

SOUTH WEST WATER LIMITED
ANNUAL REPORT AND
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021

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CHAIR'S LETTER

This has undoubtedly been a unique year for South West Water, and for everyone who works within, and supports the Company. The human tragedy of loss of life as a result of the pandemic, is something that will weigh heavy on us all for generations to come; and there is every sense that things will never quite be the same again.

The worst of times brings out the very best in people and that's so true of everyone who works at South West Water. I am so proud of the way our loyal employees and supply chain partners have responded to the challenge.

My sincere thanks go to our Executive team, who together, have led the Company through this pandemic from the front, demonstrating what it takes to be highly resilient, agile and above all compassionate. With an unwavering responsibility for critical infrastructure providing essential services to customers and communities, we have continued to deliver, given the extraordinary dedication of our exceptionally talented and hard-working employees. On behalf of the Board, I thank you all.

Balancing returns, financial sustainability and investment, we have applied a methodical and disciplined approach to create a sustainable foundation for the future.

YOUR BOARD

In July 2020 we enacted our Board internal succession plan and I was delighted to take on the role of Chair, working alongside a diverse and talented Board, one of the endearing legacies left to South West Water by our outgoing Chair, Sir John Parker. This also included the retirement of our outgoing Group Chief Executive Officer, Chris Loughlin, stepping down after fourteen years leading the Company through some exceptional times and changes. Susan Davy, previously Chief Financial Officer of Pennon and Finance and Regulatory Director of South West Water was appointed as the new Group Chief Executive Officer.

At the same time, we reviewed our Committee structure to ensure that strong governance remains at the core of our successful management of the Company. All Non-Executives now attend all Committees and to ensure we meet the requirements of Ofwat, South West Water Limited maintains separate governance arrangements from our parent company, Pennon Group plc.

In recognition of the growing importance of environmental social governance (ESG) matters for all responsible businesses, we refreshed the focus of our Sustainability Committee prioritising ESG. At the same time, we have created a new dedicated Health & Safety Committee to enable the Board to focus on our number one priority. chaired by Jon Butterworth MBE, we are already benefitting from his considerable operational experience. With an ambition to become a leader in Health & Safety performance in the industry by 2025, we know we have more to do.

OUR PERFORMANCE

We have focused on driving sustainable growth, customer service and environmental excellence in the UK Water Industry. We have consistently demonstrated robust operational and resilient financial performance for many years. We are well placed, together with significant retained earnings, to provide a sustainable platform for delivery, investment and growth.

Operationally, we have made a strong start to the new regulatory period, with c.80% of Outcome Delivery Incentives (ODIs) ahead or on track. Despite the challenges posed by the pandemic, the performance of the business has been resilient, and testament to the hard work of all our employees.

We continue to provide excellence in many areas, boosting biodiversity in our regions with improving bathing water quality, tree planting and continued leadership in nature partnerships and are committed to further improving water quality, and minimising customer supply interruptions.

We also acknowledge that we need to do more in some operational areas notably pollutions. The Board have focused significant attention on this over the course of the year, ensuring we are working collaboratively with our regulators and have a robust reduction plan in place.

PURPOSE AND CULTURE

This year, we refreshed our purpose, reflecting the wider social contract we have with all our stakeholders and the region we support. Our new purpose, Bringing Water to Life – supporting the lives of people and the places they love for generations to come, shows the importance we place on operating in the public interest for the benefit of our customers and our employees, for now and into the future, underpinned by our core values, which guide everything we do.

CHAMPIONING DIVERSITY

There has never been a more important time for responsible businesses to promote the widest level of diversity in the boardroom and beyond.

South West Water also became the first water company to sign up to Change the Race Ratio harnessing a desire to go further and faster, and leading from the front. We know that change of this magnitude takes time, bravery and commitment especially given the demographic of the regions we support. We are committed to take every opportunity to make a broader societal impact on diversity and inclusion.

Alongside this, as part of the Pennon Group, we have continued our membership of the 30% Club, and SWW has once again contributed to the industry's Women in Water initiative.

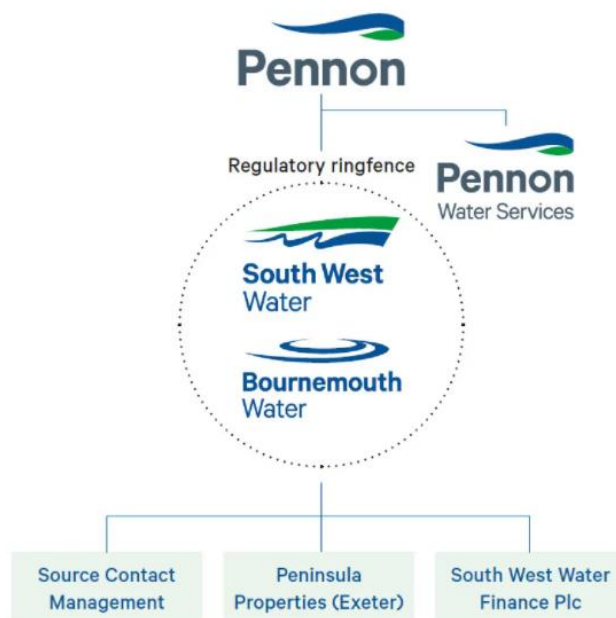
A SUSTAINABLE FUTURE

Our focus on UK Water, together with the geography of the region and communities we support, affords us a unique opportunity to be at the forefront of environmental leadership.

