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Severn Trent Water Limited

Report and financial statements for the year ended 31 March 2013

Company number 2366686

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Report and financial statements

For the year ended 31 March 2013

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At a glance

Severn Trent Water aims to be the best water and waste water company in the UK, by providing the highest standards and lowest possible charges, through great people

Our long term objectives

Over the last year, we have consulted widely with our stakeholders and customers about investment priorities for the medium and longer term. Based on that consultation, we have set out ten long term objectives

- 1 We will provide water that is good to drink
- 2 We will ensure water is always there when you need it
- 3 We will safely take your waste water away
- 4 We will provide excellent customer service
- 5 We will have the lowest possible charges
- 6 We will help you if you struggle
- 7 We will protect our water environment
- 8 We will protect the wider environment
- 9 We will make a positive difference in the community
- 10 We will finance our business sustainably

We measure our performance against 16 key performance indicators (KPIs). Details of our KPIs can be found on page 104

Where we operate

Our region stretches across the heart of the UK. We serve more than 4.2 million households and businesses, from the Bristol Channel to the Humber, and from mid-Wales to the East Midlands

Key Facts

Drinking water supplied per day
1.8bn litres

Waste water collected per day
1.4bn litres

Employees at 31 March 2013
5,631

Turnover £m
1,511.0 2013

Profit* £m
498.2 2013

*Before interest, tax and exceptional items

Delivered through four focus areas

We implement our strategy and plans by focusing on four key areas: our customers, people, process and finance. We aim to deliver the highest standards and lowest charges to our customers, through a highly skilled and committed workforce

Customers

Our household customers have the lowest average combined water and sewerage bills in England and Wales. Delivering customer satisfaction also requires us to provide water that's good to drink, always available and to take away waste water, to reflect customers' priorities in our plans, to communicate clearly, and to keep our promises and put things right if they go wrong

People

Our people are the cornerstone of our success. We strive to recruit, develop and retain the best people, provide them with great workplaces and maintain a strong culture of safety, personal responsibility and continuous improvement

Process

Our drive to work safer, better and faster is the foundation of our approach to continuous improvement. Making sure we have the right processes and systems is fundamental to achieving operational excellence.

Finance

The higher our standards, the more effectively and efficiently we work. This helps us to keep our costs low and generate progressive, sustainable returns which earn the trust of and reward for our investors. We look to finance the company in an efficient, sustainable way and maintain an investment grade credit rating.

Chief Executive's review

The world is changing for water companies and Severn Trent Water leads the way in shaping that change. We are continually improving our performance, improving our customer service and positioning the group for sustainable growth.

Delivering the future of water

The UK water industry faces significant challenges. We need to deal with the real impact of climate change and the increasing frequency of water shortages and flooding. We need to access and use water and environmental resources more efficiently. We need to keep improving customer service and customer choice whilst keeping our bills affordable. We need to maintain the significant investments that are required to ensure that our networks can deliver the essential water and waste water services. And, whilst keeping bills as low as we can for our customers, we need to generate sustainable returns for our investors.

Proposals from the Government and Ofwat will help us respond to these challenges. The changes are evolutionary, but together they add up to the largest shift in the industry's rules since privatisation.

The Water Bill will allow more competition for non-household customers, greater "upstream" competition – water trading in particular – and increase the scope for mergers and acquisitions, which should eventually lead to a more efficient industry structure.

Ofwat is considering important changes to the way it regulates, as it prepares for the next price review in 2014 (PR14). Notable differences from the current regime include separate controls for the wholesale part of the business – the networks and treatment plants – and the retail element, which manages customer relationships. This will increase focus on delivering the best customer service at lowest cost, and create more choice for non-household customers.

There will be greater emphasis on achieving objectives that companies set in consultation with their customers, helping them to innovate and benefit all stakeholders. Companies will be able to choose larger incentives for outperformance, at the risk of bigger penalties if they fall short. Also our customers and other stakeholders now have a much bigger role in influencing our next five year plan. Further details of our stakeholder engagement and the role of the Water Forum are provided on page 12.

Severn Trent Water welcomes these changes. We've been active in the debate about the future of water and we're pleased that the proposals are aligned with much of our own thinking. That's allowed us to prepare for these changes, through a strategy that creates opportunities to leverage our core skills.

Focused on continuous improvement

Our customers benefited for the fourth year running from the lowest average bills for water and sewerage combined in England and Wales. Whilst prices increased they were below the industry average. We continued to supply customers with excellent drinking water and, despite the drought at the start of the year, we once again avoided a hosepipe ban.

Severn Trent Water continued to improve its operational and environmental performance. These improvements, along with effective procurement and capital delivery, help us to be more efficient. In this Regulatory Period we are re-investing £150 million of our efficiency gains into our plant and networks to improve services for our customers further.

This investment contributed to our ongoing performance improvement. We cut leakage to a 20 year low and beat our target. Underlying levels of interruptions to supply also fell, with our Ofwat measure improving, although a handful of burst mains which affected numerous customers meant that we didn't meet our internal target. We further reduced pollution incidents, while compliance at our waste water treatment works reached a new record high, contributing to improving river water quality.

During the year, we delivered the outputs that Ofwat required from us. We were pleased to see that recent investment in the flood defences at Mythe Water Treatment Works proved their worth as the plant withstood exceptionally heavy rains and flooding. We also reduced the number of homes at risk of sewer flooding and there are now fewer properties on the 'at-risk' register than ever before.

In previous years, we've identified customer service as an area where we would like to improve. Our customer experience programme is changing the way we think about how we interact with our customers, which has led to pleasing improvements in our customer service scores, as measured by Ofwat's Service Incentive Mechanism (SIM).

This contributed to a customer satisfaction level of 4.36 out of 5 in our SIM quantitative survey, as well as falling levels of complaints. However, we know we have much further to go and we are not complacent. This includes resolving more of our customers' issues to their satisfaction on first point of contact and continuing to invest in our people, to help them form a better appreciation of our customers' needs and concerns when they have to contact us.

Our combined SIM score for 2012/13 was 78.1 against 69.9 in 2011/12. This represents a 12% year on year improvement. We created a sustainable improvement of 10% this year and we're the most improved water and waste water company.

People and culture

The performance we've delivered this year shows the quality of our people and their desire to do an excellent job. I would like to thank them for everything they have done.

We have talented and committed people throughout the company. Together, they have a wide breadth of expertise, from hydrologists and engineers to customer service experts and technologists. They apply these skills to our common mission, delivering high standards and the lowest possible charges for customers, with great people.

We've created a culture of continuous improvement that sustains our desire to do better. This culture is key. While we have a sophisticated set of tools which combine behavioral science and lean management to help us improve the way we work, it's the culture, values and attitude of our people that make those tools effective and drive us forward, every day.

Looking forward

Severn Trent Water is well positioned as the industry enters the next phase of development. We have accepted Ofwat's proposed licence modifications and are aligned to the agenda for regulatory reform and the Water Bill, both of which we continue to help shape.

Our preparations for the next Price Review 2014 (PR14) are progressing well. Customers are at the heart of our planning, through the widespread engagement we've already conducted and through our customer challenge panel, the Water Forum. Further details are provided on page 12.

Regulatory and political support for trading is growing and companies are likely to be incentivised to trade in the future. Severn Trent Water has an ongoing dialogue with neighbouring companies and we are well placed to benefit from more effective use of the country's water resources.

Looking further ahead, companies will have to ensure they're sustainably financed. The utilities sector will need to find billions of pounds for investment and it isn't certain that all of this can be done through debt. Equity is therefore likely to play a part, which means companies will have to be able to earn an appropriate return to attract that funding. We published important discussion papers on this subject during the year.

In summary, Severn Trent Water is operating from a great base. We have the right people doing the right things and delivering the right outcomes. Our customers need clean water and waste water services, and we have the right focus to prosper.

Tony Wray, Chief Executive

Our Strategy

A strategy to deliver the future of water

Our "Focus Water" strategy, with the goal of creating sustainable growth through our focus on water and waste water services drives everything that we do. As one of the UK's biggest water and waste water companies, Severn Trent Water is well positioned to succeed.

Our focus on sustainable growth means that we balance the needs of our customers, our people and the environment. Achieving this balance leads directly to good financial performance. It allows us to deliver organic growth and reliable returns over the longer term, without excessive risk.

We recognise that economic conditions are tough and that our customers have seen their incomes squeezed. While prices will inevitably rise because of the ongoing need for investment, we're determined to keep them as low as we can and deliver value for money. This means further improving our service, protecting customers from the effects of drought and floods, and providing them with water that's good to drink and always available.

Protecting the environment is also key because we and our customers depend on it to provide the resources we need.

Our people are central to our future. We work hard to make sure they have the skills and tools they need, and are motivated to continually improve our service to customers.

With significant changes in the sector approaching, we keep our strategy under constant review. This includes having open and constructive relationships with all our key stakeholders, so we understand what they expect from us. We then formally review our strategy each year so it remains relevant, balanced and sufficiently forward looking.

Today...

We're getting it right first time for customers

We've introduced new ways of working so we fix 80% of burst pipes on customers' properties that are eligible under our free repair scheme, after one call to us and with one visit. We put ourselves in our customers' shoes to understand their experience. We mapped out our processes from when our customer first contacts us to resolving the job and we reviewed how we kept our customers informed. We also stood in our employees' shoes and looked at the training we provided and the systems they used. The result is a redesigned training programme for our teams, improved collaboration between field and call centre colleagues and a better customer experience of dealing with Severn Trent Water.

Tomorrow...

We continue to invest in excellent customer service

We work hard to provide our customers with a service experience that is consistently reassuring and reliable, whilst doing whatever we can to personalise the way in which we deal with each individual customer query.

**Our Strategy
Sustainable**

Strategy aim	Highlights 2013	Key measures	
Delivering value for our customers.	<ul style="list-style-type: none"> • We met our leakage target, reduced interruptions to supply and protected more homes from sewer flooding • We maintained the lowest average bills for water and sewerage combined in England and Wales • Our Focus on Water Strategy provides value for money for our customers 	441 Ml/d Leakage megalitres per day (2012 464)	4.19 Customer written complaints per 1,000 properties (2012 4.88)
Responsible leadership, protecting the environment, thinking long term and setting high standards in everything we do.	<ul style="list-style-type: none"> • We achieved our best ever health and safety performance • We made further progress with our catchment management programme • We continued to influence the regulatory debate about the future of our industry, through a series of publications 	<ul style="list-style-type: none"> • 0.2 Lost time incidents per 100,000 hrs worked (2012 0.3) • We support the direction of the Water Bill, which is expected to become law later this year 	
Sustainable financing, ensuring we have a strong and flexible balance sheet	<ul style="list-style-type: none"> • We remained prudently financed and maintained our strong credit rating 	£758.6m Cash generated from operations (2012 £639.4)	61.3% Net Debt/RCV Gearing (2012 63.1%)

Growth

Strategy aim	Highlights 2013	Key measures	
Growth through investment in our network and services.	<ul style="list-style-type: none"> • We continued to make good progress with our preparations for PR14 • We invested £212 million in our infrastructure • We increased our regulatory capital value by £275 million 	3.9% RCV growth (2012 4.0%)	

Our business model

Water is essential to life and to the communities in which we live and work. Severn Trent Water is intrinsically linked to the life cycle of water. The customer is at the heart of our continuous drive to improve our operations and services across collection, delivery and cleaning of water.

Severn Trent Water is a regulated business. We work within five year planning cycles, known as Asset Management Plans (AMP), with customer prices set by our economic regulator, Ofwat, to allow us to fund our investment programme and cover an efficient level of operating costs. We are also subject to regulation by two quality regulators – the Drinking Water Inspectorate (DWI) and the Environment Agency (EA).

We also work with the Government (including the Department for Environment, Food and Rural Affairs and the Welsh Assembly Government) and other agencies such as the Consumer Council for Water, Natural England and Natural Resources Wales, to make sure we meet the highest customer service and environmental standards, while offering our customers the lowest prices.

Our prices and asset base are adjusted by retail price index (RPI) inflation each year. In certain circumstances we can ask for prices to be reviewed within the five year period due to costs associated with 'notified items' or 'relevant changes of circumstance'. Customer bad debt and the adoption of private drains and sewers are included in these categories for the current five year period.

The company earns a return on its asset base. We can generate additional returns if we outperform Ofwat's assumptions by becoming more efficient in the delivery of our capital programme, managing our operational costs more effectively, and by financing our business at a lower cost.

Our operating performance is assessed and benchmarked against the sector by Ofwat. At the next price review there is scope to earn additional income, or incur penalties, based on our performance.

Legal & Regulatory risks

We operate within a complex legal and regulatory environment as a water and sewerage service provider in England and Wales. As a result we face a number of risks including those associated with possible non-compliance with our legal and regulatory framework, failure to obtain support from Ofwat for our business plan for 2015-2020 and failure to meet the terms of our regulatory contract as set out in our agreed business plan for 2010-2015. We also face risks associated with possible future changes in legislation which may result in our business plans becoming unsustainable. A list of the Principal Risks facing Severn Trent Water can be found on page 33.

Business review

Overview

Industry and market

The water industry in England and Wales invests more than £3 billion each year and employs over 27,000 people. There are currently 10 water and sewerage companies in England and Wales, as well as a number of smaller water only companies.

The privatisation of the industry in 1989 has led to improvements in customer service, better drinking water and higher environmental standards. However, our sector still faces significant long term challenges. These include further improvements to operational and environmental performance, enhancing security of supply, dealing with extremes of dry and wet weather, managing the country's water resources more efficiently and in the long term, sustainably financing the industry's infrastructure investment. Our proposals for changes in our industry are informing the debate about meeting these challenges.

Key strengths

We have a number of key strengths and we work hard to maintain them. In particular:

- Our average bills for water and sewerage combined are the lowest in England and Wales
- We continually work to improve our performance and deliver cost and operational efficiencies against KPIs, which are aligned to our long term strategy
- We are committed to long term sustainability, keeping in balance the needs of our customers, the environment and our investors
- Our high standards and efficiencies keep our costs low, which in turn helps keep charges low for customers
- We have a clear strategy and business plan and a strong management team

How we measure success

Severn Trent Water has published its own set of KPIs since 2007. In 2011/12 Ofwat adopted a set of KPIs that it required all water companies to publish. Severn Trent Water has adapted its own KPIs to meet this new requirement. These KPIs provide Ofwat with an overall picture of performance against the company's commitments made as part of the AMP5 price review. Our KPIs are set out on page 104.

For the 2015-2020 period we have defined 10 long term objectives to meet customer and stakeholder needs. In April 2013 we published a consultation on our proposals for bills and services for the period ('Your water. Your choices'). This included consultation on a proposed new set of measures by which our customers, stakeholders, and regulators can see how much progress we are making towards achieving these objectives. Following the consultation, we will be finalising the measures and including them in our business plan which we will submit to Ofwat in December 2013.

Further details of our performance are provided in our Annual Regulatory Performance Report, which is available at www.stwater.co.uk

Key Facts

Customer written complaints per
1,000 properties
4.19 2013

Point of contact resolution (%)
90.0 2013

Average water and sewerage bill
£326 2012/13

Average customer cost per day
89p 2012/13

Progress against our long term objectives

Long term objective	Progress in the year
1 We will provide water that is good to drink	<ul style="list-style-type: none"> • Our drinking water quality remained high and we maintained our compliance with the DWI's standards • We invested in improvements to our water treatment plants and developed Drinking Water Safety Plans
2 We will ensure water is always there when you need it	<ul style="list-style-type: none"> • We continued to manage our water resources effectively and once again avoided any hosepipe bans • We reduced leakage to its lowest ever level and cut the underlying number of interruptions to supply
3 We will safely take your waste water away	<ul style="list-style-type: none"> • We increased waste water treatments works compliance and reduced properties on the 'at-risk' of sewer flooding register to its lowest level • We made substantial investment to improve sewer systems
4 We will provide excellent customer service	<ul style="list-style-type: none"> • We introduced a range of initiatives to improve customer service, resulting in increased customer satisfaction scores • We achieved the best improvement in customer experience across our peer group as measured by Ofwat
5 We will have the lowest possible charges	<ul style="list-style-type: none"> • Our average combined water and sewerage bills remained the lowest in England and Wales • Our bills will remain the lowest in 2013/14
6 We will help you if you struggle	<ul style="list-style-type: none"> • We helped 44,821 customers who struggled to pay bills via a range of flexible tariffs and schemes • We donated £3.0 million to the Severn Trent Trust Fund
7 We will protect our water environment	<ul style="list-style-type: none"> • We reduced pollution incidents year on year • We continued to take an industry leading role in shaping the regulatory regime and new legislation
8 We will protect the wider environment	<ul style="list-style-type: none"> • Around one quarter of our electricity needs were provided by our Severn Trent Plc group renewable energy operations • We reduced our net greenhouse gas emissions during the year and are on target to beat our business plan target by 2015
9 We will make a positive difference in the community	<ul style="list-style-type: none"> • We invested heavily into our network and treatment plants, making a substantial contribution to jobs and the local community • We talked to schools, other organisations and social housing about water efficiency, contributing to one of the lowest per capita consumptions in the country
10 We will finance our business sustainably	<ul style="list-style-type: none"> • We continued to ensure we were properly financed, with a strong balance sheet and investment grade credit rating • We continued to help shape the debate on future industry financing and published our paper, 'Changing Course through Sustainable Financing'

Business review

Performance

At Severn Trent Water we focus on four key areas – customers, people, process and finance (as we explain on page 1) Having the right people with the right skills, using the right processes, enables us to offer high quality, low cost services to our customers This in turn drives our financial results

The following pages describe what we achieved in each of these areas during the year

Customers

For the fourth year running, our average combined water and sewerage bills were the lowest in England and Wales, at £326 Our bills will remain the lowest in 2013/14

We aim to supply water that's good to drink and always available Despite the drought at the start of this year, we managed our water resources carefully and once again avoided any hosepipe bans or other limits on our customers' water use The subsequent heavy rain helped restore our reservoirs and aquifers and our water resources are now in good shape

Our water quality remained high and we maintained our compliance with the Drinking Water Inspectorate's standards at 99.98% We delivered water at the right pressure and further improved our overall performance on supply interruptions However our company KPI (performance on interruptions) was not as good as last year owing to a single burst trunk main which affected numerous customers We remain focused on cutting supply interruptions, with further investment planning to improve our performance

We continue to invest to ensure we provide the best water quality and resilience To achieve this we have numerous projects, including renewing nearly 300 km of water mains, improving resilience in South Gloucestershire, and refurbishing 5 km of the Derwent Valley aqueduct We're also renewing sections of high risk trunk mains, to minimise the risk of interruptions to supply Other significant projects include new treatment plants in Shropshire, Warwickshire, Nottinghamshire and Derbyshire, to address catchment quality issues

We made further progress with our catchment management programme during the year This involves encouraging farmers and other large land users to reduce their impact on water resources The drought and wet weather made it a difficult year for farmers, but their interest in catchment management remains high During the year, we completed around 150 water quality investigations arising from Drinking Water Safety Plans, and hit our target for catchment management investigations under the EA's National Environment Programme, receiving a positive response from the EA

One issue associated with wet weather is an increasing problem with metaldehyde, a pesticide used to control slugs and snails We took additional action from late summer, but could not prevent a number of higher pesticide results in the autumn We continue to take a leading role nationally in seeking an industry solution to metaldehyde

The intense rain in 2012 led to an increase in the number of internal severe flooding repeat incidents Last year was the second wettest year on record and parts of our region suffered severe flooding Some of our customers experienced flooding during the year and we did everything we could to help the local authorities and the EA respond, for example by providing large pumps to protect roads and properties adjacent to rivers

We are investing significant amounts in our waste water services to improve the service to our customers Further details of the investment can be found on page 16 and 17

Customer experience

We work hard to provide our customers with a service experience that is consistently reassuring and reliable, whilst doing whatever we can to personalise the way in which we deal with each individual customer query

We aspire to be an organisation that is designed around its customers, not just its network. We know that customer expectations continue to be influenced by the vast number of brands, products and technologies that they interact with. It's therefore essential for us to look at our processes, policies and general ways of working through a customer lens and not an operational lens. We started this cultural journey two years ago when we launched our Customer Experience Programme. By engaging every Severn Trent Water colleague in the practical pursuit of the best possible experience for our customers, we've succeeded in achieving a very real improvement across our key indicators of customer satisfaction.

We're proud of what we've achieved – but we won't stop until our customers consider us to be one of the very best customer service providers in the industry. We are able to benchmark our performance against that of our peer group via Ofwat's independent SIM.

Ofwat's SIM measures our customers' experience of dealing with us. The SIM score has two elements: quantitative, based on the number of customers that have to contact us, and qualitative, which assesses our service quality when they do.

We have consistently received good quantitative scores, but in the past, our quality of service has fallen short. In the last 12 months, we have focused on improving the areas our customers say are important to them, namely:

- resolving their issues or queries at first point of contact,
- being available to them when they want us, and
- keeping them informed every step of the way.

To do this, we created a cross company group to look at how we could drive improvement in our processes, response times and simplify the language we use to communicate with our customers. This helped us improve both elements of our SIM score in 2012/13.

We're pleased to have demonstrated the best improvement in SIM performance across our peer group, but we're not yet where we want to be from a benchmark perspective. And so the journey towards the best possible customer experience continues with a relentless focus on putting our customers at the heart of how we operate.

Our 'voice of the customer' tool gives us direct feedback from customers at the end of a call or when we've finished doing something for them. We get around 12,000 responses a month. This valuable feedback helps us improve our processes and how we deal with customers when they feel they need us most.

We have maintained first point of contact resolution at around 90%. Our Customer Advisors are consistently receiving satisfaction scores in the 90s and, as a result, our complaints volume continues to decline at a very healthy rate. We also further reduced written complaints, which were down 14%.

One of the important points of contact with customers is when they receive a bill from us. We've continued to improve our bill design to make them easier to understand, and to pass on useful information, such as the different ways customers can get in touch with us. We will also be introducing e-billing for customers who prefer it.

Managing debt

Some customers choose not to pay and some customers genuinely struggle to pay. In line with our commitment to fair and affordable bills for all, we operate robust processes to influence the behaviours of those who choose not to pay, which in turn controls our healthy debt levels.

For our customers who truly struggle to pay, we offer a range of flexible tariffs and schemes. These can involve matching the customer's payments, capping bills for people with low incomes who have to use large amounts of water for medical or family reasons, or allowing customers to make payments directly from their benefits. In 2012/13, we helped a total of 44,821 customers this way.

The Severn Trent Trust Fund offers an alternative avenue of support and has helped many customers over the years to fund their water bills. During the year we donated £3.0 million to the Severn Trent Trust Fund to enable the charity to support our customers who have difficulty in paying their water bills. However, a customer who struggles with their water bill is likely to struggle with other household bills. We wish to provide these customers with more meaningful support and have therefore entered into a partnership with the Citizens Advice Bureau which has the skills to help customers address their financial issues at a deeper level. We hope in this way to help our most financially vulnerable customers to manage and avoid household debts more effectively in the future.

Engaging with our customers

One of the significant differences between the process for PR14 and the previous price review is the increased role for customers and other stakeholders in helping us to formulate and challenge our plan.

The Water Forum is our customer challenge group for PR14. It includes representatives from customers, our environmental regulators and local authorities, and has an independent chair, Dame Yve Buckland, who is also national chair of the Consumer Council for Water.

The role of the Water Forum is to ensure that customer and other stakeholders' views are understood and represented by Severn Trent Water when we submit our plans to Ofwat in December 2013.

Ofwat will assess our plan against four criteria: outcomes, costs, risk and reward, and affordability and financeability. Our plan will then be categorised as 'enhanced', 'standard' or 'resubmission'. This will determine the level of scrutiny and challenge of our plan and the financial incentives available. The Water Forum reports on the quality of our customer engagement, and how well our business plan reflects customer views and priorities. It will form a key input to Ofwat's assessment against the outcomes criteria.

We also have a broader engagement programme and have run workshops on topics including managing climate change, water and waste water issues, and customer service. A wide range of stakeholders attended these sessions. We also carried out a major customer survey, to understand their willingness to pay for improvements we could deliver as part of our plan.

In April 2013, we issued another consultation paper, 'Your water Your choices', which set out our thinking on what might happen to customer bills, investment and investor returns over the next five years. This will give us further clarity on our stakeholders' views.

Today...

We're improving our flood defences in Gloucestershire

Since 2007, we've invested over £38 million across Gloucestershire to ensure we are better able to cope with extreme weather. To ensure our sewers in Gloucester can cope with heavy rainfall we have laid over 1 km of new sewers. We've protected our sewage pumping station at Longlevens with underground storage tanks and storm water pumping and at our Mythe Water Treatment Works we've installed flood protection barriers. To ensure we always have a back-up supply we've built pipelines from our other water treatment works.

Tomorrow...

We're continuing to invest across our region

Replacing our largest covered reservoir at Ambergate, Derbyshire and replacing over 7 km of sewers in Newark, Nottinghamshire are just two of our major investment schemes over the next five years. We will invest over £58 million on these two projects to ensure we continue to provide quality water and prevent sewer flooding.

People

We aim to have people with the right skills and approach to work, personal development and customer focus. To drive the behaviours we think are important, we have a Code of Conduct ('Doing the right thing – The Severn Trent way') that applies across the group and explains our approach to issues ranging from health and safety, to ethics and honesty, and to delivering excellent customer service.

A safe and healthy workforce

Protecting the health and safety of our customers, people and contractors is our number one priority. We were delighted to reduce lost time incidents once again, making 2012/13 our safest year yet.

Our MindSafety™ training programme contributed to this improvement. It teaches our people about different states of awareness, so they understand how they should work and can take responsibility for their own safety. We have coaches around the business to reinforce the MindSafety™ approach and will be running refresher programmes. Other initiatives to enhance safety during the year included improving our risk assessments and making sure that our people understand their roles and responsibilities.

