



2021/22

ANNUAL REPORT
AND ACCOUNTS
PERFORMANCE
AND PROSPECTS



Scottish Water
Trusted to serve Scotland

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OVERVIEW

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ANNUAL REPORT & ACCOUNTS 2021/22: PERFORMANCE AND PROSPECTS

This Annual Report & Accounts 2021/22: Performance and Prospects provides an open and transparent view of Scottish Water's performance in the last 12 months, the first year of our new regulatory period. We highlight what has gone well, where we fell short of delivery commitments and provide an overview of our future direction.

Scottish Water is committed to listening to our customers and constantly assess and evaluate our work to continue to drive improvements for the future. This report includes lessons we have learned and what we intend to do differently to enable continued excellent service delivery.

Our strategic plan, Our Future Together, outlines our three strategic ambitions: Service Excellence; Going Beyond Net Zero Emissions; and Delivering Great Value and Financial Sustainability. This report describes our performance and prospects in these three areas during 2021/22.

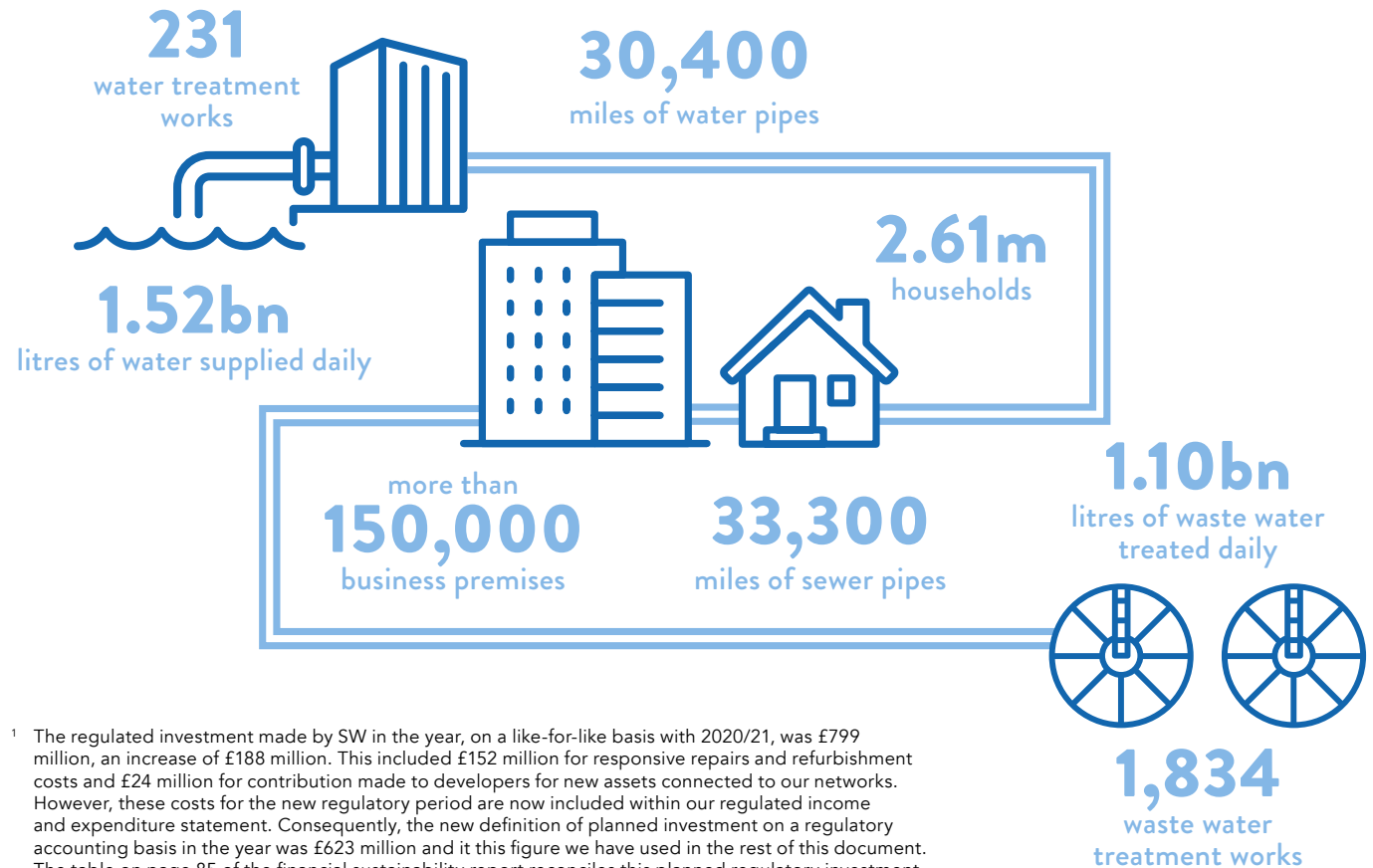


SCOTTISH WATER'S VITAL ROLE

Every day we:

- deliver 1.52 billion litres of clear, fresh drinking water; and
- remove 1.10 billion litres of waste water which we treat, recover resources from and return safely to the environment.
- Our services support over 2.6 million households and more than 150,000 business premises across Scotland.
- With more than 60,000 miles of pipes and over 2,000 treatment works we support communities across Scotland.
- In 2021/22 we invested £799 million¹, on a like-for-like basis with 2020/21 - our biggest annual investment to date.

OUR VITAL ROLE COVERS:



¹ The regulated investment made by SW in the year, on a like-for-like basis with 2020/21, was £799 million, an increase of £188 million. This included £152 million for responsive repairs and refurbishment costs and £24 million for contribution made to developers for new assets connected to our networks. However, these costs for the new regulatory period are now included within our regulated income and expenditure statement. Consequently, the new definition of planned investment on a regulatory accounting basis in the year was £623 million and it is this figure we have used in the rest of this document. The table on page 85 of the financial sustainability report reconciles this planned regulatory investment to the capital additions in the year of £581 million which were £160 million higher than 2021/21 (per note 9 to the financial statements).

CUSTOMER SERVICE PERFORMANCE 2021/22

**RANKED TOP WATER
COMPANY IN UK**
INSTITUTE OF CUSTOMER SERVICE



WE PROVIDE VITAL WATER
AND WASTE WATER SERVICES
ESSENTIAL TO DAILY LIFE

Our customers



2.61m
HOUSEHOLDS



MORE THAN
150,000
BUSINESS
PREMISES

Customer contacts

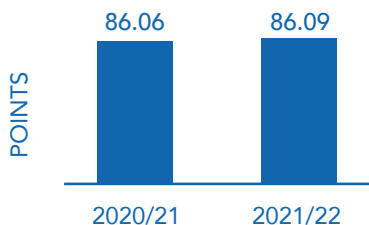


346,264
SERVICE ISSUE
CONTACTS

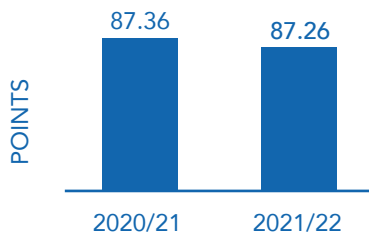
Customer experience

When compared on a like-for-like basis:

Household Customer
Experience Measure (hCEM)



Non-household Customer
Experience Measure (nhCEM)



Water supply



EVERY DAY
WE DELIVER
1.52bn
litres of clear, fresh
drinking water to taps



HIGH WATER
QUALITY
MAINTAINED

Waste water service



WE REMOVE
AND TREAT
1.10bn
litres of waste water every
day to help protect the
natural environment

Customer charges

2021/22:

INCREASE BY **2.5%**²

AROUND **£10**/YEAR HIGHER³

INCREASE BY AN AVERAGE OF **0.9%**

2022/23:

INCREASE BY **4.2%**²

AROUND **£16**/YEAR HIGHER³



AROUND HALF OF HOUSEHOLDS IN
SCOTLAND RECEIVE ADDITIONAL
FINANCIAL SUPPORT AS THEY
AUTOMATICALLY HAVE EITHER A
DISCOUNT, EXEMPTION OR
REDUCTION APPLIED TO THEIR
WATER AND WASTE WATER CHARGES.

² for those that pay full charges

³ for a Band C household

INVESTING IN OUR ASSETS

Where we are now



Large asset base

231	30,400	1,834	33,300
WATER TREATMENT WORKS	MILES OF WATER PIPES	WASTE WATER TREATMENT WORKS	MILES OF SEWER PIPES



One of the biggest critical infrastructure investors

£4.5bn ⁴	£799m ⁵
2021-27	IN 2021/22

⁴ This includes responsive repair & refurbishment costs

⁵ See previous footnote 1 on page 5

Challenges and expectations



Ageing assets

Requires doubling of investment over the next 20 years



Changing climate

Extreme weather impact on asset capacity
Impact on raw water sources



Achieving Net Zero



Forecast population change



Evolving customer expectations

How we are going to do it



Longer-term strategic approach

Asset Management Transformation Routemap
Transforming investment appraisals



Transforming our future delivery programme

Efficient delivery of increased investment



Innovating to achieve Net Zero



Collaboration with our supply chain to drive value



Transformed investment approach

Smarter investment decisions

Maximised benefits for customers, communities and the environment

NET ZERO EMISSIONS



ONE OF THE
LARGEST
ENERGY USERS
IN SCOTLAND



TOP THREE
CONSTRUCTION
INDUSTRY INVESTOR



**OPERATIONAL
AND INVESTMENT
EMISSIONS**
CALCULATED INCLUDING
FROM OUR SUPPLY CHAIN

2021/22



6%
Reduction in operational
greenhouse gas
emissions



45GWh
of on-site
self-generated
renewables



7GWh
of energy
efficiency delivered

2020

ROUITEMAP PUBLISHED

2030

NET ZERO OPERATIONAL EMISSIONS

2040

NET ZERO



Become more
energy efficient
(seeking a 20%
reduction in energy
use by 2030)



2025: no petrol or
diesel cars in fleet &
no new fossil fuel light
commercial vehicles
2030: no new fossil fuel
commercial vehicles



Embracing
innovation



Use lower carbon
energy products,
with a goal to operate
100% of our assets
using renewable
energy (through
generation or hosting)



Maximise the
energy recovered
from bioresource



Working with our
supply chain



Embracing
low carbon
construction

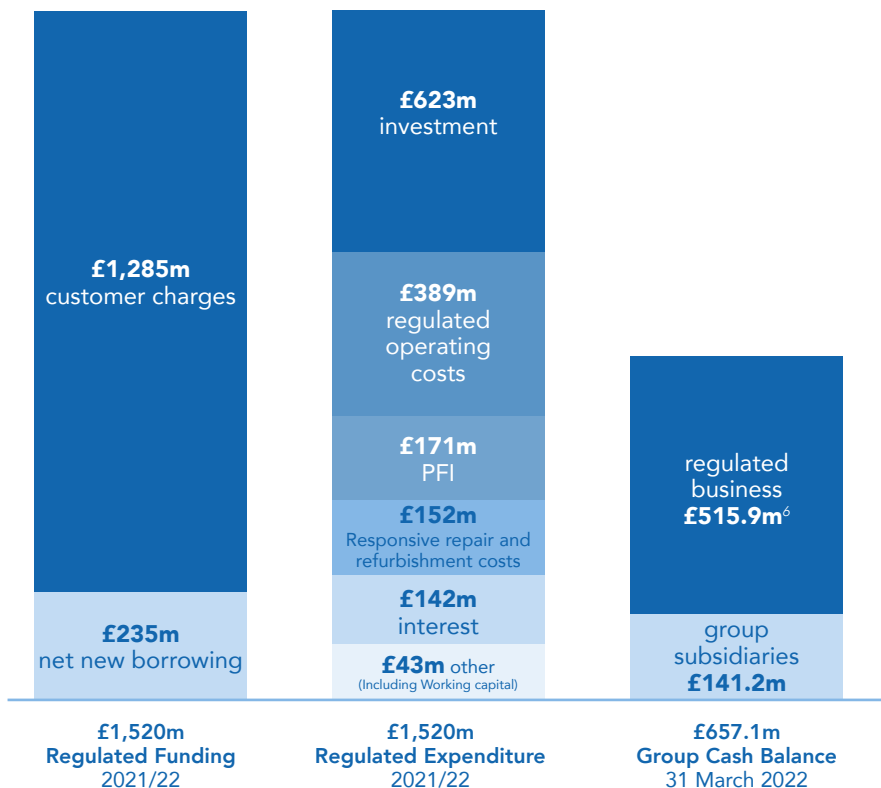


Develop natural
carbon sinks



Embracing the
circular economy

SCOTTISH WATER FINANCIAL PERFORMANCE 2021/22



⁶ Includes around £170 million to complete outstanding investment commitments made in 2015-21 and £200 million of this cash is maintained to manage the financial impact of risks and uncertainties that may arise.

Future funding need

INVESTMENT NEEDS TO
NEARLY DOUBLE BY 2040



Ageing assets



Climate change



-1% real efficiency challenge
year-on-year 2021-27

Value on tap

Scottish Water costs about £1 a day⁷.
Here's what you get for your money.



⁷ The average household is between Council Tax Band B and Band C and has a combined bill of around £1 a day.

SCOTTISH WATER


SERVING SCOTLAND FOR 20 YEARS





2002
 Founded by a merger of the West, East and North Scotland water authorities


2004
 We broke a pipe-laying records - when more than 22 miles was laid in a week in the biggest pipe rehabilitation programme in the UK to date


2006
 Business Stream was formed in preparation for retail competition being introduced in Scotland in 2008


2008
 HM The Queen opened our £120m Milngavie Water Treatment Works near Glasgow - which replaced a 150-year-old system

2011
 Deerdykes anaerobic digestion facility in Cumbernauld opened - then the largest operational facility of its kind in Scotland


2012
 Glencorse Water Treatment Works started delivering drinking water supply for around 500,000 customers - the facility receives a third of its power from an on-site hydro turbine blended into the Pentland Hills by Scotland's largest 'grass' roof

2013
 The Bridge office in Stepps, near Glasgow opened - it was built to harness 3 different types of energy technology

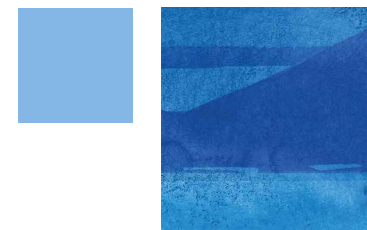
2015
 Named Best Large Employer in Scotland by Business Insider - and first support group representing LGBT employees is formed a year ahead of the establishment of our Belong network

2017
 Learn to Swim programme to teach more youngsters this life-saving skill began

2018
 Our first Top Up Tap started flowing outside the Scottish Parliament and Scotland's biggest sewer superstructure - Shieldhall Tunnel in Glasgow became operational

2020
 Launched our Routemap to achieving Net Zero emissions by 2040 and launched our Strategic Plan

2021
 Institute of Customer Service report names us in the top ten organisations in the UK for Customer Satisfaction





CHAIR'S STATEMENT

DAME SUSAN RICE



2022 is a milestone year for Scottish Water as we celebrate our 20th anniversary. The merger of three regional water authorities into one national organisation created big headlines 20 years ago. The amount and range of work done in the last two decades is remarkable. Providing customers with vital water and waste water services round-the-clock takes meticulous planning, investment, and maintenance - as well as extraordinary dedication, teamwork, and leadership.

Scottish Water has delivered all that. It's an organisation Scotland can be proud of and indeed one that stands proud among some of the best water companies in the world. Where we are today is testament to the work of many people over many years. Looking ahead, with new and emerging challenges, we will do all we can to continue to serve our customers at the highest possible level.

Looking back more recently for this latest report, we can all say that the last year was extraordinary. Against a backdrop of extreme weather caused by intensifying climate change, we faced into an unsettled economy with steep cost rises and the impacts of the Covid pandemic and the devastating ongoing conflict in Ukraine.

Like most organisations, Scottish Water has had to respond and adapt with speed and agility.

We saw increased flooding in some areas, alongside low reservoir levels in others, and significant customer interruptions in storm-hit rural areas. There was pressure on the cost of construction materials and, at times, on the availability of some essential items. Our priority, as always, has been to keep vital water and waste water services flowing across Scotland and many of those who we serve have praised our work under the challenging circumstances.

Water quality remains very high - at 99.93% - and despite having to deal with various weather-related issues our frontline teams are doing a first-class job dealing with new and historical issues and supporting customers. In addition, we continued to try out new ways to engage with customers, often at an earlier stage, to listen to their views on the service they want, so that we help Scotland flourish for future generations.

A focus on water quality and security of supply has increased as people gain a greater understanding of environment and climate issues. How well we meet our societal responsibilities has been under more scrutiny than ever from our stakeholders. Indeed, organisations across the water industry and beyond are actively having to tap into the public consciousness. We are all testing the extent to which our purpose and priorities benefit both the planet and its people now and for the future.

COP26 in Glasgow in November delivered bold intentions with urgency - we all must match rhetoric and ambition with actions. Initiating effective change and having real impact depends not just on goals but on the way organisations and their people work. Their success derives from the culture of an organisation. Now starting my eighth and final year as Chair, I can attest to how Scottish Water strives every day to do the right thing for customers and for our planet.

Our plan for transformation will help us achieve our ambitious sustainability goals. It will also enable us to develop potentially world-leading technologies to change the way water and waste water networks operate. We will continue to engage with our contractors, supply chain and industry partners to find solutions to predict network issues and resolve them more quickly. We will also reduce our emissions, embracing the circular economy and enhancing the natural environment.

Despite the enormous challenges we face and maybe because of them, the water sector is alive with innovations which offer a host of solutions and value. These are facilitated by artificial intelligence, greener materials, resource recovery and breakthrough scientific testing.



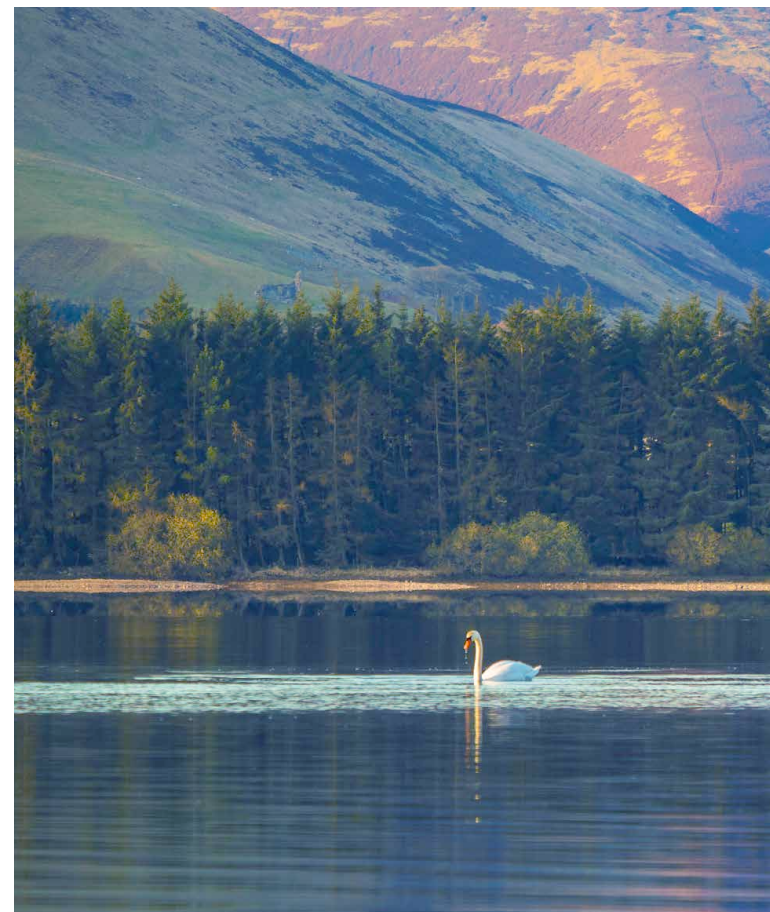
Looking ahead we will work closely with water sector stakeholders to assess the responses needed to meet the obligations of the new EU recast Drinking Water Directive, the first to be transposed post-Brexit as part of Scotland's commitment to keep pace with EU law. The directive aims to ensure access to safe drinking water for all, including those on a private supply. It will also impact how customers are informed about water charges, the quality of their drinking water and provide information about the need to make more efficient water choices.

Business Stream, one of our subsidiaries, supplies water and waste water services to customers in the competitive non-domestic market, has also had a highly successful year despite the challenges of the last 12 months. Looking ahead, Business Stream will remain focused on its transformation programme. It will also continue to build on its vision to make a positive difference to its customers, its people, the environment and local communities.

I'm proud of the way the Scottish Water Board led and guided our organisation through a challenging year. The investment mobilised during the first year of a new regulatory undertaking is never easy. The Board's stewardship has seen Scottish Water excel in many ways, each of which will deliver tangible benefits to our customers and to the country.

I would like to record my ongoing gratitude to Douglas Millican, who has announced he will step down as Chief Executive after ten years in the role. There will be more opportunities to mark Douglas' contribution to the success of Scottish Water over the coming months. In the meantime, his continued leadership through a period of transition to a new Chief Executive will be vital.

I am delighted to welcome two new Non-executives, Catriona Schmolke who joined our Board in November 2021 and Graham Dalton in April 2022. Each brings a background which complements the strengths and experience of the ongoing members. I also take this opportunity to thank outgoing Board member Jim Coyle, who steps down after five and a half years on our Board and four years as Chair of the Audit Committee and whose hard work has contributed to our success.





CHIEF EXECUTIVE'S REPORT

DOUGLAS MILLICAN

2021/22 has been challenging, with extreme weather impacting our ability to provide the continuous water and waste water services our customers rely on.

We saw the tail end of a very cold winter, which caused an increase in burst pipes and leakage, before moving into a very dry spring and summer. This led to pressures on water supply and the quality of water at customers' taps in some areas.

The dry summer was interrupted by very heavy rainstorms that deluged drainage systems and impacted local waste water networks. This resulted in an increase in sewer flooding of some customers' properties and spills to the environment. Storm Arwen struck in November with 100 mile-per-hour winds and caused devastation of property and the loss of electricity and communications, which in turn caused problems at our treatment works and interruptions to some customers' water supplies.

Despite these challenges we continued to deliver high quality services to customers and our key performance measures are mostly at or around similar levels to previous years, a remarkable achievement in testing circumstances.

Of course, it would be wrong to portray the weather extremes of the last year as something exceptional. Unfortunately, weather events that we used to classify as one-in-30 or one-in-50 year events are now happening much more frequently. At times of extreme weather, our teams have been working exceptionally hard to cope with the impact of the changing weather while maintaining vital services.

I have written before about the age and condition of our assets and how they were never designed to work in the weather conditions that we are now experiencing. Unfortunately, with each significant storm or extended dry period it is becoming more apparent just how much we need to improve our assets to maintain high quality services to customers in future. If we are to replace our ageing assets and keep pace with the impacts of climate change, higher levels of investment in our water and waste water assets are vital.

Investment

The last year was the first of our new regulatory period in which we aim to increase our investment levels significantly. Often in the first year of a new regulatory investment period, regulated utilities struggle to maintain investment levels as they put new delivery partners in place. So I am delighted that we achieved strong investment performance in the year. Our level of investment increased by £160 million from the previous year and was ahead of plan, enabled by extensive work to transform our approach to investment planning and delivery.

It speaks volumes for the work of everyone involved in our capital investment programme, that this has been possible despite the challenges of weather, Covid and a new investment period.

We plan to increase investment in future years in line with government and regulatory expectations. This will support our work to maintain and enhance water and waste water services to customers, protect the environment, enable new housing and economic growth. Increasing investment also means that we can support more jobs across our supply chain, including an expected 1,000 new graduate and apprenticeship places over the next six years.

Covid

While Covid has been an ever-present threat over the past year, we navigated it without any notable impact on service to customers.

My thanks go to all our people for adapting their ways of working to deal with the challenging circumstances, but particularly to our operational teams, who worked through many difficulties to ensure this happened.

I expect there will be more issues we will have to consider as we continue the transition to living with Covid without major restrictions. One such issue will be how we most effectively work together as an organisation after two years when office-based staff have largely worked from home. We are currently trialling new hybrid office spaces, designed for more collaboration, and will continue to consider how to achieve the best possible working arrangements to support an inclusive environment while also ensuring the efficient use of our offices.



Transformation

The future of our organisation and how we will deliver water and waste water services in the face of all the challenges and opportunities before us is the focus of our transformation programme. We must transform to continue to realise the potential for improved efficiency and performance and make the smart investment decisions that will enable us to play our part in fulfilling Scotland's water sector Vision.

Last year we reported how we were planning the transformation across all parts of Scottish Water. This year our transformation programme is moving ahead, with initiatives taking shape and starting to deliver benefits in service delivery, efficiency, and customer experience.

One such initiative is project SWIFT (Scottish Water Intelligent Field Transformation) which is transforming the planning and scheduling of work when a customer contacts us with a waste water issue. Remote diagnosis is one of the projects under SWIFT, which has triaged over 3,700 cases and prevented one-third of these being site visits by resolving customer queries remotely, enabling much faster resolutions for our customers.

Across the transformation portfolio there are dozens of initiatives like SWIFT, looking to change how we do things to make us more efficient and deliver greater value for customers and communities. These must deliver sizeable benefits to achieve the ambitions set out in our strategic plan for 2021-27: Our Future Together, while maintaining services to customers.

Net Zero

The greatest long-term challenge of our time is climate change. A key area of our transformation programme is our ambitious plan to reach Net Zero carbon emissions by 2040, five years ahead of the Scottish Government's target for Scotland. We have continued to make steady progress in some areas of our plan, including a further reduction in the energy we use and an increase in the renewable energy we generate from our assets.

We have developed strong supply chain engagement as we seek to build the partnerships that will help drive down emissions in our capital programme. We have created a separate Expert Panel dedicated to construction which involves senior leaders in Scottish Water and from our supply chain and this has driven a focus on low emission action across supply chain partners and experts in the Scottish construction industry. I am delighted that Net Zero emissions in our capital programme is breaking new ground for our sector. Our focus has been on three areas - low carbon design, low carbon materials, and low carbon construction techniques.

When we launched our Net Zero Emissions Routemap in September 2020 we recognised that such a long-term plan would inevitably require adjustments as we learn more each year and continue to develop our thinking and understanding. Often factors outside our control require us to adapt, such as the increase in demand and cost of land for tree planting. We are reviewing the potential of our own significant land-holdings for tree planting and peatland restoration as a result of this development. We have also faced supply chain issues relating to sourcing ethically produced parts for photovoltaic panels.



Water and waste water

The quality of the water we have continued to supply to customers across Scotland has remained consistently high, with drinking water quality broadly in line with last year at 99.93%. However, water quality test results at customers' taps are difficult to compare with previous years because of changes to how we carried out sampling during Covid restrictions.

While overall water quality was good, the most significant issue in the last year was the levels of manganese in tap water in areas where the extremely dry weather caused our reservoir storage to fall to previously unknown levels. Discolouration, particularly in areas of Lanarkshire, led to significant contacts from customers and stakeholders. The issue abated as reservoir levels started to return to normal. We have reviewed the incident and identified the steps we can take, including strengthening our risk assessment of raw water quality and further investment in assets, to protect supplies in future.

The manganese problem illustrates that we are likely to face more issues in future which we have not experienced in the past, due to changing weather patterns. While we will work hard to assess these risks and plan for them, it will not always be possible to prevent issues impacting the service we provide to customers.

This was the case in late 2021 when Storm Arwen caused more extensive power outages than we had ever previously experienced. Although significant back-up electricity generation was deployed, the unprecedented nature of those outages is causing us to reassess the scale of back-up generation that may be needed to maintain services during future extreme storms.

Our overall environmental performance continued to be good. Throughout the year 96% of waste water treatment works complied with their environmental licence conditions. During the year, we had 10 of the more serious category one and two Environmental Pollution Incidents (EPIs), which was 5 greater than in the previous year.

Many EPIs are caused by blockages in the sewer network when combined sewer overflows (CSOs), which are essential safety valves in the waste water network, spill waste water into burns and rivers.

Awareness of overflows and their operation has grown in the last two years among customers and stakeholders. This is partly due to people spending more time outdoors locally during pandemic restrictions. The issue has received significant media and regulatory attention across the UK.

The issue is not new to us, and we have invested significantly in our waste water networks, including CSOs, in recent years. However, we recognise the need to do more. In December we published our **Improving Urban Waters Routemap**, setting out plans to invest around £500 million in the waste water system from treatment works to CSOs, to improve the quality of waste water discharges, enhancing the health of rivers and coastal areas.

We continue to work with partners to introduce sustainable infrastructure which helps remove surface water from sewers. Our Nature Calls campaign was launched to help reduce the number of wipes flushed into sewers. It urges customers to bin wipes and calls for a ban on wipes containing plastic.





Customers and communities

The experience of our customers and communities of the services we provide, which we measure with a group of Customer Experience Measure (CEM) scores, has been broadly similar to last year despite the difficult year we have had dealing with extreme weather. This is a significant achievement in the circumstances and is due to robust planning and the hard work of our employees, particularly those in frontline service delivery roles. We have also been improving how we work with vulnerable customers by tailoring our service to better meet their needs.

Our field force of more than 1,500 people, who we rely on to operate our assets, deliver our services and respond to problems every day, is the backbone of our organisation. We are exceptionally fortunate to have a workforce that is committed to delivering for our customers, come rain or shine.

Our work to further strengthen relationships with local communities picked up again in the second half of the year. The easing of some Covid restrictions saw more Top Up Taps being installed at the request of communities, and other initiatives such as our Learn to Swim programme, delivered in partnership with Scottish Swimming, getting back up to speed.

I and many of my colleagues plan to attend community and public events, to meet as many customers as we can and speak to them directly about their experience of Scottish Water, as we did very successfully before restrictions were introduced.



Finance

Our regulated financial performance over the last year has been strong, with revenues recovering as our customers benefited from the easing of constraints associated with the pandemic, coupled with strong cost control. This has enabled us to generate £39 million greater than plan to support further investment. This performance was towards the top end of the range set out in our Delivery Plan for 2021/22 with a regulatory surplus of £336 million after allowing for £215 million of responsive repair and refurbishment costs. This surplus provides the largest element of funding for our capital programme including water quality and environmental improvement projects and replacing or refurbishing ageing assets. The balance of the capital investment programme was financed from new borrowing from the Scottish Government.

The group surplus before tax increased to £91 million (2021:£33 million) reflecting a strong recovery from the Covid-19 pandemic. A £67 million deficit after tax was recorded after recognising a £158 million tax charge that incorporated a deferred tax charge of £150 million which was impacted by the revaluation of the deferred tax balances caused by the increase in the UK's main corporation tax rate from 19% to 25% effective from 1 April 2023.

The closing Scottish Water cash balance of £516 million has been effectively financed through borrowing from the Scottish Government. £200 million of this cash is maintained to manage the financial impact of risks and uncertainties that may arise, and the balance has been committed for future investment delivery. This borrowing has been undertaken at very low interest rates that are fixed for up to 50 years, protecting costs for current and future generations of customers.

Customer charges for 2021/22 increased by 2.5%, an increase of 1.8% over Consumer Price Index (CPI) inflation, with the Scottish Government implementing an increase in support for those who can least afford to pay, meaning that nearly 50% of customers now receive some form of reduction in their water charges. This increase was broadly in line with the expectations and charges' cap set out in the Water Industry Commission for Scotland's (WICS) final determination of charges from 2021 to 2027.

We are conscious that increasing charges to pay for additional investment must take account of the difficult economic circumstances faced by many people and businesses across Scotland and yet recognise too that those conditions may continue to be challenging in the years ahead. When setting charge levels for 2022/23, and following discussions with the Scottish Government, we agreed to limit charge increases to 4.2%, in line with the October 2021 CPI inflation figure, the benchmark month we use for charge-setting.

We recognise the financial pressures on households and businesses are likely to increase for some time and doubt whether it would be feasible to return quickly to the charge level expectations set out in the final determination of charges. However, the financing set out in the final determination will be required across the 2021-27 period to enable us to deliver Ministers Objectives. We are exploring with the Scottish Government the options for securing financing that will be needed beyond that arising from charge levels that may feasibly be set. In the meantime, our healthy cash position, strong income stream, and committed borrowing from the Scottish Government enable us to continue planning, prioritising and delivering capital investment in line with Ministers Objectives for the 2021-27 period.



People

We have a highly committed workforce, a large proportion of whom have worked with us throughout the 20 years of Scottish Water and with our predecessors before. We also benefit from people who have joined us more recently, bringing skills and expertise that are vital to our future success.

We aim to provide a working environment in which all our people can thrive, and much of our transformation is geared to enabling this further. One element of increasing concern is the recruitment and retention of employees in a strong labour market, particularly for certain highly skilled roles that are in demand in other sectors of the economy. We are experiencing an increasing divergence between the rate of pay increase for some roles, particularly in the private sector, relative to the more limited flexibility allowed by Public Sector Pay Policy.

This increasing divergence in pay rates for some roles, coupled with the cost of living crisis, means more employees are looking to leave Scottish Water to earn higher salaries elsewhere. Like any other concerning trend, we are exploring with the Scottish Government the steps we can take to ensure we can attract and retain the skills we need while operating in accordance with the expectations of a responsible public sector employer.

And finally

In January I announced my intention to step down as Chief Executive after ten years in the role and twenty years on our board and executive team. The timing of my announcement will allow my successor to be appointed and take up post ahead of the planning for the next regulatory period. I will continue to lead Scottish Water through this year and secure a smooth transition to my successor.

Although the last year has thrown up many challenges, I would like to thank everyone at Scottish Water and our partners for the way they handled the pressures and contributed to our achievements this year.





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OUR BUSINESS MODEL

Who We Are

Scottish Water is a public sector body, classified as a public corporation of a trading nature, answerable to the Scottish Parliament through Scottish Ministers and therefore without shareholders. This ownership model allows the surplus generated to be reinvested in the provision of services to our customers.

Our core services are covered by the Water Industry (Scotland) Act 2002. Under that, the charges for these services must be approved annually by the Water Industry Commission for Scotland (WICS). In delivering these services effectively, we have to make use of our resources to achieve ministerial objectives at the lowest reasonable overall cost. As the economic regulator for the Scottish water industry, the WICS' mission is to manage an effective regulatory framework that encourages the industry in Scotland to provide a high-quality service and value for money to customers.

The role of the Scottish Government is as policy maker, owner and banker.

OUR PURPOSE AND STRATEGY

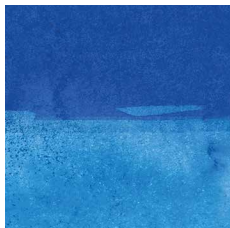
What We Do

Our purpose is to support a flourishing Scotland through being trusted to care for the water on which we all depend. We supply water and waste water services to households and are also the wholesaler to 25 Licensed Providers who operate in the water and waste water retail market for business customers in Scotland.

Using Scotland's natural resources, our assets and the skills of our people, we are committed to improving our services for customers and communities while protecting and enhancing the environment of Scotland.

We launched our strategic plan [Our Future Together in 2020](#).

As well as our new purpose, supporting a flourishing Scotland, our plan highlights the big challenges we will face in providing essential services to homes and businesses across Scotland: the impact of climate change, ageing assets, and reducing the emissions that contribute to the climate crisis.



DELIVERING MINISTERIAL OBJECTIVES IN THE 2021-27 REGULATORY PERIOD

Scottish Ministers set objectives for Scottish Water. Our objectives for the current regulatory period, 2021-2027, are:

Ministerial Objectives 2021-27:

- Take an integrated and collaborative approach to decisions to maximise the impact of resources and to achieve better outcomes for people and communities.
- Maintain or improve current levels of service over the long term, engaging to establish appropriate standards for the 2021-27 period and beyond.
- Prepare a strategy to inform the long-term asset replacement needs ensuring asset maintenance is fully integrated in the investment programme.
- Identify and provide new strategic capacity to meet the demand of all new housing development and domestic requirements of commercial and industrial development.
- Align with the Scottish Government's circular economy strategy and assess the potential for resource recovery from waste water.
- Comply with drinking water quality duties and address failures to ensure compliance with drinking water quality standards, taking steps to improve resilience and remove lead from the network.
- Improve compliance with environmental licences and limit the amount of plastics reaching the water environment through the sewer network.
- Work with stakeholders to transform how rainwater and waste water are managed to improve flooding and surface water management.
- Maintain and improve the security of its network and systems, to protect them from malicious attack.
- Make substantive progress in the 2021-27 period towards the climate change targets.
- Prepare and implement plans to manage its private finance initiative contracts which end in the 2021-27 period.

For the full list of Ministerial Objectives please visit: www.gov.scot/publications/scottish-water-directions-2020/

SERVICE EXCELLENCE

Overview

The last year has been among the most challenging we have ever faced. Over the past year we have continually adapted our ways of working to ensure excellent service delivery. The views of customers shape our delivery and we strive to engage with them to understand how we can improve.

Most customers enjoy uninterrupted services and do not experience any loss of service. When interruptions do happen there can be many reasons, such as weather conditions or asset failure, and we do all we can to minimise disruption working to rigorous targets to restore normal supply. Occasionally, customers are left without water for longer periods. Around 400 were left without water for up to three days after widespread power outages caused by Storm Arwen. We also had a significant issue with heightened levels of manganese in water supplied to customers in Lanarkshire.

A priority during the year was to maintain services to customers during a period of changing restrictions related to the pandemic with access to water and waste water especially important to public health.

CUSTOMERS AND COMMUNITIES

2021/22 Performance

Customer Experience

Our Household Customer Experience Measure (hCEM) for the last year was 86.0 which was broadly similar to the previous year when calculated on a like-for-like basis. This was achieved in many ways, including prompt and effective responses to weather incidents, continued investment to tackle known issues and personalised engagement when customers experience service issues.

Ensuring excellent service for wholesale customers also remained a focus for us. The Non-household Customer Experience Measure (nhCEM) of 87.2 was also broadly similar to the previous year when calculated on a like-for-like basis.

The impact of adverse weather conditions on our services caused a significant rise in customer service contacts. Over the course of the year there were 346,264 service issue contacts received from household customers by our Customer Engagement Centre. This is a rise of almost 40,000 on the previous year.

Outcome Performance Assessment

Evaluating how we deliver water and waste water services is critical to understanding how we are performing. The Outcome Performance Assessment (OPA) is an evolution, for this regulatory period, of the traditional regulatory points-based measure which drives our service to ensure customers receive the best service possible.

Our OPA performance for the last year has been calculated at 398. OPA performance in 2021/22 was 10 points lower than it would have been in 2020/21 if calculated then under the new methodology. When you consider the challenges we have faced in the last 12 months, notably the extreme weather, this is a strong score.



Customers and Communities

We are committed to involving customers in our decisions and strive to build relationships with them and better understand the communities we serve.

One of the areas we focused on last year was improving resilience for vulnerable customers. Some of our customers rely on our services more than others, especially those on our Priority Services Register (PSR) who may have medical conditions, young children or live with a disability.

As part of our ongoing Winter Resilience Strategy, we looked at how we could more proactively support customers in the event of an interruption, to ensure they always had access to fresh, clean water. We completed a pilot in Fife where we supplied bottled water to customers registered on our PSR, to be used in the event of an interruption to their water supply. We contacted 1,800 PSR customers in the area and 20% of them signed up for the service. We are reviewing learnings from the initiative and exploring how it can be rolled out more widely.

The Priority Services Register in Scotland is a free service which provides extra help when there is an interruption to water, gas or electricity supply. People eligible to sign up include people who are deaf, blind or have a chronic illness, mental health issue or disability. Also people aged over 60 and families with children aged under five.

We also continued to strengthen our partnerships with Capability Scotland, The Red Cross and Age Scotland to encourage people to sign up to our PSR if they qualify. We also joined with these charities to promote the importance of staying hydrated. Our partner campaign highlighted how older people have a lower volume of water in their bodies and may experience decreased thirst and how drinking between six to eight glasses of water daily is vital for their health.

Additionally, we set up an ongoing volunteering opportunity for Scottish Water staff in conjunction with Age Scotland where our people volunteer to be trained to make 'good day' telephone calls to older people throughout Scotland to help combat loneliness and isolation. The opportunity was opened to and filled by a number of volunteers and has been so successful it has been expanded to enable more employees to take part.

We received 1407 GEM (Going the Extra Mile) nominations this year - 155 more than in 2020/21. These are nominations from customers about our employees who have provided services to them. These awards provide valuable positive feedback on the way service is delivered, and to see this increase during such a challenging year is exceptional and testament to the dedication of our people.

Wholesale Customers

We are the wholesaler to the 25 Licensed Providers (LPs) who operate in the water retail market for business customers in Scotland. There are currently more than 150,000 business properties with a water or waste water service. We recover more than £330 million per year from LPs who in turn supply the end-customers.

Over the last year we continued to provide a high standard of customer experience to LPs and end-customers, which is reflected in all principal performance measures. In the last year we continued to innovate in wholesale customer service and refreshed the wholesale deferral scheme to provide relief to LPs, strengthened the market financial resilience framework, and introduced a specialist service for resolution of complex wholesale issues. We also established two stakeholder and customer forums to provide essential customer insight into the market.

We are currently working to improve the self-service functionality we offer to LPs to speed up interactions and drive service improvements and efficiencies.



Customer and Community Involvement

A newly-introduced measure - stakeholder and Communities Experience Measure (sCEM) - tracks performance in stakeholder and community relations and is reported for the first time. During 2021/22 it was recorded as 76.7, which was below target. There was a significant rise in the number of stakeholder contacts to 1,541 from 1,113 the year before. We also experienced our highest recorded monthly stakeholder contacts with 229 received in August 2021 following very heavy rainfall and a water quality incident.

Ongoing restrictions resulting from the pandemic meant we expanded our use of virtual platforms to engage effectively with customers and gain valuable insight. We also plan to restart face-to-face events this year.

The use of digital communication tools allowed us to host our Annual Consultative Meeting (ACM) online, for just the second time, and it received more than 800 views online. We received a number of questions about areas including environmental pollution from our waste water assets and how we work with developers to support home building.

Many of the contacts throughout the year related to sewer flooding and resulted from members of the public contacting their elected representatives. Our sCEM score was also impacted by the Scottish Parliament election, with around a third of seats being taken up by new MSPs, with no previous relationship with us. We are planning a programme of engagement with MSPs to raise awareness of Scottish Water.



Developer CEM

We have made a number of changes over the last 12 months impacting the development community, such as the delivery of network reinforcements to support new development, and have managed to maintain a high level of satisfaction. The number of network reinforcements required has started to increase as this change has been implemented. We continue to review our approach to determine what measures can be taken to further improve the service offered to the development community.

Customer Engagement in Decision-Making

Across Scotland, we are carrying out an increasing number of projects where we are gathering, collating and using customer insights to influence our investment decision-making. This new approach is not just about considering how a project is delivered but considering the fundamental question of what is delivered.

While customer and community engagement has always been a priority this new approach aims to produce better outcomes for communities and Scottish Water by representing community views earlier in the decision-making process. We are looking at new ways to engage with communities well in advance of projects starting and often before they are designed. We want people to be fully informed of what is planned or needed and know their preferences, views and needs.

CASE STUDY

COMMUNITY PARTNERSHIP GETS GOING AT GLADHOUSE

There has been an increase in visitors to Gladhouse Reservoir in Midlothian, which provides drinking water to thousands of customers. It has become a very popular spot for picnics, walking, cycling, water sports and wild camping. Alongside this there has been a rise in anti-social behaviour including littering, toileting, fire damage, noise pollution and vandalism which impacts local residents, wildlife and habitat.

A stakeholder group led by Scottish Water was formed with community representatives - local landowners, residents, Police Scotland, farmers, Midlothian Council, Scottish Fire & Rescue and NatureScot - which now meets regularly to discuss ways to tackle these issues.

More than 1000 people took part in an online survey asking for views on issues and solutions.

Short and medium-term activities at the site are being trialled to improve car parking, visitor behaviour and protect wildlife. Work is taking place with Midlothian Council to provide a Ranger-style presence to support responsible behaviour and visitor engagement.



