kingdom Accounting Standards and comply with the Companies Act 2006. The Company meets the definition of a qualifying entity as defined in FRS 100 'Financial Reporting Standard 100' accordingly the Company has elected to apply FRS 101, 'Reduced Disclosure Framework'.

Therefore the recognition and measurement requirements of EU-adopted IFRS have been applied, with amendments where necessary in order to comply with Companies Act 2006 and The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) as the parent company financial statements are Companies Act 2006 accounts.

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available under that standard in relation to share based payment, financial instruments, capital management, presentation of comparative information in respect of certain assets, standards not yet effective, impairment of assets and related party transactions. Where required, equivalent disclosures are given in the consolidated financial statements and also where required, equivalent disclosures are given in the Group accounts of Severn Trent Plc. The Group accounts of Severn Trent Plc are available to the public and can be obtained as set out in note 44.

The key accounting policies for the Group and the Company, which have been applied consistently, except as noted under (iii) below, in the current and preceding year, are set out below.

(iii) Changes in accounting policies – IFRS 9 and IFRS 15

In the current financial year the Group and the Company have adopted IFRS 9 'Financial Instruments' and IFRS 15 'Revenue from Contracts with Customers'.

IFRS 9 "Financial Instruments" affects the Group's and the Company's measurement and disclosure of financial instruments with effect from 1 April 2018. The classification of its financial assets and liabilities has not changed significantly as a result of the adoption of IFRS 9. The Group and the Company have not retrospectively applied the hedge accounting criteria of IFRS 9 to hedging relationships established under IAS 39 accounting. Existing hedges that qualify for hedge accounting under IAS 39 continue to qualify for hedge accounting under IFRS 9. For new hedges established following adoption of IFRS 9 the Group and the Company will determine on a case-by-case basis whether to apply the hedge accounting provisions of IFRS 9.

Provisions against trade receivables were calculated under the previous accounting policy using historical collection information and losses expected as a result of future events were not recognised. Under IFRS 9 the Group and the Company recognise a provision for the lifetime expected credit losses for trade receivables. The bad debt charge or provision is not materially different as a result.

As a result of IFRS 9 the Group has revalued its investment in Severn Trent Trimpley Limited to which it owns 49%. The Group and the Company have elected to restate comparative information for prior periods upon adoption of IFRS 9 as noted below.

The tables below show the effect of IFRS 9 adoption on the income statement and balance sheet.

Consolidated income statement (extract)
Year ended 31 March 2018

	As previously reported £m	IFRS 9 Impact £m	Restated £m
Profit before interest and tax	525.1	–	525.1
Net gains/(losses) on financial instruments	(7.2)	18.6	11.4
Profit on ordinary activities before taxation	302.0	18.6	320.6
Taxation on profit on ordinary activities	(59.6)	–	(59.6)
Profit for the period	242.4	18.6	261.0

Consolidated balance sheet (extract)
As at 31 March 2018

	As previously reported £m	IFRS 9 impact £m	Restated £m
Investments	1,470.0	18.6	1,488.6
Retained earnings	2,403.0	18.6	2,421.6

Company income statement (extract)
Year ended 31 March 2018

	As previously reported £m	IFRS 9 Impact £m	Restated £m
Profit before interest and tax	519.4	–	519.4
Net gains/(losses) on financial instruments	(7.2)	18.6	11.4
Profit on ordinary activities before taxation	293.2	18.6	311.8
Taxation on profit on ordinary activities	(58.3)	–	(58.3)
Profit for the period	234.9	18.6	253.5

Company balance sheet (extract)
As at 31 March 2018

	As previously reported £m	IFRS 9 impact £m	Restated £m
Investments	1,948.3	18.6	1,966.9
Retained earnings	2,438.9	18.6	2,457.5

The Group and the Company have elected to restate comparative information for prior periods upon adoption of IFRS 15 but as noted below, there are no material changes to amounts previously recognised and so no restatements have been made.

The core principle of IFRS 15 is that an entity should recognise revenue from the transfer of promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled to in exchange for those goods and services.

There was no change to the recognition of revenue from charges for water or waste water services. The policy for recognition of charges for water and waste water services is set out in note 2 c). The performance obligations are satisfied by the provision of water and waste water services and this was also the basis for recognising revenue under the previous accounting standard.

There was no change to the recognition of contributions from developers. The policy for recognition of contributions from developers is set out in note 2 j). The performance obligations for this income are satisfied through the ongoing supply of water and waste water services to the relevant property and this was also the basis for recognising revenue under the previous accounting standard.

b) Basis of consolidation

The consolidated financial statements include the results of Severn Trent Water Limited and its subsidiaries. Results are included from the date of acquisition or incorporation and excluded from the date of disposal.

Subsidiaries are consolidated where the Group has the power to control a subsidiary.

Non-controlling interests in the net assets of subsidiaries are identified separately from the Group's equity. Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling interests' share of changes in equity since that date.

Transactions between the Company and its subsidiaries have been eliminated on consolidation and are not included within the Group financial statements.

c) Revenue recognition

Revenue includes turnover and interest income.

Turnover represents the fair value of consideration receivable, excluding value added tax, trade discounts and inter-company sales, in the ordinary course of business for goods and services provided.

Turnover is not recognised until the service has been provided to the customer.

Turnover includes an estimate of the amount of mains water and waste water charges unbilled at the year end. The accrual is estimated using a defined methodology based upon a measure of unbilled water consumed by tariff, which is calculated from historical billing information.

Interest income is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable.

2 Accounting policies (continued)

d) Exceptional items

Exceptional items are income or expenditure, which individually or, if of a similar type, in aggregate should, in the opinion of the directors, be disclosed by virtue of their size or nature if the financial statements are to give a true and fair view.

e) Taxation

Current tax payable is based on taxable profit for the year and is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred taxation is provided in full on taxable temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred taxation is measured on a non-discounted basis using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Current and deferred tax are recognised in profit or loss, except where they relate that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are recognised in other comprehensive income or directly in equity, respectively. Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for a business combination.

A deferred tax asset is only recognised to the extent it is probable that sufficient taxable profits will be available in the future to utilise it.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities.

f) Goodwill

Goodwill represents the excess of the fair value of purchase consideration over the fair value of the net assets acquired. Goodwill arising on acquisition of subsidiaries is included in intangible assets. If an acquisition gives rise to negative goodwill this is credited directly to the income statement. Fair value adjustments based on provisional estimates are amended within one year of the acquisition, if required, with a corresponding adjustment to goodwill.

Goodwill is tested for impairment in accordance with the policy set out in note 2 k) below and carried at cost less accumulated impairment losses. Goodwill is allocated to the cash-generating unit that derives benefit from the goodwill for impairment testing purposes.

Where goodwill forms part of a cash-generating unit and all or part of that unit is disposed of, the associated goodwill is included in the carrying amount of that operation when determining the gain or loss on disposal of the operation.

g) Other intangible and non-current assets

Intangible assets acquired separately are capitalised at cost. Following initial recognition, the historical cost model is applied.

Finite life intangible assets are amortised on a straight-line basis over their estimated useful economic lives as follows:

	Years
Software	3 - 10
Other intangible assets	2 - 20

Amortisation charged on intangible assets is taken to the income statement through operating costs.

Finite life intangible assets are reviewed for impairment where indicators of impairment exist (see 2 k) below).

Intangible assets with indefinite useful lives are carried at cost less accumulated impairment losses. Such assets are reviewed for impairment at least annually and where indications of impairment exist.

Development expenditure is capitalised as an intangible asset and written off over its expected useful economic life where the following criteria are met:

- it is technically feasible to create and make the asset available for use or sale;
- there are adequate resources available to complete the development and to use or sell the asset;
- there is the intention and ability to use or sell the asset;
- it is probable that the asset created will generate future economic benefits; and
- the development cost can be measured reliably.

Research expenditure is expensed when it is incurred.

h) Property, plant and equipment

Property, plant and equipment is held at cost (or at deemed cost for infrastructure assets on transition to IFRS/FRS 101) less accumulated depreciation. Expenditure on property, plant and equipment relating to research and development projects is capitalised and depreciated over the expected useful life of those assets.

The costs of like-for-like replacement of infrastructure components are recognised in the income statement as they arise. Expenditure which results in enhancements to the operating capability of the infrastructure networks is capitalised.

Where items of property, plant and equipment are transferred to the Group from customers or developers, the fair value of the asset transferred is recognised in the balance sheet. Fair value is determined based on estimated depreciated replacement cost. Where the transfer is in exchange for connection to the network and there is no further obligation, the corresponding credit is recognised immediately in turnover. Where the transfer is considered to be linked to the provision of ongoing services the corresponding credit is recorded in deferred income and released to operating costs over the expected useful lives of the related assets.

2 Accounting policies (continued)

h) Property, plant and equipment (continued)

Where assets take a substantial period of time to get ready for their intended use, the borrowing costs directly attributable to the acquisition, construction or production of these assets are added to their cost.

Property, plant and equipment is depreciated, using the straight-line method, to its estimated residual value over its estimated useful life, with the exception of freehold land which is not depreciated. Assets in the course of construction are not depreciated until commissioned.

The estimated useful lives are:

	Years
Infrastructure assets	
Impounding reservoirs	250
Raw water aqueducts	250
Mains	80 - 150
Sewers	150 - 200
Other assets	
Buildings	30 - 80
Fixed plant and equipment	20 - 40
Vehicles and mobile plant	2 - 15

i) Leased assets

Leases where the Group or Company obtains assets which transfer substantially all the risks and rewards of ownership to the Group or Company are treated as finance leases. The lower of the fair value of the leased asset or the present value of the minimum lease payments is capitalised as an asset with a corresponding liability representing the obligation to the lessor. Lease payments are treated as consisting of a capital element and a finance charge; the capital element reduces the obligation to the lessor and the finance charge is written off to the income statement at a constant rate over the period of the lease in proportion to the capital amount outstanding. Depreciation is charged over the shorter of the estimated useful life and the lease period.

Leases where substantially all the risks and rewards of ownership remain with the lessor are classified as operating leases. Rental costs arising under operating leases are expensed on a straight line basis over the term of the lease. Leases of land are normally treated as operating leases, unless ownership is transferred to the Group at the end of the lease.

Where the Company transfers substantially all the risks and rewards of ownership of an asset to a lessee (finance lease), the assets are accounted for as if they had been sold, and the net investment in the lease is shown as a receivable due from the lessee. Over the lease term, rentals are apportioned between a reduction in the net investment in the lease and finance lease income, such that finance lease income produces a constant rate of return on the net cash investment in the lease. Finance lease income is included within finance income.

j) Grants and contributions

Grants and contributions received in respect of non-current assets, including certain charges made as a result of new connections to the water and waste water networks, are treated as deferred income and released to operating costs over the useful economic life of those non-current assets.

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

k) Impairment of non-current assets

If the recoverable amount of goodwill, an item of property, plant and equipment or any other non-current asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Recoverable amount is the higher of fair value less costs to sell or estimated value in use at the date the impairment review is undertaken. Fair value less costs to sell represents the amount obtainable from the sale of the asset in an arm's length transaction between knowledgeable and willing third parties, less costs of disposal. Value in use represents the present value of future cash flows expected to be derived from a cash-generating unit, discounted using a pre-tax discount rate that reflects current market assessments of the cost of capital of the cash-generating unit or asset. The discount rate used is based on the Group's cost of capital, adjusted for the risk profiles of individual businesses or the Company's estimated cost of capital. Goodwill is tested for impairment annually. Impairment reviews are also carried out if there is an indication that an impairment may have occurred or, where otherwise required, to ensure that non-current assets are not carried above their estimated recoverable amounts.

Impairments are recognised in the income statement.

l) Investments

Investments in subsidiaries in the Company's financial statements are stated at cost less, where appropriate, provisions for impairment. Investments in subsidiaries are reviewed for impairment in line with note 2 k) when indicators of impairment have been identified.

Other investments are initially recognised and subsequently measured at fair value. Changes in fair value are recognised in profit or loss.

m) Inventory

Inventory and work in progress is stated at the lower of cost and net realisable value. Cost includes labour, materials, transport and attributable overheads.

2 Accounting policies (continued)

n) Loans receivable

Loans receivable are measured at fair value on initial recognition, less issue fee income received. After initial recognition, loans receivable are subsequently measured at amortised cost using the effective interest rate method whereby interest and issue fee income are credited to the income statement and added to the carrying value of loans receivable at a constant rate in proportion to the loan amount outstanding.

o) Trade, receivables and accrued income

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

The Group applies simplified approach permitted by IFRS 9 for estimating expected credit losses on trade receivables. For trade receivables that are assessed not to be impaired individually, expected credit losses are estimated based on the Group's historical experience of trade receivable write-offs.

p) Retirement benefits

(i) Defined benefit schemes

The difference between the value of defined benefit pension scheme assets and defined benefit pension scheme liabilities is recorded on the balance sheet as a retirement benefit asset or obligation.

Defined benefit pension scheme assets are measured at fair value using bid price for assets with quoted prices. For scheme assets with no quoted price, the fair value is derived by using quotations from independent third parties or by using applicable valuation techniques at the end of each reporting period. Defined benefit pension scheme liabilities are measured at the balance sheet date by an independent actuary using the projected unit method and discounted at the current rate of return on high quality corporate bonds of equivalent term and currency to the liability.

Service cost, representing the cost of employee service in the period, is included in operating costs. Net finance cost is calculated by applying the discount rate used for the scheme liabilities to the net obligation.

Changes in the retirement benefit obligation that arise from:

- differences between the return on scheme assets and interest income included in the income statement;
- actuarial gains and losses from experience adjustments; and
- changes in demographic or financial assumptions,

are classified as re-measurements, charged or credited to other comprehensive income and recorded in the statement of comprehensive income in the period in which they arise.

There is no contractual agreement, or stated policy, for charging the net defined benefit cost for the Severn Trent or Dee Valley Water schemes to participating Group companies of the ultimate parent. As the net defined benefit cost for these schemes is recognised by the sponsoring employer, Severn Trent Water Limited, the full net defined benefit cost is disclosed in the Severn Trent Water Group financial statements. For the Company financial statements, contributions made by other Severn Trent Group companies are disclosed within actuarial gains and losses in the statement of comprehensive income.

(ii) Defined contribution scheme

Contributions to defined contribution pension schemes are charged to the income statement in the period in which they fall due.

q) Provisions

Provisions are recognised where:

- there is a present obligation as a result of a past event;
- it is probable that there will be an outflow of economic benefits to settle this obligation; and
- a reliable estimate of this amount can be made.

Self-insurance provisions are recognised for claims notified and for claims incurred but which have not yet been notified, based on advice from the ultimate parent company's independent insurance advisers.

Provisions are discounted to present value using a pre-tax discount rate that reflects the risks specific to the liability where the effect is material.

r) Borrowings

The accounting policy for borrowings that are the hedged item in a fair value hedge is set out in note 2 s).

All other borrowings are initially recognised at fair value less issue costs. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest rate method whereby interest and issue costs are charged to the income statement and added to the carrying value of borrowings at a constant rate in proportion to the capital amount outstanding.

Index-linked debt is adjusted for changes in the relevant inflation index and changes in value are charged to finance costs.

Borrowings denominated in foreign currency are translated to sterling at the spot rate on the balance sheet date. Exchange gains or losses resulting from this are credited or charged to gains/losses on financial instruments.

2 Accounting policies (continued)

s) Derivative financial instruments

Derivative financial instruments are stated at fair value, including accrued interest. Fair value is determined using the methodology described in note 34 a). The accounting policy for changes in fair value depends on whether the derivative is designated as a hedging instrument. The various accounting policies are described below.

Interest receivable or payable in respect of derivative financial instruments is included in finance income or costs.

Derivatives not designated as hedging instruments
Gains or losses arising on remeasurement of derivative financial instruments that are not designated as hedging instruments are recognised in gains/losses on financial instruments in the income statement.

Derivatives designated as hedging instruments
The Group and Company use derivative financial instruments such as cross currency swaps, forward currency contracts and interest rate swaps to hedge risks associated with foreign currency and interest rate fluctuations.

At the inception of each hedge relationship, the Group documents:

- the relationship between the hedging instrument and the hedged item;
- its risk management objectives and strategy for undertaking the hedge transaction; and
- the results of tests to determine whether the hedging instrument is expected to be highly effective in offsetting changes in fair values or cash flows (as appropriate) of the hedged item.

The Group and Company continue to test and document the effectiveness of the hedge on an ongoing basis.

Hedge accounting is discontinued when the hedging instrument expires, is sold, terminated or exercised or no longer qualifies for hedge accounting.

Fair value hedges
Where a loan or borrowing is in a fair value hedging relationship it is remeasured for changes in fair value of the hedged risk at the balance sheet date, with gains or losses being recognised in gains/losses on financial instruments in the income statement. The gain or loss on the corresponding hedging instrument is also taken to gains/losses on financial instruments in the income statement so that the effective portion of the hedge will offset the gain or loss on the hedged item.

If hedge accounting is discontinued, the fair value adjustment arising from the hedged risk on the hedged item is amortised to the income statement over the anticipated remaining life of the hedged item.

