Scottish Water

Always serving Scotland

Annual Report and Accounts 2012/13

Record performance, great value

Our vital role

Scottish Water is always serving Scotland, providing vital services which are essential to daily life. We continue to deliver excellent value for our customers.

We provide clean, safe and high quality drinking water to 2.4 million households and 159,000 business premises across Scotland. Every day we provide 1.3 billion litres of clear, fresh drinking water and take away 840 million litres of waste water, which we treat before returning to the environment.

We are delivering one of the largest investment programmes in the UK water industry during 2010-15. This at a time when our average household charge remains the lowest in Great Britain. In 2013/14, the average household charge in Scotland is £54 lower per year than the average household charge in England and Wales.

The quality of our drinking water is at an all-time high and our investment is delivering the benefits Scotland needs.

Contents

Your charges go towards maintaining and improving:

29,910
miles of water pipes

252
water treatment works

1.3 billion
litres of high quality drinking water every day

1,865
waste water treatment works

31,064
miles of sewer pipes

Highest ever drinking water quality

During 2012, 99.88% of samples complied with strict quality standards, representing the highest ever drinking water quality in Scotland.

Customer satisfaction at record levels

We have out-performed our Customer Satisfaction Delivery Plan target by 5%, achieving a score of over 88% – our best ever.

High investment across Scotland

£487 million of investment in 2012/13 is delivering benefits for customers while supporting thousands of construction jobs across Scotland.

Customer bills lowest in Great Britain

In 2013/14, the average combined household charge is £334, the equivalent of less than £1 a day[1]. This is £54 lower per year than the average bill in England and Wales.

Huge reduction in leakage

We have reached the Economic Level of Leakage (ELL) – the industry measure – a year ahead of target. Leakage was further reduced by 54 million litres of water per day in 2012/13.

Health and Safety recognition

Our commitment to the highest standards of health and safety was recognised by the Royal Society for the Prevention of Accidents (RoSPA). For the second year in a row, we have won the industry award for the water sector.

[1] The average household is between Council Tax Band B and Band C and has a combined bill of less than £1 a day. Individual water supply and waste water collection charges are less than £1 a day for all households (except for the individual water supply and waste water collection charges for Band H households).

"We are placing our customers at the heart of planning the future of our business, while delivering record performance and great value."

Ronnie Mercer Chair

Scottish Water is now well into its second decade and 2012/13 has seen another year of continued strong performance and leadership.

We have built a business which Scotland can be increasingly proud of, delivering welcome investment in the country's essential water and waste water infrastructure while supporting the economy, and improving service to – and the relationship with – our 5 million customers in communities from Stranraer to Shetland.

We are now into the third year of the 2010-15 regulatory period and another stage in our journey to match the best in the UK water industry.

Average household charges remain the lowest in Great Britain, while customer service levels are continuing to improve.

We are sustaining high levels of performance and placing our customers in a pivotal role in the planning for the future of the business. This year, we carried out the biggest ever consultation in the water industry in Scotland to gather the views of our customers as we look ahead to 2040.

We are working closely with Consumer Focus Scotland and the Customer Forum to ensure our business plans for 2015-21 meet our customers' expectations.

On a sad note, I want to pay tribute to the huge contribution made to the Scottish Water success story by Chief Executive Richard Ackroyd, who passed away suddenly in October 2012. In his 4 years at the helm, Richard oversaw one of the most successful periods in our development and had the foresight to build a strong leadership team, backed by dedicated employees in every community across Scotland. This ensured the business continued its rapid progress without interruption.

Douglas Millican, our former Finance and Regulation Director, has since been appointed Chief Executive, becoming only the third person to hold the role since our formation in 2002. Douglas himself has played a key role in Scottish Water's development and will take the business forward, building on Richard's legacy.

As a billion pound business, Scottish Water is looking forward as a modern, dynamic company in the spirit of the hydro nation.

In the past year, we have been focusing on areas of the business which will give us the biggest and most sustainable growth. We are re-focusing our growth strategy on promoting renewable generation through the use of our assets. We have had some early successes and are already producing about 6% of our own electricity, with the potential to substantially increase this, helping to reduce costs for the benefit of customers.

Our achievements are being noticed around the world, with our International consulting business working in Qatar, New Zealand, India and Poland, sharing the water industry knowledge and expertise we have gained on our journey to becoming an industry leader.

Scottish Water Business Stream, formed in 2006 to compete in the retail market, is delivering real benefits to business customers, who are now paying less than they would have without competition. Business Stream is now active in England and Wales as the market opens up to retail competition.

We are firmly committed to serving Scotland and all of our customers. I would like to thank my Board, management team and employees for their continued commitment to the business and our customers. We firmly believe that engaged employees result in improved performance and, as a result, customers are more satisfied with the service they receive. I would personally like to thank Pat Kelly for his long and valuable service to the Board of Scottish Water.

"We have had another excellent year of achievement, building on the success of our first 10 years."

Douglas Millican Chief Executive

Scottish Water has gone from strength to strength in the past year. Drinking water quality is at its highest ever level, service to our customers has improved further and we are delivering efficient investment in Scotland's water and waste water infrastructure, while supporting thousands of construction jobs in communities across Scotland.

In 2012/13 we delivered £487 million of investment, in line with our delivery plan. This is part of the £2.5 billion investment in this regulatory period 2010-15. We are ahead of target for delivery of the overall Q&S IIIb investment programme.

In Glasgow, we launched our £250 million investment plan to upgrade the city's waste water network, to help improve the environment of the River Clyde and its tributaries and tackle flooding.

We work every day of the year to provide high quality drinking water, protect and enhance the natural environment and support Scotland's communities and the economy. We put our customers at the heart of everything we do and every decision we make.

Customer service is measured in a number of ways known as the Overall Performance Assessment (OPA) score. This looks at 17 measures such as time without a normal water supply, water pressure, water quality and pollution incidents. We have out-performed our regulatory target on OPA and are closer than ever to being in the top quartile of the leading water companies in the UK.

We are committed to improving our service to our customers and putting them in a pivotal role in the planning for the future. The level of customer satisfaction has increased to over 88%, up 5%. We will continue to listen to our customers and work to deliver the best possible service at the lowest cost.

We have reduced the amount of water leaking from our pipes and have reached the Economic Level of Leakage (ELL) a year ahead of target.

This comes at a time when household charges continue to deliver value for money for our customers. In 2013/14 Scottish Water charges increased for the first time in 4 years, with a below the rate of inflation rise of 2.8%, the first increase since 2009. This ensures that, because of our continued efficiency programme, the average charge in Scotland is £54 a year less than the average in England and Wales.

Our household customers benefited by around £40 million from the freezing of household charges in 2012/13, at a time when many of our costs were increasing. The impact of this on the financial results was limited to a reduction in surplus of £11.9 million to £95.1 million by our achievement of further efficiencies.

We are building a sustainable business, in line with Scottish Government objectives on sustainability, carbon reduction and the growth of a hydro nation, in which Scottish Water plays a key role. The water industry – including Scottish Water – is already facing challenges, not least climate change, and seizing the opportunity for more innovation.

Scottish Water's further performance improvement in 2012/13 is due to the dedication of all our employees and their shared passion to turn Scottish Water into Scotland's most valued and trusted business. Our team leaders have engaged their teams in the challenges we face, and the opportunities presented, and have together driven our performance higher. Our performance increasingly reflects a focus on planned and predictive maintenance and management to deliver consistently excellent customer service, water quality and environmental performance. I am very grateful for the dedication of all our people at Scottish Water – whether in the meticulous planning of future service improvements, the seeking-out of new innovations or responding to customer priorities in extreme weather conditions.

I want to record how honoured I am to be appointed Chief Executive of one of Scotland's most important businesses and I look forward to building on our current strong performance.

Always serving Scotland

Scottish Water delivers clear, fresh drinking water, safely treats waste water and helps protect the environment across Scotland – every day of the year. We do this in an affordable and sustainable way while supporting economic growth.

- We aim to deliver the very highest standards of service, ensuring our customers turn on their taps and enjoy the highest quality drinking water Scotland has ever had, while we protect and enhance the natural environment of rivers, lochs and beaches across the country.
- We will continue to deliver the investment Scotland needs and will do so efficiently while building innovation into the business.
- We aim to deliver the best value for money in the UK water industry.
- We will continue to improve the performance of the water industry in Scotland, taking into account the new challenges of a changing climate and becoming a low carbon business.

This annual report highlights our success in achieving these ambitions during 2012/13 and our plans to help us deliver our vision in the future.

Scottish Water's vision is to be Scotland's most valued and trusted business, one that we can all be proud of. This is supported through:

Serving

Ensuring the customer is at the heart of our business. Always delivering a positive customer experience is a key priority and everything we do links to improving the service and the value we provide to our customers.

Responsible

Always doing the right thing for Scotland. Our investment supports the Scottish economy, benefits our customers, visitors and local communities the length and breadth of Scotland and helps protect public health and the environment.

Committed

Ensuring we have the right people, trained, proud to work for Scottish Water and committed to improving the service for our customers across Scotland. The health and safety of our people, the contractors who work for us and our customers is built into everything we do. Ensuring we are a Scottish business that people respect.

Leading

As we work to become a low carbon business we will ensure that we will be innovative in delivering service and value for our customers, while tackling climate change and taking action to protect the environment for today's customers and future generations.

Growing

Delivering the investment to help ensure our customers continue to enjoy clear, fresh drinking water from their taps and protect our environment. We will also help communities across Scotland grow and prosper and ensure that we look at innovative and creative ways to improve service and value for our customers.

Strong

We will maintain our financial strength, continue to explore innovative ways to help deliver the best value for money for our customers and protect Scottish Water for a sustainable future.

Our objectives for 2010-15

Scottish Ministers set objectives for Scottish Water for the period 1 April 2010 to 31 March 2015. This annual report looks at the third year of the delivery period 2010-15.

We are continuing to improve the level of service to our customers and our delivery plan details the specific outputs required. These were agreed with the Drinking Water Quality Regulator (DWQR), the Scottish Environment Protection Agency (SEPA) and Consumer Focus Scotland.

These outputs will continue to deliver real benefits to our customers across Scotland – clearer, fresher drinking water at their taps, protecting the natural environment and improving service levels.

To individual customers, this could mean reducing the risk of low pressure which can affect the water-using appliances in their homes, addressing odour issues from waste water treatment works in their local area or reducing the number of customer properties at risk of external flooding from overloaded sewers.

We will deliver these benefits to our customers by improving operational practices and processes, maintaining our existing assets and investing in new or enhanced assets.

Across Scotland, we are listening to the needs of communities and delivering investment in the water and waste water networks where it is most needed.

Our objectives for 2010-2015[1] include:

- Improving the quality, look and taste of drinking water for around 950,000 customers through a mixed programme of cleaning, upgrading or replacing 2,816 miles of water mains.
- Investing £1.2 billion to ensure, as a minimum, that the standards of service provided to our customers are maintained across Scotland.
- Continuing to service new development across Scotland and address water and waste water capacity to allow further growth.
- Continuing to protect Scotland's natural environment by enhancing the waste water treatment processes at 182 works and making improvements at 223 unsatisfactory intermittent discharges to rivers, lochs and coastal waters.
- Reducing odour issues at 4 waste water treatment works.
- Creating and maintaining a register of all properties affected by external sewer flooding.
- Reducing the number of customer properties that have problems with poor water pressure.
- Improving the water supply and demand balance to provide security of supply for over 800,000 customers.

We will take steps to deliver a lower carbon water service by reducing our demand for energy, driving energy efficiency and developing our renewable energy capacity.

Delivering these objectives continues to improve the water environment and water quality in Scotland and provide real value for money for our customers.

[1] The Ministerial Directions shown reflect the original position. The Directions are subject to ongoing revision through the Technical Expression change process throughout the 2010-15 regulatory period.

Household bills still less than £1 a day[1]

The average Scottish household continues to pay the equivalent of

less than £1 a day[1]

with an annual average bill of £334 a year for water and waste water services.

Comparison with English and Welsh water companies based on OFWAT published average charges

Water and Sewerage Companies	Average Household bill for 2013/14
South West	£499
Wessex	£478
Southern	£449
Welsh	£434
Anglian	£434
United Utilities	£406
England & Wales average	£388
Yorkshire	£368
Northumbrian (North East)	£359
Thames	£354
Severn Trent	£335
Scottish Water	**£334**

Scottish Water is continuing to offer our customers excellent value for money. We are delivering one of the largest investment programmes in the UK water industry while keeping the average combined Scottish household water and waste water charge, at £334, the lowest in Great Britain for 2013/14.

We are investing to improve the natural environment of rivers, lochs and coastal waters while delivering clearer, fresher drinking water to our 5 million customers in communities across Scotland.

Scottish Water's charges were increased in April 2013 for the first time in 4 years – but below the rate of inflation. The average household charge in Scotland for 2013/14 is £54 lower than the average in England and Wales.

In 2012/13, we invested £487 million – the equivalent of £199 for every household in Scotland. Our customers are benefiting from Scottish Water's continuing strong financial performance and our focus on delivering further efficiencies. Customers across Scotland are continuing to see value in the charges they pay and improvements in the service we provide. We believe these charges offer best value for our customers in these challenging economic conditions.

Scottish Water is committed to making the most of our natural resources and using our expert knowledge to deliver best value and service to our customers. Water supply and waste water collection charges help to pay for the current £2.5 billion investment programme, which is delivering the investment Scotland needs in its water and waste water infrastructure. Millions of people are turning on their taps to clearer, fresher drinking water, enjoying a cleaner environment and receiving improved customer service as a result.

[1] The average household is between Council Tax Band B and Band C and has a combined bill of less than £1 a day. Individual water supply and waste water collection charges are less than £1 a day for all households (except for the individual water supply and waste water collection charges for Band H households).

Delivering highest ever levels of service for our customers

A key focus of our vision is placing our customers at the heart of everything we do. This approach has resulted in Scottish Water recording our highest ever levels of service for our customers in 2012/13.

Scottish Water is subject to a Ministerial requirement to improve customer service. We agreed with our regulator – the Water Industry Commission for Scotland (WICS) – challenging targets to improve service for customers. Our Overall Performance Assessment (OPA) score is used to measure our success in key areas of the business. Our 2012/13 target was to achieve an OPA score of 338. We out-performed our target by 9%, reaching a score of 368. Our year-on-year improvement in services delivered to our customers continues to demonstrate how commitment to delivering real benefits to customers is vital to surpassing our OPA targets.

In the past year we have achieved record levels of customer satisfaction. The benefits we are delivering to our customers include better quality drinking water, better water pressure and a reduction in the number of homes experiencing interruptions to supply.

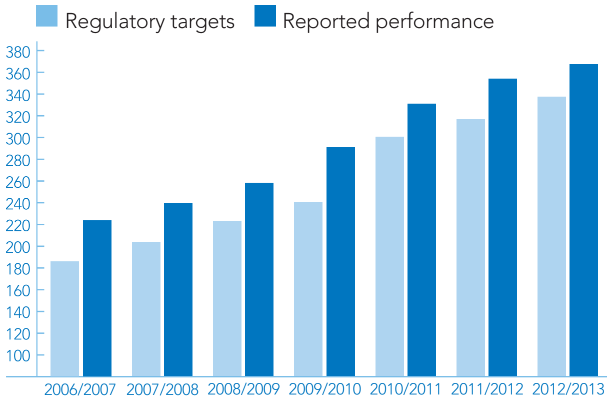
We put a real focus on listening to our customers and making it increasingly easy for them to get in touch with us, including an active and open social media presence on Twitter and Facebook.

We also measure customer satisfaction by contacting a sample of our customers who had contact with us to hear their views of how we performed. In 2012/13 we recorded our highest ever level of customer satisfaction – over 88% of customers contacted told us they were satisfied with the service they received from us. We will continue to listen to our customers and work to deliver the best possible service at the lowest cost.

Written complaints have fallen steadily, with 2012/13 seeing a 34% reduction from levels in 2011/12. This is a result of our Service Review Team continually looking at how complaints have occurred and working to improve the services we provide to our customers now and in the future.

Scottish Water's people, the men and women who provide water and waste water services to our customers across Scotland, are crucial to our success and our commitment to our customers is central to everything we do. We recognise excellence in customer service, with an internal awards process for employees which recognises our people who go the extra mile for our customers time and time again. Their professionalism, commitment and enthusiasm makes Scottish Water what it is.

Overall Performance Assessment



The key successes in 2012/13 can be attributed to improvements in a wide range of the 17 OPA indicators:

- We beat our target by 30% for environmental pollution incidents, an overall improvement of 34% on last year.
- We have improved the pressure to 938 more properties. Only 0.01% of all properties in Scotland are now affected by low pressure.
- We reduced the average number of properties affected by interruptions to supply lasting longer than 6 hours by over 7,086 – a 33% improvement on last year.
- We have reached the Economic Level of Leakage (the standard industry measure) target a year early.
- We continue to experience no hosepipe restrictions, by maintaining water supplies at all times.
- We improved our compliance in water quality, resulting in an increase of 4.15 OPA points.
- We have scored maximum OPA points for sludge disposal by ensuring all our sludge is treated according to regulations.
- We reduced by 25% the number of incidents of sewer flooding due to other causes (equipment failure, blockage or collapse of a sewer).
- We scored maximum points on the Assessed Customer Service indicator, which takes into account our performance on customer-specific activities such as our Additional Support Register, Supply Pipe Repair Policy and Compensation Policy.
- The number of written complaints dropped by 34% and we were fully compliant with our 10-day target to respond to written complaints.

Our focus on improving customer service is delivering real benefits for our customers. In 2013/14, we will build on these successes to make further improvements to the services our customers receive.

Continued investment across Scotland

During 2012/13, Scottish Water has continued the rapid transformation of the water industry in Scotland delivering clearer, fresher drinking water to our customers and improving the natural environment. Investment in £487 million of Quality and Standards (Q&S) improvements has maintained and upgraded treatment works, water mains, sewers and networks across Scotland, continuing to beat our Overall Measure of Delivery target for projects.

In the past year we have completed our major waste water projects in Airdrie and Dunoon to help protect the natural environment and our new water treatment works to supply customers in Unst, Shetland with high quality, clear, fresh drinking water. We also launched our major investment to improve Glasgow's waste water infrastructure, helping to improve the natural environment of the River Clyde and its tributaries and tackle climate change and flooding.

Improvements in Health and Safety working practices are actively promoted, resulting in improved performance and a further reduction in accidents on our sites across Scotland. This benefits construction and engineering partners and other industry bodies, taking the lessons learned on Scottish Water sites to other utility projects and developments. The Royal Society for the Prevention of Accidents (RoSPA) awards recognise the organisations that have demonstrated the best health and safety management performance in specific industry sectors. For the second year in a row, Scottish Water was the overall winner for the water industry sector, having demonstrated a consistently excellent and continuously improving performance across a wide range of key performance measures. We are the only water company to have won this prestigious award on 2 occasions.

Scottish Water continues to work more efficiently with our supply chain partners, reducing costs and helping to keep our customer charges low. We are the only water utility in the world to achieve Gold accreditation from the Chartered Institute of Purchasing and Supply (CIPS).

We are building a sustainable business in line with Scottish Government objectives on sustainability and carbon reduction. As part of this, we have started incorporating wind, hydro and solar energy into our sites to offset our power requirements at as many of our assets as possible.

Drinking water quality and standards

We have invested £78.6 million to ensure we continue to provide a high standard of quality drinking water to 2.4 million households throughout Scotland.

Environmental quality enhancements

To ensure we continue to play a key role in protecting the natural environment of Scotland, we invested £68 million on our waste water treatment works and infrastructure.

Enabling growth and development

We have invested £25.3 million to increase capacity at water and waste water treatment works and continue to address leakage within our network. This is integral to supporting the economic growth and development of Scotland's communities.

Capital maintenance

Maintaining service standards in our water and waste water treatment works and infrastructure is crucial for customers now and future generations across Scotland – our investment of £273.3 million will ensure these standards are sustained.

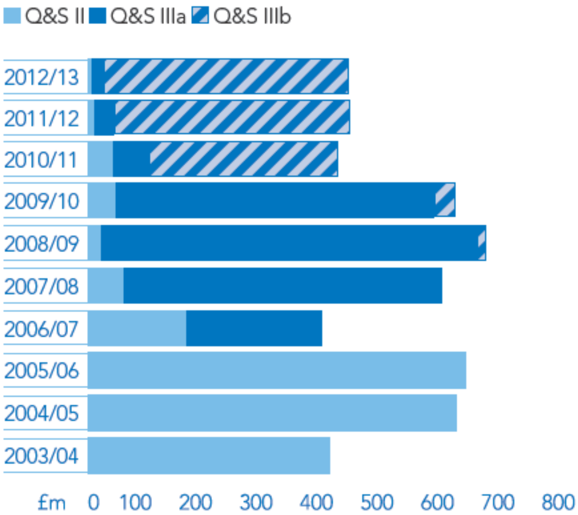
Service improvements

Investment of £13.9 million will help maintain the steady improvement of service levels for our customers.

Completion programme

We have invested £26.3 million in our completion programme to deliver the remaining projects from the previous Q&S II and Q&S IIIa programmes.

Total Q&S Capital Investment



For 2012/13, £487.4 million total is split £461.1 million for Q&S IIIb and £26.3 million for Q&S IIIa and Q&S II combined.

Continued investment across Scotland continued

The table below shows the performance highlights delivered in 2012/13, the third year of our 5 year investment programme.