As we all know, there is no silver bullet to achieving Net Zero and it requires new thinking and resolute leadership. I am personally delighted that the Water Industry is leading the way, with even more ambitious timelines to achieve Net Zero by 2030, 20 years ahead of the Government target. The Board has set out an implementation roadmap, focused around three key pillars - sustainable living, championing renewables and reversing carbon emissions, ensuring we are well placed to transform ourselves into a different kind of water company, delivering on our purpose, and putting in place the core building blocks for our next price review, and beyond.

SOUTH WEST WATER'S GROUP CONTEXT

South West Water Limited is a subsidiary of Pennon Group plc (which is South West Water's immediate and ultimate parent company), a FTSE 250 company, whose principal significant trading subsidiaries are shown below:



Note: South West Water's subsidiaries are described in note 16 (page 163).

SOUTH WEST WATER

South West Water provides regulated water and wastewater services across Cornwall, Devon and parts of Dorset and Somerset, water only services in areas of Dorset, Hampshire and Wiltshire (the Bournemouth Water area) and a small amount of non-appointed services. It is responsible for delivering the 2020-25 business plan, in both the original South West Water area of operation and the Bournemouth Water area of operation. South West Water provides retail services to residential (household) customers. On 1 April 2020, South West Water's licence was extended to provide water and waste water services to the Isles of Scilly.

PENNON WATER SERVICES

Pennon Water Services provides retail services to non-household customers. Whilst part of the wider Pennon Group, South West Water has in place robust policies and practices to ensure full competition compliance with the market codes for the non-household retail market.

SOUTH WEST WATER'S SUBSIDIARIES

Source Contact Management manages South West Water's billing, collections and customer contact activities.

Peninsula Properties (Exeter) advises South West Water on property development opportunities.

South West Water Finance acts as a financing company, raising borrowings for South West Water.

OUR STAKEHOLDERS

South West Water operates in a high profile sector with a wide stakeholder group. We are committed to listening, engaging and reflecting all our stakeholders' needs and priorities in our business plans and operations.

The work we do delivers a wide range of benefits to a variety of stakeholders, creating long-term sustainable value. Our engagement approach involves regular dialogue that is timely and open, building meaningful relationships based on trust and transparency.

We use a wide range of methods to reach our stakeholders, ranging from formal independent research, focus groups and workshops to real-time conversations.

We engage with our stakeholders in order to understand their needs and priorities, which in turn shape our strategy and social purpose:

Innovate and develop our business – by knowing how our business is experienced, perceived and understood by our stakeholders we learn how to improve

Identify our risk profile – an open and transparent approach helps us to see potential problems before they materialise

Build loyalty and satisfaction – engagement, particularly with staff, customers and regulators builds understanding and appreciation of our business

Develop advocates – strong stakeholder relationships mean we have more advocates, helping us to shape our reputation and the environment in which we operate

Our Board – takes into account stakeholders' interests when making decisions.

Our customers

We supply water and wastewater services to around one million household customers.

Customer satisfaction:

89%

We engage regularly with our customers on service quality, cost of service, value for money and our strategy. This includes regularly conducting customer satisfaction surveys, holding focus groups, co-creation workshops and convening forums, providing ongoing feedback to our teams to recognise good service and make improvements where needed. With the introduction of WaterShare+ as part of the New Deal 2020-25 business plan, customers are being offered a tangible stake and a say in the business, including the opportunity to participate in a customer Annual General Meeting, the first of which will be held in the autumn of 2021.

Customer trust score:

94%

We also engage with key trade customer bodies including CCW⁽¹⁾ – the voice for water consumers.

We have a well-established independent WaterShare customer panel which reviews and challenges our performance against our business plan commitments and, to support the development of our five-year business plan, we established an independent WaterFuture customer panel.

Find out more on page 30.

⁽¹⁾ CCW – previously known as the Consumer Council For Water

Our people

Our employees are our greatest asset. We provide the opportunity for them to be engaged at multiple levels of the business and through a variety of two-way dialogue and feedback channels.

We continually engage and communicate with our people on their health, safety and well-being, our organisational culture, promoting diversity and inclusion, training and development.

We use our annual employee trust and engagement survey as a mechanism to measure progress and obtain feedback. Our senior leaders meet once a quarter with established engagement forums where staff representatives discuss business challenges. We also recognise Trade Union partners and maintain an open dialogue with them. We hold regular Big Chat calls with employees, providing them with the opportunity to hear directly from the Executive and ask any questions they wish. Employees can also directly email the Chief Executive with comments and questions via an Ask Susan facility in addition to speak face to face during regular site visits.

Find out more on page 24.

Our Trust Index score is:

66%

Our communities

Our business operates in the heart of local communities, so we work closely with these stakeholders through regular liaison meetings and community events. Our education facilities and outreach programmes support environmental learning and our charity donation schemes support hundreds of good causes in communities where we operate.

We engage regularly with our communities on local projects and initiatives and hold regular community liaison groups around our sites. We also engage with our communities through print, digital and social media and use these channels to great effect with our behavioural change campaigns including 'Love your Loo' and Think Sink! We hold a Conservation and Recreation Forum twice a year to get input from a range of stakeholders including South West Lakes Trust, National Farmers' Union, Dartmoor National Park and the Royal Yacht Association.

We work closely with the support of South West Lakes Trust to support access to our land and sites for recreation in the South West.

Find out more on page 30.

c.2.0 million
visitors to South West
Water's reservoirs

Our environment

We work closely with a range of environmental partners including South West Lakes Trust, Westcountry Rivers Trust, The Wildlife Trust, Natural England and various conservation and environmental interest groups and charities to help ensure we deliver our environmental commitments.

We are committed to planting c.250,000 trees by 2025, supporting Water UK's commitment to plant 11 million trees by 2030.