CASE STUDY

ROUGHRIGG RESERVOIR STAYS AFTER CUSTOMERS HAVE THEIR SAY

A public consultation helped us to decide to retain Roughrigg Reservoir in North Lanarkshire. Although it's no longer part of the supply network, it needs a significant amount of work to ensure it meets safety requirements in the future.

We asked the local community for their views on its future. The vast majority described the positive impact it has on their lives, mental health and wellbeing. Taking this into account, options were reviewed and we concluded that keeping the reservoir offered many community benefits. Local community groups and stakeholders said they were grateful they were consulted and had their views heard.

We will instead now use siphons to protect downstream properties and will look to identify potential improvements to encourage more visitors to enjoy and use the scenic beauty spot.

CASE STUDY

COMMUNITY PARTNERSHIP PAVES WAY TO TACKLE FLOODING

Tillicoultry in Clackmannanshire has a long history of flooding due to its location at the southern base of the Ochil Hills.

The local community established a flooding group, Tillicoultry, Devonside and Coalsnaughton Flood Group (Tideco). The group contacted us and Clackmannanshire Council in autumn 2021 looking for us to work together to help alleviate areas of flooding.

A partnership was formed to deliver a local campaign focused on keeping unflushable items, such as wipes, nappies and period products out of the sewer system to avoid blockages.

In October the first partnership workshop took place with Clackmannanshire Council, Tideco and community members to gather local knowledge and identify key issues of impact. A plan of action is now under development focused on engagement within the local community including schools, businesses, events and media.

This approach encourages community ownership, involvement and action at the same time as delivering long-term environmental benefits.



Your Water Your Life & Top Up Taps

There are now more than 70 Top Up Taps across Scotland, where people can use refillable bottles to stay hydrated on the move, save money and help reduce single-use plastic. Use of the taps has helped to prevent the equivalent of over 1 million single-use plastic bottles.

Locations have been chosen through collaboration and partnership with communities, interest groups and other organisations. Partner organisations who have supported Top Up Taps include Historic Scotland, Loch Lomond and The Trossachs National Park, Police Scotland, NHS Lothian and Glasgow Science Centre.

The continued roll-out will see Top Up Taps installed at more than 120 sites. An online portal has allowed communities to suggest potential future locations. Since the launch of Your Water Your Life in 2018 there have been more than 1000 suggestions received to date.

There has been a steady rise in awareness of Top Up Taps and an increase in the number of people using them, the biggest of which is in the age group 18-24 years. Analysis, from independent YouGov research, for the Your Water Your Life campaign showed that of those people who used a Top Up Tap, 77% felt more positively about Scottish Water.



Learn to Swim

The successful partnership with Scottish Swimming to encourage children to be safe and confident in and around water has been extended for another three years, until March 2025.

The framework, which has Olympic gold medallist Duncan Scott and Paralympic medallist Toni Shaw as its Ambassadors, is being delivered across Scotland by 36 Leisure Trusts in more than 160 pools.

The extended partnership will see the implementation of the Scottish Water School Swimming Framework, an initiative to provide thousands of primary school pupils with the opportunity to learn to swim. This will help to ensure more children from areas of social deprivation learn to swim, a new objective for the programme.

More than 106,000 children from across Scotland - from Shetland to the Borders - got involved during the first four years of the programme.

The programme aims to reach another 100,000 children by 2025, plus 30,000 young people from areas of deprivation.



Learning and Education

Engaging with pupils and students is underlined through a strategic ambition to engage directly with every school pupil at least once during their academic journey. Our education programme reaches thousands of pupils, and we are developing different approaches to making that even more effective. Partnerships with organisations like Wild Planet Explorers, Glasgow Science Centre and Edinburgh Science Festival enable us to educate pupils about the water cycle, the environment, and the impact of climate change.

Online resources and outreach activities form the cornerstone of our approach. Building on our online primary and secondary education hubs we are developing a new digital tool to help pupils understand STEM-related career opportunities both within Scottish Water and the wider water industry. We are also developing an online interactive heat map which will demonstrate where we have successfully engaged with schools and where more outreach may be required.

Enabling Responsible Access

Our Strategic Plan highlighted our commitment to connecting customers and communities to the natural environment by enabling access to our reservoirs. In April 2021, we began a pilot project to explore how visitor experience could be improved at three locations - Carron Valley and North Third reservoirs in Stirlingshire,

Craigmaddie and Mugdock reservoirs in Milngavie, East Dunbartonshire and Gladhouse reservoir in Midlothian.

The focus in 2021/22 was to listen to customers and communities who use the sites to better understand behaviours and perceptions. Based on this feedback a range of trial improvements at pilot locations will be delivered over the coming year. These include constructing visitor car parking and establishing ranger services to help maintain sites, engage with visitors, and promote responsible access.

There was a steady increase in the number of people who visited reservoirs during the past year. Public messaging was developed, in line with national campaigns, to raise awareness and understanding of responsible behaviour and encourage responsible behaviour in accordance with the Scottish Outdoor Access Code.

Community Empowerment Act

The impact of the pandemic on the ability of community groups to organise and progress transfer meant no asset transfers were completed in the last year under the Community Empowerment (Scotland) Act 2015. The act helps to empower community bodies through the ownership or control of land and buildings. A small number of requests are currently pending. Support continued for groups enquiring about assets for potential transfer and it is anticipated there will be more substantive activity in the year ahead.

Complaints and Feedback

We had 614 written complaints last year, one more than the previous year. We take complaints seriously and resolution is a priority for us. The biggest rise in complaints was related to infrastructure (up 34% on the previous year from 67 to 90) and biggest decrease was in water quality (down by 53% on the previous year from 30 to 14). There were no upheld regulatory complaints from the Scottish Public Services Ombudsman or Drinking Water Quality Regulator (DWQR) in 2021/22.

Freedom of Information

There were 914 Freedom of Information (FOI) requests in 2021/22, an increase of 19% on the previous year. They spanned a range of subjects including environmental impact, operational issues, and financial aspects of our work. One appeal was received after a request was declined on security grounds.

The Independent Customer Group Chair's Statement

The Independent Customer Group (ICG) was established by Scottish Water at the end of March 2021 as a model for bringing a customer and community perspective directly into the strategic decision-making of the organisation. Its role is to support and challenge Scottish Water as it goes through the transformation process: to be a critical friend, a sense check, a sounding board and a stimulus for new ideas or more stretching approaches. The Group is operationally independent with a direct line of accountability to the Chair of the Scottish Water Board. It has 10 members from a wide range of backgrounds including energy, SME, community engagement, place making, regulation, local government/politics; environment and voluntary sectors.

In its first year the Group has discussed and provided views on a wide range of issues including consultation with communities on investment projects, the development of a "benefits framework", the customer code, sewer flooding, the wholesale market, performance measurement, and strategies for customer engagement and partnership working. It has also re-established the Customer Research Co-ordination Group.

Evidence from research into customers' views on water affordability, commissioned by Scottish Water with input from the ICG, underpinned the submission of the Group's

considered view on Scottish Water's pricing proposals for 2022-23. While the final outcome was in line with that view, a key lesson is the need for ongoing dialogue as proposals go through the various phases of decision-making.

Common challenges from the ICG have been the need for SW: to stand in customers' shoes and see issues in all areas of activity from the customer rather than the provider perspective; to use language and concepts that customers will understand; to see customer and community centricity as the common thread running through all parts of the organisation and to resist the creation of new silos.

The ICG understands the scope and scale of the challenges facing Scottish Water both in its delivery of essential services under the continuing fallout from the pandemic, ageing infrastructure, and the impact of climate change while at the same time pursuing the ambitious transformation agenda. The Group has been hugely impressed by the energy behind and commitment to putting customers and communities at the heart of what they do.

Agnes Robson
Chair



Prospects

Scottish Water is on a journey to become a transformed organisation and our ambition is to deepen our customer and community focus as we invest strategically for Scotland. We are already largely trusted by the people of Scotland who turn on taps and flush their toilets without a second thought. However, the nature of trust between organisations and customers is changing. It is no longer enough to just resolve customers' issues when they arise, we must be present in the everyday lives of our customers, sharing the expertise of our teams and looking to find new ways to deliver value.

Looking ahead we will work more closely across our organisation, with our partners, stakeholders, customers and communities. We will use our strengths to continuously support our customers, creating a tangible, positive impact on their lives.

Several initiatives are being developed to create the capabilities to deliver the changes needed for customers and communities.

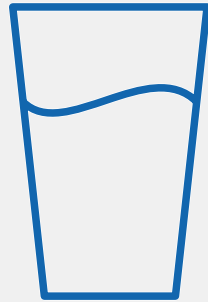
Our approach will be centred on making decisions as if the customer is in the room with us. This will be supported by enhanced customer insights and will help us deliver a new approach to national engagement.

DELIVERING CONSISTENTLY EXCELLENT WATER SUPPLY

Overview

The water we supply to our customers must meet independently monitored standards. Water at treatment works and customers' taps is tested on average once every two minutes to ensure it meets regulatory parameters and our customers' expectations and needs.

2021/22 Performance



99.93%

TOTAL WATER QUALITY
COMPLIANCE OUT OF
296,659 TESTED

SERVICE RESERVOIR SAMPLE FAILS

54
44



There were 44 coliform sample fails at service reservoirs, 10 fewer than in 2020.

WATER TREATMENT WORKS SAMPLE FAILS

24
24



There were 24 sample fails at water treatment works, the same as last year.

CRYPTOSPORIDIUM DETECTIONS

6
10



There were 10 cryptosporidium detections not mitigated by UV treatment, 4 higher than in 2020.

ANNUAL LEAKAGE

463
459



There was an annual average leakage level of 459 ML/D, a continued reduction from 463 ML/D in 2020/21.

■ 2020/21 figure ■ 2021/22 figure

Water Supply and Weather

Weather conditions during the past 12 months presented a series of challenges to our service and ability to maintain supply to customers. Storms Arwen, Corrie and Malik impacted our services whilst severe winter conditions and sustained dry weather over spring and summer also presented challenges.

CASE STUDY

STORM ARWEN - NOVEMBER 2021

Storm Arwen was “one of the most powerful and damaging winter storms of the last decade”, the Met Office said, with widespread impacts in the North East, Dumfries and Galloway and the Borders. Its impact on our infrastructure was significant due to the loss of normal power supply to many sites as well as challenging conditions which caused delays and difficulty accessing areas.

In advance of the storm we put 58 of our water treatment works - which served 1.5 million customers - onto emergency electricity generation. During the storm we deployed another 30 mobile generators to water pumping stations to pump water from tanks in our distribution network to customers. We operated a fleet of road tankers to sustain water supplies and support faster recovery of affected water networks.

Around 17,000 customers were impacted, mostly with interruptions to their water supply. Within 24 hours this had reduced to 5,000 and on the second day to less than 500, with all customers back in supply within 72 hours.

We received 1,800 calls to our call centre over the four days following the storm. We delivered more than 120,000 litres of water to communities that were out of supply for a significant length of time and hand delivered bottled water directly to 500 more remote properties.

We offered compensation to customers whose supplies were interrupted for more than 24 hours and used employees and volunteers to engage and inform customers impacted by the incident.



88 Generators



120 Pallets of bottled water (127,000 litres)



500 door to door deliveries



100 operational staff and 140 volunteers



Over 1000 welfare calls to customers



Welfare checks throughout Aberdeenshire



26 tankers deployed



25 community drop offs and 26 welfare hub deliveries

These challenges meant our services had to rapidly adapt and some of our aging infrastructure struggled to cope with the new demands



Interruptions to Supply

There were 9,504 unplanned interruptions to supply in 2021/22 - compared with 6,091 in 2020/21 - and we have determined that around 4,000 of these were due to the significant storms. When this is taken into consideration the level of unplanned interruptions was broadly in line with previous years. To reduce interruptions, we are continuing to make the network more resilient and looking ahead this will include water pipe replacement in more rural areas where many of last year's interruptions occurred.

CASE STUDY

DISCOLOURED WATER FROM LOW LEVEL RESERVOIRS IN LANARKSHIRE

The west of Scotland had its driest six-month period in 160 years leading to low water levels in our Daer and Camps reservoirs. This resulted in naturally occurring manganese entering the water supply causing discoloured water to customers in Lanarkshire. The incident led to more than 11,800 contacts from customers across a number of channels.

At Camps we brought back into operation a manganese removal process last used around 20 years ago and at Daer installed temporary treatment in the reservoir and at the water treatment works, successfully reducing manganese levels and returning service to normal. During the event we carried out extensive sampling and testing programmes working alongside DWQR and public health officials.

We have now developed improved manganese risk assessments and monitoring plans for all sources and are making permanent the temporary measures installed at Daer, whilst we consider the long-term options for the system.



Drinking Water Quality

The quality of water we supplied to customers during 2021 remained high. Sampling at customers' taps resumed in early summer 2021 but was paused again at the end of the year due to further restrictions. Although this impacted on our ability to test at customers' taps, we still completed the equivalent number of tests by using service reservoirs, volunteer properties and commercial premises to ensure the protection of public health. Tests taken during 2021 showed a compliance rate of 99.93%, which is consistent with previous years.

The annual report published by the DWQR on our 2020 performance commended our work in planning, delivering, and maintaining water services during the pandemic, calling it "exemplary".

In 2021, the DWQR declared a major incident due to the discolouration of water supplies from Daer reservoir. The discolouration was caused by low water levels and high levels of manganese which could not be effectively treated by our works. A review of the event has taken place to ensure any similar incidents are effectively managed.

CASE STUDY HIGH TECH FIRST AT NEW PEEBLES SITE

An innovative water treatment facility is being built in Peebles to replace the current works built in the 1970s. It will provide clear, fresh, high quality drinking water to customers in the Borders town for generations to come.

The £25 million site will be the first in Scotland to use a new high-quality treatment process, where we pass raw water through membranes which filter out larger organic compounds while allowing clean water molecules to pass through fine pores. This water is then treated further to ensure it meets customers' expectations and is safe to drink from the tap.

The new ceramic membrane treatment to be used at Peebles provides an improved and higher quality water treatment. The equipment is also much smaller in size and more energy efficient.

The new works has been designed to have as little visual and environmental impact as possible and includes renewable energy generation at the site.

CASE STUDY PEATLAND RESTORATION PROJECT ON LEWIS

We have been working with communities on the Isle of Lewis to restore 6 hectares of eroding, damaged peatlands and ensure they continue to act as vital carbon storage.

The peatland restoration scheme at Loch Fasgro will also help protect drinking water sources and biodiversity.

The projects have returned areas of blanket bog to more natural conditions, stopping the erosion of peat, regulating the flow of water and raising the water table, the level of water underground, and encouraging peat-forming vegetation to thrive.

When peat dries out and cracks, the carbon it had been storing since its formation is released into the atmosphere as greenhouse gases. Repairing the damage to exposed peatlands and blocking drainage ditches to raise the water table at the sites allows natural peat forming vegetation to flourish and create the foundations for new peat to form.

CASE STUDY

INVESTMENT TO HELP SECURE WATER WORKS FROM STORMS

A £15 million project is in progress which will help to ensure Turriff Water Treatment Works continues to serve 80,000 customers in the North-East.

The work will ensure the site can continue to provide communities with a reliable supply of clear, fresh drinking water for many years to come. It will also enhance the site's resilience to power cuts, reducing the risk of disruption.

Some of the key equipment at Turriff was nearing the end of its operational life and the current project brings significant modernisation, including a new Motor Control Centre and standby generator. The 10 Rapid Gravity Filters which form the main part of the water treatment process will all be refurbished and upgraded, with work due to complete by summer 2023.

Leakage

Year-on-year leakage reduction performance came under pressure during 2021/22 due to extreme weather conditions. We have worked extremely hard all year to bring down leakage with measures including advanced technology to predict where and when leakage may occur. We have managed to slightly reduce leakage levels, which fell from 463 ML/D in 2020/21 to 459 ML/D in this last year. This is a remarkable achievement in the context of the challenges of the year.

We are committed to reducing leakage across the network. Innovation and digital technology will help us improve monitoring, detection and repairs.

Prospects

The European Union adopted a new Drinking Water Directive (rDWD) which came into force in January 2021 with a two-year timeframe to apply this to the water sector in Scotland. Key features include reinforced water quality standards which are more stringent than World Health Organisation recommendations, better access to water, measures to promote tap water, including in public spaces and restaurants, to reduce plastic bottle use and measures to reduce water leakage.



Scottish Water will continue to ensure drinking water quality standards are met and this will remain a priority for us. We will also be looking at ways to address concerns about access to water, the emergence of new substances (such as microplastics), greater information about the quality and cost of drinking water and ongoing work to highlight how water is a precious resource and tips on being more water efficient.

We aim to deliver a consistently excellent water supply. To support this we are developing a water supply risk management system which will include asset capability assessments. During 2022/23, we will populate and begin to use a new risk assessment platform that we have developed to replace our ageing Drinking Water Safety Plan system. These, and other tools, are being used to identify the requirement for risk controls and associated investment needs to improve water quality.

In Inverness, we have combined a number of pilot projects to create a Smart City concept. This comprises 2,600 smart meters on non-domestic properties and hundreds of pressure sensors in the water network to help target leakage and reduce bursts through a better controlled and calmer network. Over the next 12 months we will monitor the success of these pilots and use the experience and learning to scale up into other areas across Scotland.

In terms of addressing leakage, we have recently reviewed and updated the key data components of the water balance calculation to ensure water consumption levels are accurately accounted for within our leakage reporting calculations. This in turn ensures leakage estimates are confirmed as robust and can be targeted efficiently by operational leakage teams. We have also developed a new leakage monitoring and reporting tool, Flow Sense. It went live in April 2022 and replaced the previous system with a modern, secure app. This has reduced the data input times and provides full transparency over data processing and calculations, improving the data integrity and quality.

Our £6.9 million investment project at Loch Thom Reservoir in Inverclyde scooped the award for innovation at the prestigious Scottish Civil Engineering Awards.

It recognises ground-breaking improvements, materials, ways of working, and the substantial upgrades are helping to safeguard the future of the reservoir against the impact of climate change.

CASE STUDY

BURST LEFT 2,000 GLASGOW CUSTOMERS WITHOUT WATER

Around 2,000 customers had no water supply for several hours after a burst in the Shawlands area of Glasgow in December.

The burst on an 18-inch trunk main, which was reported early in the morning, also led to localised flooding.

Our teams worked round the clock to locate, isolate and repair the burst and we kept customers and stakeholders updated with messages. We re-routed supply through an unaffected part of the network to restore supply as quickly as possible before carrying out the repair.

A local primary school and nursery closed for part of the day as a result of the incident.

Some customers were also temporarily impacted by low water pressure and discoloured water, a result of natural sediment in the main being disturbed.

TRANSFORMING WASTE WATER SERVICES

Overview

Dealing with Scotland's waste water is energy intensive and increasingly affected by climate change.

We need to invest more to keep our assets running effectively, meet our Net Zero ambition and ensure there is enough capacity to enable economic growth. It is a vital part of our service which supports daily life and protects public health and the environment.

2021/22 Performance

INTERNAL SEWER FLOODING

599
407



A total of 407 properties were affected by internal sewer flooding. Properties affected has decreased from 599 in 2020/21.

ENVIRONMENTAL POLLUTION INCIDENTS

203
282



We reported 282 EPIs, an increase of 79 from 2020/21.

SEWER BLOCKAGES

35,975
35,822



We recorded 35,822 sewer blockages, around the same as 2020/21.

COMPLIANCE AT WASTE WATER TREATMENT WORKS

97.49%
96.66%



We reported a 96.66% compliance rate for 2021/22 compared to 97.49% for 2020/21.

ODOUR COMPLAINTS

187
196



We received 196 odour complaints direct to Scottish Water, an increase of nine on the previous year.

BIOSOLIDS

117,000
119,150



We produced over 119,000 tonnes of biosolids in 2021/22, which was 2,150 tonnes more than the previous year.

■ 2020/21 figure ■ 2021/22 figure

Waste Water Collection

Sewer Flooding

Changing weather patterns present complex challenges for our waste water system. Dry weather can mean the system does not flush while wet conditions can overwhelm sewers and lead to flooding. The late summer storms, notably in Central Scotland with parts of Edinburgh worst hit, were among the most severe ever measured by the Met Office, with record rainfall over a short period. This also led to a rise in the number of Environmental Pollution Incidents (EPIs) recorded in the year.

The impact of climate change means this is a growing problem for us. The rise in the number of customer and wider stakeholder contacts we are receiving on this issue highlights this. We are committed to look at new ways to reduce flood risk and are looking at longer-term, sustainable solutions with the main aim to reduce the amount of surface water entering our sewers.

Environmental Pollution

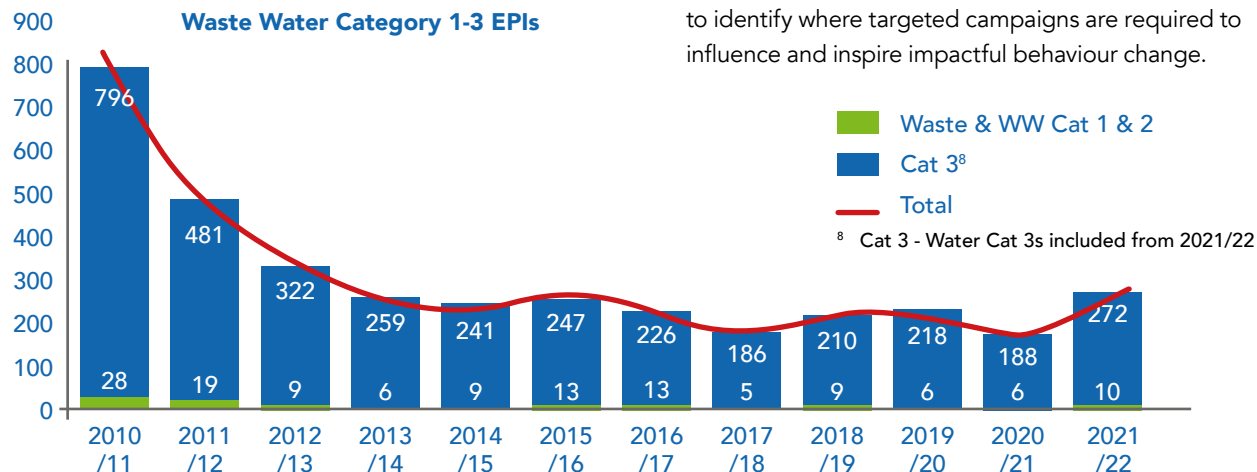
An EPI is an unlicensed discharge from the waste water network into a marine environment such as a river or the sea and all instances are reported to SEPA for investigation.

In 2021/22, we have had a total of 282 EPIs, up 88 from the previous year's figure of 194. Ten of the EPIs were in the more serious Category 1 and 2 incidents - this is five more than in 2020/21 but still a significant reduction compared to a decade ago. The majority of these incidents were associated with waste water networks, sewer blockages and water and waste water maintenance activities. When EPIs occur a full analysis of the root cause is undertaken to determine what, if any, improvement plans are needed.

As we move through the 2021-27 period, our focus will be on reducing the number of incidents which occur on our waste water network through increased intelligence and targeted planned maintenance.

Investment is required in real time network monitoring to help shift our response from being predominantly reactive, relying on SEPA or customers to inform us of issues, to proactive. We piloted network monitoring, trialling the role it could play in predicting blockages and pollution risks. Scaling up this technology would enable us to more readily identify problem areas to take pre-emptive action.

Further investment is also required to promote responsible behaviours and raise awareness of the role the customer plays. Network monitoring will support this work by helping to identify where targeted campaigns are required to influence and inspire impactful behaviour change.



CASE STUDY

FIFE RIVER POLLUTION FINE

Following an incident which led to the pollution of a river in Fife, Scottish Water was fined £6,700 in court. The incident led to the deaths of around 500 trout and salmon in the River Eden. A container of a chemical used during water treatment processes was punctured accidentally and leaked into the watercourse.

The incident, in 2018, was investigated by SEPA and Fife Council and the case was heard at Dundee Sheriff Court.

Actions were taken to improve chemical storage and management on-site and drainage systems were enhanced with additional training provided to employees.

Since 2010 Scottish Water has worked with SEPA to upgrade 104 waste water treatment works and 279 storm overflows - a £686 million investment.

SEPA undertakes comprehensive monitoring to assess the condition of Scotland's water environment. This classification brings together an assessment of water quality, water quantity, fish migration and physical condition.

The most recent classification showed 66% of Scotland's water environment overall is already in good condition. This is higher than the average across Europe and significantly higher than England at 16%, Northern Ireland at 33% and Wales at 40%.



Improving Urban Waters Routemap

Scotland is renowned for the quality of its water environments. Ageing assets and the impact of climate change present risks to this status. Action is needed to address our infrastructure which was not designed to deal with the challenges we now face. The **Improving Urban Waters Routemap** was launched in December 2021 to focus investment and improve the way the system operates and is monitored to protect the environment.

Around £500 million will be invested in Scotland's waste water network - from our treatment works to our Combined Sewer Overflows (CSOs), to protect the country's urban waters for decades to come.

Phase one has identified 108 CSOs across the country as priority for improvement. By 2024 a total of 225 CSOs will be targeted for priority investment.

The work will be carried out as part of a wider River Basin Management Plan (RBMP), developed and delivered collaboratively between us and organisations including the Scottish Government, Scottish councils, environment and community groups. The RBMP sets out a range of priority measures including working with land managers to reduce diffuse pollution from agriculture and supporting the passage of migratory fish. It will also ensure Scotland's rivers, lochs, estuaries, coastal areas and groundwater can continue to supply drinking water, support

commercial interests and be a resource which promotes health and wellbeing.

The work will see us partner with a wide range of organisations to help deliver innovative solutions around surface water removal, reducing impermeable surfaces and pursuing a more sustainable approach to addressing this issue.

Here is our routemap:

www.scottishwater.co.uk/urbanwatersroutemap

Managing Surface Water

Many towns and cities have experienced flash flooding following severe storm events in recent years. Communities have sometimes experienced days or weeks' worth of average rain falling in a matter of hours. The fixed capacity of road drains and the sewer network can be overwhelmed quickly when hit with these short, intense storms, which are likely to happen more frequently.

Most surface water is drained through underground pipes which are out of sight. Building larger pipes is expensive, carbon intensive and means rainwater cannot provide value in other ways.

Cross-sector effort is needed to develop transformational change at scale to manage surface water more sustainably. We are working with partners to jointly plan and deliver so-called 'blue-green' solutions to manage storm water as close to where it lands as possible, to mimic natural drainage, slow down the flow, and where possible stop it entering the sewer network. This brings added environmental benefits as well as reducing flood risk.

CASE STUDY

REGENERATION AT ST MARY'S

We are working with NatureScot, SEPA and Dundee City Council to develop an exciting and innovative project to improve the way storm water is managed and reduce flood risk in the St Mary's area of Dundee.

The area's St Leonard's Park is regularly affected by flooding during more intense rainstorms which can overwhelm drains and sewers.

We are looking to find new ways to reduce flooding by creating natural landscapes to capture rainwater, keeping it out of the sewer network where possible and provide a multi-functional green space for the community. Possible nature-based solutions include ponds, wetland areas and rain gardens.

The first phase of the plan will deliver a conveyance route for surface water to manage flood risk in St Mary's through to St Leonard's Park. It will manage flows in everyday rainfall events and also have storage areas to help slow down water in larger storm events.

We are looking at how the reopening of the historic Back Burn, which was diverted underground over 50 years ago, could restore a natural watercourse. We are also liaising with the community about installing a new pathway, more attractive planting and areas for growing and increasing wildlife.



Every year we deal with around 36,000 blockages at a cost to customers of £7 million. Around 80% of the blockages feature wipes. An average of 25 wet wipes are found on every 100 metres of Scottish beach, according to the Marine Conservation Society. At Cramond Beach, in the west of Edinburgh, around 30,000 wet wipes have been found and removed from the shores by volunteers.

Nature Calls Campaign

In February we launched a major new nationwide campaign urging people in Scotland to bin all wipes and calling for a ban on wipes made of plastic to help protect the environment. The Nature Calls campaign, is designed to help reduce sewer blockages and potential flooding. It was backed by a range of other organisations, including the Marine Conservation Society, Keep Scotland Beautiful and Zero Waste Scotland.

We have highlighted how last year more than 10,000 tonnes of material were removed from Scotland's waste water treatment works. Many thousands of tonnes more ended up blocking sewers, causing flooding, or being flushed into rivers during storms and heavy rain.

Our campaign urges members of the public, communities, campaigners, manufacturers, retailers and governments to work together to do the right thing for nature now and for generations to come.

Since the launch of the campaign some retailers have pledged to stop selling wipes that contain plastic. We have received cross-party support in the Scottish Parliament for a ban on wipes that contain plastic.



Odour

Odour complaints made directly to us slightly increased during the year to 196 compared to 187 the previous year. Complaints at waste water treatment works operated by PFIs totalled 338 compared to 801 last year.

Through our Odour Management Group, we have a cross-functional team regularly reviewing odour performance and opportunities for improvement and have also established links with other UK water companies as a means of sharing best practice. The group is working to reduce odour complaints in a number of ways including looking for trends when there is a report of an issue and working to identify where any investment is needed.

Seafield Waste Water Treatment Works in Edinburgh has an odour investment plan in place. We have been progressing the scope and design of the assets at the site with the aim of alleviating issues that can affect the processing of sludge, as recommended by the Independent Seafield Strategic Odour Review. The improvements will assist in managing sludge throughout the works to reduce the risk of odour.

Recycling Sludge

Scottish Water's and our PFI sludge treatment centres produced over 119,000 tonnes of biosolids in the financial year 2021/22. We aim to dispose of biosolids in a manner that balances cost, greenhouse gas emissions and our circular economy aspirations. 63% of our bioresource was recycled to agricultural land and around 12% used for land reclamation. Less than 1% was sent to landfill where there was no viable alternative. The remainder was transformed into dried pellets and used as a fuel by a third party. We are continuing to work with stakeholders to increase the volume of biosolids that can be used for agriculture.



Bathing Waters

Scotland's bathing water quality was recorded as the best since 2015 when tighter standards first came into effect. Figures for 2021 classified 99% of beaches as 'sufficient' or better for the 2022 season, an increase from 94% the previous season. 32 of the 85 beaches which are classified were rated as 'excellent'. Only one designated beach was classed as poor.

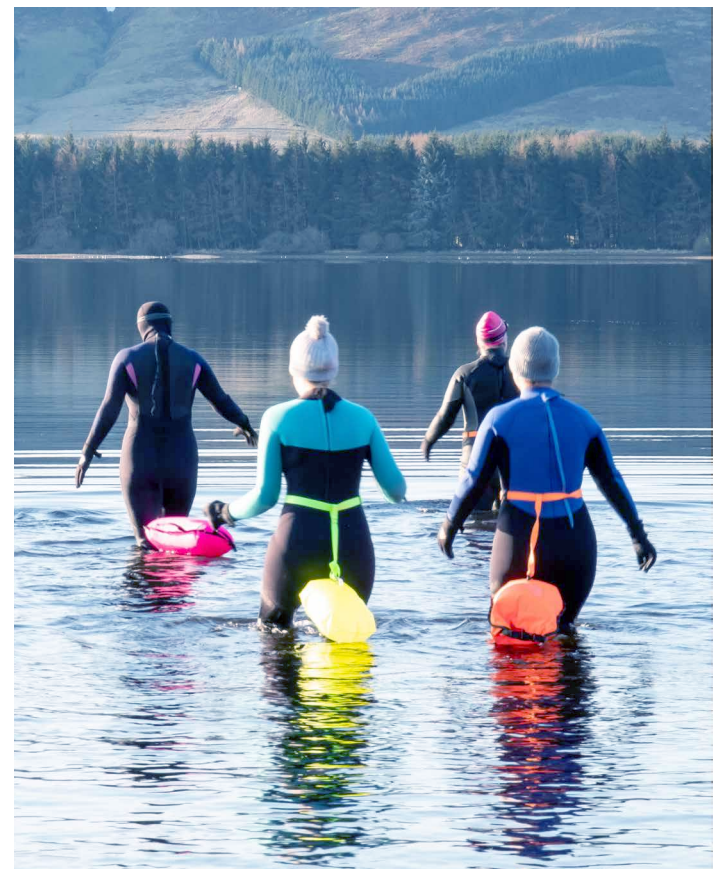
Increased awareness and scrutiny of the performance of the waste water system including Combined Sewer Overflows led to significant public and stakeholder interest and expectations. Our investment programme, including our commitment to the **Improving Urban Waters Routemap**, will target further improvements in areas where bathing water quality remains an issue.

Rockcliffe on the Solway coast had been classified as 'poor' since 2017. The quality at that beach also improved last year after SEPA authorised temporary treatment operated by Scottish Water at nearby Kippford for the 2021 season. We are working on a permanent solution for waste water treatment which will sustain this improved status for the longer term.

CASE STUDY AYR'S SOUTH BEACH TURNS THE TIDE

Scottish Water's £10 million investment at Ayr (South Beach) has driven clear improvement in water quality as it achieved a 'Good' classification in 2021. We increased storm water storage capacity and carried out temporary chemical disinfection at a local septic tank, an activity which we will now make permanent.

Additional work in the coming years will include first-time provision for properties which currently discharge to the River Doon, with around £3 million of targeted Scottish Government funding as part of a programme of improvements.



Prospects

We are already seeing how increasing periods of intense rainfall can overwhelm the sewer network. We recognise the need to look for new solutions to reduce this risk. We will work with communities, developers and other key stakeholders to ensure we plan for the removal of surface water from sewer systems at every opportunity.

We are developing long-term drainage and waste water management plans for all our catchments. We plan to publish these in 2023 with the aim of improving our knowledge and understanding of opportunities and risks of potential future work.

Working alongside SEPA we will focus investment on the highest impact intermittent network discharges. We are carrying out appraisals at 23 catchments which will be considered as part of a priority investment programme to help reduce flooding.

For surface water management we are developing our approach to transforming at three scales:

Project - all new sewer flooding, unsatisfactory intermittent discharges (UIDs) & growth projects will now include development of sustainable options to manage surface water.

Neighbourhood - We aim to develop a strategy and a programme of opportunities to be delivered in partnership with Local Authorities, SEPA and NatureScot.

City level - We are working with Aberdeen City Council and SEPA to trial an approach to integrated surface water and sustainable infrastructure planning. An initial strategy will be set out in the next 12 months.

An example of the above approach is where we are working with City of Edinburgh Council and SEPA to sustainably manage drainage and surface water and create resilience in the Craighleith area of Edinburgh. This is a first attempt to collaboratively create a single plan which can communicate the current understanding, constraints and improvement opportunities for managing storm water in a complex urban catchment with a history of flooding. This project aims to create the development of a joint planning approach which can be replicated across Scotland at a variety of scales.



ENABLING SUSTAINABLE AND INCLUSIVE ECONOMIC GROWTH



Overview

Our investment programme enables economic activity and growth as well as employment, skills development and innovation. The 2021 Hydro Nation report highlighted that the water sector, including our work, is worth £1.7 billion to the country's economy.

Working with our supply chain

2021/22 Performance

GOODS AND SERVICES

£864.6m

SPENT



In 2021/22, we spent £864.6 million on goods and services through 249 agreements and 494 suppliers (of which 386 were based in Scotland).

OUR SUPPLY CHAIN

71%

SMEs



Of the 494 suppliers in our supply chain, over 71% of our suppliers are Small Medium Enterprises (SMEs) and more than 90% of our spend is on organisations located in Scotland.

We are committed to an ethical supply chain; we want to work with suppliers who 'do the right thing' – who take issues of sustainability, human rights and ethical practices seriously.

We recognise that there may be areas of our supply chain where we find instances of modern slavery and our initial focus will be to work with our supply chain to resolve issues. If we are unable to reach an appropriate solution we will take the lead to explore alternative options and seek out other like-minded organisations to use our combined leverage to try and drive change.

We will also expand our focus beyond modern slavery to consider wider issues such as diversity and commitment to the elements of Fair Work First and these considerations will be built into procurement activity and ongoing supplier management.

Alliance Partners

In July we announced the appointment of a network of seven companies to carry out essential work across key elements of our operational services as well as deliver our capital investment programme. The procurement, which has a maximum value of more than £5 billion over 12 years, is one of the biggest ever carried out in Scotland and will support thousands of jobs in construction.

There will be a specific focus on delivering skills and development opportunities for young people, with more than 1,000 graduates and modern apprentices working at our delivery partners over the period these are in place. Most will work in STEM (Science, Technology, Engineering, and Mathematics) fields.

These partners will play a critical role in helping us achieve the change needed, on the scale and speed required to meet the dual challenges of providing services the public can rely on and addressing the impact of a changing climate on our infrastructure.

We have also secured a re-shaped Regional Services Contract, engaging small and medium enterprises, worth £530 million.

CASE STUDY

SMART CANAL HELPS CONNECT NEW HOUSING

Sighthill became the first of five housing sites to be connected to the Glasgow Smart Canal, a new flood mitigation system that will accept surface water run-off - cutting 35,000 tonnes of carbon and unlocking 110 hectares of land for 3,000 new houses to be built in North Glasgow.

The £17 million project, has been delivered by Glasgow City Council alongside Scottish Water and Scottish Canals through the Glasgow City Deal-backed by the Metropolitan Glasgow Strategic Drainage Partnership. It uses predictive weather technology and sensors to lower the water level on the Forth & Clyde Canal for surface water run-off from residential and business areas to flow into the canal.

The Smart Canal is helping to manage flood risk, allowing areas to be regenerated and also providing safe active travel routes for people. The project won the Sustainable Drainage and Flood Management Initiative of the Year at the UK Water Industry Awards in May 2021.

Working With Developers

We continuously invest in water and waste water assets to enable new housing and other economic development across the country.

Between April 2021 and March 2022 we completed 23,731 water connections and 21,581 waste water connections. This was a slight increase in water connections - up from 23,627 - and a reduction in waste water connections which were at 22,067 last year.

Development across Scotland has been recovering from the impact of Covid-19 throughout 2021/22 and development activity has remained high. Overall, the number of properties connected was in line with the previous year and there was an increase of 6% in the number of applications we received within the same period. This demonstrates how well the development community has reacted and sought to recover from the impacts of the pandemic.

2021/22 was a record year for investment in new waste water capacity to support new development with over £30 million delivered.

This year we maintained our focus on building strong relationships with the development community. As a result, we continue to see our development customer service scores increase. This progress was driven through streamlining our processes and responding faster with better quality responses to ensure developments can proceed and connect when required. A customer portal, which allows development customers to self serve, now accounts for 90% of requests from developers.

The introduction of a new Developer Customer Experience Measure to focus on driving down unwanted service contacts has been implemented, providing insight into the reasons customers contact our Development Services team. We have continued to utilise virtual meetings to improve our relationships with developers, consultants, local authorities and other stakeholders within the development community. This has increased awareness of further improvement areas and provides focus for new initiatives to drive greater customer service.

Working with developers

2021/22 Performance

WATER CONNECTIONS

23,627

23,731

we completed 23,731 water connections.



WASTE WATER CONNECTIONS

22,067

21,581

we completed 21,581 waste water connections.

APPLICATIONS

6%

6% increase in number of applications received.



■ 2020/21 figure ■ 2021/22 figure

Over the last year we have been working with developers and developing our plans for new network capacity. We anticipate a requirement for significant new capacity in our network in future years and will continue to work with the development community to provide this additional capacity just ahead of need. Further to this, a number of waste water treatment works upgrades are now under way which will provide additional capacity for development whilst protecting the environment.

Prospects

Across Scotland we have water and waste water assets that have capacity for future development and many that are already at or beyond capacity. We want to encourage development where we have available capacity and will continue to provide decision-makers in government, local authorities and the development community visibility of where capacity is available. Where it is not, we will invest to support development and from April 2021 we have started taking the lead in increasing capacity in our existing network infrastructure to support widespread growth. The volume of work to provide new capacity at our treatment works and network assets has started to increase and a number of large schemes are expected to start in 2022/23 to support new development.





PEOPLE

Overview

Scottish Water's employees - and those who work on our behalf and who we work alongside - enable the organisation to perform strongly and deliver services our customers and communities rely on us for. Our organisational character helps employees develop and learn and supports them carrying out their roles as effectively as possible.

As the Covid pandemic evolved, new ways of working have been introduced, prioritising the health and wellbeing of our people. Like all organisations, many of our people have had Covid, with some having to take time off to recover and others having to care for ill family members. Despite this the annual sickness rate was broadly in line with previous years and the impacts of Covid absences on our operations were minimal.





2021/22 Performance

During the second year of the pandemic, employees working in our field force and office-based roles have been supported to maintain service to customers and communities. While operational sites including water and waste water treatment works and laboratories remained open throughout the period, our offices were shut for most of the year. As restrictions were eased, significant planning was put in place around re-opening offices and starting to re-think their purpose.

Employee feedback in general has been positive. Tracking surveys highlighted a desire to continue to focus on employee wellbeing and approaches to flexible working. Some field staff said they felt less-informed than office-based colleagues and this will be a focus of our future employee engagement.

Providing a positive employee experience is a core part of our approach. The “Our Story” employee engagement programme was launched in November asking employees to consider the part they play in the transformation of Scottish Water and the continued delivery of vital services to the people of Scotland. Employees attended virtual events to hear first-hand testimony from colleagues on their roles, pride in working for the organisation and a focus on the future.

CASE STUDY REPURPOSING OUR OFFICES POST-COVID

Work has begun on defining the long-term strategy of what this will look and feel like for everyone in Scottish Water, including our field force. To help inform our long-term approach, we have initiated a pilot project at The Bridge office, near Glasgow, where the ground floor is being redesigned to include different zones for different types of work activity.

More flexible spaces and new technology will be made available for collaboration and connection and there will be quiet zones for work requiring focus and concentration. The design also takes account of how we can make the best use of indoor and outdoor spaces to enhance employee wellbeing.

Our Future Together also sets out our three strategic ambitions for the next 25 years and is supported by a plan for transformation.

Our Story

We set out three ambitions that we plan to achieve - that are fully aligned with our purpose, and wider water sector vision.

The Water Vision

30 years



Together with our stakeholders, we've agreed an ambitious long term collective water sector vision.

Strategic Plan

25 years



Our 25 year strategic plan is bold and challenging and will mean future changes for everyone in our business.

Character

B = Bold R = Responsible
I = Inspiring C = Caring



These are the characteristics we'll need and the type of organisation we must be.

Our Transformation Plan

10 years, 10 workstreams



Transformation is needed to make sure we unlock our full potential to become a different organisation in the way we think, plan and act.



Our Scottish Water story connects us all to the transformation journey and explains why we need to change.

Safety, Health and Wellbeing

The safety, health and wellbeing of our people and those who work on our behalf remains a constant focus.

We carried out weekly employee surveys to gain anonymous feedback on how people were feeling as the pandemic continued. This was shared with team leaders and directorates were urged to discuss feedback with their teams and offer support where needed. Monthly Scottish Water Cares wellbeing bulletins were also published.

Safety underpins all we do. We continually review and update related policies.

There were four RIDDOR (Reporting of Injuries, Diseases and Dangerous Occurrences Regulations) Incidents involving Scottish Water employees, the same as the previous year.

There was a rise in the number of RIDDOR Incidents reported by contractors with 12 reported in the last year, compared to 8 in 2020/21. This number is amongst the lowest in the UK water industry and our performance compares favourably with comparable industry sectors, when benchmarked by the Health and Safety Executive (HSE).

The number of Hazards Reported in the last year almost doubled compared to 2020/21. In the last 12 months there were 139 reported - compared with 69 the previous year. This highlights a greater awareness among our employees and people who work on our behalf, to report potential health and safety issues enabling action to be taken to prevent any potential future incidents.

Lost Time Accidents and RIDDOR Incidents

		Lost Time Accidents	RIDDOR Incidents
Scottish Water	2021/22	11	4
	2020/21	5	4
	2019/20	15	9
Contractors	2021/22	17	12
	2020/21	16	8
	2019/20	20	9
Total	2021/22	28	16
	2020/21	21	12
	2019/20	35	18

There was a slight increase in the overall sickness rate for employees in the last year, up to 2.78% from 1.91% in 2020/21. As the previous year, Covid continued to be one of the main factors in many staff absences throughout the year.