Targets specified in Ministerial Objectives

Output measure specified in Ministerial Directions	Actual 2012-2013	Cumulative Values 2010-13	Ministerial Objectives 2010-15
Customer service			
Number of sites where odour is reduced	0	3	4
Number of properties removed from low pressure register	852	2,343	2,309
Number of properties removed from low pressure register (exclusions under Water (Scotland) Act 1980)	377	515	128
Number of properties alleviated from external sewer flooding	1	32	68
Growth			
Water strategic capacity (population equivalent)	5,517	52,379	– [1]
Waste water strategic capacity (population equivalent)	897	23,922	– [1]
Drinking water quality			
Number of water treatment works receiving improved disinfection controls	8	20	31
Number of zones with reduced lead levels	21	49	64
Number of backflow prevention devices installed	72	249	268
Number of sites covered by drinking water safety plans	0	196	174
Environment			
Number of unsatisfactory intermittent discharges improved (excluding 7 stage)	8	13	24
Number of unsatisfactory intermittent discharges improved (7 stage)	13	46	214
Number of waste water treatment works discharges improved to meet new licence requirements	9	36	74
Number of waste water treatment works upgraded to meet existing licence requirements	9	19	24
Number of waste water pumping stations upgraded to comply with existing licence requirements	11	16	22
Number of waste water treatment works brought into compliance with licence non-sanitary requirements	17	24	83
Number of waste water network assets made compliant with licence requirements	63	78	230

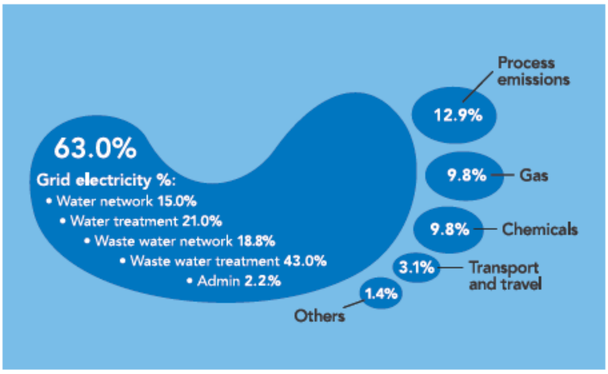
[1] Scottish Water is required to provide new strategic capacity to meet all new housing development and the domestic requirements of commercial and industrial customers.

Doing the right thing for Scotland

Our commitment to acting responsibly while reducing our costs and carbon footprint is central to making the right choices in terms of how we deliver our services. Our goal is to achieve a low carbon water industry in Scotland while delivering a service resilient to climate change.

We believe this is the right thing to do for Scotland's economy, the environment and for our customers. As a Scotland-wide business serving remote and urban communities of all sizes, we require new approaches to balancing the demands of society, the environment and the economy.

Scottish Water Greenhouse Gas Emissions Footprint 2011/12



Climate change

Increasingly frequent extreme weather events have placed a strain on Scottish Water's routine operational activities, requiring additional resources to maintain the provision of excellent customer service.

There is significant uncertainty surrounding climate change projections and how they might impact the services we provide to our customers. In 2012 we undertook work to better understand the risks we might face. This initial work has highlighted a requirement for further monitoring of how things are changing to help us take appropriate steps to deliver a resilient service.

We are committed to reducing our greenhouse gas (GHG) emissions and becoming more resilient. This must be done in ways that meet the quality, service and value expectations of our customers.

Carbon footprint

Our latest carbon footprint shows our carbon emissions have fallen by over 16,000 tonnes of CO_2e (carbon dioxide equivalents) in 2011/12 and over the past 5 years we have reduced our operational carbon footprint (CFP) by around 10%.

Our carbon footprint is being reduced despite investment to meet statutory quality enhancements. There is a clear link between enhanced treatment and energy demand. Scottish Water has both offset the increased demand and achieved a reduction in GHG emissions over the past 5 years through energy efficiency, leakage management and investment in renewables.

Our water service continues to have the lowest carbon intensity in the UK, benefiting from relatively pure water sources and widespread use of gravity in distribution.

Renewable energy

While striving towards managing and reducing energy consumption, we are also generating energy and hosting renewable technology on Scottish Water land to reduce our energy costs.

Scottish Water has installed the UK's first Difgen turbine on a strategic water main near Denny, which is managing water pressure in pipes and producing enough green energy to power up to 150 homes. We currently have 10 hydro schemes in operation, while 40 other sites are in development. Using the considerable gravity flow in large water supply pipes, Scottish Water can generate electricity and protect water treatment works from power failures. We already host third party development on some sites and are exploring the development of other wind schemes to reduce our energy demand further.

We currently generate about 6% of the electricity we consume and we are capable of significantly increasing this proportion.

Improving the environment

We are continuing to reduce the number of environmental pollution incidents (EPIs). In the past year we have reduced the number of EPIs by 34%, with a reduction of 50% in more serious Category 1 & 2 incidents over the same time period. We are working collaboratively with the Scottish Environment Protection Agency (SEPA), our environmental regulator, to help focus and target our operation and capital activities to further reduce EPIs.

We have developed our Sustainable Land Management programme to support landowners and farmers, providing education and advice on diffuse pollution following research by Audit Scotland which identified surface water as the single largest source of environmental pollution in Scotland.

Doing the right thing for Scotland continued

Leakage management

In 2012/13, we not only out-performed our annual target but also met our Ministerial Objective to reach the Economic Level of Leakage (ELL) one year ahead of schedule.

Over the past year, we reduced leakage by 54 million litres a day. We now operate at the ELL, which is the level of leakage at which it would cost more to make further reductions in leakage than to produce and supply the water to all our customers throughout Scotland. This is calculated by comparing the cost of reducing leakage against the cost of maintaining a balance between supply and demand.

This means less raw water, energy and resources are being used to treat water and provide it to homes and business premises, which helps to protect Scotland's natural environment and minimise our carbon footprint.

Since leakage targets were introduced in 2006, we have reduced leakage by nearly 50%. In 2012/13 we out-performed our reduction target by over 9.4%. Throughout that time, we have influenced research and development and made increased use of innovative technology to become a recognised leader in the field of leakage management both in the UK and internationally.

Our teams respond to bursts and leaks around the clock, helping to save water. We aim to repair reported leaks within 3 working days, and we have an expert team locating and fixing leakage which would otherwise remain underground, invisible to passers-by. Customers can now report leaks by phone or via our website, helping us locate and fix leaks faster.

Water efficiency

We remain committed to ensuring that the protection of Scotland's natural water resources is a key priority. We recognise that there are many steps we can all take to protect this valuable resource. Our Water Efficiency Plan details the key activities we undertake to help to improve the security of a sustainable water supply for our customers now and future generations.

Our approach to water efficiency is framed around 3 key areas:

- improving our assets;
- engaging with our customers; and
- working with our stakeholders and policy makers.

Improving our assets

We remain committed to working to reduce the volume of leakage across our network, while also looking to use water wisely at our assets and offices. In the past year, we have carried out a number of water usage audits at our main offices which have identified ways of further improving our internal practices. We are also investigating retrofitting water saving devices at our sites.

Engaging with our customers

We continue to engage with our customers and work in partnership with other water companies throughout the UK to promote simple but effective ways everyone can use water wisely in and around their home. We have further developed our campaign in the past year to include an interactive online water use calculator, allowing customers to calculate and compare how much water they use at home against the average person in Scotland who uses 150 litres of water a day. We have also launched a range of water efficiency films that provide advice on how to use water wisely in the kitchen, bathroom and garden.

During 2012/13, we have continued to further develop our education materials to promote water efficiency. These are being used in schools and community groups across Scotland to help customers now, and future generations, understand how we can all do simple things to use water wisely in our daily lives and help to protect the environment.

We also started work on a water efficiency trial to assess how soft measures, such as education campaigns, and hard measures, such as water efficient devices, can help our customers reduce their water consumption at home.

We will continue to develop our approach to engage with our customers and look at innovative opportunities and partnerships to promote water efficiency.

Working with our stakeholders and policy makers

We continue to work with key stakeholders, developers and policy makers to help them understand and promote the importance of more water efficient practice.

In the past year, we have been working with the Scottish Government's Building Standards on the proposed revised 2013 building standards and we are looking at ways in which we can encourage the increased water efficiency of any new developments. We are also undertaking a social housing trial which is looking at how we can work with registered social housing landlords to retrofit water efficiency measures in their properties.

We are keen to support further research and to develop understanding on water efficiency. During 2012/13, we have been working with Water Research Centre (WRc) to support research into rainwater harvesting.

We will continue to work on these 3 key areas to promote water efficiency in 2013/14.

Research and innovation

Innovation is key to sustaining high performance and delivering higher service standards. During 2012/13, research and innovation have helped us to deliver improved value and performance for our customers. We continue to find ways to further improve our service and create efficiencies in running the business, either through in-house work or in collaboration with a variety of partners.

Research engagement

During 2012/13, Scottish Water has continued to develop our research portfolio to support the strategic focus of the business. We are:

- Working in partnership with the University of Glasgow to analyse trends in water supply data to identify when there is going to be an interruption to our service. This will aid the development of procedures which will ultimately help minimise disruption to customers.
- Investigating with the University of Exeter the opportunity to vary the quality of discharges from waste water treatment works to match the environmental capacity of the receiving waters. This has the potential to allow us to reduce the treatment costs (through reduced energy and chemical use) when there are high flows in the water environment.
- Researching with Birmingham, Cranfield and Newcastle universities the extent that phosphorous (a valuable nutrient for agriculture) can be recovered from waste water processes by currently known and emerging methods.
- Working with the universities of Strathclyde and Edinburgh to develop statistical predictive models to determine the condition of our assets.
- Participating in the S3C partnership led by the University of Strathclyde on developing an asset sensor system for monitoring long-life assets such as dams or pipes.
- Supporting 9 engineering doctorate projects through STREAM, the industrial doctorate programme for the water sector led by Cranfield Water Science Institute.

European research programme

We continue to seek European partnerships through the EU Framework Programme that support our strategic aspirations. In 2012/13, we contributed towards and are playing a key role in a pan-European partnership project, worth €4.5 million. This project will benefit customers and service providers by developing a supply and demand software system that more effectively links consumption patterns of our customers to the production of water at the treatment works.

Technology development

During 2012/13, we have been working with Scottish-based technology companies to develop:

- A low-cost, small-scale ozone generation unit which has potential for rural or point-of-use applications.
- A new treatment system for small-scale applications in drinking water production.

We are also supporting 2 Scottish Water employees in the development of a device to protect drinking water supplies from potential cross-contamination from industrial applications.

Innovation in action

Scottish Water and our customers are already starting to see benefits from some key innovations we have introduced during 2012/13.

Our pump blockage detection system, developed in partnership with a Scottish-based control systems company, is helping to reduce blockages in our waste water network, save operational costs and reduce impact on our customers.

We have achieved a UK-first in a network pressure management and energy recovery system (Difgen) at Denny. This helps to minimise bursts, reduce leakage and convert the kinetic energy from the water supply network to electricity in the process.

A study into the opportunities to generate value from waste water systems has highlighted energy generation opportunities on some of our medium-sized treatment works.

Future activity

We have recently re-focused our research and innovation activities to deliver a practically focused research programme that we believe will interest the wider utility and academic community in the coming years.

We have identified 3 strategic initiatives that will help us to deliver our vision through focusing on exemplary compliance, sustainable rural communities and self-generation of energy at waste water treatment works.

We will use these initiatives to engage more effectively and build strategic relationships with academia and research providers. We will also continue to work with the enterprise community to develop relationships with suppliers which can help us achieve our aspirations over the short, medium and long term.

Through the UK Water Industry Research (UKWIR) Programme, we will work collaboratively with the wider industry on common research programmes to reduce leakage, prevent sewer flooding and reduce our carbon footprint.

Scottish Water International

Our International subsidiary is selling the skills, expertise and experience of our people, including our engineers, scientists, technicians and managers. We aim to make Scottish Water an internationally recognised business, enhancing the reputation of Scottish Water and Scotland.

We have the ability to help other countries to procure, operate and maintain publicly-owned water and waste water services effectively and efficiently. They are often dealing with similar challenges to those which we have had to face in Scotland's water industry. Our model of an independently regulated public business, which has undergone rapid transformation of efficiency and service, is in demand internationally.

Qatar

During the year, 13 of our people have worked in the Gulf state of Qatar to deliver our biggest International contract to date. We are helping to oversee management of a 5 year programme to transform the drainage and waste water service. Scottish Water International is supporting Qatar's Drainage Asset Management Programme, as a partner to leading global wet infrastructure consultants MWH.

The Public Works Authority (PWA), Qatar (Ashghal) appointed MWH Global as management contractor for the 5 year Qatar Drainage Asset Management Programme to support the organisation's goal of achieving world-class asset and operational management services.

The programme is part of Qatar's National Vision 2030 infrastructure investments, including highways, interchanges, railways, utilities and related services in response to the country's growing economy and population and recent award to host the FIFA 2022 Football World Cup.

New Zealand

One of our leakage specialists is currently working in Christchurch, New Zealand, through a contract with GHD, to support the Stronger Christchurch Infrastructure Rebuild Team. The work involves the establishment of leakage detection and management systems and processes to be incorporated in the new infrastructure following the devastating earthquake in the city in February 2011.

India

Scottish Water International supported an international business school to deliver workshops in Delhi for the Indian Ministry of Urban Development (MoUD).

The workshops focused on the structuring of public utilities, with particular reference to the Scottish Water model of public ownership with independent regulation and sustainable financing. Financing models including Public Private Partnerships (PPP), Design, Build, Finance, Operate (DBFO) and part-privatisation were addressed.

Poland

Scottish Water International has a co-operation agreement with ECM Group Polska to provide advice and support to water and waste water entities in Poland. During 2012/13, Scottish Water has prepared technical documents on managing water mains networks and treatment processes for translation into Polish. These documents have created commercial opportunities for training and document licensing which are being pursued.

Horizons

Scottish Water Horizons uses innovative ideas, knowledge and assets to encourage economic growth and the use of sustainable technologies across Scotland. We are actively working to become a sustainable, low carbon generator.

During the year, Horizons re-focused its strategy for the environmental business due to changing market conditions. Horizons is placing greater emphasis on renewable energy projects and withdrawing from the green waste and composting business.

During 2012/13, Horizons invested £5.1 million to develop renewable projects such as mini-hydro, small wind projects and food waste-to-energy schemes.

Our food waste recycling business, which offers local authorities and businesses smart food waste management solutions to avoid increasing landfill taxes, helps Scotland meet its Zero Waste ambition and generates renewable energy.

Our renewables

Our focus is on generating more renewable energy through the innovative use of Scottish Water assets, which will reduce reliance on traditional energy sources and lower Scottish Water's exposure to volatility in energy prices.

By reducing the amount of electricity we need to buy from the Grid we can reduce energy costs for the benefit of our customers, while helping to meet Scotland's renewable energy targets.

Wind

We are working with some of Europe's leading firms to jointly exploit opportunities and minimise Scottish Water's investment risk. Horizons invests in small wind schemes, typically sets of 3 (15kW) or 10 (50kW) turbine installations, at a number of our operational sites. An example in the past year has been the successful installation of 10 small-scale wind turbines in Stornoway, which are capable of generating 500kW of electricity per day – 25% of the power needs for the waste water treatment works.

Hydro

In the past year, Horizons identified 25 locations and took forward detailed development of their hydro potential. These sites demonstrated the greatest capacity for sustainable hydro energy generation with the possibility of generating 11.6GWh per year from hydro power. This includes the use of innovative Difgen technology to generate energy through pressure reduction in Scottish Water's water supply network. In 2012/13, Horizons has installed the UK's first Difgen turbine on a strategic water main near Denny.

Anaerobic digestion

Our Deerdykes Organics Recycling facility is capable of handling 23,000 tonnes of food waste a year, converting it into green electricity. This offsets about 1% of Scottish Water's annual energy demand.

Solar

During 2012/13, Horizons installed solar panel arrays at 6 Scottish Water sites, converting the natural power of sunlight into electric current. They are a particularly useful way of harnessing renewable energy in more remote locations.

Business customers

Scottish Water continues to ensure we provide a first-class service as the wholesale supplier of water and waste water services. We actively support all new entrants to the competitive water market in Scotland.

Wholesale services

The retail market for water and waste water services to non-household premises is open to competition, giving the customer choice of provider. In the case of non-household premises, Scottish Water acts as the wholesaler, providing water and waste water services to Licensed Providers who, in turn, provide services to non-household premises.

The number of Licensed Providers operational in the market increased in the past year and, with further applicants in the pipeline, the number is expected to continue to grow in the coming year. One Licensed Provider exited the market and their customers were reallocated to other Licensed Providers by the Central Market Agency, so customers experienced no break in service.

Over the year, a number of changes were made to the arrangements which govern the market to increase customer choice. Scottish Water worked with the Water Industry Commission for Scotland (WICS) and market participants to develop these arrangements. An example of changes included the launch of a meter menu, offering customers and their Licensed Providers a choice of water meter, in addition to the standard offering from Scottish Water. We also launched an online portal to assist companies and Licensed Providers with trade effluent consents, and also for them to keep track of sampling results on their discharges – a UK-first.

Business Stream

Business Stream is Scottish Water's licensed retail subsidiary, which supplies water and waste water services to business customers.

Established in 2006 as an arms-length company with its own Board and independent management team, Business Stream was formed in preparation for the opening of retail competition in 2008. The company is one of a number of competing retailers, while Scottish Water is the wholesaler to the growing market.

As well as providing licensed services such as water and waste water billing, Business Stream offers business customers a range of additional services such as water and waste water management, plant hire, and developer solutions.

So far, the company has helped its customers save more than £35 million in water efficiencies, equating to a 28,000 tonnes reduction in carbon emissions. Customers have also taken up more than £30 million of discounts, and customer satisfaction has increased by 26%.

Today, Business Stream works with more than 115,000 business customers and is using the expertise it has built up operating in Scotland's competitive market over the past 5 years to explore opportunities in the emerging non-household retail market in England.

It recently announced its first major customer switch in England, with turkey producer Bernard Matthews choosing Business Stream to supply water at its Suffolk site.

Wherever the company operates, the focus remains firmly on putting the customer at the heart of everything it does.

Doing the right thing for the future

Scottish Water is committed to playing a positive role in the lives of our customers and our people, now and in the future.

Customer engagement

We aim to engage with our customers to raise awareness of the services we provide as part of the vital role we play in daily life in terms of public health and the environment. We also want to share our knowledge and expertise in the many areas of our business, including water and waste water treatment, engineering, science, water efficiency, renewables, innovation and career opportunities.

Our approach to education is framed around 3 areas:

- engaging with our customers now and in future generations through our education programme;
- looking at innovative educational opportunities and partnerships; and
- promoting the career opportunities in Scottish Water and the water industry.

Our education programme includes a range of online Scottish Water-related activities, experiments and interactive games which have been developed for use with primary school age audiences. We continue to work to develop our education programme to ensure it links with the current Curriculum for Excellence.

Our innovative partnership approach for our Water Ways exhibit in Glasgow Science Centre (GSC) has continued to bring the message about water's journey from source to tap to a wider audience of over 320,000 children and adults in a fun, interactive and educational environment. We have also started to work with GSC to develop our outreach strategy for our education programme and, through a partnership working approach, we are looking to develop mobile educational materials, to be launched during 2013, which will allow us to take interactive educational models and activities out to schools and events to engage with our customers in communities across Scotland.

Our people

As a major employer in Scotland, we are committed to creating the right environment for our people to succeed. We believe that to become Scotland's most valued and trusted business, it is essential that our leaders are valued and trusted by the people who work for them. Leaders play a crucial role in guiding their people through change in a way that involves and engages them, and results in everyone aspiring to sustained out-performance. We take employee engagement very seriously and have achieved top quartile levels in the UK – employee satisfaction has never been higher. Our commitment to our people and to making Scottish Water a great place to work was recognised by the HR Network Scotland National Awards 2012 when we won the Best Workplace in Scotland Award.

We see our investment in the physical, emotional and mental health and wellbeing of our employees as critical to developing our resilience as an organisation. We value different perspectives and believe the diversity of our workforce delivers creative business solutions.

We are passionate about creating opportunities for young people to learn and build the skills, knowledge and experience that will help them become the next generation of water industry experts, taking the industry forward. In collaboration with our partners and relevant skills bodies, we have created qualifications, modern apprenticeship frameworks, graduate schemes and other career development opportunities at all levels in the water industry in Scotland.

In the past year, we have created new openings for 28 modern apprentices and 19 graduates on structured development programmes. We also provided places for 8 third year university interns who gained valuable experience with us and we have a further 6 graduate interns who are currently undertaking a year in industry with us since completing university. We continue to support work experience for secondary school pupils across Scotland. Our commitment to create career opportunities in the water industry also includes the TIGERS Carillion programme where, in 2012/13, we worked in partnership to support more than 25 apprentices in their skills and Modern Apprenticeship development through Scottish Water's supply chain. This partnership continues to expand and support young people into sustainable employment.

We believe that all our employees have talent and that their talents should be developed to their full potential. Our learning and development programmes gained national recognition in 2012/13 when we won 3 major awards: the Chartered Institute of Personnel and Development (CIPD) Organisational Learning Award, the Water Industry Skills Development Award and the Utility Industry Staff Development Award.

Doing the right thing for the future continued

Volunteering

Scottish Water's Volunteering Programme has now been running for over 2 years and we now have more than 1,200 employees who have taken part to help a wide variety of causes in every corner of the country. Scottish Water employees committed 4,300 working hours in 2012/13 to the benefit of charities, the environment and communities across Scotland. All our employees receive up to 2 days paid leave to participate in volunteering work which helps develop skills and teamwork, strengthens the relationship we have with local communities, and supports our Equality and Diversity outcomes.

We support employee volunteering in the following areas:

- education;
- environment; and
- local community volunteering.

In the past year, our employees have volunteered to help with our education programme at events in schools and, through partnership working, they have been involved in appropriate education-related activities in communities across Scotland. Our volunteers have presented to various groups across Scotland about the water cycle, water efficiency and the vital role Scottish Water plays in daily life. The work has ranged from our volunteers presenting to senior community groups to primary school children. This work is essential in helping to educate current and future generations of customers about the crucial role Scottish Water plays in managing this essential resource.

Scotland's rich and varied natural environment is one of the country's biggest assets. Scottish Water plays a major part in protecting and enhancing Scotland's rivers, lochs and coastal waters. The volunteering programme is helping to enhance our positive environmental impact by giving employees the opportunity to team up with local organisations on activities such as beach cleans to help make a difference in communities across Scotland.

Scottish Water is committed to working within communities. Supporting local charities is a fundamental part of this work. The past year has seen great success in our charity volunteering work. About 70 local charities have received the help of Scottish Water volunteers in everything from walking rescued greyhounds, painting a mural on a wall at a school to carol singing at a care home.