We have a commitment to achieve Net Zero carbon emissions by 2030.

We meet regularly with our environmental stakeholders on natural capital stewardship and other areas of focus. This includes regular meetings and liaison with the Wildlife Trusts in our operational areas and with the Westcountry Rivers Trust, both of whom are partners in our catchment management projects.

We also hold a twice-yearly BeachWise Forum with key stakeholders to discuss matters relating to bathing water quality.

Find out more on page 33.

c.250,000
Tree planting commitment

Net zero
Our Carbon Commitment

Our suppliers

Our supply chain partners play a vital role in supporting sustainable growth and cost base efficiency across the business. We are committed to ensuring our supply chain partners align with the same values, standards and behaviours we expect of ourselves and share the principles set out in both our Code of Conduct for Supply Chain Partners and Sustainable Procurement Policy. Through rationalising and segmenting our supply chain partners to reflect either strategic, key, preferred or transactional relationships, we are developing an approach that maximises our engagement with each supply chain partner.

We have formal contracts and framework agreements with all supply chain partners that meet the appropriate balance between commercial, quality and sustainably focused delivery whilst our e-procurement platforms support a structured, fair and transparent approach to supplier engagement. As a signatory to the EU Skills Accord, we work collaboratively to support skills development and investment throughout the supply chain and as part of our Sustainability and Net Zero strategy we will engage our supply chain so that we can better understand and manage our collective environmental impact through collaboration, we will engage our supply chain so that we can better understand and manage our collective environmental impact through collaboration.

100%

of our suppliers to be engaged with our Code of Conduct for Supply Chain Partners by end 2021/22

Our regulators

We have an open dialogue and meet regularly with our regulatory bodies – Ofwat, the Department for Environment, Food & Rural Affairs (Defra), the Environment Agency (EA), Drinking Water Inspectorate and the Health and Safety Executive (HSE) to ensure that our business plans address their priorities and concerns.

We engage regularly with all our regulators on business plans, strategy, performance, risks and opportunities and delivery for customers. We attend regular meetings, provide reports and reviews, respond to consultations and join workshops to ensure trust and transparency within these relationships.

Our policy makers

Engaging with national and local Government, MPs and Peers, Local Enterprise Partnerships, the HSE, HM Revenue & Customs, the Department for Business, Energy & Industrial Strategy (BEIS) and Defra, we have a good ongoing dialogue with policy makers and stakeholders who influence and shape our social contract.

We regularly discuss our strategy, performance and risks and opportunities with policy makers and key opinion formers. We engage through a regular meeting programme, briefings, round tables, consultation responses and through trade bodies including Water UK and British Water.

SOUTH WEST WATER'S BUSINESS MODEL

OUR STRATEGIC FOCUS AREAS

In line with our new vision of 'Bringing Water to Life' we focus on six strategic focus areas:



OUR BUSINESS MODEL

Underpinned by strong governance, our business model is designed to ensure we:

- deliver value for money services while keeping bills affordable to customers
- achieve or exceed the high quality standards set by our regulators
- safeguard our existing investments (e.g. networks, treatment works, operational assets and systems)
- minimise the impact of our activities on the environment
- ensure fair returns for our investors
- are able to meet future challenges such as climate change, resilience, population growth and new legislation.



FOR THE BENEFIT OF OUR STAKEHOLDERS

OUR CORE BUSINESS

We provide water and wastewater services in the most efficient and sustainable way possible.

Customers – Our high quality services support households and businesses in the regions we serve

Shareholders and investors – Our strong business model ensures shareholders and investors get a fair return

Regulators and stakeholders – Our engagement with regulators and key stakeholders ensures transparency of our business approach

Employees – Our employees are highly valued and are integral to our success. Their health & safety is paramount

Suppliers and contractors – The relationships we have with our suppliers and contractors are fair and deliver many regional economic benefits.

WHAT WE DO

1. We abstract water from the environment

- maintenance of dams including upgrading spillways
- maintenance and upgrades of pumps and other assets (e.g. pipework)
- generation of renewable energy using hydropower, solar panels and wind power.

2. We clean it and make it safe to drink

- maintenance of existing treatment works
- improvements to the drinking water treatment processes
- investment in ceramic membrane microfiltration and other technological advancements to improve efficiency and quality.

3. We distribute it to our customers

- ensuring that clean treated water reaches our customers at the same level of quality as when it leaves our treatment works
- ensuring reliability of supplies
- preventing leakage and bursts.

4. Our customers rely on the services we provide

- ensuring customers get excellent service when they contact us
- ensuring billing and payment systems work smoothly
- making the most of technologies and digital communications (e.g. website and social media).

5. We collect wastewater

- maintenance and upgrades of sewerage infrastructure (network and other assets)
- investment to reduce flood risk and associated pollution incident risks.

6. We treat it and return it to the environment

- maintenance and improvement of wastewater treatment assets as well as wastewater pumping stations
- wastewater treatment improvements to protect bathing and shellfish water quality
- bio-resource recycling
- energy generation from treatment processes through Combined Heat and Power (CHP) and solar panels.

OUR VALUES



TRUSTED

We do the right thing for our customers and stakeholders



COLLABORATIVE

We forge strong relationships, working together to make a positive impact



RESPONSIBLE

We keep our promises to our customers, communities and each other



PROGRESSIVE

We are always looking for new ways to improve and make life better.

OUR STRENGTHS

The best people

The talent, commitment and hard work of our people is the foundation of our success. As a responsible employer we are focused on employee retention, training and development, productivity and, above all, an unwavering commitment to health, safety and well-being.

