

Registered N<sup>o</sup>: 2366777

# Dŵr Cymru Cyfyngedig

Annual report and financial statements  
for the year ended 31 March 2023

Registered office

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## Directors and advisers

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### Directors

A Lyons	Chairman	
P Perry	Chief Executive Officer	
M Davis	Chief Financial Officer	
G Edwards	Non-executive Director	
J Kenrick	Non-executive Director	
T Crick	Non-executive Director	
D Bowen Rees	Non-executive Director	
J Hanson	Non-executive Director	
B Moorhouse	Non-executive Director	(appointed 16 <sup>th</sup> January 2023)
L Thompson	Non-executive Director	(appointed 6 <sup>th</sup> September 2022)

### Company Secretary

Nicola Foreman	(appointed 6 February 2023)
Nicola Williams	(resigned 6 February 2023)

### Independent auditor

KPMG LLP  
Assembly Square  
3 Britannia Quay  
Cardiff  
CF10 4AX

### Solicitor

Linklaters LLP  
One Silk St  
London  
EC2Y 8HQ

### Principal banker

National Westminster Bank Plc  
27 High St  
Brecon  
LD3 7LF

# Strategic report

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The Directors present the Strategic report of Dŵr Cymru Cyfyngedig for the year ended 31 March 2023.

## Principal activities

The principal activities of the Company are the supply of water and the treatment and disposal of wastewater under the Instrument of Appointment made by the Secretary of State for Wales under the Water Act 1989.

## Business review

The Company is in a strong financial position as at 31 March 2023; gearing remains low and one of the market leaders at 58% (2022: 58%) and we have retained our sector-leading credit ratings.

### Revenue:

Our revenue mainly comes from the water and wastewater services we provide to customers. Our prices are set every five years by Ofwat's price review process and this, to a large extent, determines how much we can invest in our services and infrastructure. Revenue in the year was 4% higher than last year, mainly due to price rises, which were in line with Ofwat's allowance but notably well below headline inflation in the period, partly offset by a £15 million reduction in respect of our restatements for leakage and Per Capita Consumption (PCC) data.

We are acutely aware of the pressures the current cost-of-living crisis is having on our customers. We continue to expand our range of customer assistance tariffs, with 127,000 customers now getting help to pay their bills.

### Operating Expenditure (Opex)

100% of our cost base relates to regulated activity and is therefore funded as set out in Ofwat's price determination. In this way, inflationary increases are also funded, although there is a timing difference as costs are reflected in customer bills the year after the higher costs are incurred.

### *Energy*

Our high levels of energy consumption have exposed us to the recent volatility in wholesale energy prices, although this has been partly mitigated by our power hedging policy and our self-generation capability. A combination of forward purchases, derivatives and exporting to grid of our self generated electricity typically sees us around 90% hedged on electricity costs at the start of each financial year. Our electricity bill for the year was £69 million but it would have been up to £155 million without hedging and our own renewable generation.

In early 2020, we forward purchased around 60% of our gas requirement for the five years to March 2025. The remainder is hedged by the export of biomethane from our gas-to-grid plant. We continue to invest to increase our capacity to generate our own energy and in the year we produced 22% of our total consumption requirement. We aim to increase this to 35% by 2025. While we have mitigated much of the cost pressure to date, we have paused power hedging activity while underlying prices, and the costs of hedging, are high. We are currently reviewing our purchasing strategy for the next price review period to 2030.

### *Bad debt*

Bad debt charges result from customers not paying their bills, because they are either unwilling or unable to do so. We offer a broad range of assistance to customers struggling to pay their bills, but it is inevitable that some of the bills we raise will not be paid.

Bad debt charges rose by 4% year-on-year to £25 million. The main driver was a price increase to our revenue (see 'Revenue' above). Our bad debt provision includes an estimate of the future effects of the cost-of-living crisis on the collection of debt outstanding at the year-end, equivalent to a further 1% fall in collections.

To help us focus on the challenges the current macro-economic environment poses to our customers, we monitor closely a set of measures, including:

- The proportion of customers paying by direct debit.
- The number of customers we actively monitor on our debt management system.
- The percentage of customers on track with payment terms.
- The volume and value of receipts in advance.

These indicators have remained strong throughout the past year and we do not anticipate any significant deterioration in the short term. Our bad debt as a proportion of our revenue remained stable at c.3%.

## Strategic report (continued)

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### Exceptional items

In the year to 31 March 2023, we have recognised an exceptional item totalling £30.8 million. This item represents the award of pension increases above a 5% cap. Under a 'best endeavours' clause in our pension scheme rules full RPI increases could only be awarded if certain criteria were met. In the current year scheme awards above a 5% cap have been paid by the pension scheme and, as the scheme is now in surplus, these conditions are expected to be paid in the future. Therefore, the expense in the year represents the additional awards given. In the future it is expected that changes to this assumption will be presented in Other Comprehensive Income as required under IAS19. This is disclosed as exceptional in this year as the accounting treatment of these increases through the profit and loss account will only occur this year, it is of a significant value, and it does not closely reflect day-to-day operational expenditure. For the avoidance of doubt management will make consideration of the 'best endeavours' clause in all future periods and as such any movement in estimate will be presented as Other Comprehensive Income as required under IAS19.

In the year to 31 March 2022 we have recognised an exceptional item totalling £(3.8) million. This item represents a release of the bad debt provision as a result of anticipated bad debt charges associated with the Covid-19 pandemic not materialising during the year; this is disclosed as exceptional due to its nature and with the corresponding Covid-19 charge having, in the previous year, been shown as exceptional.

### Climate change

Climate change is having a significant effect on our business. In recent years, we have experienced extreme weather events which have had a material detrimental effect on our operations and required significant remedial expenditure. During the summer of 2022, the warmest since 1976, our operating area experienced a prolonged period of hot, dry weather. It meant we had to impose a temporary hosepipe ban in parts of Pembrokeshire and a small area of Carmarthenshire. We had to spend more on tankering and redoubled our efforts to minimise leakage at a total outsourced cost of £42 million this year. During winter, we also experienced a freeze-thaw event which led to additional maintenance costs and compensation of £3 million to customers for supply interruptions.

### Leakage and per capita consumption restatement

We have restated performance data for leakage and PCC which was reported to Ofwat for the financial years 2021 and 2022. On 25 May 2023, Ofwat announced an investigation into our reporting of leakage and PCC. We have informed Ofwat that we intend to action a customer redress package of £29 million, representing approximately 3.7% of Welsh Water's regulatory revenue of £793 million in 2021-22.

The redress package consists of two elements:

- Customer rebates of £15 million to be credited to customers' accounts as soon as possible in 2023-2024. With 1.4 million customers, the rebate will amount to just over £10 per customer.
- We have proposed that at PR24 we will voluntarily forego recovery of that element of regulatory overspend during 2020-21 and 2021-22 that is attributable to leakage expenditure. This amounts to £14 million.

In this year's financial statements, we have provided for the £15 million to be refunded to customers in 2023-24. The forgone overspend recovery of £14 million will manifest itself in a lower Regulatory Capital Value (RCV) at 1 April 2025 than would otherwise be the case. As it is not appropriate to set a provision in the financial statements for future changes to RCV, this element of the customer redress package is disclosed only in the notes to the financial statements.

We believe we are proposing an appropriate package of customer redress for our regulatory misreporting 2020-21 and 2021-22, and its effects. However, the final decision rests with Ofwat and will not be known until their investigation is completed, the timing of which is uncertain.

Under normal circumstances, overspends during the AMP are partially recovered from customers at the next price control through an adjustment to the Regulated Capital Value (RCV). This would ordinarily allow 42% - amounting to £14 million - of this overspend to be recovered. The decision has been taken to forego these recoverable costs and the regulatory capital value will not be uplifted at the next Price Control.

Furthermore, we now expect to spend an additional £54 million in the remaining two years of the AMP (2024- 2025) to reduce leakage as quickly as possible.

## Strategic report (continued)

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### Interest rate management

Our primary financing objective is to secure the right amount of funding at the lowest cost. The more efficient our funding, the lower our customers' bills. We aim to have sector-leading credit ratings and gearing at around 60%, as well as considering the timing of financing activity.

Just over half of our debt, on a pre-hedged position, is index-linked to RPI inflation (31 March 2023: 54%, 31 March 2022: 51%) and this provides a natural hedge to our asset base (as measured by Ofwat's regulatory capital value) and our inflation-linked revenues. Including the impact of inflation, our average cost of debt for the year was 7.7% (2022: 5.0%).

### Gains and losses on derivative financial instruments

We manage our interest rate exposure using derivative financial instruments. We have also swapped some of our floating-rate debt to fixed-rate debt and some of our fixed-rate debt to index-linked rates using 'swaps.' After taking into account the effect of these swaps, 84% of our debt is index-linked, with the remainder at a floating or fixed rate. We also use derivatives to hedge the cost of some of our power requirements. We do not undertake any speculative trading, which is specifically prohibited under our Treasury policy established by the Board.

Unlike debt, which is included in 'borrowings' in the balance sheet, our swaps are classified as 'derivative financial instruments' under International Financial Reporting Standards and valued at fair market value at the balance sheet date. Fair values fluctuate in line with market movements, which can be volatile, and this can give rise to significant gains and losses in the income statement.

In the year the movement in the value of swaps was a non-cash gain of £115.4 million (2022: loss of £80.4 million), driven mainly by changing market expectations of interest

### Loss before tax:

The Loss before tax was £383 million, a decrease of £268 million on last year (2022: £115 million), as a result of the factors outlined above.

### Taxation:

We aim for compliance and transparency in our tax affairs and hold the Fair Tax Mark accreditation. As an organisation with a large capital investment programme, we receive capital allowances. These have the effect of deferring some of our corporation tax liabilities to future periods and help to keep customers' bills lower.

Full details of our corporation tax and deferred tax charges are provided in note 5 and our full tax strategy is available at <https://corporate.dwrcymru.com/en/library/company-statements/tax-strategy>.

### Group tax strategy:

The tax strategy is managed at a group level by the Glas Cymru Holdings Cyfyngedig Group (GCHC). The Group is committed to acting in an open and transparent way in respect of its tax affairs. We pay a range of taxes, including business rates, employer's National Insurance and environmental taxes. We do not enter into artificial tax arrangements, use tax havens or take an aggressive stance in the interpretation of tax legislation. Full details of our tax strategy are published annually on our website at [dwrcymru.com/tax-strategy](https://dwrcymru.com/tax-strategy). The Group has complied with the Tax Strategy for the year ended 31 March 2023.

### Fair tax mark accreditation:

The Fair Tax Mark is an independent certification which recognises organisations that demonstrate they are paying the right amount of corporation tax at the right time and in the right place. More than 75 businesses have now been certified since the accreditation was launched in 2014. We aim for clarity and transparency in our tax strategy and are pleased to have been the first Welsh company to have secured the Fair Tax Mark accreditation.

## Strategic report (continued)

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### Pension funding:

Dŵr Cymru's defined benefit pension asset at 31 March 2023 as reported on the balance sheet was £12 million, a £93 million increase on last year (2022: £81 million liability). This valuation has been prepared in accordance with the IAS 19 basis for accounting purposes which is not the same as the actuarial valuation of the scheme used for funding purposes. The difference between the two amounts is recognised as a surplus or obligation in the statement of financial position. Where this difference results in a defined benefit surplus, this is recognised in accordance with IFRIC 14 'IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction', on the basis that the group has an unconditional right to a refund of any surplus that may exist following the full settlement of plan liabilities in a single event.

### Cash flow:

Net cash generated from operating activities for the year ended 31 March 2023 totalled £228 million, which decreased from the £313 million generated in the previous year. The decrease is driven by lower cash generated from operations and higher interest paid.

The net cash outflow from investing activities for the year ended 31 March 2023 was £291 million, which increased from £246 million expended in the previous year. This was principally caused by a higher level of investment in our capital programme.

Net cash outflows from financing activities totalled £78 million, compared with net cash inflow of £228 million last year. The main difference is due to an intercompany loan received of £300 million in the prior year. These were subsequently on-lent to the Company.

### Capital Investment

We invested £400 million of Capital in the year as part of our record £2.0 billion AMP7 planned investment programme.

During the year, we invested a total of £400 million in our water and wastewater assets. Over the five years to 2025, we will invest a record £2.0 billion to deliver improved resilience and environmental improvements in line with Ofwat's 2019 Final Determination and our other regulatory obligations. Our total investment is split between capital additions of £322 million (these are added to the balance sheet and depreciated over the assets' useful lives) and infrastructure renewals expenditure of £78 million (maintenance costs which are fully expensed to the income statement).

We will invest an additional £100 million in river water quality improvements, most of which we plan to deliver during AMP7. This is available to us from the advantage of our Glas Cymru non-shareholder business structure being not-for-profit.

### Net asset position:

The balance sheet shows net assets of £1,546 million at 31 March 2023 (2022: £1,307 million). The net book value of property, plant and equipment has risen by £694 million (11%), a result of revaluing the Company's asset base to Dŵr Cymru's regulatory capital value. Cash balances are £363 million, reflecting the investment in capital described above. The net deferred tax liability has increased by £96 million (14%).

### Going concern:

The Directors are satisfied that the business has adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements for the year ended 31 March 2023 have been prepared on the going concern basis. (Full details are provided under "basis of preparation" in note 1 to the financial statements.)

### **Financial key performance indicators**

The Company is part of a group controlled by Glas Cymru Holdings Cyfyngedig (GCHC, the "group"). The Directors of Dŵr Cymru Cyfyngedig use group-wide key performance measures as indicators to the development, performance and position of the Company. These are discussed in the 2022-23 Annual Report and Accounts of GCHC which does not form part of this report (available on the Group's website at [Corporate Reports](#)).

Customers are at the heart of everything we do. We measure our performance via eight "Outcomes" which are based on broad groupings of targets set by Ofwat at the last price review – "Outcome Delivery Incentives" (ODIs). The groupings represent the key elements of the essential services we provide to our customers across our supply area.

The regulatory targets are supplemented by our internal business and financial planning processes. Every year targets are discussed and agreed by the Board of Directors. The Executive team is held to account by our Non-Executive Directors to ensure that the targets are sufficiently challenging and to monitor performance in accordance with those targets.

Our Company vision to Earn the Trust of our Customers Every Day underpins our approach to delivering services, and the Board is conscious of the need to set targets which maintain and build on that trust.

## Strategic report (continued)

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### Financial key performance indicators (continued)

The Board also takes the opportunity to understand the views expressed by customers and other stakeholders in the extensive engagement exercises undertaken as part of establishing Welsh Water 2050, and in the context of setting the Company's five-year business plans for 2020-25.

### Future developments

Working on our Welsh Water 2050 Strategy for the next 30-year period has allowed us to examine the role we play in the communities we serve and to have a meaningful dialogue with our customers about how we will meet the external challenges over time.

Our detailed business plan for AMP7, 2020-25 seeks to balance ensuring the affordability of the essential services we provide with the investment needed to maintain a resilient infrastructure. All gains eventually go to our customers, so that the interests of the Company and of customers are aligned, and the strategic direction of the Company takes this into account.

As well as delivering excellent service for customers, we need to manage costs carefully to keep bills as affordable as possible. The Board sets the Executive Remuneration policy which includes a significant element of variable pay, dependent on the Executive Directors delivering strong and consistent performance which achieves improved services for customers.

This is reinforced by a focus on transparency and honesty in all communications with our Members, customers and regulators, acknowledging those areas where we can still do better, and building on the progress we have made to deliver better service to customers.

### Principal risks and severity

From the perspective of the Company, the principal risks and uncertainties are integrated with the principal risks of the GCHC group and are not managed separately and are discussed in the 2022-23 Annual Report and Accounts of GCHC. These include:

- Environmental Performance and Reputation;
- Business continuity;
- climate change impacts and transition risks;
- Health and safety major incident;
- Cyber information and operational technology;
- performance and costs;
- Loss of trust, particularly by customer;
- People: talent and diversity;
- Finance risk and customers' ability to pay;

Emerging risks feature in monthly Executive team risk updates to the Board and are discussed in depth by the Board twice each year.

- public health (micropollutants in drinking water and plastics in wastewater); and
- Legislative divergence

The above emerging risks are also discussed in the 2022-23 Annual Report and Accounts of GCHC.

### S172 statement

The Directors are required to act in a manner which complies with their duties as set out in the Companies Act 2006.

The relevant provisions of Section 172 of the Companies Act require a director of a company to act in a way they consider, in good faith, would most likely promote the success of the company. In doing this, the director must have regard to, among other matters:

- the likely consequences of any decision in the long term.
- the interests of the company's employees.
- the need to foster the company's business relationships with suppliers, customers and others.
- the impact of the company's operations on the community and the environment.
- the desirability of the company maintaining a reputation for high standards of business conduct.

Set out below is an overview of how the Board has performed its duties in this regard during the year. For further information, please see the Governance Report on our Group Annual Report.

Engagement with our stakeholders plays a vital role in our decision making, allowing boardroom discussions to consider their interests and the impact on them of our decisions. While we aim to maintain a diverse range of skills, backgrounds, and experiences on the Board, we also value hearing directly from our various stakeholders throughout the year. The Board continues to seek new ways of engaging with the varying perspectives of our Customer and Communities stakeholder groups, including Developer Services and Supplier.



## Strategic report (continued)

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### Customer engagement

The customer voice is represented through the Independent Challenge Group (ICG). Board members attended a Customer Immersion Day in June 2022 to gain insight into our customers' priorities as part of our PR24 preparation, and an online Community Research Forum on the subject of Combined Storm Overflows (CSOs) in March 2023.

### The Board's obligation to promote the long-term success of the company

The potential consequences of decisions in the long term is a natural focus for our long-term investment and planning. As a customer-led business, addressing the long-term impacts on our communities and the environment are absolutely central to our strategy. Delivering that strategy necessarily involves fostering relationships with governments, regulators, suppliers and customers, but it also critically depends on colleagues across the business and in our supply chain.

### Stakeholder engagement

The Board regularly hears directly from our principal stakeholders, including our regulators, through their attendance at Board meetings. The views of regulators are gathered both directly through invitations to join our Board and Quality and Safety Committee (QSC) meetings, and indirectly as regulatory correspondence and meeting details are relayed by members of the Executive team through monthly management reports to the Board.

During 2022-23, the QSC heard directly from some of the Directors of Natural Resources Wales (June 2022) and the Chief Inspector of the Drinking Water Inspectorate (March 2023).

The Chair and Wales Chair of the Consumer Council for Water (CCW) attended the Board's meeting in December 2022.

The Chair, and Chief Executive of Ofwat, together with the Wales Director and the Senior Director of Strategy and Planning, attended the September 2023 Board meeting.

The Board heard directly from the Chair of the Board of Trustees of the pension fund in November 2022.

### Supplier engagement

Supply chain risk is noted as one of the principal strategic risks reviewed at every Board meeting, and the Board receives monthly reports from the Commercial Director, including an update on any procurement or key supplier issues. Board members also meet regularly with representatives of contractors working on our Capital Projects programme when attending site visits helps ensure that the services provided to customers, and the delivery of our investment schemes and the provision of other goods and services, are in line with our expectations and company values. We have a Supplier payment policy and we are a signatory of the UK Government Prompt Payment Code.

### Employee engagement

The Board promotes inclusivity and supports developing each individual to their full potential. Regular updates on health and safety, turnover, absence and sickness levels are received and key policies such as Equality, Diversity and Inclusivity, and pay, are reviewed at the Board or at relevant Committee meetings. There are also regular updates from the Executive on discussions with the recognized trade unions through the Senior Negotiating team and in relation to employee engagement surveys and the action plan agreed by the Executive Team in response to colleague feedback from the survey.

The Chair of the Board and Non-Executive Directors regularly meet with groups of colleagues from all business areas. Notes of the topics discussed at these meetings are taken and shared with other members of the Board. These meetings are typically held remotely, enabling a wider geographic spread of colleagues. Separate meetings are arranged with managers across the business, which have also been held remotely, but during 2023 we restarted holding informal managers' lunches with the Board.

### Engagement with Glas Members

The role of Glas Members is set out in the Governance Report of our Group Annual Report. Our Members are drawn from across the supply area and the independent Member Selection Panel, chaired by Sir Paul Silk, aims to ensure a broad spread of background, skills and experience within the Membership.

