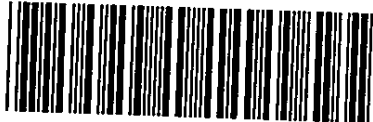


Severn Trent Water Limited

Report and financial statements for the year ended 31 March 2014

Company number 2366686



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COMPANIES HOUSE

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Strategic report

At a glance

One of the largest of the 10 regulated water and sewerage companies in England and Wales. We provide high quality services to more than 4.3 million households and businesses in the Midlands and mid-Wales.

Where we operate

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

Turnover
£1,544.8m (2013: £1,511.0m)

4.3m
Households and businesses serviced

1.4bn
Litres of waste water collected per day.

Profit*
£516.4m (2013: £495.6m (restated)**)

* Before interest, tax and exceptional items
** Adjusted for adoption of IAS 19R

1.8bn
Litres of drinking water supplied each day

5,902
Employees (as at 31 March 2014)

Who we are

Water is essential to life and to the communities in which we live and work.

At Severn Trent Water we are focused on continuing to deliver better value, better services and a healthier environment today, tomorrow and for the longer term.

Our millions of customers rely on us, so our aim is to do the right thing, acting with honesty and integrity and playing an active role in creating a sustainable future for our water and the environment.

Our principles which govern the way we work are set out in our Code of Conduct: Doing the right thing - The Severn Trent way.

Strategic report

Chief Executive's review

Introduction

I'm delighted to have joined Severn Trent Water, a forward looking and industry leading business

I appreciate all the hard work from Tony Wray and his colleagues over recent years and I'm looking forward to continuing to deliver for our customers, our regulators and our great people at Severn Trent Water

Another year of delivery

This was a good year for Severn Trent Water as we delivered on our commitments to our customers, the environment and employees

Our customers once again benefited from the lowest combined water and waste water charges in England and Wales. The cumulative price increase over the past five years is below inflation. We intend to maintain below inflation increases, on average, through to 2020.

We improved our operational performance despite difficult weather, with a hot summer followed by a winter of prolonged rain and high winds. Although the rain affected the quality of our raw water, we continued to deliver high levels of water quality compliance. Our overall water quality continues to be amongst the best in the UK, however we know we have more to do in delivering the improvements identified in the Drinking Water Inspectorate (DWI) Chief Inspector's report. We remain committed to ensuring our customers continue to receive water of the highest quality.

We further reduced the average duration of interruptions to supply. We remain on track to hit our leakage reduction target over the current regulatory cycle and we again reduced the number of properties suffering internal sewer flooding.

While our operating performance is good across most parts of our business, as the regulated business performance review details, some other performance areas did not meet the required standard. Three of the twenty indicators used to assess the long term health of our assets are not performing within the required levels. This in turn has resulted in three of the four serviceability areas (each with one failing indicator) being assessed as marginal. We recognise this performance is not what our customers expect, and we have put actions in place to address this. We have included shortfalls in our 2015-2020 business plan in recognition that we have not delivered the level of performance we had set ourselves.

Also our customer service hasn't always been as good as we would like. We are committed to delivering the best possible experience for our customers and are focusing on training, better systems and processes and new ways for customers to interact with us. One area where we have targeted improvements is on our New Connections process. We recognise the need to provide customers with a fast and efficient service and are committed to doing better to meet developers' expectations.

This year, we've again seen our efforts reflected in our improved Service Incentive Mechanism (SIM) score, as measured by Ofwat, but there is still much more to be done. Further details are provided on pages 16 and 17.

Our SIM score really matters to us – it tells us if we are delivering 5 out of 5 performance every time, every day for our customers. We know we have lots still to do and that we need to deliver improvement quickly to keep pace with changes in customer behaviours and expectations. We've made good progress in our Quantitative SIM scores with a 14% improvement this year, meaning that customers are receiving a more responsive service from us. Our Qualitative SIM score, which captures how our customers feel about their interaction with us, is where we need to place more focus in the year ahead. For the year as a whole for this measure, our score is 4.48 compared to 4.36 in 2012/13. Although this leaves us in seventh place out of the 10 water and waste water companies, we are improving at a faster than average pace.

Strategic report

Chief Executive's review

Severn Trent Water has one of the lowest levels of bad debt in the sector, at around 2.2% of revenues. This is important for our customers because those who pay bear the cost of those who don't. We therefore put considerable effort into ensuring that customers who can pay actually do pay and we have invested in new technologies that make it easier than ever to do so – see further details on page 17.

However, we recognise that economic conditions remain tough. As a responsible business, it's important that we help people who are genuinely unable to pay, so we have a comprehensive range of social tariffs. Our relationship with the Citizens Advice Bureau also helps customers to address their broader financial problems.

We continued to look after the environment during the year, with our investment programme producing further environmental improvements that also benefit our customers. We cut the number of sewer blockages and we reduced the number of serious pollution incidents by over a third. We're also improving the quality of our rivers, achieving our best ever waste water treatment works compliance of 99.29%. Knowing that we will supply them with water is critical for our customers and the security of supply index measures our ability to supply water in a drought. Our score this year was 100 (based on our Ofwat measures – see page 7), reflecting the work we've done to improve resilience and extract water sustainably.

Our tax position this year reflects an outline agreement we have reached with HMRC on a long standing discussion regarding overpayments of tax in prior periods and have now factored this into our business plan for 2015 - 2020 to support lower customer prices in the next regulatory period (AMP 6 – see further details on page 9).

This performance and continuous improvement is made possible by our committed and experienced team. Good performance is underpinned by doing things the right way, safer, better and faster. Our teams have sustained last year's industry leading safety performance – for further details see pages 20 and 21.

On behalf of all of my executive colleagues, I would like to thank our employees and supply chain partners for their continued commitment.

Looking forward, conclusion and outlook

Severn Trent Water has submitted a balanced plan for AMP6, which offers better services and continued better value for customers, along with a healthier environment. At the same time, our plan will deliver investment and growth in our business, to produce fair and sustainable returns for our investors. We continue to work with Ofwat to conclude the price review process. We expect a draft determination from Ofwat on 29 August and a final determination on 12 December 2014.

Wales remains an important area of operation for us. We welcome the publication of Welsh Government's Water Strategy and we will be playing our full part to make a success of its implementation. We also welcome the publication of the Silk Commission's report into further devolution and look forward to ongoing discussions about ensuring our customers in Wales continue to receive excellent value for money.

My focus for the next 12 months will be on making sure our customers are right at the heart of Severn Trent Water and delivering further operational and process improvements, so that we are ready to deliver on our plan for the next five years.

I look forward to working with everyone in Severn Trent Water, as we build the next phase of our journey to deliver for our customers, employees and the environment.

Liv Garfield
Chief Executive

Strategic report

Our strategy

Our aim is to drive value for our customers with a focus on water and waste water services. Our strategy delivers better value, better services and a healthier environment.

How we are organised to deliver

Severn Trent Water provides water and waste water services to over 4.3 million homes and businesses.

Our business plan for the next regulatory period (AMP6 see page 9) is driven by – and for – our customers. Our aim is to provide what our customers want and what the environment needs, whilst still keeping our charges as low as possible.

See our business model on pages 12 and 13.

What we stand for

Value

We aim to deliver value for our customers. Our customers get good value for money – quality products, the lowest possible charges and a good overall service. Our stakeholders benefit from long term sustainable growth.

Responsible leadership

We have long advocated a more socially, environmentally and financially sustainable future for our industry through our 'Changing Course' series of publications. We aim to have an open and honest conversation with our customers, our colleagues and our regulators about the changes we can all make towards a more sustainable future.

Sustainability

At Severn Trent Water we balance the interests of all our stakeholders and the environment. We believe in doing the right thing for the longer term and in operating our business in a sustainable way.

Our strategy delivers

Better value and better services for customers

We already have the lowest combined water and waste water bills in England and Wales. Through a focus on continuous improvement and efficiency, we aim to deliver the service improvements our customers want and which the environment needs, whilst keeping prices as low as possible.

A healthier environment

Our aim is to protect and enhance the environment improving the quality of our rivers and safeguarding the infrastructure that our customers and the environment depend upon. We strive to operate our business in a sustainable way, reducing the amount of water we take out of the environment, reducing our carbon emissions and generating our own renewable energy.

Our objectives

Our objectives

Image removed	Quality water	1 We will provide you with water that is good to drink
Image removed	Service you can rely on	2 We will ensure water is there when you need it
		3 We will safely take your waste water away
		4 We will provide you with excellent customer service
Image removed	Affordable bills	5 We will have the lowest possible charges
		6 We will help you if you struggle
Image removed	Responsible service	7 We will protect our local environment
		8 We will protect the wider environment
		9 We will make a positive difference in the community
Image removed	Sustainable finance	10 We will finance our business sustainably
Image removed	To achieve our objectives we need to support our great people	

Strategic report

Graphic removed

Basis		How we measure them		2013/14	2012/13	
		Water quality compliance % ^{1,2}	OW	🟢 99.96	99.98	Key
MAT		Water serviceability: non infrastructure ³	OW	🟢 MAR	STA	Black. Regulated measures including Business KPIs and Ofwat performance indicators
MAT		DWI reportable events (category 3, 4, 5)	KPI 3	🟢 24	23	Blue. Severn Trent group measure Executive Director performance measure see Remuneration Committee report on page 48
MLE		Leakage levels MLD	KPI 16/OW	🟢 441	441	OW Ofwat performance indicator
ACT		Security of Supply Index (SOSI) ⁴	KPI 14/OW	🟢 99/100	99/100	MAT Moving Annual Total
MAT		Water supply interruptions index per property mins ⁵	KPI 6/OW	🟢 16	29	QR Quarterly Review
MAT		Water serviceability: infrastructure ³	OW	🟢 MAR	STA	MLE Maximum Likelihood Estimate
		Water serviceability (internal)	KPI 8	🟢 202	80	ACT Year End Actual
		Internal sewer flooding repeat incidents number	OW	🟢 204	255	MAR Marginal
MAT		Sewerage serviceability: infrastructure ³	OW	🟢 MAR	STA	STA Stable
		Sewerage serviceability (internal)	KPI 7	🟢 57	78	🟢/🟢 Desired direction of KPI
ACT		Sewerage treatment works – failing consent limits % ²	KPI 13	🟢 0.71	0.85	Notes
MAT		Service Incentive Mechanism Qualitative (SIM) score	KPI 4	🟢 4.48	4.36	1 No longer an Ofwat KPI but still reported
ACT		Service Incentive Mechanism Quantitative (SIM) score ⁶	KPI 5	🟢 143	167	2 Measured on a calendar year basis
		Service Incentive Mechanism (Ofwat)	OW	🟢 81.55	78.11	3 Ofwat serviceability score assesses how effectively we are maintaining our network and assets against a range of measures. Assessed as either improving, stable, marginal or deteriorating
		Average combined water bill £ (outturn prices)		🟢 £335	£326	4 Score of 99 represents internal KPI and 100 is our Ofwat measure. Measure is out of 100
ACT		Debtor days ⁸	KPI 10	🟢 34.5	36.7	5 Number of minutes lost due to supply interruptions for 3 hours or longer per property served
		Customers benefiting from Watersure tariff number		🟢 9,611	7,972	6 Actual performance based wholly or partially on internal data
		Serious pollution incidents (Infrastructure category 1, 2) per 10,000 km network ^{3,9}	OW	🟢 1.27	2.17	7 Customer satisfaction and branding survey
		Pollution incidents (Infrastructure category 1, 2, 3) per 10,000 km network ^{3,9,11}	OW	🟢 77.97	66.10	8 Actual performance based on audited UK GAAP financial statements for the year ended 31 March 2014
MAT		Pollution incidents (sewerage cat 1, 2, 3) ^{3,10,11}	KPI 12	🟢 449	376	9 Number of incidents adjusted to reflect company size
MAT		Sewerage serviceability: non infrastructure ³	OW	🟢 STA	STA	10 Total number of pollution incidents (category 1, 2, 3)
		Discharge permit compliance % ²	OW	🟢 99.29	99.15	11 2012/13 figures not comparable. In 2013 the Environment Agency changed its reporting methodology for small incidents. As a result of this reclassification we now report more smaller incidents.
		Greenhouse gas emissions KCo2e	OW	🟢 510.9	520.4	12 Non compliance with consents, permits or formal client requirements during the previous 12 months.
MAT		Net energy use Gwh % ⁶	KPI 15	🟢 691	690	13 Investment excluding PDAS and IFRS adjustments.
		Satisfactory sludge disposal %	OW	🟢 100	99.93	14 Performance based on annual survey of all employees
		Investment £million		🟢 602.1	555.4	15 Actual performance across all employees and agency staff
		Interest cover %	OW	🟢 3.6	3.6	KPI 3 Drinking Water Inspectorate – Reportable events. This KPI measures the number of significant events reported to the DWI.
		Net debt/RCV gearing %	OW	🟢 58.6	57.1	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 sewerage treatment works non compliance (above ground). The index reflects a 50/50 weighting for above and below ground assets.
		Credit rating Standard & Poor's	OW	🟢 BBB+	BBB+	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.
ACT		CAPEX £m (UK GAAP, net of grants and contributions) ¹³	KPI 9	🟢 583.2	541.8	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.
ACT		OPEX £m	KPI 11	🟢 585.3	566.5	
		Post tax return on capital %	OW	🟢 6.4	6.7	
QR		Employee engagement % ¹⁴	KPI 2	🟢 81	79	
MAT		Lost time incidents per 100,000 hrs worked ¹⁵	KPI 1	🟢 0.21	0.21	

Strategic report

Market and industry overview

The water and sewerage industry in England and Wales has more than 50 million household and non-household customers. More than 30 privately-owned companies serve these customers, of which 10 – including Severn Trent Water – provide both water and sewerage services. The industry invests around £5 billion each year and employs over 35,000 people.

The water industry has achieved much in the 25 years since it was privatised. It has attracted over £100 billion of private investment to fund improvements in, among other things, customer service, drinking water and environmental standards.

However, our sector still faces significant short and long term challenges:

- customers' incomes have been squeezed, limiting their ability to pay for service improvements. We need to ensure that our services are affordable,
- the UK's population is growing, placing more pressure on our water resources and on our networks. We need to ensure we have sufficient capacity,
- we're experiencing more flooding and droughts. We need to ensure that we have resilient services able to cope with this increased volatility,
- financial markets have changed significantly since the 2008 financial crisis, raising questions about how the industry can best finance its long term investment. We need to ensure that the industry is financed sustainably,
- we still face considerable challenges to meet the requirements of the Water Framework Directive and other environmental imperatives. We need to play our part in improving the environment, at a price that is affordable to our customers, and
- some of our infrastructure is old. Whilst it has served us well it is no longer able to deliver the quality standards and reliability customers want. We need to ensure that our investments are timely, provide good value for money and will deliver many years of future service.

We have actively sought to be at the forefront of the debate about our industry's future and how we tackle these challenges, through our series of 'Changing Course' publications. We have championed a more socially, environmentally and financially sustainable water industry.

We've been pleased that many of the ideas we have championed have been reflected in the emerging UK policy and regulatory framework that is being put in place. Challenges remain, but we are encouraged by the direction of reform. We look forward to helping to make it a success.

How the industry is regulated

Severn Trent Water is a regulated business. We work within five year regulatory planning cycles, with the prices we charge our customers set at the beginning of each cycle by our economic regulator Ofwat. These five year cycles are known as Asset Management Plan (AMP) periods. We have just reached the end of the fourth year of AMP5. However, we don't just think in the short term. Having a sustainable business requires us to also balance longer term requirements that stretch beyond our five year plans. For example, our water resource plans look 25 years into the future and we study the need for investment in some of our assets over a 40 year period. We use this information to adjust our investment plans for the next AMP cycle to ensure we do the right thing for the long term whilst helping to keep customers' bills affordable.

As well as being regulated by Ofwat, our performance is monitored by

- the Drinking Water Inspectorate, which makes sure we comply with drinking water quality regulations,
- the Environment Agency ('EA'), which controls water abstraction, river pollution and flooding, and

Strategic report

Market and industry overview

- Natural Resources Wales, which brings together the work of the Countryside Council for Wales, the Environment Agency Wales and the Forestry Commission Wales to manage the natural resources of Wales, and

- Natural England who protect and improve England's natural environment

We also work with other agencies including

- the Department for Environment, Food and Rural Affairs which sets the policy context for the water industry in England,

- the Welsh Government which sets the policy context for the water industry in Wales, and

- the Consumer Council for Water which represents customers in the industry

Our business plan for AMP6

Ofwat requires us to produce business plans for each five year regulatory period. In December 2013, we submitted our business plan for the next regulatory period (AMP6), which runs from April 2015 to March 2020. This plan is currently being reviewed by Ofwat who will give us its final determination in December 2014.

Our plan is driven by – and for – our customers. The 'golden thread' running through our plan comprises four essential elements:

1 Our plan delivers better value for money

We're proud to have the lowest average combined bills in England and Wales. Our AMP6 plan delivers even better value, by limiting price rises to below the rate of inflation. This means our average price rises from 2010-20 will have been below the rate of inflation over that 10 year period.

At the same time, we'll increase overall capital investment to around £3 billion. We'll prioritise improvements in those areas most important to our customers, including better services and healthier rivers. In particular, our plan proposes to reduce:

- leakage by a further 6%,
- the length of time our customers' water supply is interrupted by 47%,
- the number of homes affected by sewer flooding by 14%, and
- our carbon footprint by 3%

We've also set challenging efficiency targets, reducing total costs in AMP6 by over £370 million, helping to keep average bills lower in 2020 than they otherwise would have been.

2 Our plan is fair and balanced

We've taken into account the interests of all our stakeholders. We're sharing the benefits of outperformance with our customers by investing an extra £150 million, to improve the service our customers receive – see further details about how we have spent this extra investment so far on page 17. We'll continue this approach in the next regulatory period, to ensure customers share in the rewards of our success and also ensure that there is no need for regulatory intervention in AMP6. We'll have the opportunity to earn more, through incentives that encourage us to deliver even better services. If we don't deliver on our commitments, penalties will result in lower prices to customers.

Strategic report

Market and industry overview

3 Our plan is robust and reliable

Our approach builds on our track record of producing robust business plans and is based on the largest customer research and engagement exercise we've ever undertaken through our Let's Talk Water consultation. We also put in place a rigorous assurance process, to test the plan's robustness.

In total, we talked to more than 16,000 customers and other stakeholders. We gave customers real choices about where their money should be spent and we were challenged hard by the Water Forum, our customer challenge group, and changed our plan as a result. The Water Forum includes representatives from customers, our environmental regulators and local authorities, and has an independent Chair, Dame Yve Buckland, who is also the Chair of the Consumer Council for Water.

4 Our plan does the right thing for the long term

We've long advocated a more socially, environmentally and financially sustainable water industry and published our first 'Changing Course' report in April 2010. Our plan is shaped by the philosophy that underpins 'Changing Course' and provides a solid foundation for the long term.

Our future plans include major investments over the next two AMP periods to increase the resilience of Birmingham's water supply.

We're also planning to make significant investment in 2015–2020 to improve the quality of rivers and on strategic resilience, which we're phasing over 10 years to ensure the right balance for customers' bills in AMP6. We plan to double our programme of sustainable urban drainage systems, to help prevent sewer flooding. We also plan to reduce the amount of water we take out of the environment per customer by 6%, further strengthening our leading position in this area.

A changing regulatory environment

The water industry continues to be affected by a number of changes to legislation and regulations.

New legislation introduced this year through the Water Act 2014 brings a number of significant changes to the way the industry operates. In particular, it will allow more competition for non-household customers and greater 'upstream' competition which should eventually lead to a more efficient industry.

The European Water Framework Directive (WFD) will be a significant driver of our future capital expenditure. It will help to protect and enhance our rivers, lakes, streams and groundwater. During 2013/14, we published a Changing Course report on implementing the WFD and shared it with the EA. This is our contribution to the debate about achieving environmental improvements at an affordable cost to customers. We've also begun to look at which technologies offer the best solution to implementing the WFD, in preparation for AMP6.

Strategic report

Market and industry overview

Case study: Better for Jessica

We made sure that we listened to our customers' problems, like Jessica's, in our AMP6 business plans

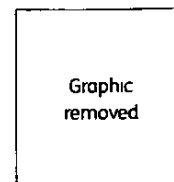
Listening to customers in shaping our plans

Tackling the nasty problem of sewer flooding for customers like Jessica Hinnett from Alfreton in Derbyshire is a top priority for our customers which came out of our Let's Talk Water consultation

Over 16,000 customers gave us their views in our biggest ever customer consultation. We made sure their voices were heard loud and clear when we submitted our AMP6 business plan to Ofwat.

Thankfully for Jessica, her problem was sorted out quickly. "I can't speak highly enough of everyone at Severn Trent who helped me at a time when I was very emotional."

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, 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 and the Environment Agency (details of these regulators are provided below).

Our prices and asset base are adjusted by 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. Severn Trent has not sought to review prices for either of these reasons during 2010-15.

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. Within the current price review there is scope to earn additional income, or incur penalties, based on our performance.