In 2012/13, organisations across Scotland have benefited from our programme. Our employees assisted Fife Countryside Rangers with conservation tasks, helped Linlithgow Angling Club with a spring clean of a local burn and spent a day working in a tree nursery with Trees for Life.

We also support activities relating to WaterAid Scotland, Scottish Water's charity of choice. Our employees contribute much of their own time to support the charity's efforts to raise vital funding for water, sanitation and hygiene projects in the developing world.

In 2012/13, Scottish Water employees have donated their time to help organise fund-raising events such as the annual WaterAid Scotland Ball, office-based raffles and even diving with sharks.

Scottish Water employees played a part in raising over £120,000 for WaterAid by climbing some of Scotland's most challenging mountains as part of the WaterAid200 Challenge. They also raised more than £10,000 on World Water Day, a United Nations day which is held annually in March, as a means of focusing attention on the importance of safe drinking water and sanitation. Scottish Water employees took part in a variety of activities to mark this important date in the calendar while also raising vital funds for WaterAid's work.

From April 2013, all money raised by WaterAid Scotland and Scottish Water employees will help to fund WaterAid's work across southern Africa. The 4 programmes in the region are: Madagascar, Malawi, Zambia and Mozambique. WaterAid is also establishing new programmes of work in Swaziland, Lesotho and Angola.

Just £15 can enable one person to access a lasting supply of safe water, improved hygiene and sanitation. The £1.5 million Scottish Water has raised over the past 10 years could transform the lives of 100,000 people by enabling them to access these basic services.

Improving services

Scottish Water is striving to become increasingly sustainable in the way we provide wholesome, high quality drinking water for our customers, while delivering safe sanitation for public health to protect and enhance Scotland's natural environment.

We are doing this by continually working to improve our processes and maintain and upgrade our existing assets and treatment works. We also invest in new or enhanced assets to ensure our services are as resilient as possible for the future and that our networks have the capacity to deal with the effects of a changing climate and increased rainfall.

Drinking water quality

The quality of Scotland's public drinking water is at an all-time high. During 2012, we carried out more than 320,000 quality tests on regulatory water samples from our water treatment works, service reservoirs and customers' taps across Scotland.

Of these samples, 99.88% of all tests met the strict microbiological and chemical regulatory standards, improving on last year's performance.

During 2012/13 we have replaced, repaired or improved 25 water treatment works and more than 635 miles of water pipes. We are also making extensive improvements in water supply networks and treatment processes to help to reduce discolouration of water supplies as a result of naturally occurring elements, such as iron and manganese, and improve the appearance and taste of drinking water for our customers.

We continue to work to ensure all our customers can enjoy the look and taste of their clear, refreshing Scottish drinking water.

Clearer, fresher drinking water – water quality

Overall compliance with microbiological and chemical standards

2012	**99.88%**
2011	99.86%
2010	99.86%
2009	99.83%
2008	99.81%
2007	99.81%
2006	99.76%
2005	99.64%
2004	99.57%
2003	99.44%
2002	99.36%

Waste water treatment

During 2012/13 we have significantly improved our waste water management performance, with more compliant waste water assets and treatment works passing strict environmental standards and a reduction in the number of pollution incidents, ensuring waste water is returned to the natural environment safely. We continue to work in collaboration with other agencies, including our environmental regulator SEPA, to find new ways to protect Scotland's natural environment.

Our drive to maintain a reduction year-on-year in environmental pollution incidents (EPIs) has resulted in a reduction from 500 in 2011/12 to 331 in 2012/13. The improvement is dramatic when compared with 824 in 2010/11. This is coupled with success in reducing the number of failing waste water treatment works to 2. In 2002, when Scottish Water was formed, the figure stood at 78.

Improving services continued

Flooding

We are committed to doing everything we can to help communities and customers by playing our part in tackling flooding and dealing with the impact of climate change and heavy rainfall.

There are many types of flooding and different organisations with various responsibilities. Scottish Water is responsible for the drainage of surface water from roofs and paved ground surfaces within boundaries. We also work to protect homes from flooding caused by sewers either overflowing or becoming blocked.

When flooding occurs, Scottish Water will offer help and support to customers and communities affected, working collaboratively with all the agencies who may have a role to play, such as SEPA and local authorities, the police and fire services.

Scottish Water is named as a Responsible Authority under the Flood Risk Management (Scotland) Act 2009. Among other duties, this requires us to participate in efforts to assess and mitigate the risk of flooding arising from the public waste water network. Currently, 6 projects are under way in partnership with local authorities and SEPA in Glasgow, Edinburgh, Grangemouth, Aberdeen, Dundee and the Irvine coastline to better understand the performance of drainage and waste water networks.

Surface Water Management Plans have to be produced by local authorities, in collaboration with Scottish Water, for areas of high-risk of flooding. These plans detail how to cope with extreme rainfall and the resulting surface water and potential flooding. They are being instigated under the Flood Risk Management (Scotland) Act 2009 which calls for Flood Risk Management Plans to be produced at a national and local level.

Glasgow investment

Across Greater Glasgow, we continue to work with our counterparts in the Metropolitan Glasgow Strategic Drainage Partnership (MGSDP) – Glasgow City Council, SEPA and others – on a number of significant projects to improve the natural environment, help reduce the risk of flooding and support the economic growth and development of the city and surrounding communities.

In early 2013, Scottish Water launched the biggest investment in the Greater Glasgow area's waste water network in more than a century when we started work on a £250 million, 5 year programme of investment which will help to improve river water quality and the natural environment of the River Clyde and its tributaries. It will also enable the Greater Glasgow area to continue to grow and develop, help to alleviate sewer flooding and deal with the effects of increased rainfall and climate change.

Together, these initiatives will help Scottish Water play our part in the success of Clyde Gateway's regeneration programme and help the city as it prepares for the Glasgow 2014 Commonwealth Games and other major events.

Sustainable Land Management

In April 2012, we launched our Sustainable Land Management (SLM) Incentive Scheme, which aims to protect and improve the quality of drinking water sources in a more sustainable, proactive way – by preventing pollutants being released in to the water environment. The scheme works in partnership with landowners, farmers and regulators and supports the delivery of practical solutions to improve drinking water quality in 6 catchment areas across Scotland which are impacted by a range of diffuse pollutants.

There has been considerable interest in the SLM Incentive Scheme since its launch. For example, in the River Ugie catchment area, more than 13% of the land managers have submitted applications to the scheme.

The detailed monitoring we are implementing in these catchments is helping us to better understand the sources and pathways of diffuse pollution. It helps us target where in the catchment our work should be focused. Furthermore, it provides a benchmark against which we can assess the success of any land-based measures taken to improve the quality of drinking water sources.

The sustainable land management approach can also be applied to other catchments in Scotland. For this reason, we have also been undertaking catchment visits for areas where land management may be having an impact on raw water quality. These visits assess the condition of the land around the watercourses, identify any poor land management practices and give recommendations to help improve drinking water quality.

Your views count

Everyone in Scotland depends on high quality, clear, fresh drinking water and the safe return of waste water to the environment. Our customers are increasingly playing a pivotal role in helping us plan for a sustainable future.

Through our customer engagement programme, we encourage our customers to give us their views on the services they receive on a daily basis, which helps us plan and assess our investment priorities.

Between November 2012 and February 2013, we held a major public consultation, Your Views Count, across Scotland to set out our future plans to:

- ensure we can continue providing high quality drinking water;
- protect and enhance the environment;
- support Scotland's economy and communities; and
- invest in future water and waste water services across Scotland.

In preparation for the public consultation, we conducted extensive research and held discussions with customer groups and stakeholders such as Consumer Focus Scotland and the Customer Forum, which both play a key role in representing the views and interests of our customers, to help us understand what is expected from our services in the future.

The consultation also set out the key challenges and opportunities that water and waste water services may face in Scotland in the next 25 years – such as climate change, demographics, legislation, resource availability, the political, economic and regulatory environment and science and technology.

During the consultation period, we carried out a wide range of activities to seek our customers' views on the future of water and waste water services in Scotland.

Customers were asked to rank their priorities for improvements in future service levels. Views were also sought on future charges and the extent to which customers would like to see less or more service improvements in return.

We believe we can continue to improve our services in the future and, with our customers' support and participation in the consultation, we aim to build on our track record for improving services and continue to develop new approaches to reliably deliver the services our customers expect.

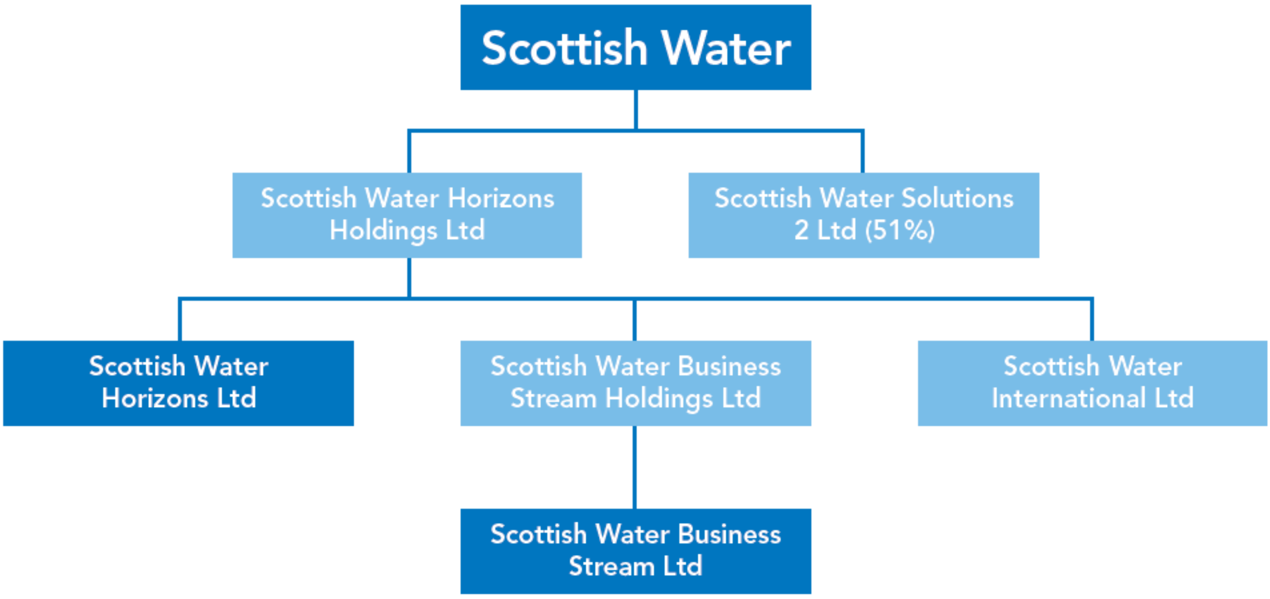
The responses are now being collated and analysed by Scottish Water.

The feedback will help shape Scottish Water's final strategic projections and business plan for 2015-21, which will be published in October 2013.

Financial and business review

Group overview
Our vision is to become Scotland's most valued and trusted business, one that we can all be proud of. Consequently, the overarching strategy for the Scottish Water group of businesses is to provide levels of service and value for money which exceed the expectations of customers, regulators and the Scottish Government while ensuring our financial strength across all parts of the Scottish Water group.

The Scottish Water group structure is summarised below:



The three main trading businesses of the Scottish Water group are: Scottish Water, which supplies households and wholesale licensed providers with regulated water and waste water services; Scottish Water Business Stream Ltd (Business Stream), our licensed retail subsidiary which supplies water and waste water services to business customers; and Scottish Water Horizons Ltd (Horizons) which provides non-regulated services to customers. Business Stream is operated and managed independently of Scottish Water in accordance with the Governance Code, which sets out the terms of separation to enable the operation of the licensed retail market for business customers.

The group surplus before tax for the year to 31 March 2013 was £95.1 million (2012: £107.0 million). Consolidated revenue in the year increased by £13.5 million to £1,145.7 million (2012: £1,132.2 million). This benefit was offset by a £28.1 million increase in costs to £866.0 million (2012: £837.9 million). Net finance costs of £184.6 million were £2.7 million lower than in 2012.

Individual business performance is reviewed below.

In the year, consolidated net debt increased by £39.6 million to £2,912.2 million (2012: £2,872.6 million). The increase was driven by additional borrowing from the Scottish Government of £100.0 million, partially offset by a £60.4 million increase in cash balances to £415.6 million. The movement in cash is summarised below:

Cash movement	Scottish Water £m	Business Stream group £m	Horizons & SW International group £m	Total £m
Opening balance at 1 April 2012	**241.0**	**110.4**	**3.8**	**355.2**
New loan from the Scottish Government	100.0	–	–	100.0
Cash generated / (utilised)	(95.5)	48.0	7.9	(39.6)
Closing cash balance as at March 2013	**245.5**	**158.4**	**11.7**	**415.6**

Cash balances within the Business Stream group of companies increased by £48.0 million over the year to £158.4 million, reflecting around £35 million of additional monies received from advance payments by customers.

Since the year end, a total of £245 million of short-term borrowing has been repaid, being £217 million by Scottish Water and £28 million by Scottish Water Business Stream Holdings Ltd (SWBSH). In addition, SWBSH is due to repay its remaining loan of £30.5 million to the Scottish Government during 2013.

Taxation

The consolidated tax charge on the income statement was £5.9 million (2012: £8.5 million). During the year, as a result of the change in the UK corporation tax rate from 24% to 23% that was effective from April 2013, deferred tax balances have been re-measured. Consequently, the effective rate for the year was 6.2% (2012: 7.9%).

Borrowing limit

Scottish Ministers set Scottish Water's (consolidated) maximum net new borrowing limit at £100.0 million for 2012/13. Actual net new borrowings in 2012/13 were £100.0 million.

Financial and business review
continued

Scottish Water

Financial framework

Scottish Water is subject to incentive-based regulation by the Water Industry Commission for Scotland (the Commission).

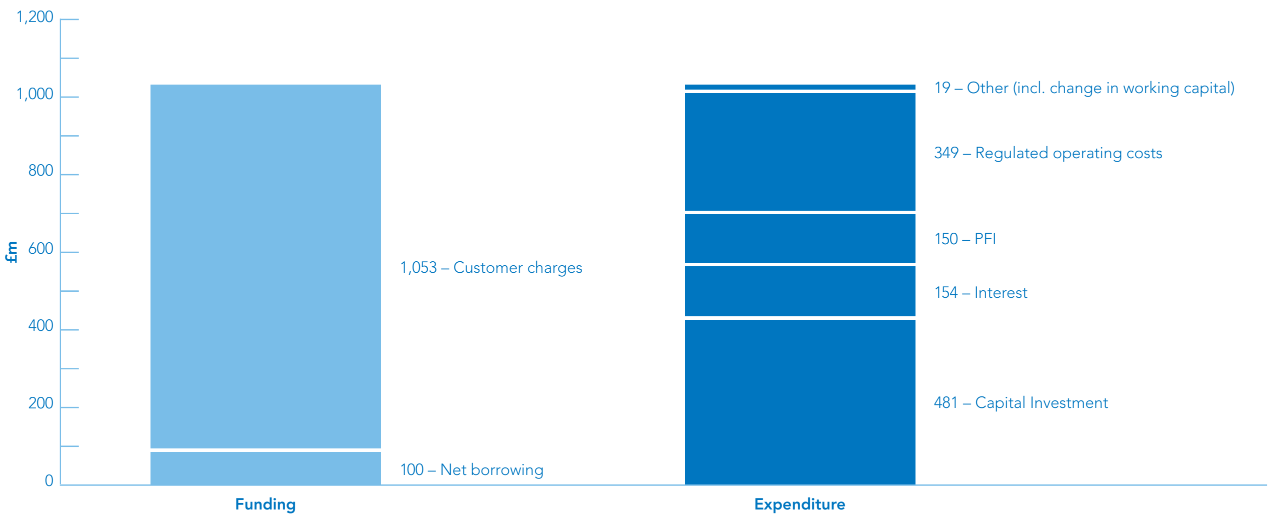
In 2009, the Commission carried out a five year price review for the 2010-15 period, which caps the prices that Scottish Water charge for water and waste water services. The combination of regulated price caps and firm constraints on borrowing from the Scottish Government creates a clearly defined limit on the financing available to Scottish Water.

Within this financial framework Scottish Water has an agreed Delivery Plan with Scottish Ministers that sets out Scottish Water's planned level of investment to deliver the required improvements and the expenditure to run its operation. Scottish Water's aim is to out-perform the targets set out in the Delivery Plan and thereby out-perform the regulatory contract.

Financial performance

The surplus before tax in the year for Scottish Water was £10.4 million lower at £63.6 million (2012: £74.0 million), reflecting the £40 million benefit to household customers of freezing household charges at a time when applicable inflation (as measured by the Retail Price Index) was 5.4%. The surplus made by Scottish Water on core service provision is required to finance our capital investment programme as is demonstrated in the chart below:

Scottish Water Funding 2012/13



Regulated revenue
Regulated revenue for the year totalled £1,053.0 million (2012: £1,045.8 million) and is analysed by category in the table below:

Regulated revenue	2012/13 £m	2011/12 £m	Change £m
Household	750.9	745.6	5.3
Wholesale	296.7	294.7	2.0
Other	5.4	5.5	(0.1)
Total regulated revenue	**1,053.0**	**1,045.8**	**7.2**

Revenue from services supplied to household customers increased by only £5.3 million to £750.9 million reflecting the increase in connected properties and the tariff freeze effective from 1 April 2012. Revenue from wholesale services supplied to Licensed Providers increased by £2.0 million or 0.7% to £296.7 million. Revenue from other sales decreased by £0.1 million to £5.4 million.

Operating costs
Total operating costs increased by £20.6 million to £807.6 million (2012: £787.0 million).

Although headline regulated operating costs of £349.3 million (2012: £340.2 million) were 2.7% or £9.1 million higher than in 2011/12, this increase was due primarily to higher charges for bad debt provisioning and local authority rates costs. However, after adjusting for these specific cost increases and the impact of inflation, like-for-like costs reduced in real terms by £1.3 million or 0.6%.

The operating cost of the PFI schemes in the year, including associated depreciation and amortisation charges, was £126.8 million, £3.4 million higher than in 2011/12 mainly because of inflation.

Depreciation and infrastructure maintenance costs decreased by £4.1 million to £329.6 million (2012: £333.7 million). Infrastructure maintenance costs were £4.7 million lower than last year, which reflects the phasing of the planned maintenance investment programme for infrastructure assets across the 2010-15 regulatory period. Non-infrastructure depreciation increased by £2.0 million as a consequence of the capital investment programme and the gain on asset sales was £1.4 million higher than in 2011/12.

Capital investment
Reported capital investment under IFRS for Scottish Water in the year was £384.2 million (2012: £347.7 million). However 2012/13 capital investment, as measured on a regulatory accounting basis, was £487.4 million (2012: £490.7 million). The table below reconciles investment as stated in the statutory accounts with investment on a regulatory accounting basis.

Reconciliation of capital additions	2013 £m	2012 £m
2012/13 investment on a regulatory accounting basis	487.4	490.7
Less base infrastructure maintenance included in operating costs under IAS 16	(96.7)	(101.9)
Less investment financed by infrastructure charges & contributions	(8.1)	(11.9)
Less SWS 1 investment realignment	–	(30.0)
Add PFI capital additions	1.6	0.8
Company capital additions per note 9 to the financial statements	**384.2**	**347.7**

Financial and business review continued

Finance costs
As at 31 March 2013, the weighted average interest cost of the outstanding long-term debt was 5.03% (2012: 5.15%). Net interest payable during the year was £154.4 million, £2.4 million lower than in 2011/12 and is analysed in the following table:

Net Interest Payable	2012/13 £m	2011/12 £m
Scottish Consolidated Fund	90.1	91.4
National Loans Fund	48.3	49.9
Public Works Loan Board	15.9	16.8
Other – net	0.1	(1.3)
Net interest payable	**154.4**	**156.8**

Finance costs associated with finance lease liabilities on PFI assets and the interest on pension scheme liabilities less the expected return on pension scheme assets increased by £0.3 million to £30.0 million (2012: £29.7 million).

During the year, net debt increased by £95.5 million to £3,023.8 million (being loans of £3,269.3 million less cash balances of £245.5 million). The increase was driven by a £100.0 million increase in borrowing from the Scottish Government, partly offset by a £4.5 million increase in cash balances.

Business Stream
The last 12 months have proved most challenging, with the economy remaining weak, reducing the volume of water consumed by customers and affecting their ability to pay for services. At the same time, we have begun to see increased competitive pressures from new entrants to the market. However, against this backdrop, Business Stream has delivered a solid set of financial results.

At the same time Business Stream has continued to grow its water and waste water solutions business, whilst taking its first steps into the English competitive market with the acquisition of its first licensed customer in January of this year.

It has continued to drive improvements in data quality and strengthened its focus on cash collection. It has continued to invest in technology to improve efficiency and provide more innovative services to customers. Key to this has been the development of a multi-channel capability, investing in more frontline staff and improving digital capability. These investments have contributed towards the increase in operating costs which rose £1.5 million or 4.4% compared to 2011/12.

The surplus before tax in the year was £35.3 million, an increase of £2.5 million or 7.6% from 2011/12. Revenue in the year, after discounts to customers, increased by £4.5 million to £361.5 million (2012: £357.0 million).

Whilst competitive pressures are expected to increase going forward, Business Stream has created a strong brand that is well positioned for long-term growth. The Westminster Government's new legislation and reforms to the English water market, creating a competitive model for the one million non-household customers by 2017, creates a significant opportunity for Business Stream in a market worth £2 billion.

Business Stream's strategy is to focus on defending its position in Scotland, using its unique experience to contribute to the reform agenda in England and to invest in for business growth.

Horizons
Horizons is responsible for the management, development and provision of non-regulated business services. Horizons' working capital requirements and investment plan are financed by organic cash flow, loans from Scottish Water Horizons Holdings, grant funding and asset disposals.

Horizons incurred an operating loss of £1.6 million before tax in the year. Due to market conditions within the Environmental business, Horizons re-focused its business strategy, placing greater emphasis on renewable energy projects and withdrawing from the green waste and composting business. Consequently, this required a write down of associated assets of £4.4 million and a restructure of the Environmental business during the financial year. Taken together, this resulted in a loss before tax of £6.0 million (2012: £1.8 million profit).