One area that has concerned us is an increase in road traffic accidents. Whilst our staff didn't cause these accidents, we are looking at ways to reduce the risk by minimising the miles they travel and providing training on safe and effective driving and preventative actions.

As well as raising safety standards, we aim to be more proactive with our people's health and well-being. In 2012/13, we appointed a new occupational health provider. We're legally required to monitor the health of some employees, for example if they're exposed to noise or vibration, or work in confined spaces. Our new occupational health provider has a mobile unit, which visits sites to monitor our people. This saves time and provides a friendlier environment than an off-site facility.

We're also working with a new provider to help employees with musculoskeletal problems. Our partner looks at job design and how we can make changes to help people back to work. We are increasingly looking to take action before problems arise.

Engaging our people

Our annual employee survey once again showed that our people are positive about working for us. Our overall Engagement Index rose to 79%, ahead of our target of 75% and the industry benchmark of 74%. The survey response rate also increased, a sign that our people know that it's important to us that they give their feedback and that we listen.

The most improved area was in people believing we are committed to customer service. Our score for commitment to customers rose from 71% to 83%.

A number of factors were behind the improved survey results. Developing our managers has made them more willing to engage with their teams and we have also put effort into making sure managers understand our business goals and can communicate them to their teams. Our continuous improvement programme also contributed, by giving our people the tools and techniques to solve problems they face at work.

Previous employee surveys showed that our people wanted to see more of our executive team and to find out how they were leading the business. This year, we ran a rolling programme where Executive Committee members went out to meet people across the business. More than 1,000 of our people attended these meetings, enabling them to ask any question they wanted. The feedback has been positive and our executives have also learned where we need to communicate better.

Developing our people

Every year, we invest significant amounts in people development, (£3.9 million in 2012/13). This year, we piloted a 'Leading for Performance' programme in our waste water business. The aim is to have leaders who can inspire and engage our people and lead them through change – an area where we know we can do better. The programme helps our leaders to understand themselves and to learn how to coach others as well as build high performing teams. After positive results, we're now rolling out the programme across all of our operational leadership.

We have many other leadership programmes, which together form our 'Line Manager Journey'. They make sure that as people move into management, they have the skills to lead effectively. For example, to drive our performance culture, we want all our employees to have a performance discussion with their manager. We run programmes for managers at all levels, so they understand the process and can have those sometimes difficult conversations.

We'll soon be launching an initiative for nearly 1,400 people in Customer Relations, called the Great People Programme. Managers will learn about creating a customer orientated culture and coaching people in customer service skills. Frontline advisors will become better at giving customers a positive and memorable experience when they get in touch with us.

As part of our talent review process, we piloted new development centres this year. These took people identified as promotable and assessed their strengths and development needs. Each person came out with an in-depth development plan.

In a changing world, we need leaders with a breadth of experience who can rise to different challenges. We therefore reintroduced our graduate programme, taking on nine high calibre people. In 2013/14, we plan to increase this to 20 and we're also considering introducing a technical graduate scheme, with progression to chartered engineering.

Finding people with the right skills is a challenge across the industry, so we further expanded our apprenticeship scheme. We now have 82 apprentices at different stages of development, including 22 we recruited in September 2012 for technical training, including two for a new environmental conservation apprenticeship. Almost all our apprentices move on to permanent jobs with us.

Through a pilot programme called 'Employee Ownership of Skills', the Government has asked employers to set out how we might use public funds alongside our own investment to improve the skills we currently have in the industry, identify the skills we'll need in the future and where we should invest

We're also continuing to support projects in the Midlands to encourage young people to study science, technology, engineering and maths (STEM) subjects in order to be able to take up engineering and technical careers in the future

Attracting a diverse workforce

Our goal is to attract a diverse range of talent, with a balance of gender and ethnicity that reflects the market we operate in. At the moment, our workforce is slightly more diverse than the sector average, with more female employees and people from black, Asian and ethnic minority groups

We have a diversity working group, with members from across the business. Its current focus is on gender diversity in leadership roles. We are also starting to get more insight into ethnic diversity

It's important that we attract the broadest range of candidates when we recruit, so we track our attraction rates across different genders and ethnic backgrounds. We have also refreshed our careers website, to make it appeal to a wider range of people

Helping our people to manage their finances

In April 2013, we auto enrolled more than 1,000 people into our pension scheme. We believe that pensions are important and we're committed to providing a competitive scheme

As many of our people told us that they didn't understand pensions, we set up a financial education programme which is now part of our ongoing training. So far, 1,200 employees have attended a session to learn about pensions, debt, mortgages, savings and other financial matters

Process

To deliver great service to our customers, we look to continuously improve our processes and technology

Our approach to continuous improvement is called Safer Better Faster. It helps our people to find ways to do things better, so we can improve our service. We continue to invest, including building and training our team of expert practitioners, who work with colleagues to help them use Safer Better Faster techniques on a daily basis

During the year, we exploited our previous investment in SAP and desktop technologies, and used our Safer Better Faster approach to improve our business processes. For example, we introduced better processes in solving bursts on private properties, fixing stop tap problems and giving our customers a better service. We implemented software to allow work crews to access maps and asset data on their laptops, so they can pinpoint leaks and blockages more efficiently. We're also increasing the use of remote monitoring to improve performance across our networks. This helps us to detect leaks and prevent supply interruptions, allowing us to respond to problems before customers are affected

One of our biggest challenges was improving how we engage with our customers at our call centres. During the year we made a strategic investment in telephony systems, to improve our customers' experience when they call us. The new system links to our other back office systems, giving our people better information to resolve customer issues during the call

By investing in our people and technology, we've reduced to almost zero the number of customers who receive an engaged tone. More customers can speak to someone quickly, so fewer are hanging up because we've kept them waiting

Using text messages, our new website and other technologies has helped us keep our customers informed about what we're doing. Live update maps on our website tell customers what's going on in their area and we're also making more use of Twitter. We want customers to contact us in the way that's best for them, and around one quarter of all contacts are now through our website, where customers can pay bills and update their details.

We increased the resilience of our technology, by investing in new data centres. We also made significant investment in business modelling software, which will allow us to model different planning scenarios for the next five years reflecting the input we have received from our PR14 customer focus group.

We are improving the efficiency of our procurement. We're working with our supply chain to get better value for money, including using our SAP system to give us more visibility of what we buy and where.

During the year, we and our One Supply Chain framework partners continued to deliver greater efficiencies in our capital programme. Our strategic relationships with our One Supply Chain partners help us to become more innovative as we work together, for example by consolidating buying throughout the supply chain.

We want to work with responsible suppliers, so we've developed guidelines and standards that we expect suppliers to meet to ensure they are aligned to our philosophy of doing the right thing and our underlying policies. These cover key areas of corporate responsibility, such as our suppliers' approach to health and safety, anti bribery and anti corruption, and environmental performance.

A number of new technologies went live in our waste water operations this year. In order to drive efficiency we are exploiting technology innovation at places such as Ashbourne where we have installed the UK's first full scale HYBACS plant. HYBACS is a treatment technology that allows us to process higher volumes, while using less energy. In Birmingham we have installed the UK's first Annamox plant to treat high concentrations of ammonia. Anaerobic ammonium oxidation intensifies the sewage treatment process, so we can use fewer and smaller assets. In Nottingham we are installing one of the UK's first struvite recovery plants to reclaim phosphate so that we can sell it on. We have also been working with a partner which provides air compressors that can reduce electricity consumption by around 20%. These play an important part in sewage treatment. More broadly, we work extensively with other organisations to develop new processes and have more than 30 academic or industrial research partners.

Environment

Delivering our environmental obligations has a real impact on our customers and the communities in which they live and work.

Managing waste water

We achieved good improvements in our environmental performance in waste water. The number of reported pollution incidents fell from 458 in the previous year to 376, a reduction of 18%. While we are one of the industry leaders at preventing the most serious pollution incidents, we can still improve in other less serious categories. We are investing in training, working on faster response times and using technology to try to predict where pollutions might occur.

We have around 1,000 sewage treatment works. Of these, only 0.85% failed to reach their compliance limits (2012: 2.54%), our best ever performance. This was down to our improvement group, which has analysed the root causes of failure and enabled us to systematically eliminate those problems, as well as the ongoing benefits of our investment programme and more remote monitoring of our sewage treatment process. This year has seen us reach half way on our £200 million major projects programme of work. Upgrades are under way to our key sewage treatment works serving Nottingham, Leicester, Worksop, Stoke, Coventry, Burton-upon-Trent and Telford. Elsewhere this year we have invested almost £204 million to maintain service to our customers and undertaken key environmental

improvements to our rivers. Looking forward, we're investing significantly in improving river water quality and have carried out a pilot study with the EA on how to achieve zero pollutions and breaches of consent.

Sewer systems are primarily designed to handle waste water, and on occasions can be overwhelmed during heavy rain events.

Sewer flooding is one of the worst service failures that can happen to a customer. During the year we have made improvements to protect 158 properties from internal flooding and 70 external areas including substantial investment to improve sewer systems in Leamington Spa and Gloucester. The number of homes on the risk of sewer flooding register is now at its lowest ever level. We expect to be ahead of our target at the end of this regulatory period.

We have a proactive programme to clean and repair our sewer network which helps to prevent blockages, pollutions, flooding and collapses of our sewerage system.

This was our first full year of managing the 37,000 km of private drains and sewers that transferred to us on 1 October 2011. While this increased the number of blockages we had to deal with, overall we saw a lower level of reactive work than we expected. We are carrying out more inspections and condition/ CCTV surveys of these assets, so we can learn more about them and have better informed plans for the future.

Deploying water resources wisely

Severn Trent Water is the only company to target a significant reduction in leakage during AMP5. We made further good progress, cutting leakage to its lowest ever level at 441 MI/d. This compares with 464 MI/d last year and our internal target of 465 MI/d. Our performance benefited from our ongoing investment programme and the relatively mild weather.

Managing water resources effectively also means helping our customers to reduce the amount they use. We have a sizeable outreach programme with schools and other organisations, to teach people about using less water. We also distribute water efficient devices and have industry leading initiatives with social housing. All of these contribute to one of the lowest per capita consumptions in the country. The overall water saving this year as a result of these measures is 3.26 MI/d, which has contributed to the continued reduction in our per capita consumption. Last year our customers used an average of 121 litres per person per day.

Protecting biodiversity

Severn Trent Water has a role in protecting and enhancing biodiversity at our sites or sites affected by our activities. We manage 12 public access sites where we work alongside volunteers and in partnership with organisations to ensure the long term biodiversity value of the sites, whilst engaging with our customers. Across our region we also own or partly manage 37 sites of special scientific interest, where we work with our regulators, tenants and others to safeguard them.

Finance

We aim to finance the company in an efficient and sustainable way, which helps to keep customer bills low by keeping our financing costs low. Our funding comes from payment of customer bills, issuing debt on the capital markets and by shareholders retaining equity in the business. We have an investment grade credit rating, with a stable outlook. We also look to the long term sustainability of our financing and during the year we published some further thoughts in 'Changing course through sustainable financing' part of our continuing Changing course series of thought papers on the future of our industry.

More information about our financial performance and our debt issuance during the year can be found in the Financial review on pages 22 to 24.

Outlook

We remain focused on achieving sustainable growth, by concentrating on our customers, people, process and finance. We aim to deliver the benefits of our investment programmes and to continuously improve the way we work, to raise standards and drive efficiency. Giving our customers an even better service is an important part of this.

Our operating environment will change as the Government passes the Water Bill and Ofwat completes its preparations for PR14. We remain at the forefront of the industry's debate about its future and will continue to help shape the legislation and regulation as it progresses.

Business review

Looking forward

Since we published the first of our Changing Course documents back in 2010, we have played a leading role in shaping the future of the UK water industry. We've continued this engagement in the last 12 months, with a series of new publications. We issued a paper on designing balanced incentives that drive the right behaviour by water companies. KPMG wrote a report for us on financing water infrastructure beyond 2015. Alongside National Grid, we produced a paper on encouraging equity financing in the water and energy sectors.

We're pleased that our efforts have been productive. The changes from the UK Government, in the form of the Water Bill, and from Ofwat in its recently published consultation on the framework for PR14, are aligned with our own proposals. Together, these promise the most significant changes to water industry regulation since privatisation in 1989.

The challenges for the industry

Water industry regulation needs to change because the sector has to deal with significant challenges in the coming years.

Affordability is another key theme for the next five years. Households are facing declining real incomes and welfare reform, intensifying the need to keep water bills as low as possible. Pressure is also coming from business customers, who want to better manage their costs and have greater choice of water supplier.

We need to respond to climate change and water scarcity. Recent experience shows that the UK's weather patterns are changing, with droughts followed by floods. Water companies need to effectively manage customer demand, make better use of existing water resources on a national rather than regional basis, and increase the network's resilience. This would also create more capacity to move water, making water trading between regions easier.

The water industry must also be more sustainable. This means rebalancing abstraction and taking less water from areas where it's already affecting the environment. It also requires the industry to reduce its bias towards capital expenditure and promote operational solutions, such as improving catchment management rather than building new treatment works.

The Water Bill

The Government is responding to these challenges through the Water Bill, which ministers hope to enact in 2013/14. This builds on its 2011 Water White Paper, which set out a vision for "a resilient, affordable and sustainable water supply network".

The Bill covers four main areas. First, it increases the scope for non-household retail competition. This is already possible to a limited extent but the Bill will make it easier for business customers to switch supplier. However, while retail competition is positive because it encourages efficiency and promotes choice, it won't transform the sector's economics.

Secondly, the Bill also allows more upstream competition and in particular water trading. This will enable better use of national water resources, a significant improvement on the current situation where companies have to look within their region for solutions to water shortages. This will lead to better resilience and lower costs for customers. However, the right economic model needs to be developed to enable water trading to happen.

Thirdly, it is designed to enhance the physical resilience of the industry by, for example, encouraging farmers and other land owners to store water and to clarify the duties of Ofwat to promote resilience.

Finally, the Bill will reform the mergers and acquisitions regime. While major mergers will still be unlikely, the changes create the potential for a more efficient industry structure, reducing costs which can be shared with customers.

Overall, the Water Bill includes measures which are broadly in line with those we set out in Changing course, and we'll continue to support it as it passes through Parliament

The PR14 framework

In January 2013, Ofwat published a consultation on its framework and approach for PR14. The proposed framework has four key elements

First, it introduces separate price controls for the retail and wholesale parts of the business. This gives companies a greater incentive to provide the best customer service at lowest cost, and will create more choice for non-household customers. The regulated capital value (RCV) will stay with wholesale, which currently generates around 90% of Severn Trent Water's revenue. This means that the vast majority of our revenues will still be based on the RCV and will be adjusted for the movement in the RPI each year.

Ofwat is aiming to be less prescriptive about what companies deliver during the next regulatory cycle, so it's asking them to set the high level outcomes they will aim to achieve. These outcomes will be focused on benefits for customers and will give companies more leeway to innovate in the way they deliver their plans.

Companies will also face fewer but greater incentives, which will focus regulation where it's needed most. Companies can choose larger incentives for outperformance but would also face more significant penalties for underperformance. The new regime will also, in theory, address the industry's bias towards capital expenditure, as the model will move more to a total expenditure (or totex) basis. Companies will be able to choose whether to recover this expenditure on a 'pay as you go' basis, which will be beneficial for cash flow, or by adding it to their RCV and earning a return, which will be better for their long term returns.

Finally, the framework has a much greater emphasis on customer and stakeholder engagement. Customer challenge groups (such as our Water Forum, which is discussed on page 12) will influence companies as they develop their plans, which should lead to plans that are better informed. Companies will still own their plans but they must show that they have listened to their challenge group and explain their approach where their view differs. The customer challenge group will also report on the quality of the company's engagement and whether it supports its business plan. This will determine the depth of Ofwat's review of the plan.

Ofwat's proposals are still at the consultation stage and there are important details that need to be finalised. For example, it's important to get the level of detail right when setting outcomes. Outcomes that are too detailed will lose the benefits of risk based regulation. Conversely, if there's not enough detail it will be hard to define meaningful measures of success. We also need to know more about key elements such as the basis for the average retail cost calculations and how the totex baseline expenditure will be set. Overall, though, the draft PR14 framework contains no surprises for us and we're supportive of it aims.

Severn Trent Water's April 2013 consultation, 'Your water Your choices' sets out outline proposals for what the company could achieve during 2015-2020, with customer bills forecast to rise by no more than inflation during the period. There are a number of important areas where there is scope for choice, however customers' and stakeholders' views will directly influence the final business plan to be submitted to Ofwat in December 2013.

Business Review

Finance

The company has delivered a good financial performance against a backdrop of continuing revenue and cost challenges. Revenues were negatively impacted by lower consumption, with bad weather in the early part of the year also driving higher operational activities and thus costs, to meet the operating performance standards our customers and regulators expect. So, to have the costs that we directly control remain flat year on year was a good performance in the circumstances. For those costs where we have less influence – power, quasi taxes and bad debts, we saw increases in the first two, while we maintained performance on bad debts at 2.1% of rising revenues. We maintained our long term plans for investment in year three of this five year regulatory plan and invested £19 million more than the previous year in infrastructure which is expensed under the FRS101 reduced disclosure framework.

The company continued to look to its long term financing, successfully issuing its first bond into the nascent UK retail bond market and issuing a new 13 year bond into the sterling wholesale market raising £500m at 3.625%, the lowest cost Severn Trent has issued in its recent history. This suggests that the bond markets remain supportive of the company and its strategy and this will remain important as we manage the refinancing of some £400 million of debt which is to become due by the end of AMP5.

Results

PBIT is profit before interest and tax, underlying PBIT is PBIT excluding exceptional items. Turnover in Severn Trent Water increased by 3.7% in 2013 to £1,511.0 million. Sales prices were increased by inflation from 1 April 2012 which gave rise to an increase in turnover of £76.2 million. Consumption from metered customers was lower year on year reducing turnover by £19.4 million. New growth and meter optants increased turnover by £1.1 million and there were other decreases amounting to £4.6 million.

Underlying PBIT increased by £1.8 million from the previous year to £498.2 million. Employment costs increased by 11.8% to £228.0 million as headcount increased by 5.7% and the average employee cost increased by 5.7%. Hired and contracted costs decreased by £9.2 million to £130.2 million. Raw materials and consumables at £43.3 million were 7.5% lower than the same period in the prior year. Bad debts were 5.3% higher at £31.8 million, representing 2.1% of turnover (2012 2.1%). An increase of 17.0% in power costs (excluding quasi taxes) to £60.6 million. Quasi taxes, which comprise rates, service charges and the carbon reduction commitment (CRC), increased by £2.5 million to £110.1 million. Other costs increased by £9.5 million to £86.6 million driven by losses made on disposal of fixed assets. Labour and related overheads capitalised were £10.2 million higher than in 2011/12, mainly due to the higher level of capital expenditure in 2012/13. Infrastructure renewals expenditure increased by £18.8 million and depreciation increased by £9.3 million.

There was an exceptional credit to PBIT of £13.3 million (2012 credit of £11.6 million), arising from a profit realised on disposal of property assets in the year.

Net interest payable fell by £10.2 million from the prior year to £223.9 million. Interest receivable and similar income fell by £3.3 million. Interest payable on bank loans, other loans and payable to group companies decreased in total by £6.9 million. Interest payable on finance leases fell by £1.3 million.

The current tax charge before exceptional tax credits was £33.5 million including a credit arising from adjustments to prior year computations of £27.2 million. These adjustments mainly arose from industry wide agreement with HMRC regarding the timing of taxation of infrastructure income. The deferred tax credit before exceptional tax credits was £6.1 million. The exceptional tax credits include

Sustainable financing

In the longer term, the water industry will need more capital. It has spent £100 billion since privatisation but the challenges outlined earlier will require further significant investment. We believe that investors will continue to fund this if they remain confident in the industry.

In our view, it's unlikely that debt can provide all this funding. High gearing transfers risks to customers and the failure of one company will affect all the others, by damaging their chances of raising further debt. The 2008/09 financial crisis also showed that companies cannot guarantee access to debt finance when they need it. Our conclusion is that there's a need for long term equity in a balanced financing structure, which means that equity holders will have to be appropriately rewarded for providing those funds.

In the short term, we also need to look at the way the weighted average cost of capital (WACC) is calculated for PR14. In current market conditions, the capital asset pricing model, which is used to calculate the WACC, could produce an unsustainable answer. Other models should be used to cross check and justify the cost of equity and debt. We also believe that it's possible to differentiate the cost of capital based on company risk. We have made all these points in a series of publications over the year and are engaged with stakeholders to discuss the future implications.

Summary

In summary, we support the general direction of the Water Bill and the PR14 framework. While the changes they propose are evolutionary rather than revolutionary, they are still significant and will help the industry to address its challenges. We're pleased to have played an important part in shaping these proposals and will continue to do so as they progress.

- a current tax credit of £40.5 million and a deferred tax charge of £38.8 million arising from the adoption of FRS 101 (see below), and,
- a deferred tax credit of £38.3 million arising from the reduction of the corporation tax rate to 23% with effect from 1 April 2013

Profit for the financial year was £250.7 million (2012 £198.2 million). The company measures its return on capital using the ratio of post tax return on regulatory capital value, which is calculated as current cost operating profit less current tax, over average regulatory capital value. For the year ended 31 March 2013 post tax return on capital was 6.7% (2012 5.7%). This is Ofwat's post-tax return on capital key performance indicator.

Capital structure

The company is funded using a mixture of equity and debt (including fixed rate, index-linked and floating rate)

	2013	2012
	£m	
Cash and cash equivalents	328.6	0.3
Loans receivable from other group companies	105.7	104.4
Loans payable to other group companies	(3,845.0)	(3,569.8)
Bank loans	(717.7)	(610.3)
Finance leases	(530.7)	(561.7)
Cross currency swaps	36.1	67.1
Net debt	(4,623.0)	(4,570.0)

Net debt at 31 March 2013 was £4,623.0 million (2012 £4,570.0 million). Of the net debt 72.6% (2012 66.7%) was represented by fixed interest borrowings and 63.9% (2012 62.7%) was represented by amounts payable after five years. Ofwat's gearing KPI is net debt as calculated in the regulatory accounts, as a percentage of year end regulatory capital value at 31 March 2013 was 61.3% (2012 63.1%).

Cash flows

Operating activities generated a net cash inflow of £704.4 million (2012 £571.6 million outflow). Net interest paid was £184.3 million (2012 £289.2 million). Net investing activities used £392.1 million (2012 £514.9 million) which mainly included capital expenditure to meet the company's obligations under the AMP5 capital programme. Dividend outflows amounted to £72.0 million (2012 £266.0 million).

Treasury management

The company's treasury affairs are managed centrally as part of the Severn Trent Plc group and in accordance with its Treasury Procedures Manual and Policy Statement. The treasury operation's primary role is to manage liquidity, funding, investment and the company's financial risk, including risk from volatility in interest and, to a lesser extent, currency rates and counterparty credit risk. Its activities are subject to a set of controls commensurate with the magnitude of the borrowings and investments under its management. The Severn Trent Water Limited board ('the board') determines matters of treasury policy and its approval is required for certain treasury transactions. The company uses financial derivatives solely for the purposes of managing risk associated with financing its normal business activities. The company does not hold or issue derivative financial instruments for financial trading purposes.

The company uses a number of currency swaps and interest rate swaps to redenominate external borrowings into the currencies and interest rate coupon required for company purposes, and energy swaps to fix future expected electricity costs. The company's policy for the management of interest rate risk is to have a balanced portfolio of debt with a mix of term and interest rate structures that diversifies its risk and is appropriate to the long life of its asset base. The details are periodically reviewed to respond to changing market and regulatory conditions and with regard to regulatory pronouncements. Except for debt raised in foreign currency, which is fully hedged, the company's business does not involve significant exposure to foreign exchange transactions. The company continues to carefully monitor liquidity. At 31 March 2013 the company had £328.6 million in cash and cash equivalents and committed undrawn facilities amounting to £500 million, of which £200m is held jointly with Severn Trent Plc. In April 2012 the company borrowed £100m under a bilateral bank facility. The facility has a term of ten years and is fully drawn. In January 2013 the company borrowed £500 million from a subsidiary undertaking, Severn Trent Utilities Finance Plc, at a rate of 3.625%. The loan has a 13 year term. Cash is invested in deposits with highly rated banks and liquidity funds and the list of counterparties is regularly reviewed and reported to the board. The company's policy for the management of interest rate risk requires that no less than 45% of the company's borrowings should be at fixed interest rates, or hedged through the use of interest rate swaps or forward rate agreements. The company's net interest charge, excluding net finance costs from pensions, was covered 3.6 times (2012: 3.5 times) by profit before interest, tax, depreciation and exceptional items (this is used for Ofwat's interest cover key performance indicator), and 2.3 times (2012: 2.3 times) by underlying PBIT.

The company's long term credit ratings are

Long term ratings

Moody's	A3
Standard & Poor's	BBB+

Adoption of FRS 101

The company has elected to adopt early the new accounting framework issued by the Financial Reporting Council. The company meets the definition of a qualifying entity under FRS 100 (Financial Reporting Standard 100). Accordingly, in the year ended 31 March 2013, the company has adopted the FRS 101 'Reduced Disclosure Framework' and has ceased to apply all UK Accounting Standards issued prior to FRS 100. Therefore the recognition and measurement requirements of EU-adopted IFRS have been applied. As a result of these changes, the company's distributable reserves were reduced by £836.0 million. In order to restore these reserves the company made a bonus issue of shares from the reserve of £378.0 million that arose on transition and then undertook a capital reduction of £1,278.0 million which reduced share capital and increased distributable reserves.