CASE STUDY DIVER SAFETY AWARD

Over the past year we have worked to review and improve standards and processing relating to diving operations. Divers can sometimes be required to support maintenance or repair work in assets such as reservoirs.

The Association of Diving Contractors (ADC) recognised this work by presenting a Client Award. An increased number of specialist contractors are available to us which improves geographic coverage, response times and safety standards.

Diversity and Inclusion

Activity is focused on four key areas to enhance approaches to diversity and inclusion. Work in this area is driven by our Public Sector Equality Duty responsibilities and our four Equality Outcomes, which were updated in 2021:

OUTCOME 1

Be renowned for creating opportunities for young people, particularly from areas of social deprivation.

OUTCOME 2

Increase representation in our workforce of women, ethnic minorities, young people and those with a disability.

OUTCOME 3

Increase diversity of our leadership bench across all under-represented groups.

OUTCOME 4

Achieve high levels of engagement and retention among those employees with under-represented protected characteristics.

We continue to encourage and support under-represented groups to apply for roles, build inclusion and to retain diverse talent to thrive and progress their careers. As well as becoming a magnet for diverse talent pipelines in recruitment, we are focused on building employee experience which is key to retention and well-being, as well as enabling an environment which creates learning and development opportunities. We are also focused on organisational capability and promoting inclusive behaviours by leaders, managers, and colleagues. Our next Public Sector Equality Duties report will be published in April 2023.

This year a systemic review of recruitment processes was launched to consider what changes could be made to attract a more diverse pool of candidates and to minimise bias within the recruitment selection process.

A new policy relating to workplace reasonable adjustments for employees with disability, health issues or neurodivergence has been introduced. Colleagues can access the right support to address any organisational barriers to enable them to thrive and perform at their best.

Our network of 9 employee-led Belong groups, each sponsored by a leader within the organisation, continue to challenge and provide support, and contribute to shaping policy development.

We collect equality monitoring that we can use effectively. Regular employee surveys have provided a greater understanding of the number of colleagues who have a particular protected characteristic, as well as the proportion of colleagues sharing different protected characteristics together with their satisfaction levels. This allows policies to be developed which help meet our equality outcomes. Our latest anonymous tracker survey suggests that 30% of respondents have at least one disability or long-term health condition.

We continue to take steps to ensure we have high quality equality data. This data helps us understand how we are doing in terms of inclusion and informs the development of future workplace arrangements.

Graduate and Modern Apprentice recruitment offers the greatest opportunity to balance workforce demographics. In 2021, 47% of our Graduate group was female, an increase from 42% in 2020. In 2021, 20% of our Modern Apprenticeship group was female, an increase from 18% in 2020.

Scottish Water's approach to flexible working for employees was recognised by judges in the Flexibility Works employer awards. They said arrangements put in place were progressive and the organisation was placed as one of the country's Top 10 flexible employers.

Bribery and Corruption Prevention

Our approach to bribery and corruption is governed by a counter fraud committee of directors and senior leaders. Policies are regularly reviewed to prevent bribery and corruption. This includes: Anti-Slavery; Code of Ethical Conduct; Whistleblowing; Anti-Bribery and Fraud Management and Response. A Policy Awareness Communication plan is rolled out annually and used to ensure all employees are aware of their rights and obligations. This includes mandatory training by appropriate role holders.

Human Rights, Dignity and Respect

We are committed to respecting Human Rights and expect people who work for and with us to show dignity and respect at work. Bullying, harassment, victimisation and discrimination are not tolerated. We promote an open and honest relationship between management and employees and commit to treating any allegations promptly, seriously, and confidentially.

Statutory Trade Union Facility Time

In the last year a total of 1384.8 hours were used as Trade Union Facility Time, which is paid time-off during working hours for employees who are also trade union representatives, allowing them to carry out trade union duties.



Recruitment and Retention of Employees

An area of growing concern for us is having the ability to attract and retain employees with the skills we require to deliver our plans. The number of job vacancies in the UK from January to March 2022 rose to a new record of 1,288,000. This level of vacancies is resulting in increased pressure to retain some of our specialist skills.

As a public body we operate within the arrangements of Public Sector Pay. We are beginning to experience retention challenges linked to remuneration and reward for some specialist roles. Key roles such as Mechanical, Electrical, Instrumentation, Control and Automation (MEICA) Engineers, Process Scientists, Project Managers and Data Scientists are already experiencing retention pressures.

Additionally, we are experiencing recruitment talent attraction challenges for some specialist positions such as Investment Analysts which is a key area of capability required to support our future planning. While we will continue to build our talent pipelines through our Graduate and Apprenticeship programmes we believe the level of risk arising from the current talent market conditions will further increase.

We are committed to supporting the Young Person's Guarantee which seeks to ensure young people in Scotland are provided with the opportunity of an apprenticeship, fair employment - including work experience, taking part in a formal volunteering programme, training or a place at a university or college. Every year we take on a number of people in a range of these roles. Our own broad apprenticeship programmes typically run for four years and focus on the integration of learning both on and off-the-job. During 2021, we had 19 graduate apprentices studying for degrees.



BEYOND NET ZERO EMISSIONS



Reducing our Carbon Emissions

Over the past year progress has been made in delivering planned Net Zero activities. We have also developed a deeper understanding of operational emissions, measures to reduce them, cost intelligence and the actions needed to accelerate reductions.

We have updated our ambitious pathway to achieve Net Zero operational emissions by 2030, ten years ahead of the original commitment in our routemap. This reflects an increased potential for new renewables on our assets - our forecast has grown from 90GWh to 120GWh, delivered by 2030. We are also working with partners to increase the number of windfarms hosted on our land.

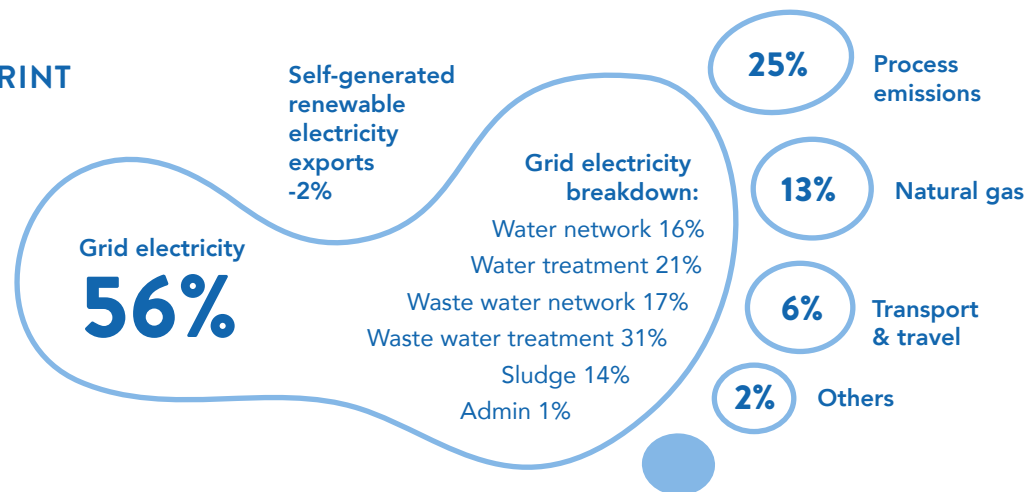
We marked the first anniversary of our Net Zero Emissions Routemap in September with the publication of our first annual update, covering progress and learnings to date. A second annual update will be published this September.

To see our routemap work go to Intro - Net Zero (scottishwaternetzero.co.uk)

Our commitment to partnership in achieving Net Zero led to the signing of the Edinburgh Declaration, an international statement led by the Scottish Government to ensure action to protect global biodiversity. We also joined the board of the Clyde Climate Forest which will see 18 million trees planted in urban and rural areas of Glasgow City Region by 2031.

While progress was made there have also been challenges. Supply chain issues led to a slippage on the renewables programme. Plans to install our most ambitious solar energy scheme at Balmore Water Treatment Works in Torrance, East Dunbartonshire our largest water treatment works, have been delayed. This was due to ethical procurement concerns relating to labour practices for solar panels manufactured in China. A full review and risk assessment of suppliers was carried out as a result.

OPERATIONAL CARBON FOOTPRINT 2021/22 GREENHOUSE GAS EMISSIONS BY SOURCE



Our approach to restoring peatland to address water quality risks and obtain carbon sequestration benefits has also been revised, with a focus on our own landholdings rather than on third party land. This was the result of a growing desire from third party landowners to retain carbon benefits. We own 22500Ha of land across Scotland and are currently reviewing our landholding for carbon capture potential.

2021/22 Operational Emissions

Our operational greenhouse gas emissions continued to reduce over 2021/22. Our carbon footprint (CFP) was 233,000tCO₂e - a 6% reduction on the previous year.

Energy Efficiency

Electricity is our largest source of emissions and in line with the emissions reduction hierarchy outlined in our routemap we are looking to reduce the amount that we consume. In the last year we completed energy efficiency projects which will save 7GWh annually - an increase in delivery since 2020/21 when we delivered 1GWh. The focus has been on improving efficiency of waste water aeration. Two major projects were completed which saw aeration systems replaced at Daldowie in Glasgow and East Kilbride's Phillipshill WWTWs. Daldowie is one of our largest sites, and the project enabled 4.2GWh benefit, nearly 1% of our electricity use.

Our purchasing strategy of hedging via Power Purchase Agreements (PPAs) and purchasing wholesale electricity in advance gave us an estimated saving of £3.7 million in 2021/22. We plan to continue to take measures to save on electricity costs in this way in the coming year and beyond.

Renewables

A total of 45GWh of renewable electricity on-site was generated again this year. In addition to renewable energy we have generated, our PFI partners have generated a further 32GWh from biogases produced by waste water treatment processes.

Renewable energy sources are vital to reaching Net Zero operational emissions by 2030. Plans will focus on the installation of more solar and hydro schemes on a much larger scale and at a faster pace to deliver more gains.

We continue to install solar photovoltaic (PV) equipment across our sites, delivered by Scottish Water Horizons. Across all our PV schemes we generated 7.8GWh - the previous year it was 6.3GWh.

Last year marked a decade of solar power production across our assets and landholdings. The first installation was in 2011 at Penwhirn Water Treatment Works in Dumfries and Galloway. Since then, £14 million has been invested enabling the production of 10MW of capacity across 53 sites. Around 32GWh of solar power has been produced over the ten years - the equivalent of powering over 8,600 homes a day.

The first battery storage facility has been installed in Perth, providing the ability to store the energy generated by the PV scheme during the day and allowing 94% of the energy generated to be used on-site. This will cut the carbon footprint of the city's treatment works by around 160 tonnes of CO₂e per year.

CASE STUDY

BIOGAS BREAKTHROUGH AT ABERDEEN SITE

A waste water treatment process which maximises the production of biogas has helped Nigg WWTW, Aberdeen, transform its carbon footprint. The CAMBI thermal hydrolysis plant was installed at the site 20 years ago. Since a programme of upgrade work was carried out in 2019, it has allowed the site to halve its greenhouse gas emissions.

Improvements have allowed additional sludge to be treated on-site, increasing the amount of biogas produced by up to 30%. This has enabled more green energy to be generated along with a reduction in the amount of fuel oil required to power the on-site boiler.

It has also diverted thousands of tonnes of sludge from going to land reclamation. The site now produces 90% of its electricity needs via two Combined Heat and Power engines, with periods where it is also exporting excess power to the national grid.

CASE STUDY

INNOVATIVE PARTNERSHIP TO A GREENER DRAM

An innovative new project is 'distilling' residues from the whisky industry into sustainable, green energy. We took part in a trial with SEPA and major distiller Chivas Brothers which saw distillery residue brought into Aberdeen's Nigg Waste Water Treatment Works for the first time, with promising results.

A process called 'co-digestion', means the residues from distilleries and breweries in the area can be added to sludge processed at Nigg, as part of a system which produces biogas.

The facility already has a process to turn sludge produced during waste water treatment into biogas - this is then used on-site instead of oil or diesel. Since October 2021, the sludge treatment centre has trialled co-digestion and this has increased biogas production.

With the addition of the distillery and brewery residues, the plant saw a saving of 58 tonnes of carbon over the 12-week trial period, which equates to 250 tonnes per year.

The teams involved in the Nigg trial have laid the groundwork to explore further opportunities for co-digestion.

Scottish Water Horizons' Deerdykes Bioresources Centre near Cumbernauld in North Lanarkshire has generated 50GWh of green electricity - the equivalent of powering 13,500 homes for a year.

Since 2010, Deerdykes has saved more than 170,000 tonnes of carbon, the equivalent of driving over six million miles in a car - or to the moon and back 12 times.



Process Emissions

Process emissions are methane and nitrous oxide, powerful greenhouse gases that are released as part of the material breakdown of organic materials and ammonia in waste water. They are the second biggest source of emissions after electricity use - and the most challenging to reduce.

Technology has been piloted which can recover methane from waste water sludge that would otherwise be lost to the atmosphere. The pilot was successful in reducing the loss of methane and enabling it to be used in power generation to displace fossil fuels and plans are ongoing to scale up deployment. Over the next 12 months, monitors to gauge nitrous oxide emissions from waste water treatment will be installed. This follows work to increase understanding of processes and how we might reduce these emissions.

Fleet

In 2021/22 our fleet drove 18.5 million miles on business. Policies to transition lease car and commercial fleet to electric vehicles (EV) were introduced. These support Scottish Government targets to phase out petrol and diesel cars and light commercial vehicles by 2025 and all new petrol and diesel commercial vehicles by 2030.

Independent research commissioned last year concluded that up to 60% of the operational fleet could transition to EVs to reduce emissions. The comprehensive review of over 1,300 vehicles identified where suitable EVs could be introduced, and the location and type of charging infrastructure required. A new EV Transition project team is in place to implement these fleet transformation opportunities to reduce our fleet related carbon emissions and reduce fuel costs.

Charging stations are vital for the rollout of EV - 49 have already been installed at 20 Scottish Water offices, treatment works and depots. Scottish Water and Scottish Water Horizons, our commercial subsidiary, are installing charging stations during the build of new renewables sites as a cost-effective way of accelerating their deployment.

Twenty new electric Nissan e-NV200 vans have been introduced to help us deliver services across the country - including by water and waste water samplers, technical teams and network operatives. Over the next 5 years we will replace nearly 800 diesel vehicles with electric. In addition, 40% of our lease car fleet has already transitioned to electric vehicles.



Investment Emissions

Working with suppliers

Our supply chain partners play a vital role in helping reduce emissions associated with our capital programme. The creation of a construction Expert Panel of senior leaders in Scottish Water, our supply chain, and experts in the Scottish construction industry, has driven a focus on low emission actions. Our Carbon Academy, created to share learning and best practice on low carbon construction has been recognised as best practice by the Institute of Civil Engineers (ICE).

Delivering Net Zero emissions in our capital programme focuses on three areas where we are looking to reduce carbon: design, materials, and construction.

This will allow us to deliver our goal to reduce carbon intensity of our investment by 75%.

To reduce investment emissions, we are working to better understand and tackle the major sources that drive them. We have worked with our partners to understand the “Top 10” materials that are driving investment emissions. All projects are now asked to report the carbon that they will generate, where previously this was only done for work valued at over £1 million. We are also able to better record and report emissions by investment programme area, highlighting that some programmes are driving emissions more than others. We are still growing our understanding of investment emissions and continue to report them as a range of 200-300tCO₂e/£m.

The supply chain is engaged in our Net Zero capital investment strategy and building real-world solutions and knowledge. Pilot activities range from off-site fabrication, trialling low carbon concrete to focusing on low carbon plant and materials to reduce time, carbon and cost on-site. Our Net Zero target was integral to the procurement of the SR21 supply chain framework.

We have seen progress in key areas including:

- **Design** - adopting circular economy principles and maintaining and refurbishing assets rather than replacing; challenging and reducing unnecessary carbon intensive steelwork.
- **Materials** - piloting low carbon concrete and using a selection of low carbon materials to replace concrete in designing tanks.
- **Construction** - adopting off-site fabrication to improve quality, reduce carbon and piloting low emission construction sites. Increasingly looking at ways to use digital technology to reduce the number of site visits and increase productivity.

Looking ahead there are key technical, behavioural, and commercial challenges across all aspects of investment delivery, and collaboration with the supply chain will be critical in addressing them.



Carbon Capture

Some of our emissions are difficult to reduce with current technology so instead carbon capture mitigation plans need to be introduced.

Plans are in place to restore peatland on our land to good condition over the next few years and all our landholdings are being screened to understand their potential to increase carbon capture and biodiversity.

We have also undertaken the first biodiversity audit of our landholdings, working with Natural Capital Research and NatureScot to create a biodiversity metric to enable us to understand our performance and target improvements.

The woodland creation schemes at Loch Katrine and Lintrathen, along with further projects in the coming years will significantly increase biodiversity. We are also developing our approach to deliver biodiversity gain when we deliver major projects and on our operational sites.

CASE STUDY NEW FOREST AT LINTRATHEN

We are creating a brand new area of woodland in Angus aimed at increasing carbon capture which will also improve biodiversity and wildlife habitats.

We have transformed c100 hectares of hillside close to Lintrathen Reservoir, which were previously a mixture of small stands of mature commercial conifers and rough grassland for grazing. We've created new woodland with a mixture of native pine and broadleaf trees including ash, oak and birch, as well as areas for commercial timber.

When it matures the site will capture a significant amount of carbon. Within a few years it could capture up to 1000 tonnes of carbon per year making a major contribution towards our Net Zero goals.

The site will also be far more beneficial for birds, insects and mammals to live in and improve biodiversity in this area.

Additionally, the logs cleared at the Lintrathen site have been converted to timber for construction and timber products ensuring the carbon captured in them is not released.



Supporting a Flourishing Scotland

As well as working to reduce emissions from our own activities, we have been looking to use our assets and resources to help reduce emissions from others in Scotland.

Heat from Sewage

We were the first utility in the UK to start heat from sewage schemes, an opportunity to extract value from waste stream as a source of renewable energy. In the last year two further schemes have been completed and one has started construction.

Supporting the Hydrogen Economy

Water is vital in the production of hydrogen which is seen as a key source of future energy to reduce emissions from fossil fuels. Work is ongoing with hydrogen developers across the country to explore options for water to supply their production sites. Projects are under way looking at how to provide water for Scottish Power and SSE hydrogen projects as well as the ACORN project at St Fergus, Aberdeenshire. We are also working with SGN on their H100 project in Levenmouth and on a study that is looking at how to convert the natural gas network in Scotland to one that transports hydrogen.

Streamlined Energy and Carbon Reporting (SECR)

Streamlined Energy and Carbon Reporting (SECR) is a UK Government requirement for certain types of organisations to report their energy and carbon emissions. It aims to encourage businesses to implement energy efficiency measures to bring both economic and environmental benefits.

This method of reporting energy and carbon emissions differs from, and is not comparable to, our established annual operational carbon footprint (CFP) reporting, which we have published since 2006/07 (see page 61 for 2021/22 footprint.)

Our operational CFP reports on the regulated business, which includes waste water treatment works operated on Scottish Water's behalf by Private Finance Initiatives (PFI), but excludes other parts of the Scottish Water Group; it also includes more sources of emissions than the SECR, such as water and waste water process emissions. In contrast, the SECR reports on the whole Scottish Water Group of companies, but excludes PFI activities (except the North-East Scotland Waste Water PFI). The two sets of emissions are therefore not comparable.

It is a requirement of SECR to disclose which robust and accepted methods are used to calculate the required information.

They are as follows:

SECR energy consumption data is dominated by electricity use by Scottish Water core business. This is from metered data, properly documented and recognised as the best method of assessment, with an accuracy range of between +/- 5% and +/- 1%. Natural gas consumption and exported Renewable Energy Guarantees of Origin (REGO) electricity are similarly calculated from metered data. Fuel is predominantly used in Scottish Water core business owned and leased (Scope 1) vehicles and is from measured fuel volumes.

The UK Water Industry Carbon Accounting Workbook, which we use for reporting our annual operational carbon footprint, has been updated to facilitate SECR. This calculates energy consumption (kilowatt-hours (kWh)) of fuels, and greenhouse gas emissions using, respectively, the densities and net calorific values (NCVs) and the emissions factors in the 2021 UK Government GHG Conversion Factors for Reporting.

Scottish Water Group	Current reporting year	Previous reporting year
	2021/22	2020/21
GROSS Energy Consumption (GWh) ⁹	569	614
NET Energy Consumption (includes REGO exports) (GWh)	553	589
Emissions from combustion of gas ¹⁰ (tCO ₂ e)	4,044	2,498
Emissions from combustion of other on-site fuels ¹¹ (tCO ₂ e)	2,121	955
Emissions from combustion of fuel for Scope 1 transport (tCO ₂ e)	11,284	11,603
Emissions from Scope 3 business travel ¹² (tCO ₂ e)	1,609	1,203
Emissions from purchased electricity (Scope 2, location-based accounting) (tCO ₂ e)	93,290	106,637
Total gross tCO ₂ e based on above	112,348	122,896
Intensity ratio: tCO ₂ e gross figure based from mandatory fields above per £1 million revenue	65	74

⁹ Gross consumption includes consumption of renewable electricity generated on site; this was not included in previous years' reporting.

¹⁰ Increase from the previous year is due to increased output at SW Horizons' district heating systems in Stirling and at an additional site developed this year in Dalmarnock.

¹¹ Previous year's consumption was particularly low.

¹² Scope 3 business travel includes travel in private vehicles and 3rd party sludge tankering; travel on public transport is excluded.

Energy Efficiency Actions

In 2021/22, upgrades to heating and lighting systems and treatment optimisation at waste water treatment works delivered 6.5 GWh per annum of energy savings. Additionally, at Scottish Water's Dumfries office a natural gas boiler was replaced with an air source heat pump saving an estimated 0.03 GWh per annum.

Prospects

The second annual update of the Net Zero Emissions Routemap will be published in September 2022. This continues to drive our organisation-wide approach to reducing emissions in key strategic areas of activity:

ELECTRICITY



TRANSPORT & TRAVEL



PROCESS EMISSIONS



INVESTMENT



GAS & FUEL OIL



STORING CARBON



TO ACHIEVE OUR NET ZERO EMISSIONS AMBITION, WE WILL:



BECOME MORE
ENERGY EFFICIENT



USE LOWER CARBON
ENERGY PRODUCTS



EMBRACE LOW CARBON
CONSTRUCTION



STORE AWAY
EMISSIONS THAT
CANNOT BE AVOIDED

Pace and scalability are critical elements to ensuring we remain on track. Innovation will also help transform our services and delivery.

We will continue to grow our knowledge and understanding and at the same time, seek to implement solutions on the ground which deliver for customers and the environment in tandem.

The development of carbon tracking and reporting will also help enhance our ability to demonstrate progress across key areas of the organisation.

We have set out the steps to transforming our greenhouse gas emissions in our Net Zero Emissions Routemap.

We will continue to develop, appraise and deliver opportunities particularly in energy efficiency, renewable energy and our vehicle fleet. We will continue to develop a 260GWh opportunity for new renewables in south-west Scotland on our land and explore other opportunities to host renewables.

We will install monitors and trial technologies at a number of waste water treatment works to improve our understanding of process emissions and reduce them.

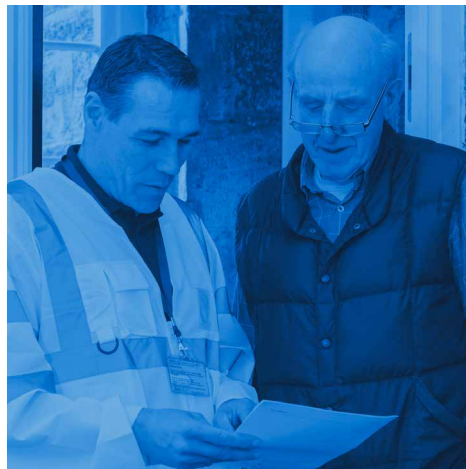
We continue to work with supply chain partners to introduce low carbon design and materials. Our investment decision processes will consider cost carbon

and wider benefits. We will develop our pathway to Net Zero investment emissions, outlining the rate at which we will reduce them over time and build our understanding of the investment needed to achieve this.

Some emissions cannot be fully eliminated. We aim to balance these by improving the ability of our land to store carbon. Over the next year we will complete screening of our landholdings for the ability to store carbon and progress opportunities to increase tree planting and restoring degraded peatland.

Scotland's natural environment is central to our identity as a nation. We will play a significant role in supporting the Environment Strategy outcomes through protecting and restoring water, seas and soils, supporting biodiversity and embracing circular economy thinking.

GREAT VALUE & FINANCIAL SUSTAINABILITY



OUR INVESTMENT PROGRAMME

Overview

Financial year 2021/22 has been a successful transition year with a significant rise in our level of capital investment.

Our total planned investment for 2021/22 was £623 million. On a like-for-like basis with 2020/21 - when including responsive repair and refurbishment expenditure it was £799 million¹³.

Most of the investment has been in the refurbishment and replacement of existing assets to continue to deliver a high level of service to our customers. This has included new or improved treatment works and networks to support quality enhancement or growth, flooding prevention and maintenance of our existing assets to ensure continued levels of service.

¹³ See previous footnote 1 on page 5

Tier 2 Investment - this is our planned capital work - total for year: £622.9 million - this was £10.9 million above our target projection for the year.

Tier 1a Investment - this is responsive repair and refurbishment of assets, plus developer contributions – total for year £176.5 million.

This increase in investment is a remarkable achievement when considered in the context of the historic trend among regulated utilities for investment levels to fall at the start of a new regulatory period.

Several things have combined to make this possible. These include the new investment planning framework developed with our economic regulator and other stakeholders and our success in putting delivery partners in place with sufficient time to plan for greater delivery capacity.

During 2021/22 a total of 6212 projects - an average 17 projects every day - were delivered. These either maintained the level of service we currently provide, facilitated growth within communities or enhanced the capability of our assets to provide improved levels of service.

CASE STUDY

STATE-OF-THE-ART WASTE WATER WORKS FOR WINCHBURGH

We are investing in a new state-of-the-art waste water treatment works upgrade in Winchburgh. This was one of our largest investment projects during 2021/22. The current site has come to the end of its life. The new works will provide increased capacity to support existing and proposed development in the West Lothian town for the next decade and beyond.

The new works will make use of state-of-the-art Nereda technology which reduces energy usage by up to a half and treats waste water more effectively. It treats waste water much more quickly than current treatments and takes away the need for pumps and mixers, meaning less energy and space is needed to treat a higher quantity of waste water. It also removes the need to use any chemicals during the treatment process which better protects the environment at local waterways.

2022/23 will bring us further challenges as we plan to deliver a further increase in total investment. This increased level of investment and associated increase in the number of live projects will require us to continue to improve our current processes and engagement with our delivery partners and local communities. This will ensure the project delivery cycle is as efficient as possible.

Our revamped supply chain is proving to be agile and flexible and is helping us deliver benefits to customers as well as securing employment for several thousand people. This includes graduates and modern apprentices who will learn on-the-job skills needed for the water sector of the future.

Key to this was the establishment of new performance measures which allowed a focus on ensuring the pace of investment was maintained and commitments met on project delivery. These include: Progress to Committed List (PCL) and Indicator of Progress of Delivery (IPOD). PCL allowed us to focus on the initiation of work in the system and promotion rates ensuring there was sufficient volumes of investment flowing through to delivery. The IPOD measure allowed us to focus on the delivery dates once an investment project was in delivery and maintained a focus on the commitments we made to our customers and stakeholders.

Market Challenges

Global market conditions have affected the availability and cost of construction materials which impacted some of our investment programme. These have included increased demand for construction materials in China, India and Europe; the impact of Brexit, cargo being delayed in the Suez Canal, ongoing Covid restrictions, the temporary shortage of lorry drivers, rising costs of materials and issues with concrete manufacture in Scotland. Similarly challenging conditions are expected to persist in the year ahead.

An example of the knock-on effect of this is the three-month delay to our major investment at Invercarnie Water Treatment Works (see case study) due to changing market conditions and an electrical sub-contractor going into administration.

Loch Ness Regional scheme, a new multi-site water treatment works to improve the treatment and supply of drinking water to customers to the south of Inverness - was also delayed due to challenges during commissioning. Work is now due to complete later this year.

CASE STUDY REVAMP AT WATER WORKS WITH ROYAL LINKS

Aberdeenshire's historic water treatment works is getting a major £52 million revamp. The treatment works at Invercarnie in Banchory, was opened by Queen Victoria in 1866.

James Simpson, one of the greatest engineers of his time, designed the works to divert water from the River Dee via a 1.3 mile tunnel to a reservoir at Invercarnie - 244ft above sea level. It is still the main source of drinking water for the region serving 300,000 customers in the north east.

A two-year project is underway to refurbish the works which will have the capacity to deliver 63 million litres of drinking water a day. A new water storage tank, air filtration plant and a new pumping station and pipework, are being installed. It is due to be completed in 2023.

2021/22 Performance

INVESTMENT
ACROSS SCOTLAND

£799m



7GWh

ENERGY EFFICIENCY
PROJECTS
CARRIED
OUT AT
OUR SITES



ACTIVITIES INVESTED IN



Supporting economic
development



Improving waste water
treatment quality



Reducing flooding and
pollution from sewers



Sustaining existing high
service for customers



Improving drinking
water quality

Prospects

More needs to be invested at quicker pace to replace our ageing infrastructure and make assets more resilient. We have completed the major refresh of our supply chain with the procurement of contractors for a new delivery vehicle around repair and refurbishment work. This was one of the key early commitments made in our Delivery Plan.

Our aim is to increase investment by 30% in this regulatory period from the previous regulatory period. Despite this, we will still face difficult choices about which investments to prioritise for delivery.

Looking ahead we can expect issues linked to ongoing inflation and the availability and price of materials for at least the next two years.

As our supply chain has been revamped it will take time for the people within it to obtain the knowledge and skills to get the most out of these partnerships, which will be in place for several years. We will continue to build capacity and skills into our supply chain. The delivery of lean and agile solutions is a priority, and we will continue to work with partners as best as we can to achieve this.

CASE STUDY COMPULSORY PURCHASE ORDER FIRST IN FORRES

We carried out our first Compulsory Purchase Order (CPO), a legal mechanism allowing us to acquire land without the consent of the owner. This supported the delivery of a major water treatment works in the Forres area.

The land was required for us to access the project site and we were granted the order after it was deemed in the public interest to obtain the land. Six owners agreed to us accessing their land but one refused and as a result we were obliged to take this action.

When investing we always look at different options, when available, and maintain a sharp commercial focus. We would only seek a CPO as a last resort in order to keep costs as low as possible for our customers.

It is critical we spend our customers' money in the right way for today and the future, building trust and confidence with our customers and stakeholders. We are a long-term business with assets that can last for decades or even centuries. Driven by our purpose and aims, we are providing clarity and consistency on how we make investment decisions. Embedding a common approach, spending each pound best to benefit our customers, communities and the environment.

We are currently developing our investment strategy to set a baseline. This is being considered as a critical component of our overall vision for Sustainable Investment Decision-Making. This will provide a full understanding of our asset systems and help inform our future investment decisions.



TRANSFORMING HOW WE WORK

Overview

Our strategic plan, Our Future Together, set out our long-term strategic ambitions and, to achieve these, we will fundamentally transform our organisation. Our 'Plan for Transformation' was published in November setting out our approach, taking account of learning from other leading organisations in the UK and beyond and listening to our workforce and sector stakeholders.

Our transformation aims to deliver a fit-for-the-future organisation which is adaptive, efficient, technologically advanced, customer focused, collaborative and proactive. Our planning also factors in expectations of customers and communities, climate change and technological progress.

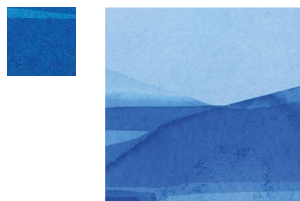
Our transformation activity can be grouped into the following themes:

Deepen our customer and community focus: putting customer and communities first

Invest strategically for Scotland: strategic decision-making and investing to deliver a low-carbon infrastructure

Become Fit for the Future: creating a lean and agile organisation

Our plan for transformation is about setting the organisation's ambitions in motion to achieve the objectives set out in Our Future Together. It means work to engage with customers, employees and business partners has begun in earnest. Transformation and change will come with unexpected challenges, but a plan which is robust but adaptable will help us achieve our ambitions.



CASE STUDY

REMOTE DIAGNOSIS: SAVING TIME, MONEY AND THE ENVIRONMENT

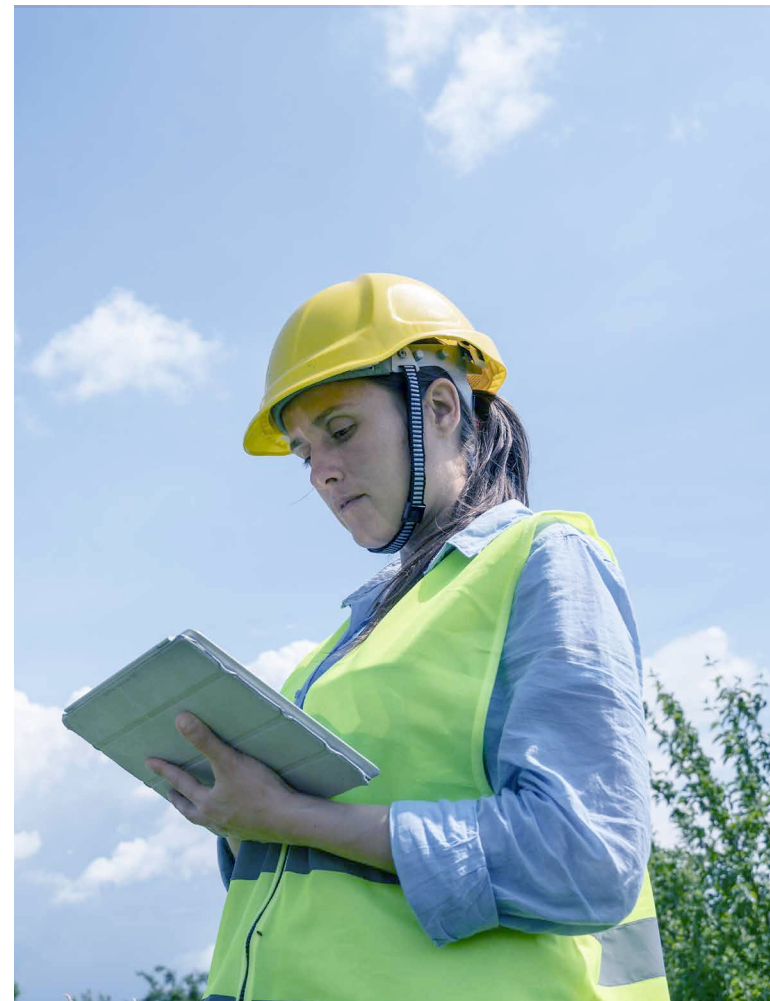
Using triage alongside a new video tool called SightCall, we can diagnose and resolve some customer issues remotely, quicker than ever before.

The new software has been adopted through the 'Scottish Water Intelligent Field Transformation' project - also known as SWIFT.

The Remote Diagnosis project has made savings of over £80,000 so far - achieved through triaging and diagnosing over 3,700 cases remotely and preventing over 1,200 site visits. That's a 33% reduction in the number of physical visits which, in turn, has reduced our carbon emissions too - in direct support of our strategic ambition to go beyond Net Zero emissions by 2040.

Implementing a triage step, involving interrogating data and systems, together with our team's knowledge has allowed us to provide an enhanced customer service, with the capability to assess and resolve customer queries faster. Our Field Response team can then reinvest the time saved on more complex tasks.

We are looking at rolling this out to other teams as well as streamlining processes to continually improve our service.



CASE STUDY

USING THE POWER OF DIGITAL TECHNOLOGY

We plan to transform waste water services with the use of new smart technology to help to predict and respond to eight out of ten unplanned escapes from the waste water network in a predictive rather than a reactive manner. The sensors detect the build up of blockages to predict potential pollution or flooding events. The aim is to minimise customer and environmental impact and enable us to provide exceptional response and customer service.

Creating an intelligent network using sensors will provide additional information on performance and trends, enhance the natural environment through reduction of environmental pollution incidents and provide better knowledge of environmental impact. We have three pilot projects underway and will monitor their success to expand the technology to other parts of the country.

CASE STUDY

MAJOR ADVANCE IN WASTE WATER TREATMENT OPERATION MONITORING

We are working on a new programme called 'Exemplar' to help us understand more about our waste water operations and to make more informed decisions about how they are operated.

We have started with improving visibility of how Laighpark WWTW in Paisley is operating. Exemplar is working to connect existing operational data, such as telemetry and weather data, with real-time data from new sources including Real-Time Control, Final Effluent Monitoring and Energy Monitoring. Operators can now view all this data using an app on their PC or mobile phone and use this to identify issues with the treatment process and prioritise what needs to be done and where.

We plan to roll the 'Exemplar' solution out to 16 of our largest waste water sites. Greater intelligence about our operational assets and treatment processes at these sites will help make more informed decisions. This will drive an increase in operational performance and help us achieve our Net Zero emissions ambition. Using the insights generated will enable us to reduce energy consumption by setting up equipment to run optimally. This will result in a double benefit of reducing electricity costs and reducing carbon emissions.

Transforming our Future Delivery

Transforming Our Future Delivery is a programme of change aimed at improving the effectiveness and efficiency of capital project delivery. It has included initiatives to get to site in half the time, improve collaborative working and decision-making and enable our people and partners to be more productive through digital and technology solutions.

Non-Complex Service Delivery

We have started to transform the way we replace, repair and refurbish assets where the value of the required work is less than £500,000.

In a major advancement, we are now streamlining this investment by reducing waiting times for work to be carried out from months, or many weeks, to just days and cutting costs. We introduced a Non-Complex Service Delivery (NCSD) app and portal to enable our people to raise, manage and deliver non-complex needs. This means work and parts can be ordered and approved automatically without the need to go through a lengthy sign-off process.

Employees can raise a need from their mobile phones or laptop and select a product or service from a standardised list. The order is then automatically processed where it meets our in-built asset management policy requirements. The team member making the request will also be notified of the exact cost involved and choose a delivery date. Since we started using NCSD we have completed 5,500 needs requests with a combined investment of £92 million. Our analysis shows this programme is on track to deliver our ten-year forecasted benefits of £37-57 million, after the £19 million cost of delivering NCSD.

Looking ahead, we predict a significant increase in non-complex investment, reinforcing the imperative to enhance the digital platform, improve the business process and challenge existing ways of working to complete the NCSD process transformation.

Prospects

We are learning from our early transformation projects and pilots, such as using sensors in our networks and streamlining our processes through our new 'solutions hub', to scale up and fast-track initiatives under the ten transformation workstreams. Over the next six months, we will also see benefits from some initiatives which we have been focused on planning until now - like working more flexibly in our larger offices, introducing a new performance management approach to all colleagues and setting up a new platform to better share data, internally and externally.

The table on pages 78 to 80 details the key objectives over the next six months for each of the workstreams.

Workstream name	Workstream outcomes	Key achievements over last six months	Key objectives for next six months
Capital Allocation and Sustainable Investment Decision-Making (SIDM)	To ensure we translate the purpose and strategies of the business to “maximise benefits of investment to customers, communities and the environment” and ensure this is ingrained throughout the organisation. The outcome is to create trust and legitimacy with customers and stakeholders.	We have: integrated the Asset Management Transformation Roadmap initiatives into our wider transformation portfolio. We've appointed a Strategy & Commercial Director to provide greater focus on long-term strategy and investment planning, and working closely with our stakeholders.	We will: finish phase 1 of our System Planning Initiative, focused around Water Supply Risk Management project and complete phase 1 of the Strategic Investment Planning initiative - with a high-level baseline.
Data & Information - Keeping our Data Healthy	Data is essential to what we do & it is therefore critical that we take care of it, manage it well, keep it healthy, accurate and appropriately protected ensuring it is trusted and connected to power our business.	We have: created a new transformation workstream to ensure we give our people and stakeholders confidence our data is well managed, protected and of high quality so it informs the right decisions to provide the best services for our customers. We've started to embed a new sustainable approach to keeping our data healthy and completed a pilot to empower and support our people to become critical 'data citizens' across the business.	We will: launch two new initiatives. One which will deliver a transparent Scottish Water reporting landscape, to answer the questions that meet the expectations of our stakeholders and customers working in collaboration with the WICS. And another to enable a seamless & transparent sharing of appropriate data beyond Scottish Water through an Open Data platform. We will continue to roll out our data citizenship making it easier for our people to work with data.
Engagement, Motivation and Place	To inspire an engaged workforce who feel listened to and who are proud to work for, and be served by, Scottish Water. To deliver the people experience of change we have defined.	We have: launched and shared our Scottish Water Story with colleagues, encouraging leaders to discuss with their people to connect with why we need to change. We've asked colleagues to share their feedback and experience of change. And we've continued to spotlight transformation progress with targeted line leader updates.	We will: complete the procurement process for consultancy support for transformation engagement. And we will focus on building a change capability programme to help our colleagues to confidently embrace and engage with change in the business.

Workstream name	Workstream outcomes	Key achievements over last six months	Key objectives for next six months
Intelligent Asset Base (IAB)	We are providing our people with the information, technology and skills to be able to plan and predict issues before they impact customers and the environment.	We have: deployed further sensors into our waste water network to predict and prevent pollution incidents and flooding, and into our Waste Water Treatment Works to alert us to condition or performance issues. We have deployed sensors and smart meters into parts of Inverness to help reduce leakage and better manage water pressure. Our pilots are already generating learning and value - helping us better plan, predict and prevent issues before they impact customers and the environment.	We will: build on the success of early pilots, and improve our processes and systems so we can scale them up effectively with enthusiastic commitment from our people.
Leadership & Skills Development	To plan for and build the skills, competencies and behaviours that will enable transformation, equipping leaders with the skills and knowledge to lead transformation and to lead with character.	We have: created a new department to integrate resourcing, learning, talent and leadership. We designed and built a new organisational competency framework which will integrate our behavioural characteristics into our performance, learning and recruitment processes.	We will: support the launch of the new performance management approach which focuses on performance, learning, wellbeing and growth. We will source suppliers for leadership development and key skills themes. We will complete plans for data and analytics, lean and agile and investment prioritisation, a strategic skills forecast linked to our capital investment programme and implementation of a digital skills programme for our operational employees.
Learning & Innovation	To create a safe learning environment where employees feel safe to experiment and innovate. To create an organisation where mindsets, habits and behaviours support learning.	We have: designed and built the systems and learning materials to support the new approach to performance.	We will: have launched the learning organisation concept to all employees and integrated learning-oriented behaviours into our key people processes.
Lean & Agile Solutions Hub	To fully “lean” enterprise wide; customer journeys, processes and governance, with; all wastage removed, standardisation inherent and routines automated. To build cross functional agile teams in key business areas, to fully exploit new ways of autonomous working.	We have: continued to focus on advancing our Transformational Solutions Hub journey re-design programme, with four live re-design labs underway, and the first journey "I Connect" now ready for deployment of the improvement recommendations. Our Functional Hub also continues to build momentum with live frontrunner improvement projects being delivered in Capital Investment.	We will: continue with the journey re-design programme within Solutions Hub, deploying improvements sequentially thereafter. Our Functional Hub deployment programme will continue to grow, and we will progress an agile working structure.