Cash flow hedges
The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in equity and the ineffective portion is charged to gains/losses on financial instruments in the income statement. When the gain or loss from the hedged underlying transaction is recognised in the income statement, the gains or losses on the hedging instrument that have previously been recognised in equity are recycled through gains/losses on financial instruments in the income statement.

If hedge accounting is discontinued, any cumulative gain or loss on the hedging instrument previously recognised in equity is held in equity until the forecast transaction occurs, or transferred to gains/losses on financial instruments in the income statement if the forecast transaction is no longer expected to occur. From this point the derivative is accounted for in the same way as derivatives not designated as hedging instruments. If the hedging instrument is terminated, the gains and losses previously recognised in equity are held in equity until either the forecast transaction occurs or the forecast transaction is no longer expected to occur.

Embedded derivatives
Where a contract includes terms that cause some of its cash flows to vary in a similar way to a derivative financial instrument, that part of the contract is considered to be an embedded derivative.

Embedded derivatives are separated from the contract and measured at fair value with gains and losses taken to the income statement if:

- the risks and characteristics of the embedded derivative are not closely related to those of the contract; and
- the contract is not carried at fair value with gains and losses reported in the income statement.

In all other cases embedded derivatives are accounted for in line with the accounting policy for the contract as a whole.

t) Share based payment

The Group operates a number of equity settled share based compensation plans for employees. The fair value of the employee services received in exchange for the grant is recognised as an expense over the vesting period of the grant.

The fair value of employee services is determined by reference to the fair value of the awards granted, calculated using an appropriate pricing model, excluding the impact of any non-market vesting conditions. The number of awards that are expected to vest takes into account non-market vesting conditions including, where appropriate, continuing employment by the Group. The charge is adjusted to reflect shares that do not vest as a result of failing to meet a non-market condition.

The grant of awards of shares of the ultimate parent Company is treated as a capital contribution and credited to reserves. When awards vest, payments made to the ultimate parent Company for the issue of shares are charged against the capital contributions previously received in respect of the same awards. Any payments in excess of capital contributions are treated as distributions.

2 Accounting policies (continued)

u) Cash flow statement

For the purpose of the cash flow statement, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with less than three months maturity from the date of acquisition and include cash and bank balances and investments in liquid funds.

Net cash and cash equivalents include overdrafts repayable on demand.

Interest paid in the cash flow statement includes amounts charged to the income statement and amounts included in the cost of property, plant and equipment.

v) Net debt

Net debt comprises borrowings including remeasurements for changes in fair value of amounts in fair value hedging relationships, cross currency swaps that are used to fix the sterling liability of foreign currency borrowings (whether hedge accounted or not) net cash and cash equivalents and loans to related parties.

w) Foreign exchange

Foreign currency transactions arising during the year are translated into sterling at the rate of exchange ruling on the date of the transaction. All profits and losses on exchange arising during the year are dealt with through the income statement.

3 New accounting policies and future requirements

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions relating to various standards that are in issue but not yet effective.

For the Severn Trent Water Group, at the balance sheet date, the following Standards and Interpretations were in issue but not yet effective.

IFRS 16 “Leases”

IFRS 16 provides a comprehensive model for the identification of lease arrangements and their treatment in the financial statements for both lessors and lessees. IFRS 16 will supersede the current lease guidance including IAS 17 Leases and the related interpretations when it becomes effective for accounting periods beginning on or after 1 January 2019. The date of initial application of IFRS 16 for the Group is 1 April 2019.

In contrast to lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements.

a) Impact of the new definition of a lease

The Group will make use of the practical expedient available on transition to IFRS 16 not to reassess whether a contract is or contains a lease. Accordingly, the definition of a lease in accordance with IAS 17 and IFRIC 4 will continue to apply to those leases entered into or modified before 1 April 2019.

The change in definition of a lease mainly relates to the concept of control. IFRS 16 distinguishes between leases and service contracts on the basis of whether the use of an identified asset is controlled by the customer. Control is considered to exist if the customer has:

- The right to obtain substantially all of the economic benefits from the use of an identified asset; and
- The right to direct the use of that asset.

The Group will apply the definition of a lease and guidance set out in IFRS 16 to all lease contracts entered into or modified on or after 1 April 2019. In preparation for the first-time application of IFRS 16, the Group has carried out an implementation project. The project has shown that the new definition in IFRS 16 will not change significantly the scope of contracts that meet the definition of a lease for the Group.

b) Impact on lessee accounting

1. Operating leases

IFRS 16 will change how the Group accounts for leases previously classified as operating leases under IAS 17 which were off balance sheet.

On initial application of IFRS 16, for all leases (except as noted below) the Group will:

a) Recognise right-of-use assets and lease liabilities in the consolidated balance sheet, initially measured at the present value of the future lease payments;

b) Recognise depreciation of right-of-use assets and interest on lease liabilities in the consolidated income statement; and

c) Separate the total amount of cash paid into a principal portion and an interest portion in the consolidated cash flow statement.

Lease incentives will be recognised as part of the measurement of the right-of-use assets and lease liabilities whereas under IAS 17 they were recognised as a lease liability incentive, amortised as a reduction of rental expenses on a straight-line basis.

Under IFRS 16, right-of-use assets will be tested for impairment in accordance with IAS 36 Impairment of Assets. This will replace the previous requirement to recognise a provision for onerous lease contracts.

For short-term leases (lease term of 12 months or less) and leases of low-value assets, the Group will opt to recognise a lease expense on a straight-line basis as permitted by IFRS 16.

As at 31 March 2019, the Group has non-cancellable operating lease commitments of £9.2 million.

A preliminary assessment indicates that £9.0million of these arrangements relate to leases other than short-term leases and leases of low-value assets, and hence the Group will recognise a right-of-use asset of £16.4 million and a corresponding lease liability of £16.4 million in respect of all these leases. The impact of profit or loss is to decrease operating costs by £1.9 million, to increase depreciation by £1.8 million and to increase interest expense by £0.5 million. There are no lease incentives or provisions of onerous leases recognised under IAS 17 to be derecognised.

The preliminary assessment indicates that £0.2 million of these arrangements relate to short-term leases and leases of low-value assets.

3 New accounting policies and future requirements (continued)

Under IAS 17, all lease payments on operating leases are presented as part of cash flows from operating activities. The impact of the changes under IFRS 16 would be to increase the cash generated by operating activities by £1.9 million and to increase net cash used in financing activities by the same amount.

The main differences between IFRS 16 and IAS 17 with respect to assets formerly held under a finance lease is the measurement of the residual value guarantees provided by the lessee to the lessor. IFRS 16 requires that the Group recognises as part of its lease liabilities only the amount expected to be payable under the residual value guarantee, rather than the maximum amount guaranteed as required by IAS 17.

Based on an analysis of the Group's finance leases as at 31 March 2019 on the basis of the facts and circumstances that exist at that date, Group has assessed that this change will not have a material impact on the amounts recognised in the Group's consolidated financial statements.

c) Impact on lessor accounting

Under IFRS 16, a lessor continues to classify leases as either finance leases or operating leases and account for those two types of leases differently. However, IFRS 16 has increased the disclosures required, in particular regarding how a lessor manages the risks arising from its residual interest in leased assets.

The Group is not a lessor in any finance leases and therefore does not believe there to be any impact with regards to the above.

There are no other standards and interpretations in issue but not yet adopted that the directors anticipate will have a material effect on the reported income or net assets of the Group.

4 Critical accounting judgements and sources of estimation uncertainty

In the process of applying the Group and Company accounting policies, the Group and Company are required to make certain judgments, estimates and assumptions that they believes are reasonable based on the information available. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results may ultimately differ from those estimates.

a) Critical accounting judgments

The Group has adopted all amendments to standards with an effective date relevant to this year end with no material impact on its results, assets or liabilities. All other accounting policies have been applied consistently.

i) Classification of costs between operating expenditure and capital expenditure

Severn Trent Water's business involves significant construction and engineering projects. Assessing the classification of costs incurred on such projects between capital expenditure and operating expenditure requires judgments to be made. The judgments are made based on objective criteria that that Group has developed to facilitate the consistent application of its accounting policies.

b) Sources of estimation uncertainty

i) Depreciation and carrying amounts of property, plant and equipment

Calculating the depreciation charge and hence the carrying value for property, plant and equipment requires estimates to be made of the useful lives of the assets. The estimates are based on engineering data and the Group's experience of similar assets. Details are set out in note 2 h). A five year change in the average remaining useful lives of property, plant and equipment would result in a £35 million change in the depreciation charge.

ii) Retirement benefit obligations

Determining the amount of the Group's retirement benefit obligations and the net costs of providing such benefits requires assumptions to be made concerning long term interest rates, inflation and longevity of current and future pensioners. Changes in these assumptions could significantly impact the amount of the obligations or the cost of providing such benefits. The Group makes assumptions concerning these matters with the assistance of advice from independent qualified actuaries. Details of the assumptions made and associated sensitivities are set out in note 27 to the financial statements.

5 Revenue

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Water and waste water services	**1,650.7**	1,574.6	**1,618.8**	1,546.6
Other services	**22.4**	32.3	**25.0**	32.4
Turnover	**1,673.1**	1,606.9	**1,643.8**	1,579.0
Finance income	**2.0**	4.5	**26.5**	25.8
	1,675.1	1,611.4	**1,670.3**	1,604.8

Income from diversions of £8.4 million (2017/18: £9.5 million), which is reimbursement of costs for diversions, is include within infrastructure maintenance expenditure within operating costs.

6 Net operating costs

Group

	2019			2018		
	Before exceptional costs	**Exceptional costs**	**Total**	Before exceptional costs	Exceptional costs	Total
	£m	**£m**	**£m**	£m	£m	£m
Wages and salaries	**236.7**	**–**	**236.7**	221.7	0.6	222.3
Social security costs	**24.4**	**–**	**24.4**	22.0	–	22.0
Pension costs	**22.7**	**9.6**	**32.3**	20.1	(8.3)	11.8
Share based payment	**8.0**	**–**	**8.0**	6.8	–	6.8
Total employee costs	**291.8**	**9.6**	**301.4**	270.6	(7.7)	262.9
Power	**90.2**	**–**	**90.2**	79.2	–	79.2
Carbon Reduction Commitment	**5.1**	**–**	**5.1**	5.9	–	5.9
Raw materials and consumables	**50.1**	**–**	**50.1**	45.8	–	45.8
Rates	**79.2**	**–**	**79.2**	81.9	–	81.9
Charge for bad and doubtful debts	**25.5**	**–**	**25.5**	25.7	–	25.7
Service charges	**35.2**	**–**	**35.2**	34.3	–	34.3
Depreciation of tangible fixed assets	**309.3**	**–**	**309.3**	304.0	16.8	320.8
Amortisation of intangible fixed assets	**29.0**	**–**	**29.0**	19.8	–	19.8
Hired and contracted services	**196.7**	**–**	**196.7**	184.6	3.5	188.1
Operating lease rentals						
- land and buildings	**0.6**	**–**	**0.6**	(0.3)	–	(0.3)
- other	**0.3**	**–**	**0.3**	0.3	–	0.3
Hire of plant and machinery	**6.2**	**–**	**6.2**	3.8	–	3.8
Research and development expenditure	**–**	**–**	**–**	2.1	–	2.1
Profit on disposal of tangible fixed assets	**(10.6)**	**–**	**(10.6)**	(4.6)	–	(4.6)
Exchange (gains)/losses	**0.1**	**–**	**0.1**	–	–	–
Infrastructure maintenance expenditure	**141.4**	**–**	**141.4**	135.2	–	135.2
Ofwat licence fees	**5.1**	**–**	**5.1**	3.6	–	3.6
Net other operating costs	**31.6**	**–**	**31.6**	36.9	–	36.9
Other operating income	**(2.4)**	**–**	**(2.4)**	(2.1)	–	(2.1)
	1,284.4	**9.6**	**1,294.0**	1,226.7	12.6	1,239.3
Release from deferred credits	**(14.7)**	**–**	**(14.7)**	(14.3)	–	(14.3)
Own work capitalised	**(163.9)**	**–**	**(163.9)**	(143.2)	–	(143.2)
	1,105.8	**9.6**	**1,115.4**	1,069.2	12.6	1,081.8

Further details of exceptional costs are given in note 7.

6 Net operating costs (continued)

Company

	2019			2018		
	Before exceptional costs	**Exceptional costs**	**Total**	Before exceptional costs	Exceptional costs	Total
	£m	**£m**	**£m**	£m	£m	£m
Wages and salaries	**234.3**	**–**	**234.3**	215.6	0.6	216.2
Social security costs	**23.9**	**–**	**23.9**	21.6	–	21.6
Pension costs	**22.3**	**9.2**	**31.5**	19.4	(8.3)	11.1
Share based payment	**7.8**	**–**	**7.8**	6.8	–	6.8
Total employee costs	**288.3**	**9.2**	**297.5**	263.4	(7.7)	255.7
Power	**87.8**	**–**	**87.8**	76.9	–	76.9
Carbon Reduction Commitment	**5.0**	**–**	**5.0**	5.7	–	5.7
Raw materials and consumables	**48.6**	**–**	**48.6**	44.6	–	44.6
Rates	**76.8**	**–**	**76.8**	80.0	–	80.0
Charge for bad and doubtful debts	**24.2**	**–**	**24.2**	25.0	–	25.0
Service charges	**34.3**	**–**	**34.3**	33.5	–	33.5
Depreciation of tangible fixed assets	**303.2**	**–**	**303.2**	297.9	16.8	314.7
Impairment	**0.5**	**–**	**0.5**	–	–	–
Amortisation of intangible fixed assets	**28.3**	**–**	**28.3**	19.8	–	19.8
Hired and contracted services	**191.1**	**–**	**191.1**	182.7	3.5	186.2
Operating lease rentals						
- land and buildings	**0.6**	**–**	**0.6**	(0.3)	–	(0.3)
- other	**0.3**	**–**	**0.3**	0.3	–	0.3
Hire of plant and machinery	**5.9**	**–**	**5.9**	3.6	–	3.6
Research and development expenditure	**–**	**–**	**–**	2.1	–	2.1
Profit on disposal of tangible fixed assets	**(10.6)**	**–**	**(10.6)**	(4.4)	–	(4.4)
Exchange losses	**0.1**	**–**	**0.1**	–	–	–
Infrastructure maintenance expenditure	**137.3**	**–**	**137.3**	134.4	–	134.4
Ofwat licence fees	**5.0**	**–**	**5.0**	3.5	–	3.5
Net other operating costs	**22.6**	**–**	**22.6**	35.7	–	35.7
Other operating income	**(2.0)**	**–**	**(2.0)**	(2.0)	–	(2.0)
	1,247.3	**9.2**	**1,256.5**	1,202.4	12.6	1,215.0
Release from deferred credits	**(14.5)**	**–**	**(14.5)**	(14.1)	–	(14.1)
Own work capitalised	**(157.9)**	**–**	**(157.9)**	(141.3)	–	(141.3)
	1,074.9	**9.2**	**1,084.1**	1,047.0	12.6	1,059.6

Further details of exceptional costs are given in note 7.

During the year the following fees were charged by the auditor:

	Group and Company	
	2019	2018
	£m	£m
Fees payables to the Company's auditor for:		
- the audit of the Company's annual accounts	**0.2**	0.4
Total audit fees	**0.2**	0.4
Fees payables to the Company's auditor and its associates for other services to the Group:		
- audit related assurance services	**0.1**	0.1
- other assurance services	**0.1**	0.1
Total non-audit fees	**0.2**	0.2

7 Exceptional items before tax

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Gain arising on pension exchange arrangement	**–**	8.3	**–**	8.3
GMP equalisation costs	**(9.6)**	–	**(9.2)**	–
Restructuring costs	**–**	(20.9)	**–**	(20.9)
Exceptional finance income	**–**	–	**21.9**	–
	(9.6)	(12.6)	**12.7**	(12.6)

On 25 October 2018, the High Court issued a judgment in the Lloyds Bank case in relation to gender equality in Guaranteed Minimum Pension rights that has an impact on the Group's defined benefit pension liabilities. An exceptional charge of £9.6 million (Company: £9.2 million) was incurred for the provision following this judgment.

The total Group net exceptional charge for the year was £9.6 million (2017/18: £12.6 million).

In the prior year, in preparing the Bioresources business for AMP7, we developed our business model and identified the actions that we needed to take to compete effectively in the new market and as a result incurred exceptional restructuring costs of £20.9 million as follows:

- Set up and restructuring costs of £2.1 million,
- Write-off of assets that will not be used in the new business £16.8 million
- Provision for costs to decommission these assets £2.0 million

Also in the prior year an exceptional gain of £8.3 million arose from the net benefit, after implementation costs, of a Pension Increase Exchange arrangement under which members of the defined benefit schemes will be offered the opportunity at retirement to exchange future non-statutory inflationary increases in a portion of their pensions earned prior to 1997 for a higher pension payment now.

The exceptional finance income in Severn Trent Water Limited of £21.9 million arose from a premium on a debt for equity exchange between Hafren Dyfrdwy Cyfyngedig and Severn Trent Water Limited. Hafren Dyfrdwy Cyfyngedig issued 132,810,685 ordinary shares of £1 each in consideration for cancellation of £110.9 million of debt. The premium on redemption of £21.9 million has been recognised as exceptional finance income in Severn Trent Water Limited.