Directors' report

The directors present their report, together with the audited financial statements of Severn Trent Water Limited for the year ended 31 March 2013

Principal activities

The company is a wholly owned subsidiary of Severn Trent Plc

The principal activities of the company are the provision and the treatment of water and the removal of waste water in the UK. There have not been any significant changes to the company's principal activities in the year under review. The directors are not aware, at the date of this report, of any likely major changes in the company's activities in the next year.

Business review

The company is required to set out in this report a fair review of the business of the company during the financial year ended 31 March 2013, the position of the company at the end of the financial year and a description of the principal risks and uncertainties facing the company (known as a 'business review'). The information that fulfils the requirements of the business review can be found in the following sections of the business review:

Review of results pages 3 – 24

Strategy and growth pages 5 – 6 and 19 – 21

Operational performance pages 10 – 18

Financial performance pages 22 – 24

KPIs page 104

Principal risks and uncertainties are detailed on page 33

Dividends and reserves

The company's dividend policy is to declare dividends which are consistent with the company's regulatory obligations. The amount declared is expected to vary each year further to consideration of these obligations. The ordinary dividend declared by the company in 2013 amounted to £72 million (2012: £266.0 million).

Directors

The directors of the company who served during the year and up to the date of this report are set out below:

Tony Ballance
Bernard Bulkin*
Richard Davey*
Andrew Duff*
Gordon Fryett*
Martin Kane*
Martin Lamb*
Michael McKeon
Baroness Noakes*
Andy Smith
Tony Wray

* non-executive director

Directors' interests

All of the directors at the year end are also directors of Severn Trent Plc. In accordance with the UKLA Listing Rule 9.8.6, their interests in the share capital of Severn Trent Plc are disclosed in the Annual Report and Accounts of that company for the year ended 31 March 2013.

None of the directors retain any notifiable interest in the shares of the company or any other subsidiaries as at 31 March 2013.

Directors' remuneration and annual bonus scheme

Remuneration for executive directors comprises the following elements:

- base salary and benefits,
- annual bonus scheme and share matching plan,
- long term incentive plan, and
- pension plan

As all directors are also directors of Severn Trent Plc, details of their emoluments can be found in the Annual Report and Accounts of Severn Trent Plc available on the Severn Trent Plc website.

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

Base salaries and benefits

Base salaries for directors are reviewed annually by the Severn Trent Plc Remuneration Committee (the 'Remuneration Committee') and take effect from 1 July. Salaries are set in line with reference to individual performance, experience, contribution, together with developments in the relevant employment market (having regard to the market median for similar roles in publicly quoted companies of a comparable size and practice in other water companies) and internal relativities. The Remuneration Committee gives due consideration to the economic climate, affordability and the broader employee salary review policy when setting base salary levels.

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

Annual Bonus Scheme

The directors' Annual Bonus Scheme ('ABS') focuses on the achievement of specific strategic goals which are intended to drive the creation of operational efficiencies and improvements in business performance. The bonus scheme operates on a balanced scorecard of measures based on the company Key Performance Indicators (KPIs), which include operational performance, leakage and customer service. The scheme attributes score points to each KPI and the bonus outturn is determined by reference to the aggregate number of points awarded across all the KPIs. Bonus targets were set and measured for the period 1 April 2012 to 31 March 2013 (detailed below).

Annual Bonus 2012/2013

In 2012/2013 each executive director had between 80% and 90% of their maximum bonus opportunity linked to the performance of Severn Trent Water (the CEO of Severn Trent Services had 10%) and a proportion measured against personal objectives. The Chief Executive, Finance Director and CEO of Severn Trent Services were also measured against the performance of Severn Trent Services.

The ABS is designed to encourage improved performance, with targets established by the Severn Trent Plc Remuneration Committee to align executive directors' interests with shareholders. The maximum annual bonus opportunity for the executive directors is 120% of salary. For the achievement of target performance, 60% of salary is awarded.

The bonus outturn in respect of Severn Trent Water performance was operated by reference to a balanced scorecard of measures, based on the KPIs. The Remuneration Committee believes that the use of the Severn Trent Water KPIs continues to be both an effective and challenging annual bonus metric and meets the needs of the business. The bonus entitlement was determined by reference to the aggregate number of points awarded across all the KPIs. The targets taken together are considered by the board to have an impact on the longer term financial performance of the company and a number of them are reported to Ofwat.

The number of KPIs for the 2012/2013 financial year was reduced from 20 to 10. This change reflects the revised suite of KPIs published by Ofwat against which they have indicated that they will assess water companies, and it is therefore appropriate to measure the company's performance consistently with those externally published measures of success.

The table below shows the points awarded by the Remuneration Committee for bonus purposes under each of the 10 KPIs in relation to the 2012/2013 ABS. As a consequence the Severn Trent Water bonus award was 77.7% of the maximum opportunity.

Key Area	KPI	Measure	2012/13 target	2012/13 actual	Points awarded
Employee	1	Lost Time Incidents per 100,000 hours worked	0.31	0.21	130
	2	Employee motivation- Quest (engagement index)	75%	79%	130
Customer	4	Service Incentive Mechanism- Qualitative	4.30	4.36	126
	5	Service Incentive Mechanism- Quantitative	203	166.7	130
	7	Serviceability – Waste Water	100	78	130
	8	Serviceability - Water	100	80	130
Financial	9	Capital Expenditure versus Final Determination	549.1	541.8	0
	11	Operating expenditure versus Final Determination	572.5	567.2	130
Environment	12	Pollution Incidents (cat 1,2 &3)	409	376	130
	16	Leakage ml/d- Post MLE	465	441	130

The bonus payments awarded are detailed below. Please note that they incorporate amounts in respect of personal targets and, in the case of the Chief Executive and Finance Director, Severn Trent Services' performance.

Director	Value of bonus award £
Tony Ballance	£195,704
Martin Kane	£288,000
Michael McKeon	£446,256
Andy Smith	£253,744
Tony Wray	£546,369

Half of the above bonus awards are deferred into shares to be held for three years following payment and subject to continued employment. If the executive is summarily dismissed without notice under his/her employment contract then the deferred bonuses are forfeited. In all other cases of cessation of employment the deferred bonus is not lost and the shares automatically vest on the dealing day after the cessation of employment. The Remuneration Committee determines whether it is appropriate to release the shares in 'good leaver' cases. A clawback provision continues to operate.

Annual bonus payments to executive directors are not pensionable.

Annual Bonus Targets for 2013/2014

The Remuneration Committee has reviewed the operation of the plan and concluded that it should operate on a similar basis for 2013/14 and that the KPIs will remain the same as those shown in the table on the previous page.

Share Matching Plan

Under the Share Matching Plan ('SMP') directors are eligible to receive matching share awards over those shares which have been acquired under the deferred share component of the annual bonus scheme as described above. For each share deferred, half a matching share is awarded subject to satisfying the Total Shareholder Return ('TSR') performance criteria. Further details of the SMP can be found in the Severn Trent Plc Annual Report and Accounts.

Long Term Incentive Plan

Directors may also participate in the Severn Trent LTIP. Under this plan conditional awards of performance shares are made to directors up to an annual maximum limit and vest after three years subject to out performance of the Return on Regulatory Capital Value ("RoRCV") set by Ofwat. RoRCV replaced TSR in 2011 to focus attention towards the creation of long term value to align with the interests of shareholders and Ofwat. Further details are contained in the Severn Trent Plc Annual Report and Accounts.

Share Incentive Plan

A company-wide Share Incentive Plan ('SIP') operates which includes a performance condition based on the award of points for the balanced scorecard KPIs used for the Annual Bonus Scheme. For the year 2012/13 awards of shares to the value of £583 will be made to all eligible employees.

Shareholding Requirements

The company operates shareholding guidelines under which executive directors are expected to build and maintain a minimum holding of shares in the Severn Trent Plc. The Chief Executive is expected to build and maintain a holding of shares to the value of 1.5 x base salary and other executive directors 1 x base salary. Executive directors are expected to retain all of the net of tax number of shares they receive through the LTIP and other share based plans and good progress is being made to meet the guideline holdings. Full details of the shareholding requirements for directors can be found in the Annual Report and Accounts of Severn Trent Plc.

Directors' and officers' indemnities

The company maintains Directors' and Officers' Liability Insurance in respect of legal action that might be brought against its directors and officers. In accordance with the company's Articles of Association, and to the extent permitted by law, in November 2011 the company indemnified each of its directors and other officers of the group against certain liabilities that may be incurred as a result of their positions with the group. The company does not have in place any indemnities for the benefit of the auditor.

Policy on the payment of creditors

The company either uses its own standard terms and conditions entitled 'General Conditions of Contract relating to the supply of Goods/Services or the Execution of Work' (copies are available from the Purchasing Department, Severn Trent Water Limited, Severn Trent Centre, PO Box 5309, Coventry CV3 9FH) or nationally agreed terms and conditions of contract such as NEC Engineering and Construction Contract Third Edition June 2005 (incorporating NEC Amendments dated June 2006) and NEC3 Professional Services Contract June 2005.

Terms of payment are stated on each purchase order issued by the company. Suppliers are able to negotiate their own payment terms which can differ from these, as part of the tender process. Trade creditors at the year end reflected 16.6 days purchases (2012: 17.2 days).

Charitable and political donations

Donations to charitable organisations during the year amounted to £60,591 (2012: £57,023). Severn Trent Water's policy is not to make any donations for political purposes in the UK, or to donate to EU political parties or incur EU political expenditure. Accordingly we have not made any political donations or incurred any political expenditure in the financial year under review.

Research and development

Expenditure on research and development is set out in note 4 to the accounts on page 49. Details of the research and development activity undertaken by the company during the year are set out in the operating and financial review on pages 3 to 24.

Employees

The average number of employees during the year was 5,458 (2012: 5,162).

Severn Trent Water believes that a diverse and inclusive culture is a key factor in being a successful business. Apart from ensuring an individual has the ability to do the job we do not discriminate in any way and make every effort to ensure that those with disabilities are able to be employed by us. We endeavour to retain employees in the workforce if they become disabled, we make all reasonable adjustments to their role and, if necessary, look for redeployment opportunities to support them in seeking an alternative role within Severn Trent Water. We ensure that training, career development and promotion opportunities are available for all our employees irrespective of their gender, race, age or disability.

Regulation: 'Ring fencing'

In accordance with the requirements of Ofwat, the board confirmed that, as at 31 March 2013, it had available to it sufficient rights and assets, not including financial resources, which would enable a special administrator to manage the affairs, business and property of the company in order that the purposes of a special administration order could be achieved if such an order were made.

Regulation: 'Cross directorships'

It is the policy of the company that directors and employees of the company may be directors of related companies when this is in the best interests of the company, and where appropriate arrangements are in place to avoid conflicts of interest.

Conflict of interests

The board has a full process in place to authorise situational conflicts in accordance with the provisions of the Companies Act 2006. At every board meeting there is a standing agenda item at the beginning of the meeting to consider and discuss whether any potential conflicts exist. If there is then that director would not participate in the discussion on that item. Half yearly reports are made to the board of all directors' conflicts and directors are reminded from time to time of their obligations. An annual review of conflicts is also carried out and is incorporated into the year end process of verifying directors' interests.

Going concern

The company operates in an industry that is currently subject to economic regulation rather than market competition. Ofwat, the economic regulator, has a statutory obligation to set price limits that it believes will enable the water companies to finance their activities. As a consequence the directors believe that the company and the group are well placed to manage their business risks despite the current uncertain economic outlook. The company and the group are funded for their investment and cash flow needs at least for the next year.

The directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. Accordingly we continue to adopt the going concern basis in preparing the Annual Report and Accounts.

Auditors


Deloitte LLP have indicated their willingness to continue as auditor and, in accordance with Section 487 of the Companies Act 2006, are deemed to be reappointed

The directors confirmed that

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

Relevant audit information means information needed by the company's auditors in connection with preparing their report. This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006

By order of the board



Bronagh Kennedy
General Counsel and Company Secretary
29 May 2013

Governance

Severn Trent Governance

Severn Trent Plc is the ultimate holding company of Severn Trent Water Limited. Since March 2007, as part of the strategy of focusing on water, the boards of directors of Severn Trent Plc and Severn Trent Water Limited have been identical.

Severn Trent Plc and Severn Trent Water Limited operate as distinct legal entities. The boards have regard to the Severn Trent Plc Board Governance document and the Severn Trent Water Limited Matters Reserved to the Board and are assisted through the management of separate agendas, meetings and minutes by Company Secretariat and are advised in their meetings by the Company Secretary where appropriate.

The relationships between Severn Trent Water Limited, the regulated entity, and our non-regulated businesses such as Severn Trent Services are monitored and controlled to ensure that we comply with our Ofwat obligations on arm's length transactions.

During the year ended 31 March 2013, Severn Trent Plc was compliant in its application of the UK Corporate Governance Code 2010 (the 'Governance Code'), with the exception that the adequacy of arrangements in relation to the group's whistleblowing procedures falls within the remit of the Corporate Responsibility Committee, rather than the Audit Committee.

The Severn Trent Plc board has established an effective committee structure to assist in the discharge of its responsibilities to the group. The terms of reference of the Audit, Remuneration and Nominations Committees comply with the provisions of the Governance Code and are available for inspection, together with the terms of reference of the Corporate Responsibility Committee and Executive Committee, on the Severn Trent Plc website (www.severntrent.com) or on written request from the Company Secretary at Severn Trent Centre, PO Box 5309, Coventry CV3 9FH.

Severn Trent has made solid progress in implementing the key components of its governance framework which are based on clear organisational structure and decision making, sound policies and standards, and assurance of the outcomes. The board and other key stakeholders need a transparent methodology which delivers and validates the outcome of activities.

The company expects roles to be performed in line with the specific annual job objectives. Employees performing their roles properly, preparing and reporting outcomes on time and to the required standard is a key component in our system of internal control.

The company continues to embed the compliance, verification and performance activities in Severn Trent. These are within business areas and sometimes within discrete functions. These confirm that operational activities have been performed properly.

Lastly, the company maintains an independent perspective on the overall framework by obtaining confirmation that the governance structure is working properly. In Severn Trent, this is obtained primarily from the Internal Audit function.

In order to provide an appropriate understanding of how these responsibilities come together for Severn Trent, the company has developed a description of the key elements over which assurance is required by the board. Internal Audit deliver an audit plan to confirm that key business risks are being mitigated.

Severn Trent Water Limited

Operating structure

Day to day operational priorities within Severn Trent Water are led by the Chief Executive of Severn Trent Plc and his executive management team, who together comprise the Executive Committee. The Executive Committee oversees the development and performance of the Severn Trent strategy. It also has accountability for achieving business results. During the year the Executive Committee structured its meetings to focus on strategy and business management, policy and planning and operational performance.

The operational structure aligns the organisation with the processes that matter to customers and drives greater efficiency.

Internal control and risk management

The board has overall responsibility for the company's system of internal control and for reviewing its effectiveness. The board reviews the effectiveness of the system of internal control including financial, operational, compliance and risk management at least annually in accordance with the requirements of the Governance Code and the guidance set out within it. The system of internal control is reviewed for effectiveness and adequacy.

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

The board reviews risk management and the adequacy of the system of internal control through the Severn Trent Plc Audit Committee. The board also keeps under review ways in which to enhance the control and audit arrangements in the company. The Audit Committee receives reports every six months from the Chief Executive on the significant risks faced by the company. These include an assessment of the effectiveness of controls over each of those risks. Action plans to improve controls where necessary are monitored regularly. Any significant control weaknesses that have been identified are also reported to the Audit Committee. The Internal Audit department provides objective assurance and advice on risk management and control. The external auditors also report on significant control issues to this committee.

The board confirms that procedures providing an ongoing process for identifying, evaluating and managing the principal risks faced by the company have been in place for the year to 31 March 2013 and up to the date of the approval of the Annual Report and Accounts.

Key elements of the company's processes and procedures are

- clearly defined and communicated strategic and business objectives,
- an organisation structure with clear lines of accountability and responsibility,
- performance management and succession planning systems,
- regular, structured reviews of business risk by senior management and the Executive Committee,
- a scheme of delegated authority, approval of plans, budgets and significant investments,
- robust business planning including the identification and implementation of relevant improvement plans, and
- monthly reporting and monitoring of financial results, regulatory compliance and other operational performance indicators, and independent assurance provided by both internal and external auditors.

Principal risks and uncertainties

The board considers the principal risks and uncertainties affecting the business activities of the company to be those detailed below

Customer Perception:

- We may be unable to improve and maintain our levels of customer service sufficiently to deliver what our customers tell us they want
- We may be unable to respond effectively to the opening up of the business retail market to competition

Legal and Regulatory Environment:

- We may be unable to effectively anticipate and/or influence future developments in the UK water industry resulting in our business plans becoming unsustainable
- Ofwat may not support our business plan submission for the next price review period (AMP6) for 2015 to 2020, or we may fail to meet some of the targets agreed with Ofwat in our current business plan
- The regulatory landscape is complex and subject to on-going change. There is a risk that processes may fail or that our processes may not effectively keep pace with changes in legislation leading to the risk of non-compliance

Operations, Assets and People:

- Our assets or processes may fail resulting in injury to an employee, contractor or member of the public
- We may fail to meet all of our regulatory targets including targets from Ofwat in relation to ongoing operational performance of our assets resulting in regulatory penalties
- Failure of certain key assets may result in inability to provide a continuous supply of quality water to large populations within our area, or in damage to third party property

Financial Risks:

- The current economic climate may increase the difficulties associated with obtaining funding for the company at similar rates to those assumed in our business plans
- Changing demographics and fluctuations in the investment market may affect our ability to fund pensions promises sustainably
- Counterparties with whom we have invested money may fail putting our investment at risk

These risks and other significant risks are managed through our established Enterprise Risk Management (ERM) process. This requires risk owners to consider possible causes and potential impacts of each risk and to assess the adequacy of mitigating controls in place. Where additional mitigation is needed, risk improvement actions are put in place and these are tracked to monitor that they are completed to schedule and have the anticipated impact to improve the management of the risk. Significant risks identified within our ERM process are reported to the Executive Committee, the Audit Committee and to the board on a regular basis.

Directors' responsibilities statement

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework. 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 judgments and accounting estimates that are reasonable and prudent,
- state whether Financial Reporting Standard 101 Reduced Disclosure Framework has been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

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

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

Independent auditor's report to the members of Severn Trent Water Limited

We have audited the financial statements of Severn Trent Water Limited for the year ended 31 March 2013 which comprise the profit and loss account, the statement of comprehensive income, the balance sheet, the statement of changes in equity and the related notes 1 to 35. The financial reporting framework that has been applied in their preparation is applicable law and Financial Reporting Standard 101 Reduced Disclosure Framework.

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.

Respective responsibilities of directors and auditor

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 March 2013 and of its profit for the year then ended,
- have been properly prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework, and
- have been prepared in accordance with the requirements of the Companies Act 2006.


Opinion on other matter prescribed by the Companies Act 2006

In our opinion, the information given in the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us, or
- the company 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 required for our audit.



Jane Whitlock (Senior Statutory Auditor)
For and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Birmingham, United Kingdom
United Kingdom
29 May 2013

Severn Trent Water Limited

Profit and loss account For the year ended 31 March 2013

	Notes	2013 £m	2012 £m
Turnover	3	1,511.0	1,457.5
Operating costs before exceptional items	4	(1,012.8)	(961.1)
Exceptional income	5	13.3	11.6
Total operating costs		(999.5)	(949.5)
Profit before interest and tax		511.5	508.0
Income from share in group undertakings		-	3.5
Interest receivable	8	101.0	104.3
Interest payable	8	(324.9)	(338.4)
Losses on financial instruments	9	(49.5)	(70.3)
Profit on ordinary activities before tax		238.1	207.1
Taxation on profit on ordinary activities before exceptional items		(27.4)	(79.3)
Taxation on exceptional items		40.0	70.4
Total taxation on profit on ordinary activities	10	12.6	(8.9)
Profit for the financial year		250.7	198.2

All results are from continuing operations in both the current and preceding year

Severn Trent Water Limited

Statement of comprehensive income For the year ended 31 March 2013

	2013 £m	2012 £m
Profit for the year	250.7	198.2
Losses on cash flow hedges	(37.6)	(81.0)
Deferred tax on losses on cash flow hedges	8.6	19.7
Amounts on cash flow hedges transferred to the profit and loss account	16.2	(0.4)
Deferred tax on transfers to the profit and loss account	(3.7)	0.1
Actuarial losses on defined benefit pension schemes	(51.4)	(108.3)
Tax on actuarial losses	10.0	25.5
Deferred tax movement arising from rate change	(3.2)	2.2
Other comprehensive loss for the year	(61.1)	(142.2)
Total comprehensive income for the year	189.6	56.0

Severn Trent Water Limited

Balance sheet As at 31 March 2013

	Notes	2013 £m	2012 £m
Fixed assets			
Goodwill	12	1 3	-
Intangible assets	13	89 0	104 3
Tangible fixed assets	14	6,738 0	6,551 5
Investments	15	347 9	347 9
Derivative financial assets	22	65 5	70 5
		7,241 7	7,074 2
Current assets			
Stocks	16	6 1	6 3
Debtors amounts falling due after more than one year	17	300 4	306 4
Debtors amounts falling due within one year	17	430 2	367 9
Derivative financial assets	22	0 9	23 4
Cash at bank and in hand		328 6	0 3
		1,066 2	704 3
Creditors amounts falling due within one year	19	(596 2)	(700 6)
Net current assets/(liabilities)		470 0	3 7
Total assets less current liabilities		7,711 7	7,077 9
Creditors amounts falling due after more than one year	20	(5,628 3)	(5,135 5)
Retirement benefit obligation	31	(383 7)	(345 8)
Provisions for liabilities and charges	23	(832 2)	(852 5)
Net assets		867 5	744 1
Capital and reserves			
Called up share capital	25	100.0	1,000 0
Profit and loss account		902.4	(515 5)
Hedging reserve	26	(134 9)	(118 4)
Infrastructure reserve	27	-	378 0
Total shareholder's funds		867 5	744 1

The financial statements were approved by the board of directors on 29 May 2013. They were signed on its behalf by



Andrew Duff
Chairman
29 May 2013
Company Number 2366686



Michael McKeon
Director

Severn Trent Water Limited

Statement of changes in equity For the year ended 31 March 2013

	Share capital £m	Share premium £m	Hedging reserves £m	Infrastructure reserves £m	Profit and loss account £m	Total £m
At 1 April 2011	1,000 0	–	(56 8)	378 0	(369 7)	951 5
Profit for the year	–	–	–	–	198 2	198 2
Losses on cash flow hedges	–	–	(81 0)	–	–	(81 0)
Deferred tax on losses on cash flow hedges	–	–	19 7	–	–	19 7
Amounts on cash flow hedges transferred to the profit and loss account	–	–	(0 4)	–	–	(0 4)
Deferred tax on transfers to the profit and loss account	–	–	0 1	–	–	0 1
Actuarial losses	–	–	–	–	(108 3)	(108 3)
Deferred tax on actuarial losses	–	–	–	–	17 7	17 7
Tax on pension contributions	–	–	–	–	7 8	7 8
Deferred tax arising from rate change	–	–	–	–	2 2	2 2
Total comprehensive income for the year	–	–	(61 6)	–	117 6	56 0
Share options and LTIPs						
- value of employees' services	–	–	–	–	3 9	3 9
- shares purchased	–	–	–	–	(18)	(18)
Deferred tax on share based payments	–	–	–	–	0 5	0 5
Dividends paid	–	–	–	–	(266 0)	(266 0)
At 31 March 2012	1,000 0	–	(118 4)	378 0	(515 5)	744 1
Profit for the year	–	–	–	–	250 7	250 7
Losses on cash flow hedges	–	–	(37 6)	–	–	(37 6)
Deferred tax on losses on cash flow hedges	–	–	8 6	–	–	8 6
Amounts on cash flow hedges transferred to the profit and loss account	–	–	16 2	–	–	16 2
Deferred tax on transfers to the profit and loss account	–	–	(3 7)	–	–	(3 7)
Actuarial losses	–	–	–	–	(51 4)	(51 4)
Tax on pension contributions	–	–	–	–	1 3	1 3
Deferred tax on actuarial losses	–	–	–	–	8 7	8 7
Deferred tax arising from rate change	–	–	–	–	(3 2)	(3 2)
Total comprehensive income for the year	–	–	(16 5)	–	206 1	189 6
Share options and LTIPs						
- value of employees' services	–	–	–	–	6 6	6 6
- shares purchased	–	–	–	–	(1 4)	(1 4)
Bonus issue of shares	378 0	–	–	(378 0)	–	–
Capital reduction	(1,278 0)	–	–	–	1,278 0	–
Current tax on share based payments	–	–	–	–	0 7	0 7
Other movements	–	–	–	–	(0 1)	(0 1)
Dividends paid	–	–	–	–	(72 0)	(72 0)
At 31 March 2013	100 0	–	(134 9)	–	902 4	867 5

Severn Trent Water Limited

Cash flow statement For the year ended 31 March 2013

	Note	2013 £m	2012 £m
Cash generated from operations	29	757.9	617.6
Tax paid		(53.5)	(67.8)
Net cash generated from operating activities		704.4	549.8
Investing activities			
Interest received		5.2	3.6
Dividends received from associates and joint ventures		–	3.5
Investment in subsidiaries		–	(177.8)
Receipts of amounts due from finance leases		0.5	113.6
Proceeds on disposal of property, plant and equipment and intangible assets		15.6	8.8
Purchases of intangible assets		(14.9)	(9.8)
Purchases of property, plant and equipment		(420.7)	(364.6)
Contributions and grants received		27.4	22.8
Net cash used in investing activities		(386.9)	(399.9)
Financing activities			
Interest paid		(167.4)	(183.5)
Closed out swap		(44.3)	–
Interest element of finance lease payments		(22.7)	(16.7)
Dividends paid to shareholders of the parent		(72.0)	(266.0)
Repayments of obligations under finance leases		(29.1)	(56.6)
Repayments of loans		(287.4)	(387.8)
New loans raised		635.1	752.7
Purchase of own shares		(1.4)	(1.8)
Net cash used in financing activities		10.8	(159.7)
Increase/(decrease) in cash and cash equivalents		328.3	(9.8)
Net cash and cash equivalents at beginning of period		0.3	10.1
Net cash and cash equivalents at end of period		328.6	0.3