International

International was established to develop business opportunities abroad using the skills and expertise in Scottish Water to offer products and specialist consultancy services to utilities, foreign governments and other international clients. Since its formation, International has delivered services in several countries including Canada, Qatar and New Zealand.

In 2012/13, International's first full year of operation, the company was in a break-even position before tax having generated £1.4 million of revenue.

Group pension arrangements

Scottish Water is a participating employer in three Local Government Pension Schemes (LGPS) – Strathclyde Pension Fund, the North East Scotland Pension Fund and the Lothian Pension Fund. These funds are administered by Glasgow City Council, Aberdeen City Council and Edinburgh City Council respectively. Business Stream is a participating employer in the Strathclyde Pension Fund.

The administering authority for each scheme is required to conduct a triennial valuation of the assets and liabilities of the scheme in line with LGPS regulations. This must be conducted by a qualified actuary. The purpose of the valuation is to review the financial position of the fund and specify the employer contribution rates for the next 3-year period. The last valuation was carried out as at 31 March 2011. The actuarial funding position at 31 March 2011 of the Group's share of each pension fund is shown in the table below.

Fund	Value of Assets £m	Total Accrued Liabilities £m	Surplus / (Deficit) £m	Funding Level %
Strathclyde	436.8	418.5	18.3	104%
North East Scotland	228.9	246.2	(17.3)	93%
Lothian	249.3	266.7	(17.4)	93%

Employee pension contributions are determined according to the level of an employee's full-time equivalent pensionable pay. A key feature of the pension arrangements is that contribution rates are applied in tiers ranging from 5.5% to 12% depending on the employee's rate of pensionable pay on 31 March. It is anticipated that this approach to employees' contribution rates will ultimately result in a 2:1 ratio between Scottish Water's contributions and employees' contributions in a fully funded scheme.

Under IAS 19, 'Employee Benefits', a snapshot is taken of pension fund assets and liabilities at a specific point in time. Movements in equity markets and discount rates create volatility in the calculation of scheme assets and liabilities. At 31 March 2013, after taking account of deferred taxation, there was a shortfall of assets over respective liabilities of £189.6 million (2012: £213.6 million).

Board Members

Executive Members

1 | Douglas Millican, Chief Executive

Douglas was appointed as Chief Executive on 1st February 2013 following a period as Interim Chief Executive from October 2012. Douglas had previously been Finance and Regulation Director since Scottish Water was formed in April 2002. He was formerly with East of Scotland Water, initially as Financial Controller and latterly as Commercial Director. Prior to this, he worked with Price Waterhouse and Tyco. He is a Chartered Accountant with a BCom from the University of Edinburgh and is an Associate Member of the Association of Corporate Treasurers.

2 | Geoff Aitkenhead, Asset Management Director

Geoff was formerly General Manager, Customer Services and Networks, at East of Scotland Water (ESW) where he led the Asset Management Group. Previously, he was Strategic Development Manager, Operations at ESW and Capital Planning Manager at Borders Regional Council. He is a graduate of Newcastle University, a member of the Chartered Institute of Water and Environmental Management and a Fellow of the Institution of Civil Engineers. Geoff is Chairman of Scottish Water Solutions and also sits on the Board of Scottish Canals. Geoff is a former Chairman of WaterAid (Scotland), an organisation dedicated to the provision of clean water and sanitation in the developing world.

3 | Chris Banks, Commercial Director

Chris was formerly Business Development Director with Ennstone plc. Previously, he was Commercial Director at Scottish Coal and Celtic Energy, following his earlier career in minerals, shipping and construction products. He gained an MA in History at Oxford University and an MBA at Cranfield School of Management. Chris is also a Fellow of Chartered Institute of Marketing and a Member of Chartered Institute of Purchasing and Supply. Chris was a Non-executive Director of Sgoiltean Ura LLP up until the end of March 2013.

4 | Peter Farrer, Chief Operating Officer

Peter was formerly Customer Service Delivery Director and, prior to that, General Manager of Business and Asset Planning.

Prior to this, Peter was General Manager of Operations and has held various other operational and engineering roles within Scottish Water's predecessor organisations, East of Scotland Water and Lothian Water and Drainage.

He has 29 years experience in the water industry since graduating from Heriot Watt University as a Civil Engineer in 1984. He is a Chartered Civil Engineer, gained an MBA from the Edinburgh Business School in 2001 and is a Fellow of the Institution of Civil Engineers and a Vice-President of the Institute of Customer Service.

Non-executive Members

5 | Ronnie Mercer
Ronnie was appointed Chair of Scottish Water in October 2007 after having been Interim Chair of Scottish Water since April 2006. Until his retirement from Scottish Power in March 2006 he was Executive Vice President – Operations at Scottish Power's PacifiCorp subsidiary and an Executive Team Member of Scottish Power. Ronnie moved to Scottish Power from British Steel in 1994 as Generation Director. In 1998 he became Managing Director of Scottish Power's Southern Water subsidiary, after which he became a Group Director in the company.

6 | Donald Emslie
Donald Emslie is Chair of CHMC Ltd, which manages hotels across the UK and Ireland. He is also Chair of Thorpe Hall Leisure Ltd which owns the Lifehouse Spa & Hotel in Essex. He has recently stepped down from his position as Chair of the Royal Lyceum Theatre and he was previously Chief Executive of SMG plc. Donald is a Fellow of the Royal Society of Arts and The Royal Television Society and has been awarded an Honorary Doctorate from Robert Gordon University for his services to television and media.

7 | James Spowart
Jim Spowart was the founder and Chief Executive of Direct Line Financial Services, Standard Life Bank and Intelligent Finance. Jim has considerable corporate experience and retired from Intelligent Finance in 2002. He was awarded an Honorary Doctorate from Edinburgh Napier University for his contribution to banking and also to the economic development of the central belt of Scotland where he created over 5,000 banking jobs. Since he retired, he has been involved in various consultancy projects and assisted many companies including providing consultancy advice to various Banks' located both abroad and in the UK. He is currently a Commissioner to the General Assembly of the Church of Scotland (Special Economics Commission).

8 | Alan Bryce
Alan was formerly Managing Director of Energy Networks and Generation at Scottish Power. A graduate of the University of Strathclyde in 1981, he is a Fellow of the Institution of Engineering and Technology. He has served as a Non-executive Director of Iberdrola USA in New York and is currently Chair of Viking Energy Scotland and an advisor in the utilities industry.

9 | Andrew Wyllie
Andrew is Chief Executive of Costain Group PLC, the worldwide construction and engineering group. Prior to taking up this role in 2005, he worked for Taylor Woodrow where he was Managing Director of the construction business and was a member of the Group Executive Committee. He is a graduate of the University of Strathclyde, has an MBA from London Business School and is a Fellow of the Institution of Civil Engineers. He is also a Fellow of the Royal Academy of Engineering, a member of the CBI Construction Council and a Companion of the Chartered Management Institute.

10 | Lynne Peacock
Lynne is a former Chief Executive of Clydesdale and Yorkshire Banks, a role that she held from 2004 until 2011. She started her career in banking in 1983 with the Woolwich, joining the Woolwich Board in 1996, and became Chief Executive in 2000.

Lynne became a Non-executive Director of Nationwide Building Society in July 2011 and joined the Board of Standard Life as a Non-executive Director in April 2012.

11 | Matt Smith OBE (not pictured)
Matt was Scottish Secretary of UNISON until 2010 and STUC President in 1999/2000. He serves as a Scottish Human Rights Commissioner, a Member of the Standards Commission for Scotland, a Member of the Employment Appeal Tribunal and a Director of Irvine Bay Urban Regeneration Company. He is an Honorary Fellow of the Scottish Council for Development and Industry and continues to serve on their Executive. Matt has served as a JP for 26 years and continues to work with a range of regulatory and charitable organisations.

12 | Douglas Reid (not pictured)
Douglas is a former Finance Director of BG Group plc's North Sea business. He joined Scottish Gas in 1979 and held various positions in gas retailing before joining BG Group's international exploration and production business unit. He held various senior management positions in Russia, Egypt, Italy, India and Trinidad and Tobago before returning to Scotland in 2009. He has gained extensive experience in a capital intensive industry, has worked with government regulators in various countries and has extensive corporate governance experience having chaired Audit Committees of various companies. Douglas is a Fellow of the Association of Chartered Certified Accountants and a Fellow of the Chartered Management Institute.

Members' report

For the year ended 31 March 2013

The Members present their annual report together with the audited financial statements for the year ended 31 March 2013.

Accounting requirements
The financial statements have been prepared in a form directed by Scottish Ministers in accordance with section 45(2) of the Water Industry (Scotland) Act 2002.

Principal activities
Scottish Water group principal activities during the year were the supply of water and waste water services to around 5 million customers in homes and businesses across Scotland covering an area of 30,410 square miles.

Scottish Water Business Stream Ltd (Business Stream), our licensed retail subsidiary, supplies water and waste water services to business customers in the competitive retail market within Scotland. Business Stream is operationally independent of Scottish Water, as required under the Governance Code agreed with the Water Industry Commission for Scotland. Its Board has two independent non-executive directors who have no other association with the Scottish Water group.

Scottish Water Horizons Ltd (SWH) is a commercial business enterprise which provides waste management and other business services.

A review of the business and future developments for Scottish Water are presented in the Chair's Statement on page 2 and in the Financial and Business Review on pages 22 to 27.

Members
The Chair and other Non-executive Members are appointed by Scottish Ministers. Executive Members are appointed by Scottish Water after receiving consent to their appointment from Scottish Ministers. The Members as at the date of the Annual Report and their biographies are set out on pages 28 to 29.

Members and their interests
All Members have declared that they had no material interests in any contracts awarded during the year by Scottish Water. A register of Members' interests is maintained at Scottish Water's head office and is open for inspection during normal office hours.

Results
The surplus for the year after taxation amounted to £89.2 million. Details of the financial results and associated accounting policies are set out on pages 42 to 75.

Research and development
To ensure that Scottish Water derives benefit from the most up-to-date research being undertaken within the industry, research expenditure is targeted towards collaborative research with other water operators and regulators within the UK. This ensures that access is gained to high value, widely based research programmes in the Environmental, Quality, Engineering, Operational and Regulatory fields. Research into issues common to the UK water industry is procured through membership of the UK Water Industry Research Centre and the Foundation of Water Research.

Political and charitable contributions
No political or charitable contributions were made during the year. However, Scottish Water supports WaterAid, a charity founded by the UK water industry, which raises funds for water related projects overseas. Employees represent Scottish Water at fundraising events and on regional fundraising committees, which are periodically provided with facilities and other support.

Employee relations and involvement
The Scottish Water group of businesses employed an average of 3,540 staff during the year. Details of the costs incurred in relation to these staff can be found in note 5 to the financial statements on page 53. Scottish Water is committed to a policy of equal opportunities for all employees irrespective of race, religion, sex, disability or age and uses a number of forums to encourage employee involvement. Employees are kept involved through a process of regular team meetings, employee newsletters and representation on consultative forums.

Scottish Water is committed to continually improving its performance in relation to Health and Safety. Through an extensive safety awareness campaign, safety briefings and ongoing training, awareness of health and safety issues is being encouraged and increased among employees.

Payment of suppliers
Scottish Water agrees terms and conditions with suppliers before business takes place. Provided that all trading terms and conditions have been complied with, it is Scottish Water's policy and practice to pay agreed invoices in accordance with the terms of payment. At 31 March 2013, the amount owed to trade creditors was equivalent to 31 days of purchases from suppliers.

Auditors
PricewaterhouseCoopers LLP chartered accountants and registered auditors were appointed as auditors by the Auditor General for Scotland in accordance with the Public Finance and Accountability (Scotland) Act 2000.

Corporate governance

Scottish Water is committed to the principles of good governance and the code of best practice with regard to corporate governance.

The Members of Scottish Water are accountable to the Scottish Government through the Scottish Water Governance Directions 2009. This statement describes how the Members comply with the requirements of the above Directions and the provisions set out in the UK Corporate Governance Code issued by the Financial Reporting Council in June 2010.

Compliance
The Members confirm that throughout the year and up to the date of approval of the Annual Report and Accounts Scottish Water complied with:

a. The relevant sections of the UK Corporate Governance Code issued by the Financial Reporting Council in June 2010; and
b. The Scottish Water Governance Directions 2009 and other Directions, requirements and guidance issued by Scottish Ministers in so far as such matters relate to the functions of Scottish Water.

The Members of the Board
The Board of Scottish Water comprised twelve members, seven Non-executive Board Members and five Executive Board Members (see Members' biographies on pages 28 to 29) until the death of Richard Ackroyd on 28th October 2012. For the remainder of the 2012/13 financial year the Board comprised seven Non-executive Board Members and four Executive Board Members. The Board has a formal schedule of matters specifically reserved to it for decision making. Reporting to the Board are the Chief Executive and the Executive Members who have responsibility for the management of Scottish Water, and the Board Committees detailed below.

In accordance with the best practice recommended in the UK Corporate Governance Code, there is a clear division of responsibilities between the Chair and the Chief Executive. Scottish Water also benefits from the expertise of its Non-executive Members whose range of experience brings independent judgement on issues of strategy and performance, which are vital to the success of Scottish Water.

During the year, the Board met on ten occasions to review Scottish Water's operational and financial performance, business strategy and risk management.

Board and Committees
Attendance at the Board and the two principal Board committees is shown in the table below.

	Board		Audit Committee		Remuneration Committee	
Name	**Held**	**Attended**	**Held**	**Attended**	**Held**	**Attended**
Ronnie Mercer	10	10	-	-	-	-
Richard Ackroyd	5*	5	-	-	-	-
Geoff Aitkenhead	10	10	-	-	-	-
Chris Banks	10	10	-	-	-	-
Alan Bryce	10	10	-	-	5	5
Donald Emslie	10	10	-	-	5	5
Peter Farrer	10	10	-	-	-	-
Pat Kelly	10	10	-	-	5	5
Douglas Millican	10	10	-	-	-	-
Lynne Peacock	10	10	4	4	-	-
James Spowart	10	10	4	4	-	-
Andrew Wyllie	10	9	4	3	-	-

* Until his death on 28th October 2012.

Remuneration Committee
The Remuneration Committee, which is chaired by a Non-executive Member, Donald Emslie, comprises two other Non-executive Members: Alan Bryce and Pat Kelly.

The Committee, in accordance with requirements of the Scottish Water Governance Directions 2009, monitors the contract terms, remuneration and other benefits for each of the Executive Members including performance related incentive schemes. The Committee met on five occasions during the year.

The Committee has access to external independent advice as it sees fit.

Corporate governance continued

Audit Committee
The Audit Committee is chaired by a Non-executive Member, Lynne Peacock who has relevant financial experience and comprises two other Non-executive Members: James Spowart and Andrew Wyllie. The Committee met on four occasions during the year.

The Committee reviews the financial reports of Scottish Water and considers the results of the Auditors' examination and review of the financial statements. It meets with management and with internal and external auditors to review the effectiveness of internal controls and business risk management. The Chair of the Audit Committee reports to the Board on internal control and risk management matters following each Audit Committee meeting. The Committee adheres to the requirements of the Audit Committee Handbook. Each year the Committee presents an annual report of its activities to the Board prior to the Board's consideration of the Annual Report.

Executive Leadership Team
The Chief Executive is responsible for the management and operation of Scottish Water within the strategy determined by the Board and is supported by an Executive Leadership Team which he chairs. The members of the Executive Leadership Team, who are also Executive Directors, are:

Douglas Millican	Chief Executive
Geoff Aitkenhead	Asset Management Director
Chris Banks	Commercial Director
Peter Farrer	Chief Operating Officer

Strategic framework
Scottish Water operates within a broad strategic framework set by Scottish Ministers. The targets and milestones that Scottish Water has agreed to meet are set out in its Group Plan. The Group Plan also sets out the resources required and proposals for meeting and out-performing the regulatory targets and delivering on its growth ambitions. Scottish Water aims to maintain a level of financial strength that would be sufficient to enable it to secure commercial debt on cost effective terms, consistent with the Scotland Act 2012.

Scottish Water generates value for its customers by planning for, and delivering, continuous efficiency improvements in operational and capital investment activities associated with its regulated water and waste water services. The efficiency improvements assumed by the Water Industry Commission for Scotland in its strategic review of charges are passed directly to customers through real reductions in water and waste water charges. The value generated by the out-performance of these efficiency targets is retained in Scottish Water until it is returned to customers through further real reductions in water and waste water charges at the next strategic review of charges, or earlier.

The profits generated from the other licensed and commercial activities are all retained within the group and invested in the future growth of the business.

Internal control
The Members of the Board recognise their responsibility for establishing, maintaining and reviewing the systems of internal control and risk management from a financial and operational perspective. These systems are designed to manage, rather than eliminate, the risk of failure to achieve business and operational objectives and to provide reasonable, but not absolute, assurance against material misstatement or loss.

The systems of internal control are compliant with the relevant sections of the UK Corporate Governance Code and the Scottish Water Governance Directions 2009. They are based on an ongoing process designed to identify those risks material to the achievement of Scottish Water's policies, aims and objectives, to evaluate those risks and to manage them effectively in accordance with good risk management practices. The risk management process has been in place for the full year under review and up to the date of approval of the Annual Report and financial statements.

Risk management
Scottish Water has established a risk policy that defines risk appetite and sets out a consistent approach to the management of risk.

The business identifies key risks at corporate and functional levels. Risks are evaluated by considering their consequences, in terms of impact and likelihood, on the achievement of service delivery and business objectives. Existing arrangements for managing the risks are considered and, where these are not perceived to be effective, action plans are drawn up which aim to achieve the right balance between risk and control.

Key risks in relation to monitoring water quality and planning for and managing water quality incidents are being managed in a reasonable and prudent manner, having regard to the current regulatory framework and available resources.

Risk management is integral to the business and financial planning process in Scottish Water and this continues to develop in line with business needs. Escalation procedures are in place.

The risk register and risk management processes are reviewed annually by the Board, twice a year by the Audit Committee and the Executive Leadership Team. In addition, each quarter, the Board reviews the status of the most significant business risks.

Control activities
Scottish Water's Internal Control Framework incorporates:

- Policy-making and strategic direction at Board level. There is a formal schedule of matters reserved for decision by Board Members.
- An organisational structure which clearly defines lines of authority and accountability.
- A statement of general principles pertaining to rules and procedures for the regulation of the business.
- Financial authority limits governing delegation of authority by the Board.
- Regular review by the Board and management of service, quality and financial performance compared to plan.
- Development of procedure manuals for staff instruction and guidance.
- Project approval, monitoring and control processes specifically developed for capital expenditure.
- High profile given by the Board and management to Health & Safety issues.

High quality personnel are viewed as an essential part of the control environment. Ethical behaviour is incorporated into staff conditions of service and demanding recruitment criteria and a policy for the development and training of staff supports ethical standards.

Control effectiveness review
Reviewing control effectiveness is a continuous process throughout the year. The Board gains assurance as to the effectiveness of internal control through a collaborative approach, based on the work of internal and external audit, other internal and external review agencies, and Executive Members' reports. The controls assurance process is co-ordinated by internal audit and incorporates self-assessment by management, independent assessment by audit, and annual statements of assurance from senior management.

Sustainable development
Scottish Water recognises the importance of fulfilling its social responsibilities. To this aim the Board has a Sustainable Development Policy that includes social, economic and environmental aspects. The Board considers sustainable development as part of its ongoing activities and in the development of its business plans.

The Board is committed to providing an active but appropriate level of support to community projects.

Information and communication
Scottish Water has developed an annual budgeting and financial and performance reporting system that compares results with budget on a monthly basis, providing information for internal and external reporting. Key performance targets have been agreed with Regulators and the Scottish Government.

Performance against these targets is reported monthly to the Board and quarterly to the Regulators and the Scottish Government. Scottish Water has an ongoing programme of developing systems to assist customer service and decision making in financial and operational areas of the business. The overall aim is to produce relevant, reliable and timely operational, financial, and compliance related information, consistent with the objectives of the business, to enable management to exercise effective control and direction.

Scottish Water has, following widespread consultation, recently updated a Consultation Code setting out how it consults external stakeholders in relation to proposals for, and the undertaking of, significant core business activities.

Members of the Board meet quarterly with officials from the Scottish Government to discuss a range of business issues.

Board and Committee performance
A formal review of performance was carried out by the Board and Committees, and actions arising from it are being implemented. Formal annual evaluation processes are in place for all Members including the Chair. Induction and ongoing training is provided for Members with specific emphasis on finance, regulation and risk analysis.

Independence of auditors
The Auditor General for Scotland is responsible to the Scottish Parliament for securing the audit of the financial statements of Scottish Water. For 2011/12 to 2015/16, the Auditor General re-appointed PricewaterhouseCoopers LLP as the auditors of Scottish Water.

Under the terms of PricewaterhouseCoopers LLP's appointment, they may not carry out any non-audit work for Scottish Water without the prior approval of Audit Scotland.

Going concern
Scottish Water operates under an annual external financing limit (EFL) set by the Scottish Government. The annual EFL controls the amount by which Scottish Water can increase its externally sourced finance, including borrowings. In addition, Scottish Water's charging structure is reviewed through a regulatory process and charges are approved annually by the Water Industry Commission for Scotland.

The Members, taking all relevant factors into account, consider that Scottish Water will have adequate resources to continue in operational existence for the foreseeable future. The accounts are therefore prepared on a going concern basis.

Public Services Reform (Scotland) Act 2010
Sections 31 and 32 of the Public Services Reform (Scotland) Act 2010 impose new duties on the Scottish Government and listed public bodies to publish information on expenditure and certain other matters as soon as is reasonably practicable after the end of each financial year.

In accordance with the Public Services Reform (Scotland) Act 2010, Scottish Water will publish the full information as required by the act on the Scottish Water website (www.scottishwater.co.uk) following the approval of the Scottish Water Annual Report and Accounts 2012/13. The report for this financial year will be available from July 2013.

Members' remuneration report

As far as is possible, Scottish Water adopts the same practice as quoted companies in the presentation of this Remuneration Report, even though it is not a quoted company.