Workstream name	Workstream outcomes	Key achievements over last six months	Key objectives for next six months
Partner Ecosystems	To be recognised as pioneers for partnership - Scottish Water and its partners have the capacity and capability to meet the new challenges we face, collaborating to meet the needs of customers, the environment and supporting a flourishing Scotland.	We have: established an innovative partnership model so that a "community of partners with aligned objectives can leverage each other's capabilities to achieve mutually beneficial outcomes". The foundations will support how we will work more collaboratively with our partners - contractors, consultants, academics, councils and suppliers. Behavioural charters have been co-created and implemented with our delivery partners to establish trust and productive working relationships in our integrated teams.	We will: implement the partnership model to demonstrate the sustainable benefit of partnering ecosystems; we will embed new ways of working and deliver digital solutions that create capacity and support our people to deliver increasing levels of investment.
Performance, Pay and Recognition	To help maximise performance of Scottish Water's talent base, where people feel supported and challenged to achieve excellence, and rewarded fairly and transparently for their efforts.	We have: begun the Modernising Reward Foundations project to introduce a new framework of job roles across Scottish Water and a replacement, fair and transparent pay and grading system. Also launched the My Story performance management approach to senior leaders in April, followed by all line leaders in May.	We will: develop a role catalogue and a set of job profiles using a common language with easy read across between roles. We will begin building new salary ranges on a new grading structure. We will launch the new My Story performance management approach by Autumn 2022. And we will begin looking at working hours and patterns, driven by customer need.
Purpose, Customer and Community Centricity	Grow the mindsets, capabilities and insights needed for Scottish Water to embed Customer and Community Centricity into everything we do. We will take decisions as if the customer was 'in the room', develop new ways to measure success and become a purpose driven organisation. Our customers trust and appreciate us as their publicly owned water and waste water services provider. We will have new service offerings to ensure we meet customers expectations now and in the future.	We have: built our customer and community centricity strategy and began working on a framework for how we will measure success. We have made progress against our ambition to become a great wholesaler, with the introduction of our Wholesale Resolution Team who are empowered to handle complex cases.	We will: identify and implement quick wins to build customer and community centric capabilities, mindsets and behaviours. We will make progress in community engagement in our process to plan, prepare and deliver investment. And we will focus on embedding customer and community centricity in all other transformation workstreams.

KEEPING SERVICES AFFORDABLE

Overview

Water and waste water charges support service delivery, investment in ageing infrastructure and improvements in water quality and environmental protection.

Higher levels of investment are needed to protect services now and over the long term, particularly in replacing ageing assets, meeting the challenges of more intense rainfall, flooding, and drought, and reducing carbon emissions.

In February we announced household charges for water and waste water services would rise by 4.2% in 2022/23. The new annual charges, collected alongside local authority council tax, mean an average bill increase of 31 pence per week. Around half of all households in Scotland receive financial support as they automatically have either a discount, exemption or reduction applied to their water and waste water charges.

We highlighted in all our communications about the increase that, in setting charges, we carefully considered the need to balance higher levels of investment with the financial challenges faced by households at the present time. We have set charges at a level that takes account of

those challenges while being open and clear that charges will need to increase further in future years. We aim to ensure increases are managed in a stable way to avoid sharp annual increases.

Water and waste water charges to LPs who supply businesses and other non-household customers also increased by 4.2%.

Prospects

We are conscious that increasing charges to pay for additional investment must take account of the difficult economic circumstances faced by many people and businesses across Scotland and yet recognise too that those conditions may continue to be challenging in the years ahead.

When setting charge levels for 2022/23, and following discussions with the Scottish Government, we agreed to limit charge increases to 4.2%, in line with the October 2021 CPI inflation figure, the benchmark month we use for charge-setting. We recognise the financial pressures on households and businesses are likely to increase for some time and doubt whether it would be feasible to return quickly to the charge level expectations set out in the final determination of charges.

However, the financing set out in the final determination will be required across the 2021-27 period to enable us to deliver Ministerial Objectives. We are exploring with the Scottish Government the options for securing financing that will be needed beyond that arising from charge levels that may feasibly be set. In the meantime, our healthy cash position, strong income stream, and committed borrowing from the Scottish Government enable us to continue planning, prioritising and delivering capital investment in line with Ministerial Objectives for the 2021-27 period.

FINANCIAL SUSTAINABILITY

The principal activities during the year were the supply of water and waste water services to homes and businesses across Scotland.

Scottish Water's regulated business supplies water and waste water services to households and is also the wholesaler to the 25 retailers (Licensed Providers) who operate in the water retail market for businesses in Scotland.

Within the Scottish Water group, our subsidiary, Business Stream, operates as a Licensed Provider, competing with other Licensed Providers in the Scottish and English markets to supply water and waste water retail services to business customers.

The group also provides non-regulated and other commercial services and, since December 2018, has owned the companies that operate four waste water treatment works in North-East Scotland, under contract to Scottish Water, through Scottish Water Horizons Holdings Ltd. This report highlights the performance over the period 1 April 2021 to 31 March 2022 for Scottish Water's group of companies.

The Members of Scottish Water's Board are accountable to the Scottish Government. Details of the current Board Members are provided on pages 110 to 113. Scottish Water's principal subsidiary undertakings, all of which are disclosed in note 11 to the financial statements, have their own Boards of directors.

Business Stream is operated in accordance with the Governance Code (agreed with the WICS). The code sets out the operating regime that Scottish Water and Business Stream must comply with to enable the operation of the licensed retail market. Business Stream has the same Chair as Scottish Water but has its own independent Board and management team. Scottish Water exercises governance over Business Stream through Scottish Water Business Stream Holdings Ltd in accordance with the above code.

The performance for the three main business areas covering regulated, Business Stream and non-regulated services is detailed on pages 88 to 90 with an overview of Group performance on pages 90 to 91.



Scottish Water - Regulated Services

Performance

The financial performance of Scottish Water's regulated activities is measured on a regulatory accounting basis. The following tables and commentary have therefore been presented on that basis. Reconciliations to Scottish Water's group results (as detailed in the Financials section on pages 143-195), along with relevant cross-references are provided opposite.

The new format Regulated Income & Expenditure Statement for the 2021-2027 period is presented opposite.

The 2021/22 financial contribution from customer revenue to planned investment was £336 million, £39 million higher than the mid-point of the original Delivery Plan updated to reflect out-turn inflation for the year. The original Delivery Plan assumed that CPI inflation would be 2% over the year but actual average CPI inflation for the year was just below 4%.

This was towards the top end of the range set out in our original Delivery Plan for 2021/22 and the reforecast set out in our Interim Prospects and Performance Report to 30 September 2021. The £39 million improvement was primarily driven by a higher volume of household billings, increased wholesale consumption as businesses benefited from the easing of constraints associated with the pandemic and proceeds from the sale of assets.

Costs before items subject to long term normative charge (LTNC¹⁴) were £15 million below the updated Delivery Plan mid-point after reflecting out-turn inflation in the year. Operating costs were £5 million lower reflecting lower travel, energy and regulatory costs. PFI costs were £7 million lower primarily due to one-off negotiated contractual changes for two of our PFI contracts and interest charges were £3 million lower.

	Actual	Updated Delivery Plan (mid-point) £m	Variance £m
Scottish Water's Regulated Income & Expenditure Statement			
Total revenue	1308.1	1284.0	24.1
Regulatory operating costs	(388.6)	(393.2)	4.6
PFI operating costs	(171.4)	(178.5)	7.1
Interest charges	(141.6)	(145.1)	3.5
Costs before items subject to LTNC	(701.6)	(716.7)	15.1
Total available to support investment before LTNC items	606.5	567.3	39.2
Responsive repair & refurbishment costs	(215.0)	(215.0)	-
Developer contributions	(30.0)	(30.0)	-
Tax paid	(25.0)	(25.0)	-
Total LTNC Items	(270.0)	(270.0)	-
Surplus in year after charging LTNC items	336.5	297.3	39.2

¹⁴ LTNC Items - Responsive repair and refurbishment costs, developer contributions and tax.

Responsive repair and refurbishment expenditure is difficult to predict over a short-term time horizon as there can be significant variability in the annual level of expenditure associated with, for example, significant water main bursts or collapsed sewers. During 2021/22 we have developed our processes to enhance cost capture. These changes have informed our decision to increase the forecast overall responsive repair and refurbishment costs with the offset being in regulated operating costs. The rebased annual normative charge of £215 million (original: £185 million) has therefore been applied. Actual expenditure in the year was £152 million. Developer contributions and taxation may also experience significant annual variability and hence we have adopted a similar normative charge approach in these areas for the same reason with normative charges of £30 million for developer contributions and £25 million for tax paid being applied. In 2021/22 actual expenditure was £25 million and £15 million respectively. So, total actual expenditure on LTNC items in the year was £191 million, £79 million lower than the LTNC but over the 2021-27 period we expect the normative charge to balance with actual expenditure incurred.

The table opposite reconciles the regulatory surplus, before LTNC items, from the table above to the consolidated surplus before tax as per the financial statements for the year to 31 March 2022.

Scottish Water's Reconciliation to consolidated Group surplus before tax	2021/22 £m
Regulated funding for planned investment before LTNC adjustments (per table above)	606.5
Deduct actual expenditure on LTNC items	(191.1)
Add back actual tax paid	14.6
Add non-core and subsidiaries surplus before tax	20.8
Less depreciation & amortisation charges	(283.2)
Less SW cloud computing arrangement costs associated with the IFRIC agenda decision	(23.8)
Add back developer contributions less infrastructure charge income awaiting investment	5.6
Planned maintenance costs less refurbishment costs capitalised	(17.8)
Group Retirement benefit obligation (*):	
Operating costs	(42.8)
Finance costs	(4.9)
IFRIC 12 PFI finance lease costs adjustment	6.9
Group Surplus Before Tax per statutory accounts	90.8

Financial Summary of Year-on-Year Performance

Revenue

Revenue for the year increased £19 million or 1.5% to £1,285 million (2021: £1,266 million¹⁵) and is analysed by category in the table opposite. The increase reflects an average charge increase of 0.9%¹⁶ for household and 2.5% for wholesale customers, and stronger household billings driven by new connections to services.

	Notes	2021/22 £m	2020/21 £m	Change £m
Regulated revenue				
Household		939.3	920.9	18.4
Wholesale		333.5	332.8	0.7
Other		12.5	12.5	-
Total regulated revenue	3	1,285.3	1,266.2	19.1

Investment

Our planned investment on a regulatory accounting basis in the year was £623 million¹⁷ which was at the upper end of our forecast range of £570 million to £650 million as outlined in our original Delivery Plan.

On a statutory accounting basis investment was £581 million which was £160 million higher than last year. The table opposite reconciles investment on a gross regulatory accounting basis with investment as stated in the statutory accounts.

	March 2022 £m
Investment	
Investment on a regulatory accounting basis	622.9
Less planned repairs charged to the Income Statement	-38.1
Add refurbishment costs capitalised	20.3
Add developer contributions	24.6
Less investment funded from infrastructure charges, refund associated with Dalmuir PFI and insurance recoveries	-24.6
Less cloud-based projects charged to income statement	-23.8
Company capital additions per note 9 to the financial statements	581.3

¹⁵ 2021 revenue figures exclude infrastructure charges income and disposal proceeds.

¹⁶ Customers who paid full charges had increases of 2.5% but this was offset by the expansion in the Water Charge Reduction Scheme for 446,000 customers which increased their reduction from 25% to 35%.

¹⁷ Total investment referred to on page 7 includes responsive repair and refurbishment and developer contributions.

Operating, PFI and Depreciation

Total operating costs decreased £3 million to £1,051 million (2021 restated : £1,054 million) in the year.

Operating and repair costs reduced by £29 million, or 4.7%, to £582 million (2021 restated: £611 million). The reduction in the year is mainly as a consequence of costs in 2020/21 being significantly impacted by the pandemic and weather-related incidents, especially following the severe winter weather experienced in January and February of 2021 of approximately £13 million. Power costs year-on-year were approximately £7 million lower reflecting our procurement strategy to secure our energy supply prior to the start of the financial year.

PFI operating costs increased £2 million, or 1.1%, to £152 million (2021 restated: £150 million). The increase is attributable to contract indexation which have been heavily impacted by gas prices. However, the increases have been offset by one-off negotiated contractual changes for two of our PFI contracts.

Total depreciation and amortisation charges, net of the gain on sale from asset disposals, increased by £7 million to £275 million (2021 restated: £268 million) due to the profile of capital investment and completed projects coming into beneficial use.

In April 2021 the IFRS Interpretations Committee published an agenda decision on the treatment of cloud computing arrangement costs. This resulted in a change to the accounting treatment of cloud-based software applications which required restatement of results for 2020/21 (see note 30 to the financial statements). The change increased costs, in net terms, by £9 million in the year (2021: a reduction of £0.2 million).

Finance costs

Net interest payable in 2021/22 decreased by £1 million to £142 million.

As at 31 March 2022, the weighted average interest cost of the outstanding long-term debt within Scottish Water's regulated business reduced to 3.2% (2021: 3.4%). This was due to the repayment of £125 million loans with a weighted average interest rate of 5.5% offset by £360 million new and replacement loans drawn down during the year from the Scottish Government with a weighted average interest rate of 1.2%. Net new loans during the year were £50 million higher than forecast in our Delivery Plan reflecting accelerated borrowing provided by the Scottish Government. It is anticipated that new borrowing will be reduced by this amount in the latter years of the 2021-27 regulatory period.



Cash balances

Cash balances within Scottish Water increased by £87 million to £516 million due to strong financial performance in the year (£39 million greater than plan), the ending of the temporary relaxation of prepaid wholesale charges introduced as part of the Covid-19 market measures for Licensed Providers and £50 million additional borrowing received from the Scottish Government to finance our investment programme.

Any large infrastructure organisation that provides an essential service requires significant access to cash to maintain its activities and to respond to unforeseen events. Our cash balances each year are largely a function of when we borrow from the Scottish Government relative to when we invest and, unlike similar infrastructure businesses, we do not have access to any other form of credit facilities.

Before the pandemic our risk appetite determined that Scottish Water (regulated business) should always hold a minimum cash balance of £100 million. However, considering the increased risks faced as a consequence of the pandemic, we increased this to holding a minimum £200 million cash balance, which is equivalent to approximately eight weeks expenditure. Given the current uncertain economic environment we will continue to hold a £200 million minimum cash balance. The balance of our cash has been committed for future investment delivery.

Prospects

We remain committed to taking all possible steps to drive for further efficiency to reduce our expenditure and our target is to achieve, at least, a 1% year-on-year real reduction (CPI-1%) in line with the challenging target set in the Final Determination.

In our 2021 Delivery Plan we outlined how we would deliver great value and financial sustainability for our customers and presented our forecast income and expenditure for the 2021/22 and 2022/23 financial years. Our latest forecast of the contribution to support planned investment for 2022/23 is a range of £300 million to £340 million after adjusting for Long Term Normative Charges and reflecting the latest view on inflation. This is lower than the level forecast in our 2021 Interim Performance and Prospects Report (£335 million to £395 million) due mainly to:

- Lower forecast revenue due to price increases being held in line with inflation as at October 2021 (4.2%) rather than increasing at CPI+2%; and
- Higher forecast operating and PFI costs as a consequence of higher inflation.



Business Stream

Overview

Revenue from this business segment totalled £629 million (2021: £574 million) (per note 3 of the financial statements). This represents 32.0% (2021: 30.4%) of the group revenue, before intercompany eliminations. The operating profit within this segment was £12.4 million (2021 restated: £17.7 million loss).

Strategic and Financial Framework

Business Stream is one of the Licensed Providers operating in the Scottish retail market and one of the retailers licensed to operate in the English market. The commercial strategy is to retain and grow market share by exploring options that will provide scale and add value through a combination of acquisition and organic growth. With the aim of being the water and waste water services supplier of choice for businesses by helping customers find the solution that's right for them, Business Stream offers additional services including water efficiency, new connections support, trade effluent consultancy and automated meter reading.

Within the Scottish Water group, the licensed and commercial activities are generally self-financing with any profits generated being retained and invested in future developments of the business. Where additional financing is required to fund operations and planned expansion, Business Stream is limited to borrowing from Scottish Water Business Stream Holdings, subject to the appropriate board approvals.

Performance Review

Business Stream's priority over the last year has been to provide on-going support to its customers and people in response to the Covid-19 pandemic and current economic climate. Despite the challenging external environment, Business Stream has continued to grow its market share, retaining its position as one of the largest retailers in the UK water market, and delivered strong results against its key business performance targets. Business Stream is part way through the delivery of an ambitious transformation programme to help ensure it can continue to deliver an excellent customer service to its growing customer base.

While the Covid-19 pandemic and containment measures have inevitably had a financial impact over the last two years, Business Stream's Balance Sheet remains strong, with net assets of £101 million at the end of March 2022.

Financial Performance

Business Stream reported a profit before tax for the year of £13 million (2020/21 restated: loss of £17 million), reflecting the partial release of Covid-19 bad debt provisions, a stronger customer base in England, and synergies realised from the acquisitions of the Southern Water and Yorkshire Water customer books.

Cash balances at 31 March 2022 were £73 million (2021: £70 million). Business Stream group cash, including Scottish Water Business Stream Holdings, increased by £2 million in the period to £97 million.

Prospects

As a water retailer, Business Stream's role is to deliver great service for its customers and to deliver a positive return for its shareholders. Business Stream is also committed to making a positive contribution to the environment and society as a whole. To help achieve this ambition, the company launched its vision to Make a Positive Difference to its customers, its people, the environment and local communities in 2019.

Since then the company has launched over 25 new initiatives to help bring its vision to life, including establishing partnerships with Business in the Community (BiTC), providing support to charities through the BiTC Business Response Network; introducing new initiatives to help support the health and wellbeing of its colleagues; sponsoring a tree planting programme to deliver 10,000 additional trees in Scotland; and launching and achieving a 20% carbon reduction pledge in the past 12 months.

Business Stream is also in the process of delivering a multi-million pound transformation programme designed to transform its systems, processes and the way it works so that it can continue to provide a market-leading experience for its customers. This will include replacing ageing technology with a scalable, resilient, modern technology platform that will directly benefit its customers, improve operational efficiency and reduce cost to serve.

Non-Regulated Businesses

Our non-regulated business activities are governed and monitored within Scottish Water Horizons Holdings and mainly operate through Scottish Water Horizons and the North-East Scotland PFI waste water treatment operations.

Revenue from this business segment totalled £50.0 million (2021: £49.8million) (per note 3 to the financial statements). This represents 2.5% (2021: 2.6%) of the group revenue, before intercompany eliminations. The operating surplus within this segment was £1.5 million higher than the same period last year at £8.6 million. This reflects £7.6 million operating profit (2021: £7.9 million) from North-East Scotland PFI waste water activities and operating profit from other non-regulated activities of £1.0 million (2021: £0.8 million loss). The profits generated from the other licensed and commercial activities are all retained within the group and invested in the future development of the business.

Investment in the year within Scottish Water Horizons (SWH) totalled £5 million with a focus on low carbon investments. SWH delivered renewable schemes at water and waste water treatment works in Edinburgh, Aberdeen, Cupar and Perth, the latter included the first with battery storage, and a large energy efficiency scheme at Dalmarnock Waste Water Treatment Works. These projects combined will generate up to 9.0GWh of renewable energy per annum and provide over 400 tonnes of carbon savings each year.

The North-East Scotland PFI waste scheme invested in additional centrifuge capacity, installation of dehumidifier biogas treatment and replacement of a CHP engine to increase the generation of energy from bioresource. Nigg Waste Water Treatment Works significantly increased the amount of waste water sludge being processed in the year by accepting sludges that were previously routed to land reclamation. A successful trial in a proprietary methane capture EloVac technology was also completed, with a permanent installation now expected. Photovoltaic panels have been installed at Fraserburgh, increasing renewable energy generation and offsetting imported electricity.

As a consequence of these investments, cash balances within the Horizons group of companies decreased by £2.7 million to £44.1 million.

Financial Performance - Group

Financial Summary

The group surplus before tax increased by £58 million to £91 million (2021 restated: £33 million). Consolidated revenue in the period increased by 4%, or £67 million, to £1,734 million (2021: £1,667 million) reflecting tariff increases effective from 1 April 2021 and increased consumption by businesses as they recover from the Covid-19 pandemic. Associated cost of sales increased by £28 million or 2.2% to £1,303 million (2021 restated: £1,275 million). Administrative costs reduced by £16 million, due mainly to lower costs associated with the pandemic and lower bad debt charges, and net financing costs reduced by £4 million to £161 million.

The results for the period also reflect the initial implementation of the IFRS Interpretations Committee (IFRIC) final agenda decision on cloud computing arrangements. Cloud computing arrangement costs expensed in the year were £28 million (2021: £13 million) with the impact reduced by a £15 million reduction in depreciation charges (2021: £12 million). These costs would have previously been capitalised as IT software and depreciated over their planned economic life. In addition, the income statement and the balance sheet as at 31 March 2021 have been restated to reflect the IFRIC decision (see notes 1.3, 9, 10 and 30 to the financial statements).

In the period, consolidated net debt increased by £143 million to £3,757 million. The increase was driven by net new borrowing in the year of £230 million partially offset by increased cash of £87 million. The movement in cash is summarised below:

	Scottish Water £m	Business Stream group £m	Horizons group £m	Group Total £m
Opening balance at 1 April 2021	428.7	94.9	46.8	570.4
Cash generated / (utilised)	87.2	2.2	(2.7)	86.7
Closing balance at 31 March 2022	515.9	97.1	44.1	657.1

These cash balances have been committed for future investment delivery or are required for working capital.



Taxation

Scottish Water was awarded the Fair Tax Mark for the second time in November 2021. The Fair Tax Mark is reviewed on an annual basis with the expectation it will be awarded in future years demonstrating the continued commitment from Scottish Water to play fair by tax.

The Fair Tax Mark is the world's first independent accreditation for fair responsible tax and it was established in response to widespread public concern about apparent tax avoidance. To meet the criteria set by the Fair Tax Foundation, Scottish Water is transparent about its tax affairs and has demonstrated with the publication of its tax strategy a firm commitment to shun tax avoidance, not take an aggressive interpretation of tax legislation and not use tax havens to secure a tax benefit.

The consolidated tax charge on the income statement to 31 March 2022 was £158 million (2021: £8 million), due primarily to a deferred tax charge of £150 million. The high deferred tax charge is a consequence of the revaluation of the deferred tax balances caused by the increase in the UK's main corporation tax rate from 19% to 25% effective from 1 April 2023. This was announced in the budget on 3 March 2021 and was substantively enacted on the 24 May 2021. Further detail is included in note 8 to the financial statements. As a consequence, the effective tax rate was 174% (2021: 23%).

Other taxes incurred by the group, and included in the cost base, totalled £84.7 million (2021: £86.0 million) and are summarised in the following table:

	March 2022 £m	March 2021 £m
National Insurance	18.9	18.2
Local Authority rates	64.2	66.5
Land fill tax	1.6	1.3
Normalised annual cost	84.7	86.0

Scottish Water is currently appealing the rateable value of its Water Undertaking listing but is unlikely to know the outcome of this until later in 2022.

Group Pension Arrangements

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

Under IAS 19 a snapshot is taken of pension fund assets and liabilities at a specific point in time. Thus, movements in equity markets and discount rates create volatility in the calculation of scheme assets and liabilities. As at 31 March 2022 the gross pension liability decreased by £170 million from £222 million at March 2021 to £52 million. The actuarial movements, net of deferred tax, are presented in the consolidated statement of comprehensive income with further detail in note 8 to the financial statements (on page 167).

Employees who joined Business Stream after December 2016 participate in a defined contribution scheme, administered by Standard Life. All Employees of the North-East Scotland Waste Water PFI also participate in a defined contribution scheme administered by Aviva.

Delivery Plan Update

The key initiatives and change programmes we will deliver over 2021/22 to 2022/23, beyond our transformation planning, are set out in the table opposite.

Strategic Objective	Service Excellence				Beyond Net Zero Emissions		Great Value and Financial Stability		
	Delivering Consistently Excellent Water Supply	Transforming Waste Water Services	Enabling Sustainable and Inclusive Economic Growth	Empowering Customers and Communities	Transforming Our Emissions	Embracing the Circular Economy & Enhancing the Natural Environment	Making Smarter Investment Choices	Transforming How We Work	Financing Our Services
What we are planning to deliver in 2021/22 - 2022/23	<ul style="list-style-type: none"> Deliver SR15 & IR18 investment milestones. Achieve accreditation for our water supply risk management system in 2023. Progress delivery of 4 priority system needs and bring forward appraisals for a minimum of a further 3 in 2021/22. Water Operational Systems Plans for all water treatment works. 	<ul style="list-style-type: none"> Deliver SR15 & IR18 investment milestones. Develop a further 3 drainage partnerships. Develop long-term plans for all waste water catchments by 2023. Expect to appraise UIDs in 23 catchments. Take ownership of Highland PFI assets in 2022 and finalise options for Daldowie PFI. 	<ul style="list-style-type: none"> Take the lead in delivering increased capacity in our existing network infrastructure. Improve our service to developers. 	<ul style="list-style-type: none"> Establish Independent Customer Group by Spring 2021 and develop a national engagement strategy. Transform wholesale service to Licensed Providers. Boost support to vulnerable customers and those most impacted by recurring issues. 	<ul style="list-style-type: none"> Appraise opportunities so we can continue the momentum in reducing our operational emissions in future years. Work with a partner to develop a 240GWh opportunity for new renewables in south-west Scotland on our land. Report on emissions driven by our investment and target opportunities. Commence pilots to improve our land to store carbon. 	<ul style="list-style-type: none"> Establish the biodiversity status of our land and identify projects to support. Pilot improving the community access to 6 popular Scottish Water reservoirs. 	<ul style="list-style-type: none"> Deliver our Asset Management Transformation Routemap. Implement (Summer 2022) portfolio reviews. Implement improvements to our project appraisals including community engagement. Procure contractor partners for a new delivery vehicle in the area of refurbishment and repair work. 	<ul style="list-style-type: none"> Roll out and embed our Scottish Water 'character'. Deliver research and innovation Routemap. Digital investment to continue cyber security focus while providing transformation opportunity. 	<ul style="list-style-type: none"> Target is to achieve, at least, a 1% year-on-year real reduction. Plan to invest between £570m to £650m and £620m to £690m in each of 2021/22 and 2022/23 respectively. Implement a framework to assess, drive improvements, and enable us to report on the delivery value for money achieved for customers.

We will invest in line with the policies we have set out, progressing larger projects through investment appraisals and learning from these experiences.

Performance Targets

Our success measures help us understand where we can make improvements and changes to make sure we continue to provide customers and communities with value and the best service.

The measures are aligned to our three strategic ambitions and have been classified under three headings:

- 'Strategic' for long-term performance trends that are strongly impacted by investment (or the need for it) and the progress of key transformation initiatives
- 'Operational' for where performance is strongly influenced by events and operational activity
- 'Investment' to manage our performance from developing needs through to investment completion

Our targets for these measures for 2022/23 are set out in the table to the opposite.

2022/23 TARGETS	
MEASURE	TARGET
STRATEGIC	
Net Zero Emissions	Net Zero by 2040
Net Zero Emissions - Operational Emissions Benefit (tCO ₂ e)	15,000 – 28,000
OPERATIONAL	
Outcome Performance Assessment for the new Measure (OPA)	395 - 410
Household Customer Experience Measure (hCEM)	85.0 - 87.78
Non-Household Customer Experience Measure (nhCEM)	85.4 - 88.66
Stakeholder & Communities Experience Measure (sCEM)	77.55 - 87.55
Contribution to Investment (from Revenue less broadly recurring costs)	£328m - £368m
Health & Safety (H&S) - RIDDOR Injury Frequency Rate (SW & Contractor)	Zero Harm
INVESTMENT	
Progress to Committed List (PCL)	100% - 110%
Indicator of Progress of Overall Delivery (IPOD)	+/- 3 months
Investment Forecast Accuracy at Commitment (IFAC)	95% - 105%

Note:

All targets are for 2022/23 other than Net Zero Emissions and Health & Safety which are long term. The Net Zero Emissions - Operational Emissions Benefit (tCO₂e) target is cumulative over 2021/22 and 2022/23.

The 'Contribution to Investment' target was set based on our broadly recurring costs increasing by 5% over 2022/23.

OUR APPROACH TO RISK MANAGEMENT

Purpose

Scottish Water operates within a complex and dynamic environment, managing asset intensive infrastructure within a highly regulated industry. Strong and systematic risk management is integral to our activities. It ensures awareness and understanding of the environment in which we operate and the influences, both within and outwith our control, which we need to consider.

Risk management supports the assessment and prioritisation of activities, enabling effective decision-making both on a proactive and reactive basis. It allows continual improvement to better manage our business. We are more likely to achieve, and potentially outperform, our business objectives by reducing negative risks (threats) and maximising positive risks (opportunities).

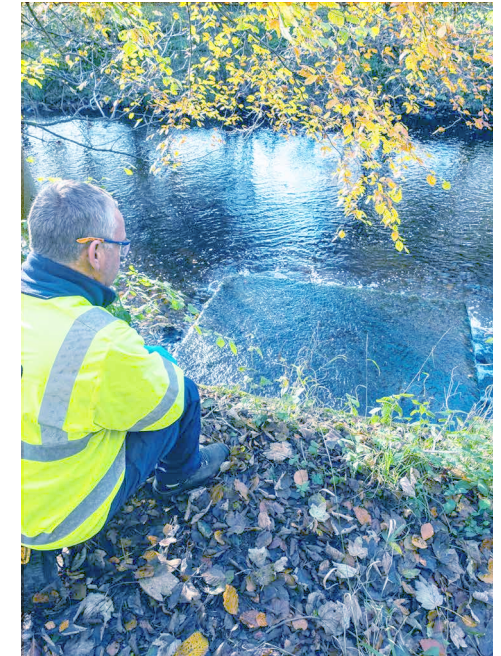
Our approach to risk is championed under three key pillars:



Ensures our people have awareness and understanding of the risks which have the potential to affect our service to customers, our ability to undertake safe working practices and our ability to achieve our key business objectives.

Equips our people to be competent and capable at managing risks effectively.

Ensures our risk management processes underpin the success of our business activities by effectively directing and empowering our people to manage risk.



Risk Governance Framework

Scottish Water's risk management framework encompasses Scottish Water and our subsidiaries: Scottish Water Horizons Limited, Aberdeen Environmental Services Limited and Scottish Water Services (Grampian) Limited.

In line with the Water Services (Governance Code) Directions 2013, the framework excludes operational risk management for Scottish Water Business Stream Limited¹⁸.

Risk Management Control Assurance

Scottish Water operates a governance structure to manage risk. While everyone in the organisation has a responsibility to support the identification, escalation and management of risk, the Scottish Water Board, supported by the Audit & Risk Committee and the Executive Leadership Team, has overall accountability for the risk management framework.

Reviews of the most significant risks are undertaken a minimum of four times per annum, with appropriate mitigation strategies developed, implemented and monitored.

To efficiently and effectively manage opportunities and threats across Scottish Water, our approach is based on the principles of the International Standard 31000 Risk Management (ISO 31000) and is tailored to meet the needs of our business and the environment in which we operate.

Our approach is designed to provide assurance that the opportunities we seek and the threats we face are understood, and that all necessary information is reported to senior managers and escalated to the Executive Leadership Team, Audit & Risk Committee and Board as appropriate to inform business decisions.

Risk Management Approach

Scottish Water has an established Risk Management Policy which was refreshed and approved by the Audit & Risk Committee and the Board in December 2021. The policy is subject to periodic reviews, with the next formal review due in 2024.

The policy sets out a clear and consistent approach to the management of risk and defines our risk appetite. This is enabled by the Corporate Risk Register and supporting risk management processes and activities.

Our risk management framework supports the identification, assessment and effective management of business risks, both individually and in aggregation. The consequence and likelihood of these risks are determined and ranked using a scoring matrix which is aligned to our risk appetite. This ensures a consistent approach is taken when assessing the overall impact to Scottish Water and our customers.

Culture

We recognise that successful risk management is dependent on having an effective culture within Scottish Water, which encompasses the knowledge, experience, beliefs and attitudes of our people.

We aim to continually cultivate a risk-aware culture by promoting a consistent tone from the top, cascaded throughout the business. We do this by outlining clear responsibilities and accountabilities for those managing risk, and recognising individuals who manage risk effectively, as well as sharing, reporting and escalating risk information in a timely manner.

Scottish Water's Character recognises our requirement to maintain and continue to build on our healthy and supportive risk culture.

Risk Appetite

The level of risk we are willing to accept in the pursuit of our business objectives is reviewed and approved by the Board in advance of and during each regulatory period, or where there is a material change to the operating environment.

We consider risks aligned to five Risk Appetite Perspectives: 'Managing our Assets', 'Working with People', 'Managing External Influences', 'Developing the Business' and 'Scottish Water Subsidiaries'. We have established Risk Appetite Statements aligned to these perspectives for key business areas.

¹⁸ The Board of Scottish Water Business Stream Holdings Limited oversees the financing risks associated with Business Stream, while Business Stream's Board is responsible for its own risk management

Underpinning each statement is a series of measurable Risk Appetite Definitions. These assist in providing a view as to whether we are operating within our appetite, or whether additional risk mitigation may be required.

These metrics are routinely reviewed by the Corporate Risk Team and risk owners and are incorporated into bi-annual reports to the Executive Leadership Team, Audit & Risk Committee and the Board. The appropriateness and effectiveness of mitigating actions is determined in accordance with the risk appetite.

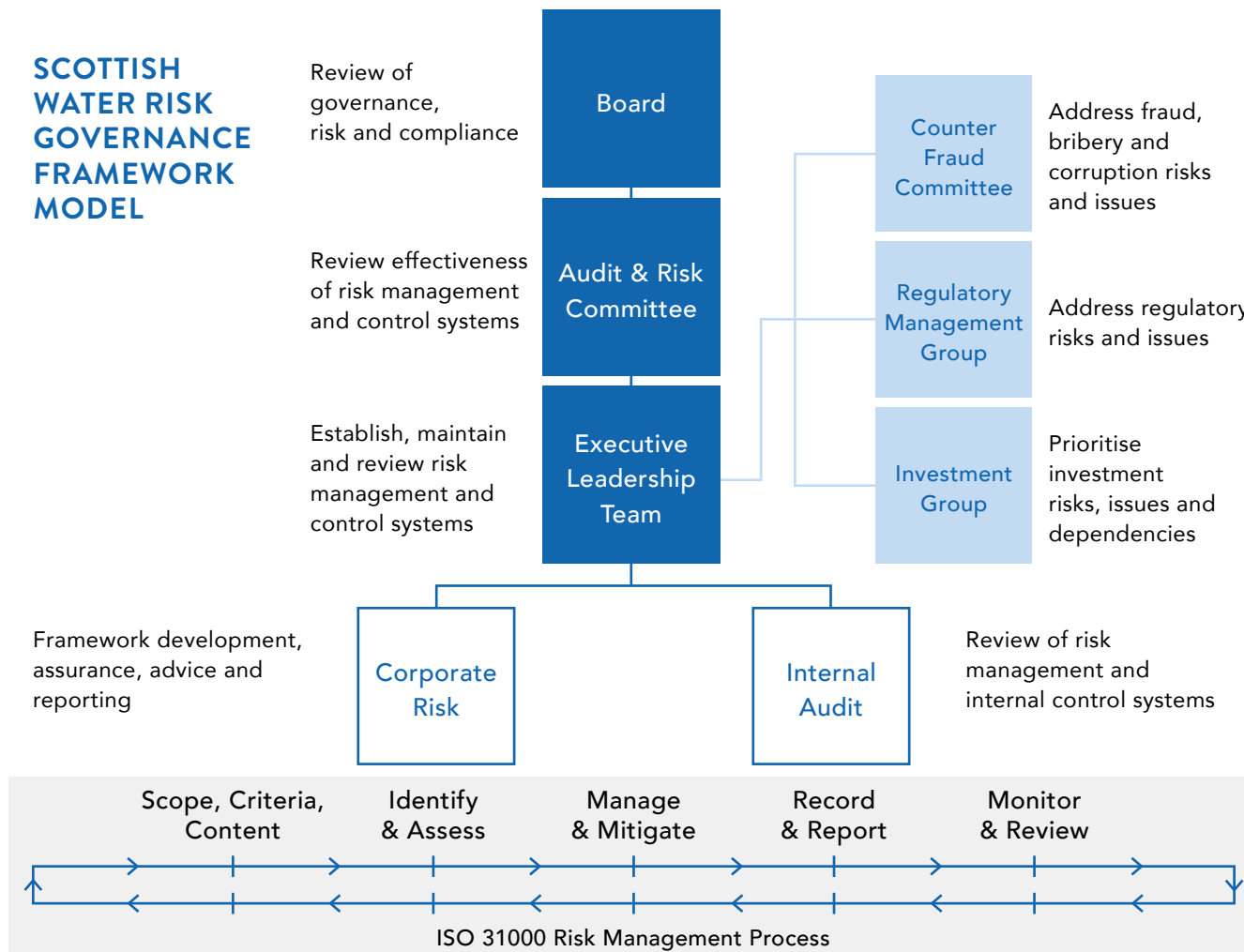
Board

The Board has overall responsibility for reviewing governance, risk and compliance. The Board receives four risk reports per year, considering principal risks and uncertainties and their mitigating actions. The Board also undertakes an annual horizon scanning exercise of the risk environment.

Audit & Risk Committee

The Audit & Risk Committee has responsibility for the risk management framework on behalf of the Board, reviewing the effectiveness of risk management and supporting control systems.

SCOTTISH WATER RISK GOVERNANCE FRAMEWORK MODEL



Executive Leadership Team

The Executive Leadership Team is responsible for establishing, maintaining and reviewing risk management and supporting control systems.

The Audit & Risk Committee and Executive Leadership Team receive risk reports aligned with our Board reporting framework, supplemented by risk spotlight reports as required.

Executive sub-committees assist with oversight of specific risk areas: the Counter Fraud Committee which meets quarterly to address fraud and corruption risks and issues; the Regulatory Management Group which meets monthly to address regulatory risks and issues; and the Investment Group which also meets monthly to address investment risks, issues and dependencies.

Corporate Risk

Scottish Water has a Corporate Risk Function. This is headed by a General Manager reporting to the Strategy & Commercial Director, who leads and manages the risk management framework and processes and is responsible for risk reporting and advice to the Executive Leadership Team, Audit & Risk Committee and the Board.

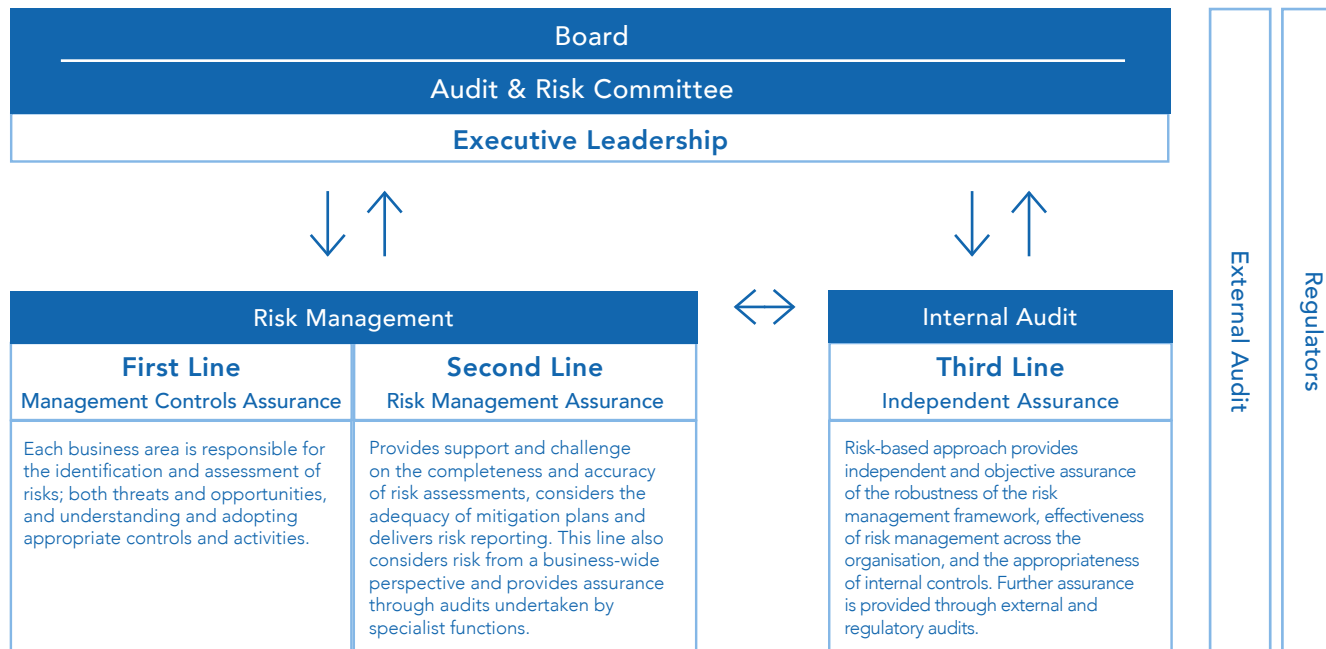
Audit

In the context of risk management, a range of audit activity is undertaken by teams across the business to provide assurance on risk controls. This is supplemented by internal and external audits and escalation processes, including an externally supported whistleblowing facility.

Risk Assurance Effectiveness

Scottish Water operates a three lines model with clearly defined roles and responsibilities. This model ensures the effectiveness of the risk management framework by providing the key governance groups with appropriate assessment, monitoring and assurance at three different points. The model below further illustrates this process.

SCOTTISH WATER THREE LINES MODEL



Principal Risks and Uncertainties

At the time of this report, the Board has carried out a robust assessment of the principal risks and uncertainties facing Scottish Water and its subsidiaries.

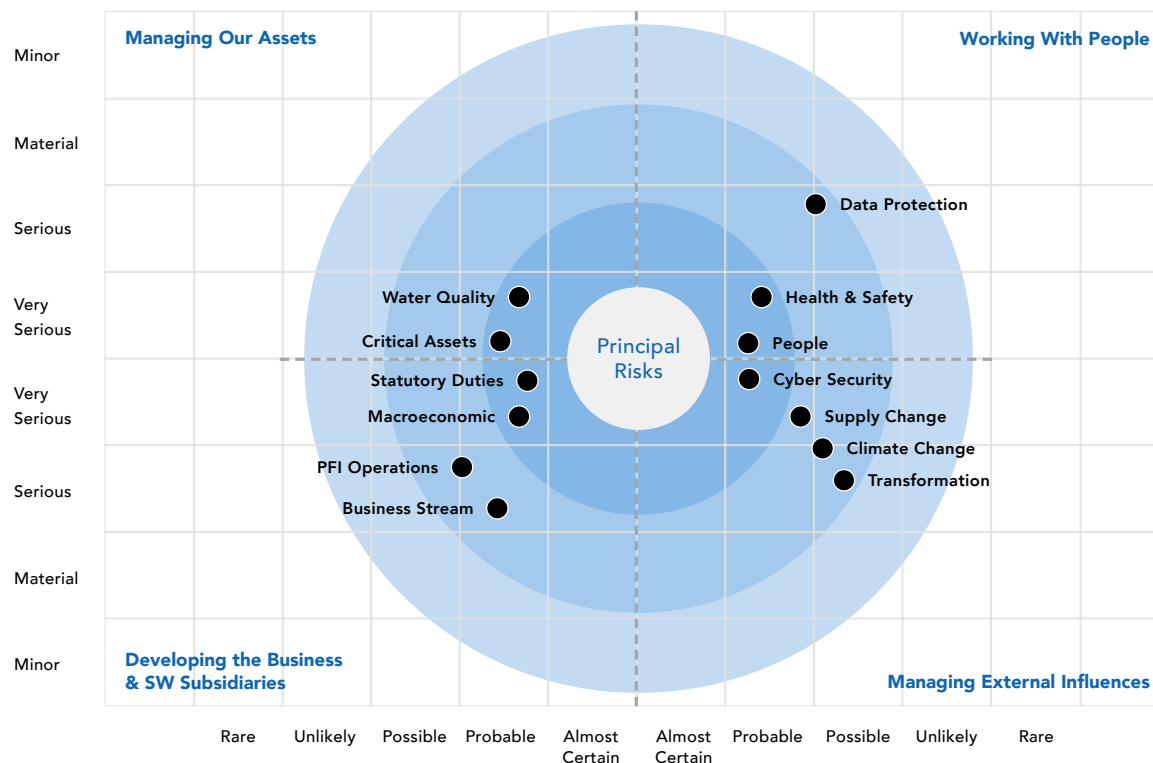
The assessment embraces quantitative stress-testing; including scenario modelling, and qualitative scenario testing incorporating reverse stress-testing. The risks identified are those we consider to be the most material to our business and our performance. Also included are those which could threaten our business model, future performance within our regulatory settlement, and short and long-term financing of Scottish Water.