Regulatory framework

Consumer Council for Water

Consumer Council for Water is an independent body designed to protect the rights of consumers. www.ccwater.org.uk

Drinking Water Inspectorate (DWI)

The Drinking Water Inspectorate makes sure companies supply water that is safe to drink and complies with all national and European standards. www.dwi.defra.gov.uk

Environment Agency (EA)

The Environment Agency is a public body set up to protect and improve the environment. www.environment-agency.gov.uk

Health and Safety Executive

The Health and Safety Executive is the enforcing authority on health and safety law. www.hse.gov.uk

Natural England

Natural England protects and improves England's natural environment. www.naturalengland.org.uk

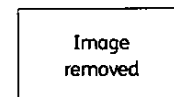
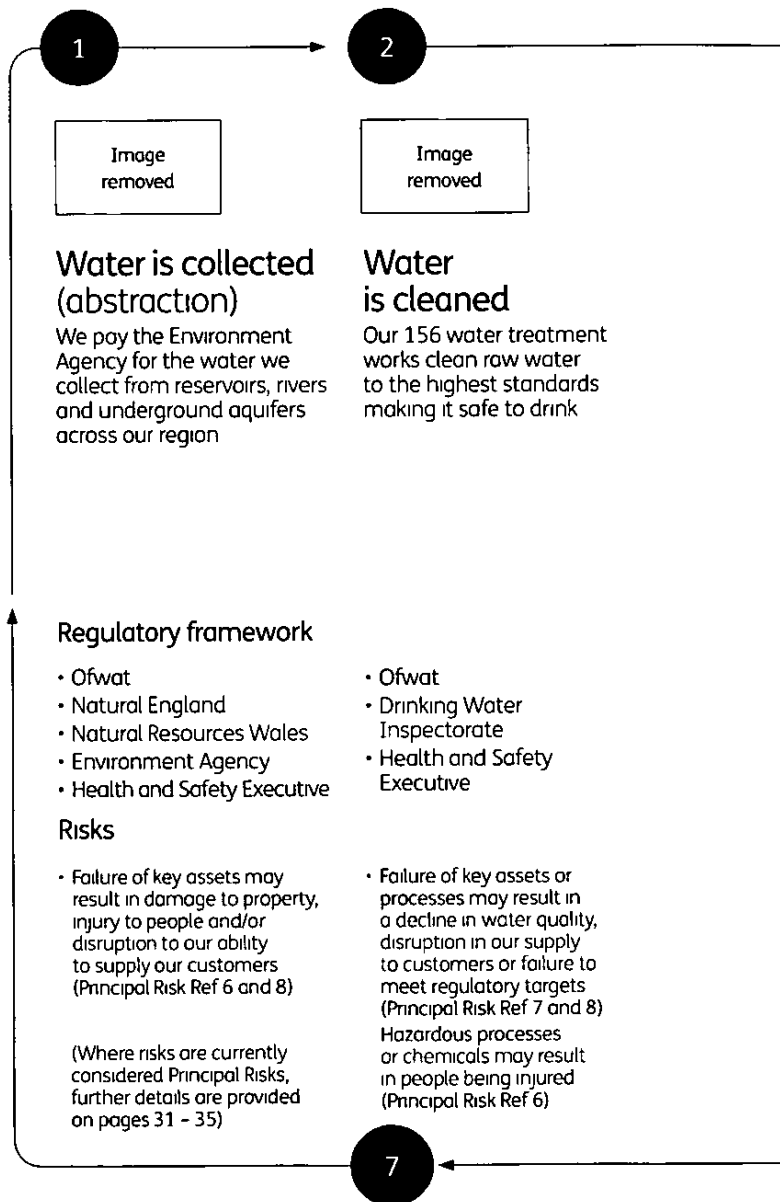
Natural Resources Wales

Natural Resources Wales brings together the work of the Environment Agency Wales, The Forestry Commission Wales and the Countryside Council for Wales. www.naturalresourceswales.gov.uk

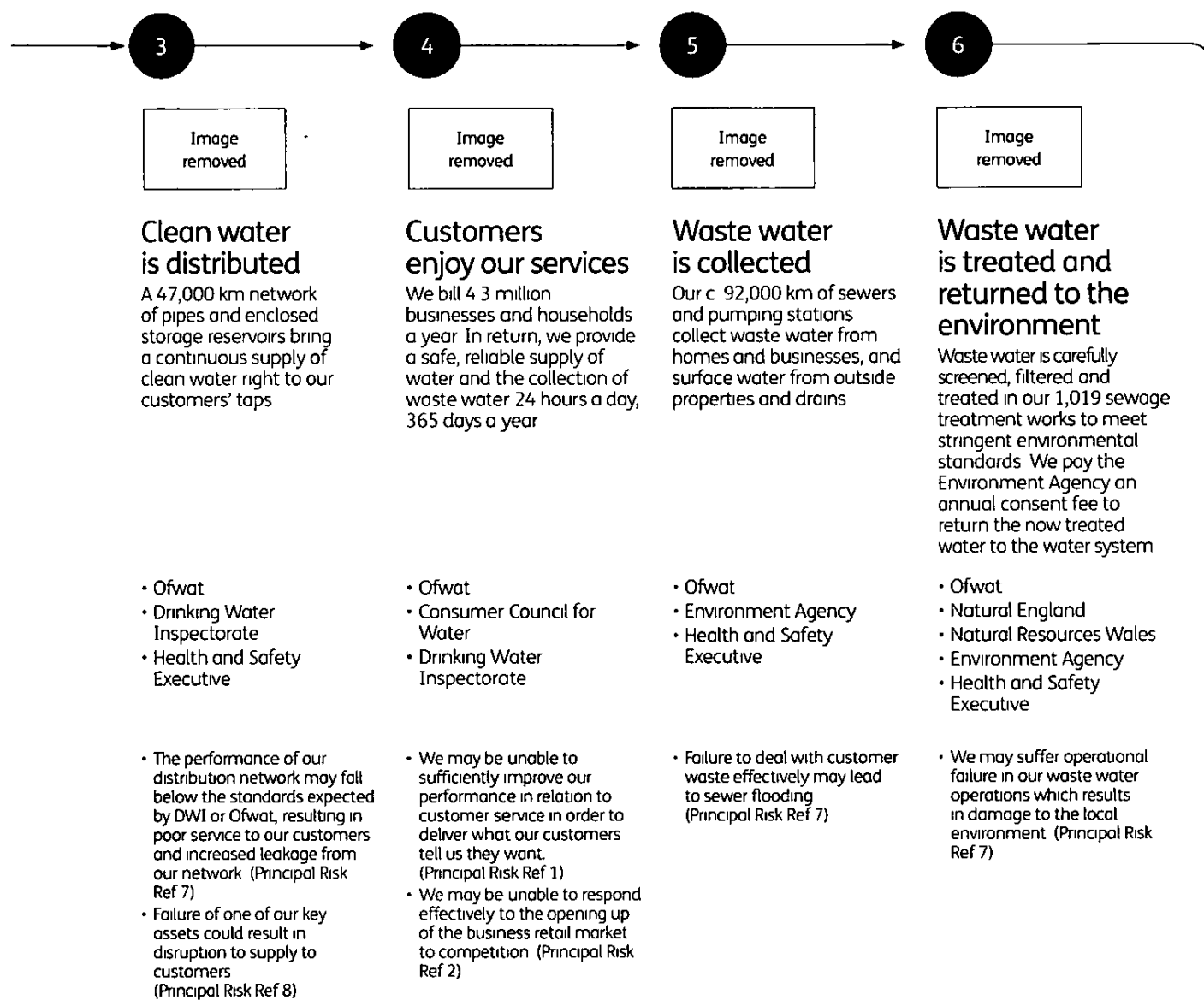
Ofwat

The economic regulator for the water and sewerage industry. It makes sure that water companies use customers' money efficiently and effectively and sets our price limits. www.ofwat.gov.uk

The role of Severn Trent Water



Strategic report



We are an investment led industry, and our capital programme this year was £602 million, or around £140 per connected property, reflecting increased investment year on year (2012/13 £555 million) in our water and sewerage networks, including finding and fixing more leaks and reducing the number of supply interruptions, improvements to our water and sewage treatment plants and upgrades to our sewer network to reduce incidents of sewer flooding. We fund this investment programme from the profits we generate, but also by borrowing money from the capital markets. Capital investment is added on to our asset base, called the RCV. Our asset base also rises in line with inflation each year. The returns that we generate for shareholders on that asset base are set by our economic regulator, Ofwat, over five year planning cycles. We can increase these returns by outperformance.

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 (Principal Risk Ref 3, 4 and 5 on pages 31 and 32).

Regulatory Framework

- Ofwat
- Health and Safety Executive
- Environment Agency
- Drinking Water Inspectorate

Strategic report

Performance review

Delivering better value, better services and a healthier environment

Our goal is to be the UK's best water and waste water company. This means we must deliver better value and better services to customers and investors, while protecting the environment on which we depend.

To reach our goal and meet our customers' needs, we set 10 long term objectives in 2013. Each year, we report against our objectives and explain how we've improved our performance.

Quality water

Objective 1 We'll provide you with water that is good to drink

Our drinking water is amongst the best in the UK and we achieved 99.96% overall compliance with the Drinking Water Inspectorate's (DWI) quality standards (2012/13 99.98%).

However, some aspects of our performance have fallen below the standard we and our customers expect. We reported one more significant event to the DWI this year than last. The two most recent DWI Chief Inspectors' reports have highlighted a number of improvement areas, and there has been one prosecution during the last year in relation to water quality. Specifically, our performance in relation to the number of outbreaks of detected coliforms (non-harmful bacteria) has exceeded the maximum level expected by Ofwat twice in three years (including 2013/14). As a result our serviceability on above ground assets is rated as marginal.

We are taking these failures extremely seriously and accept that we have more to do in order to address the issues and risks we face. We have identified several areas where improvements to our assets are required and investment programmes are already in progress. We have a programme of work dedicated to identifying and delivering improvements. We have stepped up our operational monitoring and remain committed to doing what is needed to address issues in this area at pace. We remain committed to ensuring that our customers receive water of the highest quality.

We continue to invest in our people and in our treatment works to enable us to improve our performance. For example, this year we have run a programme to improve knowledge and awareness of water quality for our network operators and operational call-centre colleagues. We are in the process of investing to renew assets and improve processes at our largest works at Frankley. At Bamford, Derbyshire, we've improved our processes to increase their resilience and ability to treat water from the local peat moors.

We continue to look to the future with our water quality strategy and our AMP6 plan will also look to addressing deteriorating raw water quality in more innovative and sustainable ways, for example, extending our catchment approach. It involves working in partnership with landowners and users to minimise the risk of pollution entering the raw water system, so we can avoid additional investment in our treatment works.

Services you can rely on

Objective 2. We will ensure water is there when you need it

Our customers expect water to be there when they turn on the tap and for leakage to be lower.

As part of our commitment to improvement we have reviewed the basis on which we calculate our leakage figure. The net impact of the improvements is neutral with respect to actual and target performance.

We maintained leakage at 441Ml/d beating our Ofwat leakage target of 456Ml/d. Severn Trent Water is one of the few companies to target lower leakage during AMP5 and we're on track to deliver an 11% leakage reduction over AMP5.

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We've further reduced the average number of minutes that customers are without supply from 29 minutes per property to 16 minutes. We're investing in new pipes, valves and other assets, and improving our ability to restore customers' supplies quickly. For example, new technology allows us to keep water flowing while we repair a pipe. We were pleased to win an award for innovation of the year at the Water Industry Achievement Awards 2014 for new equipment we have developed that improves leak detection efficiency and is particularly effective with plastic pipes which is a problem throughout the industry. This equipment has been developed by us working in partnership with Loughborough University from a research and development project through to commercial launch with Echologics.

The number of properties that experienced a supply interruption longer than 12 hours was 2,699, an increase of 142 on last year. Over 900 of these interruptions occurred following the extreme storms of February when power supplies were interrupted for extended periods. This is a key input measure to serviceability assessment. Despite an underlying improvement on this measure, and the fact that other indicators performing within or ahead of the operating ranges agreed with Ofwat, the application of the serviceability framework means our serviceability is rated as marginal.

We are committed to reducing the number of interruptions longer than 12 hours. In order to achieve this we have increased our focus on improving our risk and contingency planning and emergency response.

Towards the end of the year, we consulted on our water resources management plan. This explains how we'll provide sustainable and affordable water to our customers, over the next 25 years and beyond. We also issued our drought plan, which sets out how we'll maintain supplies during shortages.

Our future plans include major investments over the next two AMP periods to increase the resilience of Birmingham's water supply. This will extend the life of the Elan Valley Aqueduct, saving customers hundreds of millions of pounds over the coming decades and reducing risk to the UK's second largest city. We'll also continue to improve our trunk main network and strategic grid of pipes to provide customers with increased resilience.

Objective 3 We will safely take your waste water away

We continue to invest to reduce the risk of internal sewer flooding and have protected a further 121 properties this year, putting us on track for 741 properties over AMP5. Our efforts have reduced the number of customers who suffered repeated internal sewer flooding, from 255 in 2012/13 to 204 this year. We also mitigated the risk of flooding for around 160 properties this year. We're increasingly using sustainable drainage systems to reduce flooding, as well as increasing our partnership working with local authorities, the Environment Agency, local drainage boards and highways authorities.

This year, we completed our flood protection scheme in Gloucester. It has kept the town free from flooding, despite extreme weather over the last two winters. Our Royal Leamington Spa sewer improvement project, which will protect 103 properties from flooding, is going to plan and will complete in 2014. This project won a national Green Appie award for recycling excavated material and we're exploring how to extend this to other schemes.

Our overall serviceability remains marginal. We have continued to deliver good performance on five of the six indicators included in the serviceability assessment. On the sixth indicator, sewer blockages, our performance has shown an improving trend over 18 months (falling 13% last year) but remains above the target agreed with Ofwat. The improvement is reflective of the action we have taken throughout the AMP5 period. Although our overall environmental performance remains positive, and the other customer and environmental indicators within this area are performing within or ahead of the operating ranges agreed with Ofwat, the application of the serviceability framework results in a continuing 'marginal' assessment. This is consistent with the assessment included in our PR14 Plan. Our pollution performance is included within Objective 7 – We will protect our local environment – set out below.

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We've made a good start to adopting and upgrading private pumping stations, ahead of their transfer on 1 October 2016. We've already adopted and upgraded 24 stations and will adopt another 150 in the next year.

We will continue to improve our blockage and pollution performance by increasing our focus on customer education. 75% of blockages are due to unwanted items that customers put down the toilet so we are speaking to customers following any local incident and developing a broader campaign to provide more focus in this area.

Case study: Better for Sylvia

Gloucester resident Sylvia Hyett now has greater peace of mind after a £47 million investment in making our water and sewerage system robust and resilient.

Giving our customers peace of mind

In 2007, Gloucestershire suffered severe floods. Hundreds of properties suffered sewer flooding and rising river levels forced us to shut our Mythe water treatment works, leaving 140,000 properties without a piped water supply.

We were determined that our customers shouldn't have to face this again. Since 2007, we've invested nearly £47 million in making our water and sewerage system robust and resilient. We've installed 16 km of strategic water mains and 3.4 km of sewers, along with new water and sewage pumping stations, and we have built flood defences around our Mythe works.

The result is peace of mind for customers like Sylvia Hyett. Despite appalling weather, no properties have suffered sewer flooding in this area in the last two winters and our customers' water supply has been unaffected.

Said Sylvia: "We are so relieved that this work has been completed. If it rains now, for the first time in many years we can go to bed without being terrified as to what we may find in the morning... the work done by Severn Trent to prevent this will improve our lives immeasurably."

Objective 4 We will provide you with excellent customer service

We want to make it easy to be a Severn Trent Water customer. In recent years we've worked hard to offer our customers a broader choice of contact channels, and to deliver an improved experience from each of those channels. For example, today we answer more than 80% of calls within 20 seconds, and very soon we will be answering customer emails within 4 hours. We're also working hard to simplify our processes and provide our customers with more straightforward journeys through the various touchpoints of our organisation. Our company-wide Customer Experience Programme will continue to focus on practical, measurable improvements to what really matters to our customers so that we can consistently deliver to them a 5 out of 5 experience, every time, every day.

There are a number of other ways that we capture and try to measure customer satisfaction. Ofwat measures our customer service using its Service Incentive Mechanism (SIM), which has qualitative and quantitative elements. The qualitative element reflects our customers' views of our service. This year, our qualitative score rose to 4.48 from 4.36, narrowing the gap between us and our peer group. Despite our efforts we are still in seventh place for the year for this measure and we recognise that our pace of change needs to improve.

The quantitative metric reflects the number of customers who have to contact us. Our performance improved by 14%. Overall, our SIM score was 81.55, up from 78.11 last year.

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We also capture data through our 'Voice of the customer' surveys, which gives us feedback from around 10,000 customers each month. This shows that we're now resolving 94% of customer issues first time, while 93% are satisfied with the way our advisors helped them.

Customers want to interact with us in ways that are convenient to them, so we've strengthened our web self-service offering, giving customers full access on a smartphone or tablet. We're also the UK's first utility to launch Pingit, Barclays' mobile payment app. We're already exploring the next innovations that will make it easier to pay.

This year, we worked hard to understand how we could more accurately predict customer demand. This helps to ensure that we have the right resource at the right time, so we can respond faster to our customers' needs.

During the year, we continued to roll out our Great People programme. This gives our frontline advisors better customer interaction skills and helps our managers to run more customer focused operations.

Affordable bills

Objective 5. We will have the lowest possible charges for our customers

With household budgets under pressure, we are pleased that our customers benefit from the lowest combined water and sewerage bills in England and Wales, at £335 in 2013/14. Cumulatively, our prices over the last five years have risen by less than inflation, a record we intend to maintain until 2020.

This year, we have absorbed the additional operating costs of the private drains and sewers we adopted in October 2011 rather than seeking to pass these on to customers. We estimate that we'll absorb additional operating costs of up to £38 million in AMP5, with around £42 million more capital investment.

We continue to share efficiency benefits with our customers. The additional £150 million of investment we announced in May 2012 is helping to deliver our services, including cleaning our sewers, improving our sewage treatment works and reducing leakage. To date, we've invested £120 million, with the remainder to follow in 2014/15.

Customers who don't pay increase costs for those who do, so we take a rigorous approach to ensuring that everyone who can pay actually does. We have one of the industry's lowest levels of bad debt, at 2.2% of turnover.

We continually improve the way we work, so we can keep our customers' bills down and enhance our service. We have introduced common systems and processes which exploit our investment in our SAP enterprise software solution, which underpins and connects our business operations. For example, we are simplifying our 'Plan to Adopt' process (the way we build new assets) helping us to deliver greater efficiency in our capital programme.

During the year, we invested in our Customer Operations Service Centre to improve efficiency and save money. When a customer reports a problem, our agents have better information on the affected asset, work crew availability and other key factors, so we can fix problems faster and give our customers a better service. We've also invested in Netbase, a system that analyses our infrastructure's performance so we can identify where we need to focus the efforts of our work crews to rapidly stop leaks.

Collaborative working with our supply chain partners also delivers efficiencies and business improvements. In 2013/14, we renewed our 'One Supply Chain' approach for a further five years. Extending these relationships has enabled us to put together a robust capital programme for AMP6. More generally, our Procurement team has continued to help us cut the cost of the goods and services that we buy with a total of £58 million saved this year.

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Objective 6. We will help you if you struggle

Poverty rates in our region are significantly higher than the national average and we recognise that some customers genuinely struggle to pay their bills. We offer a wide range of social tariffs and schemes to help, benefiting a total of over 20,000 customers in 2013/14.

This support includes the WaterSure tariff, which caps bills for customers who have particular difficulty in paying, and Water Direct, which allows customers to arrange small deductions from benefits, to go towards their bill arrears.

The Severn Trent Trust Fund is a registered charity, which has helped many customers to meet their water bills.

The Big Difference Fund is our partnership with the Citizens Advice Bureau (CAB). The CAB helps our customers to address their broader financial issues, so they can minimise or avoid household debts more effectively in the future. During 2013/14, we donated a further £3.5 million to these funds.

Responsible business

Objective 7. We will protect our local environment

Pollution incidents are caused by unplanned discharges of water or sewage into the environment. We've further reduced the number of pollution incidents, with serious pollution incidents down by over a third. We understand that we are one of only two companies to deliver a year on year reduction in serious pollutions, as recognised by the Environment Agency (EA). Our overall environmental performance, assessed in 2012/13 by the EA as 3* (out of a possible score of 4*), has significantly improved in 2013/14. We await the EA's final assessment on performance, due to be published in summer 2014. However, there were two prosecution actions taken by the EA during the year, this highlights the need for continued improvement in our operational performance. We've increased our visibility of our final effluent quality by installing monitors at 350 sites, with 209 of these sites being commissioned and in service (compared to only 50 the previous year). We aim to have monitors at 520 sites by the end of AMP5.

We've continued to invest in our sewage treatment works and we're on track to complete our investment programme for AMP5. Our non-infrastructure improvement group has also analysed and systematically eliminated problems. As a result, only five of our 704 consented sites failed to reach their compliance limits, giving us our best ever performance of 99.29%, which has contributed to the serviceability of our above ground assets remaining stable.

We also continue to innovate, testing the Lontra Blade compressor at our Worcester sewage treatment works. The compressor is optimised for aerating waste water, to reduce the electricity we use for this process by 20%. The trial demonstrated the unit's efficiency and reliability. We've also begun work on the UK's first vertical flow reed bed. This technology offers the lowest maintenance and most environmentally friendly solution for sewage works in rural areas.

In line with the EA's National Environment Programme, we invested a further £48 million to enhance river quality, bringing our AMP5 investment to more than £150 million. This included improving processes at 15 sewage works and enabling public sewerage networks for four communities to remove polluting private discharges.

We have an important role in protecting biodiversity, including at the 38 sites of special scientific interest (SSSIs) we own or partly manage. We're working with partners such as Natural England, Natural Resources Wales, the EA, wildlife trusts and the RSPB, to bring all of our SSSIs into favourable condition by 2020. Our key visitor sites with SSSI status have been entered into Natural England's Higher Level Stewardship schemes, which aim to deliver significant environmental benefits in priority areas. In particular, we're looking to increase biodiversity and offer sustainable catchment management on our land.

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However, there are water quality issues at the SSSI at the Charnwood Reservoirs, Leicestershire. To address these we're close to finalising a 10 year agreement and lease with Leicester & Rutland Wildlife Trust (L&RWT), which will enable L&RWT to manage the woodland and reservoir margin, in line with Natural England's SSSI conservation objectives

We continue to have our woodlands certified by the Forest Stewardship Council and enter them in the Forestry Commission's woodland grant schemes. For example, a scheme at Carsington Water manages the landholding to benefit woodland birds while also holding water, so it's slowly released into catchments. We also liaise with community groups such as bird clubs, to monitor the numbers and species of birds on and around our reservoirs. Volunteer groups have helped create biodiversity habitats such as new ponds, manage reed beds and restore wildflower grasslands

Objective 8. We will protect the wider environment

Water and sewage treatment is energy intensive. We've been reporting our carbon emissions performance for more than a decade and have consistently reduced our emissions and costs, through energy efficiency, renewable energy production, improved metering and more effective use of transport. In 2013/14, our emissions totalled 511 kilo tonnes of CO₂e, a reduction of 9%. Our plan is to reduce our carbon emissions by 3% in AMP6

We've had Carbon Trust Standard accreditation since 2009 and contribute to the Carbon Disclosure Project (CDP). We've seen a year on year improvement in our CDP score, which is above the FTSE 100 average

This year, we achieved 100% compliance on satisfactory sludge disposal and implemented a new IT system to modernise our compliance monitoring and control. We also invested in biosolids storage, to mitigate the effects of severe weather, and trialled innovative solutions to ensure we can recycle biosolids during challenging weather

We've built a sector leading position in renewable energy, which now provides 23% of our energy requirements. A number of these processes use by-products or essential features of our water or sewage treatment, and are classed as part of our regulated business. During the year, we installed more efficient combined heat and power units at our largest sewage treatment works, to increase output by 10%. We're also building our first, and the UK's largest, bio-methane injection plant at Minworth, Birmingham

Objective 9 We will make a positive difference in the community

Our activities bring broad economic and social benefits to our region. According to research we commissioned from Coventry University, for every £1 we invest £1.66 is generated and retained in the regional economy (figures from 'Making a Difference', a Severn Trent Water report). With an investment programme of around £600 million in 2013/14, our contribution is considerable

We're also a major employer, of more than 5,900 people. We help young people into work through our apprenticeships and currently have more than 80 apprentices in our operations and customer services. As well as benefiting the young people involved, this helps secure the skills we'll need in the coming years

Educating our current and future customers is also key to helping people understand how to use water efficiently and what can be safely disposed of in our sewers. Our schools education programme reaches more than 45,000 children each year, so they understand the value of water. We've extended this with our company-wide Water Champions volunteering programme. This allows our people to create fun and educational water efficient gardens in local primary schools, which they can incorporate into everyday learning. This engages our local communities, while improving our people's skills and building working relationships. Also, in 2013 we were a sponsor of the Big Bang event in our region. The national Big Bang programme is the largest promotional event for science, technology,

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engineering and maths for young people in the UK and the regional event at the Ricoh Arena in Coventry, UK, involved nearly 4,000 schoolchildren

Our local communities are actively involved in helping the running of our visitor sites, volunteering nearly 20,000 hours each year on conservation, maintenance activity and providing excellent customer service. Last year we invested over £1.1 million in our visitor sites and over three million customers visited our sites during 2013, highlighting our continued commitment to offer high levels of conservation, access and recreation across our region. At Draycote Water, our reservoir site near Rugby, we have spent £330,000 over two years remodelling and refurbishing the visitor centre, building a children's play area and increasing parking facilities. Since its re-opening in April 2013 we have seen an increase in visitor numbers of almost 56%.

Sustainable finance

Objective 10 We will finance our business sustainably

We aim to finance our business sustainably, so we can invest now to protect our future services. We avoid excessive debt, which would transfer risk to our customers, and look for a sustainable mix of debt finance at the right cost, reflecting the long term nature of our investment.

Our financing needs are and will remain substantial. In AMP6 our plan suggests we will need to raise around £2.6 billion in new and refinanced debt which means it will be necessary to maintain an investment grade credit rating. Our long term credit ratings are BBB+ (Standard and Poor's) and A3 (Moody's). These are in line with regulatory assumptions and were unchanged during the year. Our gearing and interest cover remain prudent – further details can be found in the Financial review on pages 23 to 29.

Great people

To achieve our objectives, we have a flexible workforce, with people who are willing to work in new ways, embrace new skills and focus on our customers' needs.

Our employee survey showed our highest level of engagement in eight years, our engagement index reaching 81%. This compares with 79% last year and 75% for other benchmarked companies.

Particular strengths included health and safety, where our people understand our commitment and their own responsibility for working safely. Our Code of Conduct, 'Doing the right thing - the Severn Trent way', explains our approach to issues ranging from bribery and corruption to excellent customer service. Our people recognise their responsibility for complying with the Code of Conduct and our focus on doing the right thing, reflecting our continued training and engagement in this area. They also understand how the company's goals and their role contributes to the customer experience and are happy to go the extra mile when required.

As always, there are areas where we can improve. In common with many organisations, our people think we could be better at handling and communicating change. They also want us to simplify our processes, reflecting the number of new systems and processes we've introduced in recent years. In response to feedback from last year's survey, members of the Executive Committee have held events around the business meeting teams and sharing our future plans. We continue to hold events around the business, allowing employees to ask about our business and contribute their ideas.