Debra Bowen Rees, one of our Non-Executive Directors, is a member of the independent Member Selection Panel and, therefore, takes a particular interest in the Glas Membership.

The Panel carries out an annual recruitment process to refresh the Membership as Members step down (after a maximum 9-year term). The Board meets with Members in July and December each year and welcomes input from Members on key strategic issues at these meetings, where there is always an opportunity for Member feedback and discussion.

The Company Secretariat team ensures that Members are kept up to date on current issues affecting the business on a regular basis, and feeds back Member views in a report to the Board at each Board Meeting.

## Strategic report (continued)

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### Engagement with the independent challenge group

This group comprises customer and environment advocates from a broad variety of backgrounds. It meets regularly to review and comment on customer research, strategy, policy and initiatives. The Chair of the Independent Challenge Group attended the PR24 Customer Insight item on the Board's Strategy Day agenda in November 2022.

### Engagement with the independent environmental advisory panel (IEAP)

This group includes representatives from environmental non-governmental organisations (NGOs), academics and third sector organisations. The independent Environmental Adviser to the Board's Quality and Safety Committee attends meetings of the IEAP, and reports back to the Quality and Safety Committee on issues of relevance to the Committee.

### Engagement with investors

During 2022-23 we held meetings with bond investors via video conference, but in July 2022 we convened our annual Investors Meeting in person. Members of the Board and Executive team attend this meeting and the Treasury team is in regular contact with investors and credit rating agencies throughout the year. All formal communications with investors are approved by the Board, and investors receive a six-monthly Investor Report which they are welcome to follow up on with the Treasury team.

### The role of the executive team

The Dŵr Cymru Executive Team, which includes the Chief Executive and Chief Financial Officer, are responsible for the operational management of the Company. The Team are designated as senior management for the purpose of the UK Corporate Governance Code but not for the purposes of section 414C(8) of the Companies Act 2006. The Executive Team comprises the senior functional management roles and those with responsibility for interacting with the Company's principal stakeholders.

Our Managing Directors for Water, Waste Water and Retail (Household Customers) attend all Board meetings. From 6 February 2023 Nicola Foreman replaced Nicola Williams as Group Company Secretary and as a Member of the Executive Team.

### The role of the Board

The Board oversees measures to ensure that stakeholder interests are always taken into account. Papers prepared by the Executive Team for Board approval include information on relevant stakeholder considerations to be discussed as part of the debate when making decisions. This is to ensure that sufficient attention is given to stakeholder concerns, and that the interests of all relevant stakeholders are taken into account in the Board's decision making.

This includes making decisions about the long-term. As is very much aligned to our Purpose, the decisions the Board make now will have long-term implications for our customers and communities now and for generations to come. This is particularly true in relation to the long-term availability of water which is impacted by the environment, climate change and the demographics and usage habits of the communities in which we serve. The Board receives, and through its Committees, regular updates on long-term trends and considers long-term strategies for carbon and energy, water and waste water management resource planning.

Through direct engagement with employees through employee engagement sessions, informal meetings with managers and by conducting operational site visits the Board is able to see and experience first hand how our culture and values are applied across the business. Maintaining an effective culture within Welsh Water is a key component to support the delivery of our strategies and the Board's decision making needed to promote the long-term success of the Company.

By order of the Board



N Foreman  
**Company Secretary**  
16 June 2023

## Directors' report

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The performance review of the Company can be found within the Strategic Report on pages 2 to 8. This provides detailed information relating to the Company, its business model and strategy, the operation of its businesses, future developments and the results and financial position for the year ended 31 March 2023. Full details and analysis of the operational performance of Dŵr Cymru Cyfyngedig during the year to 31 March 2023 are included in the published 2022-23 Annual Report and Accounts of GCHC.

The directors have pleasure in presenting their annual report, together with the audited financial statements for the year ended 31 March 2023 on pages 23 to 63.

### Directors

The Directors of the Company who were in office during the year, and up to the date of the signing of the financial statements, are set out on page 1.

### Directors' indemnity

The Company has in place Directors' and Officers' insurance giving cover against legal action brought against the Directors and an indemnity in circumstances where a Director has not acted fraudulently or dishonestly. The indemnity is a qualifying indemnity for the purpose of the Companies Act and is for the benefit of all Directors. No claims have been made against this policy since the date of the last report.

### Employees

The Board recognises the importance of attracting, developing and retaining the right people. In accordance with best practice, we have employment policies in place which provide equal opportunities for all employees, irrespective of sex, race, colour, disability, sexual orientation, religious beliefs or marital status. Further information on the Board's methods for engaging with the workforce are on our Group Annual Report.

### Engagement with stakeholders

Details of how the Directors have had regard to the need to foster the Company's business relationships with suppliers, customers and others, and the effect of that regard, including on the principal decisions taken by the Company during the financial year, are set out in the Strategic Report on our Group Annual Report.

### Research and development

With the support of our customers, regulators, and governments alike for improved services and reducing our carbon and environmental footprint, we continue to look for better ways of working or advances in technology. We have made good progress delivering the agenda set out in our Innovation Strategy, with links to over 100 academic and other institutions, technology specialists, and global innovation concerns - see website link to Innovation Strategy - [Innovation Strategy](#). For details on our investment and research into technical and innovation projects see page 129 of the Strategic Report in the [Group Annual Report and Accounts](#).

### Corporate governance

During the year ended 31 March 2023 we have applied the principles and complied with the provisions of the 2018 UK Corporate Governance Code and Ofwat's Guidance on Board Leadership, Transparency and Governance, as updated in 2019, and as required by our Licence conditions. Further details can be found in the Governance section on our Group Annual Report.

### Persons of significant control

We maintain a Register of People with Significant Control to comply with the requirements of the Small Business, Enterprise and Employment Act 2015 (2015 Act). The Company has identified registrable relevant legal entities (RREs) within the Group structure.

### Innovation

Over the past 12 months, we have made good progress delivering the agenda set out in our Innovation Strategy which we refreshed and published in 2022 with links to over 100 academic and other institutions, technology specialists, and global innovation concerns. Our refreshed strategy confirms the original 2 drivers of our approach to innovation are still very much fit for purpose.

Firstly, to develop and progress new technologies to improve customer service, create efficiencies and reduce resource use, carbon and costs. Secondly, to use our research and evidence-led work to help shape the views of regulators and governments, and so enable new innovative policies to be developed which facilitate and support the delivery of our 2050 vision, for example, on catchment solutions and nutrient trading.

## Directors' report (continued)

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### Innovation (continued)

In 2022 we progressed 46 technology-related projects from a total of 179 which have arrived at our Innovation web-based portal. We have also won or are part of innovation projects worth £35.7 million, via the Ofwat £200 million innovation fund. Our research programme, which includes our biodiversity projects and others targeted at enabling regulatory change, has so far this AMP committed £3.3 million which is leveraged to £32 million by third-party investments, mostly from the EU LIFE fund, UKRI, and the Welsh Government. Such projects and initiatives continue to be reviewed through our well-established iLab process, and support both our AMP7 KPI targets and Welsh Water 2050 to ensure our investment remains appropriately targeted.

In May 2023 our innovative project idea to use artificial intelligence (AI) to improve the way in which water companies monitor algae levels in reservoirs was awarded £385,000 in funding from Ofwat's Innovation Fund. The project is one of 16 solutions awarded a share of the award fund in the water regulator's latest innovation competition – the Water Breakthrough Challenge.

The initiative will use artificial intelligence (AI) to transform algal monitoring into a high-throughput, high-accuracy laboratory or field-based process for a fraction of the cost of historical algal monitoring methods, allowing better risk prediction and enabling water companies to take earlier, more cost-effective and targeted actions.

The Water Breakthrough Challenge encourages initiatives that help to tackle the biggest challenges facing the water sector, such as achieving net zero, protecting natural ecosystems and reducing leakage, as well as delivering value to society.

Our research work has been used to help support policy change in the EU through Eureau, the European industry trade body. In December 2022, we were pleased to see the incorporation of the producer responsibility principle in the draft Urban Wastewater Treatment Directive, requiring the pharmaceutical industry to fund any quaternary treatment processes required to further reduce the presence of pharmaceutical products in treated sewage effluents. This sets a powerful precedent and should assist the whole water sector and pharmaceutical and chemical industries to move to a more sustainable footing. Our research programme is now focusing on a wide range of topics, including how best to progress nature-based sustainable investments for our supply area.

We ran our biennial virtual Innovation Conference in September 2022, celebrating our innovation successes to date, and looking forward to AMP8 in terms of establishing stronger partnerships to deliver improvements and efficiencies for our customers. Over 500 delegates registered to attend, and we are currently working through the various innovations and research topics raised to pick the best of them for investment and support.

We are also very active in the support of Spring Innovation Ltd, the centre of excellence for innovation in the water sector. We hope to see the new Company flourish and enable us to more efficiently undertake trials of treatment processes etc, as well as share knowledge more effectively across the whole sector.

For further information on innovation with our Group, please visit pages 129 to 132 of the [Group Annual Report and Accounts](#).

### Greenhouse gas emissions

Our greenhouse gas (GHG) emissions are reported using the water industry Carbon Accounting Workbook (CAW) managed by UK Water Industry Research. This is updated annually to accommodate new emissions factors and techniques in emissions reporting and is relied upon by the water sector to report its emissions to regulators and government. In addition to using this reporting tool our data is audited annually to ISO 14064 carbon reporting standard. Our GHG emissions data can be found in the [Group Annual Report and Accounts](#), page 120.

### Corporate social responsibility

We see ourselves as more than just a water company providing drinking water and taking away wastewater – we are at the heart of the communities we serve and want to play a positive role to improve the world around us. We are committed to playing our part in ensuring we benefit not just the customers we have now – but also our future customers.

### Education programme and our visitor attractions

In Community Education, we are now past the impact that the pandemic had on our recent performance. This year, we have seen significant improvement and have met our ambitious target to reach c.80,000 children and young people through our education programme in 2023. This is both through our outreach programme and at our education centre in Cilfynydd.

Our education programme delivers enriching, informative and practical sessions to help inspire future generations. It covers a range of important environmental and sustainability themes, while also encouraging a positive attitude towards STEM (Science, Technology, Engineering & Mathematics) subjects from an early age. Our free provision is highly regarded and in high demand from schools and practitioners.

## Directors' report (continued)

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### Education programme and our visitor attractions (continued)

The experiences, knowledge and skills captured within our outreach and education centre-based sessions also offer a strong industry link, helping our young people as they strive for future employment, lifelong learning and active citizenship. 80,212 pupils have taken part in one of our sessions, which has been delivered through 789 education sessions – and involved over 1,000 hours spent with pupils in classrooms. Despite the remnants of social restrictions on some large school hall gatherings during the beginning of the year, we delivered our education programme to significantly more pupils as the year went on. The content, created and presented by qualified teachers, uses a combination of outdoor, classroom-based, assembly hall and online sessions to ensure maximum impact.

Partnership working and online digital resources continue to be a key part of our strategy, ensuring pupils receive the utmost impact from, and access to, our education support. We have continued in a successful partnership with Keep Wales Tidy to deliver a series of online interactive sessions, simultaneously streamed into classrooms and reaching over 1,500 pupils. We have also supported Groundwork Wales in their Nant-yr-Aber Project school engagement, continued to work with NRW in the annual training and induction of teachers, and have trialled a collaborative approach with Cardiff Metropolitan University as we seek to provide development opportunities for prospective teachers. In addition to the support we offer to schools in their delivery of the national curriculum to pupils, our approach is also about providing school practitioners with the scope to enhance their teaching – and this is particularly apparent again this year.

The quality of our service and impact of our education is highlighted through teacher evaluations. 442 evaluation forms have been completed, with 99% of them indicating that schoolteachers have been 'very satisfied' with the quality of delivery.

In 2022 we saw c.739,000 visitors to our four visitor centres at Llyn Brenig in north Wales, Elan Valley in mid Wales, Llandegfedd in south-east Wales and Llys-y-Frân in the west. We also have two sites where recreational access has been improved at Lliw and Swiss Valley Reservoirs, also in the west.

### Supporting vulnerable customer and social tariffs

We are currently experiencing the worst cost-of-living crisis in the UK since the 1970s. With inflation increasing to over 10% in the fourth quarter of 2022, businesses and households have faced increasing financial pressure.

It is therefore more important than ever that we support our customers, not least given that deprivation levels in Wales are among the highest in the UK. We provide a comprehensive package of support to help customers facing affordability challenges, and run proactive communications campaigns, such as 'Here for You', throughout the year to encourage those in difficulty to contact us to discuss their circumstances.

With over 1.4 million household customers in most of Wales and parts of England, we are:

- Making available £62 million across the 5 years to 2025 to provide financial assistance to our customers.
- Supporting 127,000 of our customers via discounted bills through social tariffs – a larger number, proportionate to the Company's size, than any other water company in England and Wales.
- Proud to have earmarked over £12 million in FY 23 to support our vulnerable customers as we aim to support an additional 50,000 low-income households.
- Working with over 300 local organisations (including Citizen's Advice, Welsh Government's NEST scheme to support energy efficiency improvements, Job Centre Plus, housing associations and foodbanks) to help identify and support customers who may be eligible for a discounted bill.

From April 2023, customers on our HelpU tariff have had their annual bill capped at £291, a significant reduction on the average household bill of £499. To date, working households have usually been ineligible for financial assistance from us, but we introduced a new scheme in late 2022 which is enabling them to apply for support from our newly established Cymuned (Community) Support Fund. The scheme offers short-term support to working households who find themselves in a situation where their bills exceed their income. Qualifying households may receive a 3-month charge-free period, equating to a discount of around £100-£120 on the average bill. Those who apply need to undergo an income and expenditure assessment which is completed by trusted organisations, such as Citizens Advice. The scheme was initially introduced in across Rhondda Cynon Taf in south Wales and Denbighshire in north Wales, and we plan to extend its availability more widely.

We have also supported our employees through the cost-of-living crisis. Having already implemented the increase to the Real Living Wage for all affected employees, we worked with our recognised trade unions to make a one-off payment of either £1,000 or £2,000 to eligible colleagues in December 2022 and agreed a 6.2% pay award from 1 April 2023 for most of our employees.

## Directors' report (continued)

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### Community fund

Supporting local communities has never been more important. With the after-effects of Covid and the growing concerns of the cost-of-living crisis, customers are looking at companies such as Welsh Water to lead the way as a responsible business to support projects in their local community. Since launching our Community Fund in 2017, over £450,000 has been given to various charities and community organisations.

Projects to support environmental improvements, health and wellbeing, and education and inclusivity benefits receive between £250 and £1,000 to help make a difference in their local communities. The Fund has played a key part in supporting communities where we often have large investment schemes as it enables us to work in the community while giving something back to form part of the legacy of the investment.

### Water resilient community projects and other community activities

Over the past 12 months, we have continued to build on the success of earlier rounds of Water Resilient Communities Project activities in south Wales (Maerdy and Rhymney) and north Wales (Rhyl) and we've now moved to the western area of Newport city. This place-based project, which targets some of Wales' most deprived communities, brings together several of our services in a co-ordinated effort. An important part of its success involves developing a deeper understanding of the challenges facing customers and communities, as well as exploring opportunities to collaborate with partners as we look to increase the impact of our activities. We've now connected with 30 groups and organisations active within the area.

Our achievements in Newport include:

- Attending over 70 events in the area and engaging with c.2,500 customers. This has involved reviewing over 200 customer accounts and has led to estimated customer savings of almost £11,000. The focus in the area also led to over 250 customers joining the Priority Service Register. Following the support received from the Vulnerable Customer Community Team, one customer commented: "It is a big difference, a big help. That little bit extra that I was spending on water, is now spent on the boys."
- Promoting our free toilet leakage and water efficiency offering within the area, which led to over 140 customer appointments and the dispatch of c.500 free water saving devices.
- Identifying, analysing and initiating proactive investigations into multiple post-codes within the project area, where there is a high risk of repeat blockages.
- Proactively reaching out to customers in arrears to inform them that we would be holding a local drop-in surgery. Our debt advisors were at hand to assist customers, many of whom had been disengaged for a long time, onto a path to clear their debts. One customer involved on the day shared his appreciation: "I'm really nervous on the phone. I thought this event was a great idea. I just came down, and the gentleman has helped me out. I'm trying to sort my life out. Times are hard and every penny helps. I owe Welsh Water a lot of money. This gentleman today has put me on a tariff, and as long as I keep my payments correct, the bill will be written-off."
- Supporting jobseekers in the area through the support and expertise of our Human Resources department.
- Delivering curriculum-led school visits, which involved the trial of new educational content with c.4,000 children in local schools. This involved c.70 hours of classroom time, during which, future generations were thoroughly engaged in the learning: "In those little microscopes, I looked at a dragonfly wing. I enjoyed it so much because I got to learn about other creatures that I've never learned about before."

### Biodiversity

Our 2022 biodiversity strategy sets out our ongoing ambitions, objectives, and action plan to maintain and enhance biodiversity and ecological resilience across our operational assets and landholdings, within the fulfilment of our functions. The strategy enables the business to continue delivering its core functions while supporting our environmental regulators – NRW, the Environment Agency, and the Welsh Government – to address the biodiversity crisis we face. In so doing, we will help safeguard our environment for future generations to come, and meet the expectations of our customers.

In June 2022 the Company published its first Biodiversity Strategy – which is available at [dwrcymru.com/en/blog/biodiversity-strategy-2022](https://dwrcymru.com/en/blog/biodiversity-strategy-2022).

The strategy notes that by improving water quality, and in many cases transforming the quality of local rivers, estuaries, and coastal waters, we have also improved aquatic biodiversity and the ecology of these waters. However, when compared to our investments for water quality, and more latterly those to reduce our carbon footprint, projects to specifically improve biodiversity, whether terrestrial or aquatic, have been comparatively few.

This focus is set to change with the launch of our AMP8 business plan, which builds on our successful catchment work focused on water quality improvements in our upland drinking water catchments. It recognises that by improving and restoring terrestrial and aquatic habitats we can and will make improvements to water quality, lock up carbon, mitigate flooding risks, and improve the wellbeing of our customers.

## Directors' report (continued)

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### **Biodiversity (continued)**

Our biodiversity strategy sets out our ambitions, objectives and action plan to maintain and enhance biodiversity and ecological resilience across our operational assets and landholdings, within the fulfilment of our functions. Our strategic objectives to achieve this, as already supported by our biodiversity plan, focus on the following areas:

- Restore habitats and look after the protected sites we own.
- Work in partnership with our regulators and stakeholders and promote research opportunities.
- Improve the management of invasive non-native species (INNS).
- Develop and engage our colleagues as ambassadors and work better to understand our customers' expectations.
- Maintain and enhance biodiversity at our operational assets and landholdings.

Our biodiversity mission links directly to our duty in Section 6 of the Environment (Wales) Act 2016. It requires us to produce and publish a corporate biodiversity action plan and report progress every 3 years. Our first Biodiversity plan was published in 2017 and refreshed in 2020. Our latest updated plan will be published in 2023. By delivering this mission we will support and meet our legislative requirements relating to biodiversity and ecology, and so help move our business to a sustainable footing. The strategy aims to deliver performance improvements in both the short term and the medium term through to 2030, and ensure our plans remain aligned with the longer-term objectives of Welsh Water 2050.

### **Social**

Our company vision is to Earn the Trust of our Customers Every Day. Building strong relationships with our customers and communities is key to maintaining that trust as we deliver essential services to 3.1 million people across our supply area. It is central to our strong staff engagement that they feel able to make a positive impact through their service delivery.

### **Equality, diversity and inclusivity**

Every organisation is only as good as its people, and so we want to recruit and retain the best talent. Talent is indifferent to gender, race, or sexual orientation: it is what an individual is endowed with. We want to have the widest possible appeal to talent in all its forms and this comes by being recognised externally as having an inclusive culture, somewhere people are valued for who and what they are. We need all our people to recognise and value that culture so they talk about it to their friends and communities and spread the word that Welsh Water is a great place to work.

In the water sector, we have historically had a predominantly white male workforce. We have, therefore, continued our focus on improving our diversity across genders, LGBT+ and nonbinary, race, disability, social background and more, to better reflect the communities we serve. We are currently reviewing our targeted data-led approach underpinning our strategy to better inform us on where we need to move the dial on equality, diversity and inclusivity.