8 Employee numbers

Average number of employees (including executive directors) during the year:

	Group		Company	
	2019	2018	**2019**	2018
	Number	Number	**Number**	Number
	6,305	5,996	**6,172**	5,859

9 Directors' interests and remuneration – Group and Company

a) Directors' interests

All of the Directors as at the end of the year are also directors of Severn Trent Plc, the ultimate parent undertaking, and their interests in the share capital of that company are disclosed in the Severn Trent Plc Annual Report and Accounts for the year ended 31 March 2019. Share options were granted and exercised in accordance with the Severn Trent Sharesave Scheme as appropriate.

The Executive Directors have further interests in Severn Trent Plc ordinary shares of $97^{17}/_{19}$ p each by virtue of having received contingent awards of shares under the Severn Trent Long Term Incentive Plan (LTIP), deferred shares under the Severn Trent Annual Bonus Scheme.

The individual interests, which represent the maximum aggregate number of shares to which each individual could become entitled, are disclosed in the Annual Report and Accounts of Severn Trent Plc for the year ended 31 March 2019.

b) Directors' remuneration

The following table shows the remuneration due to directors for their services to the company during the year:

	2019	2018
	£m	£m
Short term employee benefits	**2.9**	3.3
Post-employment benefits	**–**	–
Share based payment	**1.4**	1.7
	4.3	5.0

The emoluments of the Non-Executive Directors are paid by Severn Trent Plc.

There were no retirement benefits accruing to directors (2018: none) under a defined benefit scheme and one director (2018: one director) under a defined contribution scheme.

Three directors (2018: three directors) exercised share options or received LTIP awards which vested during the year.

c) Highest paid director

	2019	2018
	£m	£m
Aggregate emoluments (excluding pension contributions)	**2.4**	2.2

The highest paid director at 31 March 2019 and 31 March 2018 was not a member of the defined benefit pension scheme.

10 Finance income

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Interest income earned on:				
Bank deposits	**0.3**	0.6	**0.1**	0.6
Amounts due from group undertakings	**1.4**	0.1	**6.9**	4.1
Amounts due from group undertakings under finance leases	**–**	–	**5.1**	5.1
Other finance income	**0.3**	3.8	**14.4**	16.0
Total interest receivable	**2.0**	4.5	**26.5**	25.8
Interest income on defined benefit scheme assets	**61.0**	62.0	**59.3**	60.3
	63.0	66.5	**85.8**	86.1

11 Finance costs

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Interest expense charged on:				
Bank loans and overdrafts	**21.8**	19.3	**21.7**	19.3
Other loans	**150.8**	181.0	**30.8**	1.2
Finance leases	**4.4**	4.4	**5.1**	5.3
Amounts payable to group undertakings	**–**	0.4	**133.9**	192.8
Amounts payable to group undertakings on finance	**–**	–	**10.6**	10.7
Total borrowing costs	**177.0**	205.1	**202.1**	229.3
Other finance expenses	**0.2**	0.1	**0.2**	0.1
Interest expense on defined benefit scheme liabilities	**74.6**	77.2	**73.4**	75.7
	251.8	282.4	**275.7**	305.1

Borrowing costs of £31.6 million (2018: £24.6 million) incurred funding eligible capital projects have been capitalised at an interest rate of 3.40% (2018: 3.89%). Tax relief of £5.4 million (2018: £4.7 million) was claimed on these costs which was credited to the income statement, offset by a related deferred tax charge of £4.8 million (2018: £4.2 million).

12 Gains/(losses) on financial instruments

	2019	2018 (restated)
	£m	£m
Gain/(loss) on swaps used as hedging instruments in fair value hedges	**0.3**	(1.1)
Gain arising on debt in fair value hedges	**0.5**	–
Exchange (loss)/gain on other loans	**(8.0)**	12.7
Loss on cash flow hedges transferred from equity	**(8.5)**	(8.5)
Hedge ineffectiveness on cash flow hedges	**1.6**	1.2
Gain/(loss) arising on swaps where hedge accounting is not applied	**28.5**	(12.6)
Amortisation of fair value adjustment on debt	**1.1**	1.1
Gain on revaluation of investment	**22.2**	18.6
	37.7	11.4

The Group's hedge accounting arrangements are described in note 34.

13 Taxation

a) Analysis of tax charge in the year

Group

	2019	2018
	Total £m	Total £m
Current tax at 19% (2018: 19%)		
Current year	**40.2**	37.4
Prior years	**(6.0)**	(4.9)
Total current tax	**34.2**	32.5
Deferred tax		
Origination and reversal of temporary differences:		
Current year	**29.5**	19.5
Prior years	**7.5**	7.6
Total deferred tax	**37.0**	27.1
	71.2	59.6

The Group current tax charge was £34.2 million (2018: £32.5 million) and the deferred tax charge was £37.0 million (2018: £27.1 million).

Company

	2019	2018
	Total £m	Total £m
Current tax at 19% (2018: 19%)		
Current year	**46.5**	36.7
Prior years	**(5.8)**	(6.3)
Total current tax	**40.7**	30.4
Deferred tax		
Origination and reversal of temporary differences:		
Current year	**28.0**	19.3
Prior years	**7.8**	8.6
Total deferred tax	**35.8**	27.9
	76.5	58.3

The Company current tax charge was £40.7 million (2018: £30.4 million) and the deferred tax charge was £35.8 million (2018: £27.9 million).

The Company earns profits primarily in the UK. Therefore the tax rate used for tax on profit on ordinary activities is the main rate for UK corporation tax.

13 Taxation (continued)

b) Factors affecting the tax charge in the year

The Group and Company tax expense for the current year is lower (2018: higher) than the standard rate of corporation tax in the UK of 19% (2018: 19%). The differences are explained below:

Group

	2019 £m	2018 (restated) £m
Profit before taxation	**406.6**	320.6
Tax at standard rate of corporation tax in the UK 19% (2018: 19%)	**77.3**	60.9
Tax effect of depreciation on non-qualifying assets	**0.9**	1.7
Other permanent differences	**(4.9)**	(3.4)
Current year impact of rate change	**(3.6)**	(2.3)
Adjustments in respect of prior years	**1.5**	2.7
Total tax charge	**71.2**	59.6

	2019 £m	2018 (restated) £m
Profit before taxation	**406.6**	320.6
Tax at standard rate of corporation tax in the UK 19% (2018: 19%)	**77.3**	60.9
Tax effect of depreciation on non-qualifying assets	**0.9**	1.7
Other permanent differences	**(4.9)**	(3.4)
Tax effect of accelerated capital allowances	**(28.2)**	(18.3)
Other timing differences	**(4.9)**	(3.5)
Adjustments in respect of prior years	**(6.0)**	(4.9)
Total current tax charge	**34.2**	32.5

Company

	2019 £m	2018 (restated) £m
Profit before taxation	**429.4**	311.8
Tax at standard rate of corporation tax in the UK 19% (2018: 19%)	**81.6**	59.2
Tax effect of depreciation on non-qualifying assets	**0.8**	1.7
Other permanent differences	**(4.5)**	(2.6)
Current year impact of rate change	**(3.4)**	(2.3)
Adjustments in respect of prior years	**2.0**	2.3
Total tax charge	**76.5**	58.3

	2019 £m	2018 (restated) £m
Profit before taxation	**429.4**	311.8
Tax at standard rate of corporation tax in the UK 19% (2018: 19%)	**81.6**	59.2
Tax effect of depreciation on non-qualifying assets	**0.8**	1.7
Other permanent differences	**(4.5)**	(2.6)
Tax effect of accelerated capital allowances	**(26.8)**	(18.2)
Other timing differences	**(4.6)**	(3.4)
Adjustments in respect of prior years	**(5.8)**	(6.3)
Total current tax charge	**40.7**	30.4

13 Taxation (continued)

c) Tax charged/(credited) directly to other comprehensive income or equity

In addition to the amount charged/(credited) to the income statement, the following amounts of tax have been charged/(credited) directly to other comprehensive income or equity:

Group

	2019 £m	2018 £m
Current tax		
Tax on share based payments	**(0.2)**	(0.8)
Tax on pension contributions	**(9.5)**	(9.2)
Total current tax credited to other comprehensive income or equity	**(9.7)**	(10.0)
Deferred tax		
Tax on actuarial gain/loss	**21.7**	18.4
Tax on cash flow hedges	**(1.5)**	0.7
Tax on share based payments	**(0.1)**	1.3
Tax on transfers to the income statement	**1.4**	1.4
Total deferred tax charged to other comprehensive income or equity	**21.5**	21.8

Company

	2019 £m	2018 £m
Current tax		
Tax on share based payments	**(0.2)**	(0.8)
Tax on pension contributions	**(9.5)**	(9.2)
Total current tax credited to other comprehensive income or equity	**(9.7)**	(10.0)
Deferred tax		
Tax on actuarial gain/loss	**21.7**	17.0
Tax on cash flow hedges	**(1.5)**	0.7
Tax on share based payments	**(0.1)**	1.3
Tax on transfers to the income statement	**1.4**	1.4
Total deferred tax charged to other comprehensive income or equity	**21.5**	20.4

14 Dividends – Group and Company

Amounts recognised as distributions to equity holders in the period:

	2019		2018	
	Pence per share	£m	Pence per share	£m
Interim dividend for the year ended 31 March	**22.51**	**225.1**	20.40	204.0

15 Goodwill - Group

	2019	2018
	£m	£m
Cost		
At 1 April	**63.5**	67.3
Additional consideration in respect of acquisition	**–**	0.2
Adjustment to provisional fair values on acquisition (note 38)	**–**	(4.0)
At 31 March	**63.5**	63.5

Goodwill impairment tests

Goodwill is allocated to the Group's cash-generating units (CGUs) identified according to country of operation and business segment.

A summary of the goodwill allocation by CGU is presented below.

	2019	2018
	£m	£m
Regulated Water and Waste Water	**63.5**	63.5
	63.5	63.5

Regulated Water and Waste Water also has an intangible asset with indefinite useful life amounting to £4.3 million (2018: £4.3 million).

On 1 July 2018 Instruments of appointments of Severn Trent Water Limited and Hafren Dyfrdwy Cyfyngedig (formerly Dee Valley Water Limited) were amended to align the areas for which the appointments were made with the national border of England and Wales. As a result, the business that the goodwill relates to is now partly in Severn Trent Water and partly Hafren Dyfrdwy consequently this goodwill is now allocated to the Regulated Water and Waste Water cash-generating unit.

The Group has reviewed the carrying value of goodwill for impairment in accordance with the policy stated in note 2. The carrying value of the Regulated Water and Waste Water CGU was determined on the basis of fair value, through a level 3 valuation, in the current year. The assessment of the valuation technique was reassessed in the year to align the valuation to reflect the capital intensive nature of the business and in line with IAS 36 to ensure that the valuation is the higher of value in use or fair value less costs to sell.

The fair value determined using a discounted cash flow calculation for the Regulated Water and Waste Water segment is based on the most recent financial projections available for the business, which cover the remainder of the current AMP period to 2020 and the following AMP period, which runs to 31 March 2025. As a regulated water company, the revenues and costs within the Regulated Water and Waste Water segment are significantly influenced by the regulatory settlement for each AMP period so management considers it appropriate for the detailed projections to be coterminous with the AMP period.

The key assumptions underlying these projections are:

Key assumption	**%**
Discount rate	6.5
RPI inflation	3.0
CPI inflation	2.0
Growth rate in the period beyond the detailed projections	1.5

The discount rate was an estimate for the weighted average cost of capital at the year-end date based on the nominal pre-tax WACC detailed in the OFWAT PR19 methodology adjusted to reflect the actual gearing of the Regulated Water and Waste Water operating segment. The rate disclosed above is the equivalent pre-tax nominal rate.

Inflation has been included in the detailed projections at 3% and 2% for RPI and CPI respectively based on the Bank of England's target rate for CPI.

15 Goodwill – Group (continued)

Cash flows beyond the end of the six year period are extrapolated using an assumed real growth rate of 1.5% in the group's regulatory capital base.

The fair value less costs to sell for the CGU exceeded its carrying value by £4,248 million. An increase in the discount rate to 7.6% or a reduction in the growth rate in the period beyond the detailed projections to 0.7% would reduce the recoverable amount to the carrying amount of the goodwill.

16 Other intangible assets – Group and Company

Group

	Computer software		Capitalised development costs and patents	Instrument of appointment	Total
	Internally generated	Purchased			
	£m	£m	£m	£m	£m
Cost					
At 1 April 2017	199.4	106.0	12.0	–	317.4
Additions	7.6	17.9	–	–	25.5
Adjustment to provisional fair values	–	–	–	4.3	4.3
At 1 April 2018	207.0	123.9	12.0	4.3	347.2
Additions	21.5	11.3	–	–	32.8
At 31 March 2019	**228.5**	**135.2**	**12.0**	**4.3**	**380.0**
Amortisation					
At 1 April 2017	(163.5)	(66.3)	(11.9)	–	(241.7)
Amortisation for the year	(7.5)	(12.2)	(0.1)	–	(19.8)
At 1 April 2018	(171.0)	(78.5)	(12.0)	–	(261.5)
Amortisation for the year	(13.7)	(15.3)	–	–	(29.0)
At 31 March 2019	**(184.7)**	**(93.8)**	**(12.0)**	**–**	**(290.5)**
Net book value					
At 31 March 2019	**43.8**	**41.4**	**–**	**4.3**	**89.5**
At 31 March 2018	36.0	45.4	–	4.3	85.7

16 Other intangible assets – Group and Company (continued)

Company

	Computer software		Capitalised development costs and patents	Total
	Internally generated	Purchased		
	£m	£m	£m	£m
Cost				
At 1 April 2017	199.4	106.0	12.0	317.4
Additions	7.6	17.9	–	25.5
At 1 April 2018	207.0	123.9	12.0	342.9
Additions	15.3	11.3	–	26.6
At 31 March 2019	**222.3**	**135.2**	**12.0**	**369.5**
Amortisation				
At 1 April 2017	(163.5)	(66.3)	(11.9)	(241.7)
Amortisation for the year	(7.5)	(12.2)	(0.1)	(19.8)
At 1 April 2018	(171.0)	(78.5)	(12.0)	(261.5)
Amortisation for the year	(13.0)	(15.3)	–	(28.3)
At 31 March 2019	**(184.0)**	**(93.8)**	**(12.0)**	**(289.8)**
Net book value				
At 31 March 2019	**38.3**	**41.4**	**–**	**79.7**
At 31 March 2018	36.0	45.4	–	81.4

Severn Trent Water Limited
Notes to the Group and Company financial statements (continued)
For the year ended 31 March 2019
17 Property, plant and equipment
Group

	Land and buildings £m	Infrastructure assets £m	Fixed plant and equipment £m	Moveable plant £m	Assets under construction £m	Total £m
Cost						
At 1 April 2017	3,293.4	5,114.2	4,023.0	53.6	591.0	13,075.2
Additions	8.9	60.4	16.3	–	594.9	680.5
Transfers on commissioning	67.8	52.2	137.4	4.4	(261.8)	–
Disposals	(2.0)	(0.3)	(12.0)	(2.7)	–	(17.0)
Reclassifications	1.4	6.5	(8.1)	–	0.2	–
Adjustments to provisional fair values	–	0.8	–	–	–	0.8
At 1 April 2018	3,369.5	5,233.8	4,156.6	55.3	924.3	13,739.5
Additions	78.4	146.8	110.0	11.5	504.4	851.1
Transfers on commissioning	37.3	26.5	101.3	2.8	(167.9)	–
Disposals	(0.8)	(0.1)	(1.6)	(4.0)	(0.9)	(7.4)
At 31 March 2019	**3,484.4**	**5,407.0**	**4,366.3**	**65.6**	**1,259.9**	**14,583.2**
Depreciation						
At 1 April 2017	(1,191.7)	(1,300.2)	(2,544.5)	(35.2)	–	(5,071.6)
Charge for the year	(84.1)	(31.5)	(184.2)	(4.2)	–	(304.0)
Disposals	1.7	–	11.3	2.6	–	15.6
Exceptional depreciation	(10.1)	–	(6.7)	–	–	(16.8)
At 1 April 2018	(1,284.2)	(1,331.7)	(2,724.1)	(36.8)	–	(5,376.8)
Charge for the year	(84.0)	(36.9)	(183.9)	(4.5)	–	(309.3)
Disposals	0.7	–	1.6	3.9	–	6.2
At 31 March 2019	**(1,367.5)**	**(1,368.6)**	**(2,906.4)**	**(37.4)**	**–**	**(5,679.9)**
Net book value						
At 31 March 2019	**2,116.9**	**4,038.4**	**1,459.9**	**28.2**	**1,259.9**	**8,903.3**
At 31 March 2018	2,085.3	3,902.1	1,432.5	18.5	924.3	8,362.7

The exceptional depreciation of £nil (2018: £16.8 million) charge arises as a result of Group restructuring in preparing our Bioresources business for AMP7. Information about this is available in note 7.