Excellent health and safety

No one should get hurt or made unwell by what we do. We've sustained our lost time incident (LTI) rate at 0.21 per 100,000 hours worked (2012/13 0.21), making us the leaders in our industry. Particular achievements included our Water Production team working for an entire year without an LTI.

We've done this through further investment and training. Our ongoing MindSafety® training programme helps our people to understand how they should work and take responsibility for their own safety.

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We've also implemented site based safety improvement teams. This gives our people ownership of the issues and allows them to fix the day-to-day problems that can affect their health, safety and wellbeing. Our proactive approach to health, safety and wellbeing continues to improve, with around 15,000 hazards identified and resolved per month.

Occupational health has been a focus for us this year. We've introduced a physiotherapy and rehabilitation service for those suffering with musculoskeletal problems, which has reduced employee absence by more than 1,000 days.

We've also developed 'Fit for the Future', which is part of our bespoke injury prevention programme. This programme not only trains people in safe and efficient manual handling but provides health and nutrition advice to support our employees in maintaining a healthy and productive career. The programme won Rehabilitation Initiative of the Year at the Rehabilitation First awards.

Our next area of focus will be mental health. We've taken part in Time to Change, England's biggest programme to end stigma and discrimination for people with mental health problems. We want to identify the gaps between supporting people with mental health issues and taking practical action. We've surveyed our people and are educating managers and employees about building personal resilience to better manage challenges at home and in work.

Developing our people

We've continued to roll out our Leading for Performance programme. This develops leaders who can coach their teams and inspire greater levels of performance. We've also run development centres for 80 managers, benchmarking them externally and internally, and helping them to create high quality personal development plans.

We continue to develop our line managers through our Line Manager Journey. So far, we've trained nearly 700 people in a range of core management skills. We've invested in IT and business skills, as well as project and programme management, with 850 training days this year in those areas.

Our Future Skills strategy encompasses our apprentice and graduate programmes. We've taken on more graduates this year, employing 20 for general leadership training and we have introduced a technical engineering programme for graduates.

A diverse workforce

A diverse and inclusive culture is important for business success. Our approach is based on doing the right thing and we're working to ensure our policies, processes and practices are open, fair and transparent.

We monitor our performance against a range of diversity measures and benchmarks, so we can use the data to inform our actions. Our workforce is slightly more diverse than the sector average. 31% of our employees are women compared to the industry average of 28.9%. 7.5% of our employees are Black, Asian & Minority Ethnic (BAME) compared to the industry average of 2%. We're building a diversity and inclusion plan to address particular areas of improvement. Our current focus is on attracting more women into operational leadership roles and ensuring that our frontline operational roles are attractive to BAME candidates. To support our goals we have carried out a complete review of our job descriptions and advertising strategy and trained over 320 managers in effective interview techniques.

Rewarding our people

We look to offer innovative rewards for our people, with a strong link to improving business performance. Through our flexible benefits scheme ('Lifestyle') employees can choose certain benefits, such as buying or selling annual leave days. We also offer a range of products, where we can use our buying power to offer employees discounts. Lifestyle won the Best Flexible Benefits Scheme at the Employee Benefits Awards in June 2013.

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Outlook

The next 12 months will see us complete the delivery of our AMP5 plan

In the coming months we will also finalise our plan for AMP6, so we can continue to deliver for our customers, employees and the environment. We'll ensure we're in a position to start delivering it from day one of AMP6.

Ofwat has committed to publishing its final determination of all companies' plans by 12 December 2014.

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Financial performance

The company has delivered a good financial performance overall with year on year improvements in turnover and underlying PBIT

Costs that we directly control were held at inflation, while other costs over which we have less direct influence, notably power costs, continued to increase at levels higher than inflation, a trend we have seen in prior years. We maintained our good performance on bad debts at 2.2% of turnover (UK GAAP), which is creditable in the current climate where household incomes remain under pressure. We continued to sustain our planned investment in the assets and infrastructure that support this long term business with total capital expenditure at £602 million up 8% on the prior year though infrastructure maintenance expenditure included in this figure and expensed under IFRS accounting rules was down £7.4 million (5%) driven by shorter term operational requirements.

With no substantial change in financing structures this year, finance costs increased to £245.2 million (2013: £236.3 million) largely as a result of the higher level of net debt.

PBIT is profit before interest and tax, underlying PBIT is PBIT excluding exceptional items as set out in note 6. Prior year comparative figures have been restated, where indicated, for the change in the accounting policy for retirement benefits. The impact is to decrease profit previously reported by £11.5 million, with an equal and opposite movement in reserves.

Results

Turnover in Severn Trent Water increased by 2.2% in 2013/14, to £1,544.8 million. Prices were increased by 1% less than November 2012 inflation of 3.0% from 1 April 2013 which gave rise to an increase in turnover of £29.8 million. The 2013 dry summer led to higher consumption from metered customers and overall increased metered consumption year on year increased turnover by £7.1 million. Growth, net of the impact of meter optants, increased turnover by £1.3 million which was offset by other decreases amounting to £4.4 million.

Underlying PBIT increased by 4.2% to £516.4 million.

Operating costs increased by 2.8% to £602.4 million in line with expectations. Depreciation increased by £3.3 million due to the impact of capital expenditure increasing the size of the asset base and there was a decrease in infrastructure renewals expenditure of £7.4 million.

Directly managed costs increased below the level of inflation at 2.8% year on year, reflecting effective cost management, while indirectly managed costs, over which we have less control, increased by 2.9%.

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	2014	2013	Increase/ (decrease)	
	£m	£m	£m	%
Directly managed costs				
Employee costs	239.5	228.0	11.5	5.0
Hired and contracted	154.2	147.6	6.6	4.5
Raw materials and consumables	42.5	43.4	(0.9)	(2.1)
Other	49.9	50.9	(1.0)	(2.0)
Costs capitalised	(92.6)	(87.1)	(5.5)	6.3
	393.5	382.8	10.7	2.8
Indirectly managed costs				
Bad debts	31.3	31.8	(0.5)	(1.6)
Power	65.3	60.6	4.7	7.8
Rates and service charges	112.3	110.1	2.2	2.0
	208.9	202.5	6.4	3.2
Operating costs	602.4	585.3	17.1	2.9

Exceptional operating items

There was an exceptional credit of £8.2 million arising from the disposal of a number of properties during the year (2013: £13.3 million credit)

Net finance costs

Net finance costs increased by 3.8% to £245.2 million. Interest payable increased to £332.2 million (2013: £324.9 million) and interest receivable and similar income fell by £1.6 million to £87.0 million.

RPI was lower year on year resulting in a reduction in the non-cash interest charge. This was offset by an increased cash interest charge on a higher level of net debt. Changes to the accounting standard IAS19 have resulted in an increase of £17.2 million in net pension finance cost (prior year figures have been restated by £12.4 million).

Gains/(losses) on financial instruments

The company uses financial derivatives solely to hedge risks associated with its normal business activities including

- Exchange rate exposure on borrowings denominated in foreign currencies,
- Interest rate exposures on floating rate borrowings, and
- Exposures to increases in electricity prices

These risks are managed centrally by the Severn Trent group treasury department. Derivative financial instruments are not held for trading.

Accounting rules require that these derivatives are revalued at each balance sheet date and, unless the criteria for cash flow hedge accounting are met, the changes in value are taken to the income statement. If the risk that is being hedged does not impact the income statement in the same period then an accounting mismatch arises from the hedging activities and there is a net charge or credit to the income statement.

Where the derivatives are held to their full term, these mismatches are expected to net out. Furthermore, the changes in value that are recorded during the lives of the derivatives, unless crystallised, do not represent cash flows. Therefore the group presents adjusted earnings figures that exclude these non-cash items. An analysis of the amounts credited to the income statement in the period is presented in note 11 to the financial statements.

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Profit for the year

Profit for the financial year was £492.2 million (2013 £239.2 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 2014 post tax return on capital was 6.4% (2013 6.7%).

Taxation

The current year tax charge for 2013/14 before exceptional items was £56.9 million (charge of £33.5 million). This includes a charge of £9.4 million arising from adjustments to prior year tax computations. In the previous year adjustments to prior year tax computations resulted in a current tax credit of £27.2 million, primarily due to an industry agreement over the treatment of infrastructure income in those computations.

An exceptional current tax credit of £59.2 million has been recognised, reflecting the anticipated refund of overpayment of tax in prior periods as HMRC has now agreed that certain capital expenditure within our water and waste water treatment works is eligible for capital allowances as plant and machinery. This has also resulted in an exceptional deferred tax credit of £56.2 million.

In the prior year the group's UK subsidiary companies adopted the new accounting standard FRS 101, which changed the basis for those companies' corporation tax computations. The most significant impact of this change is that certain amounts that had been taxed in previous years were recognised as profits and will be taxed in future periods. Therefore, to prevent such items being taxed twice, the tax already paid on such items was 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 Finance Act 2013 was enacted in the period and implemented a reduction in the corporation tax rate from 23% to 21% with effect from 1 April 2014 and then to 20% with effect from 1 April 2015. This has resulted in a further deferred tax credit of £119.3 million in the income statement and a deferred tax charge of £11.3 million in reserves.

The total tax credit for the year was £163.2 million (2013 credit of £16.1 million).

See note 12 in the financial statements for further detail.

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Cash flow

	2014 £m	2013 £m
Cash generated from operations	774 4	757 9
Net capital expenditure	(441 2)	(392 6)
Net interest paid	(198 5)	(229 2)
Tax paid	(14 5)	(53 5)
Free cash flow	120 2	82 6
Dividends	(337 6)	(72 0)
Net issue of shares	(2 8)	(1 4)
Change in net debt from cash flows	(220 2)	9 2
Non cash movements	(46 0)	(120 5)
Change in net debt	(266 2)	(111 3)
Net debt 1 April	(4,578 2)	(4,466 9)
Net debt at 31 March	(4,844 4)	(4,578 2)
Net debt comprises		
Cash and cash equivalents	19 8	328 6
Loans receivable from other group companies	107 0	121 2
Loans payable to other group companies	(4,005 4)	(3,917 5)
Bank loans	(555 2)	(717 7)
Finance leases payable	(307 0)	(317 4)
Intercompany finance leases payable	(210 7)	(213 3)
Finance leases receivable from other group companies	101 3	101 8
Cross currency swaps	5 8	36 1
	(4,844 4)	(4,578 2)

Cash generated from operations was £774.4 million (2013 £757.9 million). Capital expenditure net of grants and proceeds of sales of fixed assets was £441.2 million (2013 £392.6 million). Net interest paid decreased to £198.5 million (2013 £229.2 million).

Net debt at 31 March 2014 was £4,844.4 million (2013 £4,578.2 million). Balance sheet gearing (net debt/net debt plus equity) at the year end was 82.4 (2013 84.1). The company's net interest charge, excluding gains/(losses) on financial instruments and net finance costs from pensions, was covered 3.5 times (2013 3.5 times) by profit before interest, tax, depreciation and exceptional items, and 2.3 times (2013 2.3 times) by underlying PBIT.

Treasury management and liquidity

The company's principal treasury management objectives are

- to access a broad range of sources of finance to obtain both the quantum required and lowest cost compatible with the need for continued availability,
- to maintain an investment grade credit rating, and
- to maintain a flexible and sustainable balance sheet structure

The company continues to carefully monitor liquidity. At 31 March 2014 the company had £19.8 million (2013 £328.6 million) in cash and cash equivalents and committed undrawn facilities amounting to £500 million (2013 £500 million), of which £200 million is jointly held with Severn Trent Plc. Average debt maturity is around 16 years. The company is funded for its investment and cash flow needs up to January 2015 without recourse to committed facilities or new debt.

Cash is invested in deposits with highly rated banks and liquidity funds and the list of counterparties is regularly reviewed.

Strategic report

Financial review

Treasury policy and operations

The company's treasury affairs are managed centrally as part of the Severn Trent Plc group and in accordance with our Treasury Procedures Manual and Policy Statement. The treasury operation's role is to manage liquidity, funding, investment and our 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 determines matters of treasury policy and its approval is required for certain treasury transactions.

The group strategy is to access a broad range of sources of finance to obtain both the quantum required and lowest cost compatible with the need for continued availability. Severn Trent Water, is a long term business characterised by multi year investment programmes. The group's strategic funding objectives reflect this and the liquidity position and availability of committed funding are essential to meeting our objectives and obligations. The group aims for a balance of long term funding or commitment of funds across a range of funding sources at the best possible economic cost.

The company uses financial derivatives solely to manage risks associated with our normal business activities. The company does not hold or issue derivative financial instruments for financial trading.

Except for debt raised in foreign currency, which is fully hedged, our business does not involve significant exposure to foreign exchange transactions. We have investments in various assets denominated in foreign currencies, principally the US dollar and the euro. Our current policy is to hedge an element of the currency translation risk associated with certain foreign currency denominated assets.

The company uses cross currency swaps to convert currency debt to sterling. The effect of these swaps is that interest and principal payments on the borrowings are denominated in sterling and hence the currency risk is eliminated. The foreign currency notes and the cross currency swaps are recorded in the balance sheet at their fair values and the changes in fair values are taken to gains/(losses) on financial instruments in the income statement. Since the terms of the swaps closely match those of the underlying debt, such changes tend to be broadly equal and opposite.

The company holds interest rate swaps with a net notional principal of £361.2 million and cross currency swaps with a net notional principal of £73.6 million which economically act to hedge the interest rate risk on floating rate debt or the exchange rate risk on certain foreign currency borrowings. However, the swaps do not meet the hedge accounting rules of IAS 39 and therefore the changes in fair value are taken to gains/(losses) on financial instruments in the income statement. During the year there was a credit of £40.1 million in relation to these instruments.

The company has entered into a series of forward starting interest rate swaps with a notional principal amount of £450 million that hedge the interest rate risk on the anticipated borrowing requirements for AMP5. These swaps are treated as cash flow hedges and the changes in fair value are taken to other comprehensive income. During the year swaps with a notional principal amount of £225 million reached their start dates. Hedge accounting for these swaps was terminated as at 1 April 2013 because the company was not able to identify specific debt instruments that would qualify as the hedged items in a future hedging relationship. The fair value held in other comprehensive income at the date of termination will be amortised to the income statement over their remaining lives. This led to a charge of £4.6 million in the year.

The company manages its electricity costs through a combination of self generation forward price contracts and financial derivatives. All of our external power requirements for the first four years of AMP5 and most of the remaining year have been hedged in this way, at prices below those allowed in the Final Determination.

Strategic report

Financial review

The company's long term credit ratings are

Long term ratings

Moody's	A3
Standard and Poor's	BBB+

Pensions

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 policy statement for allocating the net defined benefit cost to individual group entities this company has recognised the full cost and deficit. However, the company only makes contributions for its own employees.

The group operates two defined benefit pension schemes, of which the UK Severn Trent Pension Scheme (STPS) is by far the largest. Formal triennial actuarial valuations and funding agreements as at 31 March 2013 for the STPS and the other smaller defined benefit pension scheme have been agreed and renewed in the year. Deficit reduction contributions in total include a payment of £40 million in 2013/14, £35 million in 2014/15, £15 million in 2015/16 and then £12 million per annum in subsequent years to 2024/25. Further payments of £8 million per annum through an asset backed funding arrangement will also continue to 31 March 2032.

As previously announced, the final salary sections of the pension schemes will close to future accrual on 31 March 2015. The final salary sections were closed to new entrants in 2006. Consequently the age profile of scheme participants is expected to rise and hence service costs are also expected to rise until future accrual ceases in 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 key actuarial assumptions for the defined benefit schemes have been updated for these accounts. On an IAS 19 basis, the estimated net position of the schemes was a deficit of £348.3 million as at 31 March 2014. This compares to a deficit of £383.7 million as at 31 March 2013. The movements in the net deficit are summarised in note 33. The funding level has increased to 84.0% (2013: 81.8%).

The major assumptions used in the valuation of the defined benefit pension schemes were as follows:

	2014	2013
Price inflation	3.3%	3.2%
Pension increases in payment	3.3%	3.2%
Pension increases in deferment	3.3%	3.2%
Discount rate	4.4%	4.4%
Remaining life expectancy for members currently aged 65 (years)		
- men	21.3	21.5
-women	24.4	24.6
Remaining life expectancy for members currently aged 45 upon retirement at 65 (years)		
- men	22.6	22.7
-women	26.0	26.2

Strategic report

Financial review

The following table summarises the estimated impact on scheme liabilities 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

Strategic report

Risk management

Our approach to risk

We manage risks within the overall governance framework which includes clear accountabilities, delegated authority limits and reward policies. These are designed to provide employees with an holistic view of effective risk management.

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

Our Enterprise Risk Management Process.

We use an established Enterprise Risk Management (ERM) process to assess and manage our most significant risks which are linked to our business objectives. Our ERM process covers all types of risk including operational, financial and legal and regulatory.

Our process considers both the possible causes of risk and what the impact would be if a risk crystallised. This enables us to consider the controls needed to minimise the likelihood of risks occurring and those which can help to maximise our resilience to risks. Resilience of our services is vital and we regularly carry out exercises jointly with other agencies such as local authorities, police and fire services. During the year we have also started an extensive training programme to increase the number of trained staff available to respond to incidents.

Key risks are reported to the Severn Trent Plc Audit Committee and discussed at the board every six months in the form of risk maps. In addition, individual risks or specific risk topics are also discussed by the board during the year. We have regular risk 'deep dives' at our executive team meetings. These take the form of updates from individual business teams on their progress with improving controls and providing effective mitigation for their most significant risks.

Risk Appetite

During the year the board held a series of discussions about our appetite for risk from four key perspectives: consistency with our culture and values, delivering what our customers need, retaining the confidence of our investors and compliance with the regulatory regime in which we operate.

The board will continue to work on refining our approach to risk appetite in the coming year. The board discussions on risk appetite, in the context of our strategy, influence the outcome of the ERM process and, in particular, how we establish an appropriate target position for each significant risk.

Financial Risks

Like all businesses, we need to plan future funding in line with business need. This is part of our normal business planning process (see Principal Risk Ref 4). The board receives regular updates relating to funding, solvency and liquidity matters.

Strategic report

Risk management

Principal Risks:

The board considers that the following represent the Principal Risks facing Severn Trent Water

Ref	What is the risk?	What does it mean for us?	What are we doing to manage the risk?
Customer perception			
1	We may be unable to improve and maintain our levels of customer service sufficiently to deliver what our customers tell us they want	<p>Failure to deliver the service customers expect will lead to customer dissatisfaction. As a regulated utility providing essential services, we recognise that customer trust is vital for us to maintain legitimacy.</p> <p>If we are unable to provide the level of service we want to our customers we may also suffer financial penalties under Ofwat's SIM.</p>	<p>We have co-ordinated programmes of work underway across all parts of Severn Trent Water to improve our processes and our technology to enable us to deliver outstanding customer service.</p> <p>Our performance as measured by Ofwat's SIM measure continues to improve. However, we are not improving as fast as some of our competitors and our performance is still not as good as we would like.</p> <p>We have set ourselves more challenging targets and our customer experience improvement programmes are working to deliver these at a faster rate for our customers.</p>
2	We may be unable to take full advantage of the opportunities presented by the opening up of the business retail market to competition	We may lose income as a result of business retail customers moving to competitors or we may fail to successfully grow our business by being unable to develop sufficiently attractive services to win new customers	Within Severn Trent Water our strategy reflects the needs of different groups of customers – whether large or small businesses and whether water is critical to their operations. We are developing our service offering which includes, for example, services to help customers understand and reduce their water consumption.
Legal and regulatory environment			
3	We may be unable to effectively anticipate and/or influence future developments in the UK water industry resulting in our business plans becoming unsustainable	We operate in a highly regulated environment. Whilst we are broadly content with the direction of changes proposed for our industry, there remains a risk that future changes could have a significant impact on Severn Trent Water.	During the year we published the fourth in our "Changing Course" series – "Changing Course through the Sustainable implementation of the Water Framework Directive" which sets out our view on an approach to implementation which is affordable for our customers. We also commissioned a report from KPMG looking at the challenges and possible solutions for

Strategic report
Risk management

Ref	What is the risk?	What does it mean for us?	What are we doing to manage the risk?
			<p>sustainable investment to maintain the water infrastructure</p> <p>We will continue to engage with our peers, Ofwat and other regulators, UK Government departments and other stakeholders to inform the direction of regulatory policy where appropriate</p>
4	<p>We may be unable to develop and deliver a 5 year business plan which is acceptable to Ofwat, our customers, other stakeholders and which is financeable within the assumptions we have used</p>	<p>We submit a business plan to Ofwat every 5 years. At each of these price reviews, we have a risk that changes will be required to our plan to meet Ofwat's expectations</p> <p>Once plans have been agreed, we face risks to delivery of the plan within the constraints and assumptions that we have adopted</p> <p>Failure to achieve the targets set out in our agreed plan for the current price review period could result in Ofwat being less willing to support our business plan submission for the next price review period and could result in additional funding requirements in the current period</p>	<p>We are using our established business planning processes to update our plan for the 2015-2020 price review period. We are engaging with Ofwat in order to respond to the feedback from their Risk Based Review. We will be submitting an updated proposal in June which reflects Ofwat's feedback, the Risk and Reward guidance and the views of our customers</p> <p>We are reviewing progress against the plan agreed for the current price review period to confirm that we expect to achieve the agreed targets or that we have included appropriate compensation in our plan for the next period where we have failed to fully deliver the required service levels and outputs</p> <p>We will continue to engage with our customer challenge group (the Water Forum) to ensure that we continue to respond to our customers when refining our plan</p>
5	<p>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</p>	<p>Our policies and processes must reflect the current legal and regulatory environment and all relevant employees must be kept aware of new requirements. Due to the spread of our operations, and changes in activity and organisational structure this is not always straightforward</p>	<p>During the year, we have maintained our focus on raising awareness of updated policies via e-learning, face to face coaching and general communications. These communications include reminders of the principles of our Code of Conduct, Doing the right thing the Severn Trent way</p> <p>We are reviewing our methods of obtaining assurance in relation to compliance issues to ensure we have a consistent approach for all</p>

Strategic report

Risk management

Ref	What is the risk?	What does it mean for us?	What are we doing to manage the risk?
			key obligations, including licence conditions, competition legislation and anti-bribery and corruption legislation
Operations, assets and people			
6	Our assets or processes may fail resulting in injury to an employee, contractor or member of the public	The nature of our work requires our employees and contractors to undertake activities or to use equipment which have potential to cause serious harm Whilst we take every precaution to prevent injury, asset failure or failure to follow agreed processes may result in someone being hurt Specific examples include failure of one of our key assets such as a reservoir which could result in injury to customers or the public	<p>Our ongoing strategy for Health, Wellbeing and Safety covers improving the management system, addressing the causes of incidents and improving health and wellbeing</p> <p>During the year, we have delivered a number of improvements including a new reporting system and a new standard for local safety improvement teams Our next steps include implementing new approaches to our safety standards and risk assessment</p> <p>In addition, to learning lessons from incidents, we continue to measure improvements in culture and the belief in our vision as well as substantial proactive safety activity to identify and remove hazards</p> <p>Our assets are subject to regular and rigorous monitoring including independent inspection of our reservoirs to ensure that they remain safe and that maintenance work is undertaken where needed</p> <p>We will continue with our programme of safety improvements and with our rigorous monitoring and maintenance regimes for critical assets</p>