Effective governance

A strong governance framework provides oversight and support to the Company including robust decision-making and performance management processes.

High-quality assets

We invest in the construction of world-class facilities and plants that use state-of-the-art technology. We engage the best people to maintain and operate our fleet of assets, to ensure we always maximise returns.

Environmental stewardship

We invest in the maintenance and improvement of our services, operations and assets and constantly seek more sustainable ways of working to protect, enhance and reduce our impact on the natural environment.

Strong relationships with our suppliers

We work closely with our suppliers and take the steps necessary to ensure their performance meets our expectations. We expect them to uphold our standards, align with our policies, protect human rights and promote good working conditions.

Efficient financing

The strength of our proposition and investor confidence in our performance and reputation, means that we are well-funded with efficient long-term financing.

Well-managed risk

Comprehensive and fully embedded risk management processes assist us in identifying and managing risks and opportunities to deliver the Company's strategy and objectives.

OUR LONG-TERM PRIORITIES

1	Leadership in UK water	We aim to lead in the water and waste sectors by capitalising on the Company's strengths, capabilities, best practice and synergies and achieving the right balance between risk and reward.
2	Efficient operations	We are focused on driving down overheads and operating in the most efficient way to minimise costs.
3	Sustainable growth	We actively seek opportunities to invest for growth, whether through investment to increase our asset portfolio, initiatives to expand our customer base or partnerships with other organisations.

Chief Executive Officer's review

I believe that the best businesses are those that value people and promote teamwork. This in turn drives innovation, agility and a passion for doing what's right – for the environment, customers and each other.

UNLOCKING POTENTIAL TO TRANSFORM AND DELIVER

One of my first priorities, as Chief Executive Officer, has been to focus everyone on helping make South West Water the best place to work for our employees, and the best company to work for in the South West. For me, great leadership is all about valuing people and unlocking the potential in everyone to deliver, driving innovation and agility. With 1,650 employees at South West Water, we value everyone.

It was therefore great to see Pennon, our Parent Company, being recognised as the winner in Britain's Most Admired Companies (Utilities) – the longest-running annual survey of corporate reputation in the UK. Most importantly, our employees are telling us that too. This year we asked employees how it feels to work for South West Water using the Great Places to Work Best Workplace Survey™. We achieved our highest ever participation rate of 81% and have officially passed the threshold to become accredited as a Great Place to Work. In a year where the pandemic has changed lives and livelihoods for everyone, I am most proud of this.

In 2020/21, our absolute focus has been on supporting our employees through COVID-19. However, our Health and Safety LTIFR performance wasn't in line with our aspiration. We believe that everyone who works for and with South West Water, should go home safely, every day. We remain committed to delivering on our strategy to 2025 to become industry leading on health and safety. For 2021/22, we aim to have our best performance ever, with a renewed focus on our cultural training and award winning HomeSafe programme, as well as continuing to focus on ensuring that all our sites and employees remain COVID-safe.

BUILDING A NEW KIND OF WATER COMPANY

At the heart of what we do, and why we do it, is an unwavering ambition to put environmental, social and governance commitments at the forefront of our decision-making, driving sustainability.

The societal responsibility of business has been under more scrutiny than ever, from all stakeholders, and it's clear that organisations need to do more to tap into the public consciousness. Organisations everywhere, across every industry, are reassessing their priorities and purpose for the good of the planet, for people and for profit – in that order – for the longer term; they're building agility and flexibility into their strategies, to be able to respond as things change and really listen to public and social sentiment. South West Water is doing just that.

We aim to become a different kind of water company, as we scale up investment in the environment, kickstarting our race to Net Zero by 2030, focusing on sustainable living, championing renewables and reversing carbon emissions, and delivering sustainable solutions for customers, communities and the regions we operate in.

Our New Deal business plan includes our largest ever environmental programme in 15 years. Our award winning Upstream Thinking programme has driven an increase in the region's biodiversity over the past 15 years and during 2020/21, we have realised another c.20,000 hectares in key catchments, improving both water quality and natural capital in our region. Our treeplanting commitment to plant 100,000 trees by 2025 has been achieved, and we continue to work closely in partnership with wildlife charities, national parks and farmers to deliver continued environmental benefits.

Getting the basics right is also core to what we do. This year, demand for our resources and access to clean drinking water has been the highest it's ever been. We are focused on delivering for our customers and ensuring quality is of the highest standard.

INNOVATION TO DELIVER A NEW RELATIONSHIP WITH CUSTOMERS

I believe there's no better way to respond to or capture public sentiment than building a deeper relationship with customers – really engaging with them and putting them at the heart of our decision-making.

That's why, as part of our New Deal K7 business plan, we launched our innovative WaterShare+ scheme, sharing £20 million of outperformance with customers, and giving them not only a say in what we do, but a stake too.

One in 16 households in our region are now shareholders in our parent Company Pennon as well as customers, heralding a new era in customer ownership – a true partnership. Our new independent WaterShare+ panel have now held two quarterly panels with customers and it's providing a strong platform to empower customers. This is just the start of real and honest customer engagement, with a richer and deeper relationship with customers.

We're also tapping into the social consciousness of our customers in new ways – having just launched South West Water's industry first Water-Saving Community Fund, empowering customers to champion and drive initiatives to save water locally, whether that's using rainwater to flush a public toilet, or water butts in community allotments. Our new Neighbourhood Fund is also supporting communities with well needed help and support to build back better post the pandemic as well as encouraging employees to give an hour to support communities and causes close to their heart.