17 Property, plant and equipment (continued)

Company

	Land and buildings £m	Infrastructure assets £m	Fixed plant and equipment £m	Moveable plant £m	Assets under construction £m	Total £m
Cost						
At 1 April 2017	3,292.6	5,052.5	3,958.4	53.6	591.0	12,948.1
Additions	8.9	60.4	16.3	–	577.6	663.2
Transfers on commissioning	67.8	52.2	137.4	4.4	(261.8)	–
Disposals	(2.0)	(0.3)	(11.7)	(2.7)	–	(16.7)
At 1 April 2018	3,367.3	5,164.8	4,100.4	55.3	906.8	13,594.6
Additions	78.8	158.0	123.1	11.5	497.7	869.1
Transfers on commissioning	37.3	26.5	101.3	2.8	(167.9)	–
Disposals	(28.3)	(68.0)	(33.2)	(4.0)	(12.5)	(146.0)
At 31 March 2019	**3,455.1**	**5,281.3**	**4,291.6**	**65.6**	**1,224.1**	**14,317.7**
Depreciation						
At 1 April 2017	(1,191.7)	(1,300.4)	(2,544.4)	(35.2)	–	(5,071.7)
Charge for the year	(84.0)	(30.9)	(178.8)	(4.2)	–	(297.9)
Disposals	1.7	–	11.3	2.6	–	15.6
Exceptional depreciation	(10.1)	–	(6.7)	–	–	(16.8)
At 1 April 2018	(1,284.1)	(1,331.3)	(2,718.6)	(36.8)	–	(5,370.8)
Charge for the year	(83.4)	(35.7)	(179.6)	(4.5)	–	(303.2)
Disposals	8.5	7.6	18.5	3.9	–	38.5
At 31 March 2019	**(1,359.0)**	**(1,359.4)**	**(2,879.7)**	**(37.4)**	**–**	**(5,635.5)**
Net book value						
At 31 March 2019	**2,096.1**	**3,921.9**	**1,411.9**	**28.2**	**1,224.1**	**8,682.2**
At 31 March 2018	2,083.2	3,833.5	1,381.8	18.5	906.8	8,223.8

The carrying amount of property, plant and equipment includes the following amounts in respect of assets held under finance leases:

Group

	Infrastructure assets £m	Fixed plant and equipment £m	Total £m
Net book value			
At 31 March 2019	**114.8**	**3.1**	**117.9**
At 31 March 2018	115.8	6.4	122.2

Company

	Land and buildings £m	Infrastructure assets £m	Fixed plant and equipment £m	Total £m
Net book value				
At 31 March 2019	**161.3**	**114.8**	**3.1**	**279.2**
At 31 March 2018	166.2	115.8	6.4	288.4

17 Property, plant and equipment (continued)

The net book value of land and buildings is analysed as follows:

Group

	2019 £m	2018 £m
Freehold	**2,116.6**	2,085.0
Short leasehold	**0.3**	0.3
	2,116.9	2,085.3

Company

	2019 £m	2018 £m
Freehold	**2,095.8**	2,082.9
Short leasehold	**0.3**	0.3
	2,096.1	2,083.2

18 Investments

	Group	Company		
	Other investments £m	Subsidiaries £m	Other investments £m	Total £m
As at 1 April 2018 (restated)	1,488.6	478.3	1,488.6	1,966.9
Additions	–	133.0	–	133.0
Gain on revaluation	22.2	–	22.2	22.2
Impairment	–	(0.5)	–	(0.5)
As at 31 March 2019	**1,510.8**	**610.8**	**1,510.8**	**2,121.6**

The Company has the following subsidiary undertakings:

Subsidiary undertaking	Country of operation and incorporation	Principal activity	Percentage and class of share capital held
Aqua Deva Limited	England and Wales	Dormant company	100% ordinary
Chester Water Limited	England and Wales	Holding company	100% ordinary
Dee Valley Group Limited	England and Wales	Holding company	100% ordinary
Dee Valley Limited	England and Wales	Holding company	100% ordinary
Dee Valley Services Limited	England and Wales	Dormant company	100% ordinary
Dee Valley Water (Holdings) Limited	England and Wales	Holding company	100% ordinary
East Worcester Water Limited	England and Wales	Finance company	100% ordinary and 100% non-voting
Hafren Dyfrdwy Cyfyngedig	England and Wales	Regulated water and waste water company	100% ordinary
Energy Supplies UK Limited	England and Wales	Dormant company	100% ordinary
North Wales Gas Limited	England and Wales	Dormant company	100% ordinary
Northern Gas Supplies Limited	England and Wales	Dormant company	100% ordinary
Severn Trent Funding Limited	England and Wales	Dormant company	100% ordinary
Severn Trent General Partnership Limited	Scotland	Finance company	100% ordinary
Severn Trent LCP Limited	England and Wales	Leasing company	100% ordinary
Severn Trent Leasing Limited	England and Wales	Leasing company	100% ordinary
Severn Trent Reservoirs Limited	England and Wales	Finance company	100% ordinary
Severn Trent Utilities Finance Plc	England and Wales	Finance company	100% ordinary
Wrexham Water Limited	England and Wales	Dormant company	100% ordinary

18 Investments (continued)

The Company has the following investment:

Associated undertaking	Country of operation and incorporation	Principal activity	Percentage and class of share capital held
Severn Trent Trimpley Limited	England and Wales	Non-trading company	49% ordinary

The Company also has an indirect investment in Severn Trent Limited Partnership and Severn Trent Limited Partnership 2, limited partnerships registered in Scotland, as a result of Severn Trent General Partnership Limited being the general partner in each partnership.

In the opinion of the Directors the fair values of the Company’s investments are not less than the amount at which they are stated in the balance sheet.

Unless stated below, the registered office of the aforementioned entities is Severn Trent Centre, 2 St John's Street, Coventry, CV1 2LZ, United Kingdom.
The registered office of the following entities is Packsaddle, Wrexham Road, Rhostyllen, Wrexham, LL14 4EH:

Dee Valley Limited
Hafren Dyfrdwy Cyfyngedig

The registered office of Severn Trent General Partnership Limited is 50 Lothian Road, Festival Square, Edinburgh, EH3 9WJ.

Severn Trent Water Limited
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19 Categories of financial assets - Group

	Note	2019 £m	2018 (restated) £m
Fair value through profit and loss			
Cross currency swaps - not hedge accounted		**18.0**	5.8
Interest rate swaps - not hedge accounted		**26.1**	11.4
Investments		**1,510.8**	1,488.6
		1,554.9	1,505.8
Derivatives designated as hedging instruments			
Cross currency swaps - fair value hedges		**19.1**	18.7
Energy hedges - cash flow hedges		**5.3**	0.3
		24.4	19.0
Total financial assets at fair value		**1,579.3**	1,524.8
Financial assets at amortised cost			
Trade receivables	20	**208.5**	183.9
Accrued income	20	**212.9**	201.9
Other amounts receivable	20	**31.2**	26.3
Amounts due from parent company	20	**80.6**	–
Amounts due from group undertakings	20	**11.1**	8.4
Amounts due from related parties	20	**100.0**	99.8
Cash at bank and in hand		**12.9**	12.1
Total financial assets at amortised cost		**657.2**	532.4
Total financial assets		**2,236.5**	2,057.2
Disclosed in the balance sheet as:			
Non-current assets			
Derivative financial assets		**68.4**	36.0
Trade and other receivables		**184.9**	99.8
Investments		**1,510.8**	1,488.6
		1,764.1	1,624.4
Current assets			
Derivative financial assets		**0.1**	0.2
Trade and other receivables		**459.4**	420.5
Cash and cash equivalents		**12.9**	12.1
		472.4	432.8
		2,236.5	2,057.2

20 Trade and other receivables

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Current assets				
Net trade receivables	**208.5**	183.9	**200.9**	174.4
Other amounts receivable	**31.2**	26.3	**30.4**	26.6
Prepayments	**13.2**	11.9	**12.9**	11.9
Net accrued income	**212.9**	201.9	**208.7**	198.4
Receivables due from group undertakings	**6.8**	8.4	**19.3**	10.2
Receivables due from group undertakings under finance leases	**–**	–	**0.6**	0.6
	472.6	432.4	**472.8**	422.1
Non-current assets				
Prepayments	**3.1**	2.1	**3.0**	2.1
Loan receivable	**100.0**	99.8	**100.0**	99.8
Receivables due from group undertakings	**4.3**	–	**4.3**	–
Receivables due from group undertakings under finance leases	**–**	–	**97.9**	98.5
Receivables due from parent company under loan agreements	**80.6**	–	**80.6**	–
Receivables due from group undertakings under loan agreements	–	–	**49.1**	62.4
	188.0	101.9	**334.9**	262.8
	660.6	534.3	**807.7**	684.9

The carrying values of trade and other receivables are reasonable approximations of their fair values.

Doubtful debt provision

Movements on the doubtful debts provision were as follows:

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
At 1 April	**128.2**	128.3	**124.5**	125.4
Charge for bad and doubtful debts	**25.5**	25.7	**24.2**	25.0
Amounts written off during the year	**(34.3)**	(25.8)	**(33.5)**	(25.9)
At 31 March	**119.4**	128.2	**115.2**	124.5

The aged analysis of receivables that are specifically provided for is as follows:

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Up to 90 days	**–**	0.5	**–**	0.5
91 - 365 days	**–**	0.8	**–**	0.8
1 - 2 years	**–**	4.9	**–**	4.9
2 - 3 years	**–**	2.5	**–**	2.5
More than 3 years	**12.3**	5.6	**11.6**	5.6
	12.3	14.3	**11.6**	14.3

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

Severn Trent Water Limited
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20 Trade and other receivables (continued)

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

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Up to 90 days	**57.0**	41.8	**54.2**	41.0
91 - 365 days	**85.2**	79.2	**81.0**	73.5
1 - 2 years	**57.9**	57.5	**54.5**	54.4
2 - 3 years	**38.7**	40.7	**38.0**	38.9
More than 3 years	**74.9**	77.4	**74.9**	75.6
	313.7	296.6	**302.6**	283.4

The amounts above are reconciled to the gross and net debtors in the table below:

Group:

	2019			2018		
	Gross	**Provision**	**Net**	Gross	Provision	Net
	£m	**£m**	**£m**	£m	£m	£m
Accrued income – not due	**214.8**	**(1.9)**	**212.9**	203.1	(1.2)	201.9
Trade receivables						
Not due	**–**	**–**	**–**	–	–	–
Overdue not specifically provided	**313.7**	**(105.2)**	**208.5**	296.6	(112.7)	183.9
Overdue and specifically provided	**12.3**	**(12.3)**	**–**	14.3	(14.3)	–
	540.8	**(119.4)**	**421.4**	514.0	(128.2)	385.8

Company:

	2019			2018		
	Gross	**Provision**	**Net**	Gross	Provision	Net
	£m	**£m**	**£m**	£m	£m	£m
Accrued income – not due	**210.6**	**(1.9)**	**208.7**	199.6	(1.2)	198.4
Trade Receivables						
Not due	**–**	**–**	**–**	–	–	–
Overdue not specifically provided	**302.6**	**(101.7)**	**200.9**	283.4	(109.0)	174.4
Overdue and specifically provided	**11.6**	**(11.6)**	**–**	14.3	(14.3)	–
	524.8	**(115.2)**	**409.6**	497.3	(124.5)	372.8

Credit risk

Trade receivables

Credit control policies and procedures are determined at the individual business unit level. By far the most significant business unit of the Group is Severn Trent Water Limited, which represents 98% of Group turnover and 96% of net trade receivables. Severn Trent Water and Hafren Dyfrdwy have statutory obligations to provide water and waste water services to domestic customers within its region. Therefore there is no concentration of credit risk with respect to its trade receivables from these services and the credit quality of its customer base reflects the wealth and prosperity of all of the domestic households within its region.

The expected credit loss rate is 1.9%.

21 Finance lease receivables – Company

Minimum lease payments receivable are as follows:

	2019 £m	2018 £m
Within 1 year	**5.7**	5.7
1 – 2 years	**5.7**	5.7
2 – 5 years	**17.0**	17.0
After more than 5 years	**221.5**	227.2
Gross obligations under finance leases	**249.9**	255.6
Less: unearned interest receivable	**(151.4)**	(156.5)
	98.5	99.1

The present value of minimum lease payments receivable are as follows:

	2019 £m	2018 £m
Within 1 year	**0.6**	0.6
1 – 2 years	**0.7**	0.6
2 – 5 years	**2.2**	2.1
After more than 5 years	**95.0**	95.8
Included in non-current liabilities	**97.9**	98.5
	98.5	99.1

The Company has granted finance leases of between 44 and 57 years in respect of concrete settling tanks. The interest terms were set at the inception of the leases. Leases bear interest at a weighted average interest rate of 5.1% (2018: 5.1%).

22 Borrowings

	Group		Company	
	2019 £m	2018 £m	2019 £m	2018 £m
Current liabilities				
Bank overdraft	**0.8**	8.4	**–**	8.8
Bank loans	**188.7**	287.9	**188.7**	287.9
Other loans	**2.8**	5.0	**2.6**	–
Loans due to parent and fellow subsidiary undertakings	**–**	–	**–**	0.2
Finance leases	**3.7**	2.9	**21.5**	19.5
Finance leases payable to other group companies	**–**	–	**3.6**	3.3
	196.0	304.2	**216.4**	319.7
Non-current liabilities				
Bank loans	**897.3**	894.2	**897.3**	894.2
Other loans	**4,729.5**	4,133.2	**894.8**	567.5
Loans due to parent and fellow subsidiary undertakings	**–**	9.3	**4,287.1**	4,015.7
Finance leases	**108.0**	111.0	**126.9**	147.8
Finance leases payable to other group companies	**–**	–	**192.2**	195.8
	5,734.8	5,147.7	**6,398.3**	5,821.0
	5,930.8	5,451.9	**6,614.7**	6,140.7

Severn Trent Water Limited
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23 Finance leases

Obligations under finance leases are as follows:

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Within 1 year	**7.0**	6.5	**39.9**	39.0
1 – 2 years	**7.5**	7.0	**41.1**	40.1
2 – 5 years	**26.1**	24.3	**67.7**	85.7
After more than 5 years	**103.7**	113.1	**347.3**	370.5
Gross obligations under finance leases	**144.3**	150.9	**496.0**	535.3
Less: future finance charges	**(32.6)**	(37.0)	**(151.8)**	(168.9)
Present value of lease obligations	**111.7**	113.9	**344.2**	366.4

Net obligations under finance leases fall due as follows:

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Within 1 year	**3.7**	2.9	**25.1**	22.8
1 – 2 years	**3.9**	3.2	**26.4**	24.5
2 – 5 years	**16.0**	13.6	**28.2**	44.3
After more than 5 years	**88.1**	94.2	**264.5**	274.8
Included in non-current liabilities	**108.0**	111.0	**319.1**	343.6
	111.7	113.9	**344.2**	366.4

The remaining terms of finance leases ranged from 1 to 13 years at 31 March 2019. Interest terms are set at the inception of the leases. Leases with capital outstanding of £111.7 million (2018: £113.9 million) bear fixed interest at a weighted average rate of 5.34% (2018: 5.34%) for the Group. Leases which bear fixed interest at a weighted average rate of 5.2% (2018: 5.2%) have capital outstanding of £306.9 million (2018: £312.8 million) for the Company. The lease obligations are secured against the related assets.

There were no contingent rents, escalation clauses or material renewal or purchase options. The terms of the finance leases do not impose restriction on dividend payments, additional debt or further leasing.

24 Categories of financial liabilities – Group

	Note	2019 £m	2018 £m
Fair value through profit and loss			
Interest rate swaps – not hedge accounted		**94.1**	98.7
Inflation swaps – not hedge accounted		**6.2**	2.8
		100.3	101.5
Derivatives designated as hedging instruments			
Interest rate swaps – cash flow hedges		**18.6**	5.9
Energy hedges – cash flow hedges		**0.4**	0.8
		19.0	6.7
Total derivative financial liabilities		**119.3**	108.2
Other financial liabilities			
Borrowings	22	**5,930.8**	5,451.9
Trade payables	25	**25.7**	12.3
Other payables	25	**19.0**	18.8
Amounts due to parent and fellow subsidiary undertakings	25	**0.8**	17.6
Total other financial liabilities		**5,976.3**	5,500.6
Total financial liabilities		**6,095.6**	5,608.8
Disclosed in the balance sheet as:			
Non-current liabilities			
Derivative financial liabilities		**119.3**	108.2
Borrowings		**5,734.8**	5,147.7
Other payables		**1.8**	–
		5,855.9	5,255.9
Current liabilities			
Borrowings		**196.0**	304.2
Trade payables		**25.7**	12.3
Other payables		**17.2**	18.8
Amounts due to parent and fellow subsidiary undertakings		**0.8**	17.6
		239.7	352.9
		6,095.6	5,608.8

25 Trade and other payables

	Group		Company	
	2019 £m	2018 £m	2019 £m	2018 £m
Current liabilities				
Trade payables	**25.7**	12.3	**25.0**	12.0
Social security and other taxes	**6.1**	5.6	**6.0**	5.5
Other payables	**17.2**	18.8	**14.2**	4.5
Accruals	**392.1**	380.1	**342.1**	336.0
Deferred income	**18.9**	14.9	**18.7**	14.7
Amounts owed to parent and fellow subsidiary undertakings	**0.8**	17.6	**52.5**	57.6
	460.8	449.3	**458.5**	430.3
Non-current liabilities				
Other payables	**1.8**	–	**–**	–
Deferred income	**1,074.1**	1,008.9	**1,063.7**	998.7
	1,075.9	1,008.9	**1,063.7**	998.7
	1,536.7	1,458.2	**1,522.2**	1,429.0

The Directors consider that the carrying value of trade payables is not materially different from their fair values.