Strategic report

Risk management

Ref	What is the risk?	What does it mean for us?	What are we doing to manage the risk?
7	We may fail to meet all of our regulatory targets including targets from Ofwat in relation to operational performance of our assets resulting in regulatory penalties	<p>If we are unable to meet operational performance targets, we may be subjected to significant regulatory penalties either within the current price review period, or applied to the next price review</p> <p>Regulatory targets apply to all of our water treatment, distribution, sewerage and sewage treatment assets. Measures are in place in relation to water quality, continuous supplies, sewer flooding, sewer collapses and pollution events</p>	<p>We continue to focus on finding and clearing blockages in our sewers and on our education programmes to help customers understand how to use our assets responsibly</p> <p>Our business plan for 2015-2020 includes considerable investment in our above ground water assets to improve the resilience of our networks, reduce interruptions and improve the service that our customers receive</p>
8	Failure of certain key assets or processes 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	<p>Some of our assets are critical to the provision of water to large populations for which there are limited alternative means of supply. These assets are regularly inspected and maintained and our assessment of the overall condition is good. If a failure were to occur the consequence would result in temporary inability to continue to serve our customers</p> <p>In addition, our IT and telephony systems are critical to our operations and failure of these systems, for example materialization of a cyber threat affecting our remote monitoring system, could have a significant effect</p>	<p>During the year, as part of our planning for the next price review period from 2015-2020, we have undertaken extensive surveys of some of our largest, most critical assets. As a result we have a better understanding of the specific points around our network which could present a threat to our continuous operation. This has helped us to prioritise our spending requirements and informed our asset management plans which drive investment in maintenance and improvement of our assets in order to maintain our service to customers</p> <p>During the year we have progressed work on implementing dual data centres to provide increased resilience for our key IT systems. We have also assessed the security of our systems in line with the '10 Steps to Cyber Security' managed by CESG</p> <p>Our business strategy for 2015-2025 includes significant investment to improve the resilience of our network, particularly by improving our ability to move water around our network</p> <p>We also have security measures to protect our assets and contingency plans to maintain supplies in the event of failure</p>

Strategic report

Risk management

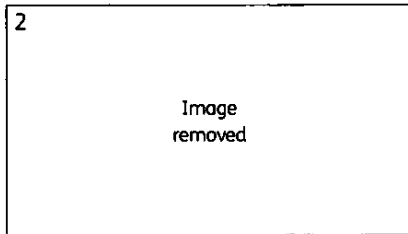
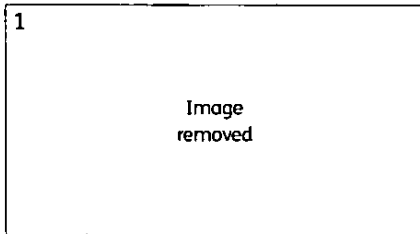
Ref	What is the risk?	What does it mean for us?	What are we doing to manage the risk?
Financial risks			
9	Changing demographics and fluctuations in the investment market may affect our ability to fund pensions promises sustainably	We provide significant funding for our schemes We may be called upon to provide more money to reduce deficits in our pensions schemes	We regularly revalue our schemes and monitor our investment performance We will continue to monitor the performance of our pensions investments and to work closely with our third party advisors to ensure that the schemes are managed effectively

The Strategic report, as set out on pages 1 to 35, has been approved by the board
By order of the board



Bronagh Kennedy
General Counsel and Company Secretary
28 May 2014

Board of directors

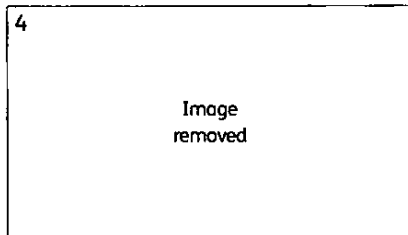
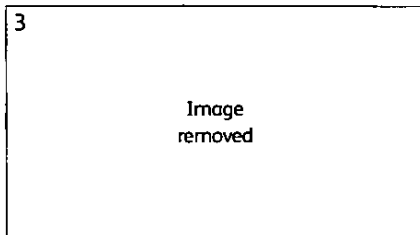


1 Dr Tony Ballance

BSc (Hons) MA (Econ) PhD (49)
 Director, Strategy and Regulation
 Appointed to the board on 2 October 2007
 Tony's extensive experience in utility policy and regulation leaves him ideally placed to lead the company's strategic and regulatory work
 Prior to joining Severn Trent he held the posts of Chief Economist for Ofwat, director of London Economics and director of Stone and Webster Consultants

External appointments

Member of Water UK Council

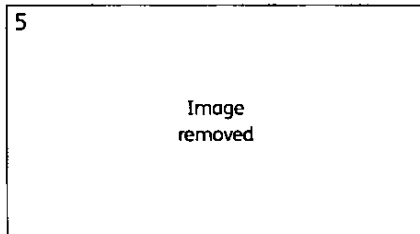


2 John Coghlan

BCom ACA (56)
 Independent non-executive director
 Appointed to the board on 23 May 2014
 John is a chartered accountant with substantial financial expertise and is a valuable addition to the board's existing skill set. He will become Chairman of the Audit Committee with effect from the conclusion of the AGM on 16 July 2014. John is currently Chairman of Inchcape Shipping Services and a non-executive director and Chairman of the Remuneration Committee of Lavendon Group plc. He was previously a non executive director of Hibu plc (formerly Yell Group plc) from June 2002 to February 2014 and Chairman of the Audit Committee. Prior to this he was a non-executive director of Ashley House plc and DX Services PLC and until 2006 he was Deputy Chief Executive and Group Finance Director of Exel Plc

External appointments

Chairman of Inchcape Shipping Services
 Non executive director and Chairman of the Remuneration Committee of Lavendon Group plc
 Chairman of Freight Transport Association Ireland Limited

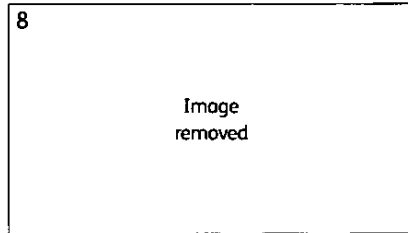
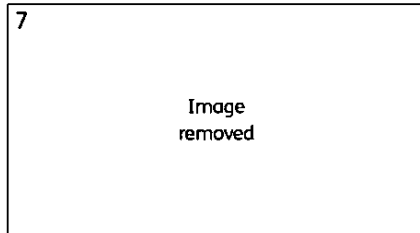


3 Richard Davey

BA (65)
 Senior independent non-executive director
 Appointed to the board on 1 January 2006
 Richard spent the majority of his executive career in investment banking at NM Rothschild and Sons, in roles including Head of Investment Banking. Richard brings invaluable specialist financial expertise to the board, the Audit Committee and as chair of the Remuneration Committee, having run Rothschild's Financial Services Group and worked with a number of high street banks and insurers. Previously he held non-executive roles at Yorkshire Building Society, where he was Vice Chairman, Freeserve Plc and Scottish Widows Fund and Life Assurance Society

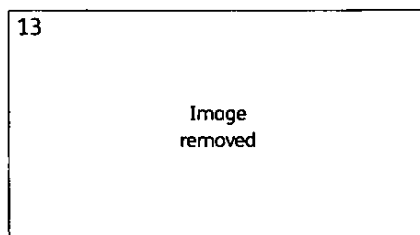
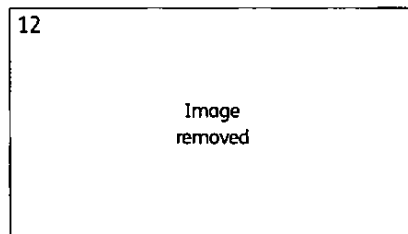
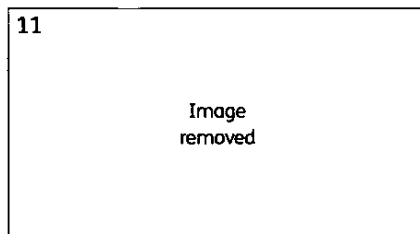
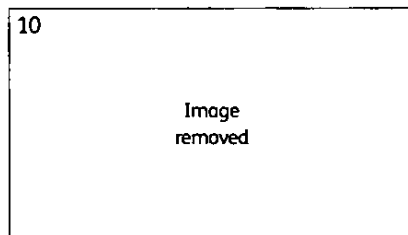
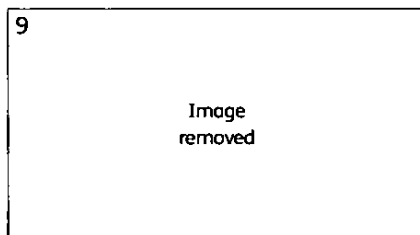
External appointments

Non-executive Chairman, member of the Risk and Solvency Committee and Chairman of the Nomination Committee of Armlin Plc



4 Andrew Duff

BSc FEI (55)
 Non-executive Chairman
 Appointed to the board on 10 May 2010 and Chairman on 20 July 2010
 Andrew's extensive experience of international and regulated business, strategic management and customer service in high profile, dynamic environments have equipped him well for the role of Chairman of the group. Andrew spent 16 years at BP in marketing, strategy and oil trading. He joined National Power in 1998 and the board of Innogy plc upon its demerger from National Power in 2000. He led the restructuring and subsequent sale of Innogy to RWE in 2003. He became CEO of the successor company, npower, and a member of the RWE Group Executive Committee. He was a non executive director of Wolsley Plc from



Governance

July 2004 until his retirement in November 2013
Andrew was appointed non-executive Deputy Chairman of Elementis plc on 1 April 2014 and became non-executive Chairman of Elementis plc on 24 April 2014

External appointments

Non-executive Chairman and Chairman of the Nomination Committee of Elementis plc
Member of the CBI President's Committee
Trustee of Macmillan Cancer Support and Earth Trust
Fellow of the Energy Institute

5 Gordon Fryett

(60)

Independent non-executive director

Appointed to the board on 1 July 2009

Gordon has extensive experience working in and with international businesses, managing significant capital expenditure. His in-depth retail expertise at both executive and operational level in a customer facing, highly competitive environment, enables him to bring substantial experience and expertise to the board and the Corporate Responsibility Committee. Gordon held the position of Group Property Director at Tesco Plc until his retirement in November 2013. He previously held a number of senior roles within the Tesco Group, including Operations Director, International Support Director and CEO Republic of Ireland.

External appointments

Alumnus of INSEAD

6 Olivia Garfield

BA (Hons) (38)

Chief Executive

Appointed to the board on 11 April 2014

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

External appointments

Non-executive director Tesco Plc

7 Martin Kane

BSc CEng CEnv MICE MIWEM FIW (61)

Non-executive director

Appointed to the board on 2 October 2007

Martin joined Severn Trent Water in 1975 and has held various senior roles giving him an extensive and unique understanding of the design, construction and operation of water and waste water treatment plants, water distribution networks and sewerage systems. Martin was Director of Customer Relations, Severn Trent Water, from May 2006 until January 2012, when he was appointed Chief Executive Officer of Severn Trent Services.

External appointments

Member of the boards of Utilities and Service Industries Training Limited and National Association of Water Companies (US)
Trustee of International Society for Trenchless Technology

8 Martin Lamb

BSc MBA (54)

Independent non-executive director

Appointed to the board on 29 February 2008

Martin has extensive experience of managing and developing large engineering businesses in all parts of the world. In May 2014, Martin left the board of IMI plc having served as Chief Executive for 13 years and after 33 years with the company. He oversaw the fundamental reshaping of IMI and held a number of senior management roles there. On 1 March 2014, Martin was appointed Chairman of Evoqua Water Technologies. His strong commercial acumen, experience of managing complex projects, and familiarity with current market pressures leave him well placed to add value to the Severn Trent business. Previously Martin was a non-executive director of Spectris plc.

External appointments

Chairman of Evoqua Water Technologies LLC
Member of the Advisory Board of AEA Investors Management (UK) Limited

9 Michael McKeon

MA CA (57)

Finance Director

Appointed to the board on 13 December 2005

Michael brings significant financial and commercial expertise to the board and has over eight years' experience of the Severn Trent group. Prior to joining Severn Trent he was Finance Director of Navar Plc and before that, held various senior roles with Rolls-Royce Plc, including Finance Director of the Aerospace Group. He has extensive international business experience having worked overseas for CarnaudMetalbox, Elf Atochem and Price Waterhouse. Michael is a chartered accountant and a member of the Institute of Chartered Accountants of Scotland.

External appointments

Non-executive director and Chairman of the Audit Committee of The Merchants Trust Plc

10 Baroness Noakes

DBE LLB FCA (64)

Independent non-executive director

Appointed to the board on 29 February 2008

Sheila brings valuable expertise to the board as an experienced director and Audit Committee Chairman of UK listed companies and with extensive and varied professional, political and public sector experience. A qualified chartered accountant, she previously headed KPMG's European and International Government practices and has been President of the Institute of Chartered Accountants in England and Wales. Sheila was appointed to the House of Lords in 2000 and has served on the Conservative front bench in various roles including as shadow treasury minister between 2003 and May 2010. Previously she held non-executive roles on the Court of the Bank of England, Hanson Plc, ICI Plc, John Laing and SThree. Sheila will retire from the board with effect from the conclusion of the 2014 AGM.

External appointments

Non-executive director, member of the Group Audit Committee and Group Nominations Committee and Chairman of the Board Risk Committee of The Royal Bank of Scotland Group Plc
Deputy Chairman, senior independent director and Chairman of the Nominations Committee of Carpetright Plc

11 The Hon Philip Remnant

CBE ACA MA (59)

Independent non-executive director

Appointed to the board on 31 March 2014

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

External appointments

Senior independent director and member of the Audit, Nominations and Remuneration Committees of Prudential Plc
Deputy Chairman of the Takeover Panel
Non-executive director of UK Financial Investments Limited
Non-executive Chairman of City of London Investment Trust plc
Governor of Goodenough College
Trustee of St Paul's Cathedral Foundation

12 Andy Smith

BTech (Hons) (53)

Director of Water Services

Appointed to the board on 2 October 2007

Andy brings a broad range of executive and operational expertise gained from diverse sectors to the board. Andy has significant experience having worked in the UK and overseas with global businesses such as BP, Mars and Pepsi, in engineering and operational management roles. Previously he was a member of the board at Boots Group Plc.

13 Dr Angela Strank

BSc PhD (Geology) (61)

Independent non-executive director

Appointed to the board on 24 January 2014

Angela is Chief Scientist at BP Group. She has held various senior strategic, technical and commercial leadership roles at BP since joining in 1982, most recently Vice President and Head of the Chief Executive's Office. In 2010 Angela was the winner of the UK First Woman's Award in Science and Technology in recognition of pioneering UK women in business and industry. Her track record and experience in strategy, technology and transformational change are a complementary addition to the board's skill set.

External appointments

Board of Governors of the University of Manchester
University College London, Energy Institute
International Advisory Board

Governance

Chairman's letter

Dear Stakeholder

At Severn Trent Water, we are committed to delivering value to our customers and building a sustainable business, which is underpinned by good governance. As a board we are accountable to our stakeholders for ensuring that effective governance processes are in place and complied with. The board's role is to

- understand and meet its obligations to the company's stakeholders,
- govern the company within a framework of prudent and effective controls which enable risk to be assessed and managed,
- approve the company's strategic objectives, and
- ensure that sufficient resources are available to enable it to meet those objectives

Good governance ensures that decisions flow down the organisation, so we implement them correctly, and that information flows up to those that need it to make decisions. Ultimately, good governance ensures that the board has access to timely, relevant and robust information, so it can run the business effectively.

In January 2014, Ofwat published 'Board leadership, transparency and governance – principles' which it considered should apply to regulated water companies. Severn Trent Water is fully supportive of Ofwat's objective of raising standards in this area.

Severn Trent Plc is the ultimate holding company of Severn Trent Water Limited. Severn Trent Plc is a listed company and during the year ended 31 March 2014 was compliant with the UK Corporate Governance Code 2012 (the 'Governance Code'), with the exception that the adequacy of arrangements in relation to whistleblowing procedures falls within the remit of the Corporate Responsibility Committee rather than the Audit Committee. The governance section of the Severn Trent Plc Annual Report and Accounts sets out how Severn Trent Plc applies the principles of the Governance Code.

Severn Trent Water's code on complying with Ofwat's principles is to continue to comply with the Governance Code at Severn Trent Plc level, with the exception that the adequacy of arrangements in relation to whistleblowing procedures will continue to fall within the remit of the Corporate Responsibility Committee rather than the Audit Committee. As a company Severn Trent Water has voluntarily chosen to apply the principles of the Governance Code to its governance arrangements. Where appropriate and reasonably practicable, Severn Trent Water will, except as stated above in relation to whistleblowing arrangements, continue to comply with the Governance Code with the exception that the board committees will continue to operate at the Severn Trent Plc level rather than duplicating the arrangements at the company level. The board considers that these arrangements are appropriate and effective.

I believe that good governance is critically dependent on behavior and culture, as well as organisation and process. The following sections of this report set out how good governance supports our activities at Severn Trent Water and describe how the board applies the principles of the Governance Code – in the way we are structured, the way we choose to behave and the way we ensure our effectiveness. Assessing our governance arrangements in terms of these headings enables us to establish the right long term behaviours, which will help us to deliver the company's strategic objectives in a sustainable manner.

I firmly believe that we will continue to deliver value and achieve sustainable growth for our company through the successful mix of good governance, a clear strategy with a supporting business plan and a strong management team to execute it.

Andrew Duff
Chairman

Governance

Compliance with the UK Corporate Governance Code

As Severn Trent Water is not a listed company it is not required to comply with the Governance Code. However, we have voluntarily chosen to apply the principles of the Governance Code to our governance arrangements, where appropriate and reasonably practicable.

The version of the Governance Code applicable to the current reporting period is the September 2012 UK Corporate Governance Code. The Governance Code is available on the Financial Reporting Council's website (www.frc.org.uk).

The boards of Severn Trent Water and Severn Trent Plc have the same directors. This structure was implemented in 2007 to reflect the fact that the company is the largest part of the Severn Trent group. This approach ensures that the company's strategic and operational issues engage the Severn Trent Plc's board and that the two companies have the same governance standards. We have processes in place to ensure the directors make formal decisions in their capacity as directors of Severn Trent Water Limited and Severn Trent Plc respectively. None of the directors represent investors and neither company has alternate directors. There is also an explicit division of responsibility between the (independent on appointment) Chairman and Chief Executive.

For the whole of the financial year ended 31 March 2014, Severn Trent Water Limited was compliant with the Governance Code, with the following exceptions:

- the board committees operate at the Severn Trent Plc level rather than the company level. Whilst the board committees are not duplicated at the company level, in practice their remit includes work in respect of the company. In particular the Audit Committee reviews Severn Trent Water's
 - Processes for producing regulatory submissions, and
 - Statutory and regulatory accounts prior to their approval by the Severn Trent Water board.

The board committees are all led by independent non-executive directors who comprise the majority of membership of each committee. Details of the committees are reported publicly in the Severn Trent Plc Annual Report and Accounts.

- the adequacy of arrangements in relation to the company's whistleblowing procedures falls within the remit of the Severn Trent Plc Corporate Responsibility (CR) Committee, rather than the Severn Trent Plc Audit Committee. The CR Committee's remit is to deal with any allegations from employees relating to any breaches under Severn Trent's Code of Conduct. The Audit Committee reviews reports of matters arising in respect of financial or internal control matters from the company's whistleblowing procedures and the company's procedures for preventing and detecting fraud and bribery, and receives reports on non-compliance. The board considers that these arrangements are appropriate.
- the company does not comply with the provisions relating to Relations with Shareholders which covers Dialogue with Shareholders and Constructive use of the AGM, as it would not be appropriate to do so, however Severn Trent Plc does fully comply.

The way we are structured

Board membership

During the year under review your board has comprised the non-executive Chairman, four executive directors, seven independent non-executive directors and one non-executive director. During the year the board announced the retirement of Dr Bernard Bulkin and the appointment of Dr Angela Strank as an independent non-executive director, with effect from 24 January 2014. The board also announced the appointment of Philip Remnant as an independent non-executive director with effect from 31 March 2014. During the year the board also announced the appointment of Liv Garfield as Chief Executive with effect from 11 April 2014. Following the year end, the board announced the appointment of John Coghlan as a non-executive director with effect from 23 May 2014 and the retirement of Baroness Noakes as a non-executive director with effect from the conclusion of the AGM on 16 July 2014.

Governance

Photographs of the members of the board, together with their biographies and a description of the complementary skills and diverse experience that they bring to bear, can be found on pages 36 and 37

We believe this unitary board brings an appropriate balance of innovation, experience, independence and challenge to ensure effective decision making

In accordance with the Governance Code, all the directors will retire at this year's Severn Trent Plc AGM and submit themselves for election or re-election by the shareholders, with the exception of Baroness Noakes who will be retiring from the board with effect from the conclusion of the 2014 AGM

Details of our policy on diversity in the boardroom are provided in the Nominations Committee report on pages 52 and 53 of the Severn Trent Plc Annual Report and Accounts

Role of the Chairman

The role of Andrew Duff, the Chairman, is to lead a unitary board, facilitating the contribution of its members at its meetings, and to be responsible for ensuring that the principles and processes of the board are maintained in line with the board governance framework

Agendas for board meetings are agreed by the Chairman in consultation with the Chief Executive and Company Secretary, although any director may request that an item be added to the agenda. The Chairman has authority to act and speak for the board between its meetings, including engaging with the Chief Executive. He reports to the board and committee chairmen as appropriate on decisions and actions taken between meetings of the board. He also meets with the non-executive directors without the executive directors present, to consider the performance of the executive directors and to provide feedback

Senior independent non-executive director

Richard Davey is the senior independent non-executive director. The board has agreed that Richard will act as Chairman of the board in the event that the Chairman is unable to do so for any reason

Non-executive directors

The independent non-executive directors are appointed to the board to contribute their independent external expertise and experience in areas of importance to the company. Their competencies include corporate finance, general finance, corporate strategy, customer care, property, environmental and technology matters, general management, transformational change and supply chain management. They also provide independent challenge and rigour to the board's deliberations and are encouraged to make independent assessments of the company's competencies. The non-executive directors, led by the senior independent non-executive director, meet without the Chairman at least once a year for them to appraise the Chairman's performance and they have other meetings during the year without executive directors present

The board has reviewed the status of the independent non-executive directors and considers them all to be independent in character and judgement as defined by the Governance Code

Following his appointment as CEO of Severn Trent Services in January 2012, Martin Kane became a non-executive director

Chief Executive

Responsibility has been delegated to the Chief Executive to implement the company's strategy. During the year under review the Chief Executive was Tony Wray, who retired on 11 April 2014. Liv Garfield succeeded Tony as Chief Executive on 11 April 2014 and is empowered to take all decisions and actions that further the company's strategy and which in her judgement are reasonable, having regard to the Chief Executive limits set out in the company's Group Authorisation Arrangements. The independent non-executive directors, led by the Chairman, appraise the Chief Executive's performance annually

Governance

Executive directors

The executive directors support the Chief Executive in driving the implementation of strategy forward in the company. They are committed to doing this in a responsible way which takes account of commitment to the Code of Conduct, the long term sustainable and responsible stewardship of the business and the delivery of better value, better services and a healthier environment for our customers and the communities in which we live and work.

Role of the Company Secretary

All directors have access to the advice and services of the Company Secretary, Bronagh Kennedy, and the Company Secretariat team. Bronagh is responsible for ensuring that the board operates in accordance with the governance framework it has adopted and that there are effective information flows to the board and between senior management and the non-executive directors.

The appointment and resignation of the Company Secretary is a matter for consideration by the board as a whole.

Terms and conditions of appointment

We have made the terms and conditions of appointment of the directors available for inspection by any person at the company's registered office during normal business hours.

Board processes

We have documented processes in place regarding

- the board's tasks and activities, and
- the matters specifically reserved for the board's decision making

The board has reserved the following for its own consideration

- the appointment of the Chief Executive, directors and the Company Secretary,
- the strategy and budgets of the company,
- decisions regarding the company required to be made by the company's constitutional documents, statute or external regulation, and
- the approval or adoption of documents, including the report and accounts, directors' statements to Ofwat concerning the Annual Regulatory Compliance Statement, required to be made by the board by the company's constitutional documents, statute or external regulation

Board meetings

We have regular scheduled meetings of the board throughout the year and any additional meetings and ad hoc committee meetings are convened as and when required.

Papers, including minutes of any board committees held since the previous board meeting and performance reports, are circulated in advance of each meeting.

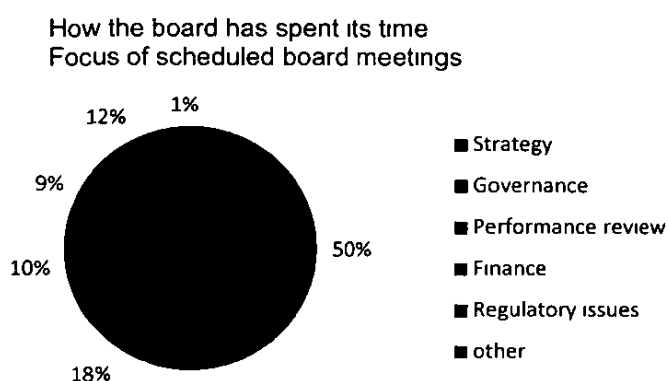
There is an agreed procedure in place which allows directors to take independent professional advice in the course of their duties and all directors have access to the advice and services of the Company Secretary. If a director has a concern over any unresolved matter they may require the Company Secretary to minute that concern.