Our principal risks are detailed via the menu links on page 100. These centre around: delivering our statutory duties; the criticality of our national infrastructure; the importance of our people, including capacity, retention and recruitment, and health and safety in our service delivery.

External threats include cyber security and climate change. We acknowledge the impact of these risks can range in scale and severity, for example significant storm events, which are relatively infrequent (although are becoming more regular), to recurrent weather impacts. Both aspects of these risks are considered and actively mitigated.

Risks also exist in the wider economic environment, including legacy impacts from Covid-19, as well as ongoing influences from geopolitics.

The risk radar below provides a visual representation of the relative likelihood and consequence of each of the principal risks and is grouped by our risk appetite perspectives. The risk radar diagram illustrates, in relative terms, the greater the likelihood and consequence of the risk, then the closer the risk is to the centre of the diagram.



Emerging Risks

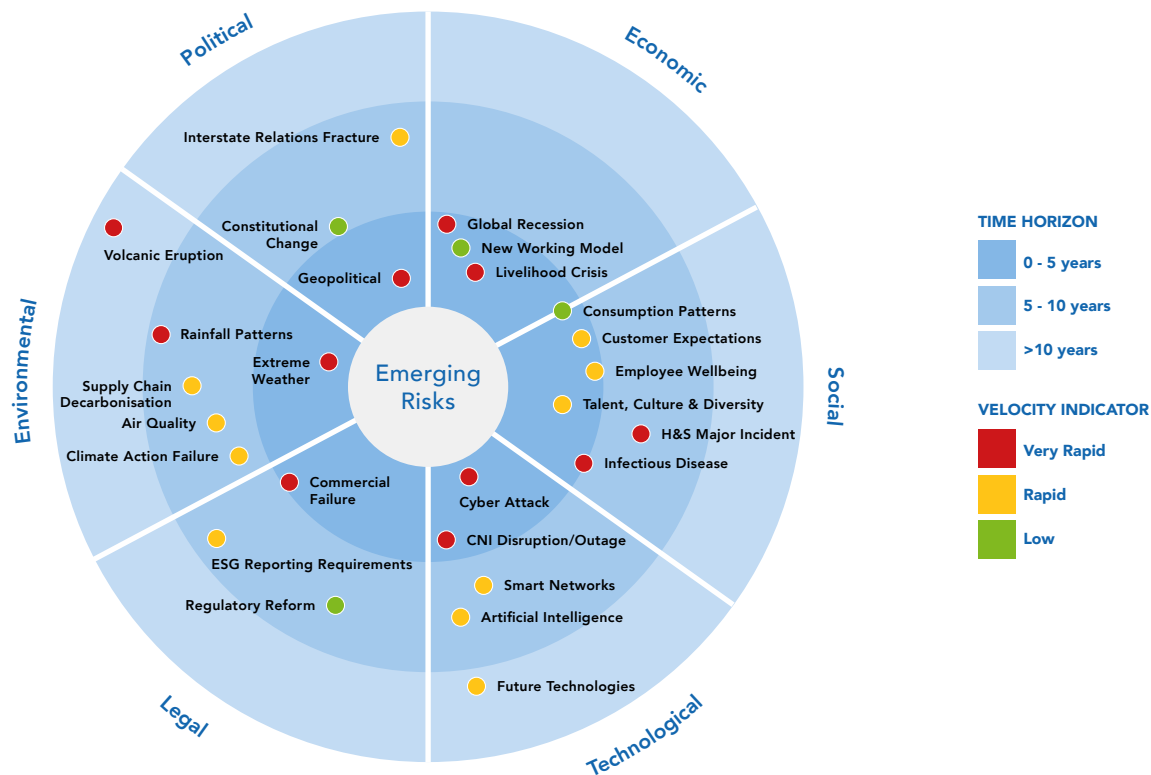
We define emerging risks as future events which present uncertainty and are challenging to fully assess due to lack of information and changing or unpredictable environments.

We undertake regular horizon scanning to monitor both the internal and external business environment, to help identify and review new and emerging risks.

These risks are more likely to have a longer-term impact, however there is the potential for the velocity (speed at which risks could impact the business) to significantly increase within a shorter time frame and affect the performance of Scottish Water. As such, these are monitored and reported a minimum of four times per annum through our existing risk processes and supplemented by an annual Board Horizon Scanning review.

The emerging risk radar opposite provides a visual representation of key emerging risks pertaining to our principal risks and uncertainties, over three time horizons with potential velocity indicators.

We also monitor emerging risks which can impact areas wider than our existing principal risks and uncertainties, such as citizen journalism, governance and corporate reporting. In the wider operating environment; potential impacts from space weather and space debris on our activities including telecommunications, and environmental impact from contaminants of emerging concern and potential loss of biosolid disposal routes.



Information on the key emerging risks with links to our principal risks and uncertainties, can be viewed via the menu links opposite.

Our principal risks are grouped within six key risk themes, and a fuller description of each risk is also provided using the menu opposite. This section also considers the movement across 2021/22, the outlook concerning emerging threats and opportunities, alongside Scottish Water's risk appetite position and key mitigations being undertaken.

In addition to the principal risks and uncertainties detailed, we also actively manage several other notable high consequence but lower likelihood risks. These include operational risks arising from key dependencies on third parties, for example electricity providers in the event of a partial or national power outage. Other high consequence lower likelihood risks, with reputational and financial impacts, can arise from damage by Scottish Water to critical national infrastructure managed by third parties, for example oil/gas transmission pipes and/or railway networks.

Additionally, we manage risk to revenue, risk of water shortage, evolving regulatory processes and risks arising from contractors not fulfilling their obligations/liabilities.

Principal Risks and Uncertainties Key Themes



- Business Financing >
- People, Wellbeing & Health & Safety >
- Cyber, Data & Information >
- Supply >
- Business Resilience >
- Developing the Business >



GOING CONCERN AND VIABILITY STATEMENTS

Members of Scottish Water's Board have concluded that it is appropriate to adopt a going concern basis in preparing the financial statements. The going concern basis confirms there are adequate resources to remain in operation for at least one year from the date the financial statements are signed.

The viability statement, required under the 2018 UK Corporate Governance Code, takes a longer-term perspective of the group's operational sustainability.

Going Concern

Scottish Water's business model, activities and the factors that could impact on its future development and performance are described in the strategic report on pages 22 to 23. The principal risks and uncertainties are described on pages 103 to 108.

Scottish Water operates under an annual borrowing limit set by the Scottish Government. The annual borrowing limit controls the amount by which Scottish Water can increase its externally sourced finance. In addition, Scottish Water's charging structure is reviewed through a regulatory process and charges are approved annually by the WICS.

As at 31 March 2022, Government loans totalled £4.4 billion and Scottish Water group held cash and cash equivalents of £657.1 million.

In considering the basis of accounting, cash flow forecasts have been prepared for a period of at least 12 months from the date of approval of these financial statements



which consider various scenarios, taking into consideration severe but plausible impact downside risks. These forecasts include the assessment of the group's strategic and financial frameworks, including the borrowing limit, operational positions and the level of the capital investment programme. Under all the scenarios, Scottish Water will be able to operate within its available facilities.

The Members, taking all relevant factors into account, consider Scottish Water will have adequate resources to continue in operational existence for the next 12 months. Accordingly, the accounts continue to be prepared on a going concern basis.

Viability Statement

In accordance with provision C.2.2 of the UK Corporate Governance Code, the Members have assessed the prospects of the group over a longer period than the 12 months required by the “Going Concern” provision. The Members consider a five-year period is appropriate because it is consistent with the period covered by the Final Determination published by the WICS in December 2020 which ensures sufficient funding for the core of the group’s activities to March 2027. Consequently, Members confirm they have a reasonable expectation the group will be able to continue in operation and meet its financial obligations as they fall due over the next five years to March 2027.

In making their assessment, the Members considered the resilience of the group, taking account of its strategic and financial frameworks, including the borrowing limit, operational positions and the level of the capital investment programme. They considered the potential impacts, in severe but reasonable scenarios, of the principal risks, set out on page 103, and the probable degree of effectiveness of current and available mitigating actions.

The key processes used by Members for their assessment are summarised below:

The business and strategic planning processes

cover the regulatory period to March 2027, based on key assumptions in respect of the funding of the business. In December 2020, the WICS published their Final Determination for the 2021-27 period. In addition, Scottish Water published its 25-year Strategic Plan for the period to 2045. Business planning is a continual process which forecasts the performance and liquidity of the group over the regulatory period but with an increased focus over the next two years. These forecasts are published within our interim and full year Annual Report & Accounts: Performance and Prospects, set out on page 87. The planning process considers base, downside and severe downside financial and economic scenarios.

Quantitative stress and scenario testing which consider the primary individual and combined quantitative risks relating to liquidity.

Qualitative scenario testing which gives a qualitative understanding of plausible but severe risk scenarios which could threaten the viability of the group and informs related management actions. The scenarios tested are based on the principal risks and include widespread contamination of water supply giving rise to emergency response and recovery, a critical infrastructure breakdown and cyber-attack.

In conclusion for this assessment, Members have assessed the prospects and viability of the group over a five-year period to March 2027.



PRINCIPAL RISKS & UNCERTAINTIES - BUSINESS FINANCING

▲ Statutory Duties	▲ Macroeconomic	▲ PFI Operations	▶ Business Stream
<p>Risk Description Risk of being unable to access full regulatory financing for 2021-27 reducing our ability to deliver the Ministerial Objectives, increasing the prospect of service deterioration and/or enforcement action.</p> <p>Risk Appetite We will always have sufficient financing through revenue and borrowing in order to undertake our activities.</p> <p>We should always have immediate access to a minimum of approximately eight weeks of operating cash to the regulated business from the group (excluding Business Stream) to enable us to protect the organisation from unplanned shocks and potential shortfalls in revenue.</p>	<p>Risk Description Risk of prolonged financial uncertainty due to macroeconomic volatility.</p> <p>Risk Appetite We will always have sufficient financing through revenue and borrowing in order to undertake our activities.</p> <p>We should always have immediate access to a minimum of approximately eight weeks of operating cash to the regulated business from the group (excluding Business Stream) to enable us to protect the organisation from unplanned shocks and potential shortfalls in revenue.</p>	<p>Risk Description Financial and operational risk should a PFI plant or operations fail to deliver in accordance with the contract terms.</p> <p>Risk Appetite Scottish Water seeks to deliver services in an efficient and cost-effective manner including via a number of PFI waste water contracts.</p>	<p>Risk Description Risk of reducing value of the business and increased demand on Scottish Water Group cash due to competitive market conditions and complex operating environments.</p> <p>Risk Appetite Business Stream will maintain a financially viable retail business.</p>
Key Mitigations: Statutory Duties	Key Mitigations: Macroeconomic	Key Mitigations: PFI Operations	Key Mitigations: Business Stream
<ul style="list-style-type: none"> Identify and understand external financial pressures influencing customers and Scottish Water costs. Work with the Scottish Government to determine how financing may be secured if it's not feasible to increase charges to the extent envisaged in WICS final determination. Monitor and manage asset performance and understand impacts should investment require to be delayed. Continue to develop and mature appropriate evidence to inform future price positions. 	<ul style="list-style-type: none"> Monitor UK & Scottish Government budget announcements and analyse impacts. Ensure modelling remains up to date with current economic forecasts. Maintain communications with CoSLA, Councils, and Licensed Providers and Scottish Government. 	<ul style="list-style-type: none"> Maintain ongoing strong relationships with PFI companies. Monitor and manage PFI company performance. Ongoing review of contingency plans for both the financing and operation of these contracts. 	<ul style="list-style-type: none"> Continue transformation of customer and cost base and focus on cash management. Undertake improvements to market customer data sets and payment arrangements. Continue transformation of customer service and cost base. Identify and target acquisition of customers, for future growth.
Emerging Threats & Opportunities		KEY: (+-) Opportunity/Threat (+) Opportunity (-) Threat	
<p>- Livelihood Crisis - natural disasters, pandemics, economic or social upheavals, wars and conflicts can result in an impact to incomes, cost of living, assets and the environment.</p>	<p>- Global Recession - the world economy has had four recessions over the past seven decades. The current economic environment could see GDP contraction and weakening of economic activity, further compounding the cost of living and future pricing.</p>	<p>- Commercial Failures - failure of key suppliers, partners, contractors or consultants, particularly during periods of economic volatility.</p>	<p>+ Business Change - we continue to seek opportunities to accelerate key initiatives, to realise delivery of business efficiencies.</p>

PRINCIPAL RISKS & UNCERTAINTIES - PEOPLE, WELLBEING & HEALTH & SAFETY

▲ People

Risk Description Risk arising from failure to attract, develop, reward and retain appropriately skilled, engaged and diverse people, and;

Risk that our people do not have sufficient resilience, capacity and / or are not effectively engaged due to the current internal and external environment, impacting our ability to deliver core services and drive transformational change.

Risk Appetite We will ensure a sufficient capacity of engaged, enabled, diverse and energised people to the required areas of the business at the appropriate times, with the required skills and competency. We will provide appropriate support to enable our people to work in a safe, healthy and well manner wherever their work location.

Key Mitigations: People

- Secure appropriate reward framework and policy positioning with Scottish Government.
- Monitor and refresh People policies in line with best practice and manage activities.
- Refresh core reward structure, reflecting need to attract and retain the essential skills and talent.
- Review recruitment processes to enhance talent attraction.
- Maintain regular engagement surveys, adapt improvement action plans as required.
- Build on change capability and adaptive capacity and resilience.
- Continue monitoring of short term and long term absence, supporting and addressing cases as appropriate.
- Review risks related to essential skills and roles which could impact key activities.
- Continue talent identification, with development and succession plans for key roles.
- Refresh a person-centric approach to performance conversations, supporting our people to contribute their best.

▶ Health & Safety

Risk Description Risk arising from our assets, activities and actions resulting in an impact on the health and safety of our people, contractors, supply chain, customers and the public.

Risk Appetite We will ensure the health and safety of our people, contractors, supply chain, customers and the public remains paramount. Our behaviours, activities and assets should therefore not place at risk the health, safety or wellbeing of Scottish Water people, contractors, supply chain, customers and the public.

Key Mitigations: Health & Safety

- Operate detailed Health & Safety Management System and supporting processes.
- Continue to review and progress our Strategic Health & Safety Improvement Plan.
- Ongoing maintenance, maturity and optimisation of process improvements, to further maintain and strengthen our H&S performance.
- Further embed health and safety in our culture and processes via training and awareness raising.
- Complete remaining site risk assessments and continue regular site inspections.
- Investigate all accidents and incidents and track necessary remedial actions, including learnings for continuous improvement.
- Continue to engage with alliances, partners and contractors to share learnings and best practice.
- Maintain regular health and safety reporting to key governance groups.

Emerging Threats & Opportunities

KEY: (+/-) Opportunity/Threat (+) Opportunity (-) Threat

(+/-) Wellbeing - the wellbeing of our people could be impacted as we continue to adapt to changing regulatory approaches across the 2021-27 period. Additionally, our significant programme of transformational change may influence wellbeing.

(-) Future diseases - pandemics or further Covid-19 variants of concern and the indirect consequences of these, including new ways of working, have the potential to impact our employee Safety, Health & Wellbeing.

(-) New Working Model - changes to traditional expectations around working set hours, hybrid working, retiring at a certain age and interrupted education are challenging the future of work.

(+) Talent Management, Culture & Diversity - policies for retaining and attracting skills and knowledge, utilising workspaces, learning and retirement planning, present opportunities for reappraisal, alongside utilising and building on technologies to devise and maintain dynamic ways of connecting and engaging with employees.

(+/-) Water Industry & Wider Supply Chain H&S Incidents - provide learning for continuous improvement, particularly in our operational environment, augmented by partnering with organisations specialising in the psychology of human factors to maintain and enhance our Health & Safety culture.

PRINCIPAL RISKS & UNCERTAINTIES - CYBER, DATA & INFORMATION

Cyber Security

Risk Description Operational, financial and reputational risk from loss of key IT service arising from a deliberate external or internal attack (physical/ virtual).

Risk Appetite Scottish Water seeks to ensure the integrity and security of the IT estate.

Key Mitigations: Cyber Security

- Organisation wide education and awareness programme rolled out.
- Utilise External Expert Vulnerability and Threat Management service.
- Undertake routine security gap analysis; plans in place to further increase maturity level.
- Undertake regular application of security patching.
- Review and test detailed disaster recovery plans.
- Participate in UK & Scottish Government and industry cyber incident exercises.
- Comply with Networks & Information Systems (NIS) Directive and compliance with Scottish Government Public Sector Cyber Resilience Action Plan.
- Retain ISO27001 (Information Security Management) certification for Scottish Water Data Centres.

Data Protection

Risk Description Risk of failure to maintain a suitable and sufficient framework to manage data protection legislative obligations.

Risk Appetite Scottish Water seeks to safeguard customer and employee data by complying with relevant standards.

Key Mitigations: Data Protection

- Continue to review and communicate data protection policies, processes and guidelines in place.
- Ongoing awareness raising of data protection and requirements under the Data Protection Act 2018.
- Maintain corporate privacy notices.
- Review and communication of processes to ensure data breaches are identified, reported and investigated in a timely manner.
- Continue to embed and review practices.

Emerging Threats & Opportunities

KEY: (+-) Opportunity/Threat (+) Opportunity (-) Threat

(-) Cyber-attacks - the UK water industry has not been subject to a notable cyber-attack in 2021/22, however we note the number of attempted and successful domestic and global attacks continues to rise;

- The Scottish Environment Protection Agency (SEPA) was subject to a serious and complex cyber-attack, which impacted data, processes and systems;
- IT Systems were disrupted at several oil companies in Germany, Belgium and the Netherlands impacting terminals storing oil and transport around the world;
- Gas stations across Iran were inoperable which affected the payment system and prevented sales via government-issued cards used to purchase fuel.

(-) Geopolitical Conflicts - such as the military conflict between Russia and Ukraine sees the imposition of escalating economic sanctions against Russia by Western countries, including the UK. Growing tensions give rise to increased risk of cyber-attacks.

(+/-) Smart Networks - enable connected devices to transfer data and capture information which can be analysed to automatically discover trends and needs, thus driving efficiencies through increased automation and machine learning. The growth in digital dependency, alongside learnings from cyber-attacks requires ongoing developments in both information and cyber security.

(+/-) Artificial Intelligence - AI is progressing rapidly and brings benefits such as Speech Interpretation and Recognition Interface (SIRI), self-driving cars, manufacturing robots and social media monitoring. This however raises concerns around data privacy, bias, loss of employee skills, knowledge and trust, should there be lack of transparency with AI adoption, leading to increased dependency on AI stability.

(+/-) Regulatory Reform - potential regulatory changes to GDPR in the near future, following the UK exit from the EU.

PRINCIPAL RISKS & UNCERTAINTIES - SUPPLY

▶ Water Quality

Risk Description Risk of delivery of water to customers which has the potential to impact health or cause significant customer concerns.

Risk Appetite As a water utility company, provision of safe drinking water remains our highest priority.

Key Mitigations: Water Quality

- Ensure skilled and trained employees operate our water assets.
- Undertake routine monitoring of the water in our catchments, and in our treatment and distribution activities.
- Undertake routine testing on water quality, beyond regulatory requirements, to manage drinking water quality and minimise associated risks.
- Direct risk management activities through the Water Supply Risk Management Group including overseeing improvements related to Drinking Water Safety Plans.
- Actively manage emerging themes/concerns via the Water Quality Improvement Group and implement appropriate actions to address these.
- Deliver significant investment to maintain and further improve water quality.
- Ensure management of detailed emergency and business continuity response plans.

▶ Critical Assets

Risk Description Risk to service to customers arising from failure of a critical asset or assets.

Risk Appetite Delivering a continuous service to our customers is paramount.

Key Mitigations: Critical Assets

- Continue to develop detailed knowledge and understanding of our critical assets.
- Undertake operational inspections, maintenance and emergency planning activities to minimise the risk and consequences of failure.
- Identify investment needs for promotion in our future investment programmes
- Meet the requirements of the Network and Information Systems Regulations (NIS) and the Scottish Government Public Sector Action Plan.

Emerging Threats & Opportunities

KEY: (+-) Opportunity/Threat (+) Opportunity (-) Threat

(+) **DWQR Annual Report** - (2020 report year) - showed compliance with water quality standards at 99.937%, demonstrating the continuing high quality of drinking water. Significant investment continues and the report covering 2021 is due for publication in autumn 2022.

(-) **Rainfall Patterns** - as rainfall intensifies, this can lead to air pollution which can significantly affect the water cycle and water sources.

(+/-) **Consumption** - changing water demand patterns driven by increasing societal focus on climate change, and aging population and population migration.

(-) **Volcanic Eruptions** - or other significant ecological events, have the potential to impact water sources across the UK and mainland Europe.

(+) **Best Practice** - BBS EN15975 Security of Drinking Water Supply compliance and certification development activities are underway.

(-) **Extreme Weather** - failure to deal with the impact of extreme and unpredictable weather events such as storms, on our assets and infrastructure.

(-) **Critical National Infrastructure (CNI)** - failure to deal with impacts from extreme weather disruption, cyber-attacks or acts of terrorism on the national electricity transmission system, telecommunications, roads, bridges and pipelines. Requires continued participation in Government and multi-agency CNI disruption reviews and application of learnings to strengthen business response and asset resilience.

PRINCIPAL RISKS & UNCERTAINTIES - BUSINESS RESILIENCE

▲ Climate Change

Risk Description Risk of failure to deal with the impact of extreme and unpredictable weather events on our assets and infrastructure, and; Risk of changes to water resource supply and demand due to climate change.

Risk Appetite As a water utility company, provision of safe drinking water remains our highest priority, and delivering a continuous service to our customers is paramount. Scottish Water seeks to treat and return waste water in a way that does not harm the environment.

Key Mitigations: Climate Change

- Undertake climate change vulnerability assessments
- Update and undertake climate change risk assessments and apply these to service risk assessments.
- Develop adaptation pathways and set out plan.
- Include carbon costing in appraisals.
- Deliver investment in water assets, including 25-year water resource and resilience planning and improved system connectivity, raw water monitoring, catchment management and capability studies.
- Deliver investment in waste water assets, including surface water management plans, treatment capability assessments and improved service resilience through flood protection of assets.

▲ Supply Chain

Risk Description Risk of failure of key suppliers, partners, contractors or consultants and/or unethical supply chain behaviours, and; Risk arising from Covid-19 legacy impacts and geopolitical conflicts on our operations.

Risk Appetite We should always endeavour to have an [ethical], sustainable and resilient supply chain to meet our investment needs..

Key Mitigations: Supply Chain

- Continue to develop and enhance relationships with key partners and suppliers.
- Maintain Supplier Risk Assessments to identify areas of emerging concern, enabling close monitoring and engagement.
- Routinely review Supplier Risk Profiles to monitor financial viability.
- Review and test Business Continuity Plans.

Emerging Threats & Opportunities

KEY: (+/-) Opportunity/Threat (+) Opportunity (-) Threat

(-) Climate Action Failure - reputational risk of not being seen to contribute to the mitigation of climate change via achievement of net zero emissions by 2040.

(+) Best Practice - a number of best practice activities are in place, and consideration of climate change is undertaken for risk and investment decisions. As understanding and approaches to climate change mature, our practices will adapt.

(+/-) Decarbonisation of Supply Chains - opportunities to reduce emissions generated from the upstream supply chain may provide climate change mitigation, however, could also introduce availability and/or cost challenges.

(-) Geopolitical/Interstate relations fracture - impacting availability of key materials and chemicals and/or supply routes.

(-) Macroeconomic - volatility resulting in increased costs across multiple supply chain categories.

PRINCIPAL RISKS & UNCERTAINTIES - DEVELOPING THE BUSINESS

► Transformation

Key Mitigations: Transformation

Risk Description Opportunities arising from the development and implementation of large-scale transformational programme required to shape the business and enable achievement of our ambitions set out within the Strategic Plan - A Sustainable Future Together.

Risk Appetite We will seek to maximise any opportunities and minimise any threats arising from transformational change.

We will explore how we can do things differently in order to create value and enhance sustainability.

- Implement the 'Plan for Transformation' setting out timescales and objectives, updating and refreshing on a regular basis.
- Keep under review the scale of transformational change required to deliver our strategic plan and ambitions.
- Prioritise and sequence the Transformation portfolio of activities reviewing and refining six-monthly.
- Manage business priorities to ensure adequate resource levels.
- Continuously engage with internal and external stakeholders.
- Deliver change programme.
- Undertake regular monitoring of progress.

Emerging Threats & Opportunities

KEY: (+-) Opportunity/Threat (+) Opportunity (-) Threat

(+/-) **Wellbeing** - could be impacted as we progress through our regulatory period 2021-27, involving important changes as we advance through a significant programme of business change.

(+/-) **Future Technologies** - increased automation through transformational activities could impact roles, relations and morale as we focus on delivering associated benefits such as smart networks or artificial intelligence.

(+/-) **New Working Model** - changes to working environments, such as office vs home working presents benefits such as efficiencies and productivity gains and requires dynamic engagement techniques to avoid employees becoming disenfranchised.

(+/-) **Changing Customer Expectations** - arising from perception of key challenges such as climate change and cost of living, requires ongoing, effective engagement and flexibility to adjust plans as appropriate over the coming years.

(+) **Delivering Business Change** - requires a dynamic Transformation routemap to seek opportunities to accelerate key transformational initiatives, to realise delivery of business benefits and efficiencies.



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BOARD MEMBERS

2021/22 BOARD MEMBER BIOGRAPHIES

Executive Members



Douglas Millican, Chief Executive

Douglas has been Chief Executive since 2012 having previously been Finance and Regulation Director since Scottish Water was formed in 2002. He was formerly with East of Scotland Water and, prior to this, he worked with Price Waterhouse and Tycos. Douglas is Chair of World Vision UK. He is a Chartered Accountant with a BCom from the University of Edinburgh and is an Associate Member of the Association of Corporate Treasurers.



Peter Farrer, Chief Operating Officer

Peter was appointed as Chief Operating Officer in 2013 having formerly been Customer Service Delivery Director, General Manager of Asset Planning and Business Performance and General Manager of Operations. Prior to this he held various operational and engineering roles within Scottish Water's predecessor organisations, East of Scotland Water and Lothian Water and Drainage. He has 37 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.



Alan Scott, Strategy & Commercial Director

Alan was appointed Strategy & Commercial Director on 31 January 2022 having served as Scottish Water's Finance Director since he joined in 2013. Alan joined Scottish Water from Balfour Beatty where he was Finance Director of UK Regional Building and Civil Engineering, having previously held the roles of Finance Director and Interim Managing Director of Balfour Beatty Engineering Services. He was Finance Director of Miller Construction for 8 years and has also held Finance Director positions in the oil service industry. He has an MA in Economics and Accounting from Aberdeen University. He qualified as a Chartered Accountant and Insolvency Practitioner with Arthur Andersen where he spent 10 years in the Corporate Recovery Services Team.

Non-executive Members



Dame Susan Rice DBE

Dame Susan was appointed Chair of Scottish Water on 1 June 2015. She is also Chair of the Scottish Fiscal Commission, the Financial Services Culture Board, the North American Income Trust and Senior Independent Director of J Sainsbury Plc. She was a member of the First Minister's Council of Economic Advisors, Managing Director of Lloyds Banking Group Scotland and previously Chief Executive and then Chair of Lloyds TSB Scotland plc. She is also the Chair of Business Stream and has held a range of other senior non-executive appointments, including a 7-year term as a Non-Executive Director of the Bank of England and 11 years as a Non-Executive Director of SSE plc. She currently sits on the Advisory Board of the UK's Place-based Climate Action Network.



Samantha Barber

Samantha Barber has worked at CEO and Board level in both the UK and internationally for over 25 years. She worked in Brussels as a Policy Advisor in the European Parliament for 4 years and was CEO at Scottish Business in the Community for 9 years. Samantha joined the Advisory Board at Scottish Power in 2007 and was appointed to the main Board of Iberdrola in 2008, serving until November 2021. She chaired the Sustainable Development and Governance Committee for over 8 years and served on the Executive Committee. Samantha is currently a Managing Director with Accenture and the European Lead for the Board Effectiveness and Sustainability. She has continuously served on not-for-profit boards since 2000.



Graham Dalton

Graham is a chartered civil engineer and fellow of the Royal Academy of Engineering with 35 years of experience planning, building and operating large scale infrastructure in the UK, Middle East and Far East. From 2016 to 2022 he was Chief Executive of the Defence Infrastructure Organisation responsible for the Defence Estate in the UK and overseas. Previously, he was Chief Executive of the Highways Agency where he built the Agency's capabilities in network operation, asset management and commercial performance before leading the change to a Government-Owned Company - Highways England - in 2015. Graham's earlier career was spent with consulting engineering firm Mouchel, and with contractor Bovis.



Steven Dickson

Steven brings more than 30 years communications, media and digital experience having worked for BT since 1989. Recent roles included leading teams across Europe, Americas and Asia Pacific focusing on global contracts, strategic controls and revenue assurance. He was a member of the leadership team in BT Group Business Services. He is also a member of the National Executive Committee for the Prospect Union, having occupied various executive positions since 2013 and been a senior negotiator on the BT Pay and Reward Committee since 2006. He also served a three-year term on the governance board of BT's pension scheme in 2018.



Iain M Lanaghan

Iain is an experienced Non-Executive Director and former Main Board finance director. He is also a Non-Executive Director and Audit Chair of UK MOD Defence Equipment and Support agency (DE&S) and of the North Sea Transition Authority. His previous Non-Executive Director and Audit Chair roles have included UK National Nuclear Laboratory. Previously, he was Finance Director of FirstGroup plc, Faroe Petroleum plc, PowerGen International and Atlantic Power. He is a member of the Institute of Chartered Accountants of Scotland, having qualified with KPMG in London.



Ken Marnoch

Ken brings 29 years of energy industry experience having worked for Shell since graduating from Heriot-Watt University in 1988. Initially based offshore in the North Sea and onshore in Aberdeen, and subsequently 17 years in assignments overseas. His recent roles include leading regional and country businesses in the Gulf of Mexico, USA and Brunei, South-East Asia focusing on corporate responsibility, safety, bottom line delivery, digitalisation and investment in people. His international career has also included leading Internal Audit, major asset and infrastructure project delivery, strategic planning, managing Government and corporate joint ventures and delivering significant organisational change.



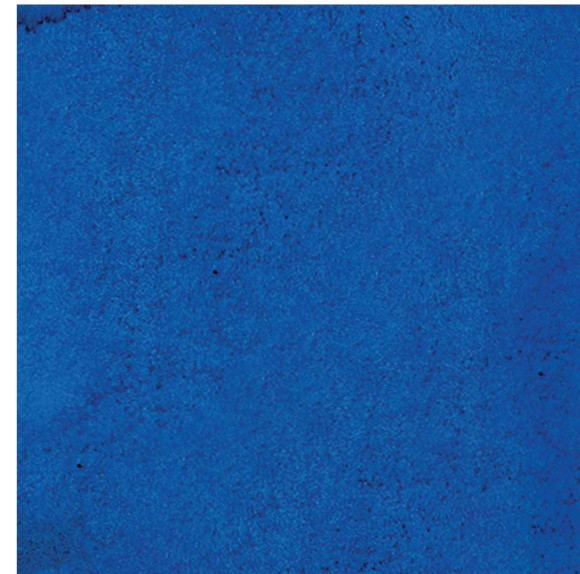
Deirdre Michie OBE

Deirdre was appointed CEO of Offshore Energies UK (OEUK) in May 2015. She has an LLB Hons in Scots Law and has extensive experience as a senior business leader in the global offshore energies industry, both upstream and downstream. As OEUK CEO, she signed the landmark North Sea Transition Deal with the UK government that is helping to deliver the low carbon energy development needed to achieve Net Zero emissions by 2050, while delivering energy security. As CEO, she drove the organisation's scope extension to include hydrogen, carbon capture and offshore wind, as well as oil and gas. Deirdre is currently a Non-Executive Board member of Scottish Water and a Board Member of Opportunity North East. She is also a member of the UK Government's North Sea Transition Forum; HMT's Oil and Gas Industry Fiscal Forum; the Scottish Government's Energy Advisory Board; and the Women's Business Council, a UK Government body focused on increasing women's contribution to economic growth. Deirdre was awarded an OBE for her services to the oil and gas industry in the Queen's Birthday Honours 2018, an Honorary Degree from Robert Gordon University and a fellowship from the North East of Scotland College.



Catriona Schmolke

Catriona is a chartered engineer and hydrogeologist with 36 years in professional services consulting predominantly in the infrastructure and utility markets. A former global Senior Vice President with USA based Jacobs. Her operations career included leadership roles in sustainability, mining, environmental management, utilities, flood risk and nuclear and solid waste disposal. She is a Fellow and Trustee of the Royal Academy of Engineering, where she is also the Vice President. For the University of Newcastle, Catriona is the Chair of the SAgE Advisory Board and the Visiting Professor in Sustainability, Risk and Resilience.



CORPORATE GOVERNANCE REPORT

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 this report and their biographies are set out on pages 110 to 113.

Executive Board appointments are based on merit and candidates will be considered against objective criteria, having due regard for the benefits of diversity on the Board, including gender. Non-executive Board appointments are made by the Public Appointments team of the Scottish Government. That team operates in accordance with the Code of Practice and the Diversity Delivers strategy published by the Ethical Standards Commissioner. Both the Code and the strategy are applicable to all public appointments.

The Board of Scottish Water comprised 11 members: 8 Non-executive Board Members and 3 Executive 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 Board 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 financial year of 2021/22, the Board met on 9 occasions to review Scottish Water's operational and financial performance, business strategy and risk management.

UK Corporate Governance Code

Scottish Water complies with the revised UK Corporate Governance Code published by the Financial Reporting Council (FRC) in July 2018, so far as applicable to its status as a Statutory Public Corporation. As Scottish Water is not a company registered under the Companies Act, the Financial Conduct Authority (FCA) listing rules are not applicable and an Annual Consultative Meeting (ACM) with stakeholders is held in place of an Annual General Meeting. The 2021 ACM was held virtually due to Covid-19 restrictions. The arrangements for appointment and termination of Board Members and their remuneration are derived from the underlying statutory regime and set out in the Members' Remuneration Report. No Senior Independent Director has been appointed as other arrangements are in place to consult with stakeholders. The Audit & Risk Committee Report on pages 118 to 123 covers the appointment of the external auditor.

Board and Committees

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

	Board		Audit Committee		Remuneration Committee	
	Held	Attended	Held	Attended	Held	Attended
Dame Susan Rice	9	9	-	-	-	-
Samantha Barber	9	9	-	-	4	4
James Coyle	9	6	6	5	-	-
Peter Farrer	9	9	-	-	-	-
Iain M Lanaghan	9	9	6	6	-	-
Ken Marnoch	9	8	-	-	4	3
Deirdre Michie	9	9	6	5	-	-
Douglas Millican	9	9	-	-	-	-
Alan Scott	9	9	-	-	-	-
Steven Dickson	9(8*)	8	-	-	4	4
Catriona Schmolke	9(4*)	4	6(2*)	2	-	-
Matt Smith	9(1*)	1	-	-	-	-
Paul Smith	9(3*)	2	6(3*)	3	-	-

Notes:

*Mr Matt Smith's term ended on 30 April 2021

*Mr Paul Smith's term ended on 29 June 2021

*Mr Steven Dickson's term commenced on 1 May 2021

*Mrs Catriona Schmolke's term commenced on 1 November 2021

Audit & Risk Committee

The Audit & Risk Committee reviews the financial reports of Scottish Water and considers the results of the auditor's examination and review of the financial statements. It meets with management and with internal and external auditors to review the effectiveness of internal controls, governance and business risk management. The Chair of the Audit & Risk Committee reports to the Board on internal control and risk management matters following each Audit & Risk Committee meeting. The Committee adheres to the requirements of the Audit and Assurance Committee Handbook. Each year the Committee presents a report of its activities to the Board prior to the Board's consideration of this report.

A more detailed report of the Audit & Risk Committee's activities is provided on pages 118 to 123.

Remuneration Committee

The Remuneration Committee monitors the contract terms, remuneration and other benefits for each of the Executive Members, including performance-related incentive schemes. The Committee has access to external independent advice as it considers appropriate. A more detailed report of the Remuneration Committee's activities is provided on page 124.

Board and Committee Performance

An internal review of Board and Committee effectiveness was undertaken during the financial year of 2021/22 and actions arising from it are being implemented. All actions arising from the external review of Board and Committee effectiveness undertaken in 2020/21 have been 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.

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 Members are:

Douglas Millican Chief Executive

Peter Farrer Chief Operating Officer

Alan Scott Strategy & Commercial Director

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 2021. 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.

Risk Management

Scottish Water operates a systematic approach to managing risk which is detailed more fully in pages 94 to 100. These risk management processes have been in place for the full year under review and up to the date of approval of this report and financial statements.



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.
- Close monitoring undertaken by the Board and management of safety, health and wellbeing issues.

High quality personnel are viewed as an essential part of the control environment. Ethical behaviour is incorporated into conditions of employment. Demanding recruitment criteria, pre-employment vetting and, where required, additional government security checks, combine with

the development and training of our people to support ethical standards.

Control Effectiveness Review

Reviewing control effectiveness is a continuous process throughout the financial 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 independent assessment by audit, and annual statements of assurance from senior management.

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 a Consultation Code setting out how it consults with 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.

External Auditor

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

Independence of External Auditor

The Auditor General for Scotland is responsible to the Scottish Parliament for securing the audit of the financial statements of Scottish Water. The Auditor General for Scotland appointed KPMG LLP as the auditor of Scottish Water for the financial years 2016/17 to 2021/22. In May 2022, KPMG LLP was re-appointed as Scottish Water's auditor for the financial years 2022/23 to 2026/27.

Under the terms of KPMG LLP's appointment, they may not carry out any non-audit work for Scottish Water without the prior approval of Audit Scotland, and must comply with Scottish Water's policy on provision of non-audit services see page 123.

AUDIT & RISK COMMITTEE REPORT



Annual statement by the Chair of the Audit & Risk Committee

I am pleased to present this report covering the role and function of the Group Audit & Risk Committee for the year ended 31 March 2022. I became Chair of the Committee in November 2021, succeeding James Coyle who continued as a Committee Member until his resignation on 31 March 2022. During the year James and I were supported by 3 other Non-executive Members: Deirdre Michie until she stepped down on 31 March 2022 to Chair the Remuneration Committee, Paul Smith until his resignation on 29 June 2021 and Catriona Schmolke following her appointment on 1 November 2021. Graham Dalton, following his appointment on 1 April 2022, will join the Committee during 2022/23.

I have relevant financial experience and my Committee members have been selected with the aim of providing the wide range of financial, governance and commercial expertise necessary to fulfil the Committee's duties and obligations. Emma Campbell, Scottish Water's Group Legal Counsel, is Secretary to the Committee.

Group Audit & Risk Committee Role and Responsibilities

The Group Audit & Risk Committee was established by the Board to support it in its responsibilities for issues of governance, risk and control and associated assurance and assessment through a process of constructive challenge. Although Scottish Water is not a listed company it does adopt and follow, as far as is appropriate, the accounting and disclosure practices of a listed company.

The governance framework adopted by the Committee links the objectives of Scottish Water's business strategy through the stages, outlined below, with the sources of assurance received from senior management and other assurance providers on the operation of key financial and risk management controls.

The Committee's main responsibilities are to oversee and report to the Board on:

- The strategic processes for the assessment of governance, risk and control and their effectiveness;

- The risk management framework, including risk appetite and horizon scanning;
- The accounting policies, the financial statements, principal risks, the interim and full year Annual Report & Accounts: Performance and Prospects reports;
- The planned activity and results of both internal and external audit, including approval of the annual Internal Audit plan and strategy and annual Cost Audit plan;
- The management response to issues identified by internal and external audit activities;
- The effectiveness of the internal control environment;
- Assurances on the corporate governance requirements for the organisation;
- Anti-fraud activities, whistleblowing processes, arrangements for special investigations and activities and reports by the Counter Fraud Committee;

- Scottish Water's arrangements for complying with legislation and Directions issued by the WICS, including the Annual Return;
- The annual plan and report prepared by the Compliance Officer;
- The annual statement published by Scottish Water under the Modern Slavery Act 2015; and
- The annual tax strategy and statement.

The Terms of Reference of the Committee are approved by the Board and, in accordance with the Scottish Government Audit and Assurance Committee Handbook, are reviewed annually by the Committee. The Committee Terms of Reference are available on the Scottish Water website.

Scottish Water's subsidiary, Scottish Water Business Stream Limited (Business Stream) operates as a Licensed Provider, competing with other Licensed Providers in the Scottish and English markets to supply water and waste water retail services to business customers. Business Stream has its own Board of Directors and is operated in accordance with the Governance Code agreed with the Water Industry Commission for Scotland (WICS). The Governance Code sets out the operating regime that Scottish Water and Business Stream must comply with to enable the operation of the licensed retail market. Business Stream has the same Chair as Scottish Water but

has its own independent Board, Audit Committee and management team. Scottish Water exercises governance over Business Stream through Scottish Water Business Stream Holdings Limited (SWBSH) in accordance with the Governance Code. As a consequence of the restrictions within the Governance Code upon disclosure of Business Stream's activities, the Group Audit & Risk Committee is in large part reliant on the Board of Business Stream to provide much of the necessary assurance, with further assurance provided through governance of Business Stream by SWBSH, as detailed below.

Committee Meetings

The Committee meets at least 4 times per year, 2 of which are co-ordinated with external reporting timetables. During 2021/22 the Committee met on 6 occasions, with an extra meeting in June 2021 to review the draft Annual Report & Accounts: Performance and Prospects.

In addition to the Committee members, the Scottish Water Board Chair, Chief Executive, Finance Director, Head of Internal Audit, Group Financial Controller, General Manager Revenue & Risk, Director of Digital and the external audit partner also attended the meetings by invitation. The Committee invites other senior management to present to the Committee on a regular basis on a variety of topics relevant to its work. In line with the Scottish Government's Audit and Assurance Committee Handbook, the Committee

meets in private, excluding any Executive Members, with the external auditor and the Head of Internal Audit at least on an annual basis, or more frequently if required.

The Committee's Activities

The Committee agrees an annual work programme including reports to be received from senior management, Internal Audit and the external auditor during the year. As well as the normal financial reporting activities, the Committee's main activities during the year included the following:

- Reviewing compliance with the 2018 UK Corporate Governance Code;
- Assessment of corporate strategic and operational risks, risk management controls including risk appetite and business culture, risk management and control systems, the monitoring and review thereof, including sources of assurance and associated public reporting covering going concern and future viability;
- Discussing the work, the issues and management actions in Internal Audit reports;
- Outcomes of investigations resulting from fraud allegations, whistleblowing and results from the Audit Scotland National Fraud Initiative;
- Forming its view of the "fair, balanced and understandable" and viability reporting obligations;

- Consideration of Scottish Water's Covid-19 short and medium-term risk assessment;
- Operation of the 2021-27 Capital Investment Value Assurance Framework;
- Update on the refresh of risk management policy, forward planning and risk horizon scanning; and
- Discussing specifically requested papers on benchmarking the approach to corporate risk management, revenue risk, transformation risk, cyber security and NIS compliance and PFI financial health.