Our work to reinforce this culture continues to be driven by:

- An experienced Equality, Diversity and Inclusivity lead working with colleagues, teams and networks across the business.
- Our well-established Inclusivity Forum which includes ambassadors for all the protected characteristics and identifies areas in which the business can improve its efforts to be more inclusive.
- Monitoring progress, using quantitative and qualitative data to highlight where barriers exist, show the impact of our interventions, and make appropriate adjustments where needed.
- Using employee-led network groups to feed back to evaluate initiatives, to assess if policies are working for everyone, and to provide a platform for feedback and improvements.

### *Internal programmes*

We want inclusivity to be at the heart of what we do at Welsh Water, and over the past 12 months, we have:

- Delivered inclusive language training to colleagues at all levels, including our Non-Executive Directors, demonstrating the importance of top-level down initiatives.
- Delivered a range of modules for colleagues around diversity to include conversations about race, being an ally, and unconscious bias.
- Had regular communication with the Executive Team on initiatives and areas for focus.
- Continued with reverse mentoring for Directors and senior managers with colleagues from different backgrounds sharing their lived experience.

### *External relationships*

We have also worked with the following organisations over the last year:

- Energy and Utility Skills – our Inclusion Lead attends these for best practice sharing across the industry looking at ways we can improve.

## Directors' report (continued)

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### Equality, diversity and inclusivity (continued)

- Business in the Community – as a signatory to the Race Charter, but also working with our dedicated inclusion adviser delivering webinars available to all colleagues. We are also part of the Age at Work Leadership group, working together with other organisations to understand the challenges and opportunities of an ageing work population and share good practice.
- Stonewall Cymru – continuing our membership as a diversity champion, taking part in the annual Stonewall Index and delivering modules for colleagues.
- Chwarae Teg – delivering a series of modules supporting development of women in the organisation.
- Mahogany Inclusion Partners – delivering a number of modules supporting development for Black, Asian or ethnic minority colleagues.
- WISE (Women in Science and Engineering) – partnering for best practice approaches that we can introduce and embed into our way of working.

### Board composition

As part of the annual effectiveness review of the Board and Board Committees, the Board considers the balance of skills, knowledge, experience, independence and diversity representation as reviewed by the Committee. The Board is alert to opportunities to improve the current level of diversity with regard to skills, experience, backgrounds, race, gender and personal attributes of Board Members. The Committee reports on its progress in implementing the Board Diversity policy and monitoring the diversity of the Board and on the Group's gender diversity ratios in its annual report. It also reports on its oversight of plans to promote diversity within our workforce to ensure that the individuals working for us are representative of the communities that we serve, in accordance with the Group's policies supporting the development of equality, diversity and inclusivity across the business. At the end of the year, 50% of our Board (2022: 33%) and 33% of the Executive team (2022: 37.5%) are female, while in the wider workforce, of those senior managers reporting directly to a member of the Executive team, 38% (2022: 23.4%) are female.

Further information please visit the Group Annual Report and Accounts for our Board composition, succession and evaluation on pages 156 to 157, [Group Annual Report and Accounts](#).

### Our support for graduates and apprentices

#### *Recruiting our future workforce*

We are continuing to invest in recruiting new talent into Welsh Water by identifying those with the right skills, attributes and behaviours to become our highly skilled workforce of the future. We continue to review the programmes we offer, and our apprentice offering is for craft roles as well as in support functions and degree apprenticeships.

We continue to partner with the University of South Wales to deliver our network75 programme which is a combined work placement and part-time study route to a degree, allowing students to work, earn and learn. Over the past 12 months, we have recruited 41 graduates and apprentices and 2 colleagues have taken part in the network75 programme.

### Auditor FY23

KPMG LLP act as Auditor to Glas Cymru Group (the Group) for the accounts for the year ended 31 March 2023. As part of the audit process we have confirmed that, as far as each Director is aware, there is no relevant audit information of which the Auditors are unaware, that they have taken any necessary steps to be made aware of any such information and to establish that the Group's Auditor is aware of that information. We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable accounting standards, give a true and fair view of the Group's performance;
- the Strategic Report includes a fair review of the performance of the business, its risks and strategy for the future; and
- the Directors consider the Annual Report to be fair, balanced and understandable.

In considering the development of the system of controls, the management team reviews the materiality and the relative cost benefit associated with each identified significant risk. The internal control systems are designed to provide reasonable assurance against misstatements, loss or failure. The process to review the effectiveness of internal control includes discussion with management on significant risk issues and a review of plans for, and results from, internal and external audit.

The Audit Committee reports the results of its review to the Board, which then draws its collective conclusion on the effectiveness of the system of internal controls. In fulfilling this responsibility, the Board considers regular reports from the Audit Committee, the Quality and Safety Committee and from management, and relies on its routine monitoring of key performance indicators and monthly reports of financial and operational performance.

Taken as a whole, these processes enable the Board to review the effectiveness of the internal control system during the course of the year. KPMG LLP will not be subject to re-appointment as Auditor to the Group (see Auditor FY24).



## Directors' report (continued)

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### Auditor FY24

Following a re-tender of external audit services completed during 2023, a decision to appoint Deloitte LLP as Auditor to the Group was approved by the Glas Cymru Board, subject to Members' approval at the AGM in July 2023. Deloitte LLP will act as Auditor of the Group for the accounts for the year ending 31 March 2024 and be subject to annual re-appointment by the Members at the AGM in respect of each subsequent financial year. Accordingly, in accordance with Section 489 of the Companies Act 2006, a resolution proposing the appointment of Deloitte LLP as Auditor of the Group will be put to the Members at the forthcoming AGM.

### Human rights

We are committed to respecting human rights in relation to colleagues, and our supply chain (see page 111 of our Group Annual Report for information on our Supplier Code of Conduct). Our internal Code of Conduct is supported by several Group policies including, Anti-bullying and Harassment, Whistleblowing, Anti-bribery and Corruption, and Anti-Fraud.

### Working collaboratively

One of the prevalent features in Wales is our ability to work in close partnerships, as is required in the case of public bodies by the Well-being of Future Generations (Wales) Act. The Act requires public bodies to demonstrate in their decision making the impact that they could have on people living in Wales in the future as well as in the present. This is to show that they are acting in accordance with the sustainable development principle, as defined in the Act. The Act directly supports 5 ways of working which are all compatible with our Vision and views on sustainability, albeit we are not a public body as defined under the Act. These are:

- To carry out sustainable development – intrinsic to the nature of our business and vision.
- Thinking for the long term – avoiding short-termism and considering how decisions will impact on the wellbeing of future as well as current generations.
- Prevention – acting early and with others to tackle the root cause of problems before they arise or get worse to bring about better outcomes for individuals, public bodies and society as a whole.
- Integration – ensuring that the full range of consequences of an action are considered so that activity in one area of work can be shaped to complement, rather than undermine, activities in others.
- Collaboration – working with others, so that as many objectives as possible can be met with the resources and expertise available and not trying to solve problems alone but understanding the benefits of involving as wide a range of people as possible in helping shape the decisions and services that will affect their lives.

### Whistleblowing

A healthy culture where individuals feel able to speak out about anything that causes them concern is an important part of our three lines of defence compliance model. Colleagues, suppliers, business partners and other stakeholders are encouraged to 'Speak Up' to raise concerns about conduct which is contrary to our values. Where appropriate, concerns will be investigated by the Business Assurance Team, reporting directly to the Audit Committee. The Committee receives reports on the outcome of investigations in private sessions with the Head of Business Assurance. We are fully committed to protecting any employee who reports a breach or suspected breach of the Code of Conduct or raises any other public interest disclosure. We publicise an external helpline, which provides an additional confidential and secure means to raise concerns.

### Sustainable Procurement Policy

We have established our sustainable procurement aspirations through collaboration with key stakeholders, covering environmental, economic and social areas. Our aspirations have been mapped against DCWW's ESG Strategy Objectives, the Well-being of Future Generations (Wales) Act and are included in our Sustainable Procurement Policy (SPP). We have assessed the impact on these sustainable procurement aspirations in the key categories we procure by undertaking risk and opportunity heatmapping of existing procurement contracts against the aspirations. We are in the process of detailing our implementation plan for deployment of the Sustainable Procurement Policy in the current financial year.

### Supply Chain Compliance Standards

We launched the Supplier Code of Conduct (SCC) in April 2021. Since then we have:

- Included supplier acceptance and confirmation of compliance with the SCC as a pass/ fail test at the Pre-Qualification Questionnaire stage tender processes.
- Incorporated compliance with the SCC as standard wording in all goods and services contracts which have been awarded, changed or extended since April 2021.
- Amended the purchase order terms and conditions to incorporate the requirements of the SCC.

## Directors' report (continued)

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### Modern Slavery Awareness

We held an annual week-long campaign on modern slavery awareness. In October 2022, Procurement, in conjunction with the Hope for Justice Alliance, engaged with and trained 36 operational Contract Managers, 15 colleagues from the Procurement and Compliance teams, and 37 suppliers (which provide services with a higher risk of modern slavery occurring in their supply chain) on how to identify the signs that modern slavery may be occurring and to confirm our reporting procedures in the event that modern slavery is suspected to be taking place. We also highlighted the Supplier Code of Conduct and the requirement to comply with this during the training sessions. Our Anti-slavery statement can be found at [dwrcymru.com/antislavery](http://dwrcymru.com/antislavery).

All members of the Procurement team have completed the Chartered Institute of Procurement and Supply's (CIPS) Ethical Procurement and Supply e-Learning and Test certification and Welsh Water successfully attained the CIPS Corporate Ethics Mark accreditation. This signals to Welsh Water's suppliers, customers, potential employees, and other stakeholders that they are dealing with an organisation that is committed to ensuring its staff are trained in ethical sourcing and supplier management, and that we have adopted ethical values in the way in which we source and manage suppliers.

### Anti-bribery, corruption and anti-fraud

Our Group policy makes it clear that we will not tolerate any acts of fraud, dishonesty, bribery, corruption, theft or improper disclosure of confidential information. The Company treats these issues very seriously and expects any issues to be reported immediately. This is reinforced by our strict policy on hospitality and gifts from suppliers, which is regularly monitored and actively enforced.

No breaches of policy were notified to Internal Audit or the external whistleblowing hotline during the period 2022-23.

### Conflicts of interest

We require our employees to perform their duties honestly and to avoid conflict between any personal, financial or commercial interests and their responsibilities to Welsh Water.

### Data protection and information security

Welsh Water is committed to ensuring that we handle the personal information of our customers and employees in a responsible and honest way, including respecting their data protection rights in compliance with legislation. Our Privacy Statement is available on our website at [Privacy-policy](#).

### Political donations

It is Board policy not to make donations to political parties or to incur political expenditure. A payment of £28,136 was made in May 2022 to Step Change to support the work the charity does in providing debt advice to our customers. We are disclosing this payment as this organisation also campaigns for government policy change, including on debt issues. However, none of the funding provided would have been used directly to support campaign work. Other than this, no donations or payments were made which would require to be disclosed under section 366 of the Companies Act 2006.

### Financial risk management

The Company's operations expose it to a variety of financial risks that include the effect of changes in debt market prices, credit risk, liquidity risk and interest rate risk. The Company has in place a risk management programme that seeks to limit the adverse effects on the financial performance of the Company by monitoring levels of debt finance and the related finance costs.

### Dividend

No dividend was declared or paid in the year (2022: none).

### Task Force on Climate-related Financial Disclosures : Climate risk assessment

Our commitment to our customers and the environment involves us mitigating and adapting to the impacts of climate change. From April 2022, certain large businesses in the UK are required by law to include climate risks in their annual reporting. Welsh Water views corporate governance as a core discipline and as such has taken the decision to report in line with these requirements by following the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). We have worked with Jacobs to produce a climate risk disclosure, covering the four key disclosure areas of the TCFD: Governance, Strategy, Risk Management, and Metrics & Targets, and recognising that this is our first year of reporting we are taking steps towards future full compliance with the 11 TCFD recommended disclosures. The full report is available at [TCFD Report](#).

### Going concern

The financial statements for FY23 have been prepared on the going concern basis. For the Directors' Going Concern statement and detail of why the Going Concern assumption is considered appropriate, see page 28 within accounting policies.

## Directors' report (continued)

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### Regulatory accounts

Condition F of the Instrument of Appointment under which Dŵr Cymru Cyfyngedig operates requires that Dŵr Cymru Cyfyngedig publish additional financial information as an 'appointed business'. A copy of this information will be published on Dŵr Cymru Cyfyngedig's website by 15 July 2023 and will also be available on request from the Company Secretary.

### Group structure

These financial statements for Dŵr Cymru Cyfyngedig cover the year to 31 March 2023. The Company's immediate parent company is Dŵr Cymru (Holdings) Limited. The entire share capital of Dŵr Cymru (Holdings) Limited is owned by Glas Cymru (Securities) Cyfyngedig, which is wholly owned by Glas Cymru Anghyfyngedig. The ultimate holding company and controlling party is Glas Cymru Holdings Cyfyngedig, a company registered in England and Wales.

### Disclosure of information to auditor

The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

By order of the Board



N Foreman  
**Company Secretary**

Registered office:  
Linea  
Fortran Road  
St Mellons  
Cardiff  
CF3 0LT

16 June 2023

## Statement of Directors' responsibilities in respect of the Strategic Report, the Directors' Report and the financial statements

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The Directors are responsible for preparing the Annual Report, Strategic Report, the Directors' 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 they have elected to prepare the financial statements in accordance with UK-adopted international accounting standards and applicable law.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with UK-adopted international accounting standards;
- assess the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations or have no realistic alternative but to do so.

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 responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect 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.

# Independent auditor's report to the members of Dŵr Cymru Cyfyngedig

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## Opinion

We have audited the financial statements of Dwr Cymru Cyfyngedig ("the Company") for the year ended 31 March 2023 which comprise the income statement, statement of comprehensive income, balance sheet, statement of changes in equity, cash flow statement, and related notes, including the accounting policies in note 1.

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 March 2023 and of its loss for the year then ended;
- have been properly prepared in accordance with UK-adopted international accounting standards; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

## Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the Company in accordance with, UK ethical requirements including the FRC Ethical Standard. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

## Going concern

The directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or to cease their operations, and as they have concluded that the Company's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over their ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

We used our knowledge of the Company, its industry, and the general economic environment to identify the inherent risks to its business model and analysed how those risks might affect the Company's financial resources or ability to continue operations over the going concern period. The risks that we considered most likely to adversely affect the Company's available financial resources and the interest cover and regulated asset ratios relevant to debt covenants over this period was the impact of increasing costs and inflation.

We considered whether these risks could plausibly affect the liquidity or covenant compliance in the going concern period by assessing the degree of downside assumption that, individually and collectively, could result in a liquidity issue, taking into account the Company's current and projected cash and facilities (a reverse stress test).

We assessed the completeness of the going concern disclosure.

Our conclusions based on this work:

- we consider that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate;
- we have not identified, and concur with the directors' assessment that there is not, a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the Company's ability to continue as a going concern for the going concern period; and
- we have nothing material to add or draw attention to in relation to the directors' statement in note 1 to the financial statements on the use of the going concern basis of accounting with no material uncertainties that may cast significant doubt over the Company's use of that basis for the going concern period, and we found the going concern disclosure in note 1 to be acceptable

However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the above conclusions are not a guarantee that the Company will continue in operation.

## Fraud and breaches of laws and regulations – ability to detect

### *Identifying and responding to risks of material misstatement due to fraud*

To identify risks of material misstatement due to fraud ("fraud risks") we assessed events or conditions that could indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud.

Our risk assessment procedures included:

- Enquiring of directors, the audit committee, internal audit and inspection of policy documentation as to the Company's high-level policies and procedures to prevent and detect fraud, including the internal audit function, and the Company's channel for "whistleblowing", as well as whether they have knowledge of any actual, suspected or alleged fraud.

## Independent auditor's report to the members of Dŵr Cymru Cyfyngedig (continued)

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- Reading Board/ audit committee minutes.
- Considering remuneration incentive schemes and performance targets for management/ directors including the AVPS and LTVPS target for management remuneration.
- Using analytical procedures to identify any unusual or unexpected relationships.

We communicated identified fraud risks throughout the audit team and remained alert to any indications of fraud throughout the audit.

As required by auditing standards, we perform procedures to address the risk of management override of controls, in particular the risk that Company management may be in a position to make inappropriate accounting. On this audit we do not believe there is a fraud risk related to revenue recognition because of the regulated nature of the revenues recognized and limited opportunity or incentive for management to manipulate these revenues.

We also identified a fraud risk related to the inappropriate accounting treatment of pension benefit increases in response to possible impacts on covenant compliance.

We performed procedures including:

- Challenging the accounting treatment of the pension benefit increases by considering the requirements of IAS 19;
- Identifying journal entries and other adjustments to test based on risk criteria and comparing the identified entries to supporting documentation. These included fixed asset, borrowings and cash entries made to unrelated accounts;
- Assessing significant accounting estimates for bias.

### *Identifying and responding to risks of material misstatement related to compliance with laws and regulations*

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience, through discussion with the directors and other management (as required by auditing standards), and from inspection of the Company's regulatory and legal correspondence and discussed with the directors and other management the policies and procedures regarding compliance with laws and regulations.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

The potential effect of these laws and regulations on the financial statements varies considerably.

Firstly, the Company is subject to laws and regulations that directly affect the financial statements including financial reporting legislation (including related companies' legislation), distributable profits legislation, taxation legislation, pension legislation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Company is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation or the loss of the Company's license to operate. We identified the following areas as those most likely to have such an effect: compliance with Ofwat regulatory legislation, Environment Agency, Drinking Water Inspectorate, National Rivers Authority, Natural Resources Wales, Wales Act, health and safety, GDPR and employment law recognising the financial and regulated nature of the Company's activities and its legal form. Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors and other management and inspection of regulatory and legal correspondence, if any. Therefore, if a breach of operational regulations is not disclosed to us or evident from relevant correspondence, an audit will not detect that breach.

For the leakage and per capita consumption reporting matter discussed in note 16 we assessed accounting treatment and disclosures against our understanding from regulator correspondence and independent third-party reports.

### *Context of the ability of the audit to detect fraud or breaches of law or regulation*

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it.

## Independent auditor's report to the members of Dŵr Cymru Cyfyngedig (continued)

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In addition, as with any audit, there remained a higher risk of non-detection of fraud, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. Our audit procedures are designed to detect material misstatement. We are not responsible for preventing non-compliance or fraud and cannot be expected to detect non-compliance with all laws and regulations.

### Strategic report and Directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

### Matters on which we are required to report by exception

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

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

We have nothing to report in these respects.

### Directors' responsibilities

As explained more fully in their statement set out on page 18, the directors are responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

### Auditor's responsibilities

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 our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not 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 aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities).

## **Independent auditor's report to the members of Dŵr Cymru Cyfyngedig (continued)**

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### **The purpose of our audit work and to whom we owe our responsibilities**

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.



**James Ledward (Senior Statutory Auditor)  
for and on behalf of KPMG LLP, Statutory Auditor**

*Chartered Accountants*

3 Assembly Square

Britannia Quay

Cardiff

CF10 4AX

**16 June 2023**



## Income statement for the year ended 31 March 2023

		2023	2022
Continuing activities	Note	£m	£m
Revenue	2	<b>841.3</b>	807.0
<b>Operating costs:</b>			
- Operational expenditure	3	<b>(374.1)</b>	(323.0)
- Impairment of trade and other receivables	3	<b>(24.8)</b>	(23.7)
- Other operating income	3	<b>5.3</b>	6.0
- Exceptional item	3	<b>(30.8)</b>	3.8
- Infrastructure renewals expenditure	3	<b>(78.0)</b>	(61.8)
- Depreciation and amortisation	3	<b>(345.6)</b>	(327.8)
		<b>(848.0)</b>	(726.5)
<b>Operating (loss) / profit</b>		<b>(6.7)</b>	80.5
Profit on disposal of property, plant and equipment		<b>0.4</b>	0.6
		<b>(6.3)</b>	81.1
<b>Financial expenses:</b>			
Financial income	4a	<b>14.7</b>	4.1
Financial expenses	4a	<b>(506.1)</b>	(281.0)
Fair value gains on derivative financial instruments	4b	<b>115.4</b>	80.4
		<b>(376.0)</b>	(196.5)
<b>Loss before taxation</b>		<b>(382.3)</b>	(115.4)
Taxation	5	<b>83.1</b>	(34.3)
<b>Loss for the year</b>		<b>(299.2)</b>	(149.7)

The notes on pages 28 to 63 form part of these financial statements.