The chart overleaf shows how the board has spent its time at scheduled board meetings. The board monitors the performance of the business at every meeting and receives monthly updates on performance against the KPIs stated on pages 6 and 7 of the Strategic report. The board also regularly discusses reports on capital efficiency. The board monitors governance matters and developments in best practice through the Governance report provided by the Company Secretary, a standing item on the board agenda. The board also formally reviews compliance with the Governance Code on an annual basis.

During the year, five additional board meetings were convened to consider the submission of the Business Plan to Ofwat and the appointment of the new Chief Executive.

Governance

In addition to formal board meetings, the board attended a full day strategy session this year, where the board and executive management management together considered the areas of future value creation across the Severn Trent business



Board attendance at scheduled meetings in 2013/14		Board attendance at additional meetings in 2013/14	
Andrew Duff	7/7	Andrew Duff	6/6
Tony Ballance	7/7	Tony Ballance	6/6
Dr Bernard Bulkin	6/6	Dr Bernard Bulkin*	2/4
Richard Davey	7/7	Richard Davey	5/6
Gordon Fryett	7/7	Gordon Fryett*	3/6
Martin Kane	7/7	Martin Kane*	5/6
Martin Lamb	7/7	Martin Lamb*	5/6
Michael McKeon	7/7	Michael McKeon	6/6
Baroness Noakes*	6/7	Baroness Noakes*	5/6
Andy Smith	7/7	Andy Smith	6/6
Dr Angela Strank	2/2	Dr Angela Strank	2/2
Tony Wray	7/7	Tony Wray	6/6

*unable to attend one meeting owing to personal reasons

* unable to attend certain additional meeting held at short notice owing to prior business commitments

Governance

The way we choose to behave

Code of Conduct. 'Doing the right thing – The Severn Trent way'

Every day Severn Trent Water employees have to make choices about what they do and how they do it. Most of the time it is clear what the right thing to do is, whether it is about doing what is safe, doing the right thing for customers, doing what is right ethically – and indeed what is right legally.

However, sometimes it is not so clear. 'Doing the right thing – The Severn Trent way' details the principles we work by. This is our Code of Conduct and explains who we are, what we stand for and how we work, it also tells our customers and business partners that they can trust and rely on us. These principles apply to everyone in Severn Trent Water. They provide a common and consistent framework for responsible business practices and set out the standards we need to follow in our day-to-day activities.

During the year we have continued to roll out the Code of Conduct to make sure that everyone in the business understands what it is all about and upholds our ethical standards. All employees are provided with a copy as part of their induction. Training sessions are also available and all teams have been encouraged to discuss it through regular communications exercises. We have also continued to roll out our Code of Conduct into our supply chain.

During autumn 2013 employees across the company attended 'Our Journey Continues' sessions which focused on the next steps in the journey to be the best water and waste water company in the UK. These sessions also provided a refresher on the importance of doing the right thing the Severn Trent way and emphasised how these principles and our Code of Conduct were at the heart of our standard ways of working.

Policies

The Code of Conduct is supported by 15 policies and our behaviours model. Further details of these can be found on the Severn Trent Plc website (www.severntrent.com). During the year we have completed the annual review of the policies to ensure they are fit for purpose.

Conflicts of interests

The board has a full documented process in place to authorise situational conflicts in accordance with the provisions of the Companies Act 2006 and under the company's articles of association.

At every board meeting there is a standing agenda item at the beginning of the meeting to consider and discuss whether any potential conflict exists. If it does then the relevant director does not attend the meeting when that item is discussed.

An annual review of conflicts is carried out and is incorporated into the year end process of verifying directors' interests. Half yearly reports are also made to the board of all directors' conflicts and directors are reminded of their obligations to disclose any potential conflicts.

In March 2014, the board approved the authorisation of the potential situational conflict arising as a consequence of the appointment of Martin Lamb as Chairman of Evoqua Water Technologies and agreed to consider the management of such conflicts if and when they arose.

Interests

No director had a material interest at any time during the year in any contract of significance with the company or any of its subsidiary undertakings.

The way we ensure our effectiveness

Induction

On joining the board, a director's induction needs are evaluated and then they are provided with a comprehensive and personalised induction pack which includes information on our business, key operations and processes, how we are regulated, how we are shaping future regulation, strategic plans, financial reports, business plans and information on our governance framework.

Governance

Meetings are arranged with members of the executive management team and with external advisers who provide support to the board. Visits to operational and office sites across the company and management presentations are also arranged for directors joining the board and subsequently throughout the year.

These arrangements have been followed for the induction of Liv Garfield, Dr Angela Strank, Philip Remnant and John Coghlan.

Continuing professional development

The directors received updates throughout the year on matters such as changes to best practice governance guidelines. The directors also have access to professional development provided by external bodies and our advisers.

Continuing professional development (CPD) requirements were considered as part of the board effectiveness review referred to below. No additional requirements were identified.

An online Directors' Resource Library and CPD repository has been created for use by the directors. The library includes a Corporate Governance Manual, Strategy Day materials and details of board training sessions. It also includes a further reading section which contains regular updates and guidance on changes to legislation and best practice.

Performance and effectiveness reviews

An independent review of the effectiveness of the board is conducted every three years. The last external review was carried out in November 2011 and an independent review will be commissioned during the 2014/15 financial year.

In January 2014, the board commenced an internal review of its effectiveness and that of its committees. The review was led by the Chairman and was assisted by the Company Secretary who conducted a series of confidential interviews with each director. Following the feedback from the board effectiveness review, a review of each individual director's performance was carried out by the Chairman.

In terms of improvements identified in the previous year's internal review, it was concluded that good progress had been made. Steps had been taken to ensure appropriate time was allocated for consideration of strategic matters. The board had considered leadership and succession planning with particular focus on the development of management below the Executive Committee level. During the year the board reviewed progress against the 5 year talent management and succession plan and the outputs from the 2012/13 talent management process. In addition, the board reviewed the company's regulatory performance position, including performance by peer companies.

This year's review confirmed continued board strengths, including the quality of the relationship between executive and non-executive directors, a diverse and complementary balance of skills and experience and effective use of time. The only suggested improvements to effectiveness were in relation to the annual offsite board strategy discussions which had been impacted by the considerable amount of time that had been required to be devoted in the year to the preparations for submission of the Final Business Plan to Ofwat. It was anticipated that should not be the case in the current year.

The board will continue to formally review progress against the recommendations arising from the board effectiveness reviews every six months.

Board committees

As previously reported on pages 38 and 39, the board committees operate at the ultimate parent company level rather than the company level. 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 (except as reported on page 39) and are available for inspection, together with the

Governance

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

Reports from the Chairmen of these committees are set out on pages 52 to 76 of the Severn Trent Plc Annual Report and Accounts, which is available online (www.severntrent.com)

Whilst the board committees are not duplicated at the company level, in practice their remit includes work in respect of the company. In particular

- (i) the Nominations Committee assists the board by keeping the composition of the board of the company under review and conducting a rigorous and transparent process when making or renewing appointments of directors to the board,
- (ii) the Audit Committee assists the board in discharging its responsibilities for the integrity of the systems of internal controls and monitoring the effectiveness and objectivity of the internal and external auditors. The Audit Committee reviews the statutory and regulatory accounts prior to their approval by the board of the company

The regulated activities carried out by the company also require two annual reporting requirements to Ofwat which are reviewed by the Audit Committee: an annual submission on the company's regulatory obligations known as the Annual Regulatory Performance Report, together with the Annual Regulatory Compliance Statement, and a statement that underpins the customer charges made by the company, known as the Principal Statement

In May 2013 the Audit Committee reviewed the assurance framework in place for the Annual Regulatory Compliance Statement process. In September and November 2013 the Audit Committee reviewed the process, timeline and assurance framework for the production of the 2014 Principal Statement and its submission to Ofwat

Deloitte make reports to Ofwat in respect of the company's regulatory accounts. The Annual Regulatory Performance Report, which provides an overall picture of company performance, covers many aspects which are not financial and the company appoints engineering consultants, Atkins, to report on those aspects. The Audit Committee receives reports from Atkins on their work as part of its review of the Annual Regulatory Returns

An additional requirement during the year was oversight of the assurance processes which were designed to ensure that a high quality plan was submitted to Ofwat as part of PR14. This involved both internal assurance processes and assurance provided by a number of external assurance providers for specific aspects of the Final Business Plan submission. The Audit Committee reviewed the overall processes in September 2013 and in November 2013 reviewed the draft reports received from the assurance providers. The Audit Committee's findings were reported to the board as part of its deliberations prior to the submission of the Final Business Plan in December 2013,

- (iii) the Corporate Responsibility Committee reviews the key non-financial risks and opportunities and monitors progress, and
- (iv) the Remuneration Committee determines the Severn Trent Plc policy on the remuneration of executive directors, other members of the Executive Committee and the Chairman of the board

Directors Report

The directors present their report, together with the audited financial statements of the group, for the year ended 31 March 2014. The Governance section set out on pages 38 to 45 forms part of this report.

Principal activity

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 Strategic report on pages 1 to 35 provides detailed information relating to the company, its business model and strategy, the operation of its business and the results and financial position for the year ended 31 March 2014.

Details of the principal risks and uncertainties facing the company are set out in the Risk management section on pages 30 to 35.

Directors and their interests

Biographies of the directors currently serving on the board are set out on pages 36 and 37.

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 2014.

None of the directors retain any notifiable interest in the shares of the company or any other subsidiaries as at 31 March 2014.

Details of directors' service agreements and the interests of the directors in the shares of Severn Trent Plc are shown on pages 60 to 76 of the Severn Trent Plc remuneration report.

Remuneration details

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

Directors' remuneration and annual bonus scheme

Remuneration for executive directors comprises the following elements:

- base salary and benefits,
- annual bonus scheme,
- 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 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 2013/14

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 2013 to 31 March 2014 (detailed overleaf).

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 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 10 KPIs employed in the previous year. 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 table below shows the points awarded by the Remuneration Committee for bonus purposes under each of the 10 selected KPIs in relation to the 2013/14 ABS. As a consequence the Severn Trent Water bonus award was 63.2% of the maximum opportunity.

Key Area	KPI	Measure	2013/14 target	2013/14 Stretch	2013/14 outturn	Points awarded
Employee	1	Lost Time Incidents per 100,000 hours worked	0.28	0.27	0.21	130
	2	Employee motivation- Quest (engagement index)	79%	80%	81%	130
Customer	4	Service Incentive Mechanism- Qualitative	4.52	4.73	4.48	99
	5	Service Incentive Mechanism- Quantitative	162	154	147	130
	7	Serviceability – Waste Water	75	66	57	130
	8	Serviceability - Water	70	68	201	0
Financial	9	Capital Expenditure versus Final Determination	0%	0.2%	0%	100
	11	Operating expenditure versus Final Determination	0%	0.6%	0%	100
Environment	12	Pollution Incidents (cat 1,2 &3)	491	475	449	130
	16	Leakage ml/d- Post MLE	456	449	453	130
Total						1079

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

Director	Value of bonus award
Tony Ballance	£161,974
Martin Kane	£126,534
Michael McKeon	£344,834
Andy Smith	£210,497
Tony Wray	£473,064

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 2014/15

The Remuneration Committee has reviewed the operation of the plan and concluded that it should operate on the following basis for 2014/15. At least 50% of the bonus will be based on the Severn Trent Water balanced scorecard (comprising the 10 KPIs outlined on the previous page), with the balance related to key business objectives and personal contribution. No more than 20% will relate to personal contribution. For 2014/15 the mix will be 50% on the Severn Trent Water scorecard, 40% on key business objectives and 10% on personal performance. Martin Kane's bonus will be based 90% on the performance of Severn Trent Services and 10% on personal objectives.

Share Matching Plan

Under the Share Matching Plan ('SMP') for 2013/14 directors were 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 2013/14 SMP can be found in the Severn Trent Plc Annual Report and Accounts. Please note that following investor feedback and our aim to simplify the executive reward package, no further awards will be made under the share matching plan from 2014.

Long Term Incentive Plan

Directors may also participate in the Long Term Incentive Plan ('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 Shareholder approval is being sought at the Severn Trent Plc AGM in July 2014 to replace the LTIP as it reaches the end of its 10 year term The performance metrics will remain the same and the award levels for 2014 will be increased to 125% of salary for the Chief Executive and 80% of salary for the other executive directors, which will incorporate the value of the SMP forgone 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 10 balanced scorecard KPIs used for the ABS For the year 2013/14 awards of shares to the value of £474 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 Severn Trent Plc Following a review of the shareholding guidelines against market practice, they have been increased from 150% to 200% of base salary in respect to the Chief Executive and from 100% to 125% of base salary in respect of the other executive directors 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 until 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

Insurance and indemnities

The company maintains Directors' and Officers' Liability Insurance in respect of legal action that might be brought against its directors and officers 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 company

Indemnities were also entered into with Dr Angela Strank, Liv Garfield and Philip Remnant and upon their appointments to the board in January, March and April 2014 respectively

Severn Trent Water does not have in place any indemnities for the benefit of the auditors

Employees

The average number of employees in the company is 5,634 (2013 5,458)

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 can take up employment with 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 the company We ensure that training, career development and promotion opportunities are available for all our employees irrespective of their gender, race, age or disability

The provision of occupational health programmes is of crucial importance and, in particular, work has been undertaken during the year to promote awareness of mental health issues and the employee assistance programme available to employees

The company actively encourages employee involvement and consultation and places emphasis on keeping its employees informed of its activity and financial performance by way of company-wide communication forums, briefings and publication to staff of all relevant information and corporate announcements To help align employees' interests with the success of the company's performance, Severn Trent offers two employee share plans The Severn Trent Sharesave Scheme, an HM Revenue and

Customs approved SAYE plan, is offered to employees on an annual basis. The Severn Trent Share Incentive Plan, approved by HM Revenue and Customs, makes an annual award of shares to employees, based on performance against the company's KPI targets.

Research and development

Expenditure on research and development is set out in note 1 (i) to the financial statements on page 65. Details of research and development activity undertaken by the company during the year is set out on pages 1 to 29 of the Strategic report.

Regulation 'Ring fencing'

In accordance with the requirements of Ofwat, the board confirmed that, as at 31 March 2014, 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 interest of the company, and where appropriate arrangements are in place to avoid conflicts of interest.

Post balance sheet events

There are no post balance sheet events.

Dividends

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 2014 amounted to £340 million (2013 £72 million).

Contributions for political purposes

The company'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 political expenditure in the financial year under review.

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 2014 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

Auditors

Deloitte LLP have indicated their willingness to continue as auditors 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

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 is well placed to manage its business risks successfully The company is funded for its investment and cash flow needed at least for next year

The directors have a reasonable expectation that the company has 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

By order of the board



Bronagh Kennedy
General Counsel and Company Secretary
28 May 2014

Directors' responsibility 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.

The directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's performance, business models and strategy.

Responsibility statement

We confirm that to the best of our knowledge

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company, and
- the management report, which is incorporated into the directors' report, includes a fair review of the development and performance of the business and the position of the company, together with a description of the principal risks and uncertainties that it faces

By order of the board

Andrew Duff
Chairman

28 May 2014



Michael McKeon
Finance Director



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

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

Opinion on financial statements of Severn Trent Water Limited

In our opinion

- give a true and fair view of the state of the company's affairs as at 31 March 2014 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

The financial statements comprise the profit and loss account, the statement of comprehensive income, the balance sheet, the statement of changes in equity, the cash flow statement and the related notes 1 to 36. The financial reporting framework that has been applied in their preparation is applicable law and Financial Reporting Standard 101 Reduced Disclosure Framework.

Going concern

We have reviewed the directors' statement contained within the Directors' Report on page 51 that the company is a going concern. We confirm that

- we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate, and
- we have not identified any material uncertainties that may cast significant doubt on the company's ability to continue as a going concern.

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

Our assessment of risks of material misstatement

The assessed risks of material misstatement described below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team

Risk	How the scope of our audit responded to the risk
<p><i>Determination of the provision for impairment of trade receivables</i></p> <p>Provisions are made against trade receivables based on historical experience of levels of recovery from accounts in particular ageing categories</p>	<p>We reviewed and challenged the information used to determine the bad debt provision by considering cash collection performance against historical trends and the level of bad debt charges over time. Specifically, we reviewed the actual history of slow paying customers in the period using data analytics to understand the collection of previously aged debtors and to recompute the ageing analysis. We also tested the key controls relating to the data used in the bad debt model and agreed a sample of this data back to its source, being the billing system.</p>
<p><i>Revenue recognition risk in relation to the estimation of unbilled revenue</i></p> <p>For water and waste water customers with water meters, the amount recognised depends upon the volume supplied, including an estimate of the sales value of units supplied between the date of the last meter reading and the year end. The estimated usage is based upon historical data and assumptions around consumption patterns.</p>	<p>We challenged the validity of management's estimate of the current year accrued revenue by comparing actual amounts billed to the estimate made in the prior year to determine the accuracy of the estimation techniques. In addition, we used data analytics to recompute the total level of unbilled revenue for the current year as well as testing the controls around the key data inputs to the model and agreed a sample of this data back to its source.</p>
<p><i>Determining the amount of retirement benefit obligations</i></p> <p>This process is complex and requires management (after taking advice from their actuarial advisers) to make a number of assumptions concerning long term interest rates, inflation, salary and pension increases, investment returns and longevity of current and future pensioners.</p>	<p>With support from the pension specialists within our audit team, we challenged the assumptions used in the calculation of the pension scheme deficit as detailed in note [x], specifically regarding the discount rate, inflation rate and mortality assumptions with reference to comparable market and other data.</p>
<p><i>Determination of current and deferred tax provisions</i></p> <p>Assessing the outcome of uncertain tax positions requires judgements to be made regarding the result of negotiations with, and enquiries from, tax authorities in a number of jurisdictions.</p>	<p>With support from the tax specialists within our audit team, we considered the likely outcomes of uncertain tax positions and reviewed correspondence with the tax authorities to assess the appropriateness of the tax provisions that have been recorded in the balance sheet.</p>

The Severn Trent Plc Audit Committee's consideration of these risks is set out on page 54 of the Severn Trent Plc Annual Report and Accounts

Our audit procedures relating to these matters were designed in the context of our audit of the financial statements as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the financial statements is not modified with respect to any of the risks described above, and we do not express an opinion on these individual matters.

Our application of materiality

We determined planning materiality for the company to be £15 million based on revenue.

We agreed with the Severn Trent plc Audit Committee that we would report to the Committee all audit differences in excess of £750,000, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds

An overview on the scope of our audit

Our audit was scoped by obtaining an understanding of the entity and its environment, including internal control, and assessing the risks of material misstatement. Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records

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

- we have not received all the information and explanations we require for our audit, or
- adequate accounting records have not been kept by the 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

We have nothing to report in respect of these matters

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made. We have nothing to report arising from this matter

Other matters

Although not required to do so, the directors have voluntarily chosen to make a corporate governance statement detailing the extent of their compliance with the UK Corporate Governance Code. We reviewed the part of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the UK Corporate Governance Code. We have nothing to report arising from our review

Our duty to read other information in the Annual Report

Under the International Standards on Auditing (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is

- materially inconsistent with the information in the audited financial statements, or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the company acquired in the course of performing our audit, or
- otherwise misleading

In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the audit committee which we consider should have been disclosed. We confirm that we have not identified any such inconsistencies or misleading statements

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. We also comply with International Standard on Quality Control 1 (UK and Ireland). Our audit methodology and tools aim to ensure that our quality control procedures are effective, understood and applied. Our quality controls and systems include our dedicated professional standards review team, strategically focused second partner reviews and independent partner reviews

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/or those further matters we have expressly agreed to report to them on in our engagement letter 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.

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 and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.



Jane Whitlock (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Birmingham, UK
28 May 2014

Severn Trent Water Limited

Profit and loss account For the year ended 31 March 2014

	Notes	2014 £m	2013 Restated (see note 2) £m
Turnover	4	1,544 8	1,511 0
Operating costs before exceptional items	5	(1,028 4)	(1,015 4)
Exceptional operating income	6	8 2	13 3
Total operating costs		(1,020 2)	(1,002 1)
Profit before interest and tax		524 6	508 9
Interest receivable	9	87 0	88 6
Interest payable	10	(332 2)	(324 9)
Net finance costs		(245 2)	(236 3)
Gains/(losses) on financial instruments	11	49 6	(49 5)
Profit on ordinary activities before tax		329 0	223 1
Current tax excluding exceptional tax credit		(56 9)	(33 5)
Deferred tax excluding exceptional credit		(14 6)	9 6
Exceptional tax credit		234 7	40 0
Total taxation on profit on ordinary activities	12	163 2	16 1
Profit for the financial year		492 2	239 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 2014

	2014	2013
	£m	Restated (see note 2) £m
Profit for the year	492.2	239.2
Other comprehensive income		
Items that will not be reclassified to the profit and loss account		
Net actuarial gain/(loss) on defined benefit pension schemes	13.2	(36.4)
Tax on net actuarial gain/loss	(2.6)	6.5
Deferred tax arising on change of rate	(11.3)	(3.2)
	(0.7)	(33.1)
Items that may be reclassified to the profit and loss account		
Gain/(loss) on cash flow hedges	11.2	(37.6)
Deferred tax on gain/loss on cash flow hedges	(2.2)	8.6
Amounts on cash flow hedges transferred to the profit and loss account in the period	3.3	16.2
Deferred tax on transfers to the profit and loss account	(0.7)	(3.7)
	11.6	(16.5)
Other comprehensive income/(loss) for the period	10.9	(49.6)
Total comprehensive income for the period	503.1	189.6

Severn Trent Water Limited

Balance sheet As at 31 March 2014

	Notes	2014 £m	2013 £m
Fixed assets			
Goodwill	14	1 3	1 3
Intangible assets	15	69 3	89 0
Tangible fixed assets	16	6,988 3	6,738 0
Investments	17	347 9	347 9
Dervative financial assets	24	30 2	65 5
		7,437 0	7,241 7
Current assets			
Stocks	18	6 4	6 1
Debtors amounts falling due after more than one year	19	284 9	300 4
Debtors amounts falling due within one year	19	450 2	430 2
Dervative financial assets	24	9 4	0 9
Cash at bank and in hand		19 8	328 6
		770 7	1,066 2
Creditors amounts falling due within one year	21	(732 3)	(596 2)
		38 4	470 0
Net current assets		38 4	470 0
Total assets less current liabilities		7,475 4	7,711 7
Creditors amounts falling due after more than one year	22	(5,406 3)	(5,628 3)
Retirement benefit obligation	33	(348 3)	(383 7)
Provisions for liabilities and charges	25	(687 2)	(832 2)
		1,033 6	867 5
Net assets		1,033 6	867 5
Capital and reserves			
Called up share capital	27	100 0	100 0
Hedging reserve	28	(123 3)	(134 9)
Profit and loss account		1,056 9	902 4
Total shareholder's funds		1,033 6	867 5

The financial statements were approved by the board of directors on 28 May 2014. They were signed on its behalf by



Andrew Duff
Chairman
28 May 2014
Company Number 02366686



Michael McKeon
Director

Severn Trent Water Limited

Statement of changes in equity For the year ended 31 March 2014

	Share capital £m	Hedging reserves £m	Infrastructure reserves £m	Profit and loss account £m	Total £m
At 1 April 2012	1,000 0	(118 4)	378 0	(515 5)	744 1
Profit for the year (restated, see note 2)	-	-	-	239 2	239 2
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)
Actuational losses (restated)	-	-	-	(36 4)	(36 4)
Deferred tax on actuational losses (restated)	-	-	-	5 2	5 2
Tax on pension contributions	-	-	-	1 3	1 3
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
Deferred tax on share based payments	-	-	-	(0 1)	(0 1)
Dividends paid	-	-	-	(72 0)	(72 0)
At 31 March 2013	100 0	(134 9)	-	902 4	867 5
Profit for the year	-	-	-	492 2	492 2
Gains on cash flow hedges	-	11 2	-	-	11 2
Deferred tax on gains on cash flow hedges	-	(2 2)	-	-	(2 2)
Amounts on cash flow hedges transferred to the profit and loss account	-	3 3	-	-	3 3
Deferred tax on transfers to the profit and loss account	-	(0 7)	-	-	(0 7)
Actuational gains	-	-	-	13 2	13 2
Deferred tax on actuational gains	-	-	-	(2 6)	(2 6)
Deferred tax arising from rate change	-	-	-	(11 3)	(11 3)
Total comprehensive income for the year	-	11 6	-	491 5	503 1
Share options and LTIPs					
- value of employees' services	-	-	-	5 8	5 8
- shares purchased	-	-	-	(2 8)	(2 8)
Dividends paid	-	-	-	(340 0)	(340 0)
At 31 March 2014	100 0	(123 3)	-	1,056 9	1,033 6

Severn Trent Water Limited

Cash flow statement For the year ended 31 March 2014

	Note	2014 £m	2013 £m
Cash generated from operations	31	774 4	757 9
Tax paid		(14 5)	(53 5)
Net cash generated from operating activities		759 9	704 4
Investing activities			
Interest received		1 8	5 2
Dividends received from subsidiaries		2 4	–
Receipts of amounts due from finance leases		5 7	0 5
Proceeds on disposal of intangible and tangible assets		10 1	15 6
Purchases of intangible assets		(8 2)	(14 9)
Purchases of tangible assets		(473 4)	(420 7)
Contributions and grants received		30 3	27 4
Net cash used in investing activities		(431 3)	(386 9)
Financing activities			
Interest paid		(186 8)	(167 4)
Closed out swap		–	(44 3)
Interest element of finance lease payments		(18 7)	(22 7)
Dividends paid		(340 0)	(72 0)
Repayments of borrowings		(168 6)	–
Repayments of obligations under finance leases		(13 0)	(29 1)
Repayment of intercompany loans		(320 2)	(287 4)
New intercompany loans raised		412 7	635 1
Purchase of shares in ultimate parent company		(2 8)	(1 4)
Net cash used in financing activities		(637 4)	10 8
(Decrease)/increase in cash and cash equivalents		(308 8)	328 3
Net cash and cash equivalents at beginning of period		328 6	0 3
Net cash and cash equivalents at end of period		19 8	328 6

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

In the prior year, the company 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 adopted FRS 101 'Reduced Disclosure Framework' and 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 36

c) Turnover

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

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

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

d) 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

e) 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

f) 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

Severn Trent Water Limited

Notes to the financial statements

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

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 tested for impairment in accordance with the policy set out in note 1m) below and carried at cost less accumulated impairment losses.

h) Intangible fixed assets

Intangible assets acquired separately are capitalised at cost. 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
Computer software	3-10
Other intangible assets	2-20

Amortisation is included within operating costs.