OPERATIONAL DELIVERY – DRIVING IMPROVED PERFORMANCE AND AGILITY

South West Water has made a robust start to K7, thanks to the tireless efforts of all our employees, and continues to demonstrate resilient performance, even through the pandemic. c.80% of ODIs are on track or ahead of target, as we focus on operational delivery, efficiency and innovation. Year on year, we are able to report improving water quality, reduced customer supply interruptions and a resilient service and consistency of supply. 2020 was the 24th consecutive year without water restrictions in the South West Water region as well as maintaining Bournemouth Water's track record of none. Additionally, we are seeing a reduction in sewer collapses and internal flooding incidents and improved wastewater compliance.

We care deeply about the environment and we have also been redoubling efforts in those areas where performance isn't where it needs to be, particularly around pollutions. We have halved the average monthly pollutions since implementing a new plan in September 2020, closing the gap through innovation, root cause analysis and improving control systems. This, together with additional resources, training and a relentless focus on delivering for customers and the environment – building stronger engagement with regulators, employees and the public – is the key to improvement.

For UK Water, this has been an unprecedented year operationally. We are accustomed to peak demand over the traditional tourist seasons and this year has been no exception but unusually we have also had higher underlying demand with more dispersed usage across our network away from our more concentrated urban environments. We have the largest proportion of second homes in Devon and Cornwall, and overall consumption has been higher than the previous year, with household consumption up +9% net of business usage down -22%.

We have concentrated on our customer's top priority of a continued supply of clean drinking water and we have not had water restrictions despite the higher demand. We have however, missed our leakage target this year despite significant activity on the network. We have got a targeted plan in place to recover our performance, and in recent weeks we are already seeing an improvement to our position.

A RESPONSIBLE BUSINESS IN THE COMMUNITIES WE SERVE

The South West's economy has been one of the hardest impacted by the pandemic, and as a responsible employer in the region, South West Water has focused on opportunities to make a bigger societal contribution with our Green Recovery Initiative. We were pleased that our proposals to provide much needed investment, have been provisionally approved by Ofwat, with a range of projects focused on improving public health, protecting the environment and addressing climate change. Up to 500 jobs will be created across the region as well as opportunities for our existing workforce to gain new green skills.

We have also continued to expand our innovative affordability and WaterCare programme, undertaking over 3,600 virtual visits to homes and households struggling to meet financial commitments and helping to unlock £2.4 million in support funds for customers. We have also seen an 11% increase in customers benefiting from one or more of our social tariffs.

Our societal responsibilities also extend to promoting social mobility, addressing inequality, providing secure employment and ensuring that people are paid fairly for work today and in the future.

I am therefore proud to announce that South West Water has become a Living Wage Foundation employer and also one of the first companies in the South West to take placements as part of the government's Kick Start scheme – offering 16-24 year olds from disadvantaged backgrounds the opportunity for paid work at South West Water in a variety of roles, and we hope they will join permanently. We have also been extending our apprenticeship programme, aiming to attract 500 apprenticeships over the next five years and for 2021 announced a new Graduate scheme, bringing in talent and future leaders for the next generation.

LOOKING AHEAD TO FUTURE GROWTH

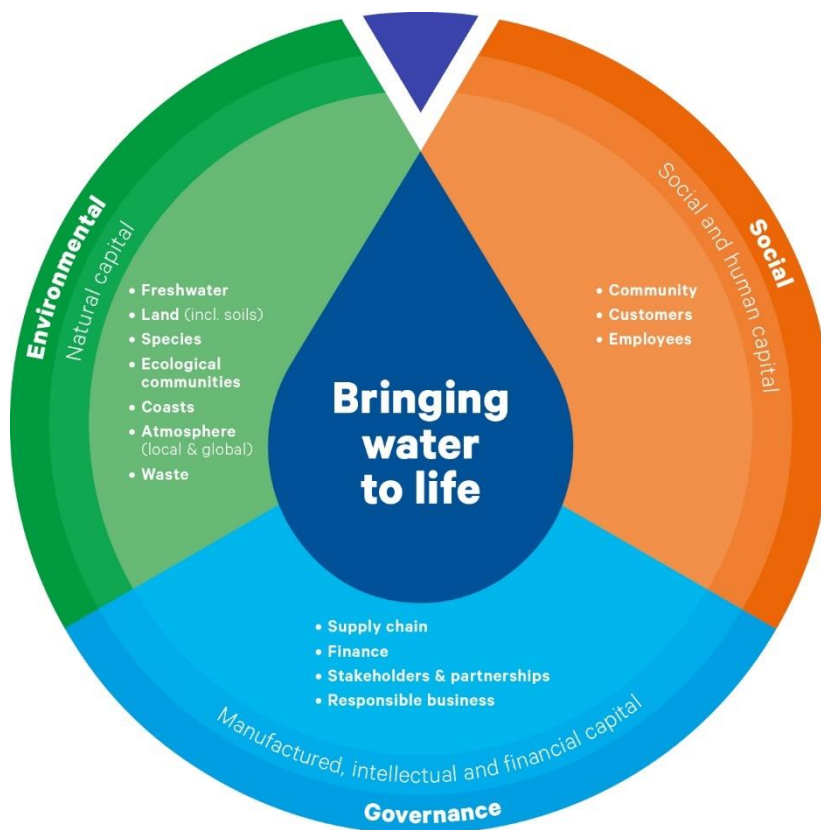
South West Water continues to be firmly focused on leading, transforming and optimising water and wastewater services. 2020/21 saw the expansion of our licence to include the Isles of Scilly, and work is well underway to deliver critical investments to improve infrastructure and assets.