## Statement of comprehensive income for the year ended 31 March 2023

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	Note	2023 £m	2022 £m
<b>Loss for the year</b>		<b>(299.2)</b>	(149.7)
<b>Items that will not be reclassified to profit or loss</b>			
Actuarial gain recognised in the pension scheme	21	<b>124.5</b>	10.5
Related deferred tax	6	<b>(31.1)</b>	2.7
Revaluation of property, plant and equipment	7	<b>593.4</b>	448.4
Related deferred tax	6	<b>(148.4)</b>	(192.3)
		<hr/>	<hr/>
		<b>538.4</b>	269.3
		<hr/>	<hr/>
<b>Total comprehensive gain for the year</b>		<b>239.2</b>	119.6

## Balance sheet as at 31 March 2023

	Note	2023 £m	2022 £m
<b>Assets</b>			
<b>Non-current assets</b>			
Property, plant and equipment	8	6,959.2	6,264.1
Intangible assets	9	202.2	203.2
Other financial assets:			
- derivative financial instruments	14	11.1	10.4
- Employee benefits	21	12.0	-
		<u>7,184.5</u>	<u>6,477.7</u>
<b>Current assets</b>			
Inventories		5.3	4.3
Trade and other receivables	10	647.2	590.9
Cash and cash equivalents	11	362.6	503.7
Other financial assets:			
- derivative financial instruments	14	12.7	31.4
		<u>1,027.8</u>	<u>1,130.3</u>
<b>Total assets</b>		<u>8,212.3</u>	<u>7,608.0</u>
<b>Liabilities</b>			
<b>Current liabilities</b>			
Trade and other payables	12	(685.0)	(614.5)
Provisions	16	(17.8)	(2.8)
Other financial liabilities:			
- borrowings	13	(94.7)	(83.3)
- derivative financial instruments	14	(15.6)	(46.9)
		<u>(813.1)</u>	<u>(747.5)</u>
<b>Net current assets</b>		<b>214.7</b>	<b>382.8</b>
<b>Non-current liabilities</b>			
Trade and other payables	12	(540.8)	(447.1)
Employee benefits	21	-	(80.7)
Provisions	16	(5.9)	(6.3)
Other financial liabilities:			
- borrowings	13	(4,438.4)	(4,145.8)
- derivative financial instruments	14	(74.9)	(177.0)
Deferred tax - net	6	(793.4)	(697.0)
		<u>(5,853.4)</u>	<u>(5,553.9)</u>
<b>Total liabilities</b>		<u>(6,666.5)</u>	<u>(6,301.4)</u>
<b>Net assets</b>		<u>1,545.8</u>	<u>1,306.6</u>
<b>Equity</b>			
Share capital	17	309.9	309.9
Capital redemption reserve		166.2	166.2
Revaluation reserve	7	1,267.0	914.7
Retained earnings		(197.3)	(84.2)
<b>Total equity</b>		<u>1,545.8</u>	<u>1,306.6</u>

The financial statements on pages 23 to 63 were approved by the Board of Directors on 16 June 2023 and were signed on its behalf by:



P M Davis  
Chief Financial Officer

Registered N<sup>o</sup> 2366777

## Statement of changes in equity for the year ended 31 March 2023

	Share capital £m	Capital redemption reserve £m	Revaluation reserve £m	Retained earnings £m	Total equity £m
At 1 April 2021	309.9	166.2	732.1	(21.2)	1,187.0
Loss for the year	-	-	-	(149.7)	(149.7)
Actuarial loss net of tax	-	-	-	13.2	13.2
Revaluation net of tax	-	-	256.1	-	256.1
Transfer to retained earnings	-	-	(73.5)	73.5	-
At 31 March 2022	309.9	166.2	914.7	(84.2)	1,306.6
Loss for the year	-	-	-	(299.2)	(299.2)
Actuarial gain net of tax	-	-	-	93.4	93.4
Revaluation net of tax	-	-	445.0	-	445.0
Transfer to retained earnings	-	-	(92.7)	92.7	0.0
At 31 March 2023	309.9	166.2	1,267.0	(197.3)	1,545.8

## Cash flow statement for the year ended 31 March 2023

	Note	2023 £m	2022 £m
<b>Cash flow from operating activities</b>			
Cash generated from operations *	18a	377.4	428.2
Interest paid	18b	(149.6)	(117.5)
Income tax received		0.6	2.3
<b>Net cash flow from operating activities</b>		<b>228.4</b>	<b>313.0</b>
<b>Cash flow from investing activities</b>			
Interest received		13.2	4.1
Purchase of property, plant and equipment		(296.6)	(237.1)
Purchase of intangible assets		(38.6)	(37.3)
Grants and contributions received		30.5	23.1
Proceeds from sale of property, plant and equipment		0.4	0.8
<b>Net cash flow from investing activities</b>		<b>(291.1)</b>	<b>(246.4)</b>
<b>Net cash flow before financing activities</b>		<b>(62.7)</b>	66.6
<b>Cash flow from financing activities</b>			
Repayment of borrowings		(2.5)	2.5
Intercompany loan received		-	300.0
Bond issue costs		-	(2.9)
Long-term loans repaid		(38.4)	(31.2)
Loan repaid to group undertaking		(20.0)	(24.5)
Payment of lease liabilities		(17.5)	(15.6)
<b>Net cash flow from financing activities</b>		<b>(78.4)</b>	<b>228.3</b>
<b>(Decrease)/increase in cash and cash equivalents</b>	19b	<b>(141.1)</b>	294.9
Cash and cash equivalents at 1 April		503.7	208.8
<b>Cash and cash equivalents at 31 March</b>	11	<b>362.6</b>	<b>503.7</b>

\* Exceptional costs are included in cash flows generated from operations.

# Notes to the financial statements

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## 1. Accounting policies for the year ended 31 March 2023

Dŵr Cymru Cyfyngedig ('the Company') is a private company incorporated, domiciled and registered in Wales in the UK. The registered number is 2366777 and the registered address is Linea, Fortran Road, St Mellons, Cardiff, CF3 0LT.

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been applied consistently to both years presented.

### Basis of preparation

The financial statements of Dŵr Cymru Cyfyngedig have been prepared and approved by the Directors in accordance with UK-adopted international accounting standards ("UK-adopted IFRS") and applicable law. The financial statements have been prepared under the historical cost convention, as modified by the revaluation of fixed assets, other financial assets and liabilities (including derivative financial instruments) at fair value through profit or loss. The presentational currency of these accounts is GBP and all balances are shown rounded in £m.

The preparation of financial statements to conform with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas including a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed on page 35.

### Going concern

The financial statements have been prepared on the going concern basis as the Directors have a reasonable expectation that the Company has adequate resources for a period of at least 12 months from the date of their approval and that there are no material uncertainties to disclose.

In assessing the appropriateness of the going concern basis of accounting the Directors have reviewed the resources available to the Company in the form of cash and committed bank facilities as well as consideration of the Company's capital adequacy.

The Directors have considered the magnitude of potential impacts resulting from uncertain future events or changes in conditions, and the likely effectiveness of mitigating actions that the directors would consider undertaking. The financial plan has been subjected to a number of severe but plausible downside scenarios in order to assess the group's ability to operate within existing covenants and facilities. These scenarios consider: the potential impacts of increased totex costs, including a significant one-off totex impact arising in the assessment period; low and high inflation environments; elevated levels of bad debt; outcome delivery incentive penalties; and the impact of these factors materialising on a combined basis. Mitigating actions were considered to include: deferral of capital expenditure; a reduction in other discretionary totex spend; and an extension of revolving credit facilities. The Directors have also assessed the potential impacts resulting from the cost-of-living crisis and interest rates presently affecting the UK, and although they generate a negative on our financials, none of these factors pose a significant concern to disclose in relation to the Group's ability to continue as a going concern.

Reduced cash flows would impact on key financial metrics, in particular interest cover ratios. In the extreme downside scenario, gearing and interest covers retain headroom within the trigger levels specified in borrowing covenants; and whilst the reduced cash flows weaken our financial metrics, they remain within the investment grade credit rating and in compliance with our borrowing covenants.

Having considered these matters, the Directors do not believe there are any material uncertainties to disclose in relation to the Company's ability to continue as a going concern.

## Notes to the financial statements (continued)

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### Changes in accounting policies and disclosures

The following new standards, amendments and interpretations have been adopted by the Company for the first time for the financial year beginning on 1 April 2022:

#### Amendments

- Reference to the Conceptual Framework (Amendments to IFRS 3)
- Property, Plant and Equipment — Proceeds before Intended Use (Amendments to IAS 16)
- Onerous Contracts — Cost of Fulfilling a Contract (Amendments to IAS 37)
- Annual Improvements to IFRS Standards 2018–2020

The adoption of these standards, amendments and interpretations has not had a material impact on the financial statements of the Company

### Future changes to accounting standards

At the date of approval of these financial statements, the following Standard and Amendments, which have not been applied in these financial statements, were in issue but not yet effective:

#### Amendments

- IAS 1 Disclosure of Accounting Policies.
- IAS 8 Definition of Accounting Estimates.
- IAS 12 Deferred Tax related to Assets and Liabilities arising from a Single Transaction.
- IFRS 17 Insurance Contracts.

During the financial year, we reviewed our exposure to IFRS 17 and concluded that we do not anticipate any impact arising from the new standard. The Directors anticipate that the adoption of this Standard and these Amendments in future periods will have no material impact on the financial statements of the Company.

### Revenue recognition

Revenue represents the income receivable in the ordinary course of business for services provided, excluding value added tax. Where services have been provided, but for which no invoice has been raised at the year-end, an estimate of the value is included in revenue. Revenue recognised reflects the value of services provided to customers in the year. Where customers have made payments in advance as at the year end, this is recognised as deferred income.

Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use of and obtain the benefits from the good or service. The Company recognises that contracts with customers are, in a majority of cases, governed by legislative requirements rather than discrete commercial arrangements. As a result, the application of judgement is important in determining the most appropriate treatment of certain income streams.

The key consideration in respect of the Company's activities is where revenues from bundled goods and services require separation, which may result in deferring or recognising revenue immediately. Our core water and sewerage supply services (including retail) constitute more than 99% of total income; however, there are some peripheral income streams which do require more in-depth consideration. All water companies have a legal obligation to allow third parties to establish an authorised connection to their networks and a number of activities may be necessary in order to achieve this, giving rise to the following transactions and accounting treatments under IFRS 15:

- Connection charges: these are amounts received from developers for connection to the network which the Company recognise as income on delivery of that performance obligation.
- Infrastructure charges and requisitions: third party contributions towards the Group's obligation to ensure future service provision to the connection or mains over its life; the Company estimate that an average connection lasts for 80 years and defer the release of charges over that period.
- Asset adoptions: usually sewers adopted at no cost, whereby the receipt of the asset is out of scope of IFRS 15 and should therefore be recognised at fair value (with deferral of related non-cash income).
- Diversions: payment in return for moving a water or sewer main to accommodate other infrastructure changes. The performance obligation is to move the main, with no additional asset creation, therefore revenue is recognised immediately.

Other operating income principally relates to sales of gas. Revenue from sales of gas is recognised upon delivery. Exports of renewable electricity is included with power costs as it is treated as a natural hedge to our consumption. Our energy strategy is to enter into contracts which fix the price of consumption less exports of future power purchases in order to reduce the impact of power price variances. Exports of electricity is recognised upon delivery.

## Notes to the financial statements (continued)

### Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segment, has been identified as the Board.

### Exceptional items

Exceptional items are those significant items which are disclosed separately by virtue of their size and/or nature to enable a true understanding of the Company's performance.

### Property, plant and equipment

The economic value of the Company's water and sewerage business is derived from the Regulatory Capital Value (RCV) set by Ofwat during its five yearly price reviews. The Company considers that a fair value approach to valuing its assets better reflects the underlying value of the assets than historical cost accounting which understates the assets' current value in use.

As at 31 March 2023 the total value of tangible and intangible fixed assets has been revalued to the Company's 'shadow-RCV' (Regulatory Capital/Asset Value), being the 31 March 2023 RCV published by Ofwat in its PR19 Final Determination as adjusted for the impact of any totex over/underspend and the Outcome Delivery Incentive rewards/penalties. The classes of asset impacted are infrastructure assets and operational structures.

The carrying value of assets is reviewed for impairment if circumstances dictate that the carrying value may not be recoverable; asset lives and residual values are reviewed annually.

Property, plant and equipment comprise:

- a) Infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls); and
- b) Other assets (including properties, overground operational structures and equipment, and fixtures and fittings).

### Infrastructure assets

Infrastructure assets comprise principally impounding reservoirs and a network of underground water and wastewater systems. For accounting purposes, the water system is segmented into components representing categories of asset classes with similar characteristics and asset lives. The wastewater system is segmented into components representing geographical operating areas, reflecting the way the Company operates its wastewater activities.

Expenditure on infrastructure assets relating to increases in capacity, enhancements or material replacements of network components is treated as additions, which are included at cost. Expenditure incurred in repairing and maintaining the operating capability of individual infrastructure components, "infrastructure renewals expenditure", is expensed in the year in which the expenditure is incurred.

The depreciation charge for infrastructure assets is determined for each component of the network and is based on each component's cost, estimated residual value and the expected remaining average useful life. The useful average economic lives of the infrastructure components range principally from 35 to 150 years.

### Other assets

Other assets are depreciated on a straight-line basis over their estimated useful economic lives, which are as follows:

Freehold buildings	60 years
Operational structures	5 – 80 years
Plant, equipment and computer hardware	3 – 40 years

Assets in the course of construction are not depreciated until commissioned. Land is not depreciated.

### Borrowing costs

Borrowing costs are general and specific borrowing costs directly attributable to the acquisition, construction and production of qualifying assets are capitalised. Qualifying assets are assets that necessarily take a substantial period of time to get ready for their intended use or sale.



## Notes to the financial statements (continued)

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### Intangible assets

Intangible assets, which comprise principally computer software, system developments and research and development, are included at cost less accumulated amortisation. Cost reflects purchase price together with any expenditure directly attributable to bringing the asset into use, including directly attributable internal costs. Research expenditure is recognised as an expense as incurred. Costs incurred on development projects are recognised as intangible assets when the relevant recognition criteria are met (as per IAS 38).

The carrying values of intangible assets are reviewed for impairment if circumstances indicate they may not be recoverable. Intangible assets are amortised on a straight-line basis over their estimated useful economic lives, which range between 3 and 20 years. These asset lives are reviewed annually.

### Leases

The Company recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, and subsequently at cost less any accumulated depreciation and impairment losses and adjusted for certain re-measurements of the lease liability.

The Company presents right-of-use assets that do not meet the definition of investment property in property, plant and equipment and lease liabilities in borrowings in the balance sheet.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate. Generally, the Company uses its incremental borrowing rate as the discount rate.

The lease liability is subsequently increased by the interest cost on the lease liability and decreased by lease payments made. It is re-measured when there is a change in future lease payment arising from a change in an index or rate or, as appropriate, changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised or a termination option is reasonably certain not to be exercised.

The Company has also elected to apply a single discount rate to the portfolio of leases that are deemed to have reasonably similar characteristics as well as to exclude any initial direct costs in the measurement of the right-of-use asset. The discount rate of 4% is based on the Company's estimated incremental borrowing rate.

All other leases that do not involve right-of-use assets are charged to the income statement over the period of the lease.

When the Company acts as a lessor, it determines at lease inception whether each lease is a finance lease or an operating lease.

To classify each lease, the Company makes an overall assessment of whether the lease transfers substantially all the risks and rewards incidental to ownership of the underlying asset. If this is the case, then the lease is a finance lease; if not, then it is an operating lease. As part of this assessment, the Company considers certain indicators such as whether the lease is for the major part of the economic life of the asset.

The Company has used a number of practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17. In particular the Company:

- did not recognise right of use assets and liabilities for leases for which the lease term ends within 12 months of the date of initial application;
- did not recognise right of use assets and liabilities for leases of low value assets (e.g. IT equipment);
- excluded initial direct costs from the measurement of the right of use asset at the date of initial application: and used hindsight when determining the lease term.

### Grants and customer contributions

Grants and customer contributions in respect of expenditure on property, plant and equipment have been offset against these assets. Grants and customer contributions in respect of revenue expenditure are credited to the income statement over the same period as the related expenditure is incurred.

### Capital expenditure programme incentive payments

The Company's agreements with its construction partners involved in delivering capital expenditure programmes incorporate incentive bonuses payable after completion of the programmes.

## Notes to the financial statements (continued)

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The cost of property, plant and equipment additions includes an accrual for incentive bonuses earned to date, relating to projects substantially completed at the year-end, where the likelihood of making the incentive payment is considered probable. Amounts recoverable from contract partners relating to targets not being achieved are recognised only on completed projects.

### Trade receivables

Trade receivables are recognised initially at fair value and measured subsequently at amortised cost less provision for impairment. They are first assessed individually for impairment, or collectively where the receivables are not significant individually. Where there is no objective evidence of impairment for an individual receivable, it is included in a group of receivables with similar credit risk characteristics and these are assessed collectively for impairment based on the expected credit loss. Movements in the provision for impairment are recorded in the income statement.

### Cash and cash equivalents

Cash and cash equivalents include highly liquid investments that are readily convertible into 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 typically include cash in hand and deposits with banks or other financial institutions.

### Pension benefits

#### i) Defined benefit scheme

The Company operates a defined benefit scheme, the DCWW Pension Scheme, which was closed to future accrual from 1 April 2017 for all members except for 18 ESPS section members. The scheme is funded by employer contributions as well as employee contributions from the remaining active members. Contribution rates are based on the advice of a professionally qualified actuary. The most recent actuarial valuation of the scheme was carried out as at 31 March 2022.

The asset recognised in the balance sheet in respect of defined benefit pension plans is the fair value of plan assets less the present value of the defined benefit obligation at the end of the reporting year. The fair value of these assets has been estimated based on the latest available observable prices, updated with reference to movements in comparable observable indices to the reporting date, and adjusted for judgements to reflect differences in the liquidity and credit components of the asset pricing. The defined benefit obligation is calculated annually by an independent actuary using the projected unit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation. In countries where there is no deep market in such bonds, the market rates on government bonds are used.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise.

Past-service costs are recognised immediately in the income statement.

#### ii) Defined contribution scheme

The Company operates a defined contribution scheme, the DCWW Group Personal Pension Plan, which all employees are eligible to join. Obligations for contributions to the scheme are recognised as an expense in the income statement in the period in which they arise.

## Notes to the financial statements (continued)

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### Other financial liabilities

Debt is measured initially at fair value, being net proceeds after deduction of directly attributable issue costs, with subsequent measurement at amortised cost. Debt issue costs are recognised in the income statement over the expected term of such instruments at a constant rate on the carrying amount.

Trade payables are obligations to pay for goods and services acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year, or in the normal operating cycle of the business.

Derivative instruments utilised by the Company are interest rate swaps, inflation swaps and power hedges. Derivative instruments are used for hedging purposes to alter the risk profile of existing underlying exposures within the Group. Derivatives are recognised initially and subsequently re-measured at fair value. During the year to 31 March 2023, one of the Company's derivatives qualified for hedge accounting (2022: none), but the Company elected not to apply hedge accounting. These instruments are carried at fair value with changes in fair value being recognised immediately in the income statement.

### Financing income and expenses

Financing expenses include interest payable, indexation on index-linked borrowings, index-linked swaps and finance charges on lease liabilities recognised in profit or loss using the effective interest method. Borrowing costs that are directly attributable to the acquisition, construction or production of an asset that takes a substantial time to be prepared for use, are capitalised as part of the cost of that asset. Financing income comprise interest receivable on funds invested.

Interest income and interest payable is recognised in profit or loss as it accrues, using the effective interest method.

### Taxation

The Company continues to invest heavily in capital expenditure for the benefit of our customers. The tax relief for this capital expenditure and the interest we pay to fund it have the effect of delaying corporation tax payments to future periods. Income tax for the year comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in other comprehensive income or directly in equity, respectively. Current tax is the expected tax payable on the taxable income for the year using rates substantially enacted at the balance sheet date, and any adjustments to tax payable in respect of prior years.