26 Deferred tax

Group

An analysis of the movements in the major deferred tax liabilities and assets recognised by the Group is set out below:

	Accelerated tax depreciation £m	Retirement benefit obligations £m	Fair value of financial instruments £m	Other £m	Total £m
At 1 April 2017	755.4	(78.8)	(44.6)	(5.4)	626.6
Charge/(credit) to income	22.9	(0.3)	1.7	2.8	27.1
Charge for adjustments to provisional fair values	0.1	–	–	1.0	1.1
Charge to equity	–	18.4	2.1	1.3	21.8
At 1 April 2018	778.4	(60.7)	(40.8)	(0.3)	676.6
Charge/(credit) to income	34.8	(2.2)	5.0	(0.6)	37.0
Charge/(credit) to equity	–	21.7	(0.1)	(0.1)	21.5
At 31 March 2019	**813.2**	**(41.2)**	**(35.9)**	**(1.0)**	**735.1**

Company

An analysis of the movements in the major deferred tax liabilities and assets recognised by the Company is set out below:

	Accelerated tax depreciation £m	Retirement benefit obligations £m	Fair value of financial instruments £m	Other £m	Total £m
At 1 April 2017	743.5	(80.5)	(44.6)	(4.4)	614.0
Charge/(credit) to income	23.8	(0.3)	1.7	2.7	27.9
Charge to equity	–	17.0	2.1	1.3	20.4
At 1 April 2018	767.3	(63.8)	(40.8)	(0.4)	662.3
Charge/(credit) to income	33.4	(2.3)	5.0	(0.3)	35.8
Charge/(credit) to equity	–	21.7	(0.1)	(0.1)	21.5
At 31 March 2019	**800.7**	**(44.4)**	**(35.9)**	**(0.8)**	**719.6**

Deferred tax assets and liabilities have been offset. The offset amounts, which are to be recovered/settled after more than 12 months, are as follows:

Group

	2019 £m	2018 £m
Deferred tax asset	**(78.1)**	(101.8)
Deferred tax liability	**813.2**	778.4
	735.1	676.6

Company

	2019 £m	2018 £m
Deferred tax asset	**(81.1)**	(105.0)
Deferred tax liability	**800.7**	767.3
	719.6	662.3

27 Retirement benefit schemes

a) Defined benefit pension schemes

i) Background

The Group operates a number of defined benefit pension schemes. The Severn Trent Pension Scheme and the Severn Trent Mirror Image Pension Scheme closed to future accrual on 31 March 2015, while the Dee Valley Water Limited Section of the Water Companies Pension Scheme, which is a sectionalised scheme, currently remains open to accrual. The defined benefit pension schemes cover increases in accrued benefits arising from inflation and pension increases. Their assets are held in separate funds administered by trustees. The trustees are required to act in the best interests of the schemes' beneficiaries. A formal actuarial valuation of each scheme is carried out on behalf of the trustees at triennial intervals by an independent professionally qualified actuary. Under the defined benefit pension schemes, members are entitled to retirement benefits calculated by reference to their pensionable service and pensionable salary history, with inflationary pension increases applying in line with the scheme rules.

The defined benefit pension schemes and the dates of their last completed formal actuarial valuations as at the accounting date are as follows:

	Date of last formal actuarial valuation
Severn Trent Pension Scheme (STPS)*	31 March 2016
Severn Trent Mirror Image Pension Scheme (STMIPS)	31 March 2016
Water Companies Pension Scheme – Dee Valley Water Limited Section (DVWS)	31 March 2017

* The STPS is by far the largest of the Group's UK defined benefit schemes, comprising over 90% of the Group's overall defined benefit obligations.

ii) Amounts included in the balance sheet arising from the Group's obligations under defined benefit pension schemes

	Group		**Company**	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Fair value of assets	**2,418.9**	2,339.8	**2,609.8**	2,540.4
Present value of the defined benefit obligations	**(2,863.2)**	(2,850.9)	**(2,815.2)**	(2,804.1)
	(444.3)	(511.1)	**(205.4)**	(263.7)
Presented on the balance sheet as:				
Retirement benefit obligation – funded schemes in surplus	**18.6**	18.2	**–**	–
Retirement benefit obligation – funded schemes in deficit	**(462.9)**	(529.3)	**(205.4)**	(263.7)
Retirement benefit obligation – unfunded schemes	**–**	–	**–**	–
Retirement benefit obligation – total	**(462.9)**	(529.3)	**(205.4)**	(263.7)
Net retirement benefit obligation	**(444.3)**	(511.1)	**(205.4)**	(263.7)

Severn Trent Water Limited

Notes to the Group and Company financial statements (continued)

For the year ended 31 March 2019

27 Retirement benefit schemes (continued)

The schemes' assets were as follows:

	Group		Company	
	2019	2018	**2019**	2018
STPS, STMIPS, and DVWS	**£m**	£m	**£m**	£m
Fair value of scheme assets				
Equities	**356.6**	360.4	**356.6**	350.4
Diversified growth funds	**–**	5.3	**–**	–
Gilts	**–**	–	**–**	–
Corporate bonds	**899.2**	825.7	**899.2**	825.7
Liability driven investment funds (LDI)	**746.0**	783.1	**713.0**	740.7
Property	**228.2**	180.7	**228.2**	180.7
Emerging markets multi-assets funds	**–**	3.9	**–**	–
High-yield bonds	**31.3**	3.4	**–**	–
Hedge funds	**–**	0.6	**–**	0.6
Contributions due from Scottish Limited Partnerships[1]	**–**	–	**257.5**	265.6
Cash	**157.6**	176.7	**155.3**	176.7
	2,418.9	2,339.8	**2,609.8**	2,540.4

1 The Scottish Limited Partnerships are subsidiaries of Severn Trent Water and therefore any movements are eliminated upon consolidation.

The majority of the assets have quoted prices in active markets, but there are a small proportion of the equity and LDI investments which are unquoted.

Movements in the fair value of the schemes' assets were as follows:

	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Fair value at 1 April	**2,339.8**	2,352.8	**2,540.4**	2,558.2
Interest income on scheme assets	**61.0**	62.0	**59.3**	60.3
Contributions paid by the group/company	**34.5**	33.8	**12.0**	9.3
Contributions from other Severn Trent Group companies	**–**	0.7	**–**	–
Contributions from scheme members	**0.1**	0.1	**–**	–
Return on plan assets (excluding amounts included in finance income)	**95.9**	(1.3)	**94.2**	(0.9)
Scheme administration costs	**(2.3)**	(1.8)	**(2.1)**	(1.6)
Benefits paid	**(110.1)**	(106.5)	**(108.1)**	(98.7)
Unwind of discount on contribution due from SLPs	**–**	–	**14.1**	13.1
Fair value at 31 March	**2,418.9**	2,339.8	**2,609.8**	2,540.4

27 Retirement benefit schemes (continued)

Movements in the present value of the schemes' defined benefit obligations were as follows:

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Present value at 1 April	**(2,850.9)**	(2,927.4)	**(2,804.1)**	(2,866.3)
Current service cost	**(0.2)**	(0.5)	**–**	–
Exceptional past service (charge)/credit	**(9.6)**	8.3	**(9.2)**	8.3
Interest cost	**(74.6)**	(77.2)	**(73.4)**	(75.7)
Contributions from scheme members	**(0.1)**	(0.1)	**–**	–
Actuarial gains arising from changes in demographic assumptions	**55.5**	21.5	**54.6**	17.5
Actuarial (losses)/gains arising from changes in financial assumptions	**(132.4)**	17.4	**(130.2)**	12.6
Actuarial gains arising from experience adjustments	**39.0**	0.6	**39.0**	0.8
Benefits paid	**110.1**	106.5	**108.1**	98.7
Present value at 31 March	**(2,863.2)**	(2,850.9)	**(2,815.2)**	(2,804.1)

Severn Trent Plc has an obligation to pay pensions to a number of former employees, whose benefits would otherwise have been restricted by the Finance Act 1989 earnings cap. In prior years, the unfunded pension scheme was recorded in Severn Trent Water Limited. As the obligations under the scheme are borne by Severn Trent Plc, the unfunded pension scheme obligation is now included within Severn Trent Plc.

The Group has assessed that is has an unconditional right to a refund of any surplus assets in each of the Schemes following settlement of all obligations to scheme members and therefore the surplus in DVWS has been recognised in full.

iii) Amounts recognised in the income statement in respect of these defined benefit schemes

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	£m	£m
Amounts (charged)/credited to operating costs				
Current service cost	**(0.2)**	(0.5)	**–**	–
Exceptional past service (charge)/credit	**(9.6)**	8.3	**(9.2)**	8.3
Scheme administration costs	**(2.3)**	(1.8)	**(2.1)**	(1.6)
	(12.1)	6.0	**(11.3)**	6.7
Amounts charged to finance costs				
Interest cost	**(74.6)**	(77.2)	**(73.4)**	(75.7)
Amounts credited to finance income				
Interest income on scheme assets	**61.0**	62.0	**59.3**	60.3
Total amount charged/(credited) to the income statement	**(25.7)**	(9.2)	**(25.4)**	(8.7)

The actual return on scheme assets was a gain of £156.9 million (2018: gain of £60.7 million).

Actuarial gains and losses have been reported in the statement of comprehensive income.

27 Retirement benefit schemes (continued)

iv) Actuarial risk factors

The Schemes typically expose the Group to actuarial risks such as investment risk, inflation risk and longevity risk.

Investment risk

The Group's contributions to the Schemes are based on actuarial calculations which make assumptions about the returns expected from the Schemes' investments. If the investments underperform these assumptions in the long term then the Group may need to make additional contributions to the Schemes in order to fund the payment of accrued benefits.

Each plan's investment strategy seeks to balance the level of investment return sought with the aim of reducing volatility and risk. In undertaking this approach reference is made to both the maturity of liabilities and the funding level of that plan. A number of further strategies are employed to manage underlying risks, including liability matching asset strategies, diversification of asset portfolios and interest rate hedging.

Currently the plan has a balanced approach to investment in equity securities, debt instruments and real estates. Due to the long term nature of the plan liabilities, we consider it appropriate to invest a portion of the plan assets in equity securities and in real estate to leverage the return generated by the fund.

Inflation risk

The benefits payable to members of the Schemes are linked to inflation measured by the RPI or CPI , subject to caps. The Group's contributions to the Schemes are based on assumptions about the future level of inflation. If inflation is higher than the levels assumed in the actuarial calculations then the Group may need to make additional contributions to the Schemes in order to fund the payment of accrued benefits.

The Schemes use Liability Driven Investment ("LDI") within the asset portfolios to hedge against the value of liabilities changing as a result of movements in long-term interest rate and inflation expectations. This structure allows the Schemes to both hedge against these risks and retain capital investment in assets that are expected to generate higher returns.

Longevity risk

The Group's contributions to the Schemes are based on assumptions about the life expectancy of Scheme members after retirement. If Scheme members live longer than assumed in the actuarial calculations then the Group may need to make additional contributions to the Schemes in order to fund the payment of accrued benefits.

v) Actuarial assumptions

The major financial assumptions used in the accounting valuation of the obligations for the STPS which represents by far the largest defined benefit obligation for the Group were as follows.

	2019	2018
	% pa	% pa
Price inflation – RPI	**3.2**	3.1
Price inflation – CPI	**2.2**	2.1
Discount rate	**2.5**	2.7
Pension increases in payment	**3.2**	3.1
Pension increases in deferment	**3.2**	3.1

The assumption for price inflation is derived from the difference between the yields on longer term fixed rate gilts and on index-linked gilts.

In setting our discount rate, we construct a yield curve. Short dated yields are taken from market rates for AA corporate bonds. Long dated yields for the curve are based on the average yield available on all long dated AA corporate bonds. We project the expected cash flows of the Schemes and adopt a single equivalent cash flow weighted discount rate based on this constructed yield curve.

27 Retirement benefit schemes (continued)

The mortality assumptions are based on those used in the latest triennial funding valuations. The mortality assumptions adopted at the year end for accounting purposes and the life expectancies at age 65 implied by the assumptions are as follows for the STPS:

	2019		2018	
	Men	**Women**	Men	Women
Mortality table used	**S2NMA**	**S2NFA**	S2NMA	S2NFA
Mortality table compared with standard table	**95%**	**99%**	95%	99%
Mortality projections	**CMI 2018**	**CMI 2018**	CMI 2017	CMI 2017
Future improvement per annum	**1.0%**	**1.0%**	1.0%	1.0%
Remaining life expectancy for members currently aged 65 (years)	**21.9**	**23.6**	22.4	24.1
Remaining life expectancy at age 65 for members currently aged 45 (years)	**22.9**	**24.8**	23.4	25.3

The calculation of the scheme obligations is sensitive to the actuarial assumptions and in particular to the assumptions relating to discount rate, price inflation (capped, where relevant) and mortality. The following table summarises the estimated impact on the group's obligations from changes to key actuarial assumptions whilst holding all other assumptions constant.

Assumption	Change in assumption	Impact on disclosed obligations
Discount rate[1]	Increase/decrease by 0.1% pa	Decrease/increase by £46/£47 million
Price inflation[2]	Increase/decrease by 0.1% pa	Increase/decrease by £40/£39 million
Mortality[3]	Increase in life expectancy by 1 year	Increase by £106 million

1 A change in discount rate is likely to occur as a result of changes in bond yield and as such would be expected to be offset to a significant degree by a change in the value of the bond assets held by the plans.
2 The projected impact resulting from a change in RPI reflects the underlying effect on pensions in payment, pensions in deferment and resultant increases in salary assumptions.
3 The change in assumption is based on triennial valuations and reflect the fact that life expectancy rates are expected to increase.

In reality, interrelationships exist between the assumptions, particularly between the discount rate and price inflation. The above analysis does not take into account the effect of these interrelationships. Also, in practice any movement in obligations arising from assumption changes are likely to be accompanied by movements in asset values – and so the impact on the accounting deficit may be lower than the impact on the obligations shown above.

In presenting the above sensitivity analysis, the present value of the defined benefit obligation has been calculated using the projected unit credit method at the end of the reporting period, which is the same as that applied in calculating the defined benefit obligation liability recognised in the balance sheet. Contribution rates are set in consultation with the trustees for each scheme and each participating employer.

vi) Effect on future cash flows

Contribution rates are set in consultation with the trustees for each scheme and each participating employer.

The average duration of the benefit obligation at the end of the year is 16 years for STPS and STMIPS (2018: 17 years) and 15 years for DVWS (2018: 16 years).

The most recent completed formal triennial actuarial valuations and funding agreements were carried out as at 31 March 2016 for the STPS and STMIPS schemes and 31 March 2014 for DVWS. As a result of the STPS and STMIPS actuarial valuations, deficit reduction contributions of £25 million were paid in the year ended 31 March 2018 and £10 million for each of the subsequent financial years ending 31 March 2019 were agreed. Payments of £8 million per annum through an asset backed funding arrangement will continue to 31 March 2032. Further inflation linked payments of £15 million per annum are being made through an additional asset backed funding arrangement, with payments having started in the financial year ending 31 March 2018 and continuing to 31 March 2031. These contributions will cease earlier should a subsequent valuation of the STPS show that these contributions are no longer needed.

27 Retirement benefit schemes (continued)

b) Defined contribution pension schemes

The Group also operates the Severn Trent Group Personal Pension, a defined contribution scheme, for certain of its UK employees.

The total cost charged to operating costs of £22.4 million (2018: £19.6 million) for the group and £22.3 million (2018: £19.4 million) for the company represents contributions payable to these schemes by the group at rates specified in the rules of the scheme. As at 31 March 2019, no contributions (2018: nil) in respect of the current reporting period were owed to the schemes.

Dee Valley Water operates two defined contribution pension schemes, neither of which were material in either the current or prior year.

28 Provisions – Group and Company

	Restructuring £m	Insurance £m	Other £m	Total £m
At 1 April 2018	0.8	8.4	13.6	22.8
Charged to income statement	–	4.9	5.6	10.5
Utilisation of provision	(0.5)	(3.2)	(5.5)	(9.2)
Unwinding of discount	–	–	0.2	0.2
At 31 March 2019	**0.3**	**10.1**	**13.9**	**24.3**

	2019 £m	2018 £m
Included in		
Current liabilities	**15.3**	16.6
Non-current liabilities	**9.0**	6.2
	24.3	22.8

The restructuring provision reflects costs to be incurred in respect of committed restructuring programmes. The associated outflows are estimated to arise over a period of up to two years from the balance sheet date.