Covid-19 Pandemic

- The Committee at its meetings throughout the year considered the risks associated with the Covid-19 pandemic which may have a significant impact on the future finances of the Scottish Water Group beyond 2021/22.
- During 2020/21, the Scottish Water Group agreed funding arrangements for the subsidiary companies to support the liquidity impacts of the Covid-19 pandemic. To date, there has been no requirement to provide any additional funding to Business Stream under these arrangements.
- The Committee will continue to keep the whole Group financial position under active review by monitoring the position in Scottish Water and relying on the SWBSH

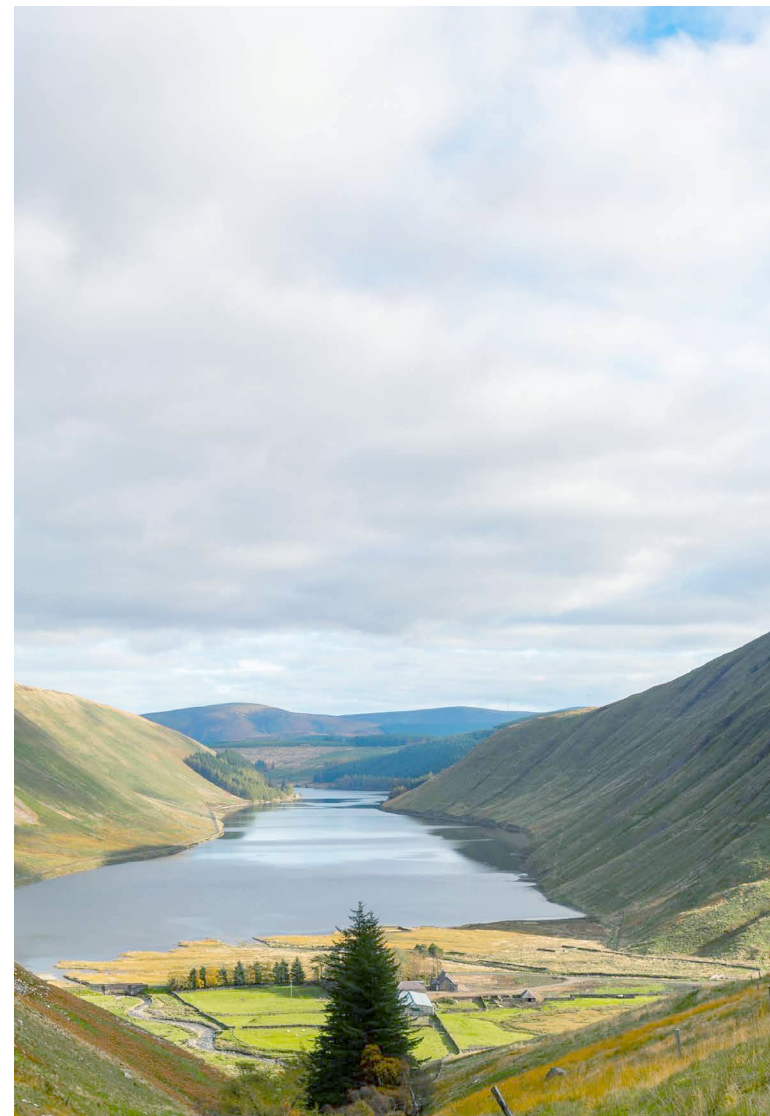
Board to monitor the position in Business Stream with cash updates to the SWBSH Board.

Financial Reporting

To inform the Committee's reports to the Board, the Committee reviewed and considered the following areas in respect of financial reporting and the preparation of the interim Accounts and the Annual Report & Accounts: Performance and Prospects:

- The appropriateness and quality of accounting policies;
- Compliance with financial reporting standards and clarity of associated disclosures; and
- Material areas in which primary judgements have been applied.

To assist in the discharge of its duties the Committee considers reports from the Scottish Water Group Financial Controller and reports from the external auditor on the outcomes of their half-year review of interim financial statements, including confirmation that the Accounts are prepared on a going concern basis.



The Committee also considered and was satisfied with the papers prepared by the Group Financial Controller and the external auditor covering the financial statements for full year 2021/22. These included a section from management supporting the going concern basis which the external auditor confirmed was appropriate. Our view was supported by statutory and regulatory provisions applicable to Scottish Water, namely that:

- The WICS published the Final Determination for 2021-27;
- The Scottish Government want the industry to be financially sustainable for the long term which requires Scottish Water to be adequately funded to meet its future challenges and that Scottish Water can count on those resources being available;
- Under the Water Industry (Scotland) Act 2002, Scottish Water is deemed to have exercised its core functions effectively in making use of those resources to achieve the Ministerial Objectives and do so at the lowest reasonable cost;
- The WICS have a duty, under the same legislation, to ensure Scottish Water's receipts are sufficient to meet the expenditure required for Scottish Water to exercise its core functions; and

- The legislation therefore ensures, as far as possible, that Scottish Water will be sufficiently funded to meet its core functions, including the power to apply to the WICS to increase Scottish Water's charges if there is a material change in Scottish Water's ability to finance expenditure on core functions.

Business Stream's Finance Director, the Chair of its Audit Committee and the external auditor are also in attendance when the Committee reviews the consolidated interim and annual financial statements. The Board of SWBSH receives reports from Business Stream's management covering financial performance and specific risks facing Business Stream.

The primary areas of judgement considered by the Group Audit & Risk Committee in relation to the 2021/22 Accounts were:

- Risks within the corporate risk register which could impact on the financial statements and judgements therein;
- The primary areas of focus included the sensitivities on future household cash collection rates and wholesale revenue collection and the associated level of bad debt provisioning;

- The delivery costs associated with Scottish Water's capital investment programme and the associated expenditure classifications;
- Covid-19 related impacts; and
- The key assumptions associated with determining the actuarial valuation of pension obligations, and the ring-fencing of the Scottish Water element of each pension fund.

After discussion of these with management and the external auditor the Group Audit & Risk Committee was satisfied that the issues raised had been properly dealt with and that appropriate disclosures have been included in the accounts. The external auditor carried out their work using an overall materiality of £14 million, representing 1% of total expenses, incurred in 2020/21 (excluding interest), in the consolidated income statement for 2021/22. However, the Committee agreed with the external auditor that the firm would report any misstatements identified during the audit above £250,000, as well as misstatements below that amount that, in their view, warranted reporting for qualitative reasons.

In addition, the Chief Scientist, the Head of Internal Audit and the Head of Horizons carried out a review to verify that the Annual Report & Accounts 2021/22: Performance and Prospects is fair, balanced and understandable, the

results of which were considered by the Committee prior to recommending Board approval of the Annual Report & Accounts 2021/22: Performance and Prospects.

Consequently, and supported by a comprehensive management and statutory accounts process, with written confirmations provided by senior management on the 'health' of the financial and risk control environment, the Committee and the Board are satisfied that the Annual Report & Accounts 2021/22: Performance and Prospects, taken as a whole, are fair, balanced and understandable, and provide the information necessary to assess Scottish Water's performance, business model and strategy.

Scottish Water's Internal Control and Risk Management Processes

Over the year the Committee received papers from Scottish Water Group Finance and the Group Legal Counsel associated with the 2018 Corporate Governance Code, one of which included a risk management assessment control schedule. This schedule included a detailed 23-point checklist supported by a detailed record of evidence sources and satisfaction ratings of that evidence.

Evidence sources were grouped into 6 categories including risk register and management processes, policy

and procedure processes, assurance statements and independent reviews.

In addition, the Committee reviews the framework of internal controls and the processes by which the organisation's control environment is evaluated. To support this, the Committee receives and considers:

- Reports from Internal Audit on the effectiveness of internal controls and issues requiring improvement, including reported fraud allegations;
- Observations from the external audit on the internal control environment and any specific control issues identified;
- Corporate risk reports summarising key risks in the corporate risk register including mitigating actions, risk trends, and summarising compliance with Scottish Water's risk appetite;
- Reports covering the quantitative and qualitative stress testing of the principal risks facing the Scottish Water group of companies;
- Topical in-depth risk assessments;
- Bi-annual report from the Counter Fraud Committee;

- An annual report from the Compliance Officer;
- An annual corporate governance report;
- An Internal Audit annual opinion and report;
- An annual report on regulatory compliance;
- An annual statement of compliance with the Modern Slavery Act 2015; and
- An annual Tax strategy.

During the year the Committee requested specific reports on cyber security and NIS compliance, Capital Investment Value for Money Assurance Framework, PFI Financial Health and wholesale revenue.

The Committee provides the Board with an annual report on the effectiveness of the internal control framework. To support this, the Committee receives an annual report and opinion from the Head of Internal Audit.

Internal Audit

The Committee approves annually the Internal Audit Charter and the annual Internal Audit plan, with any subsequent changes requiring Committee approval. It also reviews the scope and results of Internal Audit reviews and its effectiveness throughout the year, including implementation of an annual quality improvement action plan following the external quality assessment by the Institute of Internal Auditors in 2019. At each main

Committee meeting reports were received from the Head of Internal Audit. These reports included progress in delivering the Internal Audit plan, audit findings and management action plans to address these, performance in implementing management action plans, fraud allegation investigations and details of relevant Audit Scotland reports. In addition to the private meetings with the Committee members, the Chair of the Audit & Risk Committee also meets the Head of Internal Audit outside of the formal Committee meetings.

External Audit

The Auditor General for Scotland is responsible for the appointment of the Scottish Water external auditor and undertook a robust tender and assessment exercise for Scottish Water and many other public sector organisations, which resulted in the appointment of KPMG as Scottish Water's external auditor for a six-year period from 2016/17 to 2021/22. Following a tender exercise, KPMG has been re-appointed as external auditors for a further five-year period from 2022/23 to 2026/27.

The Committee received from KPMG an audit plan, including their assessment of key risks and confirmation of their independence. Following completion of their interim review and annual audit, the Committee receive an internal control report highlighting any internal control weaknesses and the management actions to address these.

Annually the Committee assess, with input from management, and provide feedback to Audit Scotland on the effectiveness of the external auditor. In addition to the private meetings with the Committee members, the Chair of the Audit & Risk Committee also meets the external audit partner outside of the formal Committee meetings.

Auditor Independence

During 2015/16, the Committee approved a policy on provision of non-audit services to Scottish Water by the firm appointed as external auditor and this was extended to all subsidiaries in 2016/17. The Committee monitors implementation of the policy through receipt of a report every six months, or as required, analysing fees paid for any non-audit work by the external auditor, with additional commentary on assignments and on work carried out or to be done relating to safeguards of independence.

Having considered compliance with our policy, the Committee is satisfied KPMG has remained independent.

Iain M Lanaghan

Chair of the Audit & Risk Committee



REMUNERATION COMMITTEE REPORT

Annual Statement by the Chair of the Remuneration Committee

I am pleased to present the Members' remuneration report for the year ended 31 March 2022, in the preparation of which I am thankful for the support of fellow Remuneration Committee Non-executive members Ken Marnoch and Steven Dickson, and new Committee member Deirdre Michie who joined us on 1 April 2022, having been a Non-executive Board member since December 2017.

The Remuneration Committee meets regularly to consider the remuneration arrangements for Executive Members, and other related remuneration matters, making recommendations to the Board. There were four meetings of the Committee in 2021/22. At each meeting a quorum of independent, Non-executive Members was present. No Executive Member was present during discussions about their own remuneration.

As required, the Committee receives internal advice and information from the Chair of Scottish Water, the Chief Executive, the Director for People, and the Group Legal Counsel. During the year the Remuneration Committee engaged Korn Ferry for the production of market-based pay data on senior executive posts.

We maintain and operate a simple remuneration structure made up of base salary and benefits, an annual out-performance incentive plan (AOIP) and a single long-term incentive plan (LTIP), which provide a clear link between pay and Scottish Water's key strategic priorities.

The key decisions made by the Committee over the 2021/22 period were as follows:

Decisions / remuneration for 2021/22

- Agreeing a base salary increase of £800 with effect from 1 April 2021 for Executive members and the Chief Executive, within the Scottish Government's Public Sector Pay Policy.
- Confirming the 2021/22 AOIP payment calculated at 30.02% of salary out of the 40% maximum opportunity for Executive Members and Chief Executive.

- Confirming the 2015-21 LTIP payment calculated at 60% of salary out of the maximum 60% opportunity for Executive Members and Chief Executive.
- Noting management's proposed salary increases for Scottish Water employees.
- Review of succession planning for posts on the Executive Leadership Team.

Decisions / remuneration for 2022/23

- Setting the structure and performance criteria for the 2022/23 AOIP.
- Commissioning a comparative market review of Executive Member remuneration.

Our Remuneration Policy and our Annual Report on Remuneration is set out on pages 125 to 139.

Samantha Barber

Chair of the Remuneration Committee

MEMBERS' REMUNERATION REPORT

The presentation of this Remuneration Report complies with the HM Treasury Financial Reporting Manual 2021/22 (December 2021) and as far as is appropriate, also adopts the same practice as listed companies even though Scottish Water is not a listed company.

1. Statement of Executive Remuneration Policy

a. General Policy

Scottish Water's purpose is to support a flourishing Scotland through being trusted to care for the water on which Scotland depends. Building on past success, we seek to provide levels of service, out-performance and efficiency which exceed the expectation of customers, regulators and the Scottish Government.

Scottish Water will continue to provide a working environment that matches the expectations placed on our people to deliver best value outcomes in an empowered organisation. 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 the organisation is perceived as a fair employer that encourages excellence, rewards performance and empowers its people while providing scope for personal development.

The overall remuneration policy aims are to:

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

b. Remuneration elements

The 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-driven business, where Executive Members' remuneration should be closely linked to corporate performance and out-performance. The aim is to pay a base salary that is competitive, but appropriate for a public corporation. Incentive pay is earned for exceeding demanding targets in the Delivery Plan, with the required degree of out-performance reviewed on an annual basis.

d. Base Salary

Scottish Water is publicly owned and accountable to the Scottish Parliament and Scottish Ministers. Within the context of public sector ownership, the company 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 subscribes to the remuneration database of Korn Ferry and uses this as required to review the remuneration of comparator organisations and industry in general against its own. This is one of the largest remuneration databases in the UK with each job subjected to the same method of job sizing.

In addition, specific benchmark analysis is carried out approximately every three years. In January 2022 the Remuneration Committee commissioned Korn Ferry to refresh this market analysis against other UK water companies and comparable UK PLCs with roles of equivalent scale. Results showed that Executive Members' base salaries ranged between 55% and 81% of industry medians, with the overall average position being 67%.

This is a deterioration from the comparative position last calculated in November 2018 (average 70% against median). This is a concern and so we are exploring with the Scottish Government steps we can take to ensure we can attract and retain the skills we need, while delivering on the pay expectations of a responsible public sector employer.

e. Annual Out-performance Incentive Plan

The Remuneration Committee maintains the right to withhold or vary AOIP payments (potentially to zero) should events undermine the financial stability or reputation of Scottish Water. Such variation may be carried out at any time prior to AOIP payments being made and may affect all or only some of the AOIP recipients. During 2021/22 there was no requirement to exercise these step-in rights.

The potential maximum annual incentive attainable for out-performance by Executive Members is 40% of base salary and is non-pensionable. Delivery Plan targets, out-performance targets, and actual performance in 2021/22 are set out on the following page.

Performance assessment is based on the incentive framework agreed by the Scottish Government in December 2020, aligned to our strategic plan in order to focus performance on our three strategic ambitions of Great Value & Financial Stability; Service Excellence; and Net Zero Emissions.

Strategic Outcome	Measure	Target	Weight	Performance
Great Value & Financial Stability (i)	Tier 1 costs (ii)	<ul style="list-style-type: none"> Sliding scale with 50% on plan and 100% for £30m below plan 	30%	£15.1m below
	PCL (progress of projects from the Development List to the Committed List)	<ul style="list-style-type: none"> Zero below target zone 50% at bottom of target zone (100% of plan) 100% at top of target zone (110% of plan) 	10%	117%
	Overall Progress of Investment Delivery	<ul style="list-style-type: none"> Zero > 3 months either side of plan 50% +/- 3 months of plan 75% +/- 2 months of plan 100% +/- 1 month of plan 	10%	+0.6 months
Service Excellence	New Outcome Performance Assessment (OPA)	<ul style="list-style-type: none"> Zero below 395 points 50% at 395 points 100% at 410 points 	15%	398 pts
	Household Customer Experience Measure (hCEM)	<ul style="list-style-type: none"> Zero below 85.0 points 50% at 85.0 points 100% at 87.78 points 	7.5%	86.09 pts
	Non-household Customer Experience Measure (nhCEM)	<ul style="list-style-type: none"> Zero below 85.4 points 50% at 85.4 points 100% at 88.66 points 	7.5%	87.26 pts
Net Zero	Operational emissions route map delivered successfully and achieving emissions reductions	<ul style="list-style-type: none"> Zero below 6,000 tCO₂e 50% at 6,000 tCO₂e 100% at 12,000 tCO₂e 	20%	7428 tCO ₂ e

The awards generated by this performance are detailed in the single figure table of the Members' Remuneration Report.

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

Notes

- (i) Financial surplus is a gateway on the AOIP scheme i.e. payments must be funded from financial out-performance; the Delivery Plan figure will be as updated for inflation and regulatory out-turn assumptions.
- (ii) Operating costs, PFI and interest relative to Delivery Plan, excluding responsive repair and refurbishment, developer contributions and tax.

f. Long-Term Incentive Plan to incentivise out-performance

For the six years to March 2021

Performance underpinning the 2015-21 LTIP was set out in the Members Remuneration Report for 2020/21 and was disclosed in last year's annual report and accounts. However, the Remuneration Committee was only able to confirm awards under the LTIP in January 2022, following independent review of performance with our regulators. Awards generated by the 2015-21 performance were paid in February 2022 and are detailed in the single figure table of this year's Members' Remuneration Report.

For the period beginning April 2021

We have developed a new structure for LTIP to address two key elements:

1. Our Strategic Outcome of Beyond Net Zero Emissions stretches across multiple regulatory contracts and so the LTIP must reflect that longer-term commitment.
2. Since first application of an LTIP scheme in 2006-10, the per-year equivalent payment potential has reduced steadily for participants, as plan and regulatory period durations have lengthened. The new scheme restores the annual equivalent value and thus the overall potential of the reward package, in line with the earlier stated aims of our Executive Remuneration Policy.

Strategic Outcome	Measure	Target	Basis	Weight
Great Value & Financial Sustainability	Overall positive Tier 1 financial surplus – Tramline Measure	Positive performance for the period within top half of Tier 1 financial tramlines	Aggregate Tier 1 surplus must be above zero for LTIP to pay out	Yes/No gateway on LTIP payments
	Transformation plan	Integrated transformation plan in operation and has delivered on planned activities for the performance period	Assessment informed by stakeholder views on the extent of progress being made to transform Scottish Water	Yes/Partial/No decision by Remuneration Committee on the extent of LTIP payable
Net Zero Emissions	Net Zero Emissions routemap targets	Meet or exceed 3-year operational emissions reduction targets for the performance period	<ul style="list-style-type: none"> • 50% at 20,000 tCO₂e reduction • 100% at 40,000 tCO₂e reduction 	Sliding scale between 20,000 and 40,000 tCO ₂ e targets

Note:

(1) tCO₂e reduction rate in line with Net Zero Emissions by 2040

(2) tCO₂e reduction rate in line with Net Zero Emissions by 2030

The degree to which the LTIP is payable considers stakeholder feedback on transformation progress. This not only links long-term incentives clearly to Scottish Water's business transformation, but provides a credibility check to maintain the integrity of the overall LTIP mechanism. The Remuneration Committee will make a holistic assessment of a systematic gathering of stakeholder sentiment, and over the long term it will be important for all stakeholders to verify that our progress warrants LTIP payments, while incentivising the continuing delivery of our strategic transformation.

In addition to the above checks, the Remuneration Committee maintains the right to withhold or vary LTIP payments (potentially to zero) should events undermine the financial stability or reputation of Scottish Water. Such variation may be carried out at any time prior to LTIP payments being made and may affect all or only some of the LTIP recipients.

Duration & Potential Value

Scottish Water's new LTIP operates through a Performance period (during which the incentive is assessed by reference to the performance criteria); and a Vesting period (during which the amount identified in the performance period is held for payment at the end of the period).

Each of these periods lasts three years and allows the LTIP to reflect the rolling nature of truly long-term performance measures, such as Net Zero Emissions. The Vesting period allows the Remuneration Committee to verify that payments earned over a three-year Performance period are not based on short-term decisions, which later prove unsupportive of longer-term performance. This allows the Remuneration Committee, if necessary, to intervene and moderate the level of incentives actually paid out.

The first payment for this new LTIP is potentially made after six years in 2027, with a value of up to 45% of a participant's salary. Further payments of 45% are possible every three years thereafter. This differs from the previous LTIP which could pay out up to 60% of participant salaries every six years.

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



Year	2021	2024	2027	2030	2033	2036
Performance Period	LTIP1 start	LTIP1 end; LTIP2 start	LTIP2 end; LTIP3 start	LTIP3 end; LTIP4 start	LTIP4 end; LTIP5 start	LTIP5 end; etc.
Vesting Period		LTIP1 start	LTIP1 end; LTIP2 start	LTIP2 end; LTIP3 start	LTIP3 end; LTIP4 start	LTIP4 end; etc.
Payment			LTIP1	LTIP2	LTIP3	LTIP4
New maximum quantum (Directors). see page 136			45% of salary	45% of salary	45% of salary	45% of salary

g. Pension

All employees, including Executive Members, are eligible to participate in the Scottish Local Government Pension Scheme (SLGPS) which is a contributory, defined benefit scheme operating under regulations determined by the Scottish Parliament. These regulations require Scottish Water to offer this pension to all employees and in the case of the Executive Members participation is via the Lothian Pension Fund. All pension scheme members may request flexible retirement from age 55, reducing their hours or grade to receive all or part of their pension while continuing to work. All members may also choose to take full Early Retirement from age 55 with a reduction in pension value applied by the pension fund.

The value of pension provided through the SLGPS is set out in section 2.c of the Members' Remuneration Report.

Non-executive Members are not eligible to receive pension benefits.

h. Benefits

A car is provided to all Executive Members for business needs. For those opting out of car provision, a car allowance is payable instead. Non-executive Members are not eligible for a car or car allowance.

Executive Members are covered by the Scottish Water Life Assurance Scheme that covers all employees.

The value of benefits received is set out in the relevant column of the single figure table in the Members' Remuneration Report.

i. Approach to recruitment remuneration

The remuneration of any new Executive Member will be agreed with the Scottish Government prior to appointment of that Member. The Remuneration Committee will recommend a recruitment package, encompassing those elements that apply to other Executive Members and that are detailed elsewhere in this remuneration policy.

If recruitment of an Executive Member requires compensation for relocation this would normally be calculated as per Scottish Water's relocation policies and would be included in any recommendation made, as would any other proposed aspect of remuneration.

The appointment and remuneration of the Chair of Scottish Water and Non-executive Members is agreed by Scottish Ministers, with regard to the daily fee framework of the Scottish Government's Pay Policy for Senior Appointments. Fees paid reflect the time commitment anticipated for each role and are detailed in the Members' Remuneration Report.

j. Payments on loss of office

Executive Members are expected to work the notice periods in their service contracts. In circumstances where it is in the operational interests of Scottish Water for an Executive Member to leave before the end of their notice period, the Remuneration Committee will consider options such as 'garden leave' or paying in lieu for all or part notice on a case-by-case basis.

The Remuneration Committee may decide that a portion of the incentive payment is payable to former Executive Members in certain "good leaver" circumstances, including departure due to redundancy and efficiency, ill-health or normal age retirement, agreed early retirement, retirement or departure with substantial notice and responsibility transition, or death in service. Any incentive payment so determined will be paid no earlier than would have been the case had the Member not left Scottish Water. If an Executive Member leaves the employ of Scottish Water for any other reason and before incentive payments under the AOIP or LTIP would be due, their payment will normally be forfeit.

Where an Executive Member leaves for reasons of efficiency or redundancy, any severance payment that may apply will be on the same terms as for any other employee leaving under such circumstances and will be as set out under the approved redundancy scheme in operation at the time. Where the Executive Member is a member of the SLGPS then access to pension benefits on leaving will be determined by the regulations of that pension scheme, as for any other SLGPS member.

No compensation is payable to any Non-executive Member if their appointment is terminated early.

k. Consideration of employment conditions elsewhere in the company

The Remuneration Committee requests and receives information as required on pay and terms and conditions for all employees in order to provide context for decisions on executive pay. This information includes comparison of the salary and total pay of the Chief Executive versus that received by other employees; as well as consideration of the ratio between the lowest and highest potential total pay in the organisation.

When determining incentive payments to be made under the AOIP, the Remuneration Committee considers the proportion of potential payment resulting to Executive Members from corporate out-performance and how that same out-performance drives incentive payments

to other employees. Any review of executive pay is informed by reports on employee and manager pay progression, consideration of public sector pay policy and an understanding of the pay adjustment opportunities available to other employees as may be negotiated with the company's recognised trades unions.

Under the Industry (Scotland) Act 2002, Schedule 3, one of the Non-executive Members appointed to the Board of Scottish Water must be a person appearing to the Scottish Ministers to have special knowledge of the interests of the employees. The Board member who fulfilled that requirement until 30 April 2021 was replaced on both the Board and The Remuneration Committee from 1 May 2021, by a new Non-executive with similar special knowledge.

I. 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
Chief Operating Officer	Peter Farrer	1 April 2013
Strategy & Commercial Director	Alan Scott	31 January 2022

All Members are required to give 6 months' notice of resignation. Scottish Water is required to give Members 12 months' notice of termination.

Alan Scott took on a new Executive Member role as Strategy & Commercial Director on 31 January 2022, having previously been Finance Director. The total of three Executive Members on the Board is unchanged and a re-shaped role of Director of Finance, reporting to the Chief Executive, was created and successfully filled internally.

Non-executive Members

Non-executive Members do not have service contracts. Expiry dates of current Non-executive appointments are as follows:

Dame Susan Rice, Chair	31 May 2023
Samantha Barber	31 March 2025
Graham Dalton	31 March 2026
Catriona Schmolke	31 October 2025
Iain M Lanaghan	31 March 2025
Steven Dickson	30 April 2025
Deirdre Michie	30 December 2025
Kenneth Marnoch	31 March 2026



2. Members' Remuneration Report

The auditors are required to report on information contained in sections 2.a to 2.d of the Remuneration Report.

a. Single Total Figure Table

Fee levels for Non-executive Members, including the Chair, for 2022/23 will increase by £2 per day with effect from 1 April 2022 and in line with Public Sector Pay Policy for Senior Appointments.

		Salary/Fees £000	Benefits ¹ £000	AOIP ² £000	Total £000	Pension ³ £000	LTIP 2015-21 ⁴ £000	Total including one -off LTIP £000
Executive Members								
Douglas Millican ⁵	2022	268	12	80	360	38	160	558
	2021	267	12	92	371	7	-	378
Peter Farrer	2022	198	11	60	269	-14	118	373
	2021	197	11	68	276	30	-	306
Alan Scott	2022	196	11	59	266	29	117	412
	2021	195	11	67	273	16	-	289
Non-executive Members⁶								
Chair - Dame Susan Rice	2022	104			104			104
	2021	104			104			104
Samantha Barber	2022	27			27			27
	2021	27			27			27
James Coyle	2022	25			25			25
	2021	27			27			27
Iain M Lanaghan	2022	24			24			24
	2021	22			22			22
Deirdre Michie	2022	22			22			22
	2021	22			22			22
Kenneth Marnoch	2022	22			22			22
	2021	22			22			22
Matt Smith ⁹	2022	2			2			2
	2021	21			22			22
Paul Smith ¹⁰	2022	5			5			5
	2021	22			22			22
Steven Dickson ¹¹	2022	20			20			20
	2021	-			-			-
Catriona Schmolke ¹²	2022	9			9			9
	2021	-			-			-
Total Remuneration	2022	922	34	199	1,155	53	395	1,603
	2021	927	34	227	1,188	53	-	1,241

Notes:

(1) Benefits include the value of car benefit or car allowance and annual life assurance premiums associated with the Scottish Water Life Assurance Scheme as described in the Executive Remuneration policy. The value of each benefit is described in a separate table opposite.

(2) Annual Out-performance Incentive Plan as described in the Executive Remuneration Policy.

(3) The value of pension benefits accrued is calculated in accordance with section 6.5.8 (d) of the HM Treasury's Government Financial Reporting Manual 2021/22. This requires the "real" increase in accrued benefits, as detailed in section 2c on page 135, to be multiplied by 20, plus the "real" increase in accrued lump sum and reduced by the contribution made by the individual member.

(4) Long-Term Incentive Plan payments covering the six years to March 2021 as described in the Executive Remuneration Policy. The £202m financial out-performance against the 2014 Final Determination and the overall performance assessment (OPA) score, resulting in these payments, was disclosed in the Members Remuneration Report 2020/21, published in last year's Annual Report & Accounts. The Remuneration Committee was able to confirm payment of awards under this LTIP in January 2022 following independent review of performance with our regulators. Payments were made in February 2022.

(5) As part of managing the transition to a new Chief Executive, £20,156 of Douglas Millican's AOIP for 2021/22 will be withheld by Scottish Water to facilitate more flexible pension arrangements when he steps-down as Chief Executive, thus avoiding any additional cost to the company.

(6) Annual fees are set on appointment and then adjusted with regard to the daily fee framework of the Scottish Government's Pay Policy for Senior Appointments and the time commitment indicated within appointment terms. In addition to preparation and attendance at Board and Committee meetings, Non-executive Members are flexible in the hours they work and, in their availability, to provide experienced, high value advice and guidance to Scottish Water.

(7) James Coyle stepped down as Audit Committee Chair on 31 October 2021 and resigned from the Board with effect from 31 March 2022, before the end of his appointment term.

(8) Iain M Lanaghan was appointed Audit Committee Chair with effect from 1 November 2021.

(9) Matt Smith stepped down from the Board at his appointment expiry date of 30 April 2021, having served two terms.

(10) Paul Smith resigned from the Board with effect from 29 June 2021, before the end of his appointment term.

(11) Steven Dickson was appointed from 1 May 2021.

(12) Catriona Schmolke was appointed from 1 November 2021.

(13) Graham Dalton was appointed from 1 April 2022 and consequently does not appear in the payment table on page 133.

b. Details of benefits received 2021/22

Name	Car benefit or car allowance £000	Life assurance premium £000	Total £000
Douglas Millican	10	2	12
Peter Farrer	10	1	11
Alan Scott	10	1	11

c. Total pension entitlements to end of financial year 2021/22

The Executive Members Douglas Millican, Peter Farrer and Alan Scott are eligible to participate in the Lothian Pension Fund, a defined benefit scheme. The table opposite presents pension accruals under the regulations of the SLGPS.

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 determined by the rules of the Scottish Local Government Pension Scheme. For pension accrued up to 31 March 2015 this is age 65. For pension benefits accrued after that date, normal retirement age is set equal to the individual's state pension age. Any pension benefits drawn before normal retirement age are usually reduced in value by actuarial factors reflecting the anticipated longer payment period.

(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.

(5) The rate of tax payable on pension savings above the lifetime allowance of £1.073m depends on how the money is paid to individuals. The current rate is 55% if the individual takes a lump sum, or 25% if the individual takes it as pension payments or cash withdrawals. This is in addition to income tax payable on the pension paid.

	Increase in accrued benefits during the year net of inflation			Accumulated total accrued benefits at 31 March 2022		Transfer Values		
	Years in Scheme	Pension £000	Lump sum £000	Pension £000	Lump sum £000	At 31 March 2022 £000	At 31 March 2021 like-for-like basis £000	Increase in 2021/22 net of Member's own contributions and inflation £000
Douglas Millican	27.1	4	-4	86	141	1,658	1,537	44
Peter Farrer	37.7	1	-5	99	183	2,082	2,001	-2
Alan Scott	8.5	3	-	23	-	325	276	20

d. Pay multiples

The table below shows how the Chief Executive's change in remuneration value compares to the average percentage change in remuneration value of the wider workforce from 2020/21 to 2021/22.

	Salary	Benefits	AOIP (ii)
Chief Executive	0.3%	0.0%	-13.0%
All employee median (i)	2.9%	0.0%	+11.3% (iii)

Notes:

(i) Change in employee salary is calculated as the change in the median paid from one year to the next

(ii) This represents the change in value of annual incentive earned in the reporting year.

(iii) Although Chief Executive and Employee AOIP are driven by the same corporate out-performance, maximum employee AOIP potential increased in the year to £1,145 (2021: £900), raising the value earned.

The Government Financial Reporting Manual sets out the method of pay multiple comparison to be used from 2021/22 onwards, so that the Chief Executive total pay figure is compared to that received by other employees at the 25th, 50th and 75th percentile of earnings. Scottish Water reported on mean pay ratios prior to 2019/20, but in that year switched to using the percentile approach and recalculated 2018/19 in the same way, to allow comparison.

Pay for executives and for all other employees is managed with reference to the Public Sector Pay Policy issued each year. The resultant median ratio of earnings of the Chief Executive to other employees is consistent with this approach.



	Remuneration ratio calculations, excluding movement in pension and LTIP (i)			
	2021/22 (ii)	2020/21	2019/20 (iii)	2018/19
Chief Executive	360	371.0	375.0	367.0
Employees (iv)				
Salary 25th percentile	27.2	26.3	-	-
25th percentile earnings	28.1	27.2	26.5	25.8
Salary 50th percentile	31.6	30.7	-	-
50th percentile earnings	32.7	31.7	30.7	29.9
Salary 75th percentile	40.5	39.3	-	-
75th percentile earnings	42.6	40.6	39.5	38.7
Ratio at 25th percentile earnings	12.8	13.6	14.2	14.2
Ratio at 50th percentile earnings	11.0	11.7	12.2	12.3
Ratio at 75th percentile earnings	8.5	9.1	9.5	9.5

The earned remuneration of the Chief Executive in the financial year 2021/22 was £360k (2021: £371k). This was 11.0 times (2021: 11.7) the median remuneration of other employees, which was £32.7k (2021: £31.7k). The change in ratio is affected by three factors: the increase in employee earnings as a result of the 2021/22 pay award which was, on average, of proportionately greater value than the salary increase awarded to the Chief Executive;

the increase in employee maximum earnable AOIP to £1,145 (2021: £900); and the decrease in the Chief Executive's earned annual incentive payment aligned with performance against corporate targets. The full range of annual earnings was from £19.5k to £360k (2021: £19.1k to £371k). The remuneration range decreased due to the same factors described above, while employee turnover also affects earnings figures from one year to the next.

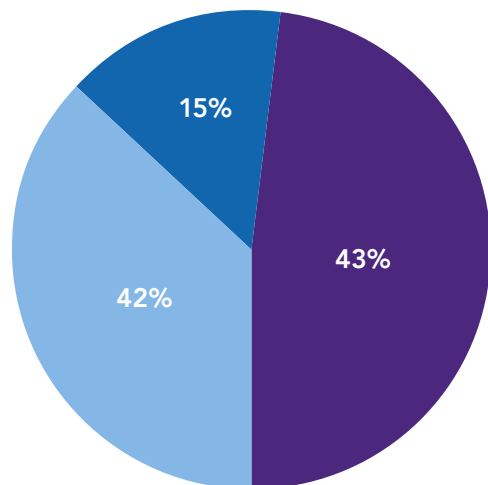
Notes:

(i) The total excludes the calculation of change in pension as the value relies heavily on length of pensionable service and so has little meaning when comparing one person (the Chief Executive) against a group of employees with varying lengths of service, i.e., an individual with greater pensionable service could see a faster increase in calculated pension value than someone with shorter pensionable service, even if they are paid the same during a financial year.

(ii) To allow like-for-like comparison, the Chief Executive figure for 2021/22 uses the total from the table at 2(a) before inclusion of the LTIP payment, which was earned for the out-performance achieved over the six year period covering 2015 to 2021 and is not an annual amount. For transparency, had the figure of £558k including the LTIP been used, the ratio to employee earnings at the 25th, 50th and 75th percentiles would have been 19.9, 17.1 and 13.1 respectively.

(iii) For comparison, the figure for the Chief Executive in 2019/20 uses the single total figure in the table at 2(a), excluding pension, as per note (i), but including the value of waived AOIP in that year of £96k.

(iv) Employee percentile earnings shown are for full time equivalent salary, benefits and AOIP earned in the reporting year for those with a full year of service, other than Executive Members. In addition, 2021/22 is the first year in which employee percentile salaries are required, but figures for 2020/21 are shown for comparison.



- Total employee pay
- Operating costs (excl. total pay)
- Capital investment on a regulatory accounting basis

e. Relative importance of spend on pay

The importance of total annual spend on pay is shown in relation to other Operating costs and Capital investment during the year. As Scottish Water is a public sector organisation owned by the Scottish Government, there were no disbursements to shareholders.

f. Implementation of Remuneration Policy in 2022/23

As described in the Executive Remuneration Policy, Scottish Water operates an Annual Out-performance Incentive Plan (AOIP) designed to incentivise and reward the out-performance of targets in plans agreed with regulators.

Strategic outcome	Measure	Target	Weight
Great Value & Financial Sustainability	Tier 1 costs (ii)	<ul style="list-style-type: none"> • Sliding scale • 50% on plan • 100% for £30m below plan 	30%
	PCL (progress of projects from the Development List to the Committed List)	<ul style="list-style-type: none"> • Zero below target zone • 50% at bottom of target zone (100% of plan) • 100% at top of target zone (110% of plan) 	10%
	Overall Progress of Investment Delivery	<ul style="list-style-type: none"> • Zero > 3 months either side of plan • 50% +/- 3 months of plan • 75% +/- 2 months of plan • 100% +/- 1 month of plan 	10%

To ensure that the AOIP targets remain suitably challenging, the degree of required out-performance has been increased consistently each year. For the 2021/27 regulatory period and beyond, the Remuneration Committee has agreed an overall performance framework with Scottish Ministers, within which the incentive targets will be set each year. For 2022/23 the out-performance targets are as follows.

g. 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 to Scottish Water. In line with this policy, Douglas Millican, Chief Executive, was appointed as a Non-executive director and trustee of World Vision UK in March 2017, from which no remuneration is payable.

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

Samantha Barber

Chair of the Remuneration Committee

26 May 2022

Service Excellence	New Outcome Performance Assessment (OPA)	<ul style="list-style-type: none"> • Zero below 395 points • 50% at 395 points • 100% at 410 points 	15%
	Household Customer Experience Measure (hCEM)	<ul style="list-style-type: none"> • Zero below 85.0 points • 50% at 85.0 points • 100% at 87.78 points 	7.5%
	Non household Customer Experience Measure (nhCEM)	<ul style="list-style-type: none"> • Zero below 85.4 points • 50% at 85.4 points • 100% at 88.66 points 	7.5%
Net Zero	Operational emissions route map delivered successfully and achieving emissions reductions	<ul style="list-style-type: none"> • Zero below 15,000 tCO₂e • 50% at 15,000 tCO₂e • 100% at 28,000 tCO₂e 	20%

Notes:

(i) Financial surplus is a gateway on the incentive plan and must be sufficient to fund AOIP payments; delivery plan baseline will be updated for inflation and regulatory out-turn assumptions.

(ii) Operating costs, PFI and interest relative to Delivery Plan, excluding responsive repair and refurbishment, developer contributions and tax, as adjusted by out-turn inflation.

MEMBERS' REPORT

The Members present the Members' report together with the audited consolidated financial statements for the year ended 31 March 2022.

The Government Financial Reporting Manual 2021/22 (FReM), published by HM Treasury, sets out the form and content for the Annual Report & Accounts 2021/22: Performance and Prospects. This includes the requirements to show a Performance Report and Accountability Report. The Members have reviewed the requirements of the FReM and are satisfied that they are covered within the Overview, Strategic and Governance reports of this report.

The Members' report comprises pages 140 to 142 and the sections of this report incorporated by reference are as follows:

Corporate governance report	See pages 114 to 117
Strategic report, including information in respect of: Scottish Water's results, key financial information and service performance, future developments and the principal risks and uncertainties faced by Scottish Water's group of companies	See pages 21 to 108
Going concern and viability statements	See pages 101 to 102
Greenhouse gas emissions	See page 61
People	See pages 53 to 59
Accounting requirements and basis of account preparation	See Note 1.2, page 157
Financial risk management	See pages 94 to 100

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.

Appointment and Replacement of Members

Schedule 3 of the Water Industry (Scotland) Act 2002 specifies Scottish Water's Board must comprise between 5 and 8 Non-executive Members and between 3 and 5 Executive Members. One Member must have special knowledge of the interests of the employees of Scottish Water. Non-executive appointments are made by the Scottish Ministers for 3 to 5 years following an open and transparent public appointment process. Executive Members are appointed by Scottish Water with the consent of the Scottish Ministers for an unidentified period. The Members appointments can be terminated under procedures set out in Paragraph 1 of Schedule 3 of the Water Industry (Scotland) Act 2002. Details of the Members' service contracts are on page 132 of the Members' Remuneration Report.

Employee Relations and Involvement

The Scottish Water group of businesses employed an average of 4,360 (2021: 4,393) 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 166. Scottish Water is committed to ensuring equality is mainstreamed into all aspects of organisational culture and practice, and all employees have equal opportunities irrespective of race, religion, sex, sexual orientation, disability or age. A number of forums are used 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 safety, health and wellbeing. Through an extensive safety awareness campaign, safety briefings and ongoing training, awareness of safety, health and wellbeing issues is being encouraged and increased among employees.

Further information can be found in the **People** section.

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. In addition, Horizons has developed and operates specialist innovation development centres at Gorthleck and Bo'ness to test new products and processes associated with the treatment of drinking water and waste water.

Further information can be found in the **Enabling Sustainable and Inclusive Growth** section.

Political Contributions

No political contributions were made during the year (2021: nil).

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 & Accounts 2021/22: Performance and Prospects. The report for this financial year will be available later in 2022.



Members' Responsibilities

The following statement, which should be read in conjunction with the statement of the auditor's responsibilities included in the Independent Auditor's Report on pages 144 to 152, is made with a view to distinguishing the respective responsibilities of the Members and of the auditor 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:

1. select suitable accounting policies and then apply them consistently;
2. make judgements and estimates that are reasonable and prudent;
3. state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
4. 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.

The Members are responsible for the maintenance and integrity of Scottish Water's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Members, as at the date of this report, consider that the Annual Report & Accounts 2021/22: Performance and Prospects taken as a whole is fair, balanced and understandable and provides the information necessary to assess Scottish Water's performance, business model and strategy.

Each of the Members, whose names and functions are listed in the Board Members section on pages 110 to 113, confirms that to the best of their knowledge and belief:

1. the Group and Company financial statements, which have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the UK and where appropriate interpreted and adapted by

the 2021/22 Government Financial Reporting Manual (FRM), give a true and fair view of the assets, liabilities, financial position and surplus of Scottish Water;

2. the Strategic Report includes a fair review of the development and performance of the business and the position of Scottish Water, together with a description of the principal risks and uncertainties that it faces.

Each of the persons who is a Member at the date of approval of this report confirms that:

1. so far as the Member is aware, there is no relevant audit information of which the Company's auditor is unaware; and
2. each Member has taken all the steps that he/she ought to have taken as a Member in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

By order of the Board,

Douglas Millican,
Chief Executive

31 May 2022

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INDEPENDENT AUDITOR'S REPORT

Independent auditor's report to the members of Scottish Water, the Auditor General for Scotland and the Scottish Parliament

Report on the audit of the financial statements

Opinion on financial statements

We have audited the financial statements in the annual report and accounts of Scottish Water for the year ended 31 March 2022 under the Water Industry (Scotland) Act 2002. The financial statements comprise the Group and Company Balance Sheets, the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated and Company Statements of Changes in Equity, the Group and Company Statements of Cash Flow and notes to the financial statements, including significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and UK adopted International Financial Reporting Standards (UK-IFRSs) and where appropriate as interpreted and adapted by the 2021/22 Government Financial Reporting Manual (the 2021/22 FReM).

In our opinion the accompanying 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 body and its group as at 31 March 2022 and of the group deficit for the year then ended;
- have been properly prepared in accordance with UK-IFRSs, and where appropriate as interpreted and adapted by the 2021/22 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.