Amounts receivable from tax authorities in relation to research and development tax relief under the RDEC scheme are recognised within operating profit in the period in which the research and development costs are treated as an expense. Where amounts are outstanding at the year end and have not been formally agreed, an appropriate estimate of the amount is included within other receivables.

### Deferred taxation

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using 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 income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax has been recognised in relation to rolled-over gains except for where reinvestment has been made in certain operational assets which the Company plans to use until the end of their useful economic life. The Company anticipates that these assets will then be scrapped for negligible proceeds, or proceeds less than their tax base, and therefore no chargeable gain is expected to arise in the future.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised.

## Notes to the financial statements (continued)

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### Provisions

Provisions for restructuring costs, restatement of leakage and per capita consumption performance, uninsured losses and billing disputes are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been estimated reliably. The provision of £15 million for the restatement of leakage and per capita performance represents the Board's decision to apply a £10 refund to every customer's bill in financial year 2023/24. Restructuring provisions comprise employee severance and pension fund top-up costs. Where the Company receives claims that are either not covered by insurance or where there is an element of the claim for which insurance cover is not available, a provision is made for the expected future liabilities. Provisions are not recognised for future operating losses.

Where there is a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligation is small.

### Financing risk management objectives and policies

Treasury activities are managed within a formal set of treasury policies and objectives, which are reviewed regularly and approved by the Board at least annually. The policies specifically prohibit any transactions of a speculative nature and the use of complex financial instruments. Certain detailed policies for managing interest rate, currency, inflation risk and liquidity risk are approved by the Board and may be changed only with the consent of Dŵr Cymru Cyfyngedig's Security Trustee. The risk is mitigated further by limiting the level of exposure to any one counterparty.

The Company uses financial instruments to raise finance and manage operational risk; these instruments principally include listed bonds, leases, bank loan facilities and derivatives.

### Credit risk

The Company's Board approved treasury policy adopts a prudent approach to cash management and timed deposits are placed for a maximum of three months with banks subject to minimum long-term rating criteria of A-/A3/A-. Bonds can be purchased from certain AA-rated counterparties with maturities of up to one year and commercial paper purchases of up to one year can be placed with certain AAA-rated supnationals only. During the year ended 31 March 2023 the maximum cash investment with a single counterparty was £100 million (2022: £100 million).

### Interest rate risk

The Company is covenanted to hedge at least 85% of its total outstanding financial liabilities into either index-linked or fixed rate obligations. As at 31 March 2023, the Company had hedges covering 100% of its total outstanding financial liabilities into either index-linked or fixed rate obligations, including free cash balances (2022: 100%). For this purpose, floating rate interest liabilities are hedged through a combination of derivative instruments and cash balances. The regulatory framework under which revenues and the regulatory asset value are indexed also exposes the Company to inflation risk. Therefore, subject to market constraints and Board approval, the Company may seek to raise new debt through index-linked instruments or enter into appropriate hedging transactions.

The Company analyses its interest rate exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions, alternative financing and hedging. Of total borrowings of £4,186 million as at 31 March 2023 (2022: £4,067 million), at the GCHC Group level, none related to floating rate debt (2022: none). The Company therefore considers overall interest rate exposure at the balance sheet date to be minimal.

As at 31 March 2023, 97.0% (2021: 94.6%) of the Company's gross debt was at fixed or index-linked (RPI) rates of interest after taking into account interest rate and RPI swaps. The hedges established to manage interest rate risks are economic in nature, but do not satisfy the specific requirements in order to be treated as hedges for accounting purposes. Accordingly, all movements in the fair value of derivative financial instruments are reflected in the income statement. This has resulted in a net liability of £67 million in the Company's balance sheet at 31 March 2023 (2022: £182 million) but, assuming that the swaps are held to maturity, this will ultimately reduce to £nil.

### Power price hedges

The Company enters into contracts which fix the price of a proportion of future power purchases in order to reduce the impact of power price variances. These contracts qualify as financial instruments and are included within the financial statements.

## Notes to the financial statements (continued)

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### Refinancing risk

Refinancing risk is managed by maintaining a balance between the continuity of funding and flexibility through the use of borrowings across a range of instruments, types and maturities. The Group's policy is to ensure that the maturity profile does not impose an excessive strain on its ability to repay loans. Under this policy, no more than 20% of the principal of Group borrowings of £4,135 million (2022: £4,019 million) can fall due in any 24 month period.

### Liquidity risk

The Company maintains committed banking facilities in order to provide flexibility in the management of its liquidity. Under the Common Terms Agreement which governs obligations to bondholders and other financial creditors, the Company is required to have cash available to fund operations for 12 months.

As at 31 March 2023, the Company had committed undrawn borrowing facilities of £200 million (2022: £200 million) and cash and cash equivalents (excluding debt service payments account) of £363 million (2022: £473 million). There is also a £10 million overdraft facility renewable on an annual basis.

As at 31 March 2023 there was also a special liquidity facility of £135 million (2022: £135 million); this is required in order to meet certain interest and other obligations that may not be funded through operating cash flow in the event of a standstill being declared by the Security Trustee, following an event of default under the Company's debt financing covenants. The facility has been provided by an insurance provider and is renewable on a rolling five-year evergreen basis.

### Capital risk

The Groups's objective when managing capital is to safeguard its ability to continue as a going concern. Given the regulatory environment in which the Group operates, capital is monitored on the basis of the gearing ratio. This is calculated as net debt (as defined in borrowing covenants) as a proportion of the Company's Regulatory Capital Value as determined by Ofwat and linked to the movements in the Retail Prices Index. As at 31 March 2023 the measure of regulatory gearing was 58% (2022: 58%).

In respect of the risks detailed above, further quantitative disclosures are provided in note 15.

## **Critical accounting estimates and judgements**

The preparation of financial statements conforming to IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates.

### Provision for impairment of trade receivables

Accounting judgement - Collective impairment losses on receivables with similar credit risk are calculated using a statistical model. Management use standardised collection rates to determine the level of bad debts. These are as follows:

Measured debt based on historical data:

- 100% of debt not recovered for a period of over two years old;
- 99% of debt between 1-2 years; and
- 5% of debt less than a year old.

Unmeasured debt based on historical data:

- 100% of debt not recovered for a period of over two years old;
- 99% of debt between 1-2 years; and
- 8% of debt less than a year old.

## Notes to the financial statements (continued)

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### Provision for impairment of trade receivables (continued)

Accounting estimate - The probability of failing to recover a debt is based on expected credit loss, determined by past experience, as shown in the bullet points above, and expected future movements in collection rates, adjusted for changes in external factors (including the estimated impact of the Covid-19 pandemic and the current affordability crisis impacting UK households). The accuracy of the impairment calculation would therefore be affected by unexpected changes to the economic situation, and to changes in customer behaviour. The key sensitivity assumptions used in the provisioning process are as follows:

- A £2 million increase in the provision, equivalent to 1% deterioration in cash collection rates, providing for the current economic situation; and
- 90% of charging orders will be recovered in future periods based on historic trend.

To the extent that the failure to recover debts in arrears alters by 5%, the provision for impairment would increase or decrease by £3.7 million (2022: £5.5 million).

### Intercompany loan expected credit losses

The Company approached its impairment assessment of intercompany loans via historical and forward-looking analyses, using both qualitative and quantitative information. A core focus of the forward-looking analysis was cash flow forecasts for the next two years, to 31 March 2025. This is aligned with the end of Dŵr Cymru Cyfyngedig (DCC, the group's operating company)'s current period of regulated revenues during which there is certainty of billed turnover values. In addition, consideration was made to the long-term viability assessment with a review period over seven years.

The above assessment led management to conclude that the Company's intercompany loan is of low credit risk, and this is supported by the Company's high-quality credit (ratings of A3, A- and A from Moody's, S&P and Fitch respectively). As such, the loan falls within 'stage 1' of IFRS 9's impairment model and 12-month expected credit losses can be calculated. These were determined to be immaterial and therefore no adjustment to carrying values nor additional disclosures were considered necessary.

### Pension benefits

The present value of the pension obligations is dependent on the actuarial calculation, which includes a number of assumptions. These assumptions include the discount rate, price inflation and mortality rates, which are used to calculate the present value of the estimated future cash outflows that will be required to meet the pension obligations. In determining the discount rate to use, the Group considers market yields of high-quality corporate bonds, denominated in sterling, that have time to maturity approximating the terms of the pension liability. Were this discount rate to reduce or increase by 0.1%, the carrying value of the pension obligations as at 31 March 2023 would increase or reduce by £5.7 million (2022: £8.8 million). The key assumptions include: discount rates, price inflation and life expectancy. It should be noted that actual rates may differ from the assumptions used due to changing market and economic conditions and longer or shorter lives of participants and, as such, this represents a key source of estimation uncertainty. Sensitivities in respect of the assumptions used during the year are disclosed in note 21.

If the scheme's assets underperform relative to the discount rate used to calculate the liabilities, this will increase the value of the projected deficit. With the exception of cash, assets consist of pooled investment funds, alternative strategy funds and property funds which are not quoted on an active market. Of total assets amounting to £412 million (2022: £427.5 million), assets with a fair value of £114.8 million (2022: £99.9 million) are Level 3 financial assets; these are considered to be the least liquid and hardest to value and are therefore subject to a higher degree of estimation. The fair value of these assets has been estimated based on the latest available observable prices, updated with reference to movements in comparable observable indices to the reporting date, and adjusted for judgements to reflect differences in the liquidity and credit components of the asset pricing. A 5% movement in the fair value of these Level 3 financial assets would increase or decrease the overall carrying value of the pension liability by £5.7 million (2022: £5 million) (See also note 21).

## Notes to the financial statements (continued)

### Accounting judgement impact on pension benefits

The mortality assumption used to calculate the present value of the pension obligations is broken down into two distinct parts. Firstly, current mortality rates (base table), and secondly, how these rates should allow for future improvements. For the present value calculation, the S3PxA base tables have been used, adjusted for weightings of 101% for males and 104% for females allowing approximately for the error in the S3PxA tables notified by the Continuous Mortality Investigation (CMI) in June 2022, with improvements in line with the CMI 2021 projection model, with a long-term trend rate of 1.0% p.a. We have applied the parameters of  $A = 0.5$ ,  $S \text{ kappa} = 7.0$  and  $W = 10\%$  to the CMI 2021 assumptions. This represents the only change from the judgements adopted last year and has been updated to reflect the mortality experience noted by the CMI in the current year. The CMI model is used by UK pension schemes and insurance companies which need to make assumptions about future mortality rates.

### Accounting for leakage and per capita consumption restatement

The Group is proposing a customer redress package totalling £29 million to address the restatement of the Group's leakage and per capita consumption performance. On 25 May 2023, Ofwat launched an investigation into "Welsh Water leakage performance". Pending Ofwat's investigation and formal acceptance of our proposed customer redress package, the ultimate financial impact remains uncertain. The customer redress package proposed, being made up of an immediate rebate to customers and the foregoing of Regulatory Capital Value (RCV) uplift, which will reduce bills in future periods, represents Ofwat's likely outcome of their investigation, referencing prior enforcement orders issued by Ofwat.

Accounting estimate: The total customer redress package proposed reflects 3.7% of the Group's 2022 regulated revenue, being the Group's best estimate as at 31 March 2023 of Ofwat's likely imposed redress. Were this percentage to increase by 0.1% in absolute terms, the financial impact would increase by £0.8 million.

Accounting judgement: The Group has applied judgement to the proposed structure of the package, splitting the redress between immediate customer rebate and foregoing future RCV. The Group's proposed customer redress package consists of £15 million, representing the Board's decision to apply a £10 refund to every customer's bill in financial year 2023/24, and £14 million for the RCV uplift the Group will forego at PR24. A provision has been recognised for the £15m element as an obligation arose during the year and will be credited to all account holders as at 31 March 2023 in the next 6 months.

A provision is not recognised at 31 March 2013 for the £14m redress element as it represents lower expected prices to be charged to customers to be agreed at a future date through the regulatory mechanism. Under the regulatory mechanism for PR24, the Group is entitled to recover regulatory overspend for 2020/21 and 2021/22 that is attributable to leakage expenditure, but the Group will not take this into account in our RCV uplift on 1 April 2025.

### Fair Value Estimation

In accordance with IFRS 13 Fair Value Measurement trading and treasury derivatives of the Company are categorised into different levels:

- **Level 1:** quoted prices (unadjusted) in active markets for identical assets or liabilities.
- **Level 2:** inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (prices) or indirectly (derived from prices).
- **Level 3:** inputs for the asset or liability not based on observable market data.

All of the Company's treasury derivatives are categorised as Level 2. In accordance with IFRS 13 an adjustment factor has been applied to the swaps based on industry standard practice to take into account credit risk by estimating future cash flows based on applicable interest rate curves. Projected cash flows are then discounted back using discount factors which are derived from the applicable interest rate curves adjusted for management's estimate of counterparty and own credit risk, where appropriate.

Trading derivatives, relating to power price hedges, are categorised as Level 2 where marked-to-market valuations are received for these trades. Where marked-to-market valuations are not received the fair values are estimated rather than observable, and are therefore categorised as Level 3.

At 31 March 2023 the fair values of derivatives were as follows:

**Level 2: Assets:** Trading derivatives £10.0 million, Treasury derivatives £13.8 million (March 2022: Trading derivatives £17.1 million, Treasury derivatives £2.7 Million).

**Liabilities:** Trading derivatives £nil, Treasury derivatives £90.5 million (March 2022: Trading derivatives nil, Treasury derivatives £223.9 million).

**Level 3: Assets:** Trading derivatives £nil (March 2022: Trading derivatives £22.0 million).

**Liabilities:** Trading derivatives £nil (March 2022: Trading derivatives £nil).

## Notes to the financial statements (continued)

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### Fair Value Estimation (continued)

Trading derivatives relate to power hedges. Treasury derivatives relate to interest rate swap contracts. All derivatives are recorded on the balance sheet at fair value.

Level 2 debt investments are valued using a discounted cash flow approach, which discounts the contractual cash flows using discount rates derived from observable market prices of other quoted debt instruments of the counterparties.

Level 3 debt instruments are valued using a discounted cash flow approach, which discounts the contractual cash flows using discount rates derived from observable market prices of other quoted debt instruments of the counterparties. Level 3 debt instruments are valued by comparing valuations from Level 2 trades for the same periods, with the valuations from observable trades being inflated or deflated to allow for any fixed price variations.

### Capitalisation

There is a high degree of judgement involved in determining whether costs, both initial and subsequent expenditure, including employee and other internal expenditure on both infrastructure and non-infrastructure assets meet the relevant criteria for capitalisation (directly attributable to the asset, provide probable economic benefit and can be measured reliably) and therefore are included in the valuation of property, plant and equipment, or alternatively should be expensed immediately. We capitalise expenditure relating to employee costs on both a direct and an indirect basis, through the use of timesheets and estimation of overhead costs that is attributable to a capital project, which is reviewed at a minimum annually. Were our capitalisation percentage to increase or decrease by 5% this would result in a financial impact of £9.3m, based on total employment costs.

This is monitored continually through a process of capital programme cost challenge and operating cost scrutiny, complemented by a third-party analysis of the capital programme breakdown between maintenance costs charged to the income statement and property, plant and equipment additions to the balance sheet.

### Useful economic life impact on depreciation

The estimated useful economic lives of Property, plant and equipment (PPE) and intangible assets is based on management's experience. When management identifies that actual useful economic lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively. Due to the significance of PPE and intangibles investment to the Company, variations between actual and estimated useful economic lives could impact operating results both positively and negatively. As such, this is a key source of estimation uncertainty. The depreciation and amortisation expense for the year was £345.6 million. A 10 per cent increase in average asset lives would have resulted in a £31.5 million reduction in this figure and a 10 per cent decrease in average asset lives would have resulted in a £34.6 million increase in this figure.

### Climate change

The natural environment within which the Company operates is constantly changing, and this influences how its water and wastewater services are to be delivered in the future. The Company has embedded ambitious climate-related targets within its strategic goals, affecting the portfolio of assets required in its operations to deliver such services. We have conducted a high-level review, in line with our TCFD disclosures, for potential impacts of climate change and environmental legislation on the Company's decarbonisation measures predominantly in respect of the valuation of the property, plant and equipment held by the Company and provisions or contingent liabilities. No amendments were considered necessary in the financial statements this year with further analysis to be conducted throughout the new financial year. We will review the impact of climate change on the financial statements annually upon further information becoming available.

The Company will continuously look to further enhance the accuracy of its useful life assessment through the introduction of more forward-looking information in asset life reviews. The Company will continue to mitigate the exposure that the carrying value of its book asset base has to climate-related risks through strategic planning activities that incorporate defined climate scenarios, climate change mitigation pledges, and long-term climate projections. The Company installs permanent flood defences and other resilience measures at the most vulnerable facilities to protect its assets.



## Notes to the financial statements (continued)

### 2. Segmental information

The Directors consider that there is only one operating segment, being the operation of water and sewerage business (and peripheral commercial activities) in the UK. As the Company has only domestic activities there is also only one geographical segment; therefore, the disclosures for this segment have also already been given in these financial statements.

While the Company operates in a single segment, its activities can be disaggregated into the following principal income streams:

	<b>2023</b>	2022
	<b>£m</b>	£m
<b>Regulated revenue</b>		
Water	<b>330.6</b>	321.6
Sewerage	<b>457.3</b>	424.2
Retail	<b>46.9</b>	55.0
<b>Total regulated revenue</b>	<b>834.8</b>	800.8
Other (non-regulated)	<b>6.5</b>	6.2
<b>Total revenue</b>	<b>841.3</b>	807.0

Regulated revenue relates to the provision of water, sewerage and related retail services operating under Dŵr Cymru Cyfyngedig's licence as part of the water industry and England and Wales, regulated by The Office of Water Trading (Ofwat).

Other (non-regulated) revenue relates to income streams which are not subject to Ofwat's price control; these principally comprise organic energy generation and certain other activities which are peripheral and/or complementary to the Company's core water and sewerage business.

On 25 May 2023, Ofwat launched an investigation into "Welsh Water's reporting of leakage and PCC and on 31 May 2023 served a S203 Notice under the Water Industry Act 1991 requiring further information from the Company.

To compensate customers, the Group is proposing customer redress totalling £29 million, of which £15 million has been provided for during the year, with further information available in note 17. The provision has been accounted for in the table above within our regulated Water revenue for the year.

## Notes to the financial statements (continued)

### 3. Operating profit

The following items have been included in arriving at the operating loss:

	2023	2022
	£m	£m
<b>Operating expenditure</b>		
Power	74.3	62.7
Chemicals	21.9	10.5
Materials and equipment	9.6	8.7
Vehicles and plant	6.6	7.6
Office expenses	5.9	5.7
Property costs	3.5	3.5
Insurance	6.6	6.8
Water and Sewerage contractors	27.1	22.4
Laboratories and analytical services	1.4	1.3
Collection commissions	1.9	3.1
IT contracts	14.9	12.9
Bought-in services and other costs	51.0	37.7
	<u>224.7</u>	<u>182.9</u>
Employee costs (note 20)	185.0	165.0
Staff costs capitalised	(79.1)	(67.5)
	<u>105.9</u>	<u>97.5</u>
Research and development credit	(0.5)	(0.6)
Rates	27.0	26.2
Natural Resources Wales/Environment Agency charges	16.3	16.5
Fees payable to auditors	0.7	0.5
<b>Total operational expenditure</b>	<u>374.1</u>	<u>323.0</u>
<b>Impairment of trade and other receivables</b>	<b>24.8</b>	23.7
<b>Other operating income</b>	<b>(5.3)</b>	(6.0)
<b>Exceptional items</b>	<b>30.8</b>	(3.8)
<b>Infrastructure renewals expenditure</b>	<b>78.0</b>	61.8
<b>Depreciation and amortisation</b>		
- Depreciation of property, plant and equipment	318.4	300.3
- Release of deferred income	(12.4)	(10.2)
- Amortisation of intangible assets	39.6	37.7
<b>Total depreciation and amortisation</b>	<u>345.6</u>	<u>327.8</u>
<b>Total operating costs</b>	<u>848.0</u>	<u>726.5</u>

The Company incurred insignificant expenses relating to short-term leases, leases of low-value assets or variable lease payments in 2023 and 2022.