1. Remuneration Committee

a. Remit

The Remuneration Committee meets regularly to consider the remuneration arrangements for Executive Members, and other related remuneration matters, and makes recommendations to the Board. No Executive Members are involved in deciding their own remuneration.

b. Membership

The Remuneration Committee is chaired by a Non-executive Member, Donald Emslie, and included two other Non-executive Members; Alan Bryce and Pat Kelly until his contract expired on 31 March 2013.

During the year external independent advice and remuneration analysis were provided by Hay Group Management Consultants. Internal advice was provided by the Chair of Scottish Water, the Chief Executive and the Director of People and Organisational Development. No Executive Member was present during discussions about their own remuneration.

c. Meetings

There were five meetings of the Committee in 2012/13. At each meeting a quorum of independent, Non-executive Members was present.

2. General remuneration policy

Scottish Water's vision is to become Scotland's most valued and trusted business, one that we can all be proud of. Scottish Water will build on its past success by seeking to provide levels of service, performance and efficiency which exceed the expectation of its customers, regulators and the Scottish Government.

Scottish Water will continue to provide a working environment that matches the expectations it places on its people to deliver best value outcomes in an empowered organisation. Scottish Water's staff remuneration and incentivisation policies are a major contributor to achieving Scottish Water's goals. This requires terms of employment for all employees that, taken together, ensure that Scottish Water is perceived as a fair employer that encourages excellence, rewards performance and empowers its people as well as providing scope for personal development.

Scottish Water's overall remuneration policy aims are to:

– Attract, develop, motivate and retain highly talented people at all levels of the organisation.
– Incentivise and reward good individual and corporate out-performance.

3. Policy on Executive Members' remuneration

a. Comparator organisations

Scottish Water is publicly owned and accountable to the Scottish Parliament and Scottish Ministers. Within the context of public sector ownership, Scottish Water seeks to attract, retain and motivate leadership talent in competition with private sector utilities and other organisations across the UK economy, as well as with employers in the public sector.

Scottish Water uses the remuneration database of Hay Group Management Ltd to review the remuneration practices of comparator organisations and industry in general against its own. This is the largest remuneration database in the UK with each job subjected to the same method of job sizing.

Scottish Water aims to pay in line with 95% of the median of an agreed industry benchmark group, reflecting remuneration levels in comparable organisations for similar work.

b. Remuneration elements

Scottish Water's Remuneration Policy for Executive Members consists of five principal elements:
– Base salary;
– Annual out-performance incentive plan (AOIP);
– Long term incentive plan (LTIP);
– Pension; and
– Allowances (for business needs, car, relocation, etc.).

c. Relative importance of performance incentives

Scottish Water is a performance-orientated organisation. It believes that Executive Members' remuneration should be closely related to corporate performance. The aim is to pay a base salary that is competitive, but appropriate for a public corporation, and provides the opportunity for extra discretionary pay to be earned for out-performance of demanding targets.

d. Annual out-performance incentive plan – 2012/13

Scottish Water has an annual out-performance incentive plan (AOIP) that is designed to incentivise and reward the out-performance of targets agreed with regulators. The targets are set out in the Delivery Plan that has been approved by Scottish Ministers, and reflect the targets set by the Water Industry Commission in its Final Determination of charges for 2010-15. The Delivery Plan targets, out-performance targets, and actual performance for each measure in 2012/13 are set out below.

Measure	Delivery Plan target	Out-performance target	Actual performance
Profit before tax excluding depreciation (measured on a regulatory accounting basis)	£375.0m	£390.0m	£401.4m
Customer service OPA performance	338	358	368
Investment delivery:			
– Q&S II/IIIa completion projects outstanding	12	12	9
– Q&S IIIb overall measure of delivery score	192	>192	205

The performance generated the following awards, based on the criteria set at the start of the year adjusted for the financial performance within Scottish Water Horizons Ltd.

Measure	% allocated	% awarded
Profit before tax excluding depreciation	40%	28%
OPA score	40%	40%
Investment delivery	20%	20%

The potential maximum annual incentive attainable for out-performance by the Executive Members is 40% of base salary and is non-pensionable. Overall AOIP awards in 2012/13 were 35% of annualised salary.

e. Long term incentive plan to incentivise out-performance in the five years to March 2015

The Long Term Incentive Plan (LTIP) has been agreed with the Scottish Government and provides clear targets for out-performance of the Water Industry Commission's Final Determination for the 2010-15 period. Payments under the scheme will be made to Executive Members for their service during the 2010 to 2015 period in January 2016. The LTIP will only be payable if there is overall financial out-performance of the Final Determination.

The plan is based on:

- 50% for performance against financial targets, being the extent to which adjusted net debt is lower in March 2015 than was assumed in the Final Determination. Maximum LTIP would be payable for at least £100 million out-performance.
- 50% for out-performance of OPA targets above those set out in the Final Determination, measured as the average performance in 2013/14 and 2014/15. Maximum LTIP will be payable for an OPA score of at least 400, 20 points higher than the Final Determination target of 380.
- The LTIP will be funded by 12% of annual salary being accumulated each year, during the five years to March 2015, ultimately vesting if earned by eligible Executive Members. Any LTIP payment will only be funded from financial out-performance after payment of any incentive awards to staff.

Confirmation of awards under the LTIP will be made following independent review of performance in the 2010-15 period by external auditors and our regulators.

Non-executive Members are not eligible for annual or long term incentive payments.

Members' remuneration report continued

4. Service contracts
Details of Executive Members' permanent contracts are set out below.

Executive Member	Name	Date of Contract
Chief Executive	Douglas Millican	1 February 2013
Asset Management Director	Geoff Aitkenhead	1 April 2002
Commercial Director	Chris Banks	1 April 2002
Chief Operating Officer	Peter Farrer	1 April 2013

All Members are required to give six months' notice of resignation. Scottish Water is required to give Members twelve months' notice of termination.

Non-executive Board Member remuneration and appointments
The Non-executive Members do not have service contracts. Non-executive Members are expected to work four days per month for Scottish Water with the exception of the Chairs of the Audit and Remuneration Committees, Lynne Peacock and Donald Emslie respectively, who work five days per month and the Chair, Ronnie Mercer, who works 2.5 days per week.

Remuneration for the Chair of Scottish Water and Non-executive Members are agreed by Scottish Ministers. Remuneration for Non-executive Members comprise a basic fee for acting as a Non-executive Member of £19,872 (2012: £19,872) but the Chairs of the Remuneration and Audit Committees receive a higher fee of £24,840 (2012: £24,840), reflecting the increased time commitment required in these roles.

No compensation is payable to any Non-executive Member if their appointment is terminated early. The expiry dates of Non-executive appointments are as follows:

Ronnie Mercer	31 March 2015
Alan Bryce	31 March 2018
Lynne Peacock	31 March 2018
James Spowart	31 March 2017
Andrew Wyllie	31 March 2017
Douglas Reid*	31 March 2017
Matt Smith*	31 March 2017
Donald Emslie	31 March 2016

* Matt Smith and Douglas Reid were appointed as Non-executive Members on 1 May 2013.

The auditors are required to report on information contained in the following sections of the Remuneration Report.

5. Members' remuneration

Details of Members' Remuneration, as defined in the Scottish Water Governance Directions 2009 by Scottish Ministers, are set out below for the year.

Remuneration in respect of 2012/13	Salary/ Fees £'000	AOIP £'000	Benefits £'000	Total £'000	Total 2011/12 £'000
Executive Members					
Geoff Aitkenhead	172	61	8	241	252
Chris Banks	159	56	11	226	234
Peter Farrer	155	55	11	221	228
Douglas Millican (i)	200	65	11	276	253
Non-executive Members					
Ronnie Mercer (Chair)	90	–	10	100	100
Alan Bryce	20	–	–	20	20
Donald Emslie	25	–	–	25	25
Lynne Peacock	25	–	–	25	20
James Spowart	20	–	–	20	20
Andrew Wyllie	20	–	–	20	20
Total Members' remuneration	**886**	**237**	**51**	**1,174**	**1,172**
Former Members					
Richard Ackroyd (ii)	153	53	7	213	380
Pat Kelly (iii)	20	–	–	20	20
David Gray (iv)	–	–	–	–	32
Total	**1,059**	**290**	**58**	**1,407**	**1,604**

(i) The salary in the year paid to Mr Millican reflects his position as Finance & Regulation Director until 31 January 2013, his responsibility as Interim Chief Executive from 29 October 2012, and his appointment as Chief Executive from 1 February 2013.
(ii) Payments made in respect of Mr Ackroyd's service up to his death on 28 October 2012.
(iii) Appointment to the Board of Scottish Water expired on 31 March 2013.
(iv) Appointment to the Board of Scottish Water expired on 31 March 2012.
(v) A car or car allowance is provided to all Executive Members and the Chair for business needs. The associated annual benefit is included in the benefits section of the table above. For Members opting out of the company car scheme, a car allowance is payable. The benefits section also includes the value of any holiday sale backs / purchases and annual life assurance premiums associated with the Scottish Water Life Assurance Scheme.
(vi) The AOIP criteria are explained on page 35.

For 2013/14 (with effect from 1 April 2013), the Committee approved an increase in salary for Peter Farrer to £172,000, reflecting his new role as Chief Operating Officer. The Committee also approved the salary for Douglas Millican in his new role as Chief Executive, effective from 1 February 2013, at £236,700, 10% less than the salary paid to the previous Chief Executive, Mr Ackroyd.

Members' remuneration report continued

6. Pension
The Executive Members Geoff Aitkenhead, Chris Banks, Peter Farrer and Douglas Millican are eligible to participate in the Lothian Pension Fund, a defined benefit scheme. Details of their benefits under this scheme are set out below.

	Increase in accrued benefits during the year net of inflation			Accumulated total accrued benefits at 31 March 2013		Transfer Values (note 4)		
	Years in Scheme	Pension £'000	Lump sum £'000	Pension £'000	Lump sum £'000	At 31 March 2013 £'000	At 31 March 2012 £'000	Increase in 2012/13 net of Members' own contributions and inflation £'000
Geoff Aitkenhead	33.4	–	–	74	196	1,630	1,582	46
Chris Banks	18.7	3	–	40	88	751	699	34
Peter Farrer	28.7	3	–	58	143	1,044	942	82
Douglas Millican	18.1	5	5	44	97	727	600	104

Notes:
1. Members of the pension scheme have the option to pay additional voluntary contributions; neither the contributions nor the resulting benefits are included in the above table.
2. The normal retirement age of Executive Members is 65.
3. The pension entitlement shown is that which would be paid annually on retirement along with the lump sum, based on service to the end of the year.
4. The transfer value of accrued pension is calculated in a manner consistent with Actuarial Guidance Note GN11.

Richard Ackroyd did not participate in the Lothian Pension Fund but Scottish Water contributed £53,696 (2012: £92,050) to his pension arrangements up to the date of his death on 28 October 2012. Geoff Aitkenhead no longer receives contributions to the Lothian Pension Fund, but an equivalent value (£41,282) was accrued and will become payable on his retirement from Scottish Water.

7. Executive Members' Directorships of other companies
The Remuneration Committee supports active development of Executive Members including their involvement with other companies and public bodies where this is compatible with fulfilling their responsibilities for Scottish Water. Any fees received are retained by the Member.

During the year ended 31 March 2013, Chris Banks held a Non-executive Director position with Sgoiltean Ura LLP, receiving £6,000 in fees (2012: £6,000). With effect from 1 April 2012, Geoff Aitkenhead has been a Non-executive Director of Scottish Canals and received fees of £4,800 (2012: nil).

This report was approved by the Board and signed on its behalf by:

Mr Donald Emslie,
Chair of the Remuneration Committee
28 May 2013

Statement of Members' responsibilities

for the preparation of the financial statements

The following statement, which should be read in conjunction with the statement of auditors' responsibilities included in the Auditors' Report on pages 40 to 41, is made with a view to distinguishing the respective responsibilities of the Members and of the auditors in relation to the financial statements.

The Members are required by the Water Industry (Scotland) Act 2002 and directions made thereunder to prepare financial statements for each financial year which give a true and fair view of the state of affairs of Scottish Water and of its income and expenditure for that period. In preparing those financial statements, the Members are required to:

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

The Members are responsible for keeping proper accounting records, which disclose with reasonable accuracy, at any time, the financial position of Scottish Water and to enable them to ensure that the financial statements comply with statute and any financial reporting requirements. They are also responsible for taking reasonable steps to safeguard the assets of the business and to prevent and detect fraud and other irregularities.

Independent auditors' report

to the Members of the Board of Scottish Water, the Auditor General for Scotland and the Scottish Parliament

We have audited the financial statements of Scottish Water and its group for the year ended 31 March 2013 under the Water Industry (Scotland) Act 2002. The financial statements comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated and Company Statements of Changes in Equity, the Group and Company Balance Sheets, the Group and Company Statements of Cash Flow and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the 2012/13 Government Financial Reporting Manual (the 2012/13 FReM).

This report is made solely to the parties to whom it is addressed in accordance with the Public Finance and Accountability (Scotland) Act 2000 and for no other purpose. In accordance with paragraph 125 of the Code of Audit Practice approved by the Auditor General for Scotland, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Respective responsibilities of the Board Members and auditor

As explained more fully in the Statement of Members' Responsibilities, the Board Members are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and are also responsible for ensuring the regularity of expenditure and income. 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) as required by the Code of Audit Practice approved by the Auditor General for Scotland. Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors. We are also responsible for giving an opinion on the regularity of expenditure and income in accordance with the Public Finance and Accountability (Scotland) Act 2000.

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 group's and company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Board Members; and the overall presentation of the financial statements. It also involves obtaining evidence about the regularity of expenditure and income. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements, irregularities, or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view in accordance with the Water Industry (Scotland) Act 2002 and directions made thereunder by the Scottish Ministers of the state of affairs of the group and of the company as at 31 March 2013 and of the surplus of the group and the company for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2012/13 FReM; and
- have been prepared in accordance with the requirements of the Water Industry (Scotland) Act 2002 and directions made thereunder by the Scottish Ministers.

Opinion on regularity

In our opinion in all material respects the expenditure and income in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers.

Opinion on other prescribed matters
In our opinion:
- the part of the Members' Remuneration Report to be audited has been properly prepared in accordance with the Water Industry (Scotland) Act 2002 and directions made thereunder by the Scottish Ministers; and
- the information given in the Financial and Business Review included in the Annual Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception
We are required to report to you if, in our opinion:
- adequate accounting records have not been kept; or
- the financial statements and the part of the Members' Remuneration Report to be audited are not in agreement with the accounting records; or
- We have not received all the information and explanations we require for our audit; or
- the Corporate Governance statement does not comply with the UK Corporate Governance Code.

We have nothing to report in respect of these matters.

PricewaterhouseCoopers LLP
Appointed Auditors
Glasgow
11 June 2013

Financial statements

Consolidated income statement

For the year ended 31 March 2013

	Note	2013 £m	2012 £m
Revenue	3	**1,145.7**	**1,132.2**
Cost of sales		(721.9)	(712.4)
Gross surplus		**423.8**	**419.8**
Administrative expenses		(144.1)	(125.5)
Operating surplus	3, 4	**279.7**	**294.3**
Finance income	7	53.3	64.9
Finance costs	7	(237.9)	(252.2)
Surplus before taxation		**95.1**	**107.0**
Taxation	8	(5.9)	(8.5)
Surplus for the year	20	**89.2**	**98.5**

Consolidated statement of comprehensive income

For the year ended 31 March 2013

	Note	2013 £m	2012 £m
Surplus for the year	20	89.2	98.5
Other comprehensive income:			
Actuarial gain/(loss) on post employment benefit obligations, net of deferred taxation	22	12.6	(10.0)
Total comprehensive income for the year		101.8	88.5

The surplus for the period and total comprehensive income for the period are attributable to the owners of Scottish Water.

Consolidated statement of changes in equity

	Note	Retained earnings £m	Other reserves £m	Total reserves £m
Balance at 1 April 2011		712.7	133.4	846.1
Surplus for the year		98.5		98.5
Other comprehensive income:				
Actuarial loss on post employment benefit obligations, net of tax	22	(10.0)		(10.0)
Total comprehensive income for the year		88.5		88.5
Balance at 31 March 2012		**801.2**	**133.4**	**934.6**
Surplus for the year		89.2		89.2
Other comprehensive income:				
Actuarial gain on post employment benefit obligations, net of tax	22	12.6		12.6
Total comprehensive income for the year		101.8		101.8
Balance at 31 March 2013	20	**903.0**	**133.4**	**1,036.4**

Company statement of changes in equity

	Note	Retained earnings £m	Other reserves £m	Total reserves £m
Balance at 1 April 2011		668.6	133.4	802.0
Surplus for the year	20	74.2		74.2
Other comprehensive income:				
Actuarial loss on post employment benefit obligations, net of tax	22	(12.0)		(12.0)
Total comprehensive income for the year		62.2		62.2
Balance at 31 March 2012		**730.8**	**133.4**	**864.2**
Surplus for the year	20	63.4		63.4
Other comprehensive income:				
Actuarial gain on post employment benefit obligations, net of tax	22	12.2		12.2
Total comprehensive income for the year		75.6		75.6
Balance at 31 March 2013	20	**806.4**	**133.4**	**939.8**

The 'Statement of changes in equity' above excludes Government loans which, in accordance with the Corporate Governance Direction, are recorded on the balance sheet under Equity. Full details of Government loans are provided in note 18.

Financial statements
continued

Balance sheets

As at 31 March 2013

		Group		Company	
	Note	2013 £m	2012 £m	2013 £m	2012 £m
Assets					
Non-current assets					
Property, plant and equipment	9	5,325.5	5,196.1	5,306.5	5,177.0
Investments	10	–	–	37.6	37.6
Deferred tax asset	15	0.2	–	–	–
		5,325.7	5,196.1	5,344.1	5,214.6
Current assets					
Inventories	11	2.4	1.9	2.2	1.7
Trade and other receivables	12	170.6	185.5	70.2	58.9
Current tax asset		1.0	1.0	0.9	0.9
Cash and cash equivalents	13	415.6	355.2	245.5	241.0
		589.6	543.6	318.8	302.5
Total assets		**5,915.3**	**5,739.7**	**5,662.9**	**5,517.1**
Liabilities					
Current liabilities					
Trade and other payables	14	(414.6)	(404.0)	(308.3)	(321.3)
Other loans and borrowings	17	(17.2)	(17.2)	(17.2)	(17.2)
Current tax liabilities		(1.9)	(4.4)	–	–
Provisions for liabilities	16	(3.2)	(5.4)	(17.6)	(5.1)
		(436.9)	(431.0)	(343.1)	(343.6)
Non-current liabilities					
Trade and other payables	14	(83.3)	(70.6)	(77.3)	(64.4)
Other loans and borrowings	17	(400.7)	(417.9)	(400.7)	(417.9)
Deferred tax liabilities	15	(386.2)	(379.7)	(386.3)	(379.0)
Retirement benefit obligations	22	(246.2)	(281.1)	(247.6)	(281.7)
Provisions for liabilities	16	(0.2)	(1.1)	(1.2)	(1.1)
		(1,116.6)	(1,150.4)	(1,113.1)	(1,144.1)
Total liabilities		**(1,553.5)**	**(1,581.4)**	**(1,456.2)**	**(1,487.7)**
Net assets		**4,361.8**	**4,158.3**	**4,206.7**	**4,029.4**
Equity					
Government loans	18	3,325.4	3,223.7	3,266.9	3,165.2
Retained earnings	20	903.0	801.2	806.4	730.8
Other reserves		133.4	133.4	133.4	133.4
		4,361.8	**4,158.3**	**4,206.7**	**4,029.4**

The financial statements on pages 42 to 75 were approved by the Board of Members on 29 May 2013 and signed on its behalf by:

Douglas Millican
Chief Executive

Statements of cash flow

For the year ended 31 March 2013

	Note	Group 2013 £m	Group 2012 £m	Company 2013 £m	Company 2012 £m
Surplus before taxation		95.1	107.0	63.6	74.1
Depreciation charges		260.1	252.6	253.6	251.1
Amortisation of grants		(1.0)	(0.9)	(0.9)	(0.9)
Surplus on disposal of property, plant and equipment		(2.1)	(0.5)	(2.1)	(0.7)
Non cash adjustment for retirement benefit obligations		(0.5)	(12.0)	(0.4)	(12.0)
Finance costs – net		184.6	187.3	184.4	186.5
Operating cashflow before changes in working capital and provisions		**536.2**	**533.5**	**498.2**	**498.1**
Changes in working capital and provisions:					
Increase in receivables		(1.6)	(17.6)	(27.8)	(6.7)
(Increase)/decrease in inventories		(0.5)	0.4	(0.5)	0.4
Increase in payables		43.6	26.9	21.0	9.0
(Decrease)/increase in provisions		(9.0)	(3.6)	6.8	(3.2)
Cash flows from operating activities		**568.7**	**539.6**	**497.7**	**497.6**
Taxation paid		(9.3)	(7.8)	–	(0.2)
Net cash generated from operating activities		559.4	531.8	497.7	497.4
Cash flows from investing activities					
Purchase of property, plant and equipment		(413.7)	(377.1)	(407.9)	(370.7)
Sale of property, plant and equipment		3.3	2.4	3.2	2.5
Government grants and other contributions		–	0.1	–	–
Infrastructure income receipts		7.1	7.8	7.1	7.8
Net cash used in investing activities		(403.3)	(366.8)	(397.6)	(360.4)
Cash flows from financing activities					
Repayments of loans		(80.0)	(96.0)	(80.0)	(96.0)
Proceeds from borrowings		180.0	146.0	180.0	146.0
Interest received		0.9	2.6	0.4	1.9
Interest paid		(181.1)	(187.3)	(180.5)	(185.7)
Payment of finance lease liabilities		(15.5)	(14.5)	(15.5)	(14.5)
Net cash used in financing activities		(95.7)	(149.2)	(95.6)	(148.3)
Net increase/(decrease) in cash and cash equivalents		**60.4**	**15.8**	**4.5**	**(11.3)**
Cash and cash equivalents at beginning of year	13	355.2	339.4	241.0	252.3
Cash and cash equivalents at end of year	13	**415.6**	**355.2**	**245.5**	**241.0**

Notes to the financial statements

For the year ended 31 March 2013

1 Accounting policies

General information
Scottish Water is a public sector body, classified as a public corporation of a trading nature, and is answerable to the Scottish Parliament through Scottish Ministers.