Basis for opinion

We conducted our audit in accordance with applicable law and International Standards on Auditing (UK) (ISAs (UK)), as required by the **Code of Audit Practice** approved by the Auditor General for Scotland. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report. We were appointed by the Auditor General on 31 May 2016. The period of total uninterrupted appointment is six years. We are independent of the body and its group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK including the Financial Reporting Council's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. Non-audit services prohibited by the Ethical Standard were not provided to the body. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusion relating to going concern basis of accounting

We have concluded that the use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Our evaluation of the assessment by the Accountable Officer and board members of the ability of the body and its group to continue to adopt the going concern basis of accounting included:

- We have considered the availability of existing funding from the Scottish Government, including reviewing the repayment profile and the external financing limit set for the period 2022 to 2024.
- We have critically reviewed the regulatory delivery plan update and forecasts prepared by Scottish Water and considered the associated economic assumptions, including downside scenarios, against our commercial understanding, increasing inflation and wider economic uncertainty.
- We considered sensitivities of the key assumptions used in the cash flow forecasts and assessed their related impact on the financial resources and headroom available.
- We also compared past budgets to actual results to assess the accuracy of budgets.
- We considered whether the going concern disclosure in note 1.2 to the financial statements gives a full and accurate description of the board's assessment of going concern, including the identified risks and dependencies.

INDEPENDENT AUDITOR'S REPORT CONTINUED

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the ability of the body and its group to continue to adopt the going concern basis of accounting for a period of at least twelve months from when the financial statements are authorised for issue.


In relation to the reporting by the body and its group on how they have applied the UK Corporate Governance Code, we have nothing material to add or draw attention to in relation to the board members' statement in the financial statements about whether the board members considered it appropriate to adopt the going concern basis of accounting.

These conclusions are not intended to, nor do they, provide assurance on the current or future sustainability of the body and its group. However, we report on the body's arrangements for financial sustainability in a separate Annual Audit Report available from the **Audit Scotland website**.

Our approach to the audit


Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

	The risk	Our Response
<p>Capital additions (£588.6 million, 2021 restated: £430.3 million)</p> <p>Refer to page 118 (Audit Committee Report), page 159 (accounting policy) and page 169 (note 9 to the financial statements)</p> <p>Risk of material misstatement v/s 2020/21</p> 	<p><i>Accounting application</i></p> <p>Capital additions related to the delivery plan for regulated activities are significant.</p> <p>Executive members are incentivised across a number of financial and other measures including profit and completion of capital investment programmes.</p> <p>There is judgement involved in the allocation of expenditure between capital and revenue which can affect profit and investment measures reported in the financial statements.</p>	<p>Our procedures included:</p> <p><i>Control design</i></p> <ul style="list-style-type: none"> • Testing the design and operating effectiveness of controls over the allocation of costs between capital and revenue within the financial ledger at the project initiation stage and on an ongoing basis; and • Testing the design and operating effectiveness of controls over the appropriateness of reclassification from assets in the course of construction. • Testing the design and operating effectiveness of controls over the approval stages of a sample of projects.. <p><i>Test of details</i></p> <ul style="list-style-type: none"> • Building on our work over control design we compared the reports of Scottish Water's capital project monitoring group at the year end to amounts recorded as capital additions; • In respect of a sample of capitalised additions, we evaluated the appropriateness of the classification as capital by considering the nature of the expenditure with reference to invoice, certificate or timesheets and considering the application of the relevant accounting policies; • We assessed a sample of items allocated to revenue expenditure and considered whether they were correctly classified by considering the application of the relevant accounting policies; and • We also inspected material journals related to capital additions and agreed amounts to supporting documentation.

INDEPENDENT AUDITOR'S REPORT CONTINUED

Key audit matters (Continued)

	The risk	Our Response
<p>Bad debt provision (£451.4 million, 2021: £427.7m million)</p> <p>Refer to page 118 (Audit Committee Report), page 161 (accounting policy) and page 188 (note 27 to the financial statements)</p> <p>Risk of material misstatement v/s 2020/21</p> 	<p><i>Forecast-based valuation</i></p> <p>There are a number of assumptions included in the calculation of the bad debt provision. The most sensitive of these is the overall forecast collection rate based on historical data.</p> <p>As at 31 March 2022, the Scottish Water regulated business reported a household revenue debtor of £495.8 million (2021: £483.0 million) and a corresponding bad debt provision of £451.4 million (2021: £427.7 million) on household billings from all years dating back to 1996-97.</p> <p>Household water debt is a statutory debt recoverable from the occupier. The household billing and cash collection is performed by local authorities and cannot be influenced by Scottish Water.</p> <p>As part of our risk assessment, we determined that the recoverability of household revenue debtors requires a high degree of estimation, in particular because of the potential effects of the Covid-19 pandemic and wider economic uncertainty.</p>	<p>Our procedures included:</p> <p><i>Control design</i></p> <ul style="list-style-type: none"> • Testing the design and operating effectiveness of controls over the review and approval of the provision and associated assumptions by management during the year and at the year end; and • Testing the design and operating effectiveness of controls in respect of the reconciliation of information provided on a monthly basis by local authorities to Scottish Water in respect of amounts billed and collected. This historical information forms the basis of the forecast collection rate. <p><i>Tests of detail</i></p> <ul style="list-style-type: none"> • We compared the information on historical collection rates, recorded by Scottish Water as the basis for the current year provision calculation, to the records held in respect of prior years; and • We agreed the total amount billed and collected in respect of 2021/22 as recorded in Scottish Water's records, to confirmations received from individual local authorities. <p><i>Historical comparison</i></p> <ul style="list-style-type: none"> • We compared the change in forecast collection rate in the current year, to the historical trend of increasing collection rates since 1996-97. <p><i>Sensitivity analysis</i></p> <ul style="list-style-type: none"> • We performed sensitivity analysis and challenged management in respect of the forecast collection rate by increasing and decreasing it based on our judgement and assessing the impact on the provision. <p><i>Assessing transparency</i></p> <ul style="list-style-type: none"> • We assessed the disclosure of sensitivities by the Members, and description of the provision in note 27 of the financial statements.

INDEPENDENT AUDITOR'S REPORT CONTINUED

Key audit matters (Continued)

	The risk	Our Response
<p>Pension liability (£38.9 million (2021: £179.8 million))</p> <p>Refer to page 118 (Audit Committee Report), page 162 (accounting policy) and page 184 (note 23 to the financial statements)</p> <p>Risk of material misstatement v/s 2020/21</p> <p>↔</p>	<p><i>Subjective valuation</i></p> <p>Small changes in the assumptions and estimates used to value the pension obligation (before deducting scheme assets) would have a significant effect on the net pension liability.</p> <p>Employees of Scottish Water participate in three local government defined benefit pension schemes; North East Scotland pension fund, the Lothian pension fund and the Strathclyde pension fund.</p>	<p>Our procedures included:</p> <p><i>Control design</i></p> <ul style="list-style-type: none"> • Testing the design and operating effectiveness of controls over the provision of membership information to the actuary who uses it, together with the assumptions, to calculate the pension obligation. <p><i>Benchmarking assumptions</i></p> <ul style="list-style-type: none"> • Challenging, with the support of our own actuarial specialists, the key assumptions applied, being the discount rate, inflation rate and mortality/life expectancy against externally derived data; and • Challenging the rate of increase in pensionable salaries assumption, by comparing it to other evidence such as the regulatory delivery plan and our understanding of Scottish Government expectations. <p><i>Assessing transparency</i></p> <ul style="list-style-type: none"> • Considering the adequacy of the disclosures in respect of the sensitivity of the deficit to these assumptions.

INDEPENDENT AUDITOR'S REPORT CONTINUED

Key audit matters (Continued)

Change to key audit matters

Going concern was considered a key audit matter in the prior year but not in the current year. We continue to perform procedures over going concern. Following the better than expected recovery post Covid-19, we have not assessed going concern as one of the most significant risks in our current year audit and, therefore, it is not separately identified in our report this year.

Our application of materiality

Materiality for the group financial statements as a whole was set at £14.6 million (2021: £13.6 million), determined with reference to a benchmark of group total expenditure of which it represents 1%. We consider total expenditure to be the most appropriate benchmark as the most significant part of the Group is its regulated business which is a Scottish Government owned body where the level of expenditure is the most important measure. Materiality for the parent company financial statements as a whole was set at £10.5 million (2021: £9.7 million), determined with reference to benchmark of total expenditure, of which it represents 1% (2021: 1%).

In line with our audit methodology, our procedures on individual account balances and disclosures were performed to a lower threshold, performance materiality, so as to reduce to an acceptable level the risk that individually immaterial misstatements in individual account balances add up to a material amount across the financial statements as a whole.

Performance materiality was set at 75% (2021: 75%) of materiality for the financial statements as a whole, which equates to £10.9 million (2021: £10.2 million) for the Group and £7.8 million (2021: £7.2 million) for the parent Company. We applied this percentage in our determination of performance materiality because we did not identify any factors indicating an elevated level of risk.

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £250,000 (2021: £250,000), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Of the group's seven (2021: seven) reporting components, we subjected four (2021: four) to full scope audits for group purposes and one (2021: one) to specified risk-focused audit procedures over profit recognition. The latter was not individually financially significant enough to require a full scope audit for group purposes, but did present specific individual risks that needed to be addressed. Together these entities accounted for 99% of each of the Group's total revenue and total expenditure and 98% of total assets. The components within the scope of our work accounted for the percentages illustrated below.

For the residual components, we performed analysis at an aggregated group level to re-examine our assessment that there were no significant risks of material misstatement within these. The work on all of the components, including the parent Company, was performed by the Group team. The component materialities ranged from £144,000 to £6.0 million, having regard to the mix of size and risk profile of the Group across the components.

INDEPENDENT AUDITOR'S REPORT CONTINUED

GROUP EXPENDITURE
£1,481.5m (2021: £1,472.70m)

GROUP MATERIALITY
£14.6m (2021: £13.6m)



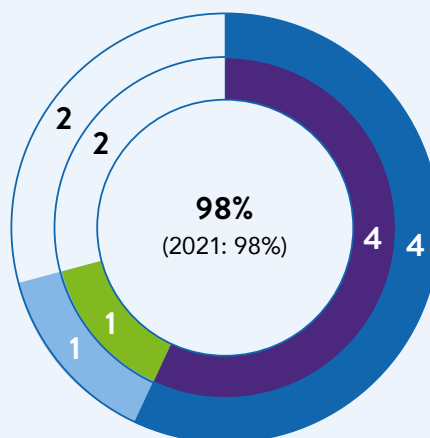
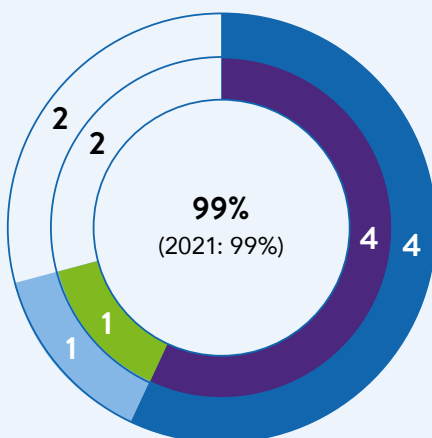
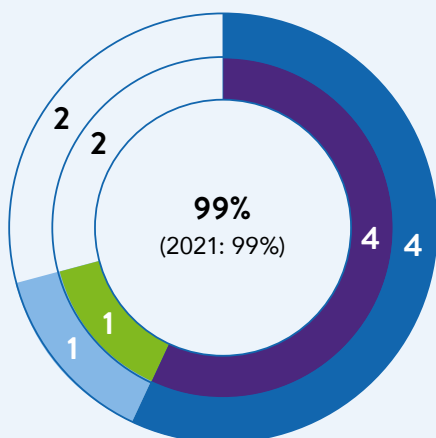
- **£14.6m**
Whole financial statements materiality (2021: £13.6m)
- **£10.9m**
Whole financial statements performance materiality (2021: £10.2m)
- **£6.0m**
Range of materiality at 7 components (£144,000 to £6.0 million) (2021: £150,000 to £2.7m)
- **£250,000**
Misstatements reported to the audit committee (2021: £250,000)

■ Group expenditure ■ Group materiality

GROUP EXPENDITURE

GROUP REVENUE

GROUP TOTAL ASSETS



KEY:

- Full scope for group audit purposes 2022
- Full scope for group audit purposes 2021
- Specified risk-focused audit procedures 2022
- Specified risk-focused audit procedures 2021
- Residual components

We were able to rely upon the Group's internal control over financial reporting in several areas of our audit, where our controls testing supported this approach, which enabled us to reduce the scope of our substantive audit work; in the other areas the scope of the audit work performed was fully substantive.

INDEPENDENT AUDITOR'S REPORT CONTINUED

Responsibilities of the board members for the financial statements

As explained more fully in the Statement of Members' Responsibilities, the Accountable Officer and board members are responsible for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework, and for such internal control as the Accountable Officer and board members determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Accountable Officer and board members are responsible for assessing the ability of the body and its group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless there is an intention to discontinue the operations of the body and its group.

Auditor's responsibilities for the audit of the financial statements

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

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities outlined above to detect material misstatements in respect of irregularities, including fraud. Procedures include:

- obtaining an understanding of the applicable legal and regulatory framework and how the body and its group are complying with that framework;
- identifying which laws and regulations are significant in the context of the body and its group;
- assessing the susceptibility of the financial statements to material misstatement, including how fraud might occur; and
- considering whether the audit team collectively has the appropriate competence and capabilities to identify or recognise non-compliance with laws and regulations.

The extent to which our procedures are capable of detecting irregularities, including fraud, is affected by the inherent difficulty in detecting irregularities, the effectiveness of the body's controls, and the nature, timing and extent of the audit procedures performed.

Irregularities that result from fraud are inherently more difficult to detect than irregularities that result from error as fraud may involve collusion, intentional omissions, misrepresentations, or the override of internal control. The capability of the audit to detect fraud and other irregularities depends on factors such as the skilfulness of the perpetrator, the frequency and extent of manipulation, the degree of collusion involved, the relative size of individual amounts manipulated, and the seniority of those individuals involved.

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

INDEPENDENT AUDITOR'S REPORT CONTINUED

Report on regularity of expenditure and income

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.

Responsibilities for regularity

The Accountable Officer is responsible for ensuring the regularity of expenditure and income. In addition to our responsibilities in respect of irregularities explained in the audit of the financial statements section of our report, we are responsible for expressing an opinion on the regularity of expenditure and income in accordance with the Public Finance and Accountability (Scotland) Act 2000.

Report on other requirements

Opinion prescribed by the Auditor General for Scotland on audited part of the Members' Remuneration Report

We have audited the part of the Members' Remuneration Report described as audited. In our opinion, the audited part of the Members' Remuneration Report has been properly prepared in accordance with the Water Industry (Scotland) Act 2002 and directions made thereunder by the Scottish Ministers.

Other information

The Accountable Officer and board members are responsible for the other information in the annual report and accounts. The other information comprises the Overview, Strategic Report, Corporate Governance Statement and other reports included in the annual report and accounts other than the financial statements, the audited part of the Members' Remuneration Report and our auditor's report thereon.

Our responsibility is to read all the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except on the Strategic Report and Corporate Governance Statement to the extent explicitly stated in the following paragraphs.

Opinion prescribed by the Auditor General for Scotland on Strategic Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the directions made under the Water Industry (Scotland) Act 2002 by the Scottish Ministers.

INDEPENDENT AUDITOR'S REPORT CONTINUED

Corporate governance statement

We have reviewed the statement by the directors and Accountable Officer in relation to going concern, longer-term viability and that part of the Corporate Governance Statement relating to the body's voluntary compliance with the provisions of the UK Corporate Governance Code.

Based on the work undertaken in the course of the audit, we have concluded that the Corporate Governance Statement for the financial year for which the financial statements are prepared has been prepared in accordance with the directions made under the Water Industry (Scotland) Act 2002 by the Scottish Ministers and that each of the following elements of the Corporate Governance Statement is materially consistent with the financial statements or our knowledge obtained during the audit:

- The statement with regards the appropriateness of adopting the going concern basis of accounting and any material uncertainties identified and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment.
- The board members' explanation as to their assessment of the prospects of the body and its group, the period this assessment covers and why they consider this period is appropriate.
- The board members' statement on fair, balanced and understandable.
- The board members' confirmation that it has carried out a robust assessment of the emerging and principal risks and the disclosures in the annual report that describes the principal risks and the procedures in place to identify emerging risks and explain how they are being managed or mitigated.
- The section of the annual report that describes the review of effectiveness of risk management and internal control systems.
- The section describing the work of the audit committee.

Matters on which we are required to report by exception

We are required by the Auditor General for Scotland to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the financial statements and the audited part of the Members' Remuneration Report are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Conclusions on wider scope responsibilities

In addition to our responsibilities for the annual report and accounts, our conclusions on the wider scope responsibilities specified in the Code of Audit Practice are set out in our Annual Audit Report.

Use of our report

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 120 of the Code of Audit Practice, we do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

[Signature]

Hugh Harvie
for and on behalf of KPMG LLP
Chartered Accountants
Saltire Court
20 Castle Terrace
Edinburgh
EH1 2 EG
[Full date]

CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31 MARCH 2022

	Note	2022 £m	2021 Restated* £m
Revenue	3	1,733.5	1,667.2
Cost of sales		(1,303.1)	(1,274.5)
Gross surplus		430.4	392.7
Administrative expenses		(178.4)	(194.5)
Operating surplus	3,4	252.0	198.2
Finance income	7	0.1	0.4
Finance costs	7	(161.3)	(165.4)
Surplus before taxation		90.8	33.2
Taxation	8	(158.0)	(7.9)
(Deficit)/surplus for the year	21	(67.2)	25.3

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 MARCH 2022

	Note	2022 £m	2021 Restated* £m
(Deficit)/surplus for the year	21	(67.2)	25.3
Other comprehensive income:			
<i>Items which will not subsequently be reclassified to the income statement</i>			
Actuarial gain on post employment benefit obligations, net of deferred taxation	23	163.5	23.0
Effective portion of changes in fair value of cash flow hedge, net of deferred taxation		3.0	1.8
Total comprehensive income for the year		99.3	50.1

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

* refer to note 30.

BALANCE SHEETS

AS AT 31 MARCH 2022

	Note	Group		Company	
		2022 £m	2021 Restated* £m	2022 £m	2021 Restated* £m
Assets					
Non-current assets					
Property, plant and equipment	9	6,813.1	6,525.9	6,773.1	6,487.2
Intangible assets	10	26.0	30.0	12.6	17.3
Investments	11	–	–	37.6	37.6
Deferred tax asset	16	3.6	5.8	–	–
		6,842.7	6,561.7	6,823.3	6,542.1
Current assets					
Inventories	12	4.2	3.9	3.8	3.5
Trade and other receivables	13	265.1	242.5	99.9	107.6
Current tax asset		11.8	4.4	11.7	3.1
Cash and cash equivalents	14	657.1	570.4	515.9	428.7
		938.2	821.2	631.3	542.9
Total assets	3	7,780.9	7,382.9	7,454.6	7,085.0
Liabilities					
Current liabilities					
Trade and other payables	15	(495.1)	(445.4)	(356.5)	(322.7)
Other loans and borrowings	18	(26.3)	(24.9)	(24.6)	(23.3)
Current tax liabilities		(2.6)	–	–	–
Provisions for liabilities	17	(11.9)	(9.0)	(14.4)	(11.6)
		(535.9)	(479.3)	(395.5)	(357.6)
Non-current liabilities					
Trade and other payables	15	(84.9)	(87.0)	(65.9)	(61.3)
Other loans and borrowings	18	(201.5)	(228.0)	(208.7)	(233.3)
Deferred tax liabilities	16	(644.7)	(441.3)	(640.3)	(436.2)
Retirement benefit obligations	23	(51.9)	(221.9)	(42.9)	(209.1)
Provisions for liabilities	17	(9.3)	(7.2)	(10.7)	(10.3)
		(992.3)	(985.4)	(968.5)	(950.2)
Total liabilities		(1,528.2)	(1,464.7)	(1,364.0)	(1,307.8)
Net assets		6,252.7	5,918.2	6,090.6	5,777.2
Equity					
Government loans	19	4,383.6	4,148.4	4,383.6	4,148.4
Retained earnings	21	1,738.2	1,641.9	1,573.6	1,495.4
Cash flow hedge reserve	27	(2.5)	(5.5)	–	–
Other reserves		133.4	133.4	133.4	133.4
		6,252.7	5,918.2	6,090.6	5,777.2

* refer to note 30.

The financial statements on pages 153 to 195 were approved by the Board of Members on 31 May 2022 and signed on its behalf by:

Douglas Millican
Chief Executive

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Note	Cash flow hedging reserves £m	Retained earnings £m	Other reserves £m	Total £m
Balance at 1 April 2020 as previously stated		(7.3)	1,614.0	133.4	1,740.1
Restatement of retained earnings in relation to Cloud computing arrangements	30	–	(20.4)	–	(20.4)
Restated balance at 1 April 2020		(7.3)	1,593.6	133.4	1,719.7
Restated Surplus for the year	21	–	25.3	–	25.3
Other comprehensive gain:					
Actuarial gain on post employment benefit obligations, net of tax	23	–	23.0	–	23.0
Effective portion of changes in fair value of cash flow hedge, net of tax	27	1.8	–	–	1.8
Total comprehensive income for the year		1.8	48.3	–	50.1
Balance at 31 March 2021		(5.5)	1,641.9	133.4	1,769.8
Deficit for the year	21	–	(67.2)	–	(67.2)
Other comprehensive gain:					
Actuarial gain on post employment benefit obligations, net of tax	23	–	163.5	–	163.5
Effective portion of changes in fair value of cash flow hedge, net of tax	27	3.0	–	–	3.0
Total comprehensive income for the year		3.0	96.3	–	99.3
Balance at 31 March 2022		(2.5)	1,738.2	133.4	1,869.1

COMPANY STATEMENT OF CHANGES IN EQUITY

	Note	Retained earnings £m	Other reserves £m	Total reserves £m
Balance at 1 April 2020 as previously stated		1,449.8	133.4	1,583.2
Restatement of retained earnings in relation to Cloud computing arrangements	30	(20.4)	–	(20.4)
Restated balance at 1 April 2020		1,429.4	133.4	1,562.8
Restated Surplus for the year	21	36.0	–	36.0
Other comprehensive gain:				
Actuarial gain on post employment benefit obligations, net of tax	23	30.0	–	30.0
Total comprehensive income for the year		66.0	–	66.0
Balance at 31 March 2021		1,495.4	133.4	1,628.8
Deficit for the year	21	(80.2)	–	(80.2)
Other comprehensive gain:				
Actuarial gain on post employment benefit obligations, net of tax	23	158.4	–	158.4
Total comprehensive income for the year		78.2	–	78.2
Balance at 31 March 2022	21	1,573.6	133.4	1,707.0

The 'Statement of changes in equity' above excludes Government loans which, in accordance with the Scottish Water Governance Directions 2009, are recorded on the balance sheet under Equity. Full details of Government loans are provided in note 19.

STATEMENTS OF CASH FLOW

FOR THE YEAR ENDED 31 MARCH 2022

	Note	Group		Company	
		2022 £m	2021 Restated* £m	2022 £m	2021 Restated* £m
Surplus before taxation		90.8	33.2	73.3	47.3
Depreciation charges	9	293.9	280.7	288.3	275.2
Amortisation of intangible asset	10	14.0	18.4	11.3	16.0
Amortisation of grants		(1.8)	(1.4)	(1.5)	(1.2)
Surplus on disposal of property, plant and equipment		(2.7)	(2.2)	(3.4)	(2.3)
Non cash adjustment for retirement benefit obligations		42.8	24.7	41.0	24.0
Finance costs - net		161.2	165.0	161.4	165.1
Operating cash flow before changes in working capital and provisions		598.2	518.4	570.4	524.1
Changes in working capital and provisions:					
Decrease / (increase) in receivables		(19.8)	5.2	10.4	(7.9)
Increase in inventories		(0.3)	–	(0.3)	(0.2)
Increase/(decrease) in payables		44.8	(60.1)	33.3	(58.3)
Increase/(decrease) in provisions		3.2	(9.5)	1.5	(11.5)
Cash flows from operating activities		626.1	454.0	615.3	446.2
Taxation paid		(12.9)	(8.4)	(14.6)	(9.6)
Net cash generated from operating activities		613.2	445.6	600.7	436.6
Cash flows from investing activities					
Purchase of property, plant and equipment		(604.9)	(467.1)	(596.7)	(458.8)
Sale of property, plant and equipment		3.6	2.4	3.9	2.5
Purchase of intangible asset	10	(10.0)	(1.1)	(6.6)	–
Government grant income received		2.0	7.1	1.8	3.7
Infrastructure income receipts		29.6	16.8	29.6	16.8
Net cash used in investing activities		(579.7)	(441.9)	(568.0)	(435.8)
Cash flows from financing activities					
Repayments of loans		(144.8)	(139.4)	(139.7)	(134.8)
Proceeds from borrowings		374.9	354.3	374.9	354.3
Interest received		0.1	0.4	–	0.2
Interest paid		(157.0)	(160.7)	(157.4)	(160.6)
Payment of finance lease liabilities		(20.0)	(19.5)	(23.3)	(22.6)
Net cash generated from financing activities		53.2	35.1	54.5	36.5
Net increase in cash and cash equivalents		86.7	38.8	87.2	37.3
Cash and cash equivalents at beginning of year	14	570.4	531.6	428.7	391.4
Cash and cash equivalents at end of year	14	657.1	570.4	515.9	428.7

* refer to note 30.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2022

1. Accounting policies

1.1 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.

1.2 Basis of preparation

The financial statements of Scottish Water for the year ended 31 March 2022 have been prepared in accordance with UK adopted and endorsed International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRIC) interpretations, and where appropriate as interpreted and adapted by the Government Financial Reporting Manual (FRM). The FRM 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, as modified by the revaluation of derivative financial instruments at fair value through profit and loss. The financial statements are prepared 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 and where appropriate as interpreted and adapted by the FRM 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 Scottish Water's accounting policies (note 2).

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

Going concern

The financial statements have been prepared on the going concern basis which the Members consider to be appropriate for the following reasons.

In considering the basis of accounting, cash flow forecasts have been prepared for a period of at least 12 months from the date of approval of these financial statements which consider various scenarios, taking into consideration severe but plausible impact downsides. These forecasts include the assessment of the group's strategic and financial frameworks, including the borrowing limit, operational positions and the level of the capital investment programme. Under all of the scenarios, Scottish Water will be able to operate within its available facilities.

Consequently, the Members are confident that Scottish Water will have sufficient funds to continue to meet its liabilities as they fall due for at least 12 months from the date of approval of these financial statements and therefore have prepared the financial statements on a going concern basis.

1.3 Changes in accounting policy

In April 2021 the IFRS Interpretations Committee (IFRIC) published an agenda decision in relation to the application of IAS 38 Intangible Assets to configuration or customisation costs in a cloud computing arrangement. The agenda decision provides new guidance specific to cloud computing arrangements and provides a framework for the accounting treatment of 'implementation costs'.

Scottish Water previously accounted for all implementation costs as Property, plant and equipment and these were subject to depreciation on a straight-line basis over the useful lives of the assets. The new guidance states that implementation costs should be recognised as an intangible asset if costs incurred meet the definition of an intangible asset under IAS 38. If it is not possible to identify an asset then the costs should be expensed in the year in which they occur. If the costs incurred are for a service that is distinct from the core software service and over the life of the contract with the supplier if the service is not distinct from the core software service.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

1. Accounting policies (continued)

Following engagement with our digital partners to identify and classify transactions relating to projects involving key systems and processes, we have been able to classify our cloud computing arrangement costs to align with the IFRIC guidance. Consequently, in the year to 31 March 2022, c.£28 million of cloud computing costs have been identified and expensed through the income statement. In addition, the group income statement, the statement of comprehensive income, and the group and company statement of changes in equity, as well as the balance sheet and cash flow statements for the year ended 31 March 2021 have been restated accordingly. A summary of the restatements for the year ended 31 March 2021 are disclosed in note 30.

1.4 Accounting standards not yet adopted by Scottish Water

As at the date of authorisation of these financial statements, Annual improvements to IFRSs 2018-2020 Cycle had been issued but was not yet effective and consequently has not been applied by Scottish Water in the preparation of the financial statements.

IFRS 16 Leases came into effect for financial periods beginning on or after 1 January 2019 for the subsidiary companies. However, the implementation for public sector was deferred by the Financial Reporting Advisory Board (FRAB) in April 2022 to 1 April 2024. IFRS 16 is not expected to have a material impact on the results and net assets of Scottish Water.

1.5 Basis of consolidation

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 direct the relevant activities of the entities, the rights to variable returns and the ability to use its power to influence the returns. Scottish Water Business Stream Limited (Business Stream) is treated as a subsidiary although there are special governance arrangements which were 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. Scottish Water is, however, satisfied that the controls and governance in place are such that consolidation is appropriate. 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 Scottish Water group of companies.

1.6 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.

1.7 Revenue recognition

Revenue is recognised to the extent it is probable that economic benefits will flow to Scottish Water and that the revenue can be reliably measured. Revenue is recognised when, or as, the performance obligations to the customer are satisfied. Revenue is shown net of associated sales taxes and 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.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

1. Accounting policies (continued)

1.8 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.

1.9 Finance income and costs

Finance income comprises interest receivable on funds invested and recognised in the income statement. Finance costs comprise interest payable on borrowings and interest on pension scheme net 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.

1.10 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 Scottish Water 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 tax 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.

1.11 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 Scottish Water 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 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.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)**1. Accounting policies (continued)**

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
Fixtures, fittings and furniture within non-specialised operational buildings	5 years
Specialised operational buildings and structures	20 to 80 years
Plant, machinery and vehicles	1 to 20 years

1.12 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 property, plant and equipment 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.

1.13 Impairment of assets

The carrying values of 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.

1.14 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.

1.15 Intangible assets

Intangible assets represent the acquisition of a non-household customer base, by Business Stream. Intangible assets are recognised at cost and treated as having a finite life. They are stated at cost less accumulated amortisation. Amortisation is charged to the income statement to write off the cost, less any residual value, on a straight-line basis over the expected useful life from the date of beneficial use. The expected useful life is currently set at 8 years.

Software intangible assets are measured at cost less accumulated amortisation and any accumulated impairment losses. Software intangible assets are amortised over a period of 3 - 5 years.

The expected useful lives and residual values are reviewed annually, and adjusted if appropriate, at the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

1. Accounting policies (continued)

1.16 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.

1.17 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

1.18 Financial instruments

Financial assets and liabilities are recognised in the 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 but under special circumstances, Scottish Water may use financial instruments to mitigate certain financial risk exposures. As such circumstances are rare, approval is required from Scottish Ministers. All treasury activities are undertaken in accordance with the permitted activities as set out in the Scottish Water Governance Directions 2009.

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, with the exception of statutory debt, 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 3 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 Scottish Water has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

e. Derivative financial instruments

In special circumstances, Scottish Water may use financial instruments to mitigate certain financial risk exposures such as foreign exchange fluctuations. As such circumstances are rare, in addition to the approval of the Scottish Water Board, approval is required from Scottish Ministers under the terms of section 42(3)(b) Water Industry (Scotland) Act 2002.

Financial derivative instruments are recognised at fair value and are re-measured to fair value each reporting period with the exception of derivatives that qualify for cash flow hedge accounting.

f. Cash flow hedges

Where the hedged risk is the variable interest rate risk in a debt instrument measured at amortised cost the effective part of any gain or loss on the derivative financial instrument is recognised in other comprehensive income (OCI). Any ineffective portion of the hedge is recognised immediately in the income statement.

When the hedging relationship ends or when a hedge no longer meets the criteria for hedge accounting, any hedging gain or loss recognised in OCI is reclassified to the income statement.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

1. Accounting policies (continued)

1.19 Employee benefit obligations

Employees of the Scottish Water group of companies participate in the Scottish Local Government Pension Scheme (SLGPS) 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 net interest cost for the period, calculated by applying the discount rate to the net pension scheme liabilities, is included in the 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.

Within the subsidiary companies there are also two defined contribution pension schemes under which the companies pay fixed contributions and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an expense in the Income Statement.

1.20 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.

1.21 Foreign currency transactions

Transactions 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.

1.22 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.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

2. Accounting estimates and judgements (continued)

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. The group has adopted IFRS 9 'Financial instruments' from 1 April 2018 which requires an expected loss method of impairment of financial assets to be used. This is based on, amongst other factors, actual collection history, forecast rates and customer category. The actual level of receivables collected may differ from those estimated, due to factors such as changes in customer behaviour, potential impact of government policy initiatives and the economic outlook, which could impact positively or negatively on operating results (see sensitivity analysis in note 27).

c. Carrying value of property, plant and equipment

Property, plant and equipment (PPE) represents the majority of the asset base and a significant proportion of annual expenditure (see funding chart on page 9). Therefore the estimates and assumptions made in determining the carrying values and related depreciation are critical to Scottish Water'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 Scottish Water'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 3 Scottish Local Government Pension Schemes (SLGPS) which are defined benefit schemes. Actuarial valuations of the schemes are carried out by the administering authorities triennially in line with SLGPS 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 23) and, while these assumptions are believed to be appropriate, a change to the assumptions would impact the surplus of Scottish Water 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.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

3. Segmental analysis

The principal activities of the Scottish Water group of companies 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 business customers in Scotland and England) and non-regulated businesses. 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.

	2022 £m	2021 £m
Revenue		
Scottish Water regulated water and waste water services	1,285.3	1,266.2
Business Stream	629.0	574.4
Scottish Water non-regulated activities	50.0	49.8
	1,964.3	1,890.4
Inter company elimination	(230.8)	(223.2)
	1,733.5	1,667.2

	2022 £m	2021 Restated £m
Operating surplus		
Scottish Water regulated water and waste water services	234.5	212.4
Business Stream	12.4	(17.7)
Scottish Water non-regulated activities	8.6	7.1
Reversal of IFRIC 12 adjustments on consolidation	(3.5)	(3.6)
	252.0	198.2

	2022 £m	2021 Restated £m
Total assets		
Scottish Water regulated water and waste water services	7,414.5	7,043.8
Business Stream	273.0	245.5
Scottish Water non-regulated activities	120.7	123.2
Reversal of IFRIC 12 adjustments on consolidation	(27.3)	(29.6)
	7,780.9	7,382.9

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

3. Segmental analysis (continued)

	Capital additions to property, plant & equipment		Depreciation on property, plant & equipment	
	2022 £m	2021 Restated £m	2022 £m	2021 Restated £m
Scottish Water regulated water and waste water services Business Stream	581.3	421.3	288.3	275.2
Scottish Water non-regulated activities	–	1.2	1.5	1.9
	7.3	7.8	4.1	3.6
	588.6	430.3	293.9	280.7

Revenue by geographical location of customers is as follows:

	Revenue	
	2022 £m	2021 £m
United Kingdom	1,733.3	1,666.9
Rest of the World	0.2	0.3
	1,733.5	1,667.2

£0.2 million of revenue has been generated outside the UK (2021: £0.3 million) and this resulted in a current tax charge of £nil (2021: £nil). The revenue was entirely derived from Australia where we have a tax residency and registered branch. There are no offices in Australia and only one member of staff in the country.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

4. Operating surplus

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

	Note	2022 £m	2021 Restated £m
Scottish Water PFI operating costs		133.0	131.3
Depreciation of property, plant and equipment	9	293.9	280.7
Amortisation of intangible asset	10	14.0	18.4
Surplus on sale of property, plant and equipment		(2.7)	(2.2)
Release of deferred income in relation to capital grants		(1.8)	(1.4)
Operating lease rentals		2.6	3.2
Auditor's remuneration			
audit fee for audit of the company and consolidated financial statements		0.3	0.3
(including £123,898 (2021: £137,221) in respect of the audit of subsidiary companies)		–	–
other services		–	–
Research and development expenditure		0.5	0.6

5. Staff costs

	Note	2022 £m	2021 £m
Wages and salaries		173.4	168.7
Social security costs		18.9	18.2
IAS 19 total service costs ¹	23	75.3	62.7
Other pension costs		0.5	0.4
Employee benefit expense		268.1	250.0
Less: charged as capital expenditure		(108.6)	(88.8)
		159.5	161.2

¹The charge in the year prior to adjustments for IAS 19 in 2022 was £32.5 million (2021: £38.0 million)

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

	2022	2021
Regulated water and waste water services	3,943	3,928
Business Stream	324	351
Scottish Water non-regulated activities	93	114
	4,360	4,393

6. Members' remuneration

Information concerning Members' remuneration, incentive schemes and pensions is detailed in the Remuneration Report on pages 125 to 139.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

7. Finance income and costs

	Note	2022 £m	2021 £m
Interest income:			
Short-term deposits		0.1	0.4
Finance income		0.1	0.4
Interest expense:			
Government loans		(140.6)	(142.1)
Other loans		(3.1)	(3.6)
Finance lease liabilities		(12.7)	(13.8)
Interest on pension scheme net liabilities	23	(4.9)	(5.9)
Finance costs		(161.3)	(165.4)
Net finance costs		(161.2)	(165.0)

8. Taxation

	Note	2022 £m	2021 Restated £m
Analysis of tax charge recognised in the income statement			
Current tax: UK corporation tax		9.6	6.5
Current tax: Adjustment in respect of prior years		(1.6)	0.8
		8.0	7.3
Deferred Tax: origination and reversal of timing differences - current year		13.8	1.2
Deferred Tax: origination and reversal of timing differences - prior years		(1.0)	(0.6)
Remeasurement of deferred tax - change in UK corporation tax rate		137.2	-
	16	150.0	0.6
Total tax charge		158.0	7.9
The charge for the year can be reconciled to the surplus per the income statement as follows:			
Group surplus before tax		90.8	33.2
Tax on surplus on ordinary activities at standard UK corporation tax rate of 19% (2021: 19%)		17.3	6.3
Adjustment in respect of prior years		(2.6)	0.2
Impact of change in UK corporation tax rate		140.2	-
Accounting gain with no capital gain		(0.9)	(0.5)
Depreciation on non qualifying additions		3.8	2.5
Other permanent differences		0.7	0.8
Deferred tax not provided		(0.4)	(1.7)
Other timing differences		(0.1)	0.3
Total tax charge for the year		158.0	7.9

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

8. Taxation (continued)

The UK Budget 2021 announcements on 3 March 2021, substantively enacted on the 24 May 2021, included measures to support economic recovery as a result of the ongoing Covid-19 pandemic. These included an increase to the UK's main corporation tax rate to 25%, which is due to be effective from 1 April 2023. These changes were substantively enacted at the balance sheet date and hence have been reflected in the measurement of deferred tax balances at the period end.

	2022 £m	2021 Restated £m
Additional Disclosure		
The table below reconciles the notional tax charge at the UK corporation tax rate to the total current tax charge for the year:		
Group surplus before tax	90.8	33.2
Tax on surplus on ordinary activities at standard UK corporation tax rate of 19% (2021: 19%)	17.3	6.3
Relief for capital allowances in excess of depreciation	(20.9)	(4.4)
Financial transactions timing differences	17.1	6.8
Utilisation of tax losses	(8.4)	(5.5)
Expenses not deductible for tax purposes	0.7	0.8
Depreciation on non qualifying additions	3.8	2.5
Adjustment in respect of prior years	(1.6)	0.8
Current tax charge for the year	8.0	7.3

The Group's current tax charge is lower than the UK headline rate of 19% primarily due to the utilisation of brought forward losses and the availability of capital allowances. Tax relief is available in relation to qualifying items of capital expenditure instead of accounting depreciation to encourage such investment. On a regulatory basis, in 2021/22, Scottish Water invested £623 million on assets, including treatment works, large diameter mains, historic sewers and IT. This investment has been aimed at improving customer service, drinking water quality, protecting the environment and supporting economic growth.

The Group is able to utilise losses carried forward in compliance with the loss restriction rules to reduce the current tax charge.

Some expenses are disallowed for tax purposes. These include the private use element of lease car rentals.

There are also various other adjustments where there is a simple timing difference between recognition of the income or expense in the accounts and in the related tax computations submitted to HMRC. The main adjustment is the movement in general provisions which are disallowed unless utilised.

For all of the timing differences, the corresponding deferred tax movements are at 25% as this is the rate of corporation tax that has been enacted as at the balance sheet date.

	Note	Group		Company	
		2022 £m	2021 £m	2022 £m	2021 £m
Tax charge recognised directly in reserves					
Deferred tax relating to:					
Pension scheme actuarial movements	23	55.2	5.4	54.3	7.0
Movements in cash flow hedge	27	0.4	0.4	–	–
Total	16	55.6	5.8	54.3	7.0

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

9. Property, plant and equipment

Note	Specialised operational properties and structures £m	Non specialised operational properties £m	Infrastructure assets £m	Restated Plant, machinery and vehicles £m	Assets under construction £m	Total £m
Group Cost						
At 1 April 2020 as previously reported	3,291.3	85.2	2,734.9	2,910.7	964.9	9,987.0
Transfer to intangible assets ³	–	–	–	(119.5)	–	(119.5)
Transfer to retained earnings ² 21	–	–	–	(32.1)	–	(32.1)
Restated balance at 1 April 2020	3,291.3	85.2	2,734.9	2,759.1	964.9	9,835.4
Additions ^{2,3}	0.1	–	–	(9.0)	439.2	430.3
Disposals ^{1,3}	(5.9)	–	–	(51.4)	–	(57.3)
Reclassifications ³	98.2	11.6	89.0	249.8	(464.7)	(16.1)
At 31 March 2021	3,383.7	96.8	2,823.9	2,948.5	939.4	10,192.3
Additions	(2.5)	–	–	2.0	589.1	588.6
Disposals	(3.7)	(3.6)	–	(129.6)	–	(136.9)
Reclassifications ³	81.8	4.4	90.9	193.0	(376.7)	(6.6)
At 31 March 2022	3,459.3	97.6	2,914.8	3,013.9	1,151.8	10,637.4
Accumulated depreciation						
At 1 April 2020 as previously reported	1,233.3	30.3	559.9	1,733.3	–	3,556.8
Transfer to intangible assets ³ 21	–	–	–	(102.3)	–	(102.3)
Transfer to retained earnings ²	–	–	–	(11.7)	–	(11.7)
Restated balance at 1 April 2020	1,233.3	30.3	559.9	1,619.3	–	3,442.8
Charge for the year	69.4	2.8	20.8	187.7	–	280.7
Disposals ^{1,3}	(5.8)	–	–	(51.3)	–	(57.1)
At 31 March 2021	1,296.9	33.1	580.7	1,755.7	–	3,666.4
Charge for the year	66.4	2.1	20.8	204.6	–	293.9
Disposals ¹	(3.0)	(3.6)	–	(129.4)	–	(136.0)
At 31 March 2022	1,360.3	31.6	601.5	1,830.9	–	3,824.3
Net book value						
At 31 March 2022	2,099.0	66.0	2,313.3	1,183.0	1,151.8	6,813.1
At 31 March 2021	2,086.8	63.7	2,243.2	1,192.8	939.4	6,525.9

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 property, plant and equipment category.

Capital grants received during the year and credited to deferred income were £0.7 million (2021: £7.1 million). Capital grants of £0.5 million were received during the year in respect of infrastructure assets.

¹Disposals include the write down of redundant assets no longer in beneficial use.

²Transfers relate to cloud computing arrangements which, prior to the IFRIC agenda decision published in April 2021, were recorded as Property, plant and equipment. A summary of the restatements is provided in note 30.