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

Severn Trent Water Limited

Notes to the financial statements

i) Research and development

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

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

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

j) 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 replacements 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

k) 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 and a corresponding liability representing the obligation to the lessor is recognised. 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.

l) 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.

m) 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. Severn Trent Water is considered to be a single cash-generating unit. Therefore where the asset does not generate cash flows that are independent from other assets, the company estimates the recoverable amount of the company as a whole. 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.

n) Investments in subsidiaries

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

o) 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

p) Retirement benefits

The company is the sponsoring employer of the Severn Trent group's defined benefit pension schemes. 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 net deficit relating to the 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. Finance income and cost are calculated by applying the discount rate used to determine the present value of the scheme liabilities at the opening balance sheet date to the value of the scheme assets or liabilities respectively.

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. Contributions made by other Severn Trent group companies have been disclosed within actuarial gains and losses in the statement of changes in 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.

q) Provisions

Provisions are recognised where

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

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

r) 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,
- loans and receivables, and
- derivatives designated as hedging instruments.

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 24 (d). Interest received in respect of derivative financial assets is included in interest receivable.

Severn Trent Water Limited

Notes to the financial statements

r) Financial instruments continued

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.

Derivatives designated as hedging instruments

The fair value of derivative financial assets that are designated as hedging instruments is determined using the methodology included in note 24(d).

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,
- other financial liabilities,
- derivatives designated as hedging instruments.

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.

Derivatives designated as hedging instruments

The fair value of derivative financial liabilities that are designated as hedging instruments is determined using the methodology included in note 24(d).

Severn Trent Water Limited

Notes to the financial statements

r) Financial instruments continued

(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

- the relationship between the hedging instrument and the hedged item,
- its risk management objectives and strategy for undertaking hedge transactions, and
- 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.

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.

s) 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 charge is adjusted to reflect shares that are not expected to 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.

t) 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 New accounting policies and future requirements

The company has adopted IFRS 13 "Fair Value Measurement" in this financial year. This standard sets out the approach to determining fair values in financial statements and provides additional guidance on how to measure fair value but does not change when fair value is permitted or required. In particular, the standard requires the company to take account of its own credit risk in determining the fair value of financial liabilities. The standard is applied prospectively and hence has no impact on amounts previously recognised. In the current period the fair value of derivative financial liabilities and the gain on financial instruments was £9.8 million higher as a result of the adoption of this standard and is reflected within note 9.

The company has also adopted IAS 19 "Employee Benefits" (revised). The revised standard changes the method of calculating the net finance cost on defined benefit pension schemes. Previously the discount rate used to calculate the scheme liabilities at the previous balance sheet date was applied to the liabilities and the expected return on the scheme's assets was applied to the assets. Under the revised standard the discount rate is applied to the net deficit to determine the net finance cost. Scheme administration costs were previously deducted from the expected return on assets. Such costs are now included in operating costs. There is no change to the measurement of the net surplus or deficit recognised in the balance sheet. The difference between the interest income calculated on the scheme assets and the actual return is recognised in other comprehensive income as an actuarial gain or loss.

Severn Trent Water Limited

Notes to the financial statements

The net impact of this change is shown below

	2014 £m	2013 £m
Profit for the period		
Operating profit	(3 0)	(2 6)
Net finance cost	(17 2)	(12 4)
Decrease in profit before tax for the period	(20 2)	(15 0)
Deferred tax	4 0	3 5
Decrease in profit for the period	(16 2)	(11 5)
Other comprehensive income		
Net actuarial gains	20 2	15 0
Tax on actuarial gains	(4 0)	(3 5)
Decrease in other comprehensive loss	16 2	11 5
Impact on net assets	-	-

IFRS 12 "Disclosure of Interests in Other Entities" was issued in May 2011 with an effective date of 1 January 2013. The EU has adopted these standards with effect from 1 January 2014 but with early application permitted. The company has elected not to apply this standard early and will adopt it with effect from 1 April 2014.

IFRS 12 provides disclosure requirements for subsidiaries, associates, joint agreements and structured entities which were previously covered in IAS 27, IAS 28 and IAS 31. Additional disclosures may be required in the company financial statements to meet the requirements of the standard.

At the date of approval of these financial statements, the following Standards and Interpretations were in issue but not yet effective. IFRS 9 "Financial Instruments" is likely to affect the measurement and disclosure of financial instruments. This standard has not yet been adopted by the EU.

Severn Trent Water Limited

Notes to the financial statements

3 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 enquiries from tax authorities. The assessments made are based on advice from independent tax advisers and the status of ongoing discussions with the tax authority.

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 j)

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

As the sponsoring employer of the Severn Trent group's defined benefit pension scheme, the company recognises the full cost and net deficit relating to the schemes. Determining the amount of 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 33 to the financial statements.

4. Revenue

The principal activity of the company is the treatment and the provision of water and the removal of waste water in England and Wales.

	2014 £m	2013 £m
Water and sewerage services	1,536.6	1,502.6
Other services	8.2	8.4
Total turnover	1,544.8	1,511.0
Interest receivable (note 9)	87.0	88.6
Total revenue	1,631.8	1,599.6

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Notes to the financial statements

5. Operating costs

	2014			2013		
	Before Exceptional costs	Exceptional costs	Total	Before Exceptional costs Restated	Exceptional costs	Total Restated
	£m	£m	£m	£m	£m	£m
Wages and salaries	185 8	-	185 8	176 3	-	176 3
Social security costs	17 3	-	17 3	16 3	-	16 3
Pension costs	30 3	-	30 3	28 8	-	28 8
Share based payments	6 1	-	6 1	6 6	-	6 6
Total employee costs	239 5	-	239 5	228 0	-	228 0
Power	65 3	-	65 3	60 6	-	60 6
Carbon reduction commitment	5 9	-	5 9	5 7	-	5 7
Raw materials and consumables	42 5	-	42 5	43 4	-	43 4
Rates	74 8	-	74 8	72 5	-	72 5
Charge for bad and doubtful debts	31 3	-	31 3	31 8	-	31 8
Service charges	31 6	-	31 6	31 9	-	31 9
Depreciation of tangible fixed assets	267 5	-	267 5	261 4	-	261 4
Amortisation of intangible fixed assets	28 0	-	28 0	28 9	-	28 9
Infrastructure maintenance expenditure	140 3	-	140 3	147 7	-	147 7
Hired and contracted services	140 3	-	140 3	130 2	-	130 2
Operating lease rentals						
- land and buildings	0 4	-	0 4	0 6	-	0 6
- other	0 3	-	0 3	-	-	-
Hire of plant and machinery	3 1	-	3 1	3 9	-	3 9
(Profit)/loss on disposal of fixed assets	(0 3)	(8 2)	(8 5)	1 4	(13 3)	(11 9)
Research and development	4 1	-	4 1	4 7	-	4 7
Foreign exchange losses	-	-	-	0 1	-	0 1
Other operating costs	55 9	-	55 9	59 0	-	59 0
	1,130 5	(8 2)	1,122 3	1,111 8	(13 3)	1,098 5
Release from deferred income	(9 5)	-	(9 5)	(9 3)	-	(9 3)
Own work capitalised	(92 6)	-	(92 6)	(87 1)	-	(87 1)
	1,028 4	(8 2)	1,020 2	1,015 4	(13 3)	1,002 1

During the year the following fees were charged by the auditors

	2014 £m	2013 £m
Fees payable to the company's auditors for		
- the audit of the company's annual accounts	0 2	0 2
- other assurance services	0 4	-
Total audit fees	0 6	0 2
Fees payable to the company's auditors for non-audit services	0 1	0 1
	0 7	0 3

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Notes to the financial statements

6. Exceptional items before tax

	2014	2013
	£m	£m
Profit on disposal of fixed assets	(8 2)	(13 3)

7. Employee information

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

	2014	2013
	Number	Number
Average number of employees	5,634	5,458

8 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 2014. 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/_{19p} each by virtue of having received contingent awards of shares under the Severn Trent Long Term Incentive Plan (LTIP), deferred shares under the Severn Trent Annual Bonus Scheme and contingent shares under the Share Matching Plan.

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 2014.

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Notes to the financial statements

b) Directors' remuneration

	2014	2013
	£m	£m
Aggregate directors' emoluments during the year (excluding pension contributions)	4.6	4.7
Pension contributions	0.1	0.1
	4.7	4.8

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

ii) Retirement benefits are accruing to one directors (2013 three directors) under a defined benefit scheme and one director (2013 two directors) under a defined contribution scheme

iii) Five directors (2013 five directors) exercised share options or received LTIP awards which vested during the year

c) Highest paid director

	2014	2013
	£m	£m
Aggregate emoluments (excluding pension contributions)	1.3	1.3

The accrued pension at 31 March 2014 for the highest paid director was £30,743 per annum (2013 £29,818 per annum). 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.

9 Interest Receivable

	2014	2013
	£m	Restated £m
Interest receivable on		
- bank deposits	1.2	0.8
- amounts due from group undertakings	1.9	1.3
- amounts due from group undertakings for finance leases	5.2	5.1
Interest income on defined benefit scheme assets	76.0	75.8
Other finance income	0.3	5.6
Dividend income	2.4	-
Total interest receivable and similar income	87.0	88.6

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Notes to the financial statements

10 Interest Payable

	2014	2013
	£m	£m
Interest payable and similar charges on		
- amounts payable to group undertakings	(201 3)	(190 1)
- amounts payable to group undertakings from finance leases	(11 3)	(11 1)
- finance leases	(9 7)	(11 3)
- bank and other loans	(15 1)	(19 2)
Pension interest cost	(91 7)	(92 2)
Other finance costs	(3 1)	(1 0)
Total interest payable and similar charges	(332 2)	(324 9)

In accordance with IAS 23 borrowing costs of £13.8 million (2013: £10.4 million) incurred funding eligible capital projects have been capitalised at an interest rate of 5.11% (2013: 5.12%)

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Notes to the financial statements

11. Gains/(losses) on financial instruments

	2014 £m	2013 £m
Loss on cross currency swaps used as hedging instruments in fair value hedges	(16 9)	(3 3)
Gain arising on adjustment for foreign currency debt in fair value hedges	16 3	3 5
Exchange gain on other loans	11 7	5 8
Ineffective portion of cash flow hedges	1 7	-
Amounts on cash flow hedges transferred from equity	(3 3)	(16 2)
Gain/(loss) arising on swaps where hedge accounting is not applied	40 1	(39 3)
	49 6	(49 5)

12 Tax on profit on ordinary activities

a) Analysis of tax credit in the year

			2014		2013	
	Before exceptional tax	Exceptional tax	Total	Before exceptional tax Restated	Exceptional tax	Total Restated
	£m	£m	£m	£m	£m	£m
Current tax						
UK corporation tax at 23% (2013 24%)						
- current year	47 5	-	47 5	60 7	(40 5)	20 2
- adjustment in respect of prior years	9 4	(59 2)	(49 8)	(27 2)	-	(27 2)
Total current tax	56 9	(59 2)	(2 3)	33 5	(40 5)	(7 0)
Deferred tax						
Origination and reversal of temporary differences						
- current year	25 4	-	25 4	(5 5)	38 8	33 3
- adjustment in respect of prior years	(10 8)	(56 2)	(67 0)	(4 1)	-	(4 1)
Exceptional credit arising from rate change	-	(119 3)	(119 3)	-	(38 3)	(38 3)
Total deferred tax	14 6	(175 5)	(160 9)	(9 6)	0 5	(9 1)
	71 5	(234 7)	(163 2)	23 9	(40 0)	(16 1)

The current tax charge before exceptional tax was £56.9 million (£33.5 million). This includes a charge of £9.4 million arising from adjustments to prior year tax computations. In the previous year adjustments to prior year tax computations resulted in a current tax credit of £27.2 million, primarily due to an industry agreement over the treatment of infrastructure income in those years computations.

Tax credits arising from unusual items in each year have been disclosed as exceptional and reduce the current total current tax charge in 2014 to a credit of £2.3 million (£7.0 million credit in 2013).

An exceptional current tax credit of £59.2 million has been recognised, reflecting the anticipated refund of overpayment of tax in prior periods as HMRC has now agreed that certain capital expenditure within our water and waste water treatment works is eligible for capital allowances as plant and machinery. This has also resulted in an exceptional deferred tax credit of £56.2 million.

In the prior year the company adopted the new accounting standard FRS 101, which changed the basis for the company's corporation tax computations. The most significant impact of this change is that certain amounts that had been taxed in previous years were recognised as profits and will be taxed in future periods. Therefore, to prevent such items being taxed twice, the tax already paid on such items was 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 Finance Act 2013 was enacted in the period and implemented a reduction in the corporation tax rate from 23% to 21% with effect from 1 April 2014 and then to 20% with effect from 1 April 2015. This has resulted in a deferred tax credit of £119.3 million in the income statement and a deferred tax charge of £11.3 million in reserves.

Severn Trent Water Limited

Notes to the financial statements

b) Factors affecting the tax credit in the year

The tax assessed for the year is lower than (2013 lower than) the standard rate of corporation tax in the UK of 23% (2013 24%)
The differences are explained below

	2014	2013
	£m	£m
Profit on ordinary activities before tax	329 0	223 1
Profit on ordinary activities multiplied by the standard UK corporation rate of 23% (2013 24%)	75 7	54 0
Tax effect of expenditure not deductible/(income not taxable) in determining taxable profits	2 6	1 9
Current year impact of rate change	(5 4)	(1 9)
Exceptional deferred tax credit arising from rate change	(119 3)	(38 3)
Adjustments to tax charge in respect of prior periods	(116 8)	(31 3)
Total tax credit for the year	(163 2)	(15 6)

c) Tax (charged)/credited to equity

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

	2014	2013
	£m	Restated £m
Current tax		
Tax on share based payments	-	0 7
Tax on pension contributions in excess of profit and loss charge	-	1 3
Total current tax (charged)/credited to equity	-	2 0
Deferred tax		
Tax on actuarial gains/losses	(2 6)	5 2
Tax on share based payments	-	-
Effect of change in tax rate	(11 3)	(3 2)
Tax on transfers to the profit and loss account	(0 7)	(3 7)
Tax on cash flow hedges	(2 2)	8 6
Total deferred tax (charged)/credited to equity	(16 8)	6 9

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Notes to the financial statements

13. Dividends on equity shares

Amounts recognised as distributions to equity holders in the period

	2014		2013	
	Pence per share	£m	Pence per share	£m
Final dividend for the year ended 31 March 2013	-	-	7.2	72.0
Interim dividend for the year ended 31 March 2014	34.0	340.0	-	-
		340.0		72.0

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

14. Goodwill

	2014	2013
	£m	£m
At 1 April	1.3	-
Additions	-	1.3
Cost and net book value at 31 March	1.3	1.3

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Notes to the financial statements

15. Intangible fixed assets

	Computer software		Other	Total £m
	Internally generated £m	Purchased £m	Internally generated £m	
Cost				
At 1 April 2013	126.9	179.9	12.0	318.8
Additions	2.3	5.9	–	8.2
Disposals	–	(74.7)	–	(74.7)
Reclassifications	43.9	(43.9)	–	–
At 31 March 2014	173.1	67.2	12.0	252.3
Amortisation				
At 1 April 2013	(118.4)	(101.9)	(9.5)	(229.8)
Amortisation for year	(13.9)	(13.5)	(0.6)	(28.0)
Disposals	0.1	74.7	–	74.8
Reclassifications	(5.1)	5.1	–	–
At 31 March 2014	(137.3)	(35.6)	(10.1)	(183.0)
Net book value				
At 31 March 2014	35.8	31.6	1.9	69.3
At 31 March 2013	8.5	78.0	2.5	89.0

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

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Notes to the financial statements

16. 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 2013	2,768 5	4,413 5	3,604 2	47 5	10,833 7
Additions	136 5	127 1	251 1	4 8	519 5
Disposals	(5 0)	(0 3)	(10 7)	(3 4)	(19 4)
At 31 March 2014	2,900 0	4,540 3	3,844 6	48 9	11,333 8
Depreciation					
At 1 April 2013	(910 8)	(1,151 3)	(2,005 1)	(28 5)	(4,095 7)
Charge for the year	(64 4)	(30 9)	(167 3)	(4 9)	(267 5)
Disposals	3 7	-	10 9	3 1	17 7
At 31 March 2014	(971 5)	(1,182 2)	(2,161 5)	(30 3)	(4,345 5)
Net book value					
At 31 March 2014	1,928 5	3,358 1	1,683 1	18 6	6,988 3
At 31 March 2013	1,857 7	3,262 2	1,599 1	19 0	6,738 0

Included in the above are assets under construction of £589 8 million (2013 £504 2 million) which are not depreciated

Cumulative borrowing costs capitalised included in the cost of tangible fixed assets amount to £48 5 million (2013 £34 7 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 2014	180 6	119 6	38 5	338 7
At 31 March 2013	184 1	120 6	54 8	359 5

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

	2014 £m	2013 £m
Freehold	1,928 2	1,857 4
Short leasehold	0 3	0 3
	1,928 5	1,857 7

Severn Trent Water Limited

Notes to the financial statements

17. Fixed asset investments

	Shares in subsidiary undertakings
	£m
Cost and net book value	
At 1 April and 31 March 2014	347.9

The company has the following investments

Subsidiary undertakings	Country of operation and incorporation	Principal activity	Percentage and class of share capital held
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

Severn Trent Water Limited

Notes to the financial statements

18. Stocks

	2014	2013
	£m	£m
Raw materials and consumables	6.4	6.1

19. Debtors

Amounts falling due within one year

	2014	2013
	£m	£m
Trade debtors	267.1	267.1
Bad debt provision	(118.2)	(111.3)
Net trade debtors	148.9	155.8
Loans receivable from group companies	12.0	15.5
Amounts receivable from group undertakings under finance leases	0.5	0.5
Other amounts due from group companies	6.3	10.5
Other debtors	23.2	27.9
Corporation tax	50.7	20.9
Prepayments and accrued income	208.6	199.1
	450.2	430.2

Amounts falling due after more than one year

	2014	2013
	£m	£m
Loans receivable from group companies	95.0	105.7
Amounts receivable from group undertakings under finance leases	100.8	101.3
Prepayments and accrued income	89.1	93.4
	284.9	300.4

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Notes to the financial statements

20. Finance lease receivables

Minimum lease payments receivable are as follows

	2014 £m	2013 £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	249 8	255 5
	278 2	283 9
Less unearned interest receivable	(176 9)	(182 1)
	101 3	101 8

The present values of minimum lease payments receivable are as follows

	2014 £m	2013 £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 7
After five years	98 6	99 1
	101 3	101 8

Disclosed in the balance sheet as

Debtors amounts falling due within one year	0 5	0 5
Debtors amounts falling due after one year	100 8	101 3
	101 3	101 8

The company has granted finance leases of between 46 and 59 years in respect to concrete settling tanks. The interest terms were set at the inception of the leases. Leases with capital outstanding of £101.3 million (2013: £101.8 million) bear interest at a weighted average interest rate of 5.1% (2013: 5.1%).