Other operating income principally comprises income from the export of internally generated gas. Exports of renewable electricity is included within power costs as it is treated as a natural hedge to our consumption. Our energy strategy is to enter into contracts which fix the price of consumption less exports of future power purchases in order to reduce the impact of power price variances. During the year, consumption charges amounted to £82.6 million (2022: £76.7 million) and we exported £15.0m (2022: £14.0 million).

#### Services provided by the Company's auditors

During the year the Group headed by Glas Cymru Holdings obtained the following services from its auditors; £630,000 was paid by the Group's wholly-owned subsidiary, Dŵr Cymru Cyfyngedig whilst the remainder were paid by the subsidiaries in the Welsh Water Holdings Limited group:

## Notes to the financial statements (continued)

### 3. Operating profit (continued)

	2023	2022
	£000	£000
<b>Audit fees</b>		
Audit of parent company and consolidated financial statements	68	35
Audit of subsidiary companies	467	305
Total audit fees	<u>535</u>	<u>340</u>
<b>Audit-related assurance services</b>		
Review of interim financial statements	60	33
Regulatory audit services pursuant to legislation	111	84
Investor report reviews	8	4
Price review assurance	3	-
Bond issuance reviews	-	25
Environment Agency levy assurance work	-	6
<b>Total cost of services provided by the Group's Auditors</b>	<u>717</u>	<u>492</u>

Regulatory audit services include audit work in respect of regulatory requirements: the Annual Performance Report.

The Board has adopted a formal policy with respect to services received from external auditors. The external auditors will not be used for internal audit services and all non-audit work will be subject to prior competitive tendering or approval by the Audit Committee.

#### Exceptional item

In the year to 31 March 2023, we have recognised an exceptional item totalling £30.8 million. This item represents the award of pension increases above a 5% cap. Under a 'best endeavours' clause in our pension scheme rules full RPI increases could only be awarded if certain criteria were met. In the current year scheme awards above a 5% cap have been paid by the pension scheme and, as the scheme is now in surplus, these conditions are expected to be paid in the future. Therefore, the expense in the year represents the additional awards given. In the future it is expected that changes to this assumption will be presented in Other Comprehensive Income as required under IAS19. This is disclosed as exceptional as the accounting treatment of these increases through the profit and loss account will only occur this year, it is of a significant value, and it does not closely reflect day-to-day operational expenditure. For the avoidance of doubt management will make consideration of the 'best endeavours' clause in all future periods and as such any movement in estimate will be presented as Other Comprehensive Income as required under IAS19.

In the year to 31 March 2022 we had recognised an exceptional item totalling £(3.8) million. This item represents a release of the bad debt provision as a result of anticipated bad debt charges associated with the Covid-19 pandemic not materialising during the year; this is disclosed as exceptional due to its nature and with the corresponding Covid-19 charge having, in the previous year, been shown as exceptional.

### 4. Net financial expenses

#### a) Financial expenses before fair value gains on derivative financial instruments

	2023	2022
	£m	£m
<b>Financial income</b>	<b>14.7</b>	4.1
Interest payable on loans	(416.0)	(226.6)
Interest payable on leases (including swaps to RPI)	(66.7)	(37.9)
Other interest payable and financial costs	(49.6)	(32.0)
Net interest charge on pension scheme liabilities	(2.1)	(0.9)
Capitalisation of borrowing costs under IAS 23 (2023 7.9%; 2022: 5.0%)	28.3	16.4
<b>Financial expenses</b>	<u>(506.1)</u>	<u>(281.0)</u>
<b>Net financial expenses before fair value adjustments</b>	<u>(491.4)</u>	<u>(276.9)</u>

## Notes to the financial statements (continued)

### 4. Net financial expenses (continued)

Included within financial expenses are amounts payable to group undertakings of £223.7 million (2022: £128.4 million).

#### b) Fair value gains on derivative financial instruments

Derivative financial instruments are held for economic hedging purposes although they do not qualify as accounting hedges. Consequently, the Group's interest rate and index-linked swaps are fair valued at each balance sheet date with the net loss or gain disclosed in the income statement. Over the life of these swaps, if held to maturity, these fair value adjustments will reverse and reduce to zero. (See note 14 in respect of derivative financial instruments recognised on the balance sheet.)

	2023	2022
	£m	£m
Fair value gains/(losses) on interest rate swaps	32.1	(158.4)
Fair value gains on index-linked swaps	112.4	207.4
Fair value (losses)/ gains on trading derivatives	(29.1)	31.4
<b>Fair value gains on derivative financial instruments</b>	<b>115.4</b>	<b>80.4</b>

Interest rate swap movements are caused by fluctuations in long-term swap rates, while the index-linked swap movements result from fluctuations in the value of index-linked gilts.

### 5. Taxation

Analysis of tax credit/(charge) in the year:

	2023	2022
	£m	£m
Current tax		
- Current tax on research and development credit	(0.1)	(0.1)
- Adjustment in respect of prior years	0.2	0.2
Total current tax	0.1	0.1
Deferred tax		
- Origination and reversal of timing differences	89.4	20.5
- Adjustment in respect of prior years	(6.4)	(0.2)
- Effect of tax rate change	-	(54.7)
Total deferred tax credit/(charge) (note 6)	83.0	(34.4)
<b>Taxation</b>	<b>83.1</b>	<b>(34.3)</b>

Current tax is corporation tax which is payable on a company's profit or loss adjusted for tax purposes, and is only charged where a taxable profit arises after these tax adjustments - see current tax reconciliation.

Operating expenditure includes a Research & Development tax credit of £0.6 million (2022: £0.6 million). The tax credit is taxable and the corresponding charge of £0.1 million (2022: £0.1 million) is shown above. The Research & Development Expenditure Credit claimed is a government incentive that provides tax credits for qualifying R&D expenditure. Claims are made based on an assessment of qualifying expenditure in accordance with the criteria specified under the incentive.

Current taxes in respect of prior years of £0.2 million (2022: £0.2 million) relate to tax credits for R&D, energy efficient capital expenditure and the remediation of contaminated land.

Deferred taxes in respect of prior years includes a £7.0 million charge (2022: £nil) arising from movements in deferred taxes resulting from changes to the valuation of interest rate and inflation linked swaps during the year. At 31 March 2022, the underlying temporary difference was expected to reverse after March 2023 when the corporation tax rate would be 25%, and accordingly deferred taxes were calculated using this rate. Following significant changes to the interest rates and inflation during the period, there has been a reversal in the current period in which the corporation tax rate is 19%. The additional tax charge of £7.0 million has been shown as a prior year item as it relates to a change in estimate made in a previous period.

In addition, the prior year deferred tax charge includes a credit of £0.5 million (2022: £0.2 million charge) relating to adjustments to deferred tax balances in respect of capital expenditure.

## Notes to the financial statements (continued)

### 5. Taxation (continued)

Deferred taxes have been calculated at 25%. A rate of 25% was also used for the previous year, with the exception of temporary differences with a tax value of £42.4 million which were expected to reverse in the year ended 31 March 2023. These were calculated using a rate of 19%, being the corporation tax rate applicable to that year.

The company estimates that expenditure of £49 million will qualify for a 130% 'super deduction' (2022: £26 million). Consequently a tax benefit of £2.8 million (£49m x 30% x 19%) has arisen in the period (2022: £1.5 million) which reduces the net deferred tax liability.

The effective rate of tax for the year is higher (2022: lower) than the standard rate of corporation tax in the UK of 19% (2022: 19%). The differences are explained below:

	2023 £m	2022 £m
<b>Total tax reconciliation</b>		
<b>Loss before tax</b>	<b>(382.3)</b>	<b>(115.4)</b>
Loss before tax multiplied by the corporation tax rate in the UK of 19% (2022: 19%)	72.6	21.9
Difference in standard rate of corporation tax (19%) and rate used to calculate deferred taxes (25%)	16.6	-
Effect of:		
Effect of tax rate change on closing deferred tax from 19% to 25%	-	(54.7)
Effect of pension payments in excess of service charge	(6.2)	-
Adjustments in respect of prior years	(2.5)	-
Depreciation charged on non-qualifying assets	(0.2)	(2.4)
Expenses not deductible for tax purposes	-	(0.1)
Corporate interest restriction	-	(0.5)
130% super deduction for plant and machinery	2.8	1.5
Total taxation	<u>83.1</u>	<u>(34.3)</u>

#### Current tax reconciliation

The table below reconciles the notional tax charge at the UK corporation tax rate to the total current tax charge for the year.

	2023 £m	2022 £m
<b>Loss before tax</b>	<b>(382.3)</b>	<b>(115.4)</b>
Expected tax charge (19%)	72.6	21.9
Depreciation in excess of capital allowances	(34.6)	(38.3)
Pension costs in excess of payments	(6.2)	(0.3)
Expenses not deductible for tax purposes	(0.2)	(0.1)
Corporate interest restriction	-	(0.5)
Fair value movements in derivatives - non taxable	21.9	15.3
IFRIC 18 - release of income not taxable	2.3	1.9
Movement in provisions deductible when paid	0.3	1.2
Capitalised interest - tax deductible when capitalised	5.4	3.1
R&D Expenditure Credits taxed in prior years	0.1	0.1
Adjustments in respect of prior years	0.2	0.2
Tax losses carried forward	(61.7)	(4.4)
Total taxation	<u>0.1</u>	<u>0.1</u>

The Company invests heavily in capital expenditure and is therefore able to claim tax relief in the form of capital allowances, a Government tax relief which aims to stimulate this type of investment. As the Company has no shareholders the surpluses it generates help keep water bills down and are also reinvested to improve the quality of services to customers, rather than

## Notes to the financial statements (continued)

### 5. Taxation (continued)

being paid to shareholders as dividends. This reinvestment is often in the form of capital expenditure which attracts further capital allowances. As a result of the Company's profit forecasts and the capital allowances it is able to claim, the Company does not expect to pay corporation tax during AMP7 (2020 – 2025).

The most significant factor impacting the Company's current tax charge is the difference between depreciation charged on property, plant and equipment in the financial statements and the tax relief claimed for this expenditure (capital allowances). Deferred taxes are recognised on the temporary difference between the carrying amount of the fixed assets in the accounts and the amount that will be deductible for tax purposes in future years. Depreciation exceeds the claim for capital allowances as the company is able to determine the amount of capital allowances it claims during each period in accordance with the tax legislation. Capital allowances have not been fully claimed this year, or in the prior period.

Treasury derivative financial instruments are carried at their fair value. Fair value gains and losses arising between balance sheet dates are recognised in the income statement but are not subject to corporation tax. Deferred taxes are recognised on the temporary difference which is equal to the net fair value of the derivatives in the financial statements less the amounts which have been deducted for tax purposes.

During the year the company elected to be treated as a 'qualifying infrastructure company' under the Public Benefit Infrastructure Exemption provided for within the corporate interest restriction legislation. As a result there is no interest restriction for the current period (2022: £0.5 million).

### 6. Deferred tax

Deferred tax is calculated in full on temporary differences under the liability method using a tax rate of 25% (2022: 25%). The movement in the deferred tax provision is as shown below:

	2023	2022
	£m	£m
At 1 April	697.0	473.0
(Credit)/charge to Income Statement	(83.1)	34.4
Charge to Revaluation reserve	148.4	192.3
Charge/(credit) to SOCI - re pensions	31.1	(2.7)
At 31 March	<u>793.4</u>	<u>697.0</u>

Analysis of amounts of deferred tax charged/(credited) to the statement of comprehensive income and revaluation reserve:

	2023	2022
	£m	£m
Defined benefit pension scheme	31.1	2.0
Increase in corporation tax rate – pension scheme	-	(4.7)
<b>Charged/(credited) to the Statement of comprehensive income</b>	<u>31.1</u>	<u>(2.7)</u>
Revaluation of fixed assets	148.4	85.2
Increase in corporation tax rate – revaluation of fixed assets	-	107.1
<b>Charged to the Revaluation Reserve</b>	<u>148.4</u>	<u>192.3</u>

## Notes to the financial statements (continued)

### 6. Deferred tax (continued)

	2023	2022
	£m	£m
Effect of:		
Tax allowances in excess of depreciation	329.4	320.0
Deferred tax on revaluation of fixed assets	565.8	446.1
Capital gains rolled over	4.0	4.0
<b>Deferred tax liability</b>	<b>899.2</b>	<b>770.1</b>
Deferred tax on tax losses c/f	(90.7)	(5.9)
Deferred tax on losses on derivative financial instruments	(16.6)	(45.5)
Pensions	3.7	(19.3)
Other tax differences	(2.2)	(2.4)
<b>Net deferred tax</b>	<b>793.4</b>	<b>697.0</b>

Deferred taxes have been recognised on the temporary difference between the carrying amount of the fixed assets in the accounts and the amounts that will be deductible for tax purposes (capital allowances) in future years. As capital allowances have exceeded the depreciation charged on the fixed assets to date, there is a deferred tax liability of £329.4 million at the balance sheet date (2022: £320.0 million).

A deferred tax liability of £565.8 million (2022: £446.1 million) has also been recognised in relation to revaluation surpluses arising from revaluing fixed assets to reflect Ofwat's 'shadow regulatory capital value'. The associated deferred tax charge is charged to the revaluation reserve.

The company had tax losses of £362.6m carried forward at 31 March 2023 (2022: £23.4m).

Deferred tax assets have been recognised in respect of all tax losses and temporary differences giving rise to deferred tax assets because it is probable that these assets will be recovered. These deferred tax assets will be recovered against the deferred tax liabilities in relation to fixed assets which will reverse in the same periods.

Deferred tax has not been provided on £133.0 million of chargeable gains which have been rolled over where the new asset has been classified as operational structure e.g. concrete tanks. These assets are typically demolished or scrapped at the end of their useful economic life and therefore we do not expect a chargeable gain will arise in the future. If deferred tax were recognised in respect of these gains, then the deferred tax liability at 31 March 2023 would increase by £33.3 million (2022: £33.3 million) being the rolled over gain multiplied by the rate used to calculate deferred taxes of 25% (2022: 25%).

### 7. Revaluation reserve

The economic value of the company's water and sewerage business is derived from the Regulatory Capital Value (RCV) set by Ofwat during its five yearly price reviews. The company considers that a fair value approach to valuing its assets better reflects the underlying value of the assets than historical cost accounting which understates the assets' current value in use.

As at 31 March 2023 the total value of tangible and intangible fixed assets for Dŵr Cymru Cyfyngedig has been revalued to the Company's 'shadow RCV', being the 31 March 2023 RCV published by Ofwat in its PR19 Final determination as adjusted for the impact of any totex over/underspend and the Outcome Delivery Incentive rewards/penalties. The classes of asset impacted are infrastructure assets and operational structures.

The carrying value of assets is reviewed for impairment if circumstances dictate that the carrying value may not be recoverable, asset lines and residual values are reviewed annually.

## Notes to the financial statements (continued)

	2023 £m	2022 £m
<b>Revaluation reserve movement</b>		
<b>Revaluation reserve as at 1 April</b>	<b>914.7</b>	732.1
Revaluation of assets to RCV	593.4	448.4
Depreciation charge on revalued assets	<u>(114.5)</u>	<u>(90.7)</u>
	<b>478.9</b>	357.7
Deferred tax on revaluation	(148.4)	(192.3)
Deferred tax on depreciation charge	<u>21.8</u>	<u>17.2</u>
	<b>(126.6)</b>	(175.1)
<b>Revaluation reserve as at 31 March</b>	<u><b>1,267.0</b></u>	<u>914.7</u>

## 8. Property, plant and equipment

Current year	Freehold land and buildings £m	Infrastructure assets £m	Operational structures £m	Plant, equipment, computer hardware £m	Total £m
<b>Cost or valuation</b>					
At 1 April 2022	42.6	3,029.5	4,891.6	281.4	8,245.1
Revaluation	-	210.8	-	-	210.8
Additions net of grants and contributions	-	205.1	215.0	0.1	420.2
Disposal	(0.6)	-	-	(2.7)	(3.3)
<b>At 31 March 2023</b>	<b>42.0</b>	<b>3,445.4</b>	<b>5,106.6</b>	<b>278.8</b>	<b>8,872.8</b>
<b>Accumulated depreciation</b>					
At 1 April 2022	25.0	-	1,682.7	273.3	1,981.0
Revaluation	-	(71.7)	(310.9)	-	(382.6)
Charge for the year	0.8	71.7	243.2	2.7	318.4
Released on disposal	(0.6)	-	-	(2.6)	(3.2)
<b>At 31 March 2023</b>	<b>25.2</b>	<b>-</b>	<b>1,615.0</b>	<b>273.4</b>	<b>1,913.6</b>
<b>Net book value</b>					
<b>At 31 March 2023</b>	<b>16.8</b>	<b>3,445.4</b>	<b>3,491.6</b>	<b>5.4</b>	<b>6,959.2</b>
<b>At 31 March 2023 (historic cost)</b>	<b>16.8</b>	<b>2,275.9</b>	<b>2,397.9</b>	<b>5.4</b>	<b>4,696.0</b>

The net book value of property, plant and equipment includes £343.3 million in respect of assets in the course of construction (2022: £297.3 million) and £118.0 million of borrowing costs capitalised in accordance with IAS 23 (2022: £96.5 million), of which £25.1 million were additions in the year (2022: £14.3 million).



## Notes to the financial statements (continued)

### 8. Property, plant and equipment (continued)

Prior Year	Freehold land and buildings	Infrastructure assets	Operational structures	Plant, equipment, computer hardware	Total
	£m	£m	£m	£m	£m
<b>Cost or valuation</b>					
At 1 April 2021	43.0	2,798.2	4,734.0	278.6	7,853.8
Additions net of grants and contributions	-	85.5	-	-	85.5
Disposal	-	145.8	157.6	4.0	307.4
At 31 March 2022	(0.4)	-	-	(1.2)	(1.6)
	<u>42.6</u>	<u>3,029.5</u>	<u>4,891.6</u>	<u>281.4</u>	<u>8,245.1</u>
<b>Accumulated depreciation</b>					
At 1 April 2021					
Revaluation	24.1	57.4	1,691.5	272.0	2,045.0
Charge for the year	-	(123.0)	(239.9)	-	(362.9)
Released on disposal	0.9	65.6	231.1	2.7	300.3
At 31 March 2022	-	-	-	(1.4)	(1.4)
	<u>25.0</u>	<u>-</u>	<u>1,682.7</u>	<u>273.3</u>	<u>1,981.0</u>
<b>Net book value</b>					
At 31 March 2022	<u>17.6</u>	<u>3,029.5</u>	<u>3,208.9</u>	<u>8.1</u>	<u>6,264.1</u>
At 31 March 2022 (historic cost)	<u>17.6</u>	<u>2,120.8</u>	<u>2,333.3</u>	<u>7.8</u>	<u>4,479.5</u>

#### Right-of-use assets

Included within the above are right-of-use assets as analysed below:

	Infrastructure assets £m	Operational structures £m	Total £m
<b>Company - 2023</b>			
Net book value at 1 April 2022	657.0	26.4	683.4
Disposal	-	(26.9)	(26.9)
Revaluation	81.6	3.4	85.0
Depreciation charge for the year	(54.0)	(2.8)	(56.8)
Net book value at 31 March 2023	<u>684.6</u>	<u>0.1</u>	<u>684.7</u>
Net book value at 31 March 2023 (historical cost basis)	<u>452.2</u>	<u>0.1</u>	<u>452.3</u>
	Infrastructure assets £m	Operational structures £m	Total £m
<b>Company - 2022</b>			
Net book value at 1 April 2021	633.3	29.0	662.3
Revaluation	62.3	3.0	65.3
Depreciation charge for the year	(38.6)	(5.6)	(44.2)
Net book value at 31 March 2022	<u>657.0</u>	<u>26.4</u>	<u>683.4</u>
Net book value at 31 March 2022 (historical cost basis)	<u>459.9</u>	<u>19.2</u>	<u>479.1</u>

The Company's leases are principally made up of water and sewerage treatment infrastructure assets and equipment in order to carry out its operations.

## Notes to the financial statements (continued)

### 9. Intangible assets

Current year	Cost £m	Amortisation £m	Net book value £m
At 1 April 2022	499.5	(296.3)	203.2
Additions/(charge for the year)	38.6	(39.6)	(1.0)
<b>At 31 March 2023</b>	<b>538.1</b>	<b>(335.9)</b>	<b>202.2</b>

Prior year	Cost £m	Amortisation £m	Net book value £m
At 1 April 2021	462.2	(258.6)	203.6
Additions/(charge for the year)	37.3	(37.7)	(0.4)
At 31 March 2022	499.5	(296.3)	203.2

Intangible assets principally comprise computer software and related system developments.