We will also continue to invest in environmental infrastructure projects that realise new revenue streams. If the first year of my tenure as Group Chief Executive Officer has taught me one thing, it's that with a great team around you, you can achieve anything, innovating and creating agility, whatever the circumstances. I believe South West Water, and everyone who works in it, has a clear ambition to deliver on our purpose, for the benefit of all our customers, shareholders and stakeholders, providing a safe and secure future for all, people and planet, and a strong platform on which to grow.

Susan Davy
Chief Executive Officer

ESG STRATEGY

Our ESG strategy continues to deliver during a year of significant change. Highlights over the past year include the creation of our new ESG Capitals Strategy and Framework including new ESG targets. We showed strong performance across external ESG ratings demonstrating our commitment and management of risk across the ESG agenda.



ENVIRONMENTAL Natural capital - protecting enhancing our environment for generations to come	
Freshwater Land (incl. soils) Species Ecological communities Coasts Atmosphere (local & global) Waste	<p>c.20,000 Hectares enhanced for biodiversity</p> <p>c.100,000 Trees planted</p> <p>5 4 EEL passes and 1 EEL screens installed</p> <p>>11,500 MWh of renewable energy generated</p>
SOCIAL Social and human capital - supporting our people and communities	
Community Customers Employees	<p>96 New talent recruited (apprentices, graduates, kickstarts)</p> <p>73% Great Place to Work Score</p> <p>>2 million visitors to our region</p> <p>70% Customer satisfaction with value for money</p>

GOVERNANCE

Manufactured, intellectual and financial capital - being a responsible business for all our stakeholders

Supply chain Finance Stakeholders & partnerships Responsible business	Improved Sustainability ESG scores 75% of Debt raised through Sustainable Finance Framework 117 engagements with investors Maintained asset health
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OUR CAPITALS STRATEGY

Our intention is that our new Capitals Framework will support decision making to deliver the best outcomes for our customers, communities and the environment. The reporting of our capital performance ('net impact') is one phase of our planned capitals implementation which includes:

- Applying appropriate valuations to inform our understanding and use of capitals information
- Embedding our capitals approach in our decision making and plan making
- Enhanced disclosure and assurance of our performance
- Collaboration with regional partners to apply capitals thinking in practice
- Enhanced reporting and assurance of our performance.

CASE STUDY: NATURAL CAPITAL THINKING

USING 40,000 TREES TO HELP IMPROVE BATHING WATER QUALITY IN COMBE MARTIN

An ambitious project to plant 40,000 trees to help improve bathing water quality in Combe Martin began in early 2021. South West Water in partnership with local landowners, North Devon Biosphere Foundation, the Environment Agency, the Woodland Trust and Natural England's Catchment Sensitive Farming Partnership will identify areas where tree planting, hedging and fencing can help protect the River UMBER from bacteriological contamination. The River UMBER flows into the sea at Combe Martin beach and can affect bathing water quality, especially during wet weather.

ESG KPI PERFORMANCE

Our ESG targets were informed by a review of the issues we and importantly our stakeholders considered of greatest importance.

2020/21 KPI	2020/21 PERFORMANCE	COMMENTARY
ENVIRONMENTAL		
To achieve at least a B-rated 'CDP Climate' disclosure assessment score.	Achieved	Achieved 2020 B rating. Replaced with greenhouse gas reduction KPI under Atmosphere .
To achieve zero serious/major or significant environmental incidents (category 1 & 2)	Missed	Three category 2 incidents in 2020. Updated in 2021/22 to reflect category 1-3 as per south west water regulatory commitment under Freshwater .
Achieve 5% biodiversity net gain across all sites with biodiversity management plans in place.	Achieved	New wildflower meadow delivered 293% improvement in biodiversity units (2.16 Biodiversity Units) at Roadford Reservoir. New KPI under Species .

2020/21 KPI	2020/21 PERFORMANCE	COMMENTARY
Evaluate relevant operational areas and projects for net natural capital gain (using defined methodology), demonstrating 3% year on year improvement from a 2019/20 baseline.	Achieved	Our 2020/21 natural capital account shows an overall improvement above 3% from the 2019/20 baseline. Our expanded capitals framework and the KPIs associated with this will replace this target for 2021/22.
SOCIAL		
Evaluate relevant operational areas and projects for net social capital gain (using defined methodology), demonstrating 3% year on year improvement from a 2019/20 baseline.	Achieved	Our 2020/21 social capital account shows an overall improvement above 3% from the 2019/20 baseline. Our expanded capitals framework and the KPIs associated with this will replace this target for 2021/22.
Annual targeted reduction in Lost Time Injury Frequency Rate (LTIFR) with overall target of 0.5 by end of 2024/25	Behind target	There have been 29 LTIs during the year, resulting in an LTIFR of 1.59. The Homesafe programme and re-focused H&S efforts within the operational businesses should deliver an improving trend to get us back on track for our long-term target of 0.5 by 2025. Target retained under Employees .
Annual targeted improvement to increase proportion of female employees in the group from 21% in 2019 to 25% in 2022.	On track	At 31 March 2021, South West Water has 22% female employees. We have updated the KPI to target at least 30% female employees in the Group by 2022.
Achieve a 65% trust index score by 2021/22, as measured by our great place to work employee survey, demonstrating continual improvement in building an engaged workforce.	On track	Trust index score rose to 66% in 2020/21. We achieved the Great Place to Work accreditation which we look to retain in 2021/22 as part of the new Employees KPI.
GOVERNANCE		
Achieve upper quartile scores in our peer group for leading external ESG disclosure assessments.	Partially achieved	Majority ESG ratings and indices improved or maintained score with FTSE4Good score in 2020 an exception and expected improving trend in 2021 score. New ESG KPI focus on Sustainalytics ESG rating under responsible business.
Ensure 2% year-on-year increase in customer satisfaction from a 2019/20 baseline.	Achieved	C-Mex performance is has improved by 6% at 80.96 (against a 2019/20 baseline of 76.35).C-Mex has been retained as a customer satisfaction target under Customers element.
Targeted annual application to ensure all suppliers are 100% compliant with the objectives identified within our Sustainable Procurement Policy by end 2021/22.	On track	Supplier ESG engagement and reporting programme to begin in 2021/22. KPI retained under Suppliers .