Severn Trent Water Limited

Notes to the financial statements

21 Creditors amounts falling due within one year

	2014	2013
	£m	£m
Bank loans	-	165.3
Loans due to parent and fellow subsidiary undertakings	306.2	72.5
Amounts owed to parent and fellow subsidiary undertakings under finance leases	2.7	2.6
Obligations under finance leases	32.0	10.5
Borrowings	340.9	250.9
Trade creditors	15.6	15.1
Other amounts owed to parent and fellow subsidiary undertakings	70.0	57.1
Other creditors	5.9	6.2
Other taxation and social security	5.2	5.1
Accruals and deferred income	270.0	261.4
Derivative financial liabilities	24.7	0.4
	732.3	596.2

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Notes to the financial statements

22. Creditors amounts falling due after more than one year

	2014 £m	2013 £m
Bank loans	555 2	552 4
Loans due to parent and fellow subsidiary undertakings	3,699 2	3,845 0
Amounts owed to parent and fellow subsidiary undertakings under finance leases	208 1	210 8
Obligations under finance leases	274 9	306 8
Borrowings	4,737 4	4,915 0
Other creditors	0 1	-
Accruals and deferred income	488 5	447 1
Derivative financial liabilities	180 3	266 2
	5,406 3	5,628 3

Borrowings are repayable as follows

	2014			2013		
	Loans not repayable by instalments £m	Finance leases £m	Total £m	Loans not repayable by instalments £m	Finance leases £m	Total £m
Financial liabilities due within one year	(306 2)	(34 7)	(340 9)	(237 8)	(13 1)	(250 9)
Between one and two years	(567 7)	(52 8)	(620 5)	(174 8)	(34 7)	(209 5)
Between two and five years	(697 9)	(86 8)	(784 7)	(1,270 3)	(117 0)	(1,387 3)
After more than five years	(2,988 8)	(343 4)	(3,332 2)	(2,952 3)	(365 9)	(3,318 2)
Total financial liabilities due after one year	(4,254 4)	(483 0)	(4,737 4)	(4,397 4)	(517 6)	(4,915 0)
	(4,560 6)	(517 7)	(5,078 3)	(4,635 2)	(530 7)	(5,165 9)

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Notes to the financial statements

Loans repayable partly or wholly after five years comprise

	5-10 years £m	10-15 years £m	15-20 years £m	>20 years £m	2014 £m
Loans due to parent and fellow subsidiary undertakings					
Fixed rate	296 2	494 0	606 3	246 8	1,643 3
Floating rate	-	20 0	13 7	-	33 7
RPI linked	-	182 3	-	874 3	1,056 6
Bank loans					
Fixed rate	150 0	-	-	-	150 0
RPI linked	105 2	-	-	-	105 2
	551 5	696 2	620 0	1,121 1	2,988 8

	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	-	789 4	597 9	246 7	1,634 0
Floating rate	-	20 8	16 8	-	37 7
RPI linked	-	35 2	141 6	851 5	1,028 3
Bank loans					
Fixed rate	150 0	-	-	-	150 0
Floating rate	-	-	-	-	-
RPI linked	102 4	-	-	-	102 4
	252 4	845 4	756 3	1,098 2	2,952 3

The weighted average interest rate on borrowings is 5.44% (2013 5.44%)

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Notes to the financial statements

23. Finance lease creditor

The minimum payments under finance leases are as follows

	2014 £m	2013 £m
Within one year	53 2	31 5
Between one and two years	71 7	54 4
Between two and five years	137 6	169 7
After five years	496 5	535 0
	759 0	790 6
Less future finance charges	(241 3)	(259 9)
Present value of lease obligations	517 7	530 7

The present values of minimum lease payments are as follows

	2014 £m	2013 £m
Within one year	34 7	13 1
Between one and two years	52 8	34 7
Between two and five years	86 8	117 0
After five years	343 4	365 9
Present value of lease obligations	517 7	530 7

Disclosed in the balance sheet as

Creditors amounts falling due within one year	34 7	13 1
Creditors amounts falling due after more than one year	483 0	517 6
	517 7	530 7

The remaining terms of finance leases ranged from 2 to 19 years at 31 March 2014. Interest terms are set at the inception of the leases. Leases with capital outstanding of £415.0 million (2013: £434.7 million) bear fixed interest at a weighted average rate of 5.4% (2013: 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

24. Financial instruments

a) Categories of financial assets held at fair value

	2014 £m	2013 £m
Fair value through profit and loss		
Interest rate swaps - not hedge accounted	12 1	21 0
	12 1	21 0
Derivatives designated as hedging instruments		
Cross currency swaps - fair value hedges	27 5	44 5
Energy swaps - cash flow hedges	-	0 9
	27 5	45 4
Total derivative financial assets	39 6	66 4

b) Categories of financial liabilities held at fair value

	2014 £m	2013 £m
Fair value through profit and loss		
Cross currency swaps - not hedge accounted	(21 7)	(8 4)
Interest rate swaps - not hedge accounted	(140 7)	(140 1)
Foreign exchange forward contracts - not hedge accounted	-	(0 1)
	(162 4)	(148 6)
Derivatives designated as hedging instruments		
Interest rate swaps - cash flow hedges	(39 6)	(116 2)
Energy swaps - cash flow hedges	(3 0)	(1 8)
	(42 6)	(118 0)
	(205 0)	(266 6)

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 prior 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 5. These contracts enable the company to mitigate interest rate risk on debt which is highly probable to be issued in AMP 5 to fund the capital programme. These have been accounted for as cash flow hedges.

During the year swaps with a notional principal of £225 million reached their start dates and hedge accounting was terminated as at 1 April 2013 because the company was not able to identify specific debt instruments that would qualify as the hedge items in a future hedging relationship.

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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 criteria of IAS 39 are met.

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 11.

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Notes to the financial statements

25 Provisions for liabilities and charges

	Deferred taxation £m	Restructuring £m	Other provisions £m	Total £m
At 1 April 2013	827.1	0.7	4.4	832.2
(Credited)/charged to profit and loss account	(160.9)	0.4	-	(160.5)
Utilised in year	-	(0.7)	(0.7)	(1.4)
Charged to other comprehensive income	16.8	-	-	16.8
Unwinding of discount	-	-	0.1	0.1
At 31 March 2014	683.0	0.4	3.8	687.2

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 (2013: 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 (2013: eight years) from the balance sheet date.

26 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 2012	935.0	(82.9)	(49.5)	40.5	843.1
Charge to profit and loss account (restated)	(5.0)	(3.5)	(1.4)	39.1	29.2
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 (restated)	-	(5.2)	(4.9)	-	(10.1)
Charge to other comprehensive income arising from rate change	-	2.1	1.0	0.1	3.2
At 1 April 2013	891.0	(88.1)	(53.7)	77.9	827.1
Reclassification	52.5	-	-	(52.5)	-
Credit to profit and loss account	(61.1)	4.5	10.4	4.6	(41.6)
Credit to profit and loss account arising from rate change	(123.1)	4.1	3.3	(3.6)	(119.3)
Charge to other comprehensive income	-	2.6	2.9	-	5.5
Charge to other comprehensive income arising from rate change	-	7.4	3.7	0.2	11.3
At 31 March 2014	759.3	(69.5)	(33.4)	26.6	683.0

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:

	2014 £m	2013 £m
Deferred tax asset	(110.0)	(151.2)
Deferred tax liability	793.0	978.3
	683.0	827.1

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27 Share capital

	2014	2013
	£m	£m
Total issued and fully paid		
1,000,000,000 ordinary shares of 10p each	100 0	100 0
	100 0	100 0

28 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 of IFRS 1

29 Infrastructure reserve

The infrastructure reserve arose on restating infrastructure assets to fair value as deemed cost on transition to FRS 101. During the previous year, bonus shares were issued from this reserve.

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30 Share based payments

At 31 March 2014 there were no options exercisable under any of the share based remuneration schemes (2013 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.

These awards are subject to Severn Trent Water's achievement of Return on Regulated Capital Value in excess of the level included in the Severn Trent Water AMP5 business plan over a three year vesting period. It has been assumed that performance against the LTIP non-market conditions will be 100% (2013 100%).

The weighted average remaining contractual life of the awards is 1.22 (2013 1.16).

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 or five years.

The weighted average share price at the date of exercise for share options exercised during the period was £18.12 (2013 £16.49). The options outstanding at 31 March 2014 had a weighted average option price of £11.25 (£10.26) and a weighted average remaining contractual life of 1.87 years (2013 1.91 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 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).

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.

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 2014. SIP shares vest with the employee on the date of grant.

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31 Cash flow statement

a) Reconciliation of operating profit to operating cash flows

	2014 £m	2013 £m
Profit before interest and tax	524.6	508.9
Depreciation of tangible fixed assets	267.5	261.4
Amortisation of intangible fixed assets	28.0	28.9
Pension service cost	22.5	23.2
Pension contributions	(63.6)	(32.5)
Pension administration costs	3.0	2.6
Share based payments charge	5.8	6.6
Profit on sale of tangible fixed assets	(8.5)	(11.9)
Deferred income movement	(9.5)	(9.3)
Provisions charged to the profit and loss account	0.4	(1.6)
Utilisation of provisions for liabilities and charges	(1.4)	(3.3)
(Increase)/decrease in stocks	(0.4)	0.2
Decrease/(increase) in debtors	2.5	(19.6)
Decrease in creditors	3.5	4.3
Cash generated from operations	774.4	757.9
Tax paid	(14.5)	(53.5)
Net cash generated from operating activities	759.9	704.4

b) Non-cash transactions

No additions to fixed assets during the year were financed by new finance leases (2013 nil) Assets transferred from developers were £28.5 million (2013 £37.0 million)

c) Exceptional cash flows

The following cash flows arose from items classified as exceptional in the profit and loss account

	2014 £m	2013 £m
Restructuring costs	-	(4.4)
Proceeds on disposal of fixed assets	9.4	15.1
	9.4	10.7

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

	As at 1 April 2013 £m	Cash flow £m	Fair value adjustments £m	RPI uplift on index-linked debt £m	Foreign exchange £m	Other non cash movements £m	As at 31 March 2014 £m
Cash and cash equivalents	328 6	(308 8)	-	-	-	-	19 8
Loans receivable from other group companies	121 2	(15 5)	-	1 3	-	-	107 0
Loans payable to other group companies	(3,917 5)	(77 0)	16 3	(28 3)	11 7	(10 6)	(4,005 4)
Bank loans	(717 7)	168 6	-	(6 1)	-	-	(555 2)
Finance leases payable	(317 4)	10 4	-	-	-	-	(307 0)
Intercompany finance leases payable	(213 3)	2 6	-	-	-	-	(210 7)
Finance leases receivable from other group companies	101 8	(0 5)	-	-	-	-	101 3
Cross currency swaps	36 1	-	(30 2)	-	-	(0 1)	5 8
Net debt	(4,578 2)	(220 2)	(13 9)	(33 1)	11 7	(10 7)	(4,844 4)

32 Financial commitments

Capital commitments are as follows

	2014 £m	2013 £m
Contracted for but not provided for	158 0	214 9

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

	2014 £m	2013 £m
Within one year	1 7	1 9
Between two and five years	4 0	6 2
After five years	4 8	5 4
	10 5	13 5

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

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33 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 for the plan as a whole.

a) Defined benefit pension schemes

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

	2014	2013
	£m	£m
Fair value of scheme assets		
Equities	870 6	877 2
Gilts	270 5	274 6
Corporate bonds	388 8	360 9
Property	148 4	147 8
Hedge funds	56 9	55 8
Cash	88 4	8 0
Total fair value of assets	1,823 6	1,724 3
Present value of the defined benefit obligations - funded schemes	(2,162 5)	(2,098 7)
	(338 9)	(374 4)
Present value of the defined benefit obligations - unfunded schemes	(9 4)	(9 3)
Liability recognised in the balance sheet	(348 3)	(383 7)

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

	2014	2013
	£m	Restated £m
Fair value at 1 April	1,724 3	1,557 2
Interest income on scheme assets	76 0	75 8
Company contributions	63 6	32 5
Contribution from intra-group asset backed funding arrangement	8 2	8 2
Other contributions from Severn Trent group companies	1 2	2 8
Contributions from scheme members	5 1	5 1
Return on plan assets (excluding amounts included in finance income)	24 9	116 3
Scheme administration costs	(3 0)	(2 6)
Benefits paid	(76 7)	(71 0)
Fair value at 31 March	1,823 6	1,724 3

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

	2014	2013
	£m	Restated £m
Present value at 1 April	2,108 0	1,903 0
Service cost	22 4	22 8
Past service cost	0 1	0 4
Interest cost	91 7	92 2
Contributions from scheme members	5 1	5 1
Actuanaal (gains)/losses arising from changes in demographic assumptions	(15 7)	155 5
Actuanaal losses arising from changes in financial assumptions	37 0	1 0
Actuanaal gains arising from experience adjustments	–	(1 0)
Benefits paid	(76 7)	(71 0)
Present value at 31 March	2,171 9	2,108 0

Of which

	2014	2013
	£m	£m
Amounts relating to funded schemes	2,162 5	2,098 7
Amounts relating to unfunded schemes	9 4	9 3
Present value at 31 March	2,171 9	2,108 0

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

	2014	2013
	£m	Restated £m
Amounts charged to operating costs		
Current service cost	(22 4)	(22 8)
Scheme administration costs	(3 0)	(2 6)
Past service cost	(0 1)	(0 4)
	(25 5)	(25 8)
Amounts charged to finance costs		
Interest cost	(91 7)	(92 2)
Amounts credited to finance income		
Interest income on scheme assets	76 0	75 8
Total amount charged to the profit and loss account	(41 2)	(42 2)

The actual return on scheme assets was a gain of £97.2 million (2013 gain of £189.5 million)

Actuanaal gains and losses for the current and prior year are reported in the statement of comprehensive income. The cumulative amount of actuanaal gains and losses recognised in equity since the adoption of the recognition and measurement principles of IFRS is a net loss of £315.7 million (2013 (restated) net loss of £319.3 million)

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

iii) Background

The group operates a number of 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

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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 1/30 and 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 schemes typically expose the company to actuarial risks such as investment risk, inflation risk and longevity risk.

Investment risk

The group's contributions to the schemes are based on actuarial calculations which make assumptions about the returns expected from the schemes' investments. If the investments underperform these assumptions in the long term then the group will need to make additional contributions to the schemes in order to fund the payment of accrued benefits.

Inflation risk

The benefits payable to members of the schemes are linked to inflation measured by the RPI. The group's contributions to the schemes are based on assumptions about the future level of inflation. If inflation is higher than the levels assumed in the actuarial calculations then the group will need to make additional contributions to the schemes in order to fund the payment of accrued benefits.

Longevity risk

The group's contributions to the schemes are based on assumptions about the life expectancy of scheme members after retirement. If scheme members live longer than assumed in the actuarial calculations then the group will need to make additional contributions to the schemes in order to fund the payment of accrued benefits.

Date of last formal actuarial valuation

Severn Trent Pension scheme (STPS)*	31 March 2013
Severn Trent Mirror Image Pension Scheme	31 March 2013

* The STPS is by far the largest of the 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 £9.4 million (2013: £9.3 million) is included as an unfunded scheme within the retirement benefit obligation.

a) Defined benefit pension schemes (continued)

(v) 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:

	2014	2013
	%	%
Price inflation	3.3	3.2
Salary increases	3.0	3.0
Pension increases in payment	3.3	3.2
Pension increases in deferment	3.3	3.2
Discount rate	4.4	4.4

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 company has adopted IAS 19 Employee Benefits Revised and therefore expected return on assets assumptions are no longer needed. The discount rate is applied to the net deficit to determine the net finance cost.

The mortality assumptions are based on those used in the triennial valuation of the STPS as at 31 March 2013.

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

Severn Trent Water Limited

Notes to the financial statements

	2014	2013
Mortality table used		
- men	"SAPS" S1NMA_L	"SAPS" S1NMA_L
- women	S1NFA_L	S1NFA_L
Mortality table compared with standard table		
- men	116%	116%
- women	92%	92%
Future improvement per annum	1 0%	1 0%
Remaining life expectancy for members currently aged 65 (years)		
- men	21 3	21 5
- women	24 4	24 6
Remaining life expectancy at age 65 for members currently aged 45 (years)		
- men	22 6	22 7
- women	26 0	26 2

a) Defined benefit pension schemes (continued)

(v) Actuarial assumptions (continued)

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 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%	Decrease/increase 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.

In presenting the above sensitivity analysis, the present value of the defined benefit obligation has been calculated using the projected unit credit method at the end of the reporting period, which is the same as that applied in calculating the defined benefit obligation liability recognised in the balance sheet.

(vi) Effect on future cash flows

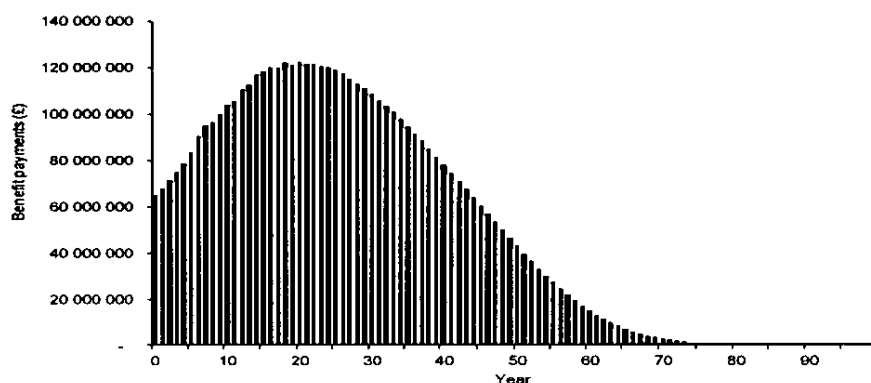
Contribution rates are set in consultation with the trustees for each scheme and each participating employer.

The average duration of the benefit obligation at the end of the year is 18 years (2013: 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



Following the completion of the triennial valuation of both schemes, future lump sum deficit contributions have been agreed with the Trustee. In respect of the shortfall, a cash contribution of £40 million was made in the current year, a further £35 million contribution will be made in the year to 31 March 2015, £15 million will be paid in the year to 31 March 2016 followed by £12 million per annum to 31 March 2025.

An annual contribution of £8.2m will also be made through an asset backing funding arrangement for at least 13 years from 31 March 2014.

b) Defined contribution pension scheme

The company participates in the group defined contribution scheme. In September 2001, the Severn Trent Group Pension Scheme (an occupational defined contribution pension scheme) was established to ensure compliance with stakeholder legislation and to provide the group with an alternative pension arrangement. This was closed to new entrants on 1 April 2005 and replaced by the Severn Trent Stakeholder Pension Scheme. The pension charge for this scheme for the year ended 31 March 2014 was £7.7 million (2013: £5.7 million).

34. 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 2014, the company had no contingent liabilities (2013: £0.2 million).

35. Related party transactions

Directors' remuneration is disclosed in note 8.

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 33.

36. 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.

Regulatory accounts – current cost financial statements

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Current cost financial statements

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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

- a) Confirm that, in their opinion, the company has sufficient financial and management resources for the next twelve months,
- b) 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,
- c) 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,
- d) 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 2014, 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



Liv Garfield
Chief Executive
For and on behalf of the board
28 May 2014

Report of the auditor

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

Independent auditors' report 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 2014 on pages 103 to 124 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 to the accounts and its Accounting Separation Methodology Statement published on the Company's website in June 2014, (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 set out on page 62, the state of the Company's affairs at 31 March 2014 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,

Report of the auditor

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

Opinion on Regulatory Accounts continued

- 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 United Kingdom Generally Accepted Accounting Practice ('UK GAAP') Financial information other than that prepared on the basis of UK GAAP 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 103 and 105 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 Financial Reporting Standards 12 and 15 be disapplied. The effect of this departure from Generally Accepted Accounting Practice and a reconciliation of the balance sheet drawn up on this basis to the balance sheet drawn up under the Companies Act 2006 is given on page 105.

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 2014 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
28 May 2014

Regulatory accounts – historical cost financial statements

Profit and loss account year ended 31 March 2014

	2014			2013		
	Appointed business £m	Non-appointed business £m	Total £m	Appointed business £m	Non-appointed business £m	Total £m
Turnover	1,524 6	12 0	1,536 6	1,492 2	10 4	1,502 6
Operating costs	(593 5)	(3 6)	(597 1)	(575 0)	(3 8)	(578 8)
Infrastructure renewals charge	(134 8)	-	(134 8)	(135 2)	-	(135 2)
Historical cost depreciation	(260 6)	-	(260 6)	(256 5)	-	(256 5)
Other operating income	8 5	-	8 5	11 8	-	11 8
Operating profit	544 2	8 4	552 6	537 3	6 6	543 9
Other income	1 8	1 8	3 6	2 1	1 8	3 9
Net interest payable	(238 0)	-	(238 0)	(278 3)	-	(278 3)
Profit on ordinary activities before taxation	308 0	10 2	318 2	261 1	8 4	269 5
Taxation on profit on ordinary activities						
- Current tax	4 6	(2 3)	2 3	9 2	(2 2)	7 0
- Deferred tax	141 5	-	141 5	3 0	-	3 0
Taxation	146 1	(2 3)	143 8	12 2	(2 2)	10 0
Profit on ordinary activities after taxation	454 1	7 9	462 0	273 3	6 2	279 5
Dividends	(332 1)	(7 9)	(340 0)	(65 8)	(6 2)	(72 0)
Retained profit/(loss) for the financial year	122 0	-	122 0	207 5	-	207 5

Statement of total recognised gains and losses year ended 31 March 2014

	2014			2013		
	Appointed business £m	Non-appointed business £m	Total £m	Appointed business £m	Non-appointed business £m	Total £m
Profit for the financial year	454 1	7 9	462 0	273 3	6 2	279 5
Actuarial gain/(loss)	(16 1)	-	(16 1)	(47 2)	-	(47 2)
Tax (charge)/credit on actuarial gain/(loss)	3 2	-	3 2	11 0	-	11 0
Tax on share based payments	-	-	-	0 7	-	0 7
Adjustment in respect of tax rate change on deferred tax	(11 3)	-	(11 3)	(2 2)	-	(2 2)
Tax charge on pension contributions	-	-	-	1 3	-	1 3
Total recognised gains and losses for the financial year	429 9	7 9	437 8	236 9	6 2	243 1

Regulatory accounts – historical cost financial statements

Balance sheet as at 31 March 2014

	2014			2013		
	Appointed business £m	Non-appointed business £m	Total £m	Appointed business £m	Non-appointed business £m	Total £m
Fixed assets						
Tangible assets	6,454 2	-	6,454 2	6,257 5	-	6,257 5
Intangible assets	1 0	-	1 0	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
	6,868 7	-	6,868 7	6,672 3	-	6,672 3
Current assets						
Stock	6 4	-	6 4	6 1	-	6 1
Debtors	592 1	-	592 1	548 6	-	548 6
Short term deposits	13 1	-	13 1	326 6	-	326 6
Cash at bank and in hand	1 2	5 5	6 7	(5 4)	7 4	2 0
Infrastructure renewal prepayment	0 8	-	0 8	(4 7)	-	(4 7)
Corporation tax receivable	50 7	-	50 7	20 9	-	20 9
	664 3	5 5	669 8	892 1	7 4	899 5
Creditors amounts falling due within one year						
Borrowings	(355 3)	-	(355 3)	(184 9)	-	(184 9)
Other Creditors						
- Creditors	(346 0)	(5 5)	(351 5)	(391 8)	(7 4)	(399 2)
	(701 3)	(5 5)	(706 8)	(576 7)	(7 4)	(584 1)
Net current liabilities	(37 0)	-	(37 0)	315 4	-	315 4
Total assets less current liabilities	6,831 7	-	6,831 7	6,987 7	-	6,987 7
Creditors amounts falling due after more than one year						
Borrowings	(4,784 6)	-	(4,784 6)	(4,878 7)	-	(4,878 7)
Other creditors	(1 5)	-	(1 5)	(1 7)	-	(1 7)
	(4,786 1)	-	(4,786 1)	(4,880 4)	-	(4,880 4)
Provisions for liabilities and charges						
- Deferred taxation	(351 6)	-	(351 6)	(498 5)	-	(498 5)
- Other provisions	(4 2)	-	(4 2)	(5 1)	-	(5 1)
Deferred income	(37 5)	-	(37 5)	(37 6)	-	(37 6)
Pension deficit	(184 8)	-	(184 8)	(199 4)	-	(199 4)
Net assets	1,467 5	-	1,467 5	1,366 7	-	1,366 7
Capital and reserves						
Called up share capital	100 0	-	100 0	100 0	-	100 0
Profit and loss account	1,367 5	-	1,367 5	1,266 7	-	1,266 7
Shareholder's funds	1,467 5	-	1,467 5	1,366 7	-	1,366 7

Regulatory accounts – historical cost financial statements

Reconciliation between statutory accounts and historical cost regulatory accounts

	2014 £m
Profit and Loss Account / Income Statement	
Turnover	
Per FRS101 statutory accounts	1,544 8
Renewables Obligation Certificate (ROC) income included in operating costs in regulatory accounts	(8 2)
Per regulatory accounts	1,536 6
Operating profit	
Per FRS101 statutory accounts	524 6
Items in FRS101 operating profit not in regulatory operating profit	
Non operating income	(3 5)
Amortisation of development costs which have previously been written off in the regulatory accounts	0 6
Depreciation of infrastructure assets	28 3
Deferred income recognised relating to fixed assets	(5 1)
Depreciation arising on capitalised borrowing costs	1 4
Items in regulatory operating profit not in FRS101 operating profit	
Difference between infrastructure renewals charge and infrastructure renewals expenditure	5 5
Goodwill amortisation	(0 3)
Other	2 9
Measurement differences	
Impairment of trade debtors	(2 7)
Difference in pension charge	0 9
Per regulatory accounts	552 6
Balance Sheet	
Tangible assets	
Net book value per FRS101 statutory accounts	6988 3
Items in FRS101 tangible assets not in regulatory tangible assets	
Remeasurement of infrastructure assets on transition to FRS101	-378 0
Cumulative impact of transferring assets from customers	-178 2
Cumulative infrastructure asset depreciation	239 4
Grants and contributions deducted from fixed assets	-255 2
Cumulative capitalised borrowing costs	-45 7
Items in regulatory tangible assets not in FRS101 tangible assets	
Cumulative difference between infrastructure renewals charge and infrastructure renewals expenditure	28 1
Infrastructure renewals accrual	-13 3
Recognition of intangible assets	69 3
Other	-0 5
Per regulatory accounts	6,454 2