Severn Trent Water Limited

Notes to the financial statements

1. Accounting policies

a) Accounting convention

The financial statements have been prepared on the going concern basis (see Directors' report) under the historical cost convention as modified by the revaluation of certain financial assets and liabilities (including derivative instruments) at fair value, and in accordance with applicable United Kingdom Accounting Standards and comply with the requirements of the United Kingdom Companies Act 2006 ('the Act'). The principal accounting policies, which have been applied consistently in the current and preceding year are set out below

b) Basis of preparation

The company is a wholly owned subsidiary of Severn Trent Plc and is included in the consolidated accounts of Severn Trent Plc. Consequently, the directors have taken advantage of the exemption available under section 400 of the United Kingdom Companies Act 2006 from preparing group accounts

The company has elected to adopt early the new accounting framework issued by the Financial Reporting Council. The company meets the definition of a qualifying entity under FRS 100 (Financial Reporting Standard 100). Accordingly, in the year ended 31 March 2013, the company has adopted FRS 101 'Reduced Disclosure Framework' and has ceased to apply all UK Accounting Standards issued prior to FRS 100. Therefore the recognition and measurement requirements of EU-adopted IFRS have been applied, with amendments where necessary in order to comply with Companies Act 2006 and The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) as these are Companies Act 2006 accounts

As permitted by FRS 101, the company has taken advantage of the disclosure exemptions available under that standard in relation to share based payments, financial instruments, capital management, presentation of comparative information in respect of certain assets, standards not yet effective, impairment of assets and related party transactions

Where required, equivalent disclosures are given in the group accounts of Severn Trent Plc. The group accounts of Severn Trent Plc are available to the public and can be obtained as set out in note 34

c) First time adoption of FRS 101

The company's date of transition to FRS 101 is 1 April 2011 and all comparative information in the financial statements has been restated to reflect the company's adoption of FRS 101, except where otherwise required or permitted by paragraphs 6 to 33 of International Financial Reporting Standard 1 – 'First Time Adoption of International Financial Reporting Standards' (IFRS 1). Details of this transition are given in note 35

The company is included in the consolidated accounts of its ultimate parent company Severn Trent Plc. Severn Trent Plc adopted IFRS for the first time in the year ended 31 March 2006. In accordance with IFRS 1, the company has measured its assets and liabilities at the carrying amounts that would be included in the Severn Trent Plc consolidated financial statements

d) Turnover

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

Turnover is not recognised until the service has been provided to the customer or the goods to which the sale relates have been despatched to the customer

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

e) Interest receivable and similar income

Interest income is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable. Dividend income from investments is recognised when the company's rights to receive payment have been established. Interest and dividend income are included in interest receivable and similar income

Severn Trent Water Limited

Notes to the financial statements

f) Exceptional items

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

g) Taxation

Current tax payable is based on taxable profit for the year. Taxable profit differs from profit before tax as reported in the profit and loss account because it excludes items of income and expenses that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred taxation is provided in full, using the liability method, on taxable temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. A deferred tax asset is only recognised to the extent it is probable that sufficient taxable profits will be available in the future to utilise it. Deferred taxation is measured on a non-discounted basis using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the company intends to settle its current tax assets and liabilities on a net basis.

h) Goodwill

Goodwill represents the excess of the fair value of purchase consideration over the fair value of the net assets acquired. Fair value adjustments based on provisional estimates are amended within one year of the acquisition, if required, with a corresponding adjustment to goodwill.

Goodwill is tested for impairment in accordance with the policy set out in note 1n) below and carried at cost less accumulated impairment losses. Goodwill is allocated to the cash-generating unit that derives benefit from the goodwill for impairment testing purposes.

i) Intangible fixed assets

Intangible assets acquired separately are capitalised at cost and are capitalised at fair value at the date of acquisition. Following initial recognition, the historical cost model is applied to intangible assets.

Intangible assets are amortised on a straight line basis over their estimated useful economic lives as follows:

	Years
Software	3-10
Other intangible assets	2-20

Amortisation charged on assets with finite lives is taken to the income statement through operating costs.

Intangible assets are reviewed for impairment where indicators of impairment exist.

Severn Trent Water Limited

Notes to the financial statements

j) Research and development

Research expenditure is expensed when it is incurred. Development expenditure is capitalised and written off over its expected useful economic life where the following criteria are met:

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

Expenditure on tangible fixed assets relating to research and development projects is capitalised and written off over the expected useful life of those assets.

k) Tangible fixed assets

Tangible fixed assets are held at cost (or at deemed cost for infrastructure assets on transition to FRS 101) less accumulated depreciation. The costs of like for like replacement of infrastructure components are recognised in the profit and loss account as they arise. Where it is probable that the expenditure will cause future economic benefits to flow to the company, then costs are capitalised.

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

Borrowing costs directly attributable to the acquisition, construction or production of assets, that necessarily take a substantial period of time to get ready for their intended use, are added to the cost of those assets until such time as the assets are ready for their intended use.

Tangible fixed assets are depreciated to their estimated residual values over their estimated useful lives, with the exception of freehold land which is not depreciated. Assets in the course of construction are not depreciated until commissioned.

The estimated useful lives are:

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

Severn Trent Water Limited

Notes to the financial statements

l) Leased assets

Where the company obtains assets under leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the company as lessee (finance leases), the lower of the fair value of the leased asset or the present value of the minimum lease payments is capitalised as an asset with a corresponding liability representing the obligation to the lessor. Lease payments are treated as consisting of a capital element and a finance charge, the capital element reducing the obligation to the lessor and the finance charge being written off to the profit and loss account at a constant rate over the period of the lease in proportion to the capital amount outstanding. Depreciation is charged over the shorter of the estimated useful life and the lease period.

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

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

m) Grants and contributions

Grants and contributions received in respect of fixed assets, including certain charges made as a result of new connections to the water and sewerage networks, are treated as deferred income and released to the profit and loss account over the useful economic life of those fixed assets.

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

Grants and contributions received in respect of non infrastructure assets are treated as deferred income and are recognised in the profit and loss account over the useful economic life of those assets.

n) Impairment of fixed assets

If the recoverable amount of goodwill, a tangible fixed asset, or any other fixed asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Where the asset does not generate cash flows that are independent from other assets, the company estimates the recoverable amount of the cash-generating unit to which the asset belongs. Recoverable amount is the higher of fair value less costs to sell or estimated value in use at the date the impairment review is undertaken. Fair value less costs to sell represents the amount obtainable from the sale of the asset in an arm's length transaction between knowledgeable and willing third parties, less costs of disposal. Value in use represents the present value of future cash flows expected to be derived from a cash-generating unit, discounted using a pre-tax discount rate that reflects current market assessments of the cost of capital of the cash-generating unit or asset.

The discount rate used is based on the estimated cost of capital of the asset or cash-generating unit.

Goodwill is tested for impairment annually. Impairment reviews are also carried out if there is an indication that an impairment may have occurred, or, where otherwise required, to ensure that fixed assets are not carried above their estimated recoverable amounts.

Impairments are recognised immediately in the profit and loss account.

o) Investments in subsidiaries

Investments in subsidiaries are stated at cost less, where appropriate, provisions for impairment.

p) Stocks

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

Severn Trent Water Limited

Notes to the financial statements

q) Retirement benefits

The company is the sponsoring employer of the Severn Trent group's defined benefit pension schemes

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

Defined benefit pension scheme assets are measured at fair value using bid price for assets with quoted prices. Defined benefit pension scheme liabilities are measured at the balance sheet date by an independent actuary using the projected unit method and discounted at the current rate of return on high quality corporate bonds of equivalent term and currency to the liability. Service cost, which is the increase in the present value of the liabilities of the group's defined benefit pension schemes expected to arise from employee service in the period, is included in operating costs. The expected return on the scheme's assets and the increase during the period in the present value of the scheme's liabilities, arising from the passage of time, are included in other finance income or cost.

Actuarial gains and losses arising from experience adjustments, changes in actuarial assumptions and amendments to pension plans are charged or credited to equity and recorded in the statement of comprehensive income.

The company participates in the Severn Trent group's defined contribution pension schemes. Contributions to defined contribution pension schemes are charged to the income statement in the period in which they fall due.

r) Provisions

Provisions are recognised where

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

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

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

s) Financial instruments

(i) Financial assets

Financial assets are classified into the following categories

- at fair value through profit or loss,
- held to maturity investments,
- available for sale financial assets, and
- loans and receivables

Financial assets at fair value through profit or loss

A financial asset is classified at fair value through profit or loss if it is so designated or if it is classified as "held for trading". Derivative financial assets that are not designated and effective as hedging instruments are required to be classified as "held for trading". The company does not hold or issue derivative financial instruments for trading.

Financial assets at fair value through profit or loss are stated at fair value, with any gains or losses arising on remeasurement recognised in gains/losses on financial instruments in the profit and loss account. Fair value is determined using the methodology described in note 22 (d). Interest received in respect of derivative financial assets is included in interest receivable.

Held to maturity investments

Where the company has the ability and intent to hold an investment to maturity the financial asset is classified as held to maturity. Such financial assets are measured at amortised cost using the effective interest rate method, with any gains or losses being recognised in the profit and loss account.

Severn Trent Water Limited

Notes to the financial statements

s) Financial instruments continued

Available for sale financial assets

After initial recognition at cost (being the fair value of the consideration paid), investments which are classified as available for sale are measured at fair value, with gains or losses recognised in other comprehensive income. When an available for sale investment is disposed of or impaired, the gain or loss previously recognised in other comprehensive income is taken to the profit and loss account. Where there is no active market in the investments and the fair value cannot be measured reliably, the investments are held at cost.

Loans and receivables

Trade receivables, loans and other receivables that have fixed or determinable payments and that are not quoted in an active market are classified as loans and receivables. Such assets are measured at fair value on initial recognition and are subsequently measured at amortised cost using the effective interest rate method unless there is objective evidence that the asset is impaired, where it is written down to its recoverable amount and the irrecoverable amount is recognised as an expense.

Trade receivables that are assessed not to be impaired individually are assessed collectively for impairment by reference to the group's historical collection experience for receivables of similar age.

(ii) Financial liabilities

Financial liabilities are classified as either

- financial liabilities at fair value through profit or loss, or
- other financial liabilities

Financial liabilities at fair value through profit or loss

A financial liability is classified at fair value through profit or loss if it is so designated or if it is classified as "held for trading". Derivative financial liabilities that are not designated and effective as hedging instruments are required to be classified as "held for trading". The company does not hold or issue derivative financial instruments for trading. Financial liabilities at fair value through profit or loss are stated at fair value, with any gains or losses arising on remeasurement recognised in gains/losses on financial instruments in the profit and loss account. Fair value is determined using the methodology described in Severn Trent Plc's group financial statements. Interest paid in respect of derivative financial liabilities is included in interest payable.

Other financial liabilities

Other financial liabilities, including borrowings, are initially recognised at fair value less transaction costs. After initial recognition, other financial liabilities are subsequently measured at amortised cost using the effective interest rate method.

(iii) Hedge accounting

The company uses derivative financial instruments such as cross currency swaps, forward currency contracts and interest rate swaps to hedge its risks associated with foreign currency and interest rate fluctuations. Such derivative instruments are recognised and measured in accordance with the accounting policies described above.

At the inception of the hedge relationship, the company documents

- a) the relationship between the hedging instrument and the hedged item,
- b) its risk management objectives and strategy for undertaking hedge transactions, and
- c) whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows (as appropriate) of the hedged item.

The company continues to test and document the effectiveness of the hedge on an ongoing basis.

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

Fair value hedges

Where a loan or borrowing is in a fair value hedging relationship it is remeasured for changes in fair value of the hedged risk at the balance sheet date, with gains or losses being recognised in gains/losses on financial instruments in the profit and loss account. The gain or loss on the hedging instrument is taken to gains/losses on financial instruments in the profit and loss account where the effective portion of the hedge will offset the gain or loss on the hedged item.

When hedge accounting is discontinued, the fair value adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to the profit and loss account from that date.

Severn Trent Water Limited

Notes to the financial statements

s) Financial instruments continued

Cash flow hedges

The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity and the ineffective portion in gains/losses on financial instruments in the profit and loss account. The gains or losses deferred in equity in this way are recycled through gains/losses on financial instruments in the profit and loss account in the same period in which the hedged underlying transaction or firm commitment is recognised in the profit and loss account.

When hedge accounting is discontinued any cumulative gain or loss on the hedging instrument recognised in equity is held in equity until the forecast transaction occurs, or transferred to gains/losses on financial instruments in the profit and loss account if the forecast transaction is no longer expected to occur.

(iv) Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value, with gains and losses reported in gains/losses on financial instruments in the profit and loss account.

t) Share based payments

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

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

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

u) Foreign currency

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

Severn Trent Water Limited

Notes to the financial statements

2 Significant accounting judgements and key sources of estimation uncertainty

In the process of applying the company's accounting policies, the company is required to make certain judgements, estimates and assumptions that it believes are reasonable based on the information available

The more significant judgements were

a) Tax provisions

Assessing the outcome of uncertain tax positions requires judgements to be made regarding the result of negotiations with and enquires from tax authorities. The assessments made are based on advice from independent tax advisers and the status of ongoing discussions with the tax authority

b) Provisions for other liabilities and charges

Assessing the financial outcome of uncertain commercial and legal positions requires judgements to be made regarding the relative merits of each party's case and the extent to which any claim against the company is likely to be successful. The assessments made are based on advice from the parent company's internal counsel and, where appropriate, independent legal advice

The key accounting estimates were

a) Depreciation and carrying amounts of tangible fixed assets

Calculating the depreciation charge and hence the carrying value for tangible fixed assets requires estimates to be made of the useful lives of the assets. The estimates are based on engineering data and the company's experience of similar assets. Details are set out in note 1 k)

b) Unbilled revenue

The company raises bills and recognises revenue in accordance with its right to receive revenue in line with the limits established by the periodic regulatory price review processes. For water and waste water customers with water meters, the amount recognised is dependent upon the volume supplied including an estimate of the sales value of units supplied between the date of the last meter read and the year end. Meters are read on a cyclical basis and the group recognises revenue for unbilled amounts based on estimated usage from the last billing to the end of the financial year. The estimated usage is based on historical data, judgement and assumptions

c) Provision for impairment of trade receivables

Provisions are made against trade receivables based on historical experience of levels of recovery from accounts in a particular ageing category. The actual amounts collected could differ from the estimated level of recovery which could impact operating results

d) Retirement benefit obligations

Determining the amount of the company's retirement benefit obligations and the net costs of providing such benefits requires assumptions to be made concerning long term interest rates, inflation, salary and pension increases, investment returns and longevity of current and future pensioners. Changes in these assumptions could significantly impact the amount of the obligations or the cost of providing such benefits. The company makes assumptions concerning these matters with the assistance of advice from independent qualified actuaries. Details of the assumptions made are set out in note 31 to the financial statements

3. Revenue

The principal activity of the company is the provision and the treatment of water and the removal of waste water in the UK. The company's activities consist solely of UK activities

	2013 £m	2012 £m
Water and sewerage services	1,502.6	1,447.7
Other services	8.4	9.8
Total turnover	1,511.0	1,457.5
Interest receivable (note 8)	101.0	104.3
Total revenue	1,612.0	1,561.8

Severn Trent Water Limited

Notes to the financial statements

4. Operating costs

	2013			2012		
	Before Exceptional costs	Exceptional costs	Total	Before Exceptional costs	Exceptional costs	Total
	£m	£m	£m	£m	£m	£m
Wages and salaries	176.3	-	176.3	159.3	2.6	161.9
Social security costs	16.3	-	16.3	14.0	0.1	14.1
Pension costs	28.8	-	28.8	26.7	(23.1)	3.6
Share based payments	6.6	-	6.6	3.9	-	3.9
Total employee costs	228.0	-	228.0	203.9	(20.4)	183.5
Power	60.6	-	60.6	51.8	-	51.8
Carbon reduction commitment	5.7	-	5.7	5.9	-	5.9
Raw materials and consumables	43.3	-	43.3	46.8	0.4	47.2
Rates	72.5	-	72.5	68.4	0.1	68.5
Charge for bad and doubtful debts	31.8	-	31.8	30.2	-	30.2
Service charges	31.9	-	31.9	33.3	-	33.3
Depreciation of tangible fixed assets	261.4	-	261.4	252.1	-	252.1
Amortisation of intangible fixed assets	28.9	-	28.9	28.7	-	28.7
Infrastructure maintenance expenditure	147.7	-	147.7	128.9	-	128.9
Hired and contracted services	130.2	-	130.2	139.4	2.9	142.3
Operating lease rentals						
- land and buildings	0.6	-	0.6	0.4	-	0.4
Hire of plant and machinery	3.9	-	3.9	4.8	-	4.8
Loss/(profit) on disposal of fixed assets	1.4	(13.3)	(11.9)	(4.2)	-	(4.2)
Research and development	4.7	-	4.7	4.1	-	4.1
Foreign exchange losses	0.1	-	0.1	0.1	-	0.1
Other operating costs	56.4	-	56.4	51.9	5.4	57.3
	1,109.1	(13.3)	1,095.8	1,046.5	(11.6)	1,034.9
Release from deferred income	(9.3)	-	(9.3)	(8.6)	-	(8.6)
Own work capitalised	(87.0)	-	(87.0)	(76.8)	-	(76.8)
	1,012.8	(13.3)	999.5	961.1	(11.6)	949.5

During the year the following fees were charged by the auditor

	2013 £m	2012 £m
Fees payable to the company's auditors for - the audit of the company's annual accounts	0.2	0.3
Total audit fees	0.2	0.3
Fees payable to the company's auditors for non-audit services	0.1	-
	0.3	0.3

Severn Trent Water Limited

Notes to the financial statements

5. Exceptional items before tax

	2013	2012
	£m	£m
Restructuring costs	-	11.5
Profit on disposal of fixed assets	(13.3)	-
Curtailment gains on defined benefit pension schemes	-	(23.1)
	(13.3)	(11.6)

6. Employee information

The average monthly number of employees (including executive directors) during the year was

	2013	2012
	Number	Number
Average monthly number of employees	5,458	5,162

7. Directors' interests and remuneration

a) Directors' interests

All of the directors as at the end of the year are also directors of Severn Trent Plc, the ultimate parent undertaking, and their interests in the share capital of that company are disclosed in the Annual Report and Accounts of that company for the year ended 31 March 2013. Share options were granted and exercised in accordance with the Severn Trent Sharesave Scheme as appropriate.

The executive directors have further interests in Severn Trent Plc ordinary shares of 97¹⁷/₁₀₀p each by virtue of having received contingent awards of shares under the Severn Trent Long Term Incentive Plan (LTIP) on 21 June 2010, 22 June 2011 and 19 June 2012, deferred shares under the Severn Trent Annual Bonus Scheme on 21 May 2010, 20 May 2011 and 9 July 2012, and contingent shares under the Share Matching Plan on 21 May 2010, 20 May 2011 and 25 May 2012.

The LTIP operates on a three year rolling basis. The Severn Trent Employee Share ownership Trust is operated in conjunction with the LTIP and Annual Bonus Scheme. Awards do not vest until they have been held in trust for three years and specific performance criteria have been satisfied. The performance criteria for the awards are based on either the company's achievement of Return on Regulated Capital Value in excess of the level included in the Severn Trent Water AMP5 business plan or Severn Trent Plc's Total Shareholder Return (TSR).

During the year, the executive directors received half of their bonus for the year ended 31 March 2013 in deferred shares under the Annual Bonus Scheme and contingent matching shares (being 50% of their deferred share award) under the Share Matching Plan. Performance targets apply to the Share Matching Plan award in the same manner as the LTIP.

The individual interests, which represent the maximum aggregate number of shares to which each individual could become entitled, are disclosed in the Annual Report and Accounts of Severn Trent Plc for the year ended 31 March 2013.

Severn Trent Water Limited

Notes to the financial statements

b) Directors' remuneration

	2013 £'000	2012 £'000
Aggregate directors' emoluments during the year (excluding pension contributions)	4,732 9	3,810 1
Pension contributions	72 8	121 2
	4,805 7	3,931 3

i) The emoluments of the non-executive directors are paid by Severn Trent Plc

ii) Retirement benefits are accruing to three directors (2012 three directors) under a defined benefit scheme and two directors (2012 two directors) under a defined contribution scheme

iii) Five directors (2012 five directors) exercised share options or received LTIP awards which vested during the year

c) Highest paid director

	2013 £000	2012 £000
Aggregate emoluments (excluding pension contributions)	1,338 6	1,034 9

The accrued pension at 31 March 2013 for the highest paid director was £29,818 (2012 £29,471). The pension entitlement is that which would be paid annually on retirement based on service to the end of the year. The highest paid director did not exercise any share options during the year.

8. Net interest payable

	2013 £m	2012 £m
Interest payable and similar charges on		
- Amounts payable to group undertakings	(190 1)	(206 6)
- Amounts payable to group undertakings from finance leases	(11 1)	(1 9)
- Finance leases	(11 3)	(12 6)
- Bank and other loans	(19 2)	(18 8)
Pension interest cost	(92 2)	(97 7)
Other finance costs	(1 0)	(0 8)
Total interest payable and similar charges	(324 9)	(338 4)
Interest receivable on		
- Bank deposits	0 8	0 7
- Amounts due from group undertakings	1 3	1 3
- Amounts due from group undertakings for finance leases	5 1	0 9
Expected return on defined benefit scheme assets	88 2	100 7
Other finance income	5 6	0 7
Total interest receivable and similar income	101 0	104 3
	(223 9)	(234 1)

In accordance with IAS 23 borrowing costs of £10.4 million (2012 £10.5 million) incurred funding eligible capital projects have been capitalised at an interest rate of 5.12% (2012 5.93%)

Severn Trent Water Limited

Notes to the financial statements

9. Losses on financial instruments

	2013 £m	2012 £m
Loss on cross currency swaps used as hedging instruments in fair value hedges	(3 3)	(4 8)
Gain arising on adjustment for foreign currency debt in fair value hedges	3 5	12 0
Exchange gain/(loss) on other loans	5 8	(0 6)
Amounts on cash flow hedges transferred from equity	(16 2)	0 4
Loss arising on swaps where hedge accounting is not applied	(39 3)	(77 3)
	(49 5)	(70 3)

10. Tax on profit on ordinary activities

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

	Before exceptional tax £m	Exceptional tax £m	2013 Total £m	2012 Total £m
Current tax				
UK corporation tax at 24% (2012 26%)				
- current year	60 7	(40 5)	20 2	72 9
- adjustment in respect of prior years	(27 2)	-	(27 2)	(5 4)
Total current tax	33 5	(40 5)	(7 0)	67 5
Deferred tax				
Origination and reversal of temporary differences				
- current year	(2 0)	38 8	36 8	7 7
- adjustment in respect of prior years	(4 1)	-	(4 1)	4 1
Exceptional credit arising from rate change	-	(38 3)	(38 3)	(70 4)
Total deferred tax	(6 1)	0 5	(5 6)	(58 6)
	27 4	(40 0)	(12 6)	8 9

The company has adopted the new accounting standard FRS 101 in the current year which has impacted the basis for the corporation tax computations. The most significant impact of this change is that certain amounts that had been taxed in previous years will now be recognised as profits and taxed in future periods. Therefore, to prevent such items being taxed twice, the tax already paid on such items is repayable. The impact of this change was an exceptional credit of £40.5 million to current tax and an exceptional charge of £38.8 million to deferred tax.

The company earns profits primarily in the UK. Therefore the tax rate used for tax on profit on ordinary activities is the standard rate for UK corporation tax. The standard rate of UK corporation tax changed from 26% to 24% with effect from 1 April 2012.

The exceptional deferred tax credit arises from the reduction in the rate at which the temporary differences are expected to reverse from 24% to 23%. On 20 March 2013 the Government announced that the main rate of corporation tax in the UK would reduce to 23% with effect from 1 April 2013 with subsequent reductions per annum to reach 20% by 1 April 2015.

Severn Trent Water Limited

Notes to the financial statements

b) Factors affecting the tax (credit)/charge in the year

The tax assessed for the year is lower than (2012 lower than) the standard rate of corporation tax in the UK of 24% (2012 26%) The differences are explained below

	2013 £m	2012 £m
Profit on ordinary activities before tax	238 1	207 1
Profit on ordinary activities multiplied by the standard UK corporation rate of 24% (2012 26%)	57 0	54 3
Tax effect of expenditure not deductible/(income not taxable) in determining taxable profits	1 9	13 6
Current year impact of rate change	(1 9)	12 7
Exceptional deferred tax credit arising from rate change	(38 3)	(70 4)
Adjustments to tax charge in respect of prior periods	(31 3)	(1 3)
Total tax (credit)/charge for the year	(12 6)	8 9

c) Tax credited to equity

In addition to the amount credited to the income statement, the following amounts of tax have been credited to equity

	2013 £m	2012 £m
Current tax		
Tax on share based payments	0 7	–
Tax on pension contributions in excess of profit and loss charge	1 3	7 8
Total current tax credited to equity	2.0	7 8
Deferred tax		
Tax on actuarial gains/losses	8 7	17 7
Tax on share based payments	–	0 5
Effect of change in tax rate	(3 2)	2 2
Tax on transfers to the profit and loss account	(3 7)	–
Tax on cash flow hedges	8.6	19 7
Total deferred tax credited to equity	10.4	40 1

Severn Trent Water Limited

Notes to the financial statements

11. Dividends on equity shares

Amounts recognised as distributions to equity holders in the period

	2013		2012	
	Pence per share	£m	Pence per share	£m
Final dividend for the year ended 31 March 2012	-	-	26.6	266.0
Interim dividend for the year ended 31 March 2013	7.2	72.0	-	-
		72.0		266.0

The company's dividend policy is to declare dividends which are consistent with the company's regulatory obligations and at a level which is decided each year after consideration of a number of factors, including regulatory uncertainty, future cash flow requirements and balance sheet considerations

The amount declared is expected to vary each year as the impact of these factors changes

12. Goodwill

	2013 £m	2012 £m
At 1 April	-	-
Additions	1.3	-
Cost and Net Book Value at 31 March	1.3	-

On 21 January 2013, the company acquired the operations and net assets of the Bndgend laboratory from Severn Trent Laboratories Limited. This resulted in purchased goodwill of £1.3 million.