The net book value of intangible assets includes £33.0 million in respect of assets in the course of construction (2022: £45.1 million).

The net book value of intangible assets includes £12.6 million of borrowing costs capitalised in accordance with IAS 23 (2022: £10.6 million) of which £3.1 million were additions in the year (2022: £2.1 million).

### 10. Trade and other receivables

	2023 £m	2022 £m
<b>Current</b>		
Trade receivables	596.9	558.0
Less provision for impairment of receivables	(73.2)	(69.5)
Trade receivables - net	523.7	488.5
Prepayments and accrued income	108.5	92.3
Other receivables	15.0	10.1
<b>Total trade and other receivables</b>	<b>647.2</b>	<b>590.9</b>

All non-current receivables are due within five years from the balance sheet date.

As at 31 March 2023, based on a review of historical collection rates it was considered that £73.2 million (2022: £69.5 million) of trade receivables were impaired and these have therefore been provided for. The impaired receivables relate mainly to the measured and unmeasured supply of water and sewerage services. Trade receivables aged greater than one month are past due; the net column shows amounts deemed not to be impaired.

The ageing of receivables was as follows:

Current year	Total	Provided	Net
Trade receivables	£m	for £m	£m
Billings in advance	408.1	-	408.1
Under one month	23.1	(0.9)	22.2
Between one and six months	40.2	(1.6)	38.6
Between six months and one year	28.2	(1.1)	27.1
Between one and two years	42.6	(32.8)	9.8
Between two and three years	26.4	(24.2)	2.2
Over three years	28.3	(12.6)	15.7
	<b>596.9</b>	<b>(73.2)</b>	<b>523.7</b>

## Notes to the financial statements (continued)

### 10. Trade and other receivables (continued)

Prior year	Total	Provided	Net
Trade receivables	£m	for	£m
		£m	
Billings in advance	384.6	-	384.6
Under one month	16.2	(1.4)	14.8
Between one and six months	30.1	(3.1)	27.0
Between six months and one year	22.6	(1.8)	20.8
Between one and two years	32.2	(30.1)	2.1
Between two and three years	22.0	(20.3)	1.7
Over three years	50.3	(12.8)	37.5
	<u>558.0</u>	<u>(69.5)</u>	<u>488.5</u>

Movements in the provision for impairment of trade receivables are as follows:

	2023	2022
	£m	£m
At 1 April	69.5	77.8
Charge to income statement	23.7	18.8
Receivables written off during the year as uncollectable	<u>(20.0)</u>	<u>(27.1)</u>
<b>At 31 March</b>	<b><u>73.2</u></b>	<b><u>69.5</u></b>

During the year the Company has written off £20.0 million of debt which had been provided for in full (2022: £27.1 million).

The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivable mentioned above.

The risk of impairment of other classes of trade and other receivables is very low. All trade and other receivables are denominated in sterling.

The tables below illustrate the impact of applying the “expected loss” model in accordance with IFRS 9. Debt provisioning is based on historical experience as adjusted for certain forward-looking factors, including the impact of charging orders which improve the underlying collectability of debt. The Company holds around 7,400 charging orders as collateral against £12 million of debt (2022: 7,000 orders against £12 million of debt).

Current year	Historical default rates %	Forward- looking adjustment %	Adjustment total %	Historical impairment £m	Forward- looking adjustment £m	Total impairment £m
Billed in advance	-	-	-	-	-	-
< 1 month	5.2%	(1.2%)	4.1%	1.2	(0.3)	0.9
1 > 6 months	5.2%	(1.2%)	4.1%	2.1	(0.5)	1.6
6 months > 1 year	5.2%	(1.2%)	4.1%	1.5	(0.3)	1.2
1 > 2 years	79.4%	(2.6%)	76.8%	33.9	(1.1)	32.8
2 > 3 years	93.3%	(1.5%)	91.8%	24.6	(0.4)	24.2
> 3 years	82.3%	(9.4%)	72.9%	15.1	(2.6)	12.5
	-	-	-	<u>78.4</u>	<u>(5.2)</u>	<u>73.2</u>

## Notes to the financial statements (continued)

### 10. Trade and other receivables (continued)

Prior year	Historical default rates %	Forward- looking adjustment %	Adjustment total %	Historical impairment £m	Forward- looking adjustment £m	Total impairment £m
Billed in advance	-	-	-	-	-	-
< 1 month	9.2%	(0.9%)	8.3%	1.9	(0.2)	1.7
1 > 6 months	10.2%	(0.9%)	9.3%	4.0	(0.4)	3.6
6 months > 1 year	11.4%	(0.9%)	10.5%	3.4	(0.3)	3.1
1 > 2 years	73.9%	(0.9%)	73.0%	30.6	(0.4)	30.2
2 > 3 years	75.9%	(2.8%)	73.1%	21.5	(0.9)	20.6
> 3 years	78.1%	(7.8%)	70.3%	12.2	(1.9)	10.3
				<u>73.6</u>	<u>(4.1)</u>	<u>69.5</u>

The Company's trade receivables provisioning methodology incorporates an "expected loss" model which also determines an appropriate level of losses against which to provide in the measured income accrual. The impact on the accrual as at 31 March 2023 is £4.1m, being a revenue provision of 5% against a gross balance of £82.0 million (2022: £4.0 million and 5%).

### 11. Cash and cash equivalents

	2023 £m	2022 £m
Cash at bank and in hand	26.3	53.8
Short-term deposits	336.3	449.9
	<u>362.6</u>	<u>503.7</u>

The effective interest rate on short-term deposits as at 31 March 2023 was 3.9% (2022: 0.7%) and these deposits had an average maturity of 46 days (2022: 31 days). All cash and cash equivalents were held in sterling.

### 12. Trade and other payables

	2023 £m	2022 £m
<b>Current</b>		
Trade payables	64.2	49.5
Capital payables	56.1	38.4
Amounts due to group undertakings	-	1.3
Social security and other taxes	3.6	3.8
Accruals and deferred income	561.1	521.5
	<u>685.0</u>	<u>614.5</u>
<b>Non-current</b>		
Deferred income	540.8	447.1

### 13. Other financial liabilities – borrowings

	2023 £m	2022 £m
<b>Current</b>		
Overdrawn funds	-	2.5
Interest accruals	30.2	7.5
Loans due to group undertakings	19.4	19.4
Term loans	44.0	36.3
Other unsecured loans	0.2	0.0
Lease liabilities	0.9	17.6
	<u>94.7</u>	<u>83.3</u>

## Notes to the financial statements (continued)

### 13. Other financial liabilities – borrowings (continued)

	2023	2022
Non-current	£m	£m
Interest accruals	20.1	40.1
Loans due to group undertakings	3,554.8	3,225.4
Term loan	486.3	502.1
Other unsecured loans	-	0.2
Lease liabilities	377.2	378.0
	<u>4,438.4</u>	<u>4,145.8</u>

A security package was granted by Dŵr Cymru Cyfyngedig (DCC), as part of the Company's bond programme for the benefit of holders of senior bonds, finance lessors and other senior financial creditors. The obligations of DCC are guaranteed by the Company, Glas Cymru (Securities) Cyfyngedig and Dŵr Cymru (Holdings) Limited. The main elements of the security package are:

- i) a first fixed and floating security over all of DCC's assets and undertaking, to the extent permitted by the Water Industry Act, other applicable law and its licence; and
- ii) a fixed and floating security given by the guarantors referred to above which are accrued on each of these companies' assets including, in the case of Dŵr Cymru (Holdings) Limited, a first fixed charge over its shares in DCC.

The Group's Class A Bonds of £1,141 million (2022: £1,075 million) benefit from a guarantee from Assured Guaranty UK Ltd. Assured Guaranty's credit rating is graded as A1/AA by Moody's, Standard and Poor's and is not rated by Fitch. The credit rating of the Class A bonds has therefore defaulted to the higher of the financial guarantor's rating or the underlying rating of these bonds of A1/AA/A from Moody's, Standard and Poor's and Fitch respectively. The underlying rating (A3/A-/A) reflects the standalone credit quality of these bonds without the benefit of the guarantee from Assured Guaranty, and is the same as the credit ratings of the Group's Class B bonds of £1,517 million (2022: £1,422 million).

The Group's Class C bonds of £500 million (2022 £500 million) were rated Baa2/BBB/BBB+ by Moody's Standard & Poor's and Fitch respectively.

All of the Group's bonds are on-lent from Dŵr Cymru (Financing) UK Plc to Dŵr Cymru Cyfyngedig.

## Notes to the financial statements (continued)

### 14. Other financial assets and liabilities - derivative financial instruments

Derivative financial instruments are held for economic hedging purposes. However, they do not qualify as accounting hedges and movements in their fair value are taken to the income statement (see note 4b).

2023	Fair values	
	Assets £m	Liabilities £m
<b>Current</b>		
Index-linked swaps	3.6	(10.3)
Interest rate swaps (intercompany)	3.3	(5.3)
Power hedging swaps	5.8	-
	<u>12.7</u>	<u>(15.6)</u>
<b>Non-current</b>		
Index-linked swaps	0.4	(44.2)
Interest rate swaps (intercompany)	6.5	(30.7)
Power hedging swaps	4.2	-
	<u>11.1</u>	<u>(74.9)</u>
<b>Total</b>	<u>23.8</u>	<u>(90.5)</u>
2022	Fair values	
	Assets £m	Liabilities £m
<b>Current</b>		
Index-linked swaps	0.5	(39.4)
Interest rate swaps (intercompany)	-	(7.5)
Power hedging swaps	30.9	-
	<u>31.4</u>	<u>(46.9)</u>
<b>Non-current</b>		
Index-linked swaps	2.2	(126.2)
Interest rate swaps (intercompany)	-	(50.8)
Power hedging swaps	8.2	-
	<u>10.4</u>	<u>(177.0)</u>
<b>Total</b>	<u>41.8</u>	<u>(223.9)</u>

The Company has reviewed all contracts for embedded derivatives that are required to be accounted for separately if they do not meet certain requirements set out in IFRS 9; the Company has no such embedded derivatives.

#### Interest rate swaps

At 31 March 2023 an interest rate swap fixes the interest rate on £192 million (2022: £192 million) of floating liabilities held by Dŵr Cymru (Financing) Limited and on-lent to the company. The maturity date of the swap is 31 March 2031 and the annual fixed interest rate is 5.67%, payable quarterly.

#### Index-linked swaps

##### Lease swaps

The index-linked swaps have the effect of index-linking the interest rate on £378 million (2022: £379 million) of lease liabilities by reference to the Retail Prices Index (RPI).

The notional amount of index-linked swaps allocated to leases as at 31 March 2023 was £384 million (2022: £389 million), representing the average balance on the leases subject to floating interest rates for the year to 31 March 2023. The notional amount amortises over the life of the swaps to match the average floating rate balances of the leases.

The principal terms of the index-linked swaps are as follows:

- Notional amount: £384 million amortising (2022: £389 million amortising)
- Average swap maturity: 12 years (2022: 14 years)
- Average interest rate: 1.64% fixed plus RPI (2022: 1.63% fixed plus RPI)

## Notes to the financial statements (continued)

### 15. Financing risk management

The policies of the Company in respect of financial risk management are included in the accounting policies note on pages 34 and 35. The numerical financial instrument disclosures as required by IFRS 7 are set out below.

#### a) Interest rate risk

The effective interest rates at the balance sheet dates were as follows:

	2023	2022
<b>Assets:</b>		
Cash and cash equivalents	3.9%	0.7%
<b>Liabilities:</b>		
Intercompany loans	4.6%	3.1%
Term loans	3.0%	0.6%
Other unsecured loans	4.6%	4.3%
Lease obligations	6.1%	2.3%

Trade and other receivables and payables are non interest-bearing.

The effective interest rates ignore the effect of the interest rate and index-linked swaps set out in note 14. They also exclude the indexation charge applicable to certain portions of the intercompany loan.

#### b) Liquidity risk

2023	Within 1 year £m	1 - 2 years £m	2 - 5 years £m	> 5 years £m	Total £m
<b>Assets:</b>					
Cash and cash equivalents	362.6	-	-	-	362.6
Trade and other receivables	647.2	-	-	-	647.2
	<u>1,009.8</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,009.8</u>
<b>Liabilities:</b>					
Intercompany loan	19.4	19.7	1,112.1	2,423.0	3,574.2
Term loans	44.0	71.0	185.9	229.4	530.3
Other unsecured loans	0.2	-	0.1	-	0.3
Finance lease obligations	0.9	250.8	33.0	93.4	378.1
Trade and other payables	685.0	12.4	37.1	491.3	1,225.8
Future interest payable	161.4	148.2	333.8	698.8	1,342.2
	<u>910.9</u>	<u>502.1</u>	<u>1,702.0</u>	<u>3,935.9</u>	<u>7,050.9</u>
<b>2022</b>	<b>Within 1 year £m</b>	<b>1 - 2 years £m</b>	<b>2 - 5 years £m</b>	<b>&gt; 5 years £m</b>	<b>Total £m</b>
<b>Assets:</b>					
Cash and cash equivalents	503.7	-	-	-	503.7
Trade and other receivables	590.9	-	-	-	590.9
	<u>1,094.6</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,094.6</u>
<b>Liabilities:</b>					
Cash and cash equivalents	2.5	-	-	-	2.5
Intercompany loan	19.4	22.2	624.3	2,578.9	3,244.8
Term loans	36.3	65.3	188.8	248.0	538.4
Other unsecured loans	-	-	0.1	0.1	0.2
Lease liabilities	17.6	1.0	282.6	94.4	395.6
Trade and other payables	614.5	10.2	30.6	406.3	1,061.6
Future interest payable	128.8	114.8	314.5	583.7	1,141.8
	<u>819.1</u>	<u>213.5</u>	<u>1,440.9</u>	<u>3,911.4</u>	<u>6,384.9</u>

## Notes to the financial statements (continued)

### 15. Financing risk management (continued)

The minimum lease payments fall due as follows:

	2023 £m	2022 £m
<b>Gross lease liabilities</b>		
Within one year	24.0	24.5
Between two and five years	319.5	257.5
After five years	127.4	167.6
	<u>470.9</u>	<u>449.6</u>
Future interest	(92.8)	(54.0)
<b>Net lease liabilities</b>	<u>378.1</u>	<u>395.6</u>
Net lease liabilities are repayable as follows:		
<b>Within one year (note 13)</b>	<u>0.9</u>	<u>17.6</u>
Between two and five years	283.8	283.6
After five years	93.4	94.4
<b>Total over one year (note 13)</b>	<u>377.2</u>	<u>378.0</u>

#### c) Fair values

The fair values of the Company's derivative financial instruments are set out in note 14. The fair value of the intercompany loan is £3,052.5 million (2022: £3,702.9 million). The fair values of the Company's other non-derivative financial instruments are equal to the book values.

#### d) Borrowing facilities

At 31 March 2023 Dŵr Cymru (Financing) UK PLC had a special liquidity facility of £135 million (2022: £135 million), which it is required to maintain in order to meet certain Group interest and other obligations that cannot be funded through operating cashflow of the Company, in the event of a standstill being declared by the Security Trustee. A standstill would arise in the event that Dŵr Cymru Cyfyngedig defaults on its debt financing covenants. The facility is a 5 year evergreen facility provided by an insurance provider.

All of the above facilities are at floating rates of interest.

#### e) Capital risk management

##### Gearing ratios (Glas Cymru Holdings Cyfyngedig group)

	2023 £m	2022 £m
Total borrowings	(4,185.6)	(4,065.5)
Less: cash and cash equivalents	379.4	515.1
Net debt	<u>(3,806.2)</u>	<u>(3,550.4)</u>
Regulatory capital value (RCV)	7,161.3	6,460.3
Total capital	3,355.1	2,909.9
Less: unamortised bond costs and swap indexation	(357.2)	(170.7)
Total capital per bond covenants	<u>2,997.9</u>	<u>2,739.2</u>
<b>Gearing ratio</b>	<u>58%</u>	<u>58%</u>

As set out on pages 35, the Company monitors its capital structure based on a regulatory gearing ratio which compares its net debt with the Ofwat-determined RCV.

Under the Common Terms Agreement regulatory gearing is calculated as the level of net debt in the whole business securitisation relative to the regulatory capital value.



## Notes to the financial statements (continued)

### 16. Provisions

	Restructuring provision £m	Uninsured loss provision £m	Other provision £m	Provision for loss on swap closure £m	Total £m
At 1 April 2022	3.7	4.3	0.5	0.6	9.1
Charged to income statement	-	1.1	15.0	(0.1)	16.0
Unused amounts reversed	-	-	-	-	-
Utilised in year	(0.6)	(0.8)	-	-	(1.4)
<b>At 31 March 2023</b>	<b>3.1</b>	<b>4.6</b>	<b>15.5</b>	<b>0.5</b>	<b>23.7</b>

#### Split as amounts to be utilised:

Within one year	1.4	1.4	15.0	-	17.8
After more than one year	1.7	3.2	0.5	0.5	5.9
<b>At 31 March 2023</b>	<b>3.1</b>	<b>4.6</b>	<b>15.5</b>	<b>0.5</b>	<b>23.7</b>

	Restructuring provision £m	Uninsured loss provision £m	Other provision £m	Provision for loss on swap closure £m	Total £m
At 1 April 2021	10.5	4.6	0.5	0.7	16.3
Charged to income statement	-	1.3	-	(0.1)	1.2
Unused amounts reversed	(4.8)	-	-	-	(4.8)
Utilised in year	(2.0)	(1.6)	-	-	(3.6)
At 31 March 2022	3.7	4.3	0.5	0.6	9.1
Split as amounts to be utilised:					
Within one year	1.4	1.4	-	-	2.8
After more than one year	2.3	2.9	0.5	0.6	6.3
At 31 March 2022	<b>3.7</b>	<b>4.3</b>	<b>0.5</b>	<b>0.6</b>	<b>9.1</b>

#### Restructuring provision

This provides for the cost of a reduction in the headcount of 182 to meet a challenging cost efficiency target for the regulatory period 2020 to 2025. This forecast is reassessed each year.

For the year to 31 March 2022, £4.8 million restructuring cost was released following lower-than-expected headcount reductions in the prior year, partially recovered through natural attrition and a delay in the profiling of reductions. This amount was written back to the income statement.

#### Uninsured loss provision

This provision is in respect of uninsured losses and instances where insurance does not cover a deductible amount. The utilisation period of these liabilities is uncertain due to the nature of claims but is estimated to be within five years.

#### Other provisions

Other provisions are made for certain other obligations which arise during the ordinary course of the Company's business.

Dwr Cymru's 2021-22 Annual Report and Accounts disclosed that reported leakage and per capita consumption (PCC) data for 2020-21 and 2021-22 was subject to an ongoing internal review. This included an independent report into leakage and PCC reporting which identified two main areas of non-compliance with the Ofwat prescribed methodology for reporting Leakage and PCC. The reviews concluded that reported leakage performance had been understated for the two years and that reported PCC data had been overstated for the same period. We shared with Ofwat the detailed findings of our review, including remedial actions to be taken to address the control weaknesses identified, and our proposed customer redress. On 25 May 2023, Ofwat launched an investigation into "Welsh Water's reporting of leakage and PCC and on 31 May 2023 served a S203 Notice under the Water Industry Act 1991 requiring further information from the Company.

To compensate customers, the Company is proposing customer redress totalling £29 million. Our ultimate financial liability for this matter remains uncertain pending Ofwat's formal acceptance of our proposed customer redress package and the outcome of its own investigation. Having due regard to these uncertainties, we have, under other provisions, provided for £15 million of the total £29 million customer redress package, representing the Board's decision to apply a £10 refund to every customer's bill in financial year 2023-24. The remaining £14 million represents the Regulatory Capital Value (RCV) uplift the Company will forego at PR24. Under the regulatory mechanism for PR24, the Company is entitled to recover regulatory overspend for 2020-21 and 2021-22 that is attributable to leakage expenditure, but we will not take this into

## Notes to the financial statements (continued)

### 16. Provisions (continued)

account in our RCV uplift on 1 April 2025. As we are unable to set a provision in the financial statements for changes to future RCV, this element of the customer redress package is only disclosed in the financial statements.