Regulatory accounts – current cost financial statements

Profit and loss account appointed business year ended 31 March 2014

	Notes	2014			2013		
		Water £m	Sewerage £m	Total £m	Water £m	Sewerage £m	Total £m
Turnover	4a						
Unmeasured - household		351 1	371 5	722 6	354 0	373 3	727 3
Unmeasured - non-household		3 6	9 6	13 2	3 4	9 2	12 6
Measured - household		200 9	186 3	387 2	186 5	164 0	350 5
Measured - non-household		133 7	170 5	304 2	127 2	175 5	302 7
Trade effluent		-	10 9	10 9	-	12 3	12 3
Bulk supplies/intercompany payments		5 3	-	5 3	5 0	-	5 0
Other third party services		36 6	39 6	76 2	38 6	38 8	77 4
Other sources		1 1	3 9	5 0	1 8	2 6	4 4
Total Turnover		732 3	792 3	1,524 6	716 5	775 7	1,492 2
Current operating cost - wholesale	4c	(462 7)	(456 7)	(919 4)	(456 0)	(443 6)	(899 6)
Current operating cost - retail	4c	(60 4)	(66 8)	(127 2)	(58 7)	(64 8)	(123 5)
Other operating income		2 5	2 8	5 3	4 9	5 5	10 4
Working capital adjustment		(2 6)	(2 9)	(5 5)	(3 0)	(3 4)	(6 4)
Current cost operating profit		209 1	268 7	477 8	203 7	269 4	473 1
Other income				1 8			2 1
Net interest payable				(238 0)			(278 3)
Financing adjustment				80 5			113 8
Current cost profit before taxation				322 1			310 7
Taxation on profit on ordinary activities							
- Current tax				4 6			9 2
- Deferred tax				141 5			3 0
Taxation				146 1			12 2
Current cost profit attributable to shareholders after taxation				468 2			322 9
Dividend				(332 1)			(65 8)
Current cost retained profit/(loss)				136 1			257 1
Net revenue movement out of tariff basket		(1 0)	1 0	-	0 2	(0 4)	(0 2)
Back-billing amount identified		0 6	1 0	1 6	0 4	1 2	1 6

Regulatory accounts – current cost financial statements

Statement of total recognised gains and losses: appointed business year ended 31 March 2014

	2014 £m	2013 £m
Profit for the financial year	468 2	322 9
Actuarial gain/(loss)	(16 1)	-
Tax on actuarial gain/loss	3 2	-
Adjustment in respect of tax rate change on deferred tax	(11 3)	-
Total recognised gains and losses for the financial year	444 0	322 9

Regulatory accounts – current cost financial statements

Balance sheet: appointed business as at 31 March 2014

	Notes	2014	2013
		Total £m	Total £m
Fixed assets			
Tangible assets	5	51,521 3	50,159 5
Intangible assets		1 0	1 3
Investments - loan to group company		65 6	65 6
Investments - other		347 9	347 9
		51,935 8	50,574 3
Current assets			
Working Capital	7	45 3	60 6
Debtors		209 4	161 4
Short term deposits		13 1	326 6
Cash at bank and in hand		1 2	(5 4)
Infrastructure renewal accrual		0 8	(4 7)
Corporation tax receivable		50 7	20 9
		320 5	559 4
Creditors amounts falling due within one year			
Borrowings		(355 3)	(184 9)
Other Creditors			
- Creditors		(2 2)	(59 1)
		(357 5)	(244 0)
Net current liabilities		(37 0)	315 5
Total assets less current liabilities		51,898 8	50,889 7
Creditors amounts falling due after more than one year			
Borrowings		(4,784 6)	(4,878 7)
Other creditors		(1 5)	(1 8)
		(4,786 1)	(4,880 4)
Provisions for liabilities and charges			
- Deferred taxation		(351 6)	(498 5)
- Other provisions		(4 2)	(5 1)
Pension deficit		(184 8)	(199 4)
Net assets		46,572 1	45,306 2
Capital and reserves			
Called up share capital		100 0	100 0
Profit and loss account		1,118 6	1,004 5
Current Cost Reserve		45,353 5	44,201 7
Shareholder's funds		46,572 1	45,306 2

Regulatory accounts – current cost financial statements

Cash flow statement year ended 31 March 2014

	Notes	2014			2013		
		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	903 2	8 2	911 4	888 7	15 8	904 5
Returns on investments and servicing of finance		(195 4)	-	(195 4)	(228 6)	-	(228 6)
Taxation paid		(12 2)	(2 3)	(14 5)	(51 3)	(2 2)	(53 5)
Capital expenditure							
Gross cost of purchase of tangible fixed assets		(489 9)	-	(489 9)	(443 2)	-	(443 2)
Grants and contributions received		38 6	-	38 6	36 2	-	36 2
Infrastructure renewals expenditure		(140 3)	-	(140 3)	(147 7)	-	(147 7)
Proceeds on disposal of fixed assets		10 1	-	10 1	15 6	-	15 6
Net cash outflow from investing activities		(581 5)	-	(581 5)	(539 1)	-	(539 1)
Investment in subsidiaries		-	-	-	-	-	-
Equity Dividends Received		2 4	-	2 4	-	-	-
Equity dividends paid		(332 1)	(7 8)	(339 9)	(65 8)	(6 2)	(72 0)
Net cash outflow before management of liquid resources and financing		(215 6)	(1 9)	(217 5)	3 9	7 4	11 3
Management of liquid resources		313 6	-	313 6	(326 5)	-	(326 5)
Net cash flow before financing		98 0	(1 9)	96 1	(322 6)	7 4	(315 2)
Net cash inflow from financing		(91 4)	-	(91 4)	317 1	-	317 1
Net (decrease)/increase in cash		6 6	(1 9)	4 7	(5 5)	7 4	1 9

Notes to the regulatory accounts

Year ended 31 March 2014

1 Regulatory reporting

The regulatory accounts as reported on pages 55 to 76 should be read in conjunction with the operating and financial review on pages 23 to 29 for further understanding of the performance of the business

In particular, attention is drawn to pages 46 and 49 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 46)

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

- 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

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 1 05 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 WSRA 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.seventrentwater.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 page [xx] of the Severn Trent Water Limited Annual Report and Accounts 2014.

4 Analysis of current cost turnover and operating costs

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

	2014
	£m
Final Determination (appointed only)	1,411.8
Impact of higher/(lower) inflation	93.7
Final Determination adjusted for inflation movement	1,505.5
Optants	0.9
New Properties	(9.2)
Demolitions	(1.8)
Consumption changes - commercial	11.3
Consumption changes - domestic	15.3
	1,522.0
Other	2.6
Actual outturn (appointed only)	1,524.6

Actual income for year ended 31 March 2014 is £112.8m more than allowed for in the final determination. Of this, £93.7m is driven by higher RPI. Higher consumption accounts for £26.6m. The remaining (£7.5m) 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

	2014
	£m
Billed	1,529.5
Movement in accrual	7.1
Total turnover (appointed and non-appointed)	1,536.6

c) Analysis of operating costs

2014	Water				
	Resources £m	Raw water distribution £m	Treatment £m	Treated distribution £m	Water total £m
Operating expenditure					
Power	8.2	2.2	24.8	7.4	42.6
Income treated as negative expenditure	(0.2)	-	-	-	(0.2)
Service charges	11.0	-	0.3	-	11.3
Bulk supply imports	7.2	-	3.8	-	11.0
Other operating expenditure	9.8	1.6	48.1	85.7	145.2
Local authority rates	4.8	1.6	20.1	17.6	44.1
Exceptional items	-	-	-	-	-
Total operating expenditure excluding third party services	40.8	5.4	97.1	110.7	254.0
Capital maintenance					
Infrastructure renewals charge	1.0	2.4	-	82.1	85.5
Current cost depreciation	8.8	4.6	50.8	54.2	118.4
Recharges to other business units	-	-	-	-	-
Recharges from other business units	-	-	-	-	-
Amortisation of deferred credits	(0.1)	(0.1)	(0.8)	(0.5)	(1.5)
Amortisation of intangible assets	-	-	-	-	-
Total capital maintenance excluding third party services	9.7	6.9	50.0	135.8	202.4
Third party services					
Operating expenditure	3.7	-	1.1	0.8	5.6
Infrastructure renewals charge	-	-	-	-	-
Current cost depreciation	0.2	-	0.5	-	0.7
Total operating costs	54.4	12.3	148.7	247.3	462.7

4 Analysis of current cost turnover and operating costs**c) Analysis of operating costs continued**

2014	Sewerage				
	Sewage collection £m	Sewage treatment £m	Sludge treatment £m	Sludge disposal £m	Sewerage total £m
Operating expenditure					
Power	8.3	21.9	(0.8)	-	29.4
Income treated as negative expenditure	-	(5.3)	(5.3)	-	(10.6)
Service charges	3.5	5.5	-	-	9.0
Other operating expenditure	41.6	68.2	40.4	13.4	163.6
Local authority rates	0.3	24.5	4.3	-	29.1
Exceptional items	-	-	-	-	-
Total operating expenditure excluding third party services	53.7	114.8	38.6	13.4	220.5
Capital maintenance					
Infrastructure renewals charge	49.3	-	-	-	49.3
Current cost depreciation	34.2	125.0	26.8	0.6	186.6
Recharges to other business units	-	-	-	-	-
Recharges from other business units	-	-	-	-	-
Amortisation of deferred credits	(1.3)	(0.2)	-	-	(1.5)
Amortisation of intangible assets	-	-	-	-	-
Total capital maintenance excluding third party services	82.2	124.8	26.8	0.6	234.4
Third party services					
Operating expenditure	-	-	1.8	-	1.8
Infrastructure renewals charge	-	-	-	-	-
Current cost depreciation	-	-	-	-	-
Total operating costs	135.9	239.6	67.2	14.0	456.7

2014	Wholesale Total		
	Water Total £m	Sewerage Total £m	Wholesale total £m
Operating expenditure			
Power	42.6	29.4	72.0
Income treated as negative expenditure	(0.2)	(10.6)	(10.8)
Service charges	11.3	9.0	20.3
Bulk supply imports	11.0	-	11.0
Other operating expenditure	145.2	163.6	308.8
Local authority rates	44.1	29.1	73.2
Exceptional items	-	-	-
Total operating expenditure excluding third party services	254.0	220.5	474.5
Capital maintenance			
Infrastructure renewals charge	85.5	49.3	134.8
Current cost depreciation	118.4	186.6	305.0
Recharges to other business units	-	-	-
Recharges from other business units	-	-	-
Amortisation of deferred credits	(1.5)	(1.5)	(3.0)
Amortisation of intangible assets	-	-	-
Total capital maintenance excluding third party services	202.4	234.4	436.8
Third party services			
Operating expenditure	5.6	1.8	7.4
Infrastructure renewals charge	-	-	-
Current cost depreciation	0.7	-	0.7
Total operating costs	462.7	456.7	919.4

4 Analysis of current cost turnover and operating costs

2014	Retail		
	Household £m	Non- household £m	Retail total £m
Operating expenditure			
Customer services	34.3	2.3	36.6
Debt management	9.1	1.9	11.0
Doubtful debts	26.9	7.1	34.0
Meter reading	5.6	0.8	6.4
Services to developers	-	0.2	0.2
Other operating expenditure	19.9	2.1	22.0
Local authority rates	0.5	0.1	0.6
Exceptional items	-	-	-
Total operating expenditure excluding third party services	96.3	14.5	110.8
Third party services operating expenditure	-	-	-
Total operating expenditure	96.3	14.5	110.8
Capital maintenance			
Current cost depreciation	15.1	1.4	16.5
Amortisation of deferred credits	(0.1)	-	(0.1)
Amortisation of intangible assets	-	-	-
Total capital maintenance	15.0	1.4	16.4
Total operating costs	111.3	15.9	127.2
Debt written off	21.8	4.2	26.0

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 2013	419 0	122 9	1,746 9	1,894 0	4,182 8
Reclassification adjustment	0 3	0 4	(3 7)	1 2	(1 8)
RPI adjustment	10 6	3 1	41 5	44 9	100 1
Disposals	(6 3)	(0 6)	(15 9)	(34 2)	(57 0)
Additions	1 8	0 1	65 9	69 8	137 6
At 31 March 2014	425 4	125 9	1,834 7	1,975 7	4,361 7
Depreciation					
At 1 April 2013	286 4	73 8	994 4	1,184 1	2,538 7
Reclassification adjustment	(0 3)	0 2	(1 7)	0 5	(1 3)
RPI adjustment	7 3	1 9	25 4	30 0	64 6
Disposals	(2 9)	(0 6)	(15 8)	(33 8)	(53 1)
Charge for the year	9 0	4 6	51 3	54 2	119 1
At 31 March 2014	299 5	79 9	1,053 6	1,235 0	2,668 0
Net book value					
At 31 March 2014	125 9	46 0	781 1	740 7	1,693 7
At 1 April 2013	132 6	49 1	752 5	709 9	1,644 1
Infrastructure assets					
Gross replacement cost					
At 1 April 2013	1,060 1	1,379 1	3 7	12,198 1	14,641 0
RPI adjustment	26 0	33 8	0 3	301 5	361 6
Additions	1 2	0 8	0 6	63 2	65 8
At 31 March 2014	1,087 3	1,413 7	4 6	12,562 8	15,068 4

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 2013	963 6	4,151 6	705 0	5 6	5,825 8
Reclassification adjustment	(6 0)	3 6	6 7	1 6	5 9
RPI adjustment	23 7	96 0	20 3	0 2	140 2
Disposals	(9 1)	(27 8)	(10 1)	(1 0)	(48 0)
Additions	44 1	142 5	64 1	0 1	250 8
At 31 March 2014	1,016 3	4,365 9	786 0	6 5	6,174 7
Depreciation					
At 1 April 2013	565 9	2,206 3	418 5	4 0	3,194 7
Reclassification adjustment	(5 0)	3 6	3 9	0 9	3 4
RPI adjustment	14 6	55 1	12 3	0 1	82 1
Disposals	(8 8)	(27 7)	(9 8)	(1 0)	(47 3)
Charge for the year	34 2	125 0	26 8	0 6	186 6
At 31 March 2014	600 9	2,362 3	451 7	4 6	3,419 5
Net book value					
At 31 March 2014	415 4	2,003 6	334 3	1 9	2,755 2
At 1 April 2013	397 7	1,945 3	286 5	1 6	2,631 1
Infrastructure assets					
Gross replacement cost					
At 1 April 2013	53,342 0	11 6	-	-	53,353 6
RPI adjustment	1,308 6	0 1	-	-	1,308 7
Disposals	-	-	-	-	-
Additions	53 9	2 1	-	-	56 0
At 31 March 2014	54,704 5	13 8	-	-	54,718 3

			Wholesale Total
	Water Total £m	Sewerage Total £m	Wholesale Total £m
Non-Infrastructure assets			
Gross replacement cost			
At 1 April 2013	4,182 8	5,825 8	10,008 6
Reclassification adjustment	(1 8)	5 9	4 1
RPI adjustment	100 1	140 2	240 3
Disposals	(57 0)	(48 0)	(105 0)
Additions	137 6	250 8	388 4
At 31 March 2014	4,361 7	6,174 7	10,536 4
Depreciation			
At 1 April 2013	2,538 7	3,194 7	5,733 4
Reclassification adjustment	(1 3)	3 4	2 1
RPI adjustment	64 6	82 1	146 7
Disposals	(53 1)	(47 3)	(100 4)
Charge for the year	119 1	186 6	305 7
At 31 March 2014	2,668 0	3,419 5	6,087 5
Net book value			
At 31 March 2014	1,693 7	2,755 2	4,448 9
At 1 April 2013	1,644 1	2,631 1	4,275 2
Infrastructure assets			
Gross replacement cost			
At 1 April 2013	14,641 0	53,353 6	67,994 6
RPI adjustment	361 6	1,308 7	1,670 3
Disposals	-	-	-
Additions	65 8	56 0	121 8
At 31 March 2014	15,068 4	54,718 3	69,786 7

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 2013	262.7	24.4	287.1
Reclassification adjustment	(3.8)	(0.3)	(4.1)
RPI adjustment	6.5	0.4	6.9
Disposals	(26.2)	(2.8)	(29.0)
Additions	3.4	0.4	3.8
At 31 March 2014	242.6	22.1	264.7
Depreciation			
At 1 April 2013	176.8	15.8	192.6
Reclassification adjustment	(1.9)	(0.2)	(2.1)
RPI adjustment	4.7	0.3	5.0
Disposals	(26.0)	(2.8)	(28.8)
Charge for the year	15.1	1.4	16.5
At 31 March 2014	168.7	14.5	183.2
Net book value			
At 31 March 2014	73.9	7.6	81.5
At 1 April 2013	85.9	8.6	94.5

6 Analysis of capital expenditure, grants and land sales

	2014			2013		
	Gross £m	Grants & contributions £m	Net £m	Gross £m	Grants & contributions £m	Net £m
Capital expenditure - water						
Base						
Infrastructure renewals expenditure (IRE)	97 7	(8 9)	88 8	105 4	(7 5)	97 9
Maintenance non-infrastructure (MNI)	101 3	(2 9)	98 4	98 3	(3 3)	95 0
Enhancements						
Infrastructure enhancements	65 8	(15 5)	50 3	50 7	(15 7)	35 0
Non-infrastructure enhancements	37 9	-	37 9	32 3	(0 4)	31 9
Total capital expenditure - water	302 7	(27 3)	275 4	286 7	(26 9)	259 8
Grants and contributions - water						
Developer contributions		(11 7)			(11 0)	
Infrastructure charge receipts - new connections		(6 6)			(6 0)	
Other contributions		(9 0)			(9 9)	
Total grants and contributions - water		(27 3)			(26 9)	
Capital expenditure - sewerage						
Base						
Infrastructure renewals expenditure (IRE)	54 7	(3 2)	51 5	51 1	(1 3)	49 8
Maintenance non-infrastructure (MNI)	183 9	-	183 9	151 6	(0 1)	151 5
Enhancements						
Infrastructure enhancements	37 5	(8 0)	29 5	34 9	(5 9)	29 0
Non-infrastructure enhancements	59 0	(0 1)	58 9	64 2	(2 2)	62 0
Large projects capex						
Infrastructure enhancements	-	-		-	-	-
Non-infrastructure enhancements	-	-		-	-	-
Total capital expenditure - sewerage	335 1	(11 3)	323 8	301 8	(9 5)	292 3
Grants and contributions - sewerage						
Developer contributions		(1 1)			(1 7)	
Infrastructure charge receipts - new connections		(7 0)			(6 4)	
Other contributions		(3 2)			(1 4)	
Total grants and contributions - sewerage		(11 3)			(9 5)	
Total capital expenditure - water and sewerage	637 8	(38 6)	599 2	588 5	(36 4)	552 1
Land sales - Proceeds from disposals of protected land			10 1			15 6

7 Working capital

	RESTATED	
	2014	2013
	£m	£m
Stock	6 4	6 1
Trade debtors		
Measured household	45 5	47 7
Unmeasured household	74 0	78 5
Measured non-household	21 8	21 7
Unmeasured non-household	0 6	0 5
Other	6 6	2 7
Measured income accrual	174 0	165 8
Prepayments and other debtors	60 2	70 2
Interco Drs	-	-
Trade creditors	(15 6)	(15 5)
Deferred income - customer advance receipts	(138 0)	(127 0)
Capital creditors and accruals	(41 4)	(33 7)
Accruals and other creditors	(148 8)	(156 4)
Working capital	45 3	60 6
Total revenue outstanding - household	218 2	219 6
- non-household	32 5	29 3

There has been no significant movement in our total gross debt outstanding (0.4%)

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

	2014	2013
	£m	£m
Current cost operating profit	477 8	473 1
Working capital adjustment	5 5	6 4
Movement in working capital	7 6	(30 7)
Receipts from other income	1 8	2 1
Current cost depreciation after amortisation of deferred income	319 1	312 9
Current cost profit on disposal of tangible fixed assets	(5 3)	(10 3)
Infrastructure renewals charge	134 8	135 2
Other non-cash profit and loss items	(38 1)	-
Net cash inflow from operating activities	903 2	888 7

9 Analysis of net debt

	Fixed interest rate £m	Floating interest rate £m	Index linked £m	Total £m
Bank Loans	150 0	300 0	105 2	555 2
Loans due from parent and fellow subsidiary undertakings	-	(107 0)	-	(107 0)
Loans due to parent and fellow subsidiary undertakings	2,626 7	318 1	1,056 6	4,001 4
Finance Lease receivables	(101 3)	-	-	(101 3)
Finance Lease payables	412 0	105 7	-	517 7
Total net borrowings	3,087 4	616 8	1,161 8	4,866 0
Impact of interest rate swaps entered into by the company	366 4	(366 4)	-	-
Total borrowings	3,453 8	250 4	1,161 8	4,866 0
Total borrowings				4,866 0
Overdraft				(6 7)
Short term deposits				(13 1)
Net Debt				4,846 2
Regulatory capital value				7,617 6
Gearing				63 6%
Full year equivalent nominal interest cost	187 1	2 7	51 7	241 5
Full year equivalent cash interest payment	187 1	2 7	22 1	211 9
Indicative interest rates				
Indicative weighted average nominal interest rate	5 4%	1 1%	4 5%	4 9%
Indicative weighted average cash interest rate	5 4%	1 1%	1 9%	4 3%
Weighted average years to maturity	10 0	1 9	35 4	15 0

The Severn Trent Water Regulatory Accounts have been prepared on a single company basis for 2013/14 (consistent with the prior year) Up to and including 2011/12, we prepared regulatory accounts based on the Severn Trent Water consolidated group The table below sets out a reconciliation between net debt on a single company basis and net debt on a consolidated basis, as well as the resultant effect on gearing

	£m
Severn Trent Water Limited net debt as at 31 March 2014	4,846 2
Intra group loans and leases	-380 8
Net debt held in STW subsidiaries	-0 6
Severn Trent Water Limited net debt - consolidated basis	4,464 8
Year end RCV	7,617 6
Gearing based on net debt on consolidated basis	58 6%

Supplementary Regulatory Accounting Disclosures – unaudited

Year ended 31 March 2014

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

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	13.9	May 2013 - July 2014	3 Month LIBID
East Worcester Water Limited	Repaid	2.3	October 2013	3 Month LIBID
Severn Trent Leasing Limited	Borrowed	8.5	March 2014	0.0475
Severn Trent Leasing Limited	Repaid	0.6	April 2013 - January 2014	0.0475
Severn Trent Plc	Borrowed	112.0	September 2013 - March 2014	LIBOR + 0.6%
Severn Trent Plc	Repaid	46.0	October 2013 - March 2014	LIBOR + 0.6%
Severn Trent Utilities Finance Plc	Repaid	0.02	January 2014	3 Month 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 2013/14 amounted to £340.0 million (2013: £72.0 million), being 34.0p per share (2013: 7.2p per share)

c) Transfer of assets/liabilities

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	0.8
Water, tankering, reception, treatment and disposal of waste	Various	Market rent	0.5
Sale of crops	Severn Trent Green Power Ltd	Cost	0.9
Management charge	Severn Trent Plc	Cost	6.1
			8.3

Services supplied to the appointee by associated companies

Company	Turnover	Nature of transactions	Services supplied to the appointee			
			Competitive letting £m	Other market testing £m	No market £m	Total £m
Derwent Insurance Ltd	7.9	Insurance services	-	6.1	-	6.1
Severn Trent Services Ltd	5.9	Supply of materials and other engineering services	1.4	-	-	1.4
Severn Trent Green Power Ltd	3.2	Supply of Electricity	-	1.2	-	1.2
Severn Trent Plc (mgmt charge)	-	Pass through costs	-	-	1.2	1.2
	17.0		1.4	7.3	1.2	9.9

e) Omission rights

None

f) Waivers

None

g) Guarantees

None

Supplementary Regulatory Accounting Disclosures – unaudited

Year ended 31 March 2014

Analysis of properties

	2014		2013	
	Water	Sewerage	Water	Sewerage
Number of properties ('000s)				
Households billed	3,138.4	3,580.3	3,126.8	3,563.8
Non-households billed	182.8	197.8	183.5	200.0
Household voids	132.6	149.6	124.7	154.1
Non-household voids	29.9	50.2	28.7	41.9
Properties served by new appointee in supply area as at 1 April 2009	8.0	8.0	6.0	6.0
Per capita consumption (excluding supply pipe leakage) l/h/d				
Unmeasured household	138.3		129.9	
Measured household	112.6		104.6	
Volume (Ml/d)				
Bulk supply export	55.2	-	59.2	-
Bulk supply import	351.6	-	370.0	-
Distribution input	1,817.9		1,766.3	