The insurance provision relates to self-insurance. The associated outflows are estimated to arise over a period of up to five years from the balance sheet date.

Other provisions include provisions for dilapidations and commercial disputes. The associated outflows are estimated to arise over a period up to three years from the balance sheet date.

29 Share capital

	2019 £m	2018 £m
Total issued and fully paid share capital		
1,000,100,000 ordinary shares of 0.1 pence (2018: 1,000,100,000)	**1.0**	1.0

30 Hedging reserve – Group and Company

The hedging reserve arises from gains or losses on interest rate swaps taken directly to equity under the hedge accounting provisions of IFRS 9 and the transition rules of IFRS 1.

31 Capital management – Group

The Group’s principal objectives in managing capital are:

- to access a broad range of sources of finance to obtain both the quantum required and lowest cost compatible with the need for continued availability;
- to manage exposure to movements in interest rates to provide an appropriate degree of certainty as to its cost of funds;
- to minimise exposure to counterparty credit risk;
- to provide the Group with an appropriate degree of certainty as to its foreign exchange exposure;
- to maintain an investment grade credit rating; and
- to maintain a flexible and sustainable balance sheet structure.

The Group seeks to achieve a balance of long term funding or commitment of funds across a range of funding sources at the best possible economic cost. The Group monitors future funding requirements and credit market conditions to ensure continued availability of funds.

The Group has continued to increase exposure to low floating interest rates.

The Group's dividend policy is to declare dividends which are consistent with the Group's regulatory obligations and at a level which is decided each year after consideration of a number of factors, including regulatory uncertainty, future cash flow requirements and balance sheet considerations. The amount declared is expected to vary each year as the impact of these factors changes.

The Group's capital at 31 March was:

	2019 £m	2018 £m
Cash and cash equivalents	**12.9**	12.1
Bank overdrafts	**(0.8)**	(8.4)
Bank loans	**(1,086.0)**	(1,182.1)
Other loans	**(4,732.3)**	(4,138.2)
Loans due from/(to) parent company	**80.6**	(9.3)
Obligations under finance leases	**(111.7)**	(113.9)
Cross currency swaps	**37.1**	24.5
Loans due from joint ventures	**100.0**	99.8
Net debt	**(5,700.2)**	(5,315.5)
Equity attributable to owners of the company	**(2,507.5)**	(2,324.8)
Total capital	**(8,207.7)**	(7,640.3)

32 Fair values of financial instruments – Group

a) Fair value measurements

The valuation techniques that the Group applies in determining the fair values of its financial instruments on a recurring basis are described below. The techniques are classified under the hierarchy defined in IFRS 13 which categorises valuation techniques into Levels 1 - 3 based on the degree to which the fair value is observable. The Group's valuation techniques include Levels 2 and 3 given the wide range of financial instruments below:

	2019 £m	2018 £m	Valuation techniques and key inputs
Cross currency swaps			Discounted cash flow
Assets	**37.1**	24.5	Future cash flows are estimated based on forward interest rates from observable yield curves at the period end and contract interest rates discounted at a rate that reflects the credit risk of counterparties. The currency cash flows are translated at spot rate.
Interest rate swaps			Discounted cash flow
Assets	**26.1**	11.4	Future cash flows are estimated based on forward interest rates from observable yield curves at the period end and contract interest rates discounted at a rate that reflects the credit risk of counterparties.
Liabilities	**(112.7)**	(104.6)	
Energy swaps			Discounted cash flow
Assets	**5.3**	0.3	Future cash flows are estimated based on forward electricity prices from observable indices at the period end and contract prices discounted at a rate that reflects the credit risk of counterparties.
Liabilities	**(0.4)**	(0.8)	
Inflation swap			Discounted cash flow
Liabilities	**(6.2)**	(2.8)	Future cash flows on the RPI leg of the instrument are estimated based on observable forward inflation indices. Future cash flows on the CPI leg of the instrument are estimated based on the future expected differential between RPI and CPI. Both legs are discounted using observable swap rates at the period end, at a rate that reflects the credit risk of counterparties. This is considered to be a Level 3 valuation technique. The change in value during the year was recognised in the income statement.
Investment			Net asset value
Asset	**1,510.8**	1,488.6	The fair value of the investment is considered to be the Group's share of its net assets.

Changes in the carrying values of instruments that are measured using a Level 3 technique were as follows:

	Inflation swaps £m	Investment £m
At 1 April 2017	–	1,470.0
(Losses)/gains recognised in profit or loss	(2.8)	18.6
At 31 March 2018	(2.8)	1,488.6
(Losses)/gains recognised in profit or loss	(3.4)	22.2
At 31 March 2019	**(6.2)**	**1,510.8**

32 Fair values of financial instruments – Group (continued)

b) Comparison of fair value of financial instruments with their carrying amounts

The Directors consider that the carrying amounts of cash and short term deposits, bank overdrafts, loans due from joint ventures, trade receivables and trade payables approximate their fair values. The carrying values and estimated fair values of other financial instruments are set out below:

	2019		2018	
	Carrying value £m	**Fair value £m**	Carrying value £m	Fair value £m
Floating rate debt				
Bank loans	**818.1**	**818.3**	917.1	918.6
Currency bonds	**37.9**	**37.9**	38.2	38.2
Floating rate notes	**147.8**	**148.0**	147.7	153.0
Loan from parent company	**–**	**–**	9.3	9.3
	1,003.8	**1,004.2**	1,112.3	1,119.1
Fixed rate debt				
Bank loans	**150.0**	**150.0**	150.0	150.0
Sterling bonds	**2,591.0**	**2,956.8**	2,356.9	2,700.2
Fixed rate notes	**673.3**	**707.4**	343.4	347.6
Other loans	**2.9**	**2.8**	5.0	5.0
Finance leases	**111.6**	**119.1**	113.9	122.5
	3,528.8	**3,936.1**	2,969.2	3,325.3
Index-linked debt				
Bank loans	**117.9**	**126.7**	115.0	124.9
Sterling bonds	**1,190.8**	**2,007.8**	1,158.8	1,964.9
Other loans	**88.6**	**67.2**	88.2	87.1
	1,397.3	**2,201.7**	1,362.0	2,176.9
	5,929.9	**7,142.0**	5,443.5	6,621.3

The above classification does not take into account the impact of unhedged interest rate swaps or cross currency swaps.

Fixed rate sterling and currency bonds are valued using market prices, which is a Level 2 valuation technique.

Index-linked bonds are rarely traded and therefore quoted prices are not considered to be a reliable indicator of fair value. Therefore, these bonds are valued using discounted cash flow models with discount rates derived from observed market prices for a sample of bonds, which is a Level 3 valuation technique.

Fair values of the other debt instruments are also calculated using discounted cash flow models, which is a Level 3 valuation technique.

33 Risks arising from financial instruments – Group

The Group's activities expose it to a variety of financial risks:

- market risk (including interest rate risk exchange rate risk and other price risk);
- credit risk;
- liquidity risk; and
- inflation risk.

The Group's overall risk management programme addresses the unpredictability of financial markets and seeks to reduce potential adverse effects on the Group's financial performance or position.

Financial risks are managed by a central treasury department (Group Treasury) under policies approved by the Board of Directors. The Board has established a Treasury Management Committee to monitor treasury activities and to facilitate timely responses to changes in market conditions when necessary. Group Treasury identifies, evaluates and hedges financial risks in close co-operation with the Group's operating units. The Board defines written principles for overall risk management, as well as written policies covering specific areas such as exchange rate risk, interest rate risk, credit risk and the use of derivative and non-derivative financial instruments. The Group's policy is that derivative financial instruments are not held for trading but may be used to mitigate the Group's exposure to financial risk. The types of derivative instruments held and the related risks are described below.

Interest rate swaps are held to mitigate the Group's exposure to changes in market interest rates. Further details are set out in sections a) (i) and note 34 below.

Cross currency swaps are held to mitigate the Group's exposure to exchange rate movements on amounts borrowed in foreign currencies. Further details are set out in section a) (ii) below.

Energy swaps are held to mitigate the Group's exposure to changes in electricity prices. Further details are provided in note 34 below.

Severn Trent Water and Hafren Dyfrdwy operate under a regulatory environment where sales prices are linked to inflation measured by RPI. In order to mitigate the risks to cash flow and earnings arising from fluctuations in RPI, the Group holds debt instruments where the principal repayable and interest cost is linked to RPI. Ofwat, the economic regulator, has announced a phased transition from RPI to CPIH as the measure of inflation in the regulatory model. The Group has entered into RPI/CPI swaps to mitigate the risk of a mismatch between debt linked to RPI and revenues linked to CPIH.

a) Market risk

The Group is exposed to fluctuations in interest rates and, to a lesser extent, exchange rates. The nature of these risks and the steps that the Group has taken to manage them are described below.

(i) Interest rate risk

The Group's income and its operating cash flows are substantially independent of changes in market interest rates. The Group's interest rate risk arises from long-term borrowings.

Borrowings issued at variable rates expose the Group to the risk of adverse cash flow impacts from increases in interest rates.

Borrowings issued at fixed rates expose the Group to the risk of interest costs above the market rate when interest rates decrease.

The Group's policy is to maintain 40% to 70% of its interest bearing liabilities in fixed rate instruments in AMP6. In measuring this metric, management makes adjustments to the carrying value of debt to better reflect the amount that interest is calculated on. Details of the adjustments made are set out below:

	2019 £m	2018 £m
Net debt (note 38)	**5,700.2**	5,315.5
Cash and cash equivalents	**12.9**	12.1
Loan due from parent company	**80.6**	-
Loans due from joint ventures and associates	**100.0**	99.8
Cross currency swaps included in net debt at fair value	**37.1**	24.5
Fair value hedge accounting adjustments	**(28.8)**	(30.4)
Exchange on currency debt not hedge accounted	**(16.8)**	(8.5)
Interest bearing financial liabilities	**5,885.3**	5,413.0

33 Risks arising from financial instruments – Group (continued)

The Group manages its cash flow interest rate risk by borrowing at fixed or index-linked rates and by using interest rate swaps. Under these swaps the Group receives floating rate interest and pays fixed rate interest calculated by reference to the agreed notional principal amounts. In practice the swaps are settled by transferring the net amount. These swaps have the economic effect of converting borrowings from floating rates to fixed rates. The Group has entered into a series of these interest rate swaps to hedge future interest payments to beyond 2030.

The following tables show analyses of the Group's interest bearing financial liabilities by type of interest. Debt which is hedged by interest rate swaps is included in the category after taking account of the impact of the swap. Debt raised in foreign currencies has been included at the notional sterling value of the payable leg of the corresponding cross currency swap since this is the amount that is exposed to changes in interest rates.

Valuation adjustments that do not impact the amount on which interest is calculated, such as fair value hedge accounting adjustments, are excluded from this analysis.

The net principal amount of unhedged swaps is shown as an adjustment to floating rate and fixed rate debt to demonstrate the impact of the Group's interest rate swaps on the amount of liabilities bearing fixed interest.

2019	Floating rate £m	Fixed rate £m	Index-linked £m	Total £m
Overdrafts	(0.8)	–	–	**(0.8)**
Bank loans	(818.1)	(150.0)	(117.9)	**(1,086.0)**
Other loans	(167.8)	(3,239.5)	(1,279.4)	**(4,686.7)**
Finance leases	–	(111.7)	–	**(111.7)**
	(986.7)	**(3,501.2)**	**(1,397.3)**	**(5,885.2)**
Impact of swaps not matched against specific debt instruments	(348.4)	348.4	–	–
Interest bearing financial liabilities	**(1,335.1)**	**(3,152.8)**	**(1,397.3)**	**(5,885.2)**
Proportion of interest bearing financial liabilities that are fixed		**54%**		
Weighted average interest rate of fixed rate debt		**4.19%**		
Weighted average period for which interest is fixed (years)		**8.8**		

2018	Floating rate £m	Fixed rate £m	Index-linked £m	Total £m
Overdrafts	(8.4)	–	–	(8.4)
Bank loans	(917.1)	(150.0)	(115.0)	(1,182.1)
Other loans	(167.6)	(2,684.7)	(1,247.0)	(4,099.3)
Loans due to parent company	(9.3)	–	–	(9.3)
Finance leases	–	(113.9)	–	(113.9)
	(1,102.4)	(2,948.6)	(1,362.0)	(5,413.0)
Impact of swaps not matched against specific debt instruments	(349.6)	349.6	–	–
Interest bearing financial liabilities	(1,452.0)	(2,599.0)	(1,362.0)	(5,413.0)
Proportion of interest bearing financial liabilities that are fixed		48%		
Weighted average interest rate of fixed rate debt		4.34%		
Weighted average period for which interest is fixed (years)		8.7		

33 Risks arising from financial instruments – Group (continued)

Interest rate swaps not hedge accounted

The Group has a number of interest rate swaps which are not accounted for as cash flow or fair value hedges. Economically these swaps act to fix the interest cost of debt within the Group which is denominated as floating rate and fixed rate debt, but they do not achieve hedge accounting under the strict criteria of IAS 39. This has led to a credit of £19.7 million (2018: charge of £7.8 million) in the income statement.

	Average contract fixed interest rate		Notional principal amount		Fair value	
	2019	2018	**2019**	2018	**2019**	2018
	%	%	**£m**	£m	**£m**	£m
Pay fixed rate interest						
2-5 years	**4.98**	–	**(150.0)**		**(25.8)**	–
5-10 years	**5.14**	5.06	**(150.0)**	(300.0)	**(34.9)**	(65.6)
10-20 years	**5.45**	5.46	**(75.0)**	(73.7)	**(33.5)**	(32.5)
	5.13	5.16	**(375.0)**	(373.7)	**(94.2)**	(98.1)
Receive fixed rate interest						
5-10 years	**3.36**	3.36	**225.0**	225.0	**15.8**	11.4
10-20 years	**2.75**	2.75	**400.0**	400.0	**10.4**	(0.6)
	2.97	3.01	**625.0**	625.0	**26.2**	10.8
			250.0	251.3	**(68.0)**	(87.3)

Interest rate sensitivity analysis

The sensitivity after tax of the Group's profits, cash flow and equity, including the impact on derivative financial instruments, to reasonably possible changes in interest rates at 31 March is as follows:

		2019		2018
	1.0%	**-1.0%**	1.0%	-1.0%
	£m	**£m**	£m	£m
Profit or loss	**(48.5)**	**54.3**	(47.8)	54.0
Cash flow	**(10.8)**	**10.8**	(11.6)	11.6
Equity	**(48.5)**	**54.3**	(47.8)	54.0

(ii) Exchange rate risk

Except for debt raised in foreign currency, which is hedged, the Group's business does not involve significant exposure to foreign exchange transactions and therefore the sensitivity of the Group's results to changes in exchange rates is not material.

In order to meet its objective of accessing a broad range of sources of finance, the Group has raised debt denominated in currencies other than sterling. In order to mitigate the Group's exposure to exchange rate fluctuations, cross currency swaps were entered into at the time that the debt was drawn down to swap the proceeds into sterling debt bearing interest based on LIBOR.

Where the terms of the receivable leg of the swap closely match the terms of the underlying debt, the swaps are expected to be effective hedges, hence the swaps have been accounted for as fair value hedges. The notional value and fair value of these swaps is shown in note 32 a).

The Group also has a number of fixed to floating rate cross currency swaps with a notional sterling value of 98.3 million (2018: £98.3 million) which are not accounted for as fair value hedges. Economically these swaps act to mitigate the exchange rate risk of debt within the Group which is denominated in foreign currency, but they are not designated hedges under IFRS 9. This has led to a credit of £12.2 million (2018: charge of £17.7 million) in the income statement which is offset by the exchange loss of £8.6 million (2018: exchange gain of £12.7 million) on the underlying debt.

33 Risks arising from financial instruments – Group (continued)

The Group's gross and net currency exposures arising from currency borrowings are summarised in the tables below. These show, in the relevant currency, the amount borrowed and the notional principal of the related swap or forward contract. The net position shows the Group's exposure to exchange rate risk in relation to its currency borrowings.

2019	Euro €m	US Dollar $m	Yen ¥Bn
Borrowings by currency	(19.9)	(180.0)	(2.0)
Cross currency swaps - hedge accounted	19.9	30.0	2.0
Cross currency swaps - not hedge accounted	–	150.0	–
Net currency exposure	**–**	**–**	**–**

2018	Euro €m	US Dollar $m	Yen ¥Bn
Borrowings by currency	(19.9)	(150.0)	(2.0)
Cross currency swaps - hedge accounted	19.9	–	2.0
Cross currency swaps - not hedge accounted	–	150.0	–
Net currency exposure	–	–	–

b) Credit risk

Operationally the Group has no significant concentrations of credit risk. It has policies in place to ensure that sales of products are made to customers with an appropriate credit history, other than in Severn Trent Water Limited and Hafren Dyfrdwy Cyfyngedig, whose operating licences obliges them to supply domestic customers even in cases where bills are not paid. Amounts provided against accounts receivable and movements on the provision during the year are disclosed in note 20.