PRIORITY PROGRAMMES

Our priority programmes focus progress in particular areas of our ESG strategy. COVID-19 has of course impacted progress on some aspects but at the same time has accelerated other areas for example infrastructure to support smarter working programme. We have decided to extend these programmes a further year (2021 to 2022). A summary of progress in 2020/21 is provided below.

COMMUNITY BENEFIT AND SOCIAL VALUE

We launched our 2020 to 2050 community vision “To sustainably improve our services while having a positive impact on the communities we serve and the people we employ.” As well as announcing a new Neighbourhood and Water-Saving Community Fund providing direct support to community groups and initiatives. We will be building on these programmes over the coming year whilst establishing ways to better measure our community impact to support our capitals framework and place-based approaches to investment.

SUSTAINABLE TRANSPORT, TRAVEL AND SMARTER WORKING

COVID-19 has meant the planned roll out of new agile working approaches was necessarily accelerated which enabled all of our office based staff who were able to work effectively from home as a result of the lockdowns. The new IT capability has facilitated new ways of working which will now continue post lockdown.

We are undertaking trials of new electric vehicles (EV) with the ambition to roll out further EVs across our fleet in support of our Net Zero strategy and we have announced continued support for sustainable travel choices such as the cycle to work scheme.

CIRCULAR WORKPLACE

Our employees told us in our recent company survey that we should be a leader in sustainability. The objective of the programme is to ensure a consistent approach to workplace sustainability, to implement and maintain the best standards possible at our head office and to facilitate improvements in Company wide sustainability in our workplaces. This will involve employee engagement on sustainability best practice, collaboration with our key service providers, provision of new recycling infrastructure at our sites and link across to operational focussed energy efficiency, waste management and water efficiency programmes.

ESG PERFORMANCE – EXTERNAL BENCHMARKING

Our ESG performance is assessed by a number of independent ESG rating agencies. Our performance across these assessments is a useful indicator of our progress with our ESG strategy both in confirming ESG topics where we are performing well, but also, importantly, areas we still need to improve. Overall we improved or maintained performance across all indices except FTSE4Good (based on March 2020 assessment). We have worked hard over the past year to improve our overall ESG performance and disclosures and are confident this will return an improving trend when the 2021 scores are announced.

EXTERNAL ASSESSOR	ASSESSED SCORE	
Sustainalytics	16.8 ESG risk (previous rating: 19.9)	75/100 ESG rating (previous rating: 69)
MSCI	AA MSCI ESG Indexes (previous rating: AA)	
Dow Jones	52/100 (previous rating: 49/100)	
CDP	B Rating CDP Climate change rating (previous rating: B)	B- CDP Water Security (previous rating: B-)

FTSE4Good	3.5/5 (previous rating: 3.6/5)
ISS	Prime status ISS Corporate Rating (previous rating: Prime)
GRESB	B GRESB Infrastructure public disclosure (previous rating: B)

ESG KPI PERFORMANCE

2021/22 KPIs

We have updated our 2021/22 ESG targets, as set out below to reflect the new strategy and expanded ESG Capitals framework.

We will create new 3-year targets over the coming year (for the period April 2022 – March 2025). To inform this update, we will review our materiality assessment, the UN Sustainable Development Goals (SDGs) and how our new targets can further support implementation of the goals.

ENVIRONMENT		
Capital	Target	Link to SDG
Species	Deliver our biodiversity enhancement target of 93,150 hectares (cumulative) of land in active management	SDG 15 – Life on land
Ecological communities	Plant 50,000 trees per year towards our new target of 250,000 by 2025	SDG 15 – Life on land
Land & soils (incl soils)	Restore 300 hectares of peatland across the South West	SDG 15 – Life on land
Freshwater	Reduce water use within our operations by 6 Megalitres/day	SDG 12 – Responsible Consumption and Protection
	Reduction in category 1-3 pollution incidents per 10,000km sewers	SDG 6 – Clean water and sanitation
Atmosphere (local & global)	Reduce scope 1 & 2 (market-based) emissions by 3% towards our Net Zero 2030 target	SDG 13 – Climate action
	Increase renewable generation (MWh) by 4%	SDG 7 – Affordable and clean energy
Coasts	Improve bathing water quality at 2 designated bathing waters / beaches	SDG 14 – Life below water
Waste	Improve our operational waste recycling rate by 2%	SDG 12 – Responsible Consumption and Protection
SOCIAL		
Employees	Maintain the Great Place to Work accreditation	SDG 8 – Decent work and economic growth
	Increase REACH ⁽¹⁾ recruitment by 2%	SDG 5 – Gender equality
	Increase the proportion of female employees in the Group to at least 30%	SDG 5 – Gender equality
	Target top 25 ranking in Hampton Alexander Index	SDG 5 – Gender equality
	Targeted reduction in Lost Time Injury Frequency Rate (LTIFR) at 1.1 (23 LTIs) with overall target of 0.5 LTIFR by end of	SDG 3 – Good health and well-being