³During the year all software assets previously recorded as plant, machinery and vehicles have been reclassified and are disclosed in note 10

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

9. Property, plant and equipment (continued)

Note	Specialised operational properties and structures £m	Non specialised operational properties £m	Infrastructure assets £m	Restated Plant machinery and vehicles £m	Assets under construction £m	Total £m
Company Cost						
At 1 April 2020 as previously reported	3,282.1	85.2	2,734.9	2,841.8	961.9	9,905.9
Transfer to intangible assets ³	–	–	–	(119.5)	–	(119.5)
Transfer to retained earnings ² 21	–	–	–	(32.1)	–	(32.1)
Restated balance at 1 April 2020	3,282.1	85.2	2,734.9	2,690.2	961.9	9,754.3
Additions	0.1	–	–	(11.9)	433.1	421.3
Disposals ^{1 3}	(5.7)	–	–	(50.5)	–	(56.2)
Reclassifications ³	95.7	11.6	89.0	249.8	(462.2)	(16.1)
At 31 March 2021	3,372.2	96.8	2,823.9	2,877.6	932.8	10,103.3
Additions	(2.5)	–	–	–	583.8	581.3
Disposals ¹	(3.1)	(3.6)	–	(128.7)	–	(135.4)
Reclassifications ³	74.3	4.4	90.9	193.0	(369.2)	(6.6)
At 31 March 2022	3,440.9	97.6	2,914.8	2,941.9	1,147.4	10,542.6
Accumulated depreciation						
At 1 April 2020 as previously reported	1,231.1	30.3	559.9	1,689.6	–	3,510.9
Transfer to intangible assets ³	–	–	–	(102.3)	–	(102.3)
Transfer to retained earnings ² 21	–	–	–	(11.7)	–	(11.7)
Restated balance at 1 April 2020	1,231.1	30.3	559.9	1,575.6	–	3,396.9
Charge for the year	68.2	2.8	20.8	183.4	–	275.2
Disposals ¹	(5.6)	–	–	(50.4)	–	(56.0)
At 31 March 2021	1,293.7	33.1	580.7	1,708.6	–	3,616.1
Charge for the year	65.1	2.1	20.8	200.3	–	288.3
Disposals ¹	(2.7)	(3.6)	–	(128.6)	–	(134.9)
At 31 March 2022	1,356.1	31.6	601.5	1,780.3	–	3,769.5
Net book value						
At 31 March 2022	2,084.8	66.0	2,313.3	1,161.6	1,147.4	6,773.1
At 31 March 2021 30	2,078.5	63.7	2,243.2	1,169.0	932.8	6,487.2

¹Disposals include the write down of redundant assets no longer in beneficial use.

²Transfers relate to cloud computing arrangements which, prior to the IFRIC agenda decision published in April 2021, were recorded as Property, plant and equipment. A summary of the restatements is provided in note 30.

³During the year all software assets previously recorded as plant, machinery and vehicles have been reclassified and are disclosed in note 10

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

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 Scottish Water group and company.

	Group Total £m	Company Total £m
Cost		
At 31 March 2020, 2021 and 2022	492.7	568.8
Accumulated depreciation		
At 1 April 2020	271.3	315.6
Charge for the year	13.1	15.3
At 31 March 2021	284.4	330.9
Charge for the year	13.0	15.3
At 31 March 2022	297.4	346.2
Net book value		
At 31 March 2022	195.3	222.6
At 31 March 2021	208.3	237.9

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

10. Intangible asset

Investment intangible assets relate to the acquisition of the non-household customer base of Southern Water Services Limited in April 2017 and, in October 2019, of the non-household customer books of Yorkshire Water Business Services and Three-Sixty, both part of the Kelda Group. The investments are treated as having a finite life and are being amortised on a straight-line basis over the expected useful life, currently set at 8 years. The cost, additions, amortisation charge and carrying value are shown in the table below.

Software intangible assets relate to implementation costs associated with cloud computing software that meet the definition of an intangible asset under IAS38 and software that is controlled by Scottish Water and/or its subsidiaries. Software intangible assets are amortised on a straight-line basis over a period of 3-5 years. The cost, additions, amortisation and carrying value are shown in the table below.

Group	Note	Software £m	Investments £m	Total £m
Cost				
At 1 April 2020 as previously reported		–	22.7	22.7
Transfer from Property, plant and equipment	9	119.5	–	119.5
Restated balance at 1 April 2020		119.5	22.7	142.2
Additions		17.2	–	17.2
Disposals	9	(10.9)	–	(10.9)
At 31 March 2021		125.8	22.7	148.5
Additions		9.5	0.5	10.0
Disposals ¹		(58.0)	–	(58.0)
At 31 March 2022		77.3	23.2	100.5
Accumulated depreciation				
At 1 April 2020 as previously reported		–	8.7	8.7
Transfer from Property, plant and equipment	9	102.3	–	102.3
Restated balance at 1 April 2020		102.3	8.7	111.0
Amortisation charge		16.0	2.4	18.4
Disposals	9	(10.9)	–	(10.9)
At 31 March 2021		107.4	11.1	118.5
Amortisation charge		11.4	2.6	14.0
Disposals*		(58.0)	–	(58.0)
At 31 March 2022		60.8	13.7	74.5
Net book value				
At 31 March 2022		16.5	9.5	26.0
At 31 March 2021		18.4	11.6	30.0

*Disposals include the write down of redundant assets no longer in beneficial use.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

10. Intangible asset (continued)

Company	Note	Software £m	Investments £m	Total £m
Cost				
At 1 April 2020 as previously reported		–	–	–
Transfer from Property, plant and equipment	9	119.5	–	119.5
Restated balance at 1 April 2020		119.5	–	119.5
Additions		16.1	–	16.1
Disposals	9	(10.9)	–	(10.9)
At 31 March 2021		124.7	–	124.7
Additions		6.6	–	6.6
Disposals *		(58.0)	–	(58.0)
At 31 March 2022		73.3	–	73.3
Accumulated depreciation				
At 1 April 2020 as previously reported		–	–	–
Transfer from Property, plant and equipment	9	102.3	–	102.3
Restated balance at 1 April 2020		102.3	–	102.3
Amortisation charge		16.0	–	16.0
Disposals	9	(10.9)	–	(10.9)
At 31 March 2021		107.4	–	107.4
Amortisation charge		11.3	–	11.3
Disposals *		(58.0)	–	(58.0)
At 31 March 2022		60.7	–	60.7
Net book value				
At 31 March 2022		12.6	–	12.6
At 31 March 2021		17.3	–	17.3

*Disposals include the write down of redundant assets no longer in beneficial use.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

11. Investments

	Company	
	2022 £m	2021 £m
Cost and net book value		
At 31 March	37.6	37.6

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 ¹	Scotland	100.0	Holding company
Scottish Water Business Stream Limited ²	Scotland	100.0	Licensed water and waste water services
Scottish Water Horizons Limited ¹	Scotland	100.0	Commercial non regulated water and waste water services
Scottish Water International Limited ¹	Scotland	100.0	Non trading
Scottish Water Solutions 2 Limited	Scotland	100.0	Non trading
Aberdeen Environmental Services Limited ³	Scotland	100.0	PFI concession operator
Scottish Water Services (Grampian) Limited ¹	Scotland	100.0	Waste water services operator
Bandwidth Energy Limited ^{5*}	Scotland	100.0	Heat from waste water projects
Aberdeen Environmental Services (Holdings) Limited ⁴	Scotland	100.0	Holding Company
Aberdeen Holdco Limited ¹	England & Wales	100.0	Holding Company

¹ owned by Scottish Water Horizons Holdings Limited

² owned by Scottish Water Business Stream Holdings Limited

³ owned by Aberdeen Environmental Services (Holdings) Limited

⁴ owned by Aberdeen Holdco Limited

⁵ owned by Scottish Water Horizons Limited

Scottish Water owns shares in a further 8 companies which did not trade during the year ended 31 March 2022. 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. The companies are:

Scottish Water Ltd

Scottish Water Retail Ltd

Scottish Water Technology Ltd

Scottish Water Utilities Ltd

Scottish Water Wholesale Ltd

OneSource Infrastructure Services Ltd

Water Solutions Ltd

Business Stream Ltd⁶

⁶ owned by Scottish Water Business Stream Limited

*Bandwidth Energy Limited is exempt from the requirement of the Companies Act 2006 relating to the audit of accounts under Section 479A of the Companies Act 2006.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

12. Inventories

	Group		Company	
	2022 £m	2021 £m	2022 £m	2021 £m
Raw materials and consumables	4.4	4.0	4.0	3.6
Less provision held	(0.2)	(0.1)	(0.2)	(0.1)
	4.2	3.9	3.8	3.5

All inventories will be recovered within 12 months.

During the year to March 2021, inventories recognised within cost of sales were £1.8 million (2021: £1.8 million).

13. Trade and other receivables

	Note	Group		Company	
		2022 £m	2021 restated £m	2022 £m	2021 £m
Trade receivables	27	658.2	644.8	511.8	494.9
Less provision for impairment of trade receivables	27	(503.4)	(491.1)	(454.4)	(430.7)
Net trade receivables		154.8	153.7	57.4	64.2
Other receivables		32.2	31.0	27.7	28.2
Prepayments and accrued income		78.1	57.8	13.7	12.9
Amounts due from subsidiaries		–	–	1.1	2.3
		265.1	242.5	99.9	107.6

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

Balance at 1 April	491.1	452.3	430.7	411.8
Charge for the year	24.2	48.3	27.7	26.0
Amounts written down during the year	(11.9)	(9.5)	(4.0)	(7.1)
Balance at 31 March	503.4	491.1	454.4	430.7

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

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

14. Cash and cash equivalents

	Group		Company	
	2022 £m	2021 £m	2022 £m	2021 £m
Cash at bank and in hand	162.3	170.6	21.1	28.9
Short-term bank deposits	494.8	399.8	494.8	399.8
Cash and cash equivalents per the statement of cash flows	657.1	570.4	515.9	428.7

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

In Business Stream, during November 2021, letters of credit to the value of £14.1 million (2021: £12.7 million) were renewed in relation to ongoing wholesale prepayments made to English wholesalers.

15. Trade and other payables

	Note	Group		Company	
		2022 £m	2021 £m	2022 £m	2021 £m
Current					
Trade payables		47.6	60.7	6.5	19.1
Non trade payables and accruals		105.7	106.5	105.3	105.3
Accruals		210.3	192.8	142.3	155.6
Payments received in advance		88.3	48.9	61.8	34.1
Other payables		31.9	26.6	0.7	0.8
Deferred income		6.6	5.4	1.1	1.1
Other taxes and social security		4.7	4.5	4.2	4.1
Amounts due to subsidiaries		–	–	34.6	2.6
		495.1	445.4	356.5	322.7
Non-current					
Payments received in advance		62.4	58.8	55.9	50.1
Deferred income		19.1	21.4	10.0	11.2
Other financial liabilities - interest rate swap	27	3.4	6.8	–	–
		84.9	87.0	65.9	61.3

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

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

16. Deferred taxation

The following are the deferred tax liabilities and assets recognised by Scottish Water and the 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 2020		495.5	(41.9)	(12.4)	(12.1)	429.1
Charge/(credit) to income statement	8	2.7	(5.6)	6.4	(2.9)	0.6
Charge to reserves	8	–	5.4	–	0.4	5.8
At 31 March 2021		498.2	(42.1)	(6.0)	(14.6)	435.5
Charge/(credit) to income statement	8	175.7	(26.1)	4.2	(3.8)	150.0
Charge to reserves	8	–	55.2	–	0.4	55.6
At 31 March 2022		673.9	(13.0)	(1.8)	(18.0)	641.1
Company						
At 1 April 2020		491.9	(41.1)	(10.3)	(14.3)	426.2
Charge/(credit) to income statement		3.1	(5.6)	6.8	(1.3)	3.0
Credit to reserves	8	–	7.0	–	–	7.0
At 31 March 2021		495.0	(39.7)	(3.5)	(15.6)	436.2
Charge/(credit) to income statement		174.3	(25.3)	3.5	(2.7)	149.8
Charge to reserves	8	–	54.3	–	–	54.3
At 31 March 2022		669.3	(10.7)	-	(18.3)	640.3

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	
	2022 £m	2021 £m	2022 £m	2021 £m
Deferred tax assets	(3.6)	(5.8)	–	–
Deferred tax liabilities	644.7	441.3	640.3	436.2
At 31 March 2022	641.1	435.5	640.3	436.2

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 income 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 Scottish Water 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 £128.6m (2021: £107m) for both the Company and the group. No tax is expected to be payable in this regard.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

17. Provisions for liabilities

	Income uncertainty provision £m	Restructure and other provision £m	Total £m	
Group				
At 1 April 2020	22.6	1.5	24.1	
Charged to the income statement	(4.8)	(0.7)	(5.5)	
Utilised during the year	(2.4)	–	(2.4)	
At 31 March 2021	15.4	0.8	16.2	
Charged to the income statement	7.5	0.1	7.6	
Utilised during the year	(2.5)	(0.1)	(2.6)	
At 31 March 2022	20.4	0.8	21.2	
Company				
At 1 April 2020	30.3	1.3	31.6	
Charged to the income statement	(4.7)	(0.9)	(5.6)	
Utilised during the year	(4.1)	–	(4.1)	
At 31 March 2021	21.5	0.4	21.9	
Charged to the income statement	6.6	–	6.6	
Utilised during the year	(3.4)	–	(3.4)	
At 31 March 2022	24.7	0.4	25.1	
	Group		Company	
	2022 £m	2021 £m	2022 £m	2021 £m
Analysis of total provisions				
Current	11.9	9.0	14.4	11.6
Non-current	9.3	7.2	10.7	10.3
	21.2	16.2	25.1	21.9

The income uncertainty provision relates to non-household revenues. The reconciliation process, through the Central Market Agency (CMA), relating to each financial year will normally be finalised 18 months after the end of the relevant financial year. It is expected that the provision will be utilised over 2023 and 2024.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

18. Other loans and borrowings

	Group		Company	
	2022 £m	2021 £m	2022 £m	2021 £m
Current				
Non-government loans	5.2	5.0	–	–
Obligations under finance leases	21.1	19.9	24.6	23.3
	26.3	24.9	24.6	23.3
Non current				
Non-government loans	25.6	30.9	–	–
Obligations under finance leases	175.9	197.1	208.7	233.3
	201.5	228.0	208.7	233.3
Total				
Non-government loans	30.8	35.9	–	–
Obligations under finance leases	197.0	217.0	233.3	256.6
	227.8	252.9	233.3	256.6

(i) Non-government loans

Other loans are repayable as follows:

	Note	Up to 1 year £m	1-2 years £m	3-5 years £m	6-10 years £m	Total £m
Other loans						
- SW subsidiaries	20	5.2	5.8	19.8	–	30.8
At 31 March 2022		5.2	5.8	19.8	–	30.8
At 31 March 2021		5.0	5.2	18.6	7.1	35.9

Non-government loans of £30.8 million represent amounts borrowed by a subsidiary under a facility agreement with a consortium of banks which bear interest at a margin over LIBOR and are repayable in instalments over the period ending 31 March 2027. On 1 April 2022 LIBOR was replaced by the Sterling Overnight Night Index Average rate (SONIA). These are secured by fixed and floating charges over the undertaking, property, assets and rights of that and over the parent company's shares in that subsidiary. These loans have certain covenants attached.

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

	Book value 2022 £m	Book value 2021 £m	Fair value 2022 £m	Fair value 2021 £m
Non-government loans	30.8	35.9	33.9	39.4

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

18. Other loans and borrowings (continued)

(ii) Finance lease liabilities - PFI liabilities

Group

Future finance lease commitments are as follows:

	Minimum lease payments		Present value of minimum lease payments	
	2022 £m	2021 £m	2022 £m	2021 £m
Amounts payable:				
Within one year	32.7	32.7	21.1	19.9
Between one and 5 years	120.8	127.0	107.1	108.4
After 5 years	108.4	135.0	68.8	88.7
Present value of minimum lease payments including finance charges	261.9	294.7		
Less future finance charges	(64.9)	(77.7)		
Present value of minimum lease payments	197.0	217.0	197.0	217.0

Company

Future finance lease commitments are as follows:

	Minimum lease payments		Present value of minimum lease payments	
	2022 £m	2021 £m	2022 £m	2021 £m
Amounts payable:				
Within one year	38.4	38.5	24.6	23.3
Between one and 5 years	143.7	150.0	128.8	128.7
After 5 years	125.6	157.8	79.9	104.6
Present value of minimum lease payments including finance charges	307.7	346.3		
Less future finance charges	(74.4)	(89.7)		
Present value of minimum lease payments	233.3	256.6	233.3	256.6

PFI - Service concession arrangements

Upon its creation in April 2002 Scottish Water inherited 9 concession contracts which had been entered into with 9 private sector consortia (PFI Cos) by its 3 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 9 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. On 19 December 2018, the companies operating the contract for Aberdeen were acquired by Scottish Water Horizons Holdings Limited, with Scottish Water remaining a client under the contract.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

18. Other loans and borrowings (continued)

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 for 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 FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

19. Government loans

	Group and Company	
	2022 £m	2021 £m
Government loans	4,383.6	4,148.4

Scottish Water's borrowing powers are defined in Section 42 of the Water Industry (Scotland) Act 2002.

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

Group and company	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	85.0	42.1	248.5	295.5	3,214.6	3,885.7
National Loans Fund	32.0	94.0	142.4	180.0	32.5	480.9
Public Works Loan Board	5.5	1.0	7.2	2.8	0.5	17.0
At 31 March 2022	122.5	137.1	398.1	478.3	3,247.6	4,383.6
At 31 March 2021	124.7	122.5	433.1	474.9	2,993.2	4,148.4

b. Fair values

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

	Book value		Fair value	
	2022 £m	2021 £m	2022 £m	2021 £m
Scottish Consolidated Fund	3,885.7	3,597.1	4,610.9	4,810.7
National Loans Fund	480.9	530.9	592.0	694.8
Public Works Loan Board	17.0	20.4	21.3	26.9
	4,383.6	4,148.4	5,224.2	5,532.4

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

20. Analysis of net debt

	Note	As at 1 April 2021 £m	Increase in cash £m	Movement in debt £m	As at 31 March 2022 £m
Group					
Cash and cash equivalents	14	570.4	86.7	–	657.1
Government loans	19	(4,148.4)	–	(235.2)	(4,383.6)
Other loans	18	(35.9)	–	5.1	(30.8)
Net debt		(3,613.9)	86.7	(230.1)	(3,757.3)
Company					
Cash and cash equivalents	14	428.7	87.2	–	515.9
Government loans	19	(4,148.4)	–	(235.2)	(4,383.6)
Net debt		(3,719.7)	87.2	(235.2)	(3,867.7)

21. Retained earnings reserve

	Note	Retained earnings excluding actuarial gains £m	Actuarial gains/ (losses) on pension obligations £m	Retained earnings including actuarial gains/(losses) £m
Group				
At 1 April 2020 as previously reported		1,723.1	(109.1)	1,614.0
Restatement of retained earnings in relation to Cloud computing arrangements	9	(20.4)	–	(20.4)
Restated balance at 1 April 2020		1,702.7	(109.1)	1,593.6
Retained surplus for the year restated		25.3	–	25.3
Actuarial gain net of deferred taxation	23	–	23.0	23.0
At 31 March 2021		1,728.0	(86.1)	1,641.9
Retained deficit for the year		(67.2)	–	(67.2)
Actuarial gain net of deferred taxation	23	–	163.5	163.5
At 31 March 2022		1,660.8	77.4	1,738.2
Company				
At 1 April 2020 as previously reported		1,558.6	(108.8)	1,449.8
Restatement of retained earnings in relation to Cloud computing arrangements	9	(20.4)	–	(20.4)
Restated balance at 1 April 2020		1,538.2	(108.8)	1,429.4
Retained surplus for the year restated		36.0	–	36.0
Actuarial gain net of deferred taxation	23	–	30.0	30.0
At 31 March 2021		1,574.2	(78.8)	1,495.4
Retained deficit for the year		(80.2)	–	(80.2)
Actuarial gain net of deferred taxation	23	–	158.4	158.4
At 31 March 2022		1,494.0	79.6	1,573.6

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

22. Results of Scottish Water (the Company)

Of the results for the financial year, a retained deficit of £80.2 million (2021: £36.0 million surplus) 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 or a statement of comprehensive income for Scottish Water alone.

23. 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 Scottish Local Government Pension Scheme administered by Aberdeen, Edinburgh and Glasgow City Councils respectively. The schemes provide defined benefits based on career average pensionable pay. Actual pension costs for the year for each fund, as a % of pensionable pay, were 18.2% (2021: 18.5%), 20.7% (2021: 31.8%) and 19.3% (2021: 19.3%) respectively.

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.

A full actuarial valuation was carried out at 31 March 2020 for all 3 funds and updated at 31 March 2022 by a qualified independent actuary, to take account of the requirements of IAS 19.

The major assumptions used by the actuaries were:

	2022 %	2021 %
Rate of increase in pensionable salaries	3.30	2.85
Rate of increase in pensions payment	3.30	2.85
Discount rate	2.70	1.95
CPI inflation rate	3.30	2.85

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

	North East Scotland Years	Lothian Years	Strathclyde Years
Retiring at 31 March 2022			
Male	21.4	20.5	19.9
Female	24.1	23.3	22.6
Retiring at 31 March 2042			
Male	23.0	22.0	21.3
Female	26.2	25.2	24.7

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 liability £m
Rate of increase in pensionable salaries	+/- 0.1% per annum	Increase / decrease by c. 0.28%	Increase / decrease by c. £6m
Discount rate	+/- 0.1% per annum	Increase / decrease by c. 1.84%	Decrease / increase by c. £41m
CPI Inflation rate	+/- 0.1% per annum	Increase / decrease by c. 1.54%	Increase / decrease by c. £34m
Longevity	Increase life expectancy by 1 year	Increase by c. 3.0%	Increase by c. £67m

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

23. Pensions (continued)

Guaranteed Minimum Pension (GMP) equalisation

In considering the potential impact of gender indexation of guaranteed minimum pensions (GMP), actuarial advice has been sought. In the case of the North East Scotland Pension Fund (NESPF), the Lothian Pension Fund (LPF) and the Strathclyde Pension Fund (SPF) the GMP adjustment has been calculated at approximately 0.25%, 0.3% and 0.4% of liabilities at 31 March 2021 respectively. This equates to a past service cost of £1.4million for NESPF, £2.1million for LPF and £3.8million for SPF. The total £7.3 million was recognised in the gross pension liability at 31 March 2021. No further past service cost adjustment was required at 31 March 2022.

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

Note	Group		Company	
	2022 £m	2021 £m	2022 £m	2021 £m
Total fair value of assets	2,170.4	2,051.9	2,123.7	2,008.0
Present value of scheme liabilities	(2,222.3)	(2,273.8)	(2,166.6)	(2,217.1)
Gross pension liability	(51.9)	(221.9)	(42.9)	(209.1)
Related deferred tax asset	16	13.0	10.7	39.7
Net pension liability	(38.9)	(179.8)	(32.2)	(169.4)

Scheme assets are stated at their bid values.

Reconciliation of opening and closing retirement benefit liabilities and assets.

Note	Group		Company	
	2022 £m	2021 £m	2022 £m	2021 £m
Movements in liabilities during the year:				
Opening value of total liabilities	(2,273.8)	(1,897.0)	(2,217.1)	(1,858.0)
Total service cost	5	(75.3)	(72.8)	(60.9)
Interest on pension scheme liabilities	7	(44.6)	(43.5)	(42.8)
Contributions by members		(9.7)	(9.4)	(9.2)
Actuarial gain/(loss)		124.0	119.3	(302.2)
Benefits paid		57.1	56.9	56.0
Closing value of total liabilities	(2,222.3)	(2,273.8)	(2,166.6)	(2,217.1)
Movement in assets during the year:				
Opening fair value of total assets		2,051.9	2,008.0	1,640.9
Interest on pension scheme assets	7	39.7	38.9	37.0
Contributions by members		9.7	9.4	9.2
Contributions by the employer		31.5	30.9	37.7
Actuarial gain		94.7	93.4	339.2
Benefits paid		(57.1)	(56.9)	(56.0)
Closing fair value of assets		2,170.4	2,123.7	2,008.0
Gross deficit in the schemes at 31 March		(51.9)	(42.9)	(209.1)

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

23. Pensions (continued)

Return on assets

As required by IAS 19, the expected return on assets for all asset categories is equal to the discount rate. It is assumed that assets with higher volatility will no longer generate higher returns.

	Note	Group		Company	
		2022 £m	2021 £m	2022 £m	2021 £m
Actual return on pension scheme assets		134.4	383.2	132.3	376.2
Actuarial gain in other comprehensive income in the consolidated statement of comprehensive income					
Gross actuarial gain recognised in the pension fund		218.7	28.4	212.7	37.0
Deferred tax movement	16	(55.2)	(5.4)	(54.3)	(7.0)
Net actuarial gain recognised in other comprehensive income in the consolidated statement of comprehensive income	21	163.5	23.0	158.4	30.0

Amounts recognised in the consolidated income statement

	Note	2022 £m	2021 £m
Total service cost	5	75.3	62.7
Interest cost on pension scheme net liabilities (see above)	7	4.9	5.9
		80.2	68.6

The unpaid contributions outstanding at the year end included in other payables (note 15) was nil (2021: £0.4 million). It is estimated that Scottish Water will make contributions of £29.3 million to the pension funds in financial year 2022/23.

History of experienced gains and losses

	2022 £m	2021 £m
Group		
Difference between the expected and actual return on scheme assets:		
Amount	94.7	345.4
Fair value of assets	2,170.4	2,051.9
Experienced gains on scheme liabilities:		
Amount	0.6	23.6
Present value of liabilities	2,222.3	2,273.8
Changes in assumptions underlying the present value of scheme liabilities:		
Amount	123.4	(340.6)
Total variance between pension fund actuarial assumptions and actual experience	218.7	28.4
Gross deficit in the schemes at 31 March	(51.9)	(221.9)

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

23. Pensions (continued)

	2022 £m	2021 £m
Company		
Difference between the expected and actual return on scheme assets:		
Amount	93.4	339.2
Fair value of assets	2,123.7	2,008.0
Experienced gains on scheme liabilities:		
Amount	0.7	23.9
Present value of liabilities	2,166.6	2,217.1
Changes in assumptions underlying the present value of scheme liabilities:		
Amount	118.6	(326.1)
Total variance between pension fund actuarial assumptions and actual experience	212.7	37.0
Gross deficit in the schemes at 31 March	(42.9)	(209.1)

24. Commitments

a. Capital commitments

Scottish Water has contracted capital commitments of £455.6 million (2021: £541.4 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

Scottish Water 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.

Scottish Water also leases vehicles under cancellable operating lease agreements. Scottish Water 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:

	2022 £m	2021 £m
Within one year	2.3	1.9
Between one and five years	4.5	3.8
After five years	15.8	10.1
	22.6	15.8

25. Contingent assets and liabilities

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.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

25. Contingent assets and liabilities (continued)**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.

26. Related party transactions

Scottish Water has related party relationships with the Scottish Government, with its subsidiaries (note 11), 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 and associated interest charges. Details of the loans from the Scottish Government are shown in note 19.

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 Drinking Water Quality Regulator, 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.

Subsidiaries

During the year Scottish Water entered into the following transactions with its subsidiaries (note 11):

	2022 £m	2021 £m
Wholesale water and waste water services to Business Stream	198.3	191.2
Sale of waste water services to other subsidiaries	0.5	0.5
Purchase of waste water services from other subsidiaries	24.3	24.4
Seconded staff costs charged to subsidiaries	2.9	4.1
Other operating costs charged to subsidiaries	1.7	1.3
Purchase of renewable development and vesting services	3.3	2.5

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. Scottish Water'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 125 to 139. Scottish Water's Non-executive Members hold additional roles within other organisations (see Members on pages 110 to 113).

27. 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 Strategic report on pages 21 to 108 and Corporate Governance report on pages 114 to 117.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

27. Financial instruments and risks (continued)**a. Qualitative risk disclosures****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 Government borrowings are at fixed interest rates. Therefore Scottish Water is not deemed to bear any interest rate risk.

Other borrowings, following the acquisition of Aberdeen Environmental Services Limited (note 11), are linked to LIBOR and are therefore exposed to changes in LIBOR which could have a material effect on interest costs from year to year and over time. In order to manage the exposure to movements in LIBOR a floating interest rate to fixed rate swap exists. The fair values of these derivatives at the balance sheet date are determined by reference to their market values, which are provided by a third party (note 15). On 1 April 2022 LIBOR was replaced by the Sterling Overnight Night Index Average rate (SONIA).

Currency risk

In special circumstances, Scottish Water may use financial instruments to mitigate certain financial risk exposures such as foreign exchange fluctuations. As such circumstances are rare, in addition to the approval of the Scottish Water Board, approval is required from Scottish Ministers under the terms of section 42(3)(b) Water Industry (Scotland) Act 2002.

b. Categories of financial assets and liabilities and fair values

Scottish Water's financial assets and liabilities comprise trade and other receivables (note 13), cash and cash equivalents (note 14), borrowings (notes 18 and 19) and trade and other payables (note 15). No trading in derivative financial instruments was undertaken.

Basis of determining fair value

The financial assets of Scottish Water fall into the 'loans and receivables' category. The financial liabilities of Scottish Water 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 arm's 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 18 and 19.

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.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

27. Financial instruments and risks (continued)

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

	Group		Company	
	2022 £m	2021 £m	2022 £m	2021 £m
Trade receivables per note 13:				
Trade receivables	658.2	644.8	511.8	494.9
Less provision for impairment of trade receivables	(503.4)	(491.1)	(454.4)	(430.7)
Net trade receivables	154.8	153.7	57.4	64.2
Analysed between:				
Household receivables	495.8	483.0	495.8	483.0
Less provision for impairment	(451.4)	(427.7)	(451.4)	(427.7)
Net household receivables	44.4	55.3	44.4	55.3
Business customer receivables	162.4	161.8	16.0	11.9
Less provision for impairment	(52.0)	(63.4)	(3.0)	(3.0)
Net business customer receivables	110.4	98.4	13.0	8.9

Household water and waste water services are billed to customers by the 32 Councils as an element of the annual Council Tax bills. The Councils 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 by the Councils. Debt since the establishment of the former Water Authorities in 1996 continues to be collected. As at 31 March 2022 trade receivables in respect of household customers totalled £495.8 million with a provision of £451.4 million (2021: £483.0 million and £427.7 million respectively).

The sensitivities regarding the principal assumptions used to measure the level of the household bad debt provision are:

Assumption	Change in assumption %	Approximate impact on bad debt charge £m
Overall household collection rate	+/- 0.01%	Increase / decrease by c. £1.7m
In-year household bad debt provision charge	+/- 0.10%	Increase / decrease by c. £0.9m

As at 31 March 2022 trade receivables from business customers totalled £162.4 million (2021: £161.8 million). The ageing analysis of trade receivables from business customers and the related provisioning is as follows:

Group	Total £m	Current £m	< 3 months overdue £m	3-12 months overdue £m	> 12 months overdue £m
Gross receivable	162.4	47.9	46.3	23.7	44.5
Provision	(52.0)	-	(4.7)	(16.0)	(31.3)
Net trade receivable as at 31 March 2022	110.4	47.9	41.6	7.7	13.2
Gross receivable	161.8	63.1	34.7	25.0	39.0
Provision	(63.4)	-	(10.3)	(19.2)	(33.9)
Net trade receivable as at 31 March 2021	98.4	63.1	24.4	5.8	5.1

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

27. Financial instruments and risks (continued)

	Total £m	Current £m	< 3 months overdue £m	3-12 months overdue £m	> 12 months overdue £m
Company					
Gross receivable	16.0	10.3	2.1	2.3	1.3
Provision	(3.0)	–	(0.1)	(1.6)	(1.3)
Net trade receivable as at 31 March 2022	13.0	10.3	2.0	0.7	–
Gross receivable	11.9	7.4	1.2	1.9	1.4
Provision	(3.0)	–	(0.2)	(1.4)	(1.4)
Net trade receivable as at 31 March 2021	8.9	7.4	1.0	0.5	–

Group

Other financial Liabilities - Interest rate swap

As at the acquisition of Aberdeen Environmental Services Limited on 19 December 2018, the floating interest rate to fixed rate interest swap liability had a carrying value of £10.9 million. Any gains or losses on the effective portion of the hedging instruments are recognised within the Consolidated statement of comprehensive income or as an expense within the Consolidated income statement. The maturity of the interest rate swap coincides with the maturity of the loan (31 March 2027).

Interest rate swap - financial liability	Note	£m
Balance at 31 March 2021		(6.8)
Effective portion of changes in fair value of cash flow hedge		3.4
Balance at 31 March 2022	15	(3.4)

The fair values of these derivatives at the balance sheet date are determined by reference to their market values, which are provided by a third party.

The cash flow hedge reserve in the balance sheet, and the corresponding change in fair value recognised in the Consolidated statement of comprehensive income, reflect the movement in the interest rate swap liability net of deferred taxation.

	Cash flow hedging reserve		
	Gross reserve £m	Deferred tax £m	Net reserve £m
Balance at 31 March 2021	6.8	(1.3)	5.5
Effective portion of changes in fair value of cash flow hedge	(3.4)	0.4	(3.0)
Balance at 31 March 2022	3.4	(0.9)	2.5

28. 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.

29. Regulatory information

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

The WICS monitors Scottish Water's performance on efficiency and customer service and approves the code of practice. Each year the WICS publishes reports on the exercise of its functions. In preparing these reports, the WICS assesses the 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 WICS may make regulatory amendments to figures published in Scottish Water's audited financial statements to ensure like for like comparisons with other companies.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2022 (CONTINUED)

30. Changes to Accounting Policy

A summary of the restatements required for the year ended 31 March 2021 as a result of the April 2021 IFRS Interpretations Committee (IFRIC) agenda decision in relation to the application of IAS 38 Intangible Assets to cloud computing arrangements (note 1.3) is provided below.

Group	Note	As previously Reported £m	Adjustments £m	Restated £m
Balance sheet				
At 1 April 2020				
Property, plant and equipment	9	6,430.2	(37.6)	6,392.6
Intangible Assets	10	14.0	17.2	31.2
Trade and other receivables	13	246.8	-	246.8
Total assets		6,691.0	(20.4)	6,670.6
Retained earnings	21	1,614.0	(20.4)	1,593.6
At 31 March 2021				
Property, plant and equipment	9	6,568.4	(42.5)	6,525.9
Intangible Assets	10	11.6	18.4	30.0
Trade and other receivables	13	239.6	2.9	242.5
Total assets		6,819.6	(21.2)	6,798.4
Retained earnings	21	1,663.1	(21.2)	1,641.9

Company	Note	As previously Reported £m	Adjustments £m	Restated £m
Balance sheet				
At 1 April 2020				
Property, plant and equipment	9	6,395.0	(37.6)	6,357.4
Intangible Assets	10	-	17.2	17.2
Trade and other receivables	13	98.9	-	98.9
Total assets		6,493.9	(20.4)	6,473.5
Retained earnings	21	1,449.8	(20.4)	1,429.4
At 31 March 2021				
Property, plant and equipment	9	6,524.7	(37.5)	6,487.2
Intangible Assets	10	-	17.3	17.3
Trade and other receivables	13	107.6	-	107.6
Total assets		6,632.3	(20.2)	6,612.1
Retained earnings	21	1,515.6	(20.2)	1,495.4

Consolidated statement of comprehensive income**For the year ended 31 March 2021**

Cost of sales	(1,273.7)	(0.8)	(1,274.5)
Surplus for the year	26.1	(0.8)	25.3
Total comprehensive income	50.9	(0.8)	50.1

Cash flow statements

This change in accounting policy resulted in a restatement of the comparative year. The impact was a decrease in net operating cash inflows and a decrease in net cash outflows from investing activities of £15.8 million for group and £27.9 million for the company.

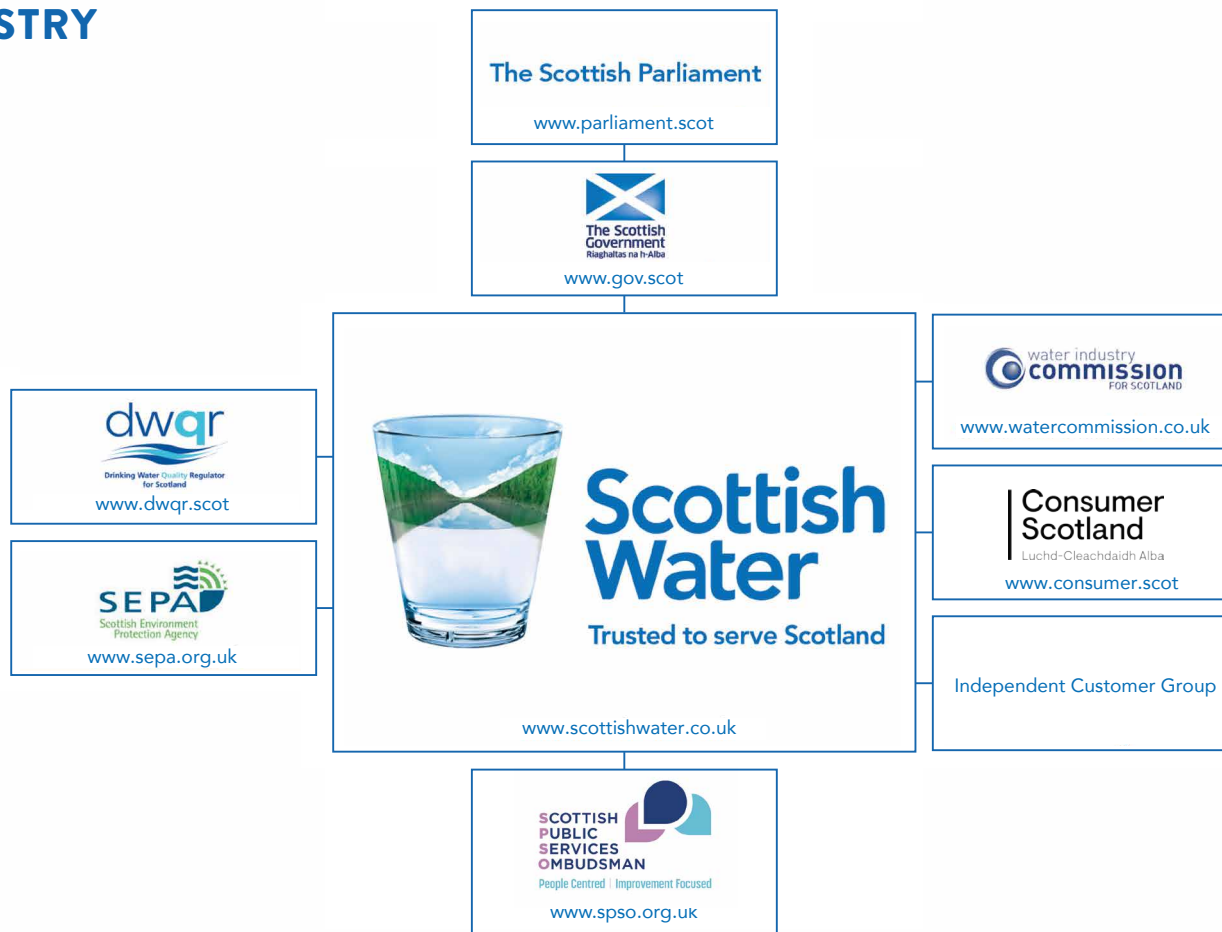
DIRECTION BY THE SCOTTISH MINISTERS

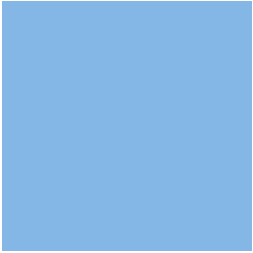
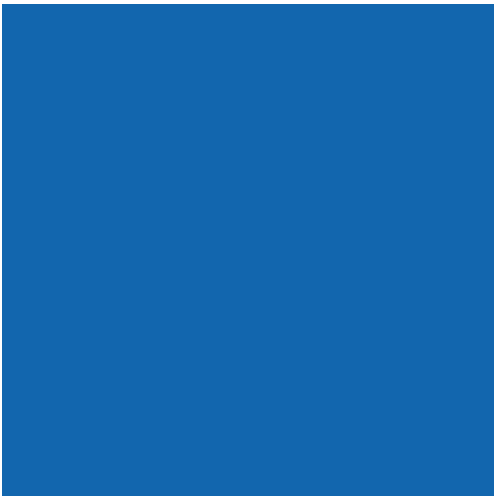
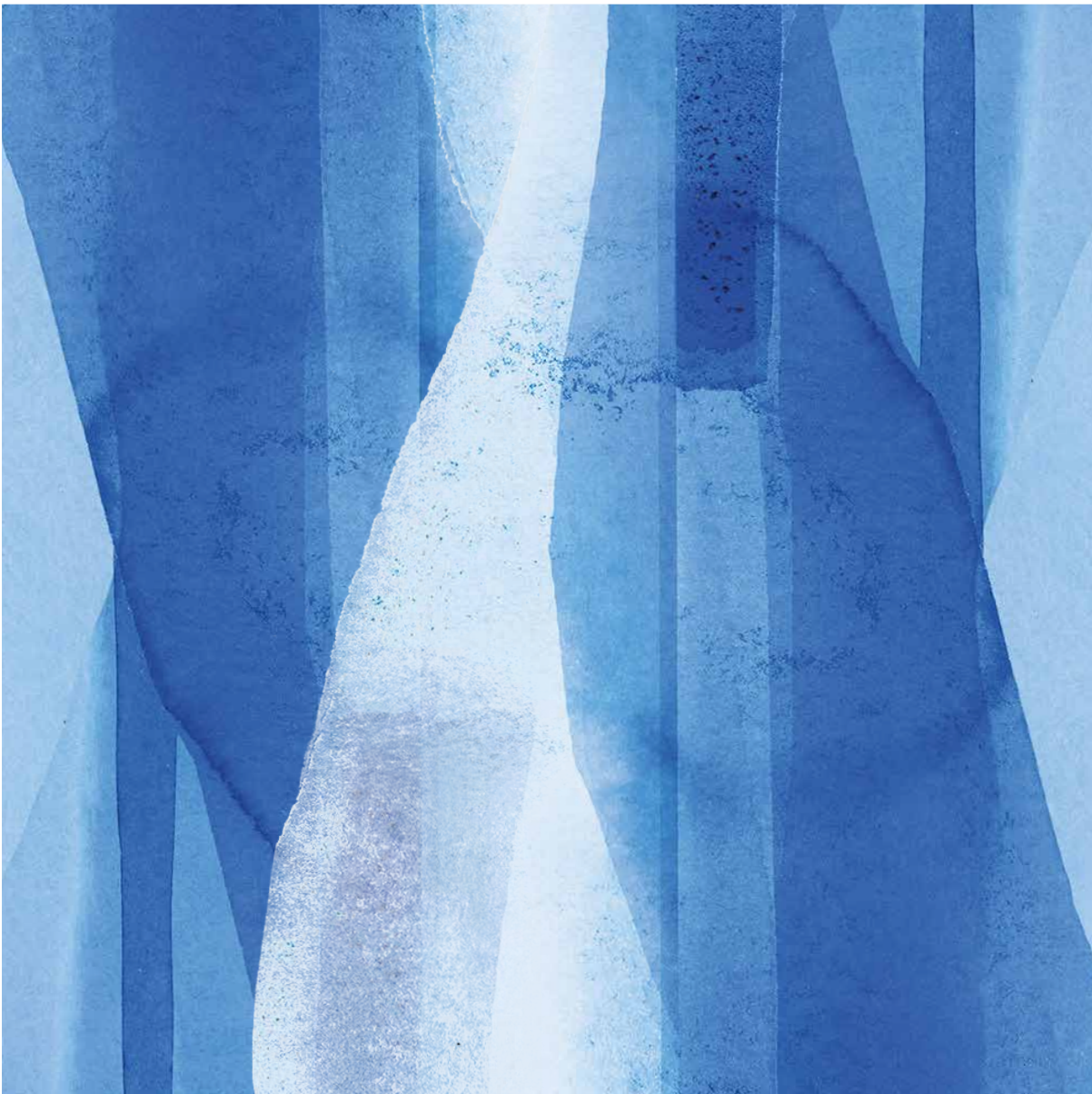
IN ACCORDANCE WITH SECTION 45(2) OF THE WATER INDUSTRY (SCOTLAND) ACT 2002

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	Ayrshire strategic resilience	£31,100,000
		Invercarnie WTW Improvements	£19,100,000
		Bonnycraig WTW Improvements	£15,800,000
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	Scottish Amateur Swimming Association*	£250,000
Gifts	£100	None	–

THE WATER INDUSTRY IN SCOTLAND





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