The principal accounting policies applied in the preparation of the consolidated financial statements are set out below.

Basis of preparation
The financial statements of Scottish Water for the year ended 31 March 2013 have been prepared in accordance with EU adopted and endorsed International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRIC) interpretations, as interpreted by the International Government Financial Reporting Manual (FReM). The FReM is published by HM Treasury and is available from their website.

The consolidated financial statements have been prepared on the going concern basis under the historical cost convention, in a form directed by Scottish Ministers in accordance with section 45(2) of the Water Industry (Scotland) Act 2002. The Company's financial statements have been prepared on the same basis and, as permitted by Section 408 of the Companies Act 2006, no income statement or statement of comprehensive income is presented for the Company.

Scottish Water's accounting policies, as set out below, have been consistently applied to all the years presented, unless otherwise stated.

Scottish Water's financial statements have been prepared in accordance with IFRS since 1 April 2008. The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies (note 2).

There were no new standards, amendments or IFRIC interpretations effective for the first time for the current financial period.

As at the date of authorisation of these financial statements, the following IFRSs were in issue but not yet effective. Consequently, Scottish Water has not applied these new IFRSs and IFRICs in the preparation of the financial statements. The impact on Scottish Water's financial statements of the future adoption of the standards is currently under review.

- IFRS 9 'Financial Instruments' will establish principles for the financial reporting of financial assets that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of the entity's future cash flows. This will be applicable for annual periods commencing on or after 1 January 2015 but is still awaiting endorsement by the EU.
- Amendments to IAS 1 'Presentation of items of Other Comprehensive Income', effective for annual periods commencing on or after 1 July 2012.

The following standards are applicable to annual periods commencing on or after 1 January 2013 and have been endorsed by the EU.

- IFRS 10 'Consolidated Financial Statements' introduces a new approach to determining which investees should be consolidated and provides a single model to be applied in the control analysis for all investees.
- IFRS 11 'Joint Arrangements' focuses on the rights and obligations of joint arrangements, rather than the legal form. It distinguishes joint arrangements between joint operations and joint ventures.
- IFRS 12 'Disclosure on Interests in Other Entities' contains the disclosure requirements for entities that have interests in other entities including subsidiaries, joint arrangements (i.e. joint operations or joint ventures), associates and/or unconsolidated structured entities.
- IFRS 13 'Fair Value Measurement' replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance. It defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for all fair value measurements.
- IAS 27 'Separate Financial Statements' and IAS 28 'Associates and Joint Ventures' have been revised following the issue of IFRS 10 and IFRS 11.
- IAS 19 'Employment Benefits' has been amended, currently referred to as "IAS19R". The main changes require a revised allocation of costs for defined benefit pension schemes between the income statement and other comprehensive income and prohibit the use of the "corridor approach" to spread recognition of actuarial gains losses – which is not used by Scottish Water; a different measurement basis for asset returns; a revised definition of short- and long-term benefits to employees; and revised criteria for the recognition of termination benefits.

The consolidated financial statements are presented in Pounds Sterling which is the functional and presentational currency of Scottish Water and its subsidiaries.

1 Accounting policies continued

Basis of consolidation

a. Subsidiaries

The consolidated financial information incorporates the results of Scottish Water (the Company) and its trading subsidiaries. The consolidated financial information does not include the non trading subsidiaries as permitted under section 405 of the Companies Act 2006. Subsidiaries are all entities over which Scottish Water has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one half of the voting rights. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account. Scottish Water Business Stream Limited (Business Stream) is treated as a subsidiary although special governance arrangements, established in conjunction with the Water Industry Commission for Scotland and associated with the conditions attached to Business Stream's licence for the supply of water and waste water services, limit Scottish Water's control over its operating policies. Subsidiaries are fully consolidated from the date on which control is transferred to Scottish Water; they are de-consolidated from the date when control ceases.

Intercompany transactions, balances and any unrealised gains on transactions between Scottish Water related companies have been eliminated within the consolidated financial statements. Uniform accounting policies have been adopted across the Group.

b. Jointly controlled operations

The nature of the contractual agreements between Scottish Water and the other shareholders in both Scottish Water Solutions Limited (SWS) and Scottish Water Solutions 2 Limited (SWS2) are such that the parties are engaged in joint activities that do not constitute an entity carrying on a trade or business in its own right. Consequently, SWS and SWS2 have been accounted for under IAS 31 'Interests in joint ventures', as jointly controlled operations. On this basis Scottish Water accounts directly for its own gross assets, liabilities and cash flows in the joint operations.

Operating segments

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

Revenue recognition

Revenue is recognised to the extent that it is probable economic benefits will flow to the Group and that the revenue can be reliably measured. Revenue is not recognised until the service has been provided to the customer. Revenue is shown net of value added tax and after eliminating sales between the Scottish Water related companies. Where services have been provided, but for which no invoice has been raised at the year end, an estimate of the value is included in revenue.

Revenue comprises charges to customers for water and waste water services, and related services provided during the year in the normal course of business. For measured customers, revenue includes an estimate of the value of water and waste water services supplied to customers between the date of the last meter reading and the year end. For unmeasured customers billed in advance, income is deferred and released to the income statement throughout the year.

Research and development expenditure

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects which either do not meet the criteria defined in IAS 38 'Intangible assets' or are deemed to be not material, are recognised as an expense as incurred. Development costs which meet the relevant criteria are capitalised and written off over their expected useful lives. Development costs previously recognised as an expense are not recognised as an asset in subsequent periods.

Finance income and costs

Finance income comprises interest receivable on funds invested and expected returns on pension scheme assets recognised in the income statement. Finance costs comprise interest payable on borrowings and interest on pension scheme liabilities. Interest income and costs are recognised in the income statement as they accrue, on an effective interest rate method.

Borrowing costs incurred by Scottish Water that are not directly attributable to the acquisition, construction or production of qualifying assets are expensed in the period in which they are accrued.

Notes to the financial statements continued

For the year ended 31 March 2013

1 Accounting policies continued

Taxation
The tax expense for the year comprises current and deferred tax. Tax is recognised in the income statement, unless it relates to items recognised directly in reserves in which case it is recognised in reserves.

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

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

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

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

Property, plant and equipment
Property, plant and equipment comprises water and waste water infrastructure assets and other assets, being overground assets including operational properties, plant, machinery and vehicles.

Property, plant and equipment are included at historical cost less accumulated depreciation and impairment. Cost includes the acquisition or construction cost together with any expenditure directly attributable to bringing the asset into use, including directly attributable internal costs and, where material, borrowing costs. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that the future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred. All items of property, plant and equipment, with the exception of land and assets under construction, are subject to depreciation.

Infrastructure assets
The infrastructure assets comprise a network of water and waste water systems including mains, sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls. Expenditure on infrastructure assets, which relates to increases in capacity or enhancements of the network, is treated as additions. Expenditure incurred in maintaining and repairing the operating capability of the network is expensed in the year in which it is incurred. Depreciation is calculated for each component of the network with similar characteristics and asset lives.

Other assets
All other property, plant and equipment are depreciated on a straight-line basis over their estimated useful economic lives.

Depreciation
Depreciation is charged to the income statement to write-off cost, less residual values, on a straight-line basis over the estimated operational lives of the assets, from the date of beneficial use. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. Freehold land and assets under construction are not depreciated. The estimated useful lives for assets depreciated are as follows:

Infrastructure assets	80 to 150 years
Non-specialised operational buildings and structures	60 years
Specialised operational buildings and structures	20 to 80 years
Plant, machinery and vehicles	1 to 20 years

1 Accounting policies continued

Leased assets
Leases where Scottish Water control through ownership, beneficial entitlement or otherwise, any significant residual interest in the assets at the end of the service concession agreements are treated as finance leases. Private Finance Initiative (PFI) contracts are treated as finance leases, in accordance with IFRIC 12.

Assets held under finance leases are recognised as part of the property, plant and equipment of the Group at their fair value or, if lower, at the present value of the minimum lease payments, as determined at the inception of the PFI contract. The corresponding liability is included in the Balance Sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation. Finance charges are charged directly to the income statement. The property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset and the lease term.

All other leases are categorised as operating leases. Payments made under operating leases are charged to the income statement over the term of the lease on a straight-line basis.

Impairment of assets
The carrying values of the Group's non-current assets are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be justified. An impairment loss is recognised for the amount by which the asset's carrying value exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

Capital grants and customer contributions
Capital grants and customer contributions in respect of infrastructure assets are deducted from the cost of the non-current asset. Grants and contributions received in respect of non-infrastructure assets are credited to deferred income and are released to the income statement over the expected useful lives of the relevant non-current assets.

Investments
Investments in subsidiaries, held as non-current assets, are stated at cost less any provision for impairment. Any impairment is charged to the income statement as it arises.

Inventories
Inventories and work in progress are stated at the lower of cost or net realisable value. Cost is determined using the first-in, first-out (FIFO) method. Cost includes all costs incurred in bringing each asset to its present location and condition. The valuation of work in progress is based on the cost of labour and materials plus appropriate overheads.

Financial instruments
Financial assets and liabilities are recognised in Scottish Water's balance sheet when an obligation is identified and released as that obligation is fulfilled. Scottish Water's financial instruments comprise trade and other receivables, cash and cash equivalents, borrowings, as well as trade and other payables that arise directly from operations. Scottish Water's policy is not to trade or speculate in financial instruments. All treasury activities are undertaken in accordance with the permitted activities as set out in the Scottish Water Governance Directions 2009. No trading in derivative financial instruments was undertaken.

a. Trade receivables
Trade receivables are recorded at net realisable value after deducting a provision where there is evidence that Scottish Water will not be able to collect all amounts due. The provision is calculated by applying expected recovery rates, based on actual historical cash collection performance, to the aged debt profile of the outstanding debt. Trade receivable balances are written off when Scottish Water determines that it is unlikely that future remittances will be received. Trade receivables do not carry any interest.

b. Cash and cash equivalents
Cash and cash equivalents include cash in hand and deposits with banks, which have a maturity of three months or less from the date of acquisition and which are subject to an insignificant risk of change in value.

c. Trade and other payables
Trade and other payables are stated at cost.

d. Interest-bearing loans and borrowings
Borrowings are recognised initially at fair value and are subsequently stated at amortised cost. Overdrafts and non Government loans are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

Notes to the financial statements continued

For the year ended 31 March 2013

1 Accounting policies continued

Employee benefit obligations
Employees of Scottish Water participate in the Local Government Pension Scheme administered by Aberdeen, Glasgow and Edinburgh City Councils, all of which are defined benefit schemes. Pension scheme assets are measured using the bid market values. Pension scheme liabilities are measured using the projected unit actuarial method and are discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability.

Any increase in the present value of liabilities within the defined benefit pension schemes expected to arise from employee service in the period is charged to operating surplus. The expected return on the schemes' assets and the increase during the period in the present value of the schemes' liabilities arising from the passage of time are included in finance income and finance costs. Actuarial gains and losses are recognised in full as an item of 'other comprehensive income' in the consolidated statement of comprehensive income. Pension scheme deficits and surpluses, to the extent that the surplus is considered recoverable, are recognised in full and presented on the face of the balance sheet.

Provisions
Provisions are recognised when there is a present obligation for a past event, for which it is probable that a transfer of economic benefits will be required and a reliable estimate can be made of the amount of the obligation. Provisions currently relate to onerous property rental costs, income uncertainty and redundancy costs associated with employees who will leave Scottish Water under voluntary redundancy and early retirement. Pension related liabilities associated with employees who have left Scottish Water under the voluntary severance scheme are recognised in the pension liability.

Foreign currency transactions
Transaction in foreign currencies are translated at the exchange rate ruling at the date of the transactions. Foreign exchange gains and losses resulting from (i) the settlement of such transactions and (ii) the retranslation to exchange rates ruling at the balance sheet date of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

Indebtedness to the Scottish Ministers
Loans from the National Loans Fund, the Scottish Consolidated Fund and other Government borrowings are treated as part of equity, including loan repayments due within one year, in accordance with the Scottish Water Governance Directions 2009.

2 Accounting estimates and judgements

The preparation of financial statements to conform to IFRS requires the use of estimates, assumptions and judgements that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts for revenue and expenses during the reporting period. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Although based on management's best knowledge of the amount, event or actions, actual results may ultimately differ from these estimates, the effect of which is recognised in the period in which the facts giving rise to the revision arise.

The most critical of these accounting judgement and estimation areas are noted below.

a. Revenue recognition
Revenue relating to metered customers includes an estimate of the value of water or waste water services supplied between the date of the last meter reading and the year end. At the balance sheet date, the estimated consumption by customers will either have been billed (estimated billed revenue) or accrued (unbilled revenue). Using historical consumption patterns, management apply judgement to the measurement of the quantum of the estimated consumption and to the valuation of that consumption. The judgements applied, and the assumptions underpinning these judgements, are considered to be appropriate. However, a change in these assumptions would have no material impact upon the amount of revenue recognised.

b. Impairment of trade and other receivables
Scottish Water and each of its subsidiaries evaluate the recoverability of their trade receivables as at the reporting date and assess the allowances for doubtful receivables based on experience. These allowances are based on, amongst other factors, actual collection history and customer category. The actual level of receivables collected may differ from those estimated, due to factors such as changes in customer behaviour or the economic outlook, which could impact positively or negatively on operating results.

2 Accounting estimates and judgements continued

c. Carrying value of property, plant and equipment

Property, plant and equipment (PPE) represents the majority of the Group's asset base and a significant proportion of the Group's annual expenditure (see funding graph on page 24. Therefore the estimates and assumptions made in determining the carrying values and related depreciation are critical to the Group's financial performance and position.

The estimated useful economic lives and residual values of PPE are based on management's judgement and experience. Due to the significance of PPE investment, variations between actual and estimated economic lives could impact on operating results both positively and negatively. When management identifies that actual useful economic lives differ materially from the estimates used, the relevant depreciation charge is adjusted prospectively. However, historically, any changes to estimated useful lives and residual values have not resulted in material changes to the Group's depreciation charges.

Each financial year, in accordance with IAS 23 'Borrowing costs', Scottish Water calculates the amount of borrowing which would be attributable to the PPE acquired or under construction. To date these amounts have been immaterial and therefore not capitalised.

d. Provisions

The assessments undertaken in recognising provisions and contingencies have been made in accordance with IAS 37 'Provisions, Contingent Liabilities and Contingent Assets'. The evaluation of the likelihood of the contingent events has required the best judgement by management regarding the probability of exposure to potential loss. Should circumstances change following unforeseen developments, this likelihood could alter.

e. Retirement benefits

Scottish Water and its subsidiaries are participating employers in three Local Government Pension Schemes (LGPS) which are defined benefit schemes. Actuarial valuations of the schemes are carried out by the administering authorities triennially in line with LGPS regulations. The assumptions in relation to the cost of providing post-retirement benefits during the period are set after consultation with qualified actuaries. These assumptions include discount rates, returns on the schemes' assets, pay growth and increases to pension payments (see note 22) and, while these assumptions are believed to be appropriate, a change to the assumptions would impact the surplus of the Group and the carrying amount of pension obligations. These assumptions may differ from the actual results due to changes in market and economic conditions and longer or shorter lives of participants.

3 Segmental analysis

The principal activities of the Scottish Water Group are the supply of water and waste water services to household and business customers across Scotland. In view of the integrated nature of Scottish Water's operational activities, the financial statements include all of the costs of water and waste water collection, treatment and distribution within cost of sales.

Scottish Water's reportable segments are the provision of regulated water and waste water services, Business Stream (a Licensed Provider in the supply of water and waste water services to non-household customers) and other trading activities. The other trading activities include the results of Horizons, Scottish Water International and Scottish Water's non-regulated activities. These operating segments reflect the internal management reporting that are reviewed regularly by the Board in order to allocate resources to and assess the performance of the segments.

An analysis of revenue, operating surplus and total assets by segment is provided below:

	2013 £m	2012 £m
Revenue		
Regulated water and waste water services	1,053.0	1,045.8
Business Stream	361.5	357.0
Other trading activities	20.2	20.2
	1,434.7	1,423.0
Less Intercompany elimination	(289.0)	(290.8)
	1,145.7	**1,132.2**

During the year Business Stream generated £9.9 million (2012: £10.2 million) of non-licensed trading revenue bringing the total revenue from other trading activities for the Group to £30.1 million (2012: £30.4 million).

Notes to the financial statements continued

For the year ended 31 March 2013

3 Segmental analysis continued

	2013 £m	2012 £m
Operating surplus		
Regulated water and waste water services	247.5	260.3
Business Stream	36.6	34.7
Other trading activities	(5.6)	1.7
	278.5	296.7
Add/(less) Intercompany elimination	1.2	(2.4)
	279.7	**294.3**

Business Stream's operating surplus from non-licensed trading activities during the year was £1.5 million (2012: £3.5 million) bringing the total operating loss from other trading activities for the Group to £4.1 million (2012: £5.2 million surplus).

	2013 £m	2012 £m
Total assets		
Regulated water and waste water services	5,624.8	5,477.7
Business Stream	259.4	238.9
Other trading activities	31.1	23.1
	5,915.3	**5,739.7**

	Capital additions to property, plant & equipment		Depreciation on property, plant and equipment	
	2013 £m	2012 £m	2013 £m	2012 £m
Regulated water and waste water services	384.2	347.7	253.6	251.1
Business Stream	1.8	2.1	1.6	1.3
Other trading activities	4.7	4.1	4.9	0.2
	390.7	**353.9**	**260.1**	**252.6**

Revenue and operating surplus by geographical location of customers is as follows:

	Revenue		Operating surplus	
	2013 £m	2012 £m	2013 £m	2012 £m
United Kingdom	1,144.3	1,132.1	279.7	294.6
Rest of the World	1.4	0.1	–	(0.3)
	1,145.7	**1,132.2**	**279.7**	**294.3**

4 Operating surplus

Operating surplus is arrived at after charging/(crediting):

	Note	2013 £m	2012 £m
PFI operating costs		109.1	105.8
Depreciation of property, plant and equipment	9	260.1	252.6
Surplus on sale of property, plant and equipment		(2.1)	(0.5)
Release of deferred income in relation to capital grants		(1.0)	(0.9)
Operating lease rentals		2.8	2.5
Auditors' remuneration – audit fee for audit of the company and consolidated financial statements (including £26,000 (2012: £19,000) in respect of the audit of subsidiary companies)		0.2	0.2
– other sevices		–	–
Research and development expenditure		1.1	0.9

5 Staff costs

	Note	2013 £m	2012 £m
Wages and salaries		114.2	111.9
Social security costs		9.7	9.3
IAS 19 current service costs relating to current period	22	19.9	17.7
Other pension costs (Remuneration Report, section 6)		0.1	0.1
Employee benefit expense		**143.9**	**139.0**
Less: charged as capital expenditure		(40.2)	(33.9)
Less: seconded staff charged to Scottish Water Solutions Limited and Scottish Water Solutions 2 Limited		(0.8)	(1.0)
		102.9	**104.1**

The average number of people (including Executive and Non-executive Members) employed by Scottish Water, split by activity, during the year was:

	2013	2012
Regulated water and waste water services	3,184	3,140
Business Stream	268	218
Other trading activities	71	64
Scottish Water Solutions Limited and Scottish Water Solutions 2 Limited secondees	17	20
	3,540	**3,442**

Notes to the financial statements continued

For the year ended 31 March 2013

6 Members' remuneration

Information concerning Members' remuneration, incentive schemes and pensions is detailed in the Remuneration Report on pages 34 to 38. No Member or Director had, during the year or at the end of the year, any material interest in any contract of significance in relation to Scottish Water's business.

7 Finance income and costs

	Note	2013 £m	2012 £m
Interest income:			
Short-term deposits		0.9	2.6
Expected return on pension scheme assets	22	52.4	62.3
Finance income		**53.3**	**64.9**
Interest expense:			
Government loans		(155.2)	(159.7)
Other loans		(0.4)	(0.5)
Finance lease liabilities		(25.5)	(26.3)
Interest on pension scheme liabilities	22	(56.8)	(65.7)
Finance costs		**(237.9)**	**(252.2)**
Net finance costs		**(184.6)**	**(187.3)**

8 Taxation

	Note	2013 £m	2012 £m
Analysis of tax charge recognised in the income statement			
Current tax: UK corporation tax		6.8	9.2
Deferred tax: Origination and reversal of timing differences	15	(0.9)	(0.7)
Total taxation charge		**5.9**	**8.5**
The charge for the year can be reconciled to the surplus per the income statement as follows:			
Group surplus before tax		95.1	107.0
Tax on surplus on ordinary activities at standard UK corporation tax rate of 24% (2012: 26%)		22.8	27.8
Adjustment in respect of prior years		(2.2)	14.5
Remeasurement of deferred tax due to change in UK corporation tax rate		(19.2)	(38.6)
Accounting gain with no capital gain		(0.5)	–
Depreciation on non qualifying additions		5.0	4.8
Total tax charge for the year		**5.9**	**8.5**

		Group		Company	
	Note	2013 £m	2012 £m	2013 £m	2012 £m
Tax charge recognised directly in reserves					
Deferred tax relating to:					
Pension scheme actuarial movements	15	7.2	6.0	7.1	5.3

During the year, as a result of the change in the UK corporation tax rate from 24% to 23% that will be effective from 1 April 2013, deferred tax balances have been remeasured.

Changes to the UK corporation tax system were announced in the March 2013 budget statement. The Finance Act 2013 is expected to reduce the main rate of corporation tax to 21% from 1 April 2014. A further reduction of 1% is expected to be enacted separately to reduce the rate to 20% by 1 April 2015. These changes had not been substantively enacted at the balance sheet date and so are not included in these financial statements.

The effect of the expected reduction to 21% with effect from April 2014, if applied to the deferred tax balance at 31 March 2013, would be to reduce the deferred tax liability by £34.2 million. This would increase the surplus for the year by £39.1 million and decrease other comprehensive income by £4.9 million.

The effect of the further expected reduction to 20% with effect from April 2015, if applied to the deferred tax balance at 31 March 2013, would be to reduce the deferred tax liability by £17.1 million. This would increase the surplus for the year by £19.6 million and decrease other comprehensive income by £2.5 million.