Cash deposits and derivative contracts are only placed with high credit quality financial institutions, which have been approved by the Board. Group Treasury monitors the credit quality of the approved financial institutions and the list of financial institutions that may be used is approved annually by the Board. The Group has policies that limit the amount of credit exposure to any one financial institution.

Credit risk analysis

At 31 March, the aggregate credit limits of authorised counterparties and the amounts held on short term deposits were as follows:

	Credit limit		Amount deposited	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Double A range	**105.0**	105.0	–	–
Single A range	**700.0**	650.0	–	–
Triple B range	**–**	10.0	–	–
	805.0	765.0	–	–

The fair values of derivative assets analysed by credit ratings of counterparties were as follows:

	Derivative assets	
	2019 £m	2018 £m
Double A range	**1.4**	–
Single A range	**67.1**	36.2
	68.5	36.2

33 Risks arising from financial instruments – Group (continued)

c) Liquidity risk

i) Committed facilities

Prudent liquidity management requires sufficient cash balances to be maintained; adequate committed facilities to be available and the ability to close out market positions. Group Treasury manages liquidity and flexibility in funding by monitoring forecast and actual cash flows and the maturity profile of financial assets and liabilities, and by keeping committed credit lines available.

At the balance sheet date the Group had committed undrawn borrowing facilities expiring as follows:

	2019 **£m**	2018 £m
2-5 years	**885.0**	610.0

ii) Cash flows from non-derivative financial instruments

The following tables show the estimated cash flows that will arise from the Group's non-derivative net financial liabilities. The information presented is based on the earliest date on which the Group can be required to pay and represents the undiscounted cash flows including principal and interest.

Interest and inflation assumptions are based on prevailing market conditions at the year-end date.

2019 **Undiscounted amounts payable:**	**Floating rate** **£m**	**Fixed rate** **£m**	**Index linked** **£m**	**Trade payables** **£m**	**Payments on financial liabilities** **£m**
Within 1 year	(201.0)	(122.5)	(27.6)	(25.7)	**(376.8)**
1 - 2 years	(12.0)	(277.0)	(29.7)	–	**(318.7)**
2 - 5 years	(339.0)	(1,165.6)	(221.5)	–	**(1,726.1)**
5 - 10 years	(448.4)	(1,359.6)	(412.3)	–	**(2,220.3)**
10 - 15 years	(50.8)	(1,206.0)	(217.9)	–	**(1,474.7)**
15 - 20 years	–	(246.1)	(145.6)	–	**(391.7)**
20 - 25 years	–	(413.4)	(176.3)	–	**(589.7)**
25 - 30 years	–	–	(208.5)	–	**(208.5)**
30 - 35 years	–	–	(652.7)	–	**(652.7)**
35 - 40 years	–	–	(3,248.6)	–	**(3,248.6)**
40 - 45 years	–	–	(22.8)	–	**(22.8)**
45 - 50 years	–	–	(358.6)	–	**(358.6)**
Total	**(1,051.2)**	**(4,790.2)**	**(5,722.1)**	**(25.7)**	**(11,589.2)**

Undiscounted amounts receivable:	**Loans due from joint ventures** **£m**	**Trade and other receivables** **£m**	**Cash and short term deposits** **£m**	**Amounts due from group undertakings** **£m**	**Receipts from financial assets** **£m**
Within 1 year	–	459.4	12.9	6.8	**479.1**
1-2 years	100.0	–	–	84.9	**184.9**

33 Risks arising from financial instruments – Group (continued)

2018 Undiscounted amounts payable:	Floating rate £m	Fixed rate £m	Index linked £m	Trade payables £m	Payments on financial liabilities £m
Within 1 year	(314.9)	(135.7)	(26.7)	(12.3)	(489.6)
1 - 2 years	(9.2)	(116.1)	(28.2)	–	(153.5)
2 - 5 years	(32.2)	(982.6)	(223.1)	–	(1,237.9)
5 - 10 years	(758.8)	(1,333.6)	(199.9)	–	(2,292.3)
10 - 15 years	(52.7)	(1,056.0)	(436.2)	–	(1,544.9)
15 - 20 years	–	(60.9)	(139.0)	–	(199.9)
20 - 25 years	–	(298.8)	(167.7)	–	(466.5)
25 - 30 years	–	–	(199.2)	–	(199.2)
30 - 35 years	–	–	(649.7)	–	(649.7)
35 - 40 years	–	–	(2,273.6)	–	(2,273.6)
40 - 45 years	–	–	(1,068.1)	–	(1,068.1)
45 - 50 years	–	–	(374.2)	–	(374.2)
Total	(1,167.8)	(3,983.7)	(5,785.6)	(12.3)	(10,949.4)

Undiscounted amounts receivable:	Loans due from joint ventures £m	Trade and other receivables £m	Cash and short term deposits £m	Amounts due from group undertakings £m	Receipts from financial assets £m
Within 1 year	–	182.7	12.1	8.4	203.2
1 - 2 years	99.8	–	–	–	99.8

Index-linked debt includes loans with maturities up to 51 years. The principal is revalued at fixed intervals and is linked to movements in the Retail Price Index. Interest payments are made biannually based on the revalued principal. The principal repayment equals the revalued amount at maturity. The payments included in the table above are estimates based on the forward inflation rates published by the Bank of England at the balance sheet date.

(iii) Cash flows from derivative financial instruments

The following tables show the estimated cash flows that will arise from the Group's derivative financial instruments. The tables are based on the undiscounted net cash inflows/(outflows) on the derivative financial instruments that settle on a net basis and the undiscounted gross inflows/(outflows) on those derivatives that require gross settlement. When the amount payable or receivable is not fixed, the amount disclosed has been determined by reference to the projected interest and foreign currency rates derived from the forward curves existing at the balance sheet date. Actual amounts may be significantly different from those indicated below.

	Derivative liabilities			**Derivative assets**				
						Cross currency swaps		
2019	**Interest rate swaps**	**Inflation swaps**	**Energy swaps**	**Interest rate swaps**	**Energy swaps**	**Cash receipts**	**Cash payments**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Within 1 year	(27.9)	–	–	16.7	0.1	6.2	(3.2)	**(8.1)**
1 - 2 years	(14.2)	–	–	0.3	0.6	6.2	(3.2)	**(10.3)**
2 - 5 years	(41.0)	(0.3)	(0.4)	0.6	4.7	18.3	(9.7)	**(27.8)**
5 - 10 Years	(30.2)	(1.7)	–	0.4	–	164.7	(144.1)	**(10.9)**
10 - 15 Years	(7.5)	(2.5)	–	(0.1)	–	16.9	(8.6)	**(1.8)**
15 – 20 years	–	10.4	–	–	–	–	–	**10.4**
	(120.8)	**5.9**	**(0.4)**	**17.9**	**5.4**	**212.3**	**(168.8)**	**(48.5)**

33 Risks arising from financial instruments – Group (continued)

2018	Derivative liabilities: Interest rate swaps	Derivative liabilities: Inflation swaps	Derivative liabilities: Energy swaps	Derivative assets: Interest rate swaps	Derivative assets: Energy swaps	Derivative assets: Cross currency swaps: Cash receipts	Derivative assets: Cross currency swaps: Cash payments	Total
	£m	**£m**	£m	£m	**£m**	£m	£m	£m
Within 1 year	(13.4)	–	–	5.1	0.2	1.1	(0.2)	(7.2)
1 - 2 years	(13.6)	–	–	1.7	–	1.1	(0.3)	(11.1)
2 - 5 years	(44.3)	0.2	(0.8)	3.5	0.1	3.4	(1.1)	(39.0)
5 - 10 Years	(32.9)	0.8	–	3.9	–	23.3	(13.0)	(17.9)
10 - 15 Years	(13.0)	1.6	–	–	–	17.5	(8.8)	(2.7)
15 – 20 years	–	(6.7)	–	–	–	–	–	(6.7)
	(117.2)	(4.1)	(0.8)	14.2	0.3	46.4	(23.4)	(84.6)

d) Inflation risk

The Group's parent company, Severn Trent Water, operates under a regulatory environment where its prices are linked to inflation measured by RPI. Its operating profits and cash flows are therefore exposed to changes in RPI. In order to mitigate and partially offset this risk, Severn Trent Water has raised debt which pays interest at a fixed coupon based on a principal amount that is adjusted for the change in RPI during the life of the debt instrument (index-linked debt). The amount of index-linked debt at the balance sheet date is shown in section a) (i) interest rate risk, and the estimated future cash flows relating to this debt are shown in section c) (ii) cash flows from non-derivative financial instruments.

Inflation rate sensitivity analysis

The finance cost of the Group's index-linked debt instruments varies with changes in RPI rather than interest rates. The sensitivity at 31 March of the Group's profit and equity to reasonably possible changes in RPI is set out in the following table. This analysis relates to financial instruments only and excludes any RPI impact on Severn Trent Water's revenues and Regulated Capital Value, or accounting for defined benefit pension schemes.

	2019		2018	
	+1.0%	**-1.0%**	+1.0%	-1.0%
	£m	**£m**	£m	£m
Profit or loss	**(11.3)**	**11.3**	(11.8)	11.8
Equity	**(11.3)**	**11.3**	(11.8)	11.8

34 Hedge accounting – Group

The Group uses derivative financial instruments to hedge exposures to changes in exchange rates and interest rates. Hedge accounting is adopted for such instruments where the criteria set out in IFRS 9 are met.

a) Fair value hedges

(i) Cross currency swaps

The Group raises debt denominated in currencies other than sterling. Cross currency swaps are entered into at the time that the debt is drawn down to swap the proceeds into sterling debt bearing interest based on LIBOR in order to mitigate the Group's exposure to exchange rate fluctuations. Where the terms of the receivable leg of the swap closely match the terms of the underlying debt, the swaps are expected to be effective hedges.

At the year end the amounts of cross currency swaps designated as fair value hedges were as follows:

	Notional		Fair Value	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Euro	**11.4**	11.4	**10.1**	10.4
US dollar	**23.2**	–	**0.3**	–
Yen	**8.5**	8.5	**8.8**	8.3
	43.1	19.9	**19.2**	18.7

b) Cash flow hedges

The Group has entered into interest rate swaps under which it has agreed to exchange the difference between fixed and floating interest rate amounts calculated on agreed notional principal amounts. Such contracts enable the Group to mitigate the risk of changing interest rates on future cash flow exposures arising from issued variable rate debt. Where the hedge is expected to be highly effective these interest rate swaps are accounted for as cash flow hedges.

Details of interest rate swaps that have been accounted for as cash flow hedges are summarised below:

	Average contract fixed interest rate		Notional principal amount		Fair Value	
	2019	2018	**2019**	2018	**2019**	2018
Period to maturity	**%**	%	**£m**	£m	**£m**	£m
5-10 years	**1.70**	1.73	**100.0**	100.0	**(3.7)**	(0.9)
10-20 years	**1.80**	1.83	**298.0**	298.0	**(14.8)**	(5.0)
	1.80	1.80	**398.0**	398.0	**(18.5)**	(5.9)

The Group has entered into a series of energy swaps under which it has agreed to exchange the difference between fixed and market prices of electricity at six-monthly intervals up to March 2020.

Details of energy swaps that have been accounted for as cash flow hedges are summarised below:

	Average contract fixed interest rate		Notional principal amount		Fair Value	
	2019	2018	**2019**	2018	**2019**	2018
Period to maturity	**£/MWh**	£/MWh	**MWh**	MWh	**£m**	£m
Less than 1 year	**48.6**	47.6	**21,955**	43,680	**0.1**	0.2
1-2 years	**44.7**	48.6	**372,240**	21,955	**2.0**	–
2-5 years	**43.7**	40.5	**788,280**	547,460	**2.7**	(0.7)
5-10 years	**47.7**	–	**43,680**	–	**0.1**	–
	44.2	41.3	**1,226,155**	613,095	**4.9**	(0.5)

35 Share based payment – Group

The Group operates a number of share based remuneration schemes for employees. During the period, the Group recognised total expenses of £8.0 million (2018: £6.8 million) related to equity settled share based payment transactions.

The weighted average share price of Severn Trent Plc during the period was £19.27 (2018: £21.25).

At 31 March 2019, there were no options exercisable (2018: none) under any of the share based remuneration schemes.

a) Long Term Incentive Plans ('LTIPs')

Under the LTIPs, conditional awards of shares may be made to executive directors and senior staff. Awards are subject to performance conditions and continued employment throughout the vesting period.

Awards outstanding

The awards are subject to Severn Trent Water's achievement of Return on Regulated Equity in excess of the level included in the Severn Trent Water AMP6 business plan over a three year vesting period. It has been assumed that performance against the LTIP non-market conditions will be 100% (2018: 100%).

Details of changes in the number of awards outstanding during the year are set out below:

	Number of awards
Opening at 1 April 2017	487,409
Granted during the year	200,615
Vested during the year	(126,356)
Lapsed during the year	(19,435)
Outstanding at 1 April 2018	542,233
Granted during the year	272,057
Vested during the year	(155,989)
Lapsed during the year	(36,331)
Outstanding at 31 March 2019	**621,970**

Details of LTIP awards outstanding at 31 March were as follows:

		Number of awards	
Date of grant	Normal Date of vesting	**2019**	2018
July 2015	2018	**-**	156,940
July 2016	2019	**172,089**	184,678
July 2017	2020	**181,071**	200,615
July 2018	2021	**268,810**	-
		621,970	542,233

b) Employee Sharesave Scheme

Under the terms of the Sharesave Scheme, the Board may grant the right to purchase ordinary shares in Severn Trent Plc to those employees who have entered into an HMRC approved Save As You Earn contract for a period of three or five years.

35 Share based payment – Group (continued)

Options outstanding

Details of changes in the number of options outstanding during the year are set out below:

	Number of share options	Weighted average exercise price
Outstanding at 1 April 2017	3,027,207	1,572p
Granted during the year	1,058,944	1,652p
Forfeited during the year	(42,224)	1,636p
Cancelled during the year	(130,418)	1,665p
Exercised during the year	(418,806)	1,306p
Lapsed during the year	(8,557)	1,367p
Outstanding at 1 April 2018	3,486,146	1,625p
Granted during the year	1,296,107	1,474p
Forfeited during the year	(55,181)	1,663p
Cancelled during the year	(397,597)	1,654p
Exercised during the year	(709,042)	1,532p
Lapsed during the year	(6,000)	1,575p
Outstanding at 31 March 2019	**3,614,433**	1,585p

Sharesave options outstanding at 31 March were as follows:

			Number of awards	
Date of grant	**Normal date of exercise**	**Option price**	**2019**	2018
January 2013	2016 or 2018	1,241p	**–**	108,034
January 2014	2017 or 2019	1,331p	**142,790**	148,805
January 2015	2018 or 2020	1,584p	**224,136**	831,411
January 2016	2019 or 2021	1,724p	**538,380**	603,931
January 2017	2020 or 2022	1,663p	**641,211**	759,196
January 2018	2021 or 2023	1,652p	**783,709**	1,034,769
January 2019	2022 or 2024	1,474p	**1,284,207**	–
			3,614,433	3,486,146

35 Share based payment – Group (continued)

c) Fair value calculations

The fair values of the share awards made and share options granted during the year were calculated using the Black Scholes method. The principal assumptions and data are out below:

	2019			2018		
	LTIP	**SAYE**		LTIP	SAYE	
		3 year scheme	**5 year scheme**		3 year scheme	5 year scheme
Share price at grant date (pence)	**1,884**	**1,849**	**1,849**	2,341	2,138	2,138
Option life (years)	**3**	**3.5**	**5.5**	3	3.5	5.5
Vesting period (years)	**3**	**3**	**5**	3	3	5
Expected volatility (%)	**18.2**	**18.2**	**18.2**	18.2	18.2	18.2
Expected dividend yield (%)	**4.0**	**4.0**	**4.0**	4.1	4.1	4.1
Risk free rate (%)	**n/a**	**0.6**	**0.8**	n/a	0.5	0.8
Fair value per share (pence)	**1,866**	**303**	**284**	2,328	375	351

Expected volatility is measured over the three years prior to the date of grant of the awards or share options. Volatility has been calculated based on historical share price movements.

The risk free rate is derived from yields at the grant date of gilts of similar duration to the awards or share options.

The dividend yield is calculated using the expected dividend for the year divided by the share price at the date of grant.

36 Acquisitions – Group

On 15 February 2017, Severn Trent Water Limited acquired 100% of the issued share capital of Dee Valley Group Plc comprising all subsidiaries including the regulated water company Dee Valley Water Limited. This acquisition was made through a scheme of arrangement including cash consideration of £79.0 million and the issue of loan notes with a value of £5.2 million.

The acquisition was accounted for using the acquisition method. Goodwill of £66.0m was capitalised attributable to the anticipated future synergies and outperformance arising as a result of the acquisition. The goodwill valuation was based on management's best estimates of the fair values of the assets and liabilities acquired. Given the proximity to the year end, full detailed fair value exercises were not able to be completed before the approval of the financial statements for the year ended 31 March 2017.

The fair value exercises were completed in the prior year and resulted in the revisions to the provisional fair values as set out in the following table.