13. Intangible fixed assets

	Computer software		Other	Total £m
	Internally generated £m	Purchased £m	Internally generated £m	
Cost				
At 1 April 2012	121.0	172.2	12.0	305.2
Additions	5.9	7.7	-	13.6
At 31 March 2013	126.9	179.9	12.0	318.8
Amortisation				
At 1 April 2012	(101.8)	(90.2)	(8.9)	(200.9)
Amortisation for year	(16.6)	(11.7)	(0.6)	(28.9)
At 31 March 2013	(118.4)	(101.9)	(9.5)	(229.8)
Net book value				
At 31 March 2013	8.5	78.0	2.5	89.0
At 31 March 2012	19.2	82.0	3.1	104.3

Development costs have been capitalised in accordance with IAS 38 'Intangible Assets' and are therefore not treated, for dividend purposes, as a realised loss.

Severn Trent Water Limited

Notes to the financial statements

14. Tangible fixed assets

	Land and buildings £m	Infrastructure assets £m	Fixed plant and equipment £m	Vehicles and mobile plant £m	Total £m
Cost					
At 1 April 2012	2,646.9	4,310.3	3,407.6	45.1	10,409.9
Additions	129.1	103.3	213.2	6.0	451.6
Disposals	(7.5)	(0.1)	(16.6)	(3.6)	(27.8)
At 31 March 2013	2,768.5	4,413.5	3,604.2	47.5	10,833.7
Depreciation					
At 1 April 2012	(856.7)	(1,121.7)	(1,853.4)	(26.6)	(3,858.4)
Charge for the year	(59.9)	(29.6)	(166.7)	(5.2)	(261.4)
Disposals	5.8	-	15.0	3.3	24.1
At 31 March 2013	(910.8)	(1,151.3)	(2,005.1)	(28.5)	(4,095.7)
Net book value					
At 31 March 2013	1,857.7	3,262.2	1,599.1	19.0	6,738.0
At 31 March 2012	1,790.2	3,188.6	1,554.2	18.5	6,551.5

Included in the above are assets under construction of £504.2 million (2012 £380.8 million) which are not depreciated

Cumulative borrowing costs capitalised included in the cost of tangible fixed assets amount to £34.7 million (2012 £24.3 million)

The carrying amount of tangible fixed assets includes the following amounts in respect of assets held under finance leases

	Land and buildings £m	Infrastructure assets £m	Fixed plant and equipment £m	Total £m
Net book value				
At 31 March 2013	184.1	120.6	54.8	359.5
At 31 March 2012	188.0	121.2	74.2	383.4

The net book value of land and buildings is analysed as follows

	2013 £m	2012 £m
Freehold	1,857.4	1,789.9
Short leasehold	0.3	0.3
	1,857.7	1,790.2

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Notes to the financial statements

15. Fixed asset investments

The company has the following investments which principally affected its profits or net assets

Subsidiary undertakings	Country of operation and incorporation	Principal activity	Percentage and class of share capital held	Shares in subsidiary undertakings £m
Cost and net book value				
At 1 April and 31 March 2013				347.9
East Worcester Water Limited	England and Wales	Finance company	100% Ordinary & 100% non-voting	
Severn Trent General Partnership Limited	Scotland	Finance company	100% Ordinary	
Severn Trent LCP Limited	England and Wales	Leasing company	100% Ordinary	
Severn Trent Leasing Limited	England and Wales	Leasing company	100% Ordinary	
Severn Trent Reservoirs Limited	England and Wales	Finance company	100% Ordinary	
Severn Trent Utilities Finance Plc	England and Wales	Finance company	100% Ordinary	

The company also has an indirect investment in Severn Trent Limited Partnership, a limited partnership registered in Scotland, as a result of Severn Trent General Partnership Limited being the general partner

In the opinion of the directors the fair values of the company's investments are not less than the amount at which they are stated in the balance sheet

16. Stocks

	2013 £m	2012 £m
Raw materials and consumables	6.1	6.3

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Notes to the financial statements

17. Debtors

Amounts falling due within one year

	2013 £m	2012 £m
Trade debtors	267.1	246.7
Bad debt provision	(111.3)	(100.9)
Net trade debtors	155.8	145.8
Amounts owed by group undertakings	26.0	8.9
Amounts receivable by group undertakings under finance leases	0.5	0.5
Other debtors	27.9	28.7
Corporation tax	20.9	-
Prepayments and accrued income	199.1	184.0
	430.2	367.9

Amounts falling due after more than one year

	2013 £m	2012 £m
Loans owed by group undertakings	105.7	104.4
Amounts receivable by group undertakings under finance leases	101.3	102.6
Prepayments and accrued income	93.4	99.4
	300.4	306.4

Severn Trent Water Limited

Notes to the financial statements

18. Finance lease receivables

Minimum lease payments receivable are as follows

	2013 £m	2012 £m
Within one year	5 7	5 7
Between one and two years	5 7	5 7
Between two and five years	17 0	17 0
After five years	255 5	261 1
	283 9	289 5
Less unearned interest receivable	(182 1)	(186 4)
	101 8	103 1

The present values of minimum lease payments receivable are as follows

	2013 £m	2012 £m
Within one year	0 5	0 5
Between one and two years	0 5	0 5
Between two and five years	1 7	1 6
After five years	99 1	100 5
	101 8	103 1

Disclosed in the balance sheet as

Debtors amounts falling due within one year	0 5	0 5
Debtors amounts falling due after one year	101 3	102 6
	101 8	103 1

The company has granted 46-59 year finance leases in respect to concrete settling tanks. The interest terms were set at the inception of the leases. Leases with capital outstanding of £101.8 million (2012: £103.1 million) bear interest at a weighted average interest rate of 5.1% (2012: 5.1%).

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Notes to the financial statements

19. Creditors: amounts falling due within one year

	2013 £m	2012 £m
Bank loans	165 3	-
Loans due to parent and fellow subsidiary undertakings	-	229 6
Amounts owed to parent and fellow subsidiary undertakings under finance leases	12 6	23 2
Obligations under finance leases	0 5	-
Borrowings	178 4	252 8
Trade creditors	15 1	14 8
Amounts owed to parent and fellow subsidiary undertakings	129 6	120 8
Other creditors	6 2	8 8
Corporation tax payable	-	36 8
Other taxation and social security	5 1	4 9
Accruals and deferred income	261 4	261 6
Derivative financial liabilities	0 4	0 1
	596 2	700 6

20. Creditors: amounts falling due after more than one year

	2013 £m	2012 £m
Bank loans	552 4	610 3
Loans due to parent and fellow subsidiary undertakings	3,845 0	3,340 2
Amounts owed to parent and fellow subsidiary undertakings under finance leases	316 4	319 7
Obligations under finance leases	201 2	218 8
Borrowings	4,915 0	4,489 0
Accruals and deferred income	447 1	407 6
Derivative financial liabilities	266 2	238 9
	5,628 3	5,135 5

Borrowings are repayable as follows

	2013			2012		
	Loans with other repayment terms £m	Finance leases £m	Total £m	Loans with other repayment terms £m	Finance leases £m	Total £m
Financial liabilities due within one year	(165 3)	(13 1)	(178 4)	(229 6)	(23 2)	(252 8)
Between one and two years	(174 8)	(34 7)	(209 5)	(181 5)	(41 5)	(223 0)
Between two and five years	(1,270 3)	(117 0)	(1,387 3)	(905 2)	(136 1)	(1,041 3)
After more than five years	(2,952 3)	(365 9)	(3,318 2)	(2,863 8)	(360 9)	(3,224 7)
Total financial liabilities due after one year	(4,397 4)	(517 6)	(4,915.0)	(3,950 5)	(538 5)	(4,489 0)
	(4,562 7)	(530 7)	(5,093 4)	(4,180 1)	(561 7)	(4,741 8)

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Notes to the financial statements

Loans repayable partly or wholly after five years comprise

	Rate of interest %	Weighted average interest rate %	5-10 years £m	10-15 years £m	15-20 years £m	>20 years £m	2013 £m
Loans due to parent and fellow subsidiary undertakings							
Fixed rate	3.6-6.3	5.1	-	789.4	597.9	246.7	1,634.0
Floating rate	1.0-1.2	1.0	-	20.8	16.8	-	37.7
RPI linked	1.5-4.0	1.9	-	35.2	141.6	851.5	1,028.3
Bank loans							
Fixed rate	4.5	4.5	150.0	-	-	-	150.0
RPI linked	1.5	1.5	102.4	-	-	-	102.4
			252.4	845.4	756.3	1,098.2	2,952.3

	Rate of interest %	Weighted average interest rate %	5-10 years £m	10-15 years £m	15-20 years £m	>20 years £m	2012 £m
Loans due to parent and fellow subsidiary undertakings							
Fixed rate	4.9-6.3	5.7	397.0	295.6	590.1	246.8	1,529.5
Floating rate	1.0-1.9	1.2	-	19.4	17.4	-	36.8
RPI linked	1.5-4.0	2.3	-	34.1	137.3	826.1	997.5
Bank loans							
Fixed rate	4.5	4.5	150.0	-	-	-	150.0
Floating rate	1.1	1.1	150.0	-	-	-	150.0
			697.0	349.1	744.8	1,072.9	2,863.8

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Notes to the financial statements

21. Finance lease creditor

The minimum payments under finance leases are as follows

	2013 £m	2012 £m
Within one year	31.5	30.7
Between one and two years	54.4	52.4
Between two and five years	169.7	186.8
After five years	535.0	573.9
	790.6	843.8
Less future finance charges	(259.9)	(282.1)
Present value of lease obligations	530.7	561.7

The present values of minimum lease payments are as follows

	2013 £m	2012 £m
Within one year	13.1	23.2
Between one and two years	34.7	41.5
Between two and five years	117.0	136.1
After five years	365.9	360.9
Present value of lease obligations	530.7	561.7

Disclosed in the balance sheet as:

Creditors - amounts falling due within one year	13.1	23.2
Creditors - amounts falling due after more than one year	517.6	538.5
	530.7	561.7

The remaining terms of finance leases ranged from 2 to 19 years at 31 March 2013. Interest terms are set at the inception of the leases. Leases with capital outstanding of £415.0 million (2012: £434.7 million) bear fixed interest at a weighted average rate of 5.4% (2012: 5.4%). The lease obligations are secured over the related assets.

There were no contingent rents, escalation clauses or material renewal or purchase options. The terms of the finance leases do not impose restriction on dividend payments, additional debt or further leasing.

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Notes to the financial statements

22. Financial instruments

a) Categories of financial assets held at fair value

	2013 £m	2012 £m
Fair value through profit and loss		
Cross currency swaps - fair value hedges	44.5	67.7
Interest rate swaps - not hedge accounted	21.0	23.8
Energy swaps - cash flow hedges	0.9	2.4
Total derivative assets	66.4	93.9

b) Categories of financial liabilities held at fair value

	2013 £m	2012 £m
Fair value through profit and loss		
Cross currency swaps - not hedge accounted	(8.4)	(0.5)
Interest rate swaps - cash flow hedges	(116.2)	(80.4)
Interest rate swaps - not hedge accounted	(140.1)	(156.5)
Energy swaps - cash flow hedges	(1.8)	(1.4)
Foreign exchange forward contracts - not hedge accounted	(0.1)	(0.2)
	(266.6)	(239.0)

c) Derivatives

The company enters into a variety of derivative financial instruments to manage its exposure to interest rate and foreign exchange rate risk. These risks are managed centrally by the Severn Trent group treasury department. Derivative financial instruments are not held for trading.

Interest rate swaps

The company has interest rate swaps in place to manage its exposure to interest rate risk arising from its anticipated borrowing requirements for the remainder of AMP 5. Under the terms of the interest rate swaps, the company agrees with other parties to exchange, mainly semi-annually, the difference between fixed contract and floating rate interest rate swaps to hedge future debt. Economically these act to fix the interest cost of debt which is denominated as floating rate, but do not achieve hedge accounting under the strict criteria of IAS 39.

During the year the company terminated three of these contracts, with a notional value of £100 million, at a cash outlay of £44.3 million.

The company has also entered into a number of interest rate swaps with future start dates in AMP 6. These contracts enable the company to mitigate interest rate risk on debt which is highly probable to be issued in AMP 6 to fund the capital programme. These have been accounted for as cash flow hedges.

Cross currency swaps

The company holds cross currency swaps to manage the exchange rate risk arising from foreign currency borrowings. Under the terms of the contracts, the company agrees with other parties to swap the foreign currency proceeds into sterling debt bearing interest based on LIBOR. The terms of the receivable leg of the swap closely match the terms of the underlying debt hence these are expected to be effective hedges. These are accounted for as fair value hedges where the strict criteria of IAS 39 are met.

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Notes to the financial statements

Forward foreign exchange contracts

The company does not have a significant transactional exposure to exchange rates but holds a small number of forward foreign exchange contracts which are not material. These are not in designated hedge relationships and so are classified as 'Held for trading'.

Energy swaps

The company has entered into a series of energy swaps under which it has agreed to exchange the difference between fixed and market prices of electricity at six-monthly intervals up to March 2015.

d) Fair value measurements recognised in the balance sheet

The fair values of financial instruments that were measured subsequent to initial recognition at fair value, were based on observable inputs other than quoted prices for identical instruments.

The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows estimated and discounted based on the application of yield curves derived from quoted interest rates.

Cross currency swaps and forward exchange contracts are valued by reference to quoted forward exchange rates at the balance sheet date and yield curves derived from quoted interest rates matching the maturities of the contracts.

e) Changes in value of financial instruments at fair value

Changes in fair value which are included in the profit and loss account are set out in note 9.

Changes in the amounts deferred in equity during the period relating to cash flow hedges were as follows:

	2013 £m	2012 £m
Fair value losses deferred in equity at the start of the period	(87 0)	(5 6)
Fair value losses recognised in equity in the period	(37 6)	(81 0)
Amounts transferred to finance costs in the period	16 2	(0 4)
Fair value losses deferred in equity at the end of the period	(108 4)	(87 0)

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Notes to the financial statements

23. Provisions for liabilities and charges

	Deferred taxation £m	Restructuring £m	Other provisions £m	Total £m
At 1 April 2012	843.1	1.8	7.6	852.5
Charged to profit and loss account	(5.6)	(0.7)	(0.9)	(7.2)
Utilised in year	(10.4)	(0.4)	(2.9)	(13.7)
Unwinding of discount	-	-	0.6	0.6
At 31 March 2013	827.1	0.7	4.4	832.2

The restructuring provision reflects costs to be incurred in respect of committed programmes. Substantially all of the associated outflows are expected to occur within one year (2012: one year) of the balance sheet date.

Other provisions consist of dilapidation costs and onerous leasehold property costs. The associated outflows are expected to arise over a period of up to seven years (2012: eight years) from the balance sheet date.

24. Deferred tax

An analysis of the movements in the major deferred tax liabilities and assets recognised by the company is set out below.

	Accelerated tax depreciation £m	Retirement benefit obligation £m	Fair value of financial instruments £m	Other £m	Total £m
At 1 April 2011	1,015.3	(75.9)	(13.2)	16.1	942.3
Charge to profit and loss account	(2.2)	4.9	(17.6)	26.2	11.3
Credit to profit and loss account arising from rate change	(72.6)	3.1	0.5	(1.4)	(70.4)
Credit to other comprehensive income	-	(17.7)	(19.7)	(0.5)	(37.9)
Credit to other comprehensive income arising from rate change	(5.5)	2.7	0.5	0.1	(2.2)
At 1 April 2012	935.0	(82.9)	(49.5)	40.5	843.1
Charge to profit and loss account	(5.0)	-	(1.4)	39.1	32.7
Credit to profit and loss account arising from rate change	(39.0)	1.4	1.1	(1.8)	(38.3)
Credit to other comprehensive income	-	(8.7)	(4.9)	-	(13.6)
Charge to other comprehensive income arising from rate change	-	2.1	1.0	0.1	3.2
At 31 March 2013	891.0	(88.1)	(53.7)	77.9	827.1

Deferred tax assets and liabilities have been offset. The offset amounts, which are to be recovered/settled after more than 12 months, are as follows:

	2013 £m	2012 £m
Deferred tax asset	(151.2)	(177.7)
Deferred tax liability	978.3	1,020.8
	827.1	843.1

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Notes to the financial statements

25. Share capital

	2013	2012
	£m	£m
Total issued and fully paid		
1,000,000,000 ordinary shares of 10p each (2012 £1)	100 0	1,000 0
	100 0	1,000 0

On 22 March 2013 the company made a bonus issue of 378 million £1 ordinary 'B' shares from the infrastructure reserve that was created on transition to FRS 101 (see note 35) This increased share capital to £1,378 0 million

On the same date, the parent company passed a resolution to reduce the nominal value of each ordinary share to 10p and cancelled the ordinary 'B' shares The reduction in share capital of £1,278 0 million that resulted has been credited to reserves

26. Hedging reserve

The hedging reserve arises from gains or losses on interest rate swaps taken to equity under the hedge accounting provisions of IAS 39 and the transition rules under IFRS 1

27. Infrastructure reserve

The infrastructure reserve arose on restating infrastructure assets to fair value as deemed cost on transition to FRS 101 During the year, bonus shares were issued from this reserve Further details can be found in note 25

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Notes to the financial statements

28. Share based payments

At 31 March 2013 there were no options exercisable under any of the share based remuneration schemes (2012 nil)

a) Long Term Incentive Plan (LTIP)

Under the LTIP annual conditional awards of shares in the ultimate parent company may be made to executive directors and senior staff. Awards are subject to performance conditions and continued employment throughout the vesting period.

During the year awards of 96,530 shares (2012 108,744 shares) were made with a fair value of £15.36 (2012 £12.16). These awards are subject to achievement of turnover and profit targets in the year ending 31 March 2014.

b) Employee Sharesave Scheme

Under the terms of the Sharesave Scheme, the board of the ultimate parent company may grant the right to purchase ordinary shares in Severn Trent Plc to those employees who have entered into an HMRC approved Save As You Earn contract for a period of three, five or seven years.

The weighted average share price at the date of exercise for share options exercised during the period was £16.49 (2012 £15.00). The options outstanding at 31 March 2013 had a weighted average option price of £10.26 (£9.49) and a weighted average remaining contractual life of 3.13 years (2012 2.89 years).

c) Share Matching Plan (SMP)

Under the Share Matching Plan members of the Executive Committee receive matching share awards over those shares which have been acquired under the deferred share component of the annual bonus scheme. Matching shares may be awarded at a maximum ratio of one matching share for every one deferred share and are subject to a three year vesting period. During the year matching shares were awarded at a ratio of 0.5 to 1.

Matching shares are subject to total shareholder return over three years measured relative to the companies ranked 51-150 by market capitalisation in the FTSE Index (excluding investment trusts). This replicates the LTIP performance condition for the July 2010 award.

The number of shares subject to an award will increase to reflect dividends paid through the performance period on the basis of such notional dividends being reinvested at the then prevailing share price. Awards will normally vest as soon as the Remuneration Committee determines that the performance conditions have been met provided that the participant remains in employment at the end of the performance period.

During the year 17,676 (2012 18,251) matching shares with a fair value of £11.43 (2012 £8.84) were awarded to 9 (2012 9) employees.

d) Share Incentive Plan (SIP)

Under the SIP the board may grant share awards to employees of group companies. During the year the board has announced that it will make awards under the SIP based on performance against Severn Trent Water's targets for its Key Performance Indicators. Eligible employees will be entitled to shares to a maximum value of £750. It is expected that these awards will be made in August 2013. SIP shares vest with the employee on the date of grant.

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Notes to the financial statements

29 Cash flow statement

a) Reconciliation of operating profit to operating cash flows

	2013 £m	2012 £m
Profit before interest and tax	511 5	508 0
Depreciation of property, plant and equipment	261 4	252 1
Amortisation of intangible assets	28 9	28 7
Pension service cost	23 2	22 6
Curtailment credit	–	(23 1)
Pension contributions	(32 5)	(51 1)
Share based payments charge	6 6	3 9
Profit on sale of property, plant and equipment	(11 9)	(4 2)
Deferred income movement	(9 3)	(8 6)
Provisions charged to the income statement	(1 6)	1 7
Utilisation of provisions for liabilities and charges	(3 3)	(4 2)
Decrease/(increase) in stocks	0 2	(0 1)
Increase in debtors	(19 6)	(118 5)
Decrease in creditors	4 3	10 4
Cash generated from operations	757 9	617 6
Tax paid	(53 5)	(67 8)
Net cash generated from operating activities	704 4	549 8

b) Non-cash transactions

No additions to property, plant and equipment during the year were financed by new finance leases (2012 nil) Assets transferred from developers were £23 0 million (2012 £37 0 million)

c) Exceptional cash flows

The following cash flows arose from items classified as exceptional in the income statement

	2013 £m	2012 £m
Restructuring costs	(4 4)	(14 4)
Proceeds on disposal of fixed assets	15 1	–
	10 7	(14 4)

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Notes to the financial statements

d) Reconciliation of movement in cash and cash equivalents to movement in net debt

	As at 1 April 2012 £m	Cash flow £m	Fair value adjustments £m	RPI uplift on index-linked debt £m	Other non cash movements £m	As at 31 March 2013 £m
Cash and cash equivalents	0.3	328.3	-	-	-	328.6
Loans receivable from other group companies	104.4	-	-	-	1.3	105.7
Loans payable to other group companies	(3,569.8)	(247.6)	3.4	(32.4)	1.4	(3,845.0)
Bank loans	(610.3)	(100.0)	-	(7.4)	-	(717.7)
Other loans	-	-	-	-	-	-
Finance leases	(561.7)	29.1	-	-	1.9	(530.7)
Cross currency swaps	67.1	-	(11.3)	-	(19.7)	36.1
Net debt	(4,570.0)	9.8	(7.9)	(39.8)	(15.1)	(4,623.0)

30. Financial commitments

Capital commitments are as follows

	2013 £m	2012 £m
Contracted for but not provided for	214.9	159.8

In addition to these commitments, the company has longer term expenditure plans which include investments to achieve improvements in performance mandated by Ofwat and to provide for growth in demand for water and sewerage services

At the balance sheet date, the company had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows

	2013 £m	2012 £m
Within one year	1.9	1.3
Between two and five years	6.2	5.1
After five years	5.4	4.9
	13.5	11.3

Operating lease payments represent rentals payable by the company for certain of its office properties, plant and equipment

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31. Retirement benefit scheme

The company is the sponsoring employer of the defined benefit pension schemes operated by the Severn Trent group in the UK. As there is no contractual agreement or stated policy for allocating the net defined benefit cost to individual group entities this company has recognised the full cost and deficit.

The amounts disclosed below are the plan as a whole as presented in these financial statements.

a) Defined benefit pension schemes

(1) Amount included in the balance sheet arising from the company's obligations under defined benefit pension schemes

	2013 £m	2012 £m
Fair value of scheme assets		
Equities	877.2	798.6
Gilts	274.6	235.2
Corporate bonds	360.9	339.1
Property	147.8	105.7
Hedge funds	55.8	52.6
Cash	8.0	26.0
Total fair value of assets	1,724.3	1,557.2
Present value of the defined benefit obligations - funded schemes	(2,098.7)	(1,894.4)
	(374.4)	(337.2)
Present value of the defined benefit obligations - unfunded schemes	(9.3)	(8.6)
Liability recognised in the balance sheet	(383.7)	(345.8)

Movements in the fair value of the scheme assets were as follows

	2013 £m	2012 £m
Fair value at 1 April	1,557.2	1,473.4
Expected return on scheme assets	88.2	100.7
Company contributions	32.5	51.1
Contribution from intra-group asset backed funding arrangement	8.2	-
Other contributions from Severn Trent group companies	2.8	2.4
Contributions from scheme members	5.1	5.6
Actuarial gains/(losses) recognised in the statement of comprehensive income	101.3	(4.5)
Benefits paid	(71.0)	(71.5)
Fair value at 31 March	1,724.3	1,557.2

Other contributions from Severn Trent group companies are included in actuarial gains/losses recognised in the statement of comprehensive income.