Notes to the financial statements continued

For the year ended 31 March 2013

9 Property, plant and equipment

	Specialised operational properties and structures £m	Non-specialised operational properties £m	Infrastructure assets £m	Plant, machinery and vehicles £m	Assets under construction £m	Total £m
Group						
Cost						
At 1 April 2011	2,556.7	68.6	1,768.9	2,104.4	910.0	7,408.6
Additions	0.8	–	–	2.1	351.0	353.9
Disposals	(1.3)	(1.0)	–	(5.4)	–	(7.7)
Reclassifications	211.1	1.9	66.4	248.4	(527.8)	–
At 31 March 2012	2,767.3	69.5	1,835.3	2,349.5	733.2	7,754.8
Additions	1.6	–	–	1.8	387.3	390.7
Disposals	(1.5)	(0.7)	–	(2.9)	–	(5.1)
Reclassifications	69.9	0.4	88.7	139.5	(298.5)	–
At 31 March 2013	2,837.3	69.2	1,924.0	2,487.9	822.0	8,140.4
Accumulated depreciation						
At 1 April 2011	794.9	25.7	415.5	1,075.8	–	2,311.9
Charge for the year	67.9	1.2	13.4	170.1	–	252.6
Disposals	–	(0.7)	–	(5.1)	–	(5.8)
At 31 March 2012	862.8	26.2	428.9	1,240.8	–	2,558.7
Charge for the year	70.7	4.2	13.8	171.4	–	260.1
Disposals	(0.6)	(0.6)	–	(2.7)	–	(3.9)
At 31 March 2013	932.9	29.8	442.7	1,409.5	–	2,814.9
Net book value						
At 31 March 2013	**1,904.4**	**39.4**	**1,481.3**	**1,078.4**	**822.0**	**5,325.5**
At 31 March 2012	1,904.5	43.3	1,406.4	1,108.7	733.2	5,196.1

All capital investment is recognised initially within assets under construction. When assets are capable of performing the function for which they were constructed and come into beneficial use, they are reclassified and transferred from assets under construction to the appropriate fixed asset category.

Capital grants received during the year and credited to deferred income were £nil (2012: £0.1 million). No capital grants were received during the year in respect of infrastructure assets.

9 Property, plant and equipment continued

	Specialised operational properties and structures £m	Non-specialised operational properties £m	Infrastructure assets £m	Plant, machinery and vehicles £m	Assets under construction £m	Total £m
Company						
Cost						
At 1 April 2011	2,552.7	68.6	1,768.9	2,092.8	902.4	7,385.4
Additions	0.8	–	–	–	346.9	347.7
Disposals	(1.3)	(1.0)	–	(4.7)	–	(7.0)
Reclassifications	202.0	1.9	66.4	248.3	(518.6)	–
At 31 March 2012	2,754.2	69.5	1,835.3	2,336.4	730.7	7,726.1
Additions	1.6	–	–	–	382.6	384.2
Disposals	(1.5)	(0.7)	–	(2.3)	–	(4.5)
Reclassifications	69.6	0.4	88.7	139.1	(297.8)	–
At 31 March 2013	2,823.9	69.2	1,924.0	2,473.2	815.5	8,105.8
Accumulated depreciation						
At 1 April 2011	794.4	25.7	415.5	1,067.6	–	2,303.2
Charge for the year	67.7	1.2	13.4	168.8	–	251.1
Disposals	–	(0.7)	–	(4.5)	–	(5.2)
At 31 March 2012	862.1	26.2	428.9	1,231.9	–	2,549.1
Charge for the year	66.2	4.2	13.8	169.4	–	253.6
Disposals	(0.6)	(0.6)	–	(2.2)	–	(3.4)
At 31 March 2013	927.7	29.8	442.7	1,399.1	–	2,799.3
Net book value						
At 31 March 2013	**1,896.2**	**39.4**	**1,481.3**	**1,074.1**	**815.5**	**5,306.5**
At 31 March 2012	1,892.1	43.3	1,406.4	1,104.5	730.7	5,177.0

Notes to the financial statements continued

For the year ended 31 March 2013

9 Property, plant and equipment continued

Included within specialised operational properties and structures and plant, machinery and vehicles are the following PFI assets which are held under finance leases. These assets are included within the previous tables for both the Group and the Company.

	Specialised operational properties and structures £m	Plant, machinery and vehicles £m	Total £m
Group and Company			
Cost			
At 1 April 2011, 31 March 2012 and 31 March 2013	221.7	347.1	568.8
Accumulated depreciation			
At 1 April 2011	43.9	134.0	177.9
Charge for the year	3.7	11.6	15.3
At 31 March 2012	47.6	145.6	193.2
Charge for the year	3.7	11.6	15.3
At 31 March 2013	51.3	157.2	208.5
Net book value			
At 31 March 2013	**170.4**	**189.9**	**360.3**
At 31 March 2012	174.1	201.5	375.6

10 Investments

	Company 2013 £m	Company 2012 £m
Cost and net book value		
At 1 April 2012	37.6	37.6
Increase of shareholding in Scottish Water Horizons Holdings Limited	–	34.6
Transfer of shareholding in Scottish Water Business Stream Holdings Limited	–	(34.6)
At 31 March 2013	**37.6**	**37.6**

During 2011/12 the Scottish Water group of companies was restructured to optimise the financing of Scottish Water's non-regulated trading activities. In November 2011, Scottish Water transferred its shareholding in Scottish Water Business Stream Holdings Limited (and its subsidiary Scottish Water Business Stream Limited) to Scottish Water Horizons Holdings Limited (SWHH). In January 2012, Scottish Water International Limited was set up and is 100% owned by SWHH.

Investment in subsidiaries

Principal subsidiary undertakings	Country of incorporation	% of Ordinary shares and votes held	Principal activity
Scottish Water Horizons Holdings Limited	Scotland	100.0	Holding company
Scottish Water Business Stream Holdings Limited *	Scotland	100.0	Holding company
Scottish Water Business Stream Limited **	Scotland	100.0	Licensed water and waste water services
Scottish Water Horizons Limited *	Scotland	100.0	Commercial non regulated water and waste water services
Scottish Water International Limited *	Scotland	100.0	Overseas consultancy

* owned by Scottish Water Horizons Holdings Limited
** owned by Scottish Water Business Stream Holdings Limited

Scottish Water owns shares in a further seven companies, which did not trade during the year ended 31 March 2013. The companies' financial statements have not been consolidated as permitted by Section 405 of the Companies Act 2006, as they did not trade during the year and the issued share capital is immaterial.

Group
Investment in Jointly Controlled Operations
On 6 April 2010 Scottish Water Solutions 2 Limited (SWS2) commenced trading. This company is jointly owned with Thistle Water Limited and will deliver part of Scottish Water's capital investment programme for the 2010 to 2015 regulatory period. The nature of the contractual agreement between Scottish Water and the other shareholder in SWS2 is such that the parties are engaged in joint activities that do not constitute an entity carrying on a trade or business in its own right. Consequently, SWS2 is accounted for, under IAS 31 'Interests in Joint Ventures', as a Jointly Controlled Operation. Details of the investment is as follows:

	Country of incorporation	% of Ordinary shares and votes held	Principal activity
Scottish Water Solutions 2 Limited	Scotland	51.0	Contracting services

Scottish Water Solutions Limited (SWS), formed in June 2002 and jointly owned with Stirling Water Limited and UUGM Limited, delivered the majority of Scottish Water's capital investment programme for the 2006 to 2010 regulatory period. In May 2012, SWS delivered the last remaining project to Scottish Water and is currently in the process of being wound down.

10 Investments continued

Summary aggregated financial information on jointly controlled entities – 51%:

	2013 £m	2012 £m
Current assets	14.4	22.8
Current liabilities	14.4	22.8
Income	73.8	79.5
Expenses	73.8	79.5

The information detailed above for 2013 was extracted from the financial statements for SWS and SWS2. SWS and SWS2 themselves have no contingent liabilities and there are no contingent liabilities relating to Scottish Water's interest in SWS or SWS2.

11 Inventories

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Raw materials and consumables	2.5	2.0	2.3	1.8
Less provision held	(0.1)	(0.1)	(0.1)	(0.1)
	2.4	**1.9**	**2.2**	**1.7**

All inventories will be recovered within 12 months.

12 Trade and other receivables

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Trade receivables	492.7	445.7	416.1	376.9
Less provision for impairment of trade receivables	(389.4)	(358.3)	(376.5)	(346.0)
Net trade receivables	103.3	87.4	39.6	30.9
Other receivables	24.0	23.5	22.8	21.0
Prepayments and accrued income	43.3	74.6	7.7	5.5
Amounts due from subsidiaries	–	–	0.1	1.5
	170.6	**185.5**	**70.2**	**58.9**

The following table shows the development of the provision for impairment of trade receivables:

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Balance at 1 April	358.3	331.7	346.0	322.0
Charge for the year	36.4	31.3	30.5	24.3
Amounts written down during the year	(5.3)	(4.7)	–	(0.3)
Balance at 31 March	389.4	358.3	376.5	346.0

Management considers the carrying value of trade and other receivables are equal to the fair value.

13 Cash and cash equivalents

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Cash at bank and in hand	191.7	68.3	51.6	20.1
Short-term bank deposits	223.9	286.9	193.9	220.9
Cash and cash equivalents per the statement of cash flows	**415.6**	**355.2**	**245.5**	**241.0**

The fair values of cash and cash equivalents are not different from those disclosed above.

14 Trade and other payables

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Current				
Trade payables	28.5	26.3	26.6	23.9
Non trade payables and accruals	80.2	86.5	79.5	86.4
Accruals	162.8	146.1	143.8	133.6
Payments received in advance	99.0	84.9	5.0	8.9
Other payables	19.2	20.6	4.2	5.5
Deferred income	2.2	2.5	1.3	1.1
Other taxes and social security	2.8	2.6	2.5	2.5
Amounts due to subsidiaries	–	–	25.5	24.9
Amounts due to jointly owned operations	19.9	34.5	19.9	34.5
	414.6	**404.0**	**308.3**	**321.3**
Non-current				
Other payables	61.7	47.8	61.7	47.8
Deferred income	21.6	22.8	15.6	16.6
	83.3	**70.6**	**77.3**	**64.4**

The fair values of trade and other payables are not different from those disclosed above.

15 Deferred taxation

The following are the deferred tax liabilities and assets recognised by the Group and movements thereon during the current and prior reporting periods:

	Note	Accelerated capital allowances £m	Retirement benefit obligations £m	Tax losses £m	Other £m	Total £m
Group						
At 1 April 2011		520.4	(73.8)	(64.4)	(7.8)	374.4
Charge/(credit) to income statement	8	(2.3)	0.3	2.8	(1.5)	(0.7)
Charge to reserves	22	–	6.0	–	–	6.0
At 31 March 2012		518.1	(67.5)	(61.6)	(9.3)	379.7
Charge/(credit) to income statement	8	3.7	3.7	(7.5)	(0.8)	(0.9)
Charge to reserves	22	–	7.2	–	–	7.2
At 31 March 2013		**521.8**	**(56.6)**	**(69.1)**	**(10.1)**	**386.0**
Company						
At 1 April 2011		519.4	(73.3)	(64.3)	(8.0)	373.8
Charge/(credit) to income statement		(2.5)	0.4	2.8	(0.8)	(0.1)
Charge to reserves	22	–	5.3	–	–	5.3
At 31 March 2012		516.9	(67.6)	(61.5)	(8.8)	379.0
Charge/(credit) to income statement		4.6	3.6	(6.9)	(1.1)	0.2
Charge to reserves	22	–	7.1	–	–	7.1
At 31 March 2013		**521.5**	**(56.9)**	**(68.4)**	**(9.9)**	**386.3**

Certain deferred tax assets and liabilities have been offset, including the asset balances analysed in the tables above. The following is an analysis of the deferred tax balances (after offset) for financial reporting purposes:

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Deferred tax assets	(0.2)	–	–	–
Deferred tax liabilities	386.2	379.7	386.3	379.0
At 31 March	**386.0**	**379.7**	**386.3**	**379.0**

The Members believe that the deferred tax assets will be recoverable against projected taxable profits over the foreseeable future in the companies to which they relate.

No deferred tax is provided on temporary differences arising on investments in subsidiaries because, in each case, the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future. The amount of temporary differences associated with investments in subsidiaries for which a deferred tax liability has not been recognised is £103 million (2012: £72 million) for both the Company and the Group. No tax is expected to be payable in this regard.

16 Provisions for liabilities

	Restructure provision £m	Income uncertainty provision £m	Other £m	Total £m
Group				
At 1 April 2011	7.8	3.4	0.6	11.8
Charged to the income statement	1.7	1.4	0.1	3.2
Utilised during the year	(8.3)	–	(0.2)	(8.5)
At 31 March 2012	1.2	4.8	0.5	6.5
Charged/(released) to the income statement	3.7	(4.8)	0.3	(0.8)
Utilised during the year	(2.3)	–	–	(2.3)
At 31 March 2013	**2.6**	**–**	**0.8**	**3.4**
Company				
At 1 April 2011	7.1	3.4	0.6	11.1
Charged to the income statement	1.6	1.4	0.1	3.1
Utilised during the year	(7.8)	-	(0.2)	(8.0)
At 31 March 2012	0.9	4.8	0.5	6.2
Charged/(released) to the income statement	3.5	10.7	0.3	14.5
Utilised during the year	(1.9)	–	–	(1.9)
At 31 March 2013	**2.5**	**15.5**	**0.8**	**18.8**

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Analysis of total provisions				
Current	3.2	5.4	17.6	5.1
Non-current	0.2	1.1	1.2	1.1
	3.4	6.5	18.8	6.2

The restructuring provision relates to redundancy costs associated with employees who will leave Scottish Water under voluntary redundancy and early retirement. It is expected that the provision will be utilised within the next year. Pension related liabilities associated with employees who have left Scottish Water under the voluntary severance scheme are recognised in the pension liability (note 22).

The income uncertainty provision relates to non-household revenues. The reconciliation process, through the Central Market Agency, relating to each financial year would normally be finalised 18 months after the end of the relevant financial year. The reduction in the group provision reflects the progress made in stabilising the settlement processes and data. At the company level, the provision represents the agreed intercompany settlement positions forecast for the relevant financial years. At 31 March 2013, the settlement reports for 2008/09 and 2009/10 had been finalised, whereas the 2010/11 and 2011/12 financial years had not yet been finalised. It is expected that the provision will be utilised during 2014.

The other provision of £0.8 million relates primarily to onerous property rental costs which will be utilised over the next two years.

Notes to the financial statements continued

For the year ended 31 March 2013

17 Other loans and borrowings

	2013 £m	2012 £m
Group and Company		
Current		
Non-government loans	0.9	1.7
Obligations under finance leases	16.3	15.5
	17.2	**17.2**
Non current		
Non-government loans	1.5	2.4
Obligations under finance leases	399.2	415.5
	400.7	**417.9**
Total		
Non-government loans	2.4	4.1
Obligations under finance leases	415.5	431.0
	417.9	435.1

(i) Non-government loans
Other loans are repayable as follows:

	Up to 1 year £m	1-2 years £m	3-5 years £m	6-10 years £m	Total £m
At 31 March 2013	0.9	0.5	–	1.0	2.4
At 31 March 2012	1.7	0.9	0.5	1.0	4.1

The carrying amounts and fair value of the non-government borrowings are as follows:

	Book value 2013 £m	Book value 2012 £m	Fair value 2013 £m	Fair value 2012 £m
Non-government loans	2.4	4.1	3.1	5.0

(ii) Finance lease liabilities – PFI liabilities
Future finance lease commitments are as follows:

	Minimum lease payments		Present value of minimum lease payments	
	2013 £m	2012 £m	2013 £m	2012 £m
Amounts payable:				
Within one year	40.9	40.9	16.3	15.5
Between one and five years	163.5	163.6	97.0	91.7
After five years	467.1	507.9	302.2	323.8
Present value of minimum lease payments including finance charges	671.5	712.4		
Less future finance charges	(256.0)	(281.4)		
Present value of minimum lease payments	415.5	431.0	415.5	431.0

17 Other loans and borrowings continued

PFI – Service concession arrangements
Upon its creation in April 2002 Scottish Water inherited nine concession contracts which had been entered into with nine private sector consortia ("PFI Cos") by its three predecessor authorities (i.e. East of Scotland Water Authority, North of Scotland Water Authority and West of Scotland Water Authority). Scottish Water acts as the client body to the nine private sector consortia that provide waste water and sludge treatment and disposal services to Scottish Water.

These contracts are based over a wide geographic area including the Aberdeen, Dundee, Edinburgh, Glasgow and Inverness conurbations as well as the Ayrshire, Fife and Moray coasts.

Characteristics of the arrangements
Description
The length of these contracts varies between 25 and 40 years with expiry dates ranging from December 2021 through to October 2040. Under the terms of these contracts the private sector have either upgraded or built new waste water and sludge treatment assets, and, in certain circumstances, network assets (e.g. sewers and pumping stations) in order to meet Scottish Water's legal obligations in respect of the treatment and disposal of these products. These consortia are also responsible for the operation and maintenance of these assets over the lifetime of each contract.

Significant terms
The key terms relate to the basis upon which Scottish Water pays the services provided by the PFI Cos. The levels of such payments are predominantly dependent upon the volume of waste water and sludge treated, although in a minority of contracts there is either a partial availability payment element or some part of the payment is linked to the strength of the waste water. Scottish Water also has the power to levy payment deductions where the level of service falls below pre-determined standards, primarily linked to the quality of the treated waste water.

The contracts are structured such that either party may seek to amend the basis upon which the service is provided, primarily where driven by a change in law. This is subject to a formal variation procedure and is ultimately dependent upon the parties reaching agreement on the contractual changes required to give effect to the specific variation.

Nature and extent of rights and obligations
Scottish Water's primary obligations are to deliver waste water to the PFI Cos and thereafter pay for the treatment services provided, making the appropriate deduction where the PFI Cos fail to meet the appropriate performance standards. The PFI Cos provided the initial construction services through a sub-contract and also entered into a separate sub-contract for the operation and maintenance of these assets once satisfactorily commissioned. All such projects are now in their operational phase.

A majority of the contracts have limited extension options. However, termination during the contractual period can arise for a number of reasons including default (by either the PFI Co or Scottish Water), force majeure, uninsurable events or voluntary termination by Scottish Water. Each contract contains a formula from which termination compensation payable by Scottish Water is derived.

Other than each party's unilateral right to propose an amendment to a contract, the most likely circumstance which would give rise to the re-negotiation of a contract is as a result of a change in law which requires the manner in which the treatment and disposal service is delivered to be changed, in order to ensure it meets the requirements of such legislative changes.

The contracts also stipulate a range of handback conditions linked to the remaining life of certain assets.

Notes to the financial statements continued

For the year ended 31 March 2013

18 Government loans

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Government loans	3,325.4	3,223.7	3,266.9	3,165.2

Scottish Water's borrowing powers are defined in Section 42 of the Water Industry (Scotland) Act 2002. The limit at 31 March 2013 on these powers was that total net new borrowings for the year ended 31 March 2013 should not exceed £100.0 million. Net new borrowings were £100.0 million in the year.

Government loans, both short and long-term, are recorded on the balance sheet under Capital and Reserves in accordance with the Scottish Water Governance Directions 2009. Other debt is recorded under short and long-term payables following best practice.

a. Analysis of borrowings by type and maturity

	Up to 1 year £m	1-2 years £m	3-5 years £m	6-10 years £m	Over 10 years £m	Total £m
Scottish Consolidated Fund – SW Company	261.1	80.5	223.0	421.3	1,413.5	2,399.4
Scottish Consolidated Fund – subsidiaries	58.5	–	–	–	–	58.5
Scottish Consolidated Fund – SW Group	319.6	80.5	223.0	421.3	1,413.5	2,457.9
National Loans Fund	7.0	5.0	68.0	173.0	448.9	701.9
Public Works Loan Board	19.9	29.5	70.1	34.7	11.4	165.6
At 31 March 2013	**346.5**	**115.0**	**361.1**	**629.0**	**1,873.8**	**3,325.4**
At 31 March 2012	310.4	109.4	353.4	589.1	1,861.4	3,223.7

b. Fair values

The carrying amounts and fair value of the Government borrowings are as follows:

	Book value 2013 £m	Book value 2012 £m	Fair value 2013 £m	Fair value 2012 £m
Scottish Consolidated Fund	2,457.9	2,315.8	2,871.0	2,660.3
National Loans Fund	701.9	735.9	992.1	1,008.4
Public Works Loan Board	165.6	172.0	215.7	231.0
	3,325.4	3,223.7	4,078.8	3,899.7

19 Analysis of net debt

	Note	As at 1 April 2012 £m	Increase in cash £m	Decrease/(increase) in debt £m	As at 31 March 2013 £m
Group					
Cash and cash equivalents	13	355.2	60.4	–	415.6
Government loans	18	(3,223.7)	–	(101.7)	(3,325.4)
Other loans	17	(4.1)	–	1.7	(2.4)
Net debt		(2,872.6)	60.4	(100.0)	(2,912.2)
Company					
Cash and cash equivalents	13	241.0	4.5	–	245.5
Government loans	18	(3,165.2)	–	(101.7)	(3,266.9)
Other loans	17	(4.1)	–	1.7	(2.4)
Net debt		(2,928.3)	4.5	(100.0)	(3,023.8)

20 Reserves

	Note	Retained earnings excluding actuarial gains/(losses) £m	Actuarial gains/(losses) on pension obligations £m	Retained earnings including actuarial gains/(losses) £m
Group				
At 1 April 2011		918.8	(206.1)	712.7
Retained surplus for the year		98.5	–	98.5
Actuarial loss, net of deferred taxation	22	–	(10.0)	(10.0)
At 31 March 2012		**1,017.3**	**(216.1)**	**801.2**
Retained surplus for the year		89.2	–	89.2
Actuarial gain, net of deferred taxation	22	–	12.6	12.6
At 31 March 2013		**1,106.5**	**(203.5)**	**903.0**
Company				
At 1 April 2011		872.6	(204.0)	668.6
Retained surplus for the year		74.2	–	74.2
Actuarial loss, net of deferred taxation	22	–	(12.0)	(12.0)
At 31 March 2012		**946.8**	**(216.0)**	**730.8**
Retained surplus for the year		63.4	–	63.4
Actuarial gain, net of deferred taxation	22	–	12.2	12.2
At 31 March 2013		**1,010.2**	**(203.8)**	**806.4**

Notes to the financial statements continued

For the year ended 31 March 2013

21 Results of Scottish Water (the Company)

Of the results for the financial year, a retained surplus of £63.4 million (2012: £74.2 million), is dealt with in the consolidated financial statements of Scottish Water. The Members have taken advantage of the exemption available under section 408 of the Companies Act 2006 and do not present an income statement for Scottish Water alone.