	2018 £m
Goodwill recognised at 1 April 2017 based on provisional fair values	66.0
Additional consideration in respect of acquisition	0.2
Adjustments to provisional fair values for:	
Recognition of Dee Valley Water Limited's Instrument of Appointment	(4.3)
Revisions to estimated fair value of property, plant and equipment	(0.8)
Deferred tax on changes in fair value	1.1
Goodwill recognised at 31 March 2018 based on final fair values	**62.2**

Details of the adjustments made to the provisional fair values are set out below.

Dee Valley Water Limited holds an Instrument of Appointment as a water undertaker under the Water Act 1989 issued by the Secretary of State for Wales (the Licence). The Licence has no fixed term and requires 25 year's notice of termination. Under the Licence, Dee Valley Water Limited has an exclusive right to supply water to household and non-household customers within a geographic area defined in the licence. On 23 March 2018 Ofwat announced that it had agreed to vary the terms of the Licence with effect from 1 July 2018 to amend the geographic area to include those parts of Wales previously served by Severn Trent Water and to exclude certain parts of England previously served by Dee Valley Water.

Water undertakers are subject to a framework of economic regulation operated by the Water Services Regulation Authority (Ofwat). Under this framework water undertakers are permitted to set wholesale tariffs that would enable an efficient company to earn a post-tax return on a notional amount known as the Regulatory Capital Value (RCV). They are also allowed to earn a net margin on their retail costs. Ofwat sets the post-tax return at a rate that it considers to be the weighted average cost of capital for companies operating in the sector based on an assumed gearing level. Therefore the Licence, together with the net operating assets, enables Dee Valley Water Limited to earn post-tax returns with a net present value equivalent to the RCV plus a net return on retail activities.

To determine the fair value of the licence we have taken the RCV at 31 March 2017 from Ofwat's Final Price Control Determination published in December 2014 adjusted to current prices at the acquisition date, added an allowance for the value of the Retail business and compared this with the fair value of the operating assets acquired. This resulted in a valuation of £4.3 million for the licence.

The goodwill acquired represents future outperformance of the regulatory settlement and synergies arising from the combination of the group's regulated water businesses.

37 Discontinued operations

Water Plus joint venture

On 1 March 2016 the Group announced its intention, subject to approval from the Competition and Markets Authority ('CMA'), to enter into a joint venture with United Utilities PLC to compete in the non-household water and waste water retail markets in Great Britain. On 3 May 2016 the CMA announced approval of the joint venture. On this date the Group determined that completion of the proposed transaction became highly probable and the non-household retail business was classified as a disposal group and a discontinued operation with effect from this date.

During the prior year, the Group wrote off the remaining balance on the non-household retail receivable amounts that were retained when that business was transferred to Water Plus. An additional £1.5 million was charged to operating costs in discontinued operations in respect of this.

The results of discontinued operations are disclosed separately in the income statement.

The loss for the year from discontinued operations was as follows:

	2019	2018
	£m	£m
Turnover	**–**	–
Total operating costs	**–**	(1.5)
Loss before tax	**–**	(1.5)
Attributable tax credit	**–**	0.3
Loss for the year	**–**	(1.2)

The Group and Company did not dispose of any assets during this disposal.

The net cash flows arising from the disposal groups were as follows:

	2019	2018
	£m	£m
Cash flow from operating activities	**–**	–

The Group and Company did not recognise any cash flows from the disposal.

38 Cash flow statement

a) Reconciliation of operating profit to operating cash flows

	Group		Company	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Profit before interest and tax from continuing operations	**557.7**	525.1	**559.7**	519.4
Loss for the year from discontinued operations	**–**	(1.2)	**–**	(1.2)
Profit before interest and tax	**557.7**	523.9	**559.7**	518.2
Depreciation of property, plant and equipment	**309.3**	304.0	**303.2**	297.9
Amortisation of intangible assets	**29.0**	19.8	**28.3**	19.8
Pension service cost	**9.6**	(7.8)	**9.2**	(8.3)
Defined benefit pension scheme administration costs	**2.3**	1.8	**2.1**	1.6
Exceptional impairment - fixed assets	**–**	16.8	**–**	16.8
Defined benefit pension scheme contributions	**(34.5)**	(33.8)	**(12.0)**	(9.3)
Share based payments charge	**8.0**	6.8	**7.8**	6.8
Profit on sale of property, plant and equipment and intangible assets	**(10.6)**	(4.6)	**(10.6)**	(4.4)
Deferred income movement	**(14.5)**	(14.3)	**(14.1)**	(14.1)
Provisions charged to the income statement	**10.5**	12.1	**10.5**	12.1
Utilisation of provisions for liabilities and charges	**(9.2)**	(4.1)	**(9.2)**	(4.1)
Operating cash flows before movements in working capital	**857.6**	820.6	**874.9**	833.0
Increase in inventory	**(3.0)**	(0.9)	**(3.0)**	(0.9)
(Increase)/decrease in amounts receivable	**(42.4)**	(36.7)	**(64.9)**	(51.1)
Increase/(decrease) in amounts payable	**(3.3)**	5.0	**13.9**	18.5
Cash generated from operations	**808.9**	788.0	**820.9**	799.5
Tax paid	**(20.9)**	(14.9)	**(19.0)**	(13.0)
Net cash generated from operating activities	**788.0**	773.1	**801.9**	786.5

b) Non-cash transactions

No additions to property, plant and equipment during the year were financed by new finance leases (2018: nil). Assets transferred from developers at no cost were recognised at their fair value of £41.4 million (2018: £35.6 million).

c) Exceptional cash flows

	Group and company	
	2019	2018
	£m	£m
Disposal of fixed assets	**–**	11.0
Costs of pension exchange arrangement	**–**	(0.7)
	–	10.3

38 Cash flow statement (continued)

d) Reconciliation of movement in cash and cash equivalents to movement in net debt

Group

	As at 1 April 2018	Cash flow	Fair value adjustments	RPI uplift on index-linked debt	Foreign exchange	Other non-cash movements	**As at 31 March 2019**
	£m	£m	£m	£m	£m	£m	**£m**
Net cash and cash equivalents	3.7	8.4	–	–	–	–	**12.1**
Loans receivable/(payable) with parent company	(9.3)	89.9	–	–	–	–	**80.6**
Bank loans	(1,182.1)	100.0	–	(2.9)	–	(1.0)	**(1,086.0)**
Other loans	(4,138.2)	(552.0)	1.6	(32.3)	(8.0)	(3.4)	**(4,732.3)**
Finance leases	(113.9)	2.2	–	–	–	–	**(111.7)**
Cross currency swaps	24.5	–	12.6	–	–	–	**37.1**
Loans due from joint ventures	99.8	–	–	–	–	0.2	**100.0**
Net debt	**(5,315.5)**	**(351.5)**	**14.2**	**(35.2)**	**(8.0)**	**(4.2)**	**(5,700.2)**

Liabilities from financing activities comprise bank loans, other loans and finance leases.

Company

	As at 1 April 2018	Cash flow	Fair value adjustments	RPI uplift on index-linked debt	Foreign exchange	Other non-cash movements	**As at 31 March 2019**
	£m	£m	£m	£m	£m	£m	**£m**
Net cash and cash equivalents	0.4	11.0	–	–	–	–	**11.4**
Loans receivable from other group companies	62.4	99.5	–	1.8	–	(34.0)	**129.7**
Loans payable to other group companies	(4,015.9)	(237.0)	–	(32.3)	–	(1.9)	**(4,287.1)**
Bank loans	(1,182.1)	100.0	–	(2.9)	–	(1.0)	**(1,086.0)**
Other loans	(567.5)	(322.2)	1.6	–	(8.0)	(1.3)	**(897.4)**
Finance leases	(167.3)	18.9	–	–	–	–	**(148.4)**
Intercompany finance leases payable	(199.1)	3.3	–	–	–	–	**(195.8)**
Intercompany finance leases receivable	99.1	(0.6)	–	–	–	–	**98.5**
Cross currency swaps	24.5	–	12.6	–	–	–	**37.1**
Loans due from joint ventures	99.8	–	–	–	–	0.2	**100.0**
Net debt	**(5,845.7)**	**(327.1)**	**14.2**	**(33.4)**	**(8.0)**	**(38.0)**	**(6,238.0)**

Liabilities from financing activities comprise bank loans, other loans and finance leases.

39 Contingent liabilities – Group and Company

a) Bonds and guarantees

Group undertakings have entered into bonds and guarantees in the normal course of business. No liability (2018: £nil) is expected to arise in respect of either bonds or guarantees.

b) Banking arrangements

The banking arrangements of the Group operate on a pooled basis with certain fellow group undertakings. Under these arrangements participating companies guarantee each other’s balances only to the extent that their credit balances can be offset against overdrawn balances of other Severn Trent group companies.

At 31 March 2019 the Group's maximum liability under these arrangements was £nil million (2018: £nil million).

At 31 March 2019 the Company's maximum liability under these arrangements was £nil million (2018: £nil million).

40 Financial and other commitments – Group and Company

a) Investment expenditure commitments

Capital commitments are as follows:

	2019 £m	2018 £m
Contracted for but not authorised in the financial statements	**359.2**	395.0

In addition to these contractual commitments, the Group and Company have longer term expenditure plans which include investments to achieve improvements in performance mandated by the Director General of Water Services (Ofwat) and to provide for growth in demand for water and waste water services.

b) Leasing commitments

At the balance sheet date the Group and Company had outstanding commitments for future minimum operating lease payments under non-cancellable operating leases, which fall due as follows:

	2019 £m	2018 £m
Within 1 year	**1.7**	1.1
1 - 5 years	**2.2**	2.2
After more than 5 years	**5.3**	4.2
	9.2	7.5

Operating lease payments represent rentals payable by the Group for certain of its office properties, plant and equipment.

41 Post balance sheet events – Group and Company

There are no post balance sheet events.

42 Related party transactions – Group and Company

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not included in this note. Transactions between the Group, joint ventures and ultimate parent Severn Trent Plc are disclosed below.

Trading transactions

	Transactions with fellow subsidiary undertakings		Transactions with ultimate parent		Transactions with joint ventures	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
Sale of services	**4.7**	3.5	**–**	–	**335.0**	354.9
Purchase of services	**2.3**	5.6	**1.7**	1.5	**–**	–
Net interest income	**–**	–	**(1.4)**	0.1	**3.8**	2.2
	7.0	9.1	**0.3**	1.6	**338.8**	357.1
Balances outstanding at 31 March:						
Amounts due from related parties	**8.0**	5.4	**2.0**	3.0	**2.3**	44.9
Amounts due to related parties	**(0.2)**	(2.0)	**(0.1)**	(15.6)	**–**	–
Loans due from related parties > 1 year	**–**	–	**80.6**	–	**100.0**	99.8
Loans due to related parties	**–**	–	**–**	(9.3)	**–**	–
Dividends payable to related parties	**225.1**	204.0	**–**	–	**–**	–
	232.9	207.4	**82.5**	(21.9)	**102.3**	144.7

The related parties are fellow subsidiary undertakings and the ultimate parent Severn Trent Plc.

42 Related party transactions – Group and Company (continued)

Remuneration of key management personnel

Key management personnel comprise the members of STEC during the year.

The remuneration of the Directors is included within the amounts disclosed below.

	2019 £m	2018 £m
Short term employee benefits	**6.5**	6.4
Post-employment benefits	**–**	–
Share based payments	**2.9**	3.5
	9.4	9.9

The retirement benefit schemes entered into by the Group are considered to be related parties. Details of transactions and balances with the retirement benefit schemes are disclosed in note 27.

43 Alternative performance measures – Group

Financial measures or metrics used in this report that are not defined by IFRS are alternative performance measures ('APMs'). The Group uses such measures for performance analysis because they provide additional useful information on the performance and position of the Group. Since the Group defines its own alternative performance measures, these might not be directly comparable with other companies' alternative performance measures. These measures are not intended to be a substitute for, or superior to, IFRS measurements.

a) Exceptional items

Exceptional items are income or expenditure which individually or, if of a similar type, in aggregate should, in the opinion of the directors, be disclosed by virtue of their size or nature if the financial statements are to give a true and fair view. In this context, materiality is assessed at the segment level.

b) Underlying PBIT

Underlying profit before interest and tax is profit before interest and tax excluding exceptional items as recorded in the income statement. This provides a consistent measure of operating performance excluding distortions caused by exceptional items.

c) Net debt

Net debt comprises borrowings including remeasurements for changes in fair value of amounts in fair value hedging relationships, cross currency swaps that are used to fix the sterling liability of foreign currency borrowings (whether hedge accounted or not), net cash and cash equivalents, and loans to joint ventures. See note 38.

d) Effective interest rate

The effective interest rate is calculated as net finance costs, excluding net finance costs from pensions, plus capitalised finance costs divided by the monthly average net debt during the year.

$$\frac{\textit{(net finance costs – net finance costs from pensions + capitalised finance costs)}}{\textit{(monthly average net debt)}}$$

	2019 £m	2018 £m
Net finance costs	**188.8**	215.9
Net finance costs from pensions	**(13.6)**	(15.2)
Capitalised interest	**31.6**	24.6
	206.8	225.3
Average net debt	**5,486.7**	5,085.2
Effective interest rate	**3.8%**	4.4%

This APM is used as it shows the average interest rate that is attributable to the average net debt of the business.

43 Alternative performance measures – Group (continued)

e) Effective cash cost of interest

The effective cash cost of interest is calculated on the same basis as the effective interest rate except that it excludes finance costs that are not paid in cash but are accreted to the carrying value of the debt (principally RPI adjustments on index-linked debt).

$$\frac{\text{net finance costs} - \text{net finance costs from pensions} - \text{RPI interest} + \text{capitalised finance costs}}{\text{monthly average net debt}}$$

	2019 **£m**	2018 £m
Net finance costs	**188.8**	215.9
Net finance costs from pensions	**(13.6)**	(15.2)
RPI interest	**(35.2)**	(51.2)
Capitalised interest	**31.6**	24.6
	171.6	174.1
Average net debt	**5,486.7**	5,085.2
Effective cash cost of interest	**3.1%**	3.4%

This is used as it shows the average cash interest rate based on the net debt of the business.

f) PBIT interest cover

The ratio of profit from continuing operations before interest, tax and exceptional items to net finance costs excluding net finance costs from pensions.

$$\frac{\text{Underlying PBIT}}{\text{net finance costs} - \text{net finance costs from pensions}}$$

	2019 **£m**	2018 £m
Underlying PBIT	**567.3**	537.7
Net finance costs	**188.8**	215.9
Net finance costs from pensions	**(13.6)**	(15.2)
Net finance costs excluding finance costs from pensions	**175.2**	200.7

	ratio	ratio
PBIT interest cover ratio	**3.2**	2.7

This is used to show how the underlying PBIT of the business covers the financing costs associated only with net debt on a consistent basis.

43 Alternative performance measures – Group (continued)

g) EBITDA and EBITDA interest cover

The ratio of profit from continuing operations before interest, tax, exceptional items, depreciation and amortisation to net finance costs excluding net finance costs from pensions.

$$\frac{\textit{(underlying PBIT + depreciation + amortisation)}}{\textit{(net finance costs – net finance costs from pensions)}}$$

	2019 £m	2018 £m
Underlying PBIT	**567.3**	537.7
Depreciation	**309.3**	304.0
Amortisation	**29.0**	19.8
EBITDA	**905.6**	861.5
Net finance costs	**188.8**	215.9
Net finance costs from pensions	**(13.6)**	(15.2)
Net finance costs excluding finance costs from pensions	**175.2**	200.7
	ratio	ratio
EBITDA interest cover ratio	**5.2**	4.3

This is used to show how the EBITDA of the business covers the financing costs associated only with net debt on a consistent basis.

h) Underlying effective current tax rate

Current tax charge for the year on continuing operations, excluding prior year charges, exceptional current tax, and current tax on exceptional items and on financial instruments, divided by profit from continuing operations before tax, net gains/losses on financial instruments, exceptional items and share of net profit of joint ventures accounted for using the equity method.

$$\frac{\textit{(Current year current tax charge in the income statement – tax on exceptional items – tax on financial instruments)}}{\textit{(PBT – share of net profit of JVs – exceptional items – net losses on financial instruments)}}$$

	2019	**Current tax thereon**	2018	Current tax thereon (restated)
	£m	**£m**	£m	£m
Profit before tax	**425.2**	**(40.2)**	302.0	(37.4)
Adjustments:				
Exceptional items	**9.6**	**–**	12.6	(0.7)
Net gains on financial instruments	**(37.7)**	**(2.6)**	(11.4)	(3.3)
	397.1	**(42.8)**	303.2	(41.4)
Underlying effective current tax rate		**11.3%**		13.7%

44 Ultimate parent undertaking

The immediate parent undertaking is Severn Trent Draycote Limited.

The ultimate parent undertaking and controlling party is Severn Trent Plc, which is the parent undertaking and controlling party of the smallest and largest group to consolidate these financial statements. Copies of the Severn Trent Plc consolidated financial statements can be obtained from Severn Trent Plc's registrars at Equiniti, Aspect House, Spencer Road, Lancing, West Sussex, BN99 6DA.