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Movements in the present value of the defined benefit obligations were as follows

	2013 £m	2012 £m
Present value at 1 April	1,903 0	1,765 5
Service cost	22 8	22 6
Past service cost	0 4	–
Interest cost	92 2	97 7
Net curtailment gain	–	(23 1)
Contributions from scheme members	5 1	5 6
Actuarial losses recognised in the statement of comprehensive income	155 5	106 2
Benefits paid	(71 0)	(71 5)
Present value at 31 March	2,108 0	1,903 0

Of which

	2013 £m	2012 £m
Amounts relating to funded schemes	2,098 7	1,894 4
Amounts relating to unfunded schemes	9 3	8 6
Present value at 31 March	2,108 0	1,903 0

(ii) Amounts recognised in the profit and loss account in respect of these defined benefit pension schemes

	2013 £m	2012 £m
Amounts charged to operating costs		
Current service cost	(22 8)	(22 6)
Exceptional curtailment gain	–	23 1
Past service cost	(0 4)	–
	(23 2)	0 5
Amounts charged to finance costs		
Interest cost	(92 2)	(97 7)
Amounts credited to finance income		
Expected return on scheme assets	88 2	100 7
Total amount credited/(charged) to the profit and loss account	(27 2)	3 5

The actual return on scheme assets was a gain of £189.5 million (2012 gain of £95.9 million)

Actuarial gains and losses for the current and prior year are reported in the statement of comprehensive income. The cumulative amount of actuarial gains and losses recognised in equity since the adoption of the recognition and measurement principles of IFRS is a net loss of £334.2 million (2012 net loss of £280.1 million)

In addition, contributions made by other Severn Trent group entities are also included in actuarial gains and losses recognised in the statement of comprehensive income

Severn Trent Water Limited

Notes to the financial statements

(iii) Background

The Severn Trent group operates two defined benefit pension schemes in the UK, covering the majority of UK employees. The defined benefit pension schemes are funded to cover future salary and pension increases and their assets are held in separate funds administered by trustees. The trustees are required to act in the best interests of the schemes' beneficiaries. A formal actuarial valuation of each scheme is carried out on behalf of the trustees at triennial intervals by an independent professionally qualified actuary. Under the defined benefit pension schemes, members are entitled to retirement benefits calculated as a proportion (varying between $\frac{1}{30}$ and $\frac{1}{80}$ for each year of service) of their salary for the final year of employment with the group or, if higher, the average of the highest three consecutive years' salary in the last ten years of employment.

The defined benefit pension schemes will close to future accrual on 31 March 2015. A new defined contribution pension scheme has been established and members of the defined benefit pension schemes will then become members of the new defined contribution pension scheme. The existing defined contribution pension scheme will also be replaced by the new pension arrangements with effect from 1 April 2015.

From 1 April 2012 new employees have been automatically enrolled into this scheme and those employees who were not members of a Severn Trent scheme were automatically enrolled into this scheme from 1 April 2013.

The final salary sections of the pension schemes listed below are closed to new entrants and the age profile of scheme participants is expected to rise and hence service costs are also expected to rise until the schemes are closed to future accrual.

The schemes typically expose the company to actuarial risks such as market risk, interest rate risk and longevity risk.

The UK defined benefit pension schemes and the date of their last formal actuarial valuation are as follows:

	Date of last formal actuarial valuation
Severn Trent Pension scheme (STPS)*	31 March 2010
Severn Trent Mirror Image Pension Scheme	31 March 2010

* The STPS is by far the largest of the Severn Trent group's UK defined benefit schemes.

The group has an obligation to pay pensions to a number of former employees, whose benefits would otherwise have been restricted by the Finance Act 1989 earnings cap. Provision for such benefits amounting to £9.3 million (2012: £8.6 million) is included as an unfunded scheme within the retirement benefit obligation.

(iv) Actuarial assumptions

The major assumptions used in the valuation of the STPS (also the approximate weighted average of assumptions used for the valuations of all group schemes) were as follows:

	2013 %	2012 %
Price inflation	3.20	3.10
Salary increases	3.00	3.60
Pension increases in payment	3.20	3.10
Pension increases in deferment	3.20	3.10
Discount rate	4.40	4.90
Long term rate of return on		
Equities	6.60	6.80
Gilts	3.10	3.30
Corporate bonds	4.30	4.90
Property	5.50	5.80
Hedge funds	6.00	6.30
Cash	3.10	3.90

Severn Trent Water Limited

Notes to the financial statements

The assumption for price inflation is derived from the difference between the yields on longer term fixed rate gilts and on index-linked gilts. The discount rate is set by reference to AA rated sterling 18 year corporate bonds.

The expected rate of return on scheme assets is based on market expectations at the beginning of the period for returns over the life of the benefit obligation. For gilts and corporate bonds the expected rates of return are based on market yields. For equities, property and hedge funds, a risk premium has been added to the gilt rate.

The mortality assumptions are based on those used in the triennial valuation of the STPS as at 31 March 2010 updated by a further investigation carried out in connection with the 2013 valuation, which indicated that members' life expectancy had not been as high as the previous investigation had predicted.

The mortality assumptions adopted at the year end and the life expectancies at age 65 implied by the assumptions are as follows:

	2013	2012
Mortality table used		
- men	"SAPS" S1NMA_L	"SAPS" S1NMA_L
- women	S1NFA_L	S1NFA_L
Mortality table compared with standard table		
- men	116%	110%
- women	92%	78%
Future improvement per annum	1.0%	0.5%
Remaining life expectancy for members currently aged 65 (years)		
- men	21.5	21.2
- women	24.6	25.1
Remaining life expectancy at age 65 for members currently aged 45 (years)		
- men	22.7	21.8
- women	26.2	25.9

The calculation of the scheme liabilities is sensitive to the actuarial assumptions and in particular to the assumptions relating to discount rate, price inflation and mortality. The following table summarises the estimated impact on scheme liabilities and service cost resulting from changes to key actuarial assumptions whilst holding all other assumptions constant.

Assumption	Change in assumption	Impact on scheme liabilities
Discount rate	Increase/decrease by 0.1%	Decrease/increase by £38 million
Price inflation	Increase/decrease by 0.1%	Increase/decrease by £35 million
Mortality	Increase in life expectancy by 1 year	Increase by £55 million

In reality, interrelationships exist between the assumptions, particularly between the discount rate and price inflation. The above analysis does not take into account the effect of these interrelationships.

(v) Effect on future cash flows

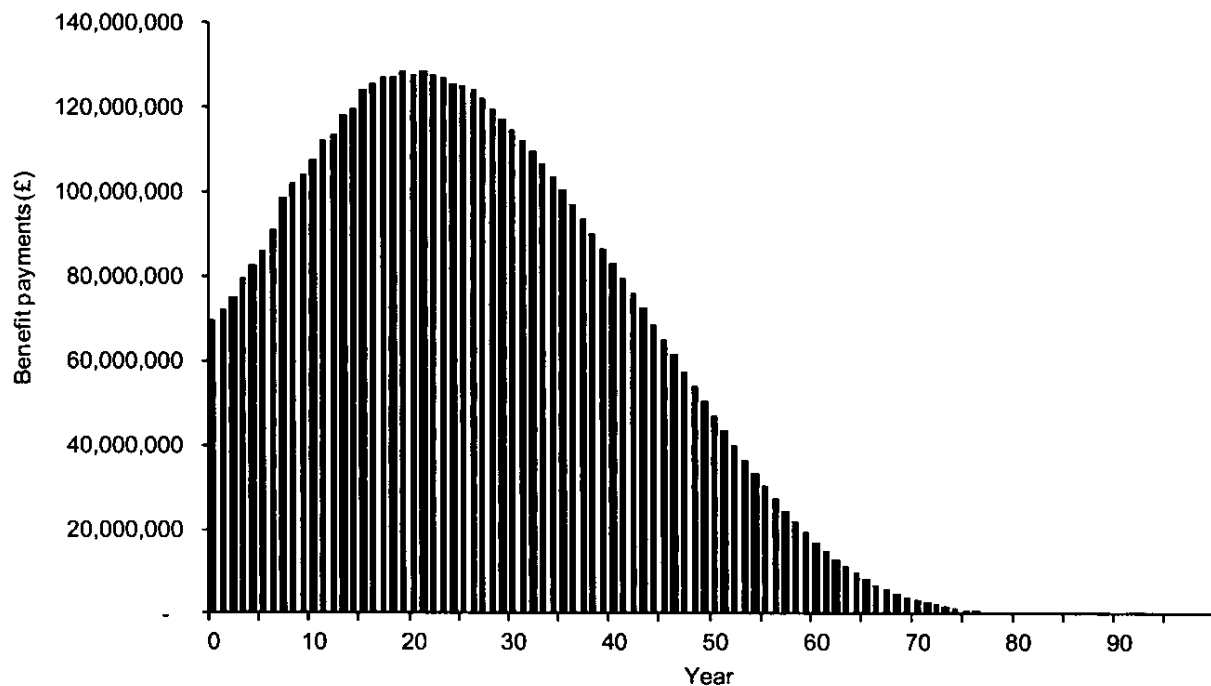
Contribution rates are set in consultation with the trustees for each scheme and each participating employer.

The average duration of the benefit obligation at the end of the year is 18 years (2012: 18 years). The expected cash flows payable from the scheme are presented in the graph below.

Severn Trent Water Limited

Notes to the financial statements

Severn Trent Pension Scheme - expected benefit payments



It is anticipated that normal contributions to the scheme in the year ended 31 March 2014 will be unchanged. The triennial valuations for both schemes for the year ending 31 March 2013 is in progress. Pending completion of this valuation, future lump sum deficit contributions will include a payment of £10 million per annum in cash and a further £8 million per annum through an asset backed funding arrangement.

Severn Trent Water Limited

Notes to the financial statements

(vi) History of actual and expected performance of pension scheme assets and liabilities

	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Present value of defined benefit obligations	(2,108 0)	(1,903 0)	(1,765 5)	(1,747 9)	(1,308 0)
Fair value of scheme assets	1,724 3	1,557 2	1,473 4	1,393 0	1,075 0
Deficit in schemes	(383 7)	(345 8)	(292 1)	(354 9)	(233 0)
Difference between actual and expected return on scheme assets	101 3	(4 5)	12 2	270 4	(329 8)
Experience adjustments on scheme liabilities	(155 4)	(106 2)	105 1	19 8	(7 9)

b) Defined contribution pension scheme

The company also operates a defined contribution scheme. This scheme is operated as part of the Severn Trent Group Pension Scheme and commenced operation on 1 September 2001. The pension charge for this scheme for the year ended 31 March 2013 was £5.7 million (2012: £4.2 million).

32. Contingent liabilities

The banking arrangements of the company operate on a pooled basis with certain fellow group undertakings. Under these arrangements participating companies guarantee each others balances only to the extent that their credit balances can be offset against overdrawn balances of other Severn Trent group companies. As at 31 March 2013, the company had contingent liabilities of £0.2 million (2012: £0.8 million).

33. Related party transactions

Transactions with the directors of the company are disclosed in note 7.

The retirement benefit schemes entered into by the company are considered to be related parties. Details of transactions and balances with the retirement benefit schemes are disclosed in note 31.

34. Ultimate parent undertaking

The immediate parent undertaking is Severn Trent Draycote Limited.

The ultimate parent undertaking and controlling party is Severn Trent Plc, which is the parent undertaking and controlling party of the smallest and largest group to consolidate these financial statements. Copies of the Severn Trent Plc consolidated financial statements can be obtained from Severn Trent Plc's registrars at Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA.

Severn Trent Water Limited

Notes to the financial statements

35. Transition to FRS 101

This is the first year that the company has presented its financial statements under FRS 101. The last financial statements prepared under the previous UK accounting framework were for the year ending 31 March 2012. Therefore the date of transition was 1 April 2011.

Reconciliation of equity at 1 April 2011

	As previously reported £m	Effect of transition £m	Under FRS 101 £m
Fixed assets			
Intangible fixed assets	-	123.5	123.5
Tangible fixed assets	6,029.8	372.8	6,402.6
Derivative financial assets	-	77.6	77.6
Investments	235.7	-	235.7
	6,265.5	573.9	6,839.4
Current assets			
Stock	6.3	(0.2)	6.1
Debtors - amounts falling due in more than one year	43.2	2.7	45.9
Debtors - amounts falling due within one year	345.4	-	345.4
Derivative financial assets	-	25.7	25.7
Cash at bank and in hand	10.1	-	10.1
	405.0	28.2	433.2
Creditors - amounts falling due within one year	(552.3)	(18.0)	(570.3)
Net current liabilities	(147.3)	10.2	(137.1)
Total assets less current liabilities	6,118.2	584.1	6,702.3
Creditors - amounts falling due after more than one year	(3,912.8)	(594.8)	(4,507.6)
Retirement benefit obligation	(198.4)	(93.7)	(292.1)
Provisions for liabilities and charges	(438.3)	(512.8)	(951.1)
Net assets	1,568.7	(617.2)	951.5
Capital and reserves			
Share capital	1,000.0	-	1,000.0
Profit and loss account	568.7	(938.4)	(369.7)
Hedging reserve	-	(56.8)	(56.8)
Infrastructure reserve	-	378.0	378.0
Shareholder's funds	1,568.7	(617.2)	951.5

Severn Trent Water Limited

Notes to the financial statements

Reconciliation of equity at 31 March 2012

	As previously reported £m	Effect of transition £m	Under FRS 101 £m
Fixed assets			
Intangible fixed assets	-	104 3	104 3
Tangible fixed assets	6,111 1	440 4	6,551 5
Derivative financial assets	-	70 5	70 5
Investments	413 5	(65 6)	347 9
	6,524 6	549 6	7,074 2
Current assets			
Stock	6 4	(0 1)	6 3
Debtors amounts falling due in more than one year	137 6	168 8	306 4
Debtors amounts falling due within one year	370 6	(2 7)	367 9
Derivative financial assets	-	23 4	23 4
Cash at bank and in hand	0 3	-	0 3
	514 9	189 4	704 3
Creditors amounts falling due within one year	(686 8)	(57 1)	(743 9)
Net current (liabilities)/assets	(171 9)	132 3	(39 6)
Total assets less current liabilities	6,352 7	681 9	7,034 6
Creditors amounts falling due after more than one year	(4,348 2)	(744 0)	(5,092 2)
Retirement benefit obligation	(170 1)	(175 7)	(345 8)
Provisions for liabilities and charges	(513 8)	(338 7)	(852 5)
Net assets	1,320 6	(576 5)	744 1
Capital and reserves			
Share capital	1,000 0	-	1,000 0
Profit and loss account	320 6	(836 1)	(515 5)
Hedging reserve	-	(118 4)	(118 4)
Infrastructure reserve	-	378 0	378 0
Shareholder's funds	1,320 6	(576 5)	744 1

Severn Trent Water Limited

Notes to the financial statements

Reconciliation of profit for the year ended 31 March 2012

	As previously reported £m	Effect of transition £m	Under FRS 101 £m
Turnover	1,457 5	-	1,457 5
Operating costs before exceptional items	(954 7)	(5 4)	(961 1)
Net exceptional income	10 3	1 3	11 6
Total operating costs	(944 4)	(4 0)	(949 5)
Profit before interest and tax	513 1	(5 1)	508 0
Income from share in group undertakings	3 5	-	3 5
Interest receivable	92 7	11 6	104 3
Interest payable	(334 9)	(3 6)	(338 4)
Losses on financial instruments	-	(70 3)	(70 3)
Profit on ordinary activities before tax	274 4	(67 3)	207 1
Taxation on profit on ordinary activities	(176 0)	167 1	(8 9)
Taxation on exceptional items	98 4	99 8	198 2

Transitional adjustments

Under FRS 101, the company applies the recognition and measurement requirements of EU-adopted IFRS, but makes amendments where necessary in order to comply with the Companies Act 2006 Act and The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410), given that the financial statements that it prepares are Companies Act accounts

The company is included in the consolidated accounts of its ultimate parent company Severn Trent Plc. Severn Trent Plc adopted IFRS for the first time in the year ended 31 March 2006. In accordance with IFRS 1 'First-time adoption of International Financial Reporting Standards', the company has measured its assets and liabilities at the carrying amounts that would be included in the Severn Trent Plc consolidated financial statements

The differences between the amounts previously reported and those under FRS 101 are shown above

The key areas of difference are as follows

Fixed assets

Intangible assets

Under IAS 38 'Intangible Assets', software and development costs, which are capitalised as tangible fixed assets under the previous reporting framework, are classified as intangible assets. This has led to a reclassification of £104.3 million at 31 March 2012

Infrastructure assets

Previously, the company's water and waste water infrastructure assets were accounted for in accordance with the renewals accounting provisions of Financial Reporting Standard 15 'Tangible Fixed Assets'. Such provisions are not present within International Accounting Standard 16 'Property, plant and equipment' (IAS 16)

Under renewals accounting, the water and waste water infrastructure networks are assumed to be single assets. Expenditure on infrastructure assets relating to increases in capacity or enhancements to the networks and on maintaining the operating capability of the networks in accordance with defined standards of service is capitalised. The depreciation charged is the estimated anticipated level of annual expenditure required to maintain the operating capability of the networks. Grants and contributions relating to the maintenance of the operating capability of the infrastructure network are taken into account in determining this charge. Grants and contributions relating to enhancement of the infrastructure network are deducted from the costs of fixed assets

Severn Trent Water Limited

Notes to the financial statements

Under IAS 16 this treatment may not be applied. Significant parts within the infrastructure networks have been identified and useful lives and residual values determined so that each significant part may be depreciated individually.

Infrastructure assets have been valued at the carrying amount at which they have been included in Severn Trent Plc's consolidated financial statements. This increases net assets by £540.0 million as at 31 March 2012 compared with that previously reported. Included in this figure are capitalised borrowing costs of £23.9 million and assets transferred from customers of £131.0 million which have been recognised at fair value under IFRIC 18 'Transfers of assets from customers'. Grants and contributions of £234.5 million relating to the enhancement of the infrastructure network have been credited to deferred income. Those related to maintaining the operating capability of the infrastructure network are recognised in the profit and loss account.

The significant parts recognised within the water and waste water networks have been based upon asset class since no single pipe or section of sewer is significant compared with the total value of the networks. This has led to the identification of 4 significant parts (impounding reservoirs, raw water aqueducts, mains and sewers) which have been assigned zero residual values at the end of their useful lives. The lives allocated to these significant parts range from 80 – 250 years. The depreciation on these assets results in an additional charge of £28.2 million in the 2012 FRS 101 profit and loss account compared with that previously reported.

Under the previous reporting framework, maintenance expenditure was included in the calculation of the infrastructure renewals charge and was smoothed over an Asset Management Period (AMP). Under IAS 16, repairs and maintenance expenditure is charged to the profit and loss account in the period in which it is incurred. This will introduce a level of volatility into the profit and loss account since the level of such expenditure can fluctuate significantly from one reporting period to the next, over a single AMP. The difference in the infrastructure renewals charge previously reported and the repairs and maintenance expenditure for the year results in an additional credit to the profit and loss account of £7.4 million to that previously reported.

Financial instruments

Under FRS 101, the company must apply IAS 39 'Financial Instruments: Recognition and Measurement' (IAS 39).

Investments

Amounts of £65.6 million, which were previously recognised as investments in subsidiary entities, are classified as loans and other receivables under IAS 39 and therefore, have been reclassified as debtors in the balance sheet as at 31 March 2012.

Derivatives

The most significant impact of applying IAS 39 is in relation to derivatives, principally interest rate swaps and cross currency swaps that are held to hedge the company's exposure to changes in interest rates and exchange rates.

Under IAS 39 the fair value of these derivatives must be recognised on the balance sheet, with fair value movements being recognised in the profit and loss account unless cash flow hedge accounting is applied. This has the potential to introduce considerable volatility in the profit and loss account and balance sheet. The net impact of recognising the fair value of derivatives on the balance sheet at 31 March 2012 is to reduce net assets by £145.2 million and reduce the profit for the year by £82.0 million.

Hedge accounting

Where strict criteria are met, IAS 39 permits hedge accounting to be applied to reduce volatility in the profit and loss account and balance sheet. Where debt instruments are designated for fair value hedge accounting, the carrying value of debt is adjusted through profit and loss for changes in value that are attributable to the hedged risk. The change in value offsets the fair value movement on the derivative. In order to apply this treatment, it must be demonstrated that the derivative has been, and will continue to be, an effective hedge of the hedged risk in the underlying debt within the criteria set out in IAS 39. Any hedge ineffectiveness, provided it is within the range deemed acceptable by IAS 39, is recognised immediately within the profit and loss account.

Fair value hedge accounting has been applied for the majority of the company's currency debt instruments, resulting in a fair value adjustment to debt of £66.1 million as at 31 March 2012. A fair value gain on debt of £5.9 million was recognised in the year ended 31 March 2012, offsetting a loss on the hedging instruments of £4.8 million. All designated hedges were effective in the period.

Where hedge accounting is not applied, currency debt has been revalued at the spot rate at the balance sheet date.

Severn Trent Water Limited

Notes to the financial statements

In addition, the company holds a portfolio of forward starting interest rate swaps which are designated as cash flow hedges for future debt instruments expected to be raised in the remainder of AMP 5 to finance the company's capital programme. The fair value of these swaps at 31 March 2012 was £80.4 million. Fair value movements are deferred in equity until they can be recycled through the profit and loss account to offset the future profit and loss effect of changes in hedged risk.

Finance leases

Leases which were previously classified as operating leases under the previous reporting framework have been reclassified as finance leases under the provisions of IAS 17 'Leases'. This has resulted in a reduction in net assets as at 31 March 2012 of £113.2 million.

Retirement benefit obligations

Under FRS 17 'Retirement Benefits' (FRS 17) the company recognised its share of the underlying assets and liabilities of the two defined benefit pensions schemes that are operated by the Severn Trent group.

Under IAS 19 'Employee Benefits' (IAS 19) the sponsoring employer recognises the net defined benefit cost and associated retirement benefit obligation of the pension scheme. The company is the sponsoring employer of the Severn Trent Pension Scheme and the Severn Trent Mirror Image Pension Scheme. As a result the company is required to recognise the net defined benefit cost and associated retirement benefit obligation of both schemes in full. This has resulted in a reduction in net assets of £27.7 million at 31 March 2012 and in profit of £0.2 million for the year ended 31 March 2012.

In 2012 the company made a payment of £98 million to a subsidiary entity, being the net present value of future cash flows to be made into the pension scheme as part of an asset backed funding arrangement, as agreed with the Trustees. Under the previous reporting framework this was treated as a reduction to the retirement benefit obligation. This payment does not reduce the deficit from a Severn Trent Plc group perspective and therefore, is presented as a prepayment within debtors under FRS 101.

In addition, under FRS17 a deferred tax asset of £53.7 million was disclosed as a reduction to the pension deficit on the balance sheet. Deferred tax on pensions is disclosed within the deferred tax provision under IAS 19.

Deferred tax

Under the previous reporting framework, the company had elected to apply discounting to its deferred tax liability. Under IAS 12 'Income Taxes' (IAS 12), discounting of deferred tax balances is not permitted.

The impact of eliminating discounting from the accounting for deferred tax is to reduce the deferred tax charge in the year ended 31 March 2012 by £156.3 million and to increase the deferred tax liability at that date by £210.0 million.

IAS 12 takes a different conceptual approach to deferred tax from that applied by FRS 19 'Deferred Tax' (FRS 19). Under IAS 12 deferred tax must be provided for on all temporary differences between the carrying amount of an asset or liability in the balance sheet and its tax base whereas under FRS 19 deferred tax must be provided for on timing differences between the treatment of items in the tax computation and the profit and loss account. This change in approach results in deferred tax provisions under FRS 101 for items which under FRS 19 would be permanent differences and hence would not be provided for. The impact on the company's FRS 101 financial statements is to decrease the deferred tax charge in the year ended 31 March 2012 by £20.1 million and to increase the deferred tax liability at that date by £190.2 million.

Other FRS 101 adjustments result in an increase in the deferred tax charge of £9.0 million in the year ended 31 March 2012 and a decrease in the deferred tax liability at that date of £7.8 million.

The net impact of the above adjustments and the reclassification of the deferred tax pension asset from the retirement benefit obligation to deferred tax provisions is to increase the deferred tax liability as at 31 March 2012 by £338.7 million. These adjustments change the deferred tax charge of £108.5 million in the year ended 31 March 2012 to a £58.9 million credit.

Regulatory accounts

Regulatory accounts index

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Statement of disclosure of information to auditor

In the case of each of the persons who are directors of the company at the date when this report was approved so far as each of the directors are aware, there is no relevant audit information of which the company's auditor is unaware, and each of the directors has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the company's auditor is aware of that information

Relevant audit information means information needed by the company's auditor in connection with preparing their report. This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006

Water Industry Act 1991

Further to the requirements of company law, the directors are required to prepare financial statements which comply with the requirements of Condition F Instrument of Appointment of the company as a water and sewerage undertaker under the Water Industry Act 1991 and Regulatory Accounting Guidelines issued by the Water Services Regulation Authority. This additionally requires the directors to

- Confirm that, in their opinion, the company has sufficient financial and management resources for the next twelve months,
- Confirm that, in their opinion, the company has sufficient rights and assets which would enable a special administrator to manage the affairs, business and property of the company,
- Report to the Water Services Regulation Authority changes in the company's activities which may be material in relation to the company's ability to finance its regulated activities,
- Undertake transactions entered into by the appointed business, with or for the benefit of associated companies or other businesses or activities of the appointed business, at arm's length, and

e) Keep proper accounting records which comply with Condition F

Diversification and the protection of the core business – Condition F6a

Severn Trent Water hereby advises

a) That in the opinion of the directors, the Appointee will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the Regulated Activity (including the investment programme necessary to fulfil the Appointee's obligations under the Appointment), and

b) That in the opinion of the directors, the Appointee will for at least the next 12 months, have available to it management resources which are sufficient to enable it to carry out those functions

Ring Fencing – Condition K3 1

In accordance with the requirements of the Water Services Regulation Authority, the board confirmed that, as at 31 March 2013, it had available to it sufficient rights and assets, not including financial resources, which would enable a special administrator to manage the affairs, business and property of the company in order that the purposes of a special administration order could be achieved if such an order were made

Tony Wray
Chief Executive
For and on behalf of the board
29 May 2013



Report of the auditor

To the Water Services Regulation Authority and the Directors of Severn Trent Water Limited

Report of the independent auditor to the Water Services Regulation Authority ("WSRA") and Directors of Severn Trent Water Limited

We have audited the Regulatory Accounts of Severn Trent Water Limited for the year ended 31 March 2013 on pages 83 to 101 which comprise

- the regulatory historical cost accounting statements, comprising the regulatory historical cost profit and loss account, the regulatory historical cost balance sheet, the regulatory historical cost statement of total recognised gains and losses and the historical cost reconciliation between statutory and regulatory accounts and the related notes to the historical cost accounting statements including the statement of accounting policies, and
- the regulatory current cost accounting statements for the appointed business, comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes to the current cost financial statements, including the statement of accounting policies

These Regulatory Accounts have been prepared in accordance with the basis of preparation and accounting policies set out in the Statement of Accounting Policies

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

Respective responsibilities of the WSRA, the directors and auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page [x], the directors are responsible for the preparation of the Regulatory Accounts and for their fair presentation in accordance with the basis of preparation and accounting policies. Our responsibility is to audit and express an opinion on the Regulatory Accounts in accordance with International Standards on Auditing (UK and Ireland), except as stated in the 'Scope of the audit of the Regulatory Accounts' below, and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities' issued by the Institute of Chartered Accountants in England and Wales. Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the Regulatory Accounts

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

We have not assessed whether the accounting policies are appropriate to the circumstances of the Company where these are laid down by Condition F. Where Condition F does not give specific guidance on the accounting policies to be followed, our audit includes an assessment of whether the accounting policies adopted in respect of the transactions and balances required to be included in the Regulatory Accounts are consistent with those used in the preparation of the statutory financial statements of the company. Furthermore, as the nature, form and content of Regulatory Accounts are determined by the WSRA, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK & Ireland).