### 17. Share capital

	2023	2022
	£m	£m
<b>Authorised</b>		
501,050,000 (2022: 501,050,000) ordinary shares of £1 each	<u>501.1</u>	<u>501.1</u>
<b>Allotted and fully paid</b>		
309,876,374 (2022: 309,876,374) ordinary shares of £1 each	<u>309.9</u>	<u>309.9</u>

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

### 18. Net cash flow from operating activities

#### a) Cash generated from operations

Reconciliation of operating (loss)/profit to cash generated from operations:	<b>2023</b>	2022
	£m	£m
Operating (loss)/profit	(6.7)	80.5
<b>Adjustments for:</b>		
Depreciation and amortisation	345.6	327.8
<b>Changes in working capital:</b>		
Increase in trade and other receivables	(56.4)	(23.5)
Increase in trade and other payables	51.7	50.6
Increase in inventories	(1.0)	-
Pension contributions	29.6	-
Decrease in provisions	14.6	(7.2)
	<u>38.5</u>	<u>19.9</u>
<b>Cash generated from operations</b>	<u>377.4</u>	<u>428.2</u>

We have recognised an exceptional item which represents the award of pension increases above a 5% cap. Under a 'best endeavours' clause in our pension scheme rules full RPI increases could only be awarded if certain criteria were met. No additional cash contributions were required by the Group to award these increases.

#### b) Interest paid

	<b>2023</b>	2022
	£m	£m
Interest payable per Income Statement	506.1	281.0
<b>Less non-cash items:</b>		
Indexation on index-linked bonds	(348.0)	(160.5)
Indexation on index-linked debt	(33.9)	(18.0)
Amortisation of bond issue costs	(1.5)	(1.5)
Interest charge on pension scheme liabilities	(2.1)	(1.6)
Amortisation of bond issue premium	0.8	0.8
Effect of capitalisation under IAS 23	28.3	16.4
(Decrease)/increase in accruals	(2.9)	0.9
	<u>(356.5)</u>	<u>(163.5)</u>
<b>Interest paid</b>	<u>149.6</u>	<u>117.5</u>

## Notes to the financial statements (continued)

### 19. Analysis and reconciliation of net debt

Net debt is defined as the value of cash and cash equivalents and the intercompany loan less net accrued interest and total borrowings.

a) Net debt at the balance sheet date may be analysed as:	2023 £m	2022 £m
Cash and cash equivalents	<u>362.6</u>	<u>503.7</u>
	<b>362.6</b>	<b>503.7</b>
Debt due after one year	(4,041.1)	(3,727.7)
Debt due within one year	(63.6)	(58.2)
Lease liabilities	(378.1)	(395.6)
Accrued interest	<u>(50.3)</u>	<u>(47.6)</u>
	<b>(4,533.1)</b>	<b>(4,229.1)</b>
<b>Net debt</b>	<b>(4,170.5)</b>	<b>(3,725.4)</b>
b) The movement in net debt during the year may be summarised as:	2023 £m	2022 £m
Net debt at start of year	(3,725.4)	(3,612.9)
Movement in net cash	(141.1)	294.9
Movement in debt	<u>78.4</u>	<u>(229.1)</u>
<b>Movement in net debt arising from cash flow</b>	<b>(62.7)</b>	<b>65.8</b>
Movement in accrued interest	(2.7)	0.9
Indexation of index-linked debt	(379.0)	(178.5)
Other non-cash movements	<u>(0.7)</u>	<u>(0.7)</u>
<b>Movement in net debt during the year</b>	<b>(445.1)</b>	<b>(112.5)</b>
<b>Net debt at end of year</b>	<b>(4,170.5)</b>	<b>(3,725.4)</b>

Non-cash movements relate to the recognition of lease liabilities under IFRS 16.

### 20. Employees and Directors

#### a) Directors' emoluments

The aggregate emoluments of the Directors of Dŵr Cymru Cyfyngedig for their services as Directors of the Company are set out below:

	2023 £000	2022 £000
Salary (including benefits in kind)	1,089	1,119
Fees	<u>605</u>	<u>556</u>
	<b>1,694</b>	<b>1,675</b>
Long-term incentive plan	-	<u>146</u>
<b>Highest paid Director: P Perry (2022: P Perry)</b>		
Aggregate emoluments <sup>1</sup>	<u>380</u>	<u>503</u>
Accrued pension under defined benefit scheme	412	73
Long-term incentive plan	-	99

<sup>1</sup> excluding pension accrual and long-term incentive plan

## Notes to the financial statements (continued)

### 20. Employees and Directors (continued)

Retirement benefits are accruing for one Director (2022: one) under defined benefit schemes. None of the Directors are a member of the defined contribution scheme (2022: none).

Remuneration payable to the Executive Directors in respect of the financial year ended 31 March 2023 was as follows:

- When reviewing Executive salaries, the Committee considered the proposed increases for the wider workforce, and business and individual performance to date in FY23, and the rates of the National Living Wage and Real Living Wage. The Committee decided to accept the recommendation of the Executive Directors that it would be appropriate to award an increase lower than the increase for the wider workforce. The wider workforce had an agreement in place to award an increase in line with CPIH in December. However, in partnership with our trade unions we agreed an increase of 6.2%, (3% lower than CPIH in December 2022) and a cost of living payment of £2,000. The Executive team members were awarded a 4.0% increase. All increases were with effect from April 2023.
- Under the AVPS, up to 100% of salary can be earned in any year. The overall performance achieved for FY23 in the Executive Directors' AVPS was 41.39%. This compares with 40% in 2021-22.
- Under the LTVPS for the period 2020 to 2025, performance is assessed annually against interim goals. Interim payments are made up to 60% of maximum for each of the two elements: Totex performance; and Overall ODI outcomes for performance development measures. Overall performance is assessed over the five-year period of the AMP. This could result in payment or recovery of any under or overpaid amounts in the final year.
- The scorecard outcomes under both the AVPS and LTVPS were, in the Committee's view, a balanced reflection of the business performance in a very challenging year for the business and the wider water industry. However, as announced on 11 May 2023, the Executive Directors have elected to waive their entitlement to a variable pay-out in respect of FY23 under both the AVPS and the LTVPS and the Committee accepted this. While a number of the AVPS and LTVPS targets were either partially or fully met, this decision reflects the individuals' recognition of their duties to manage the environmental impact of our operations (particularly river water quality). The Executive Directors are aware of the high level of public sentiment in this regard, and in a year when the extreme weather events impacted our wider ability to manage these challenges, Peter Perry and Mike Davis did not feel it appropriate to receive variable pay for FY23.

(Further details are provided in the 2023 Remuneration Report which forms part of GCHC's 2023 annual report and consolidated financial statements.)

#### b) Staff costs during the year

	2023	2022
	£m	£m
Wages and salaries	156.3	137.9
Social security costs	17.6	14.9
Other pension costs	11.1	12.2
	<u>185.0</u>	<u>165.0</u>

Of the above, £79.1 million (2022: £67.5 million) has been capitalised, being the investment cost of employees' work on the capital programme.

#### Average monthly number of people (including executive directors) employed by the Company

	2023	2022
	Number	Number
Regulated water and sewerage activities	<u>3,554</u>	<u>3,547</u>

The Board delegates certain of the Company's strategic and operational activities to the Dŵr Cymru Executive, a senior management group comprising both executive Directors and employees. Total remuneration of these key personnel was as follows:

	2023	2022
	£m	£m
Executive Directors	1.1	1.1
Other key personnel	3.5	3.3
	<u>4.6</u>	<u>4.4</u>

## Notes to the financial statements (continued)

### 21. Pension commitments

The Company operates a funded defined benefit pension scheme for current employees (based on final pensionable salary and pensionable service), the DCWW Pension Scheme. The assets of the scheme are held in a separate trustee-administered fund.

The Welsh Water Pension Scheme was closed to new members from 31 December 2005 and closed to the majority of sections of the scheme to future accruals from 1 April 2017. A new defined contribution scheme, the Dŵr Cymru Defined Contribution Scheme, was introduced from 1 January 2006.

#### EFRBS

During 2011, the Company put arrangements in place via an Employer-Financed Retirement Benefit Scheme (EFRBS) for four 'capped' Executive Members of the scheme. The accrual of benefits under this agreement is conditional on remaining a member of the DCWW Pension Scheme. At 31 March 2023, there were two remaining Executive Members with entitlements under this arrangement, one of whom is in receipt of his benefits.

#### Risks

Through the Scheme, the Company is exposed to numerous risks, the most significant of which are detailed below:

- Asset volatility:

Scheme liabilities are calculated using discount rates set with reference to bond yields (although discount rate methodology differs for accounting and funding purposes). If Scheme assets deliver a return which is lower than the discount rate, this will create or increase the Scheme deficit (all other things being equal). The Scheme holds various return seeking assets which are expected to outperform bonds in the long-term, albeit at the risk of short-term volatility.

- Movement in bond yields:

A decrease in corporate bond yields will increase the Scheme liabilities, although this will be partially offset by an increase in the value of the Scheme's bond holdings.

- Inflation risk:

As a large majority of the members' benefits are linked to inflation (subject to maximum annual caps), a high level of inflation will result in an increase of benefits attributable to the members, which will in turn increase the Scheme's liabilities.

- Life expectancy:

The Scheme's obligations are to provide members with benefits for the remainder of their lives, so an increase in life expectancy will result in the Scheme paying members' benefits over a longer period, which will in turn increase the Scheme's liabilities.

#### Defined benefit scheme

A full actuarial valuation of the scheme was undertaken as at 31 March 2022 by Joanne Eynon of Quantum Advisory, an independent, professionally qualified actuary, using the projected unit method. This valuation has been updated at 31 March 2023 and the principal assumptions made by the actuaries were:

	2023	2022
Discount rate	4.6%	2.8%
RPI Inflation assumption	3.3%	3.7%
Rate of uncapped pension increases	3.3%	N/A
Rate of capped pension increases	3.2%	3.5%
Post retirement mortality (life expectancy):		
- Current pensioners aged 65 - males	86.8 years	86.8 years
- Current pensioners aged 65 - females	89.0 years	89.2 years
- Future pensioners aged 65 (currently aged 45) - males	87.8 years	87.8 years
- Future pensioners aged 65 (currently aged 45) - females	90.2 years	90.3 years

Mortality experience since 2020 does not provide reliable data to set a future assumption due to the effects of COVID 19. The disclosures at 31 March 2023 therefore use the CMI 2021 mortality projection model with an initial improvement parameter of 0.5 and a 10% weighting applied to 2020 and 2021 mortality experience. Other CMI parameters are as in the core model, with a long-term trend rate of 1.0% p.a.

The inflation risk premium (IRP) remains the same as the prior year at 0.4%.

## Notes to the financial statements (continued)

### 21. Pension commitments (continued)

Changes in the defined benefit obligation are as follows:

	2023 £m	2022 £m
At 1 April	504.5	528.9
Current service cost	0.2	0.4
Interest expense	14.0	10.3
Remeasurement: (gain)/loss from change in financial assumptions	(135.7)	(18.5)
Benefits paid	(16.4)	(16.6)
Past service cost	30.8	-
At 31 March	<u>397.4</u>	<u>504.5</u>

Changes in the fair value plan assets are as follows:

	2023 £m	2022 £m
At 1 April	427.5	442.7
Interest income	11.7	8.7
Actuarial (losses)/gains	(11.2)	(8.0)
Contributions	0.5	0.7
Benefits paid	(16.4)	(16.6)
At 31 March	<u>412.1</u>	<u>427.5</u>

#### Scheme assets

	2023 £m	2022 £m
Cash	9.7	5.3
Equity and Bonds	287.6	322.3
Other	114.8	99.9
<b>Total assets</b>	<u>412.1</u>	<u>427.5</u>

With the exception of cash, assets consist of pooled investment funds which are not quoted on an active market, shown by category in the table above. Of the total, assets with a fair value of £114.8 million (2022: £99.9 million) are Level 3 financial assets; these are considered to be the least liquid and hardest to value, and are therefore subject to a higher degree of estimation. See also the critical accounting estimates in note 1. Experience gains and losses are differences between the actual events as they have turned out and the assumptions that they were made as at the date of the earlier actuarial valuation and changes in the actuarial assumption during the year.

Charges to the income statement and other comprehensive income are as follows:

	2023 £m	2022 £m
<b>Income statement:</b>		
Service costs	0.2	0.4
Interest costs	2.2	1.7
Exceptional pension increases	30.8	-
<b>Total charged to the income statement</b>	<u>33.2</u>	<u>2.1</u>
<b>Other comprehensive income:</b>		
Actuarial loss on plan assets	(11.2)	(8.0)
Actuarial gain on defined benefit obligation	135.7	18.5
<b>Total credit to the statement of comprehensive income</b>	<u>124.5</u>	<u>10.5</u>

A past service cost of £30.8 million has been recognised during the year representing the award of pension increases under the 'best endeavours' clause in our pension scheme rules where full RPI increases are awarded if certain criteria are met. This has been recognised as an exceptional item as our defined benefit liability at 31 March 2023 provides for future pension increases above the 5% 'best endeavours' clause cap and as such any movement in estimate in future periods will be presented as Other Comprehensive Income as required under IAS 19. Further information on the recognition of the exceptional item is available in note 3 on page 41.

## Notes to the financial statements (continued)

### 21. Pension commitments (continued)

	2023 £m	2022 £m
Present value of funded obligations	(397.4)	(504.5)
Fair value of plan assets	412.1	427.5
	14.7	(77.0)
EFRBS unfunded liability	(2.7)	(3.7)
Net defined benefit liability recognised in the balance sheet	12.0	(80.7)

The difference between the two amounts is recognised as a surplus or obligation in the statement of financial position. Where this difference results in a defined benefit surplus, this is recognised in accordance with IFRIC 14 'IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction', on the basis that the Group has an unconditional right to any excess funds that may exist following the closure of the pension scheme once all members have left the plan and their benefits have been settled.

There were no special contributions paid in the year to 31 March 2023 (2022: £none).

	Change in assumption	Increase in liabilities £m
Discount rate	0.30%	17.1
Price inflation	0.30%	17.1
Life expectancy	1 year	9.6

The above sensitivity analysis is based on isolated changes in each assumption while holding all other assumption constant. In practice, this is unlikely to occur, and there is likely to be some level of correlation between the movements in different assumptions. We have updated the above sensitivity to 0.3%, from 0.1% in the prior year, to reflect the present volatility seen in the markets.

#### Effect on future cash flows

The level of contributions is reviewed at each triennial valuation. The latest of which was 31 March 2022.

Under the current Schedule of Contributions, no deficit recovery contributions are expected to be paid for the year-ending 31 March 2024. Future service contributions (consisting of amounts payable by members and the Company) will be in the region of £0.2 million.

The duration of the Scheme's liabilities is approximately 14 years.

#### Regulatory framework

The Scheme is funded and governed in line with the requirements of the Pensions Regulator. We have not made any allowance for any minimum funding requirements under IFRIC14.

The Scheme operates under trust law and the corporate trustee (Welsh Water Pension Trustee Limited) is responsible for its day-to-day governance. The Trustee Directors are assisted in the management of the Scheme by experienced professionals such as actuaries, administrators, and investment consultants.

The Trustees have put in place a diversified investment strategy which aims to meet the liabilities of the Scheme. Details are set out in the Scheme's Statement of Investment Principles. Day-to-day decisions around asset selection have been delegated to BlackRock as their fiduciary investment manager.

#### High inflation

For most Scheme Sections, pensions in payment (and in some instances deferred benefits) are increased on 1 April each year by the Retail Prices Index ("RPI") as measured over the relevant period, being the annual change in RPI announced for the previous September, December or January.

### 21. Pension commitments (continued)

## Notes to the financial statements (continued)

As a result of current high levels of inflation, many Scheme sections received a full RPI increase in both April 2022 and April 2023 via a 'best endeavours' rule (broadly a pension increase cap that is waived if the Scheme can afford to pay higher increases without requiring company contributions). The Trustee and Group also agreed to provide a 3% discretionary pension increase, on top of the capped increases of 5%, to Scheme sections that have a cap and are not subject to the best endeavours rule.

### Reduction in duration

Since the preparation of the accounting disclosures at 31 March 2022, the duration of the Scheme's liabilities is expected to have fallen from 19 years to 14 years at 31 March 2023. This is due to an increase in the yields used to set the discount rate and the impact of a new actuarial valuation as at 31 March 2022.

## 22. Lessor

	2023	2022
	£m	£m
Operating lease	0.1	0.1
Lease income- waste facility sites to Welsh Water Organic Waste Limited		

The Company leases land to Cardiff Council, currently the site of a composting facility which is operated by a fellow Group company, Welsh Water Organic Energy Limited, providing food and green waste services. The Company has classified this lease as an operating lease because it does not transfer substantially all the risks and rewards incidental to the ownership of the land. The lease payments are index-linked to RPI.

The remaining term of the lease is 9 years, with the total undiscounted current minimum lease receipts amounting to £0.9m.

## 23. Capital and other financial commitments

The Company's business plan at 31 March 2023 shows net capital expenditure and infrastructure renewals expenditure of £429 million (2022: £400 million) during the next financial year. While only a portion of this amount has been formally contracted for, the Company is effectively committed to a majority of the total as part of the capital investment programme approved by its regulator, Ofwat.

## 24. Related party transactions

Intercompany interest payable to Dŵr Cymru (Financing) UK plc (DCF), another member of the GCHC group, was £223,724,205 during the year (2022: £128,361,000). As at 31 March 2023 the balance outstanding on the intercompany loan and accrued interest from DCF stood at £3,226,711,324 (2022: £3,085,276,653). All borrowings raised by DCF are immediately on-lent to the company on an arms-length basis. The intercompany loan is subject to the terms and conditions of the whole business securitisation structure of Glas Cymru Anghyfyngedig and its subsidiaries. DCC, in its capacity as debtor, repays such principal and interest as is due on each borrowing on the due date plus 0.01%. An intercompany loan from Glas Cymru Anghyfyngedig and Dŵr Cymru Holdings Limited of £1,971,000 (2022: £1,971,000) and £2,812,458 (2022: £2,812,458) remains outstanding as at 31 March 2023. Interest payable on this loan has been waived.

As at 31 March 2023 intercompany trading balances owing to the Company were: Welsh Water Infrastructure Limited £3,560 (2022: £13,350), Welsh Water Organic Energy (Cardiff) Limited £2,098,786 (2022: £1,153,352), Welsh Water Organic Energy Limited £13,655 (2022: £nil), Cambrian Limited £25,419 (2022: £20,239), Glas Cymru Anghyfyngedig £8,481 (2022: £8,481), Glas Cymru Holdings Limited £74,290 (2022: £18,901) and Welsh Water Organic Waste £480,661 (2022: £55,131).

During the year no dividends were paid or received (2022: £nil). There were no other transactions with companies that are part of the GCHC Group.

## 25. Elan Valley Trust Fund



## Notes to the financial statements (continued)

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In 1984 Dŵr Cymru Authority entered into a conditional sale and purchase agreement with Severn Trent Water Authority for the sale of the aqueduct and associated works by which the bulk supply to Severn Trent reservoirs is conveyed.

The sum of £31.7 million, representing the consideration for the conditional sale, was invested in a trust fund. The principal function of the fund was to provide an income to Dŵr Cymru Authority, whilst preserving the capital value of the fund in real terms. Dŵr Cymru Authority's interest in this fund was vested in Dŵr Cymru Cyfyngedig under the provisions of the Water Act 1989.

The assets of the fund are not included in these financial statements. As at 31 March 2023 the market value of the trust fund was £90.0 million (2022: £109.0 million). Interest receivable includes £3.5 million (2022: £3.2 million) in respect of distributions from the Elan Valley Trust Fund.

### **26. Immediate and ultimate holding company**

The immediate parent Company is Dŵr Cymru (Holdings) Limited and the ultimate holding Company and controlling party is Glas Cymru Holdings Cyfyngedig, both of which are registered in England and Wales. The largest and smallest group within which the results of the Company are consolidated is that headed by Glas Cymru Holdings Cyfyngedig and Glas Cymru Anghyfyngedig respectively. Both consolidated financial statements can be obtained from the Company Secretary at Linea, Fortran Road, St Mellons, Cardiff, CF3 0LT.