22 Pensions

Employees of Scottish Water participate in the North East Scotland Pension Fund, the Lothian Pension Fund and the Strathclyde Pension Fund, which are part of the Local Government Pension Scheme administered by Aberdeen, Edinburgh and Glasgow City Councils respectively. The schemes provide defined benefits based on final pensionable pay. Actual pension costs for the year for each fund, as a % of pensionable pay, were 19.3% (2012: 19.3%), 24.0% (2012: 24.0%) and 19.3% (2012: 19.3%) respectively.

A full actuarial valuation was carried out at 31 March 2011 for all three funds and updated at 31 March 2013 by a qualified independent actuary, to take account of the requirements of IAS 19.

The major assumptions used by the actuaries were:

	2013 %	2012 %
Rate of increase in pensionable salaries	2.5	2.5
Rate of increase in pensions payment	2.7	2.7
Discount rate	4.3	4.7
Inflation rate	2.7	2.7

Longevity assumptions on retiring at age 65 adopted for each fund:

	North East Scotland Years	Lothian Years	Strathclyde Years
Retiring at 31 March 2013			
Male	22.4	20.6	21.2
Female	25.4	23.0	23.6
Retiring at 31 March 2033			
Male	24.6	22.8	23.5
Female	27.8	25.6	25.5

The sensitivities regarding the principal assumptions used to measure the liability in the Funds are:

Assumption	Change in assumption	Approximate Impact on IAS 19 liability %	Approximate Impact on IAS 19 deficit £m
Rate of increase in pensionable salaries	+/- 0.5% per annum	Increase / decrease by c. 2.5%	Increase / decrease by c. £33 million
Discount rate	+/- 0.5% per annum	Decrease / increase by c. 10%	Decrease / increase by c. £133 million
CPI Inflation rate	+/- 0.5% per annum	Increase / decrease by c. 7%	Increase / decrease by c. £93 million
Longevity	Increase life expectancy by 1 year	Increase by c. 3.0% – 4.0%	Increase by c. £40 million to £53 million

22 Pensions continued

Scottish Water's share of the assets in the schemes and the expected rate of return were:

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Total market value of assets	1,087.4	935.2	1,073.8	924.7
Present value of scheme liabilities	(1,333.6)	(1,216.3)	(1,321.4)	(1,206.4)
Gross pension liability	**(246.2)**	**(281.1)**	**(247.6)**	**(281.7)**
Related deferred tax asset	56.6	67.5	56.9	67.6
Net pension liability	(189.6)	(213.6)	(190.7)	(214.1)

Scheme assets are stated at their bid values.

Reconciliation of opening and closing retirement benefit liabilities and assets

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Movements in liabilities during the year:				
Opening value of total liabilities	(1,216.3)	(1,199.2)	(1,206.4)	(1,189.2)
Current service cost	(19.9)	(17.7)	(18.9)	(16.8)
Interest on pension scheme liabilities	(56.8)	(65.7)	(56.3)	(65.1)
Contributions by members	(6.5)	(6.4)	(6.1)	(6.1)
Actuarial (loss)/gain	(69.5)	39.5	(69.0)	37.7
Impact of curtailments	(1.0)	(2.4)	(1.0)	(2.4)
Benefits paid	36.4	35.6	36.3	35.5
Closing value of total liabilities	(1,333.6)	(1,216.3)	(1,321.4)	(1,206.4)
Movement in assets during the year:				
Opening fair value of total assets	935.2	915.2	924.7	907.3
Expected return on pension scheme assets	52.4	62.3	51.8	61.7
Contributions by members	6.5	6.4	6.1	6.1
Contributions by the employer	39.4	28.0	38.2	27.1
Actuarial (loss)/gain	89.7	(52.4)	88.7	(53.3)
Impact of settlements	0.6	11.3	0.6	11.3
Benefits paid	(36.4)	(35.6)	(36.3)	(35.5)
Closing fair value of assets	1,087.4	935.2	1,073.8	924.7
Gross deficit in the schemes at 31 March	(246.2)	(281.1)	(247.6)	(281.7)

Notes to the financial statements continued

For the year ended 31 March 2013

22 Pensions continued

Return on assets
As required by IAS 19, the expected return on assets is based on the long-term expectation of returns for each asset class at the beginning of the year. As next year's disclosures will be produced under IAS19R (the revised standard), the expected return on assets for all asset categories is equal to the discount rate. Assets with higher volatility will no longer generate higher returns.

	Group		Company	
	2013 £m	**2012 £m**	**2013 £m**	**2012 £m**
Actual return on pension scheme assets	142.2	10.2	140.5	10.1
Actuarial gain/(loss) in other comprehensive income in the consolidated statement of comprehensive income				
Variance between pension fund actuarial assumptions and actual experience	20.2	(12.9)	19.7	(15.6)
Impact of settlements and curtailments	(0.4)	8.9	(0.4)	8.9
Gross actuarial gain/(loss) recognised in the pension fund	**19.8**	**(4.0)**	**19.3**	**(6.7)**
Deferred tax movement	(7.2)	(6.0)	(7.1)	(5.3)
Net actuarial gain/(loss) recognised in other comprehensive income in the consolidated statement of comprehensive income	**12.6**	**(10.0)**	**12.2**	**(12.0)**

Amounts recognised in the consolidated income statement

	Note	**2013 £m**	**2012 £m**
Total current service cost	5	19.9	17.7
Interest cost on pension scheme liabilities	7	56.8	65.7
Expected return on pension scheme assets	7	(52.4)	(62.3)
		24.3	21.1

The unpaid contributions outstanding at the year end included in other payables (note 14) was £2.0 million (2012: £2.2 million). It is estimated that Scottish Water will make contributions of £21.5 million to the pension funds in financial year 2013/14.

22 Pensions continued

History of experience gains and losses

Group	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Difference between the expected and actual return on scheme assets:					
Amount	89.7	(52.4)	4.8	189.1	(184.0)
Fair value of assets	1,087.4	935.2	915.2	843.9	615.5
Experienced gains/(losses) on scheme liabilities:					
Amount	1.9	56.4	2.3	(0.4)	13.1
Present value of liabilities	1,333.6	1,216.3	1,199.2	1,306.7	838.9
Changes in assumptions underlying the present value of scheme liabilities:					
Amount	(71.4)	(16.9)	93.7	(420.8)	(12.1)
Total variance between pension fund actuarial assumptions and actual experience	**20.2**	**(12.9)**	**100.8**	**(232.1)**	**(183.0)**
Gross deficit in the schemes at 31 March	(246.2)	(281.1)	(284.0)	(462.8)	(223.4)

Company	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Difference between the expected and actual return on scheme assets:					
Amount	88.7	(53.3)	4.8	187.7	(183.5)
Fair value of assets	1,073.8	924.7	907.3	837.5	611.5
Experienced gains/(losses) on scheme liabilities:					
Amount	1.9	54.7	2.3	(0.4)	13.3
Present value of liabilities	1,321.4	1,206.4	1,189.2	1,297.1	834.4
Changes in assumptions underlying the present value of scheme liabilities:					
Amount	(70.9)	(17.0)	93.1	(416.6)	(12.2)
Total variance between pension fund actuarial assumptions and actual experience	**19.7**	**(15.6)**	**100.2**	**(229.3)**	**(182.4)**
Gross deficit in the schemes at 31 March	(247.6)	(281.7)	(281.9)	(459.6)	(222.9)

23 Commitments

a. Capital commitments
The Group has contracted capital commitments of £175.5 million (2012: £233.4 million) relating to property, plant and equipment at the balance sheet date. These commitments are expected to be settled within the following two financial years.

b. Operating lease commitments
The Group leases various operational properties and offices under non-cancellable operating lease agreements. The lease terms are between 1 and 99 years, with the majority of lease agreements being renewable at the end of the lease period at market rates.

The Group also leases vehicles under cancellable operating lease agreements. The Group is able to give notice at any time within the lease period for the termination of these agreements. Termination costs are incurred on early termination. The lease expenditure charged to the consolidated income statement during the year is disclosed in note 4.

The total minimum lease payments under non-cancellable operating leases are as follows:

	2013 £m	2012 £m
Within one year	1.9	2.0
Between one and five years	5.6	5.5
After five years	19.3	19.1
	26.8	26.6

24 Contingent liabilities

Scottish Water has the following contingent liabilities in respect of companies limited by guarantees:

Central Market Agency
The Central Market Agency (CMA), a company limited by guarantee, co-ordinates the non-household retail market for business customers in Scotland. As a market participant, Scottish Water is liable to pay charges to the CMA to cover part of the operating, financing and any other capital costs of the organisation. These charges are set annually in advance and approved by the CMA Board. Scottish Water's liability, as a member, for the debts and liabilities of the CMA is limited to £1.

Water Regulatory Advisory Service
Water Regulatory Advisory Service Limited (WRAS) is a company established by all UK water companies as a company limited by guarantee to provide guidance on the development and application of the Water Regulations (England and Wales) and the Water Byelaws (Scotland). WRAS operates on a subscription basis. Scottish Water's liability, as a member, in the event of the company going into default, is limited to £1. Scottish Water may withdraw from the company by giving one year's notice.

25 Related party transactions

The Group has related party relationships with the Scottish Government, with its subsidiaries and jointly controlled operations (note 10), and with its Members and Executive Management. Details of transactions between the Group and other related parties are disclosed below.

Scottish Government
Scottish Water is a public corporation of a trading nature sponsored by the Scottish Government. During the year Scottish Water had various material transactions with the Scottish Government, namely the drawdown and repayment of loans. Details of the loans from the Scottish Government are shown in note 18.

During the year Scottish Water had various material transactions with entities for which the Scottish Government is regarded as the parent. The main entities which fall into this category are the Local Authorities, the Scottish Environment Protection Agency, the Water Industry Commission for Scotland and the Central Market Agency. However, as permitted under IAS 24 'Related Party Disclosures' paragraph 25, Scottish Water is exempt from the disclosure requirements of IAS 24, paragraph 18 in respect of these government related entities.

Jointly controlled operations
In the course of normal operations, Scottish Water contracted on an arms-length basis with Scottish Water Solutions Limited (a Joint Arrangement between Scottish Water, Stirling Water Limited and UUGM Limited) and Scottish Water Solutions 2 Limited (a Joint Arrangement between Scottish Water and Thistle Water Limited). The aggregate transactions which are considered to be material and which have not been disclosed elsewhere in the financial statements are summarised below, gross of value added tax:

	2013 £m	2012 £m
Sales and costs charged to Scottish Water Solutions Limited	0.4	2.9
Purchases from Scottish Water Solutions Limited	(17.5)	(19.5)
Amounts due to Scottish Water Solutions Limited (note 14)	–	2.3
Sales and costs charged to Scottish Water Solutions 2 Limited	9.6	10.3
Purchases from Scottish Water Solutions 2 Limited	(154.5)	(167.2)
Amounts due to Scottish Water Solutions 2 Limited (note 14)	19.9	32.2

In May 2012, Scottish Water Solutions Limited (SWS) delivered the last remaining project to Scottish Water under the 2006-10 investment programme. In September 2012, SWS arrived at a commercial settlement with Scottish Water to buy itself out of its remaining defects liability. As a consequence, SWS has no remaining trading activities and is in the process of being wound down.

Subsidiaries
During the year the Company entered into the following transactions with its subsidiaries (note 10):

	2013 £m	2012 £m
Sale of water and waste water services	289.0	290.8

Key management personnel
The key management under IAS 24 'Related Party Disclosure' is defined as those persons who have authority and responsibility for planning, directing and controlling the entity's activities, directly or indirectly. The Group's key management comprises the Executive Members and Non-executive Members. The remuneration of the Members is determined by Scottish Water's Remuneration Committee in accordance with its stated policy. Further information about the remuneration and pension details of individual Members is provided in the Members' Remuneration Report on pages 34 to 38.

Notes to the financial statements continued

For the year ended 31 March 2013

26 Financial instruments and risks

The management of Scottish Water and the execution of strategy are subject to a number of risks as detailed below. All risks are reviewed by the Board and appropriate processes are in place to monitor and mitigate them. See the Corporate Governance report on pages 31 to 33.

a. Qualitative risk disclosures

Operational and business risk

This is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It also includes losses due to external factors such as the market situation or government regulations. Reputational risk is included in this category. The risk register and risk management processes identify key operational and other risks and are reviewed on a regular basis.

Credit risk

Credit risk is the risk that Scottish Water is exposed to loss if another party fails to perform its financial obligation to Scottish Water. Credit risk arises from cash, cash equivalents and deposits with banks and financial institutions, as well as credit exposures to wholesale and retail customers, including outstanding receivables and committed transactions. Scottish Water monitors its credit exposure to its counterparties via their credit ratings (where applicable) and through its policy, thereby limiting its exposure to any one party to ensure that they are within Board approved limits and that there are no significant concentrations of credit risk. The maximum exposure to credit risk for receivables and other financial assets is represented by their carrying amount.

Liquidity risk

Liquidity risk is the risk that Scottish Water will have insufficient funds to meet its liabilities. Scottish Water's policy is to ensure that it has adequate financial resources to enable it to finance its day-to-day operations and capital investment programme, based on cash flow projections, while adhering to the annual limits set by the Scottish Government for new borrowings. Scottish Water's borrowing powers are defined in Section 42 of the Water Industry (Scotland) Act 2002.

Interest rate risk

All of Scottish Water's borrowings are at fixed interest rates. Therefore Scottish Water is not deemed to bear any interest rate risk.

b. Categories of financial assets and liabilities and fair values

Scottish Water's financial assets and liabilities comprise trade and other receivables (note 12), cash and cash equivalents (note 13), borrowings (notes 17 and 18) and trade and other payables (note 14). No trading in derivative financial instruments was undertaken.

Basis of determining fair value

The financial assets of the Group and the Company fall into the 'loans and receivables' category. The financial liabilities of the Group and the Company fall into the category of 'financial liabilities measured at amortised cost'.
Fair value is the amount at which a financial instrument could be exchanged in an arms-length transaction between informed and willing partners, other than in a forced or liquidation sale, and excludes accrued interest.

The carrying amounts of financial assets and liabilities, excluding borrowings, are equal to their fair values. Borrowings are held at cost in the balance sheet but the fair value is disclosed in notes 17 and 18.

Credit risk

Cash and cash equivalents comprise cash in hand and deposits which are readily convertible to cash. These are subject to insignificant risk of change in value or credit risk.

The trade receivables total includes an allowance for impairment. Trade receivables comprise receivables from business customers and receivables from domestic household customers.

	Group		Company	
	2013 £m	2012 £m	2013 £m	2012 £m
Trade receivables per note 12:				
Trade receivables	492.7	445.7	416.1	376.9
Less provision for impairment of trade receivables	(389.4)	(358.3)	(376.5)	(346.0)
Net trade receivables	103.3	87.4	39.6	30.9
Analysed between:				
Household receivables	409.6	372.3	409.6	372.3
Less provision for impairment	(372.8)	(344.9)	(372.8)	(344.9)
Net household receivables	36.8	27.4	36.8	27.4
Business customer receivables	83.1	73.4	6.5	4.6
Less provision for impairment	(16.6)	(13.4)	(3.7)	(1.1)
Net business customer receivables	66.5	60.0	2.8	3.5

26 Financial instruments and risks continued

Household water and waste water services are billed to customers by Local Authorities as an element of the annual Council Tax bills. The Local Authorities are responsible for the collection and transfer to Scottish Water of the amounts due in accordance with the statutory regulations. Household charges are billed by individual financial year and are payable within the same year. Provision is made against outstanding debt, in respect of prior years, based primarily on historical collection rates and the near-term business outlook. Household water and waste water debt is a statutory debt recoverable from the occupier. Debt since the establishment of the former Water Authorities in 1996 continues to be collected. As at 31 March 2013 trade receivables in respect of household customers totalled £409.6 million with a provision of £372.8 million (2012: £372.3 million and £344.9 million respectively).

As at 31 March 2013 trade receivables from business customers totalled £83.1 million (2012: £73.4 million). The ageing analysis of trade receivables from business customers and the related provisioning is as follows:

	Total £m	Current £m	<3 months overdue £m	3-12 months overdue £m	>12 months overdue £m
Group					
Gross receivable	83.1	48.9	12.7	14.4	7.1
Provision	(16.6)	–	(2.1)	(7.4)	(7.1)
Net trade receivable as at 31 March 2013	66.5	48.9	10.6	7.0	–
Gross receivable	73.4	47.3	9.0	11.3	5.8
Provision	(13.4)	–	(2.0)	(5.6)	(5.8)
Net trade receivable as at 31 March 2012	60.0	47.3	7.0	5.7	–
Company					
Gross receivable	6.5	2.6	1.1	1.2	1.6
Provision	(3.7)	–	(0.9)	(1.2)	(1.6)
Net trade receivable as at 31 March 2013	2.8	2.6	0.2	–	–
Gross receivable	4.6	2.0	0.6	1.1	0.9
Provision	(1.1)	–	–	(0.2)	(0.9)
Net trade receivable as at 31 March 2012	3.5	2.0	0.6	0.9	–

27 Ultimate controlling body

Scottish Water is a public sector body, classified as a public corporation of a trading nature, and is answerable to the Scottish Parliament through Scottish Ministers.

Direction by the Scottish Ministers

In accordance with section 45(2) of the Water Industry (Scotland) Act 2002

28 Regulatory information

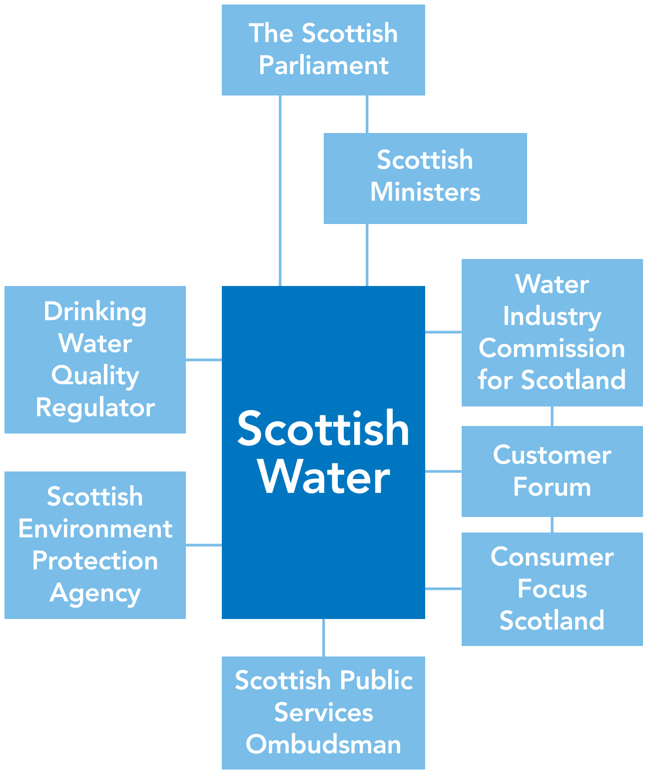
The Water Industry Commission for Scotland (the 'Commission') has the general function of promoting interests for customers in relation to the provision of core services. The Commission determines Scottish Water's price limits and approves Scottish Water's annual charges scheme.

The Commission monitors Scottish Water's performance on efficiency and customer service and approves our code of practice. Each year the Commission publishes reports on the exercise of its functions. In preparing these reports, the Commission assesses our performance by using information supplied by Scottish Water and by making comparisons with information obtained on other regulated water companies. In carrying out this performance monitoring, the Commission may make regulatory amendments to figures published in Scottish Water's audited financial statements to ensure like for like comparisons with other companies.

Under the Scottish Water Governance Directions 2009, which are available on the Scottish Government website, Scottish Water is required to disclose details of certain types of expenditure which exceed given thresholds and which are not disclosed elsewhere in the Annual Report and Accounts. The required information is presented in the following table:

Project expenditure	Threshold	Project	Cost
Capital expenditure on major works including improvements to existing assets	£10 million	National Operations Centre – Phase 2	£15.0 million
Purchase of individual capital items, including land, with a life of more than one year	£1 million	None	–
Advertising	£1 million	None	–
Sponsorship	£10,000	None	–
Gifts	£100	None	–

How our industry is run



The Scottish Parliament
Holds Scottish Water and Ministers to account and regularly calls executives to its committees to give progress updates.

Scottish Ministers
Set the objectives for Scottish Water and appoint the Chair and Non-executive Members.

Scottish Water
Responsible for providing water and waste water services to household customers and wholesale Licensed Providers. Delivers the investment priorities of Ministers within the funding allowed by the Water Industry Commission for Scotland.

Water Industry Commission for Scotland (WICS)
Economic regulator. Sets charges and reports on costs and performance.

Drinking Water Quality Regulator (DWQR)
Responsible for protecting public health by ensuring compliance with drinking water quality regulations.

Scottish Environment Protection Agency (SEPA)
Responsible for environmental protection and improvement.

Scottish Public Services Ombudsman (SPSO)
Responsible for investigating complaints about public services in Scotland, including Scottish Water, once the services' complaints procedure has been completed and sharing lessons from complaints to improve the delivery of public services.

Consumer Focus Scotland (CFS)
Responsible for representing the views and interests of Scottish Water customers and is a statutory consultee for matters relating to the Scottish water industry. Responsibilities of CFS customer representation function transferred to Consumer Futures in May 2013.

Customer Forum
Responsible for ensuring that the customer's voice is part of the price setting process and at the heart of key decisions that affect the services Scottish Water customers pay for.

Other Regulators
Like other utilities, Scottish Water is also regulated by the Health and Safety Executive (HSE) and the Scottish Road Works Commissioner.

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