The Company has presented the allocation of operating costs and assets in accordance with the accounting separation policy set out in note 2(y) to the accounts and its Accounting Separation Methodology Statement published on the Company's website in June 2013, (the "Methodology Statement"). We are not required to assess whether the methods of cost allocation set out in the Methodology Statement are appropriate to the circumstances of the Company or whether they meet the requirements of the WSRA, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK & Ireland).

Opinion on Regulatory Accounts

In our opinion, the Regulatory Accounts

- fairly present in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA, in respect of the Accounting Separation Tables the Methodology Statement, and the accounting policies

Report of the auditor

To the Water Services Regulation Authority and the Directors of Severn Trent Water Limited

Opinion on Regulatory Accounts continued

set out on page 89, the state of the Company's affairs at 31 March 2013 on an historical cost and current cost basis, and its historical cost and current cost profit and its current cost cash flow for the year then ended,

- have been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines, the accounting policies and the Methodology statement

Emphasis of matter - Basis of preparation

Without modifying our opinion on the Regulatory Accounts, we draw attention to the fact that the Regulatory Accounts have been prepared in accordance with Condition F of the Appointment and the Regulatory Accounting Guidelines, the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention

The Regulatory Accounts are separate from the statutory financial statements of the Company and have not been prepared under the basis of Financial Reporting Standard 101 Reduced Disclosure Framework ('FRS101') Financial information other than that prepared on the basis of FRS 101 does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in statutory financial statements prepared in accordance with the Companies Act 2006 Furthermore, the regulatory historical cost accounting statements on pages 83 and 84 have been drawn up in accordance with Regulatory Accounting Guideline 3.07, in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly, that the relevant sections of International Accounting Standards 16 and 37 have been disapplied The effect of this departure from FRS 101 and a reconciliation of the balance sheet drawn up on this basis to the balance sheet drawn up in accordance with FRS 101 under the Companies Act 2006 is given on page 85

Opinion on other matters prescribed by Condition F

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

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

Other matters

- The nature, form and content of Regulatory Accounts are determined by the WSRA It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the WSRA's purposes Accordingly, we make no such assessment
- Our opinion on the Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2013 on which we report, which are prepared for a different purpose Our audit report in relation to the statutory financial statements of the Company (our 'statutory audit') was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 Our statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a statutory audit report and for no other purpose In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our statutory audit report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing



Jane Whitlock (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Birmingham, United Kingdom
29 May 2013

Regulatory accounts – historical cost financial statements

Profit and loss account year ended 31 March 2013

	2013				2012			
	Appointed business £m	Non-appointed business £m	Inter segment £m	Total £m	Appointed business £m	Non-appointed business £m	Inter segment £m	Total £m
Turnover	1,492.2	10.4	-	1,502.6	1,438.5	9.0	-	1,447.5
Operating costs	(710.2)	(10.1)	6.3	(714.0)	(668.9)	(9.7)	6.1	(672.5)
Historical cost depreciation	(256.5)	-	-	(256.5)	(248.8)	-	-	(248.8)
Other operating income	11.8	6.3	(6.3)	11.8	4.1	6.1	(6.1)	4.1
Operating profit	537.3	6.6	-	543.9	524.9	5.4	-	530.3
Other income	2.1	1.8	-	3.9	1.9	2.2	-	4.1
Net interest payable	(278.3)	-	-	(278.3)	(245.4)	-	-	(245.4)
Profit on ordinary activities before taxation	261.1	8.4	-	269.5	281.4	7.6	-	289.0
Taxation on profit on ordinary activities								
- Current tax	9.2	(2.2)	-	7.0	(65.6)	(1.9)	-	(67.5)
- Deferred tax	3.0	-	-	3.0	(108.5)	-	-	(108.5)
Taxation	12.2	(2.2)	-	10.0	(174.1)	(1.9)	-	(176.0)
Profit on ordinary activities after taxation	273.3	6.2	-	279.5	107.3	5.7	-	113.0
Dividends	(65.8)	(6.2)	-	(72.0)	(260.3)	(5.7)	-	(266.0)
Retained profit/(loss) for the financial year	207.5	-	-	207.5	(153.0)	-	-	(153.0)

Statement of total recognised gains and losses year ended 31 March 2013

	2013				2012			
	Appointed business £m	Non-appointed business £m	Inter segment £m	Total £m	Appointed business £m	Non-appointed business £m	Inter segment £m	Total £m
Profit for the financial year	273.3	6.2	-	279.5	107.3	5.7	-	113.0
Actuarial gain/(loss)	(47.2)	-	-	(47.2)	(105.7)	-	-	(105.7)
Tax (charge)/credit on actuarial gain/(loss)	11.0	-	-	11.0	28.3	-	-	28.3
Tax on share based payments	0.7	-	-	0.7	-	-	-	-
Adjustment in respect of tax rate change on deferred tax	(2.2)	-	-	(2.2)	(2.9)	-	-	(2.9)
Tax charge on pension contributions	1.3	-	-	1.3	(2.9)	-	-	(2.9)
Total recognised gains and losses for the financial year	236.9	6.2	-	243.1	24.1	5.7	-	29.8

Regulatory accounts – historical cost financial statements

Balance sheet as at 31 March 2013

	2013			2012		
	Appointed business £m	Non-appointed business £m	Total £m	Appointed business £m	Non-appointed business £m	Total £m
Fixed assets						
Tangible assets	6,257.5	-	6,257.5	6,113.4	-	6,113.4
Intangible assets	1.3	-	1.3	-	-	-
Investments - loan to group company	65.6	-	65.6	65.6	-	65.6
Investments - other	347.9	-	347.9	347.9	-	347.9
	6,672.3	-	6,672.3	6,526.9	-	6,526.9
Current assets						
Stock	6.1	-	6.1	6.3	-	6.3
Debtors	427.5	-	427.5	406.4	-	406.4
Short term deposits	326.6	-	326.6	0.1	-	0.1
Cash at bank and in hand	(5.4)	7.4	2.0	0.2	-	0.2
	754.8	7.4	762.2	413.0	-	413.0
Creditors amounts falling due within one year						
Creditors	(391.8)	(7.4)	(399.2)	(392.9)	-	(392.9)
Borrowings	(169.4)	-	(169.4)	(3,534.7)	-	(3,534.7)
Corporation tax payable	20.9	-	20.9	(36.8)	-	(36.8)
Infrastructure renewal accrual	(4.7)	-	(4.7)	(17.2)	-	(17.2)
	(545.0)	(7.4)	(552.4)	(3,981.6)	-	(3,981.6)
Net current liabilities	209.8	-	209.8	(3,568.6)	-	(3,568.6)
Total assets less current liabilities	6,882.1	-	6,882.1	2,958.3	-	2,958.3
Creditors amounts falling due after more than one year						
Borrowings	(4,773.1)	-	(4,773.1)	(1,044.4)	-	(1,044.4)
Other creditors	(1.7)	-	(1.7)	(1.8)	-	(1.8)
	(4,774.8)	-	(4,774.8)	(1,046.2)	-	(1,046.2)
Provisions for liabilities and charges						
- Deferred taxation	(498.5)	-	(498.5)	(504.6)	-	(504.6)
- Other provisions	(5.1)	-	(5.1)	(9.3)	-	(9.3)
Deferred income	(37.6)	-	(37.6)	(37.7)	-	(37.7)
Pension deficit	(199.4)	-	(199.4)	(170.1)	-	(170.1)
Net assets	1,366.7	-	1,366.7	1,190.4	-	1,190.4
Capital and reserves						
Called up share capital	100.0	-	100.0	1,000.0	-	1,000.0
Profit and loss account	1,266.7	-	1,266.7	190.4	-	190.4
Shareholder's funds	1,366.7	-	1,366.7	1,190.4	-	1,190.4

Regulatory accounts – historical cost financial statements

Reconciliation between statutory accounts and historical cost regulatory accounts

	2013 £m
Profit and Loss Account / Income Statement	
Turnover	
Per FRS101 statutory accounts	1,511 0
Renewables Obligation Certificate (ROC) income	(8 4)
Per regulatory accounts	1,502 6
Operating profit	
Per FRS101 statutory accounts	511 5
Non operating income	(3.9)
Historical cost infrastructure assets	0 6
Difference between infrastructure renewals charge and depreciation	11.9
Capitalisation difference - depreciation	24 4
Impairment of trade debtors	(1 5)
Pensions	1 0
Other	(0 1)
Per regulatory accounts	543 9
Balance Sheet	
Tangible assets	
Net book value per FRS101 statutory accounts	6,738 0
Infrastructure renewals accrual	(11 7)
Cumulative impact of transferring assets from customers	(155 1)
Grants and contributions deducted against fixed assets	(231 7)
Recognition of Intangible assets	89 0
Transitional fair value adjustment	(378 0)
Capitalised borrowing costs	(33.3)
Infrastructure renewals expenditure	989 1
Infrastructure renewals charge	(962 7)
Infrastructure depreciation	211 1
Other	2 8
Per regulatory accounts	6,257.5

Regulatory accounts – current cost financial statements

Profit and loss account: appointed business year ended 31 March 2013

	Notes	2013			2012		
		Water £m	Sewerage £m	Total £m	Water £m	Sewerage £m	Total £m
Turnover	4a						
Unmeasured - household		354 0	373 3	727 3	342 6	362 2	704 8
Unmeasured - non-household		3 4	9 2	12 6	3 4	9 2	12 6
Measured - household		186 5	164 0	350 5	176 3	160 7	337 0
Measured - non-household		127 2	175 5	302 7	132 0	159 0	291 0
Trade effluent		-	12 3	12 3	-	10 7	10 7
Bulk supplies/intercompany payments		5 0	-	5 0	4 8	-	4 8
Other third party services		38 6	38 8	77 4	35 5	38 3	73 8
Other sources		1 8	2 6	4 4	1 1	2 7	3 8
Total Turnover		716 5	775 7	1,492 2	695 7	742 8	1,438 5
Current operating cost - wholesale	4c	(456 0)	(443 6)	(899.6)	(423 8)	(419 3)	(843 1)
Current operating cost - retail	4c	(58 7)	(64 8)	(123 5)	(60 7)	(65 8)	(126 5)
Other operating income		4 9	5 5	10 4	1 9	2 0	3 9
Working capital adjustment		(3 0)	(3 4)	(6 4)	(1 5)	(1 7)	(3 2)
Current cost operating profit		203 7	269 4	473 1	211 6	258 0	469 6
Other income				2 1			1 9
Net interest payable				(278 3)			(245 5)
Financing adjustment				113 8			114 4
Current cost profit before taxation				310 7			340 4
Taxation on profit on ordinary activities							
- Current tax				9 2			(65 6)
- Deferred tax				3 0			(108 5)
Taxation				12 2			(174 1)
Current cost profit attributable to shareholders after taxation				322 9			166 3
Dividend				(65 8)			(260 3)
Current cost retained profit/(loss)				257 1			(94 0)
Net revenue movement out of tariff basket		0 2	(0.4)	(0 2)	(0 2)	1 4	1 2
Back-billing amount identified		0 4	1 2	1 6	0 4	2 3	2 7

Statement of total recognised gains and losses: appointed business year ended 31 March 2013

	2013 £m	2012 £m
Profit for the financial year	322 9	166 3
Actuational gain/(loss)	(47 2)	(105 7)
Tax on actuational gain/loss	11 0	28 3
Tax on share based payments	0 7	-
Adjustment in respect of tax rate change on deferred tax	(2 2)	(2 9)
Tax charge on pension contributions	1 3	(2 9)
Total recognised gains and losses for the financial year	286 5	83 1

Regulatory accounts – current cost financial statements

Balance sheet: appointed business as at 31 March 2013

	Notes	2013 £m	2012 £m
Fixed assets			
Investments		413 5	413 5
Tangible assets	5	72,364 3	69,948 4
Intangible assets		1 3	-
Third party contributions since 1989/90		(22,204 8)	(21,454 1)
		50,574 3	48,907 8
Working capital	7	224 5	195 6
Short term deposits		321 2	0 3
Infrastructure renewals accrual		(4 7)	(17 2)
Working capital		51,115 3	49,086 5
Non-operating assets and liabilities			
Borrowings		(169 4)	(3,534 7)
Non trade debtors		-	0 6
Non trade creditors due within one year		(182 7)	(176 6)
Corporation tax payable		20 9	(36 8)
Total non-operating assets and liabilities		(331 2)	(3,747 5)
Creditors amounts falling due after more than one year			
Borrowings		(4,773 1)	(1,044 4)
Other creditors		(1 8)	(1 7)
		(4,774 9)	(1,046 1)
Provision for liabilities and charges			
Deferred taxation		(498 5)	(504 4)
Other provisions		(5 1)	(9 4)
Pension deficit		(199 4)	(170 1)
Net provisions		(703 0)	(683 9)
Net assets		45,306 2	43,609 0
Capital and reserves			
Called up share capital		100 0	1,000 0
Profit and loss account		1,004.5	(118 4)
Current cost reserve		44,201 7	42,727 4
		45,306 2	43,609 0

Regulatory accounts – current cost financial statements

Cash flow statement year ended 31 March 2013

	Notes	2013			2012		
		Appointed business £m	Non-appointed business £m	Total £m	Appointed business £m	Non-appointed business £m	Total £m
Net cash inflow from operating activities	8	888 6	15 8	904 4	859 5	7 6	867 1
Returns on investments and servicing of finance		(228 6)	-	(228 6)	(289 1)	-	(289 1)
Taxation paid		(51 3)	(2 2)	(53 5)	(65 9)	(1 9)	(67 8)
Capital expenditure							
Gross cost of purchase of tangible fixed assets		(443 2)	-	(443 2)	(375 9)	-	(375 9)
Grants and contributions received		36 2	-	36 2	24 3	-	24 3
Investment in subsidiaries		-	-	-	(177 8)	-	(177 8)
Infrastructure renewals expenditure		(147 7)	-	(147 7)	(128 9)	-	(128 9)
Proceeds on disposal of fixed assets		15 6	-	15 6	8 8	-	8 8
Net cash outflow from investing activities		(539 1)	-	(539.1)	(649 5)	-	(649 5)
Equity dividends paid		(65 8)	(6 2)	(72.0)	(260 3)	(5 7)	(266 0)
Net cash outflow before management of liquid resources and financing		3 8	7 4	11 2	(405 3)	-	(405 3)
Management of liquid resources		(326 5)	-	(326 5)	3 9	-	3 9
Net cash flow before financing		(322 7)	7 4	(315 3)	(401 4)	-	(401 4)
Net cash inflow from financing		317 1	-	317 1	395 5	-	395 5
Net (decrease)/increase in cash		(5 6)	7 4	1.8	(5 9)	-	(5 9)

Notes to the regulatory accounts

Year ended 31 March 2013

1 Regulatory reporting

The regulatory accounts as reported on pages 83 to 102 should be read in conjunction with the operating and financial review on pages 3 to 24 for further understanding of the performance of the business

In particular, attention is drawn to pages 26 and 27 of the Directors' report which sets out the link between Directors' pay and standards of performance

2 Accounting policies for historical cost and current cost financial statements

a) Basis of preparation

The regulatory financial statements are separate from the statutory financial statements of the company. They have been prepared on a going concern basis (see Directors' Report on page 29)

The regulatory financial statements have been prepared in accordance with Condition F of the Instruments of Appointment of the Water and Sewerage Undertakers and the Regulatory Accounting Guidelines as issued by the WSRA

Where the Regulatory Accounting Guidelines do not specifically address an accounting issue, then they require UK GAAP to be followed. IN13 does not permit the regulatory accounts to be based on the new FRS100 accounting framework issued by the Financial Reporting Council and therefore UK GAAP prior to FRS 100 has been applied in preparing these regulatory accounts. Financial information other than that prepared wholly on the basis of UK GAAP may not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 2006

In previous years the regulatory accounts have been based on the consolidated statutory accounts of Severn Trent Water Limited and its subsidiaries. Following the adoption of FSR 101 the company no longer prepares consolidated statutory accounts. These regulatory accounts have therefore been prepared for the company as a stand alone entity and do not include the results or net assets of its subsidiaries

b) Turnover

Turnover represents income receivable from regulated water activities, excluding value added tax

Turnover includes an estimation of the amount of mains water and waste water charges unbilled at the year end. The accrual is estimated using a defined methodology based upon a measure of unbilled water consumed by tariff, which is calculated from historical billing information. There has been no changes in methodology in the year

Turnover is not recognised in respect of unoccupied properties. Properties are classified as unoccupied when

- The company is informed that a customer has left a property and it is not expected to be reoccupied immediately,
- New properties are connected but are not occupied,

- Properties are disconnected following a customer's request, or
- The identity of the customer is unknown

The following activities are undertaken to ensure properties classified as unoccupied are in fact not occupied

- Where the company is informed that the customer has left a property and the property is expected to be occupied by someone else, a welcome letter is sent to the property encouraging the occupier to contact the company
- If there is no response to the welcome letter within two months a void letter is sent to the property explaining that we have classified the property as empty and may schedule the property for disconnection
- Meter readings are taken for metered unoccupied properties, where consumption is recorded, a letter is sent to the property
- Inspections are organised throughout the year by geographical area

c) Operating costs

Income relating to electricity generation (Renewable Obligation Certificate income) is deducted from operating costs

d) Bad and doubtful debts

Provisions are charged to operating costs to reflect the company's assessment of the risk of non recoverability of debtors. Provisions are calculated based on the age of the debtor balance and the company's previous collection experience for balances of that age. The bad debt provisioning rates are updated annually to reflect the latest collection performance data from the company's billing system

The company's bad debt write off policy has remained unchanged and has been consistently applied in the current and the prior years

The policy specifies that debt can only be written off if the following criteria are met

- The debt is actually a legitimate charge against the debtor. If it is considered that part or all of the debt is incorrect or unsubstantiated, then such elements are dealt with through the issue of a credit note,

2 Accounting policies continued

- All available economic options for collection of the debt have been pursued or that debt recovery procedures have proved to be abortive or uneconomic to continue. Uneconomic circumstances are those where, following the application of debt recovery procedures
 - the customer could not be traced without incurring an unreasonable degree of expenditure,
 - the company has an insufficiently sound case to justify further expenditure on debt recovery procedures, or
 - the likelihood of recovering the debt is so small in particular circumstances that further expenses on debt recovery cannot be justified
- The customer does not have any assets or has insufficient assets on which to levy execution,
- The customer is bankrupt or has gone into liquidation and no dividend has been, or is likely to be, received,
- The customer has died without leaving an estate or has left an insufficient estate on which to levy execution, and
- The company has been unable to prove its case in court

The above write-off rules apply primarily to customers to whom the company has ceased to provide a service. Only in exceptional circumstances is debt relating to continuing customers considered for write off.

e) Research and development

Expenditure on research and development projects is charged to the profit and loss account in the year in which it is incurred.

f) Leased assets

Where the company obtains assets under leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases), the assets are accounted for as if they had been purchased and the fair value of the minimum lease payments is shown as an obligation to the lessor. Lease payments are treated as consisting of a capital element and a finance charge, the capital element reducing the obligation to the lessor and the finance charge being written off to the profit and loss account over the period of the lease in proportion to the capital amount outstanding. Depreciation is charged over the shorter of the estimated useful life and the lease period.

Where the company obtains assets under leasing arrangements where substantially all the risks and rewards of ownership remain with the lessor, these are classified as operating leases. Rental costs arising under operating leases are expensed on a straight line basis over the term of the lease.

Where the company transfers substantially all the risks and rewards of ownership of an asset to a lessee (finance lease), the assets are accounted for as if they had been sold, and

the net investment in the lease is shown as a receivable due from the lessee. Over the lease term, rentals are apportioned between a reduction in the net investment in the lease and finance lease income, such that finance lease income produces a constant rate of return on the net cash investment in the lease. Finance lease income is included within interest receivable and similar income.

g) Goodwill

Goodwill represents the excess of the fair value of purchase consideration over the fair value of the net assets acquired. Fair value adjustments based on provisional estimates are amended within one year of the acquisition, if required, with a corresponding adjustment to goodwill.

Goodwill is amortised over its estimated useful life which is 5 years. Provision for any impairment is made as described below.

h) Impairment of goodwill and fixed assets

Impairments of goodwill and fixed assets are calculated as the difference between the carrying value of the net assets of income generating units, including where appropriate investments and goodwill, and their recoverable amounts. Recoverable amount is defined as the higher of net realisable value or estimated value in use at the date the impairment review is undertaken.

Net realisable value represents the net amount that can be generated through sale of assets. Value in use represents the present value of expected future cash flows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit.

Impairment reviews are carried out if there is some indication that impairment may have occurred, or, where otherwise required, to ensure that goodwill and fixed assets are not carried above their estimated recoverable amounts.

Impairments are recognised in the profit and loss account and, where material, are disclosed as exceptional.

i) Investments

Investments held as fixed assets are stated at cost less amounts written off.

j) Stock

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

k) Provisions

Provisions are recognised where

- a) There is a present obligation as a result of a past event,
- b) It is probable that there will be an outflow of economic benefits to settle this obligation, and
- c) A reliable estimate of this amount can be made.

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

2 Accounting policies continued

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

l) Pension costs

The company operates both defined benefit and defined contribution schemes

For defined benefit schemes the amounts charged to operating profit are the current and past service costs and gains and losses on settlements and curtailments. They are included as part of staff costs. Past service costs are recognised immediately in the profit and loss account if the benefits have vested. If the benefits have not vested immediately the costs are recognised over the period until vesting occurs. The interest costs and the expected return on assets is shown as a net amount of other finance costs or credits adjacent to interest. Actuarial gains and losses are recognised immediately in the statement of total recognised gains and losses.

Defined benefit schemes are funded, with the assets of the scheme held separately from those of the company, in separate trustee administered funds. Pension scheme assets are measured at bid price and liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the scheme liabilities. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date. The resulting defined benefit asset or liability, net of the related deferred tax, is presented separately.

Costs of defined contribution pension schemes are charged to the profit and loss account when they fall due.

m) Current and deferred taxation

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

Deferred taxation is provided in respect of timing differences between the treatment of certain items for taxation and accounting purposes only to the extent that the company has an obligation to pay more tax in the future or a right to pay less tax in the future. Deferred tax is measured on a non-discounted basis using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

n) Derivatives and other financial instruments

Debt instruments

The costs of debt instruments are charged to the profit and loss account over the term of the debt at a constant rate on the carrying amount. Such costs include the cost of issue and any discount to face value arising on issue, or any premium arising on maturity.

Derivative financial instruments

Financial instruments, in particular, interest rate swaps and currency swaps, are used to manage the financial risks arising from the business activities of the company and the financing of those activities.

Energy swaps are used to manage the risks of future fluctuations in electricity prices. There is no trading activity in financial instruments.

Financial instruments are accounted for as follows:

Interest rate swaps are used to hedge the company's exposure to movements in interest rates. The interest payable or receivable on such swaps is accrued in the same way as interest arising on deposits or borrowings. Interest rate swaps are not revalued to fair value.

Currency swaps are used to hedge the company's exposure to movements in foreign exchange rates. The interest payable or receivable on such swaps is accrued in the same way as interest arising on deposits or borrowings. Currency swaps are not revalued to fair value but are recognised in the balance sheet at the difference between the swap rate and the spot rate at the balance sheet date and offset against the associated hedged borrowings.

Energy swaps are not revalued to fair value.

o) Share based payments

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

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

p) Foreign currency

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

The following policies apply to the historical cost financial statements only

q) Basis of preparation

The historical cost financial statements have been prepared under the historical cost convention.

r) Tangible fixed assets and depreciation

Tangible fixed assets comprise

Infrastructure assets

Infrastructure assets comprise a network of systems being mains and sewers, impounding and pumped raw water storage reservoirs, dams, and sludge pipelines.

2 Accounting policies continued

Expenditure on infrastructure assets relating to increases in capacity or enhancements of the network and on maintaining the operating capability of the network in accordance with the defined standards of service is treated as an addition and included at cost after deducting grants and contributions (see note 2t)

The depreciation charged for infrastructure assets is the estimated, anticipated level of annual expenditure required to maintain the operating capability of the network less the estimated, anticipated level of relevant annual grants and contributions, calculated over a medium to long period (being 15 years) In accordance with RAG 105 the difference between the infrastructure renewals charge and infrastructure renewals expenditure is held as an accrual or prepayment on the balance sheet This is a departure from the provisions of FRS 15, which requires the infrastructure renewals charge to be recorded as a depreciation charge and deducted from the carrying amount of the asset, and FRS 12 which does not allow provisions for future maintenance

Other assets

Other assets are included at cost less accumulated depreciation

Cost includes all costs which are directly attributable to bringing the asset into working condition for its intended use Directly attributable costs on self constructed assets include an element of the 'overhead burden', which is the cost of overheads which would not have been incurred in the absence of capital works Directly attributable costs on self constructed assets are capitalised up to the point where the asset is capable of operating in the manner intended by management

Finance costs are not capitalised

Freehold land is not depreciated Assets in the course of construction are not depreciated until commissioned Other assets are depreciated on a straight line basis over their estimated economic lives, which are principally as follows

	Years
Buildings	30 - 80
Fixed plant and equipment	20 - 40
Vehicles, mobile plant and computers	2 - 15

s) Grants and contributions

Grants and contributions received in respect of non infrastructure assets are treated as deferred income and are recognised in the profit and loss account over the useful economic life of those assets

In accordance with industry practice, grants and contributions relating to infrastructure assets have been deducted from the cost of fixed assets

Those grants and contributions relating to the maintenance of the operating capability of the infrastructure network are taken into account in determining the depreciation charged for infrastructure assets

The following policies apply to the current cost financial statements only

t) Basis of preparation

These accounts have been prepared for the Appointed Business in accordance with guidance issue by the WSRAs for modified real term financial statements suitable for regulation in the water industry They measure profitability on the basis of real financial capital maintenance, in the context of assets which are valued at their current cost value to the business, with the exception of specialised operational and infrastructure assets

The accounting policies used are the same as those applied in the historical cost accounts except where set out below

u) Tangible fixed assets

Assets in operational use are valued at the replacement cost of their operating capability To the extent that the regulatory regime does not allow such assets to earn a return high enough to justify that value, this represents a modification of the value to the business principle Also, no provision is made for the possible funding of future replacements of assets by contributions from third parties and, to the extent that some of the tangible fixed assets would on replacement be so funded, replacement cost again differs from value to the business Redundant assets are valued at their recoverable amounts

An Asset Management Plan (AMP) survey of existing assets as at 31 March 2008 was undertaken during 2008/09 and the adjustments to asset values as a result of that exercise were included within tangible fixed assets In the intervening years, between AMP surveys, values are restated to take account of changes in the general level of inflation, as measured by changes in Retail Price Index (RPI), and any other significant changes in asset records identified during the year

i) Non infrastructure assets

Specialised operational assets

The gross replacement cost of specialised operational assets has been derived using the latest cost information provided by the AMP

The unamortised portion of third party contributions received is deducted in arriving at net operating assets, as described in note 1t)

Non-specialised operational assets

Non-specialised operational assets are valued on the basis of open market value for existing use at 31 March 1991 and have been expressed in current terms by adjusting for movements in property values

ii) Infrastructure assets

Mains, sewers, impounding and pumped raw water storage reservoirs, dams and sludge pipelines are valued at replacement cost, determined principally on the basis of unit cost data provided by the AMP

iii) Other assets

All other assets are valued on the basis of data provided by the AMP

2 Accounting policies continued

iv) Surplus land

Surplus land was valued at the current market value for the purposes of the AMP. Any proceeds on disposal to be passed onto customers will be taken into account, in accordance with the requirements contained in Condition B of the Instruments of Appointment as Water and Sewerage Undertakers.

v) Grants and other third party contributions

Grants, infrastructure and other third party contributions received since 31 March 1990 are carried forward to the extent that any balance has not been credited to revenue. The balance carried forward is restated for the change in RPI for the year and treated as a reduction to fixed assets.

w) Real financial capital maintenance adjustments

These adjustments are made to historical cost operating profit in order to arrive at profit after the maintenance of financial capital in real terms.

Working capital adjustment – this is calculated by applying the change in RPI over the year to the opening total of trade debtors and stock, less trade creditors.

Financing adjustment – this is calculated by applying the change in RPI over the year to the opening balance of net finance, which comprises all assets and liabilities in the

balance sheet apart from those included in working capital and excluding fixed assets, deferred taxation provision, index linked debt and dividends payable.

x) Transferred assets

Assets transferred to the company include assets transferred at 1 October 2011 under the Private Drains and Sewers Transfer Regulations (June 2011). These are included in fixed assets at their Modern Equivalent Asset value with a corresponding credit to third party contributions.

y) Accounting separation

The tables presenting the analysis of operating costs and fixed assets (the 'accounting separation' tables, as described in note 4 and 5) have been prepared in accordance with our Accounting Separation Methodology Statement which can be found at www.severntrentwater.co.uk. The methodology statement explains the bases for allocations of costs and assets and has been updated for changes to the requirements in the year. There have otherwise been no major changes. Wherever possible, direct costs and assets have been directly attributed to business units. Where this is not possible, appropriate cost allocations have been applied as described in the methodology.

3 Directors' Remuneration

Information regarding Directors' Remuneration can be found on pages 57 to 70 of the Severn Trent Plc Annual Report and Accounts 2013.

4 Analysis of current cost turnover and operating costs

a) Reconciliation of current cost turnover to actual outturn per Final Determination (FD)

	2013
	£m
Final Determination (appointed only)	1,390.5
Impact of higher/(lower) inflation	87.1
Final Determination adjusted for inflation movement	1,477.6
Optants	1.3
New Properties	(7.2)
Demolitions	(1.3)
Consumption changes - commercial	7.7
Consumption changes - domestic	20.2
	1,498.3
Other	(6.1)
Actual outturn (appointed only)	1,492.2

Actual income for the year ended 31 March 2013 is £101.7m more than allowed for in the final determination. Of this, £87.1m is driven by higher RPI. Higher consumption accounts for £27.9m. The remaining £13.3m is accounted for by a combination of optants, new properties, demolitions and other.

4 Analysis of current cost turnover and operating costs

b) Reconciliation of amounts billed and amounts recorded as historical cost turnover

	2013
	£m
Billed	1,490.8
Movement in accrual	11.8
Total turnover (appointed and non-appointed)	1,502.6

c) Analysis of operating costs

2013	Water				
	Resources £m	Raw water distribution £m	Treatment £m	Treated distribution £m	Water total £m
Operating expenditure					
Power	7.2	1.9	22.3	6.9	38.3
Income treated as negative expenditure	(0.3)	-	-	-	(0.3)
Service charges	10.9	-	0.3	-	11.2
Bulk supply imports	7.0	-	4.3	-	11.3
Other operating expenditure	10.0	1.6	47.6	85.6	144.8
Local authority rates	4.7	1.5	19.5	17.0	42.7
Exceptional items	-	-	-	-	-
Total operating expenditure excluding third party services	39.5	5.0	94.0	109.5	248.0
Capital maintenance					
Infrastructure renewals charge	1.6	4.7	-	80.1	86.4
Current cost depreciation	8.9	4.6	48.9	53.8	116.2
Recharges to other business units	-	-	-	-	-
Recharges from other business units	-	-	-	-	-
Amortisation of deferred credits	(0.1)	(0.1)	(1.0)	(0.6)	(1.8)
Amortisation of intangible assets	-	-	-	-	-
Total capital maintenance excluding third party services	10.4	9.2	47.9	133.3	200.8
Third party services					
Operating expenditure	3.7	-	1.0	1.0	5.7
Infrastructure renewals charge	-	-	-	-	-
Current cost depreciation	0.2	-	1.3	-	1.5
Total operating costs	53.8	14.2	144.2	243.8	456.0

4 Analysis of current cost turnover and operating costs

c) Analysis of operating costs continued

2013	Sewerage				
	Sewage collection £m	Sewage treatment £m	Sludge treatment £m	Sludge disposal £m	Sewerage total £m
Operating expenditure					
Power	8.8	26.5	4.7	-	40.0
Income treated as negative expenditure	-	(10.7)	(10.7)	-	(21.4)
Service charges	3.5	5.5	-	-	9.0
Other operating expenditure	45.4	68.1	36.3	9.0	158.8
Local authority rates	0.2	24.3	3.6	-	28.1
Exceptional items	-	-	-	-	-
Total operating expenditure excluding third party services	57.9	113.7	33.9	9.0	214.5
Capital maintenance					
Infrastructure renewals charge	48.8	-	-	-	48.8
Current cost depreciation	34.7	117.8	27.1	0.5	180.1
Recharges to other business units	-	-	-	-	-
Recharges from other business units	-	-	-	-	-
Amortisation of deferred credits	(1.4)	(0.2)	-	-	(1.6)
Amortisation of intangible assets	-	-	-	-	-
Total capital maintenance excluding third party services	82.1	117.6	27.1	0.5	227.3
Third party services					
Operating expenditure	-	-	1.8	-	1.8
Infrastructure renewals charge	-	-	-	-	-
Current cost depreciation	-	-	-	-	-
Total operating costs	140.0	231.3	62.8	9.5	443.6

2013	Retail		
	Household £m	Non- household £m	Retail total £m
Operating expenditure			
Customer services	31.2	2.2	33.4
Debt management	8.3	1.5	9.8
Doubtful debts	29.7	3.6	33.3
Meter reading	5.2	0.8	6.0
Services to developers	-	0.2	0.2
Other operating expenditure	18.4	3.6	22.0
Local authority rates	0.3	-	0.3
Exceptional items	-	-	-
Total operating expenditure excluding third party services	93.1	11.9	105.0
Third party services operating expenditure	-	-	-
Total operating expenditure	93.1	11.9	105.0
Capital maintenance			
Current cost depreciation	17.0	1.5	18.5
Amortisation of deferred credits	-	-	-
Amortisation of intangible assets	-	-	-
Total capital maintenance	17.0	1.5	18.5
Total operating costs	110.1	13.4	123.5
Debt written off	18.7	4.8	23.5

5 Analysis of tangible fixed assets by asset type within service

	Water				
	Resources £m	Raw water distribution £m	Treatment £m	Treated distribution £m	£m
Non-Infrastructure assets					
Gross replacement cost					
At 1 April 2012	404.3	118.3	1,630.8	1,516.5	3,669.9
Reclassification adjustment	-	0.6	8.5	265.8	274.9
RPI adjustment	13.6	4.0	51.6	56.6	125.8
Disposals	(0.7)	(0.1)	(7.5)	(8.8)	(17.1)
Additions	1.8	0.1	63.5	63.9	129.3
At 31 March 2013	419.0	122.9	1,746.9	1,894.0	4,182.8
Depreciation					
At 1 April 2012	268.7	66.6	915.7	935.9	2,186.9
Reclassification adjustment	(0.2)	0.4	4.1	164.5	168.8
RPI adjustment	9.2	2.3	31.3	37.5	80.3
Disposals	(0.4)	(0.1)	(6.9)	(7.6)	(15.0)
Charge for the year	9.1	4.6	50.2	53.8	117.7
At 31 March 2013	286.4	73.8	994.4	1,184.1	2,538.7
Net book value					
At 31 March 2013	132.6	49.1	752.5	709.9	1,644.1
At 1 April 2012	135.6	51.7	715.1	580.6	1,483.0
Infrastructure assets					
Gross replacement cost					
At 1 April 2012	1,025.3	1,333.6	3.3	11,761.3	14,123.5
RPI adjustment	33.6	43.7	0.4	389.1	466.8
Additions	1.2	1.8	-	47.7	50.7
At 31 March 2013	1,060.1	1,379.1	3.7	12,198.1	14,641.0

5 Analysis of tangible fixed assets by asset type within service continued

	Sewerage				
	Sewage collection £m	Sewage treatment £m	Sludge treatment £m	Sludge disposal £m	£m
Non-Infrastructure assets					
Gross replacement cost					
At 1 April 2012	924 0	3,901 0	672 9	6 4	5,504 3
Reclassification adjustment	(19 4)	(16 4)	(18 0)	(0 8)	(54 6)
RPI adjustment	29 7	119 0	25 6	0 2	174 5
Disposals	(2 5)	(11 9)	(2 0)	(0 2)	(16 6)
Additions	31 8	159 9	26 5	-	218 2
At 31 March 2013	963 6	4,151 6	705 0	5 6	5,825.8
Depreciation					
At 1 April 2012	522 5	2,037 3	384 2	3 7	2,947 7
Reclassification adjustment	(7 3)	(6 1)	(6 0)	(0 1)	(19.5)
RPI adjustment	18 1	67 6	15 0	0 1	100 8
Disposals	(2 1)	(10 3)	(1 8)	(0 2)	(14.4)
Charge for the year	34 7	117 8	27 1	0 5	180 1
At 31 March 2013	565 9	2,206 3	418.5	4 0	3,194 7
Net book value					
At 31 March 2013	397 7	1,945 3	286.5	1 6	2,631 1
At 1 April 2012	401 5	1,863 7	288 7	2 7	2,556 6
Infrastructure assets					
Gross replacement cost					
At 1 April 2012	51,597 3	8 5	-	-	51,605.8
RPI adjustment	1,693 4	0 1	-	-	1,693 5
Disposals	(0 1)	-	-	-	(0 1)
Additions	51 4	3 0	-	-	54 4
At 31 March 2013	53,342 0	11 6	-	-	53,353 6

5 Analysis of tangible fixed assets by asset type within service continued

	Retail		
	Household £m	Non- household £m	Total £m
Non-Infrastructure assets			
Gross replacement cost			
At 1 April 2012	448 0	51 1	499 1
Reclassification adjustment	(192 9)	(27 4)	(220 3)
RPI adjustment	8 2	0 8	9 0
Disposals	(2 7)	(0 3)	(3 0)
Additions	2 1	0 2	2 3
At 31 March 2013	262 7	24 4	287 1
Depreciation			
At 1 April 2012	287 2	32 4	319 6
Reclassification adjustment	(130 9)	(18 4)	(149 3)
RPI adjustment	5 6	0 5	6 1
Disposals	(2 1)	(0 2)	(2 3)
Charge for the year	17 0	1 5	18 5
At 31 March 2013	176 8	15 8	192 6
Net book value			
At 31 March 2013	85 9	8 6	94 5
At 1 April 2012	160 8	18 7	179 5

6 Analysis of capital expenditure, grants and land sales

	2013			2012		
	Gross £m	Grants & contributions £m	Net £m	Gross £m	Grants & contributions £m	Net £m
Capital expenditure - water						
Base						
Infrastructure renewals expenditure (IRE)	105.4	(7.5)	97.9	91.0	(0.1)	90.9
Maintenance non-infrastructure (MNI)	98.3	(3.3)	95.0	69.2	(2.0)	67.2
Enhancements						
Infrastructure enhancements	50.7	(15.7)	35.0	44.8	(12.7)	32.1
Non-infrastructure enhancements	32.3	(0.4)	31.9	31.3	(0.6)	30.7
Total capital expenditure - water	286.7	(26.9)	259.8	236.3	(15.4)	220.9
Grants and contributions - water						
Developer contributions		(11.0)			(8.9)	
Infrastructure charge receipts - new connections		(6.0)			(4.4)	
Other contributions		(9.9)			(2.1)	
Total grants and contributions - water		(26.9)			(15.4)	
Capital expenditure - sewerage						
Base						
Infrastructure renewals expenditure (IRE)	51.1	(1.3)	49.8	39.9	(1.9)	38.0
Maintenance non-infrastructure (MNI)	151.6	(0.1)	151.5	146.2	-	146.2
Enhancements						
Infrastructure enhancements	34.9	(5.9)	29.0	25.9	(5.0)	20.9
Non-infrastructure enhancements	64.2	(2.2)	62.0	50.5	(2.6)	47.9
Large projects capex						
Infrastructure enhancements	-	-	-	-	-	-
Non-infrastructure enhancements	-	-	-	-	-	-
Total capital expenditure - sewerage	301.8	(9.5)	292.3	262.5	(9.5)	253.0
Grants and contributions - sewerage						
Developer contributions		(1.7)			(2.5)	
Infrastructure charge receipts - new connections		(6.4)			(5.1)	
Other contributions		(1.4)			(1.9)	
Total grants and contributions - sewerage		(9.5)			(9.5)	
Total capital expenditure - water and sewerage	588.5	(36.4)	552.1	498.8	(24.9)	473.9
Land sales - Proceeds from disposals of protected land			15.6			8.8

7 Working capital

	2013 £m	2012 £m
Stock	6 1	6 4
Trade debtors		
Measured household	47 7	43 3
Unmeasured household	78 5	69 3
Measured non-household	21 7	25 7
Unmeasured non-household	0 5	0 8
Other	2 7	2 6
Measured income accrual	165 8	155 6
Prepayments and other debtors	166 0	165 1
Trade creditors	(15 1)	(14 8)
Deferred income - customer advance receipts	(130 2)	(132 9)
Capital creditors and accruals	(33 7)	(36 1)
Accruals and other creditors	(85 5)	(89 4)
Working capital	224 5	195 6
Total revenue outstanding - household	219 6	195 7
- non-household	29.3	33 6

Total gross debt outstanding is £248.9 million (2012 £229.3 million) which represents an increase of £19.6m (8.5%). The increase has been largely driven by a combination of price increase and by timing of bad debt write offs

The company's overall cash collection performance has remained consistent with prior years

8 Reconciliation of appointed business current cost operating profit to net cash inflow from operating activities

	2013 £m	2012 £m
Current cost operating profit	473 1	469 6
Working capital adjustment	6 4	3 2
Movement in working capital	(30 7)	25 8
Receipts from other income	2 1	1 9
Current cost depreciation after amortisation of deferred income	312.9	301 0
Current cost profit on disposal of tangible fixed assets	(10 4)	(3 9)
Infrastructure renewals charge	135 2	127 2
Other non-cash profit and loss items	-	(65 3)
Net cash inflow from operating activities	888.6	859 5

The 2012 other non-cash profit and loss items consist primarily of £51.8 million excess of pension contributions paid and curtailment gain over pension current service charge

9 Analysis of net debt

	Fixed interest rate £m	Floating interest rate £m	Index linked £m	Total £m
Bank Loans	150 0	300 0	267 7	717 7
Loans due from parent and fellow subsidiary undertakings	-	(121 2)	-	(121 2)
Loans due to parent and fellow subsidiary undertakings	2,616 5	168 1	1,028 3	3,812 9
Finance Lease receivables	(101 8)	-	-	(101 8)
Finance Lease payables	415 0	115 7	-	530 7
Total net borrowings	3,079 7	462 6	1,296 0	4,838 3
Impact of interest rate swaps entered into by the company	139 9	(139 9)	-	-
Total borrowings	3,219 6	322 7	1,296 0	4,838 3
Total borrowings				4,838.3
Overdraft				5 4
Short term deposits				(326 6)
Net Debt				4,517.1
Regulatory capital value				7,364 2
Gearing				61 3%
Full year equivalent nominal interest cost	175 6	4 0	69 8	249 4
Full year equivalent cash interest payment	175 6	4 0	26 2	205 8
Indicative interest rates				
Indicative weighted average nominal interest rate	5 5%	1 2%	5 4%	5 2%
Indicative weighted average cash interest rate	5 5%	1 2%	2 0%	4 3%
Weighted average years to maturity	12 0	3 7	31 8	16 5

Supplementary Regulatory Accounting Disclosures – unaudited

Year ended 31 March 2013

Information in respect of transactions during the year with any other business or activity of the appointee or any associated company

a) Borrowings or sums lent

Sums borrowed and repaid by the appointee during the year from associated companies were

		Principal amounts £m	Repayment dates	Interest rates %
East Worcester Water Limited	Borrowed	11 0	July 2012	3 Months LIBID
Severn Trent Plc	Borrowed	401 5	April 2012 to March 2013	LIBOR + 0 825%
Severn Trent Plc	Repaid	417 0	April 2012 to March 2013	LIBOR + 0 825%
Severn Trent Reservoirs Limited	Borrowed	0 3	October 2012	3 Months LIBID
Severn Trent Leasing Limited	Repaid	0 8	January 2013	4 75%
Severn Trent Leasing Limited	Borrowed	8 2	March 2013	4 75%
Severn Trent Utilities Finance	Repaid	0 1	April 2012	3 Months LIBID

b) Dividends

The company's dividend policy is to declare dividends which are consistent with the company's regulatory obligations and at a level which is decided each year after consideration of a number of factors, including regulatory uncertainty, market expectations, actual and potential efficiencies, future cash flow requirements and balance sheet considerations

The amount declared is expected to vary each year as the impact of factors changes. The ordinary dividend declared and paid by the company in 2012/13 amounted to £72 0 million (2012 £266 million), being 7 2p per share (2012 26 6p per share)

c) Transfer of assets/liabilities

During the year, the appointee acquired the following assets from associated companies as follows: Severn Trent Laboratories Limited, fixed assets £1 9m, stock £0 3m and goodwill £1 3m; Midland Land Portfolio Limited, land and buildings £4 2m

d) Supply of services

Services supplied by the appointee to associated companies

Nature of transactions	Company	Terms	£m
Service charges in respect of payroll, legal, transport and other	Various	Cost	0 4
Water, tankering, reception, treatment and disposal of waste	Various	Market rent	0 7
Sale of crops	Severn Trent Green Power Ltd	Cost	0 6
Management charge	Severn Trent Plc	Cost	6 3
			8 0

Services supplied to the appointee by associated companies

Company	Turnover	Nature of transactions	Services supplied to the appointee			Total £m
			Competitive letting £m	Other market testing £m	No market £m	
Derwent Insurance Ltd	7 6	Insurance services	-	6 0	-	6 0
Severn Trent Laboratories Ltd	19 5	Analytical services	1 4	-	2 3	3 7
Severn Trent Metering Services Ltd	3 9	Meter installation and maintenance	2 5	-	0 1	2 6
Severn Trent Services Ltd	4 2	Supply of materials and other engineering services	1 6	-	-	1 6
Severn Trent Green Power Ltd	2 7	Supply of Electricity	-	1 0	-	1 0
Cognica Ltd	0 9	Asset management	0 1	-	-	0 1
Severn Trent Plc (mgmt charge)	-	Pass through costs	-	-	1 2	1 2
	38 8		5 6	7 0	3 6	16 2

e) Omission rights

None

f) Waivers

None

g) Guarantees

None

Supplementary Regulatory Accounting Disclosures – unaudited

Year ended 31 March 2013

Analysis of properties

	2013		2012	
	Water	Sewerage	Water	Sewerage
Number of properties ('000s)				
Households billed	3,126.8	3,563.8	3,124.0	3,556.5
Non-households billed	183.5	200.0	186.1	203.2
Household voids	124.7	154.1	109.2	133.3
Non-household voids	28.7	41.9	26.1	39.1
Properties served by the appointee in supply area as at 1 April 2009	6.0	6.0	4.0	4.0
Per capita consumption (excluding supply pipe leakage) l/h/d				
Unmeasured household	129.9		133.1	
Measured household	104.6		109.4	
Volume (Ml/d)				
Bulk supply export	59.2	-	56.7	-
Bulk supply import	370.0	-	377.9	-
Distribution input	1,766.3		1,830.6	

Supplementary Regulatory Accounting Disclosures – unaudited

Year ended 31 March 2013

Delivering against our Key Performance Indicators (KPIs)

Basis	KPI No	KPI	2011/12 Performance	2012/13 Performance
MAT	1	Lost time incidents per 100,000 hrs worked ¹	0.3	0.2
QR	2	Employee motivation % ²	75%	79%
MAT	3	DWI Reportable events (Category 3,4,5) ⁶	30	23
MAT	4	Service Incentive Mechanism - Qualitative ³	3.96	4.36
MAT	5	Service Incentive Mechanism - Quantitative ^{3,4}	205	167
MAT	6	Unplanned interruptions (per 1000 properties)	11.12	12.48
MAT	7	Serviceability Waste	N/A	78
MAT	8	Serviceability Water	N/A	80
ACT	9	Capex - £m	N/A	541.8
ACT	10	Debtor days ⁵	35.8	36.7
ACT	11	Opex - £m	548	567.2
MAT	12	Pollution incidents (Category 1,2,3) ^{3,6}	458	376
ACT	13	Sewage treatment works - failing consent limits %	2.54%	0.85%
ACT	14	Security of Supply ³	99	99
MAT	15	Net energy use GWh ⁴	679	690
MLE	16	Leakage MI/d - Post MLE ³	464	441

Notes

MAT = Moving Annual Total

QR = Quarterly Review

MLE = Maximum Likelihood Estimate

ACT = Year end actual

- 1 Actual performance across all employees and agency staff
- 2 Performance based on annual survey of all employees
- 3 As reported in the Annual Regulatory Performance Report. Performance figures are provisional at this stage as the Annual Regulatory Performance Report will be published on the Company's website (www.stwater.co.uk) on 17 June 2013.
- 4 Actual performance based wholly or partially on internal data
- 5 Actual performance based on audited financial statements for the year ended 31 March 2013
- 6 Measure for calendar year to 31 December 2012

KPI 3

Drinking Water Inspectorate – Reportable events. This KPI measures the number of significant events reported to the DWI.

KPI 7

Serviceability Waste Water. This KPI is an index based on pollutions and blockages (both measures of how our below ground assets are performing) and sewage treatment works non compliance (above ground). The index reflects a 50/50 weighting for above and below ground assets.

KPI 8

Serviceability Water. This index is based on mains bursts and supply interruptions greater than 12 hours (both measures of how our below ground assets are performing) and Water Treatment Works (WTW) non compliance (above ground). The index reflects a 50/50 weighting for above and below ground assets.

KPI 14

Security of Supply Index (SOSI) is a measure of how resilient we are against periods of drought. The index calculation is based upon the difference between the water available to use and the volume of water we expect to put into our supply network in order to meet demand.