	2024/25	
Customers	2% year on year increase in SWW C-MeX ⁽²⁾ performance	SDG 6 – Clean water and sanitation

Community	Increase number of community investment schemes supported we support by 20	SDG 11 – Sustainable cities and communities
	Increased visitor numbers to our region by 2%	SDG 11 – Sustainable cities and communities
GOVERNANCE		
Responsible business	Achieve Sustainalytics ESG Rating Score of 75 or above	SDG 12 – Responsible consumption and protection
	Maintain asset health as measured by performance across basket of asset health metrics	SDG 6 – Clean water and sanitation
Finance	Target 50% of total finance raised within the Sustainable Financing Framework	SDG 8 – Decent work and economic growth
	Target 30,000 customers on one of our support tariffs	SDG 1 – No poverty
Supply chain	Target 100% compliance with the objectives within our Sustainable Procurement Policy	SDG 11 - Sustainable cities and communities
	Pay all our suppliers within 30 days	SDG 8 – Decent work and economic growth

⁽¹⁾Race, Ethnicity and Cultural Heritage (REACH)

⁽²⁾C-MeX – Customer Measure of Experience

OUR GREEN RECOVERY INITIATIVE

The South West's economy has been one of the hardest hit by COVID-19, and as a responsible business in the region, South West Water is focused on opportunities to make an even bigger and more societal contribution.

Our Green Recovery Initiative provides much needed investment that will support the creation of up to 500 additional jobs across our regions over the next four years and provide further opportunities for South West Water's existing workforce to gain new green skills.

Our Initiative has been supported by our customers with an acceptance rating of 81% along with support from South West Water's independent WaterShare+ Advisory Panel.

Following a detailed assessment by Regulators, in early May, Ofwat published their draft green economic recovery decision, outlining £81 million of additional environmental investment, with no impact to customer bills up to 2025.

Our proposals incorporate an important and manageable set of schemes in addition to our existing business plan commitments through to 2025, and allows us to take extra action on the most pressing environmental issues reflecting our customer priorities:

- **Knapp Mill water treatment works advancement** – completion of a new water treatment works in Christchurch for Bournemouth Water customers, 18 months ahead of current schedule, benefiting c.160,000 customers with a more reliable, high-quality water supply
- **Water resources grid enablement** – protecting water resources for future generations for c.250,000 customers, addressing supply risks in North Devon, and supporting resilience in other parts of the country
- **Smarter, healthier homes** – empowering customers to save water, save money and have even safer and more resilient supplies to their homes, through new pilot initiatives to trial ways to help customers save water, protect customers from the costs of supply pipe failures, and reducing health risks from lead pipes
- **Transforming river quality** – reduce harm from storm overflows and piloting approaches to achieving river bathing water quality for the benefit of all those who use them
- **Catchment management** – an extension to our award winning land regeneration schemes using nature-based solutions which improve water quality, alleviate flooding, enhance natural habitats and reduce the South West’s carbon footprint on the road to achieving Net Zero.

NET ZERO STRATEGY

As part of a world first national sector-wide commitment of its kind, we have made a commitment to Net Zero Carbon by 2030. Additionally, we have signed the Race to Zero pledge through which we will extend the activities in our Net Zero boundary towards a 2045 target. Our commitments will focus our strategy enabling us to transform into a different kind of water company. South West Water’s approach to Net Zero is aligned to our purpose and values as a responsible business.

THREE KEY PILLARS

Our strategy is structured around three key pillars:

Sustainable living

- Reducing emissions through changes to our operational practices, increasing energy efficiency, and switching to lower carbon fuel sources.
- Meeting our commitments to reduce leakage and help customers to use less - protecting the environment and saving carbon.

Championing Renewables

- Maximising our own self-generation of renewable energy at our sites across our region - working with partnerships and utilising our expertise.
- Where we cannot generate enough ourselves to meet all our needs, 100% of the energy we purchase will be from renewable sources.

Reversing Carbon Emissions

- Working in partnership to deliver natural carbon sequestration through activities such as peatland restoration and tree planting.
- Supporting the development of innovative solutions to develop low carbon footprint processes through research and development (R&D).

ALIGNMENT TO ESG STRATEGY

Our new ESG Capitals framework and strategy on page 16 will ensure carbon is integrated into our decision making but also that net zero plans consider wider environmental and social impacts.

MORE THAN JUST CARBON

Our tree planting and peatland restoration activity will contribute to global climate regulation through protecting and enhancing these natural carbon stores as well as delivering further local environmental and societal benefits or 'ecosystem services' such as flood protection and water quality improvements.

NEXT STEPS ON OUR NET ZERO STRATEGY

We will look to transparently report our progress towards our Net Zero targets both in terms of our overall footprint and our wider contribution to positive climate action.

We are committed to better understanding emissions sources across our value chain. For example we have estimated and reported Scope 3 emissions for the past two years and we will expand our collaboration look to work with our key suppliers to obtain more specific information on emissions associated with the goods and services they supply.

As our Net Zero Carbon journey evolves, we will report progress so we can work collaboratively with our stakeholders towards our common climate goals.

OUR PEOPLE

At South West Water, we believe our people are our best asset. Our people strategy, approved by the Board in 2017, 'talented people doing great things for customers and each other' means that we are focused on doing everything we can to recruit, train, develop and support all of our employees, whatever their background, experience or outlook, unlocking their potential now and for the longer term.

SUPPORTING OUR EMPLOYEES THROUGH A CHALLENGING COVID-19 YEAR

We have always been fully aware of the essential service we provide for customers and the requirements to ensure that whatever the weather or circumstance, we must keep water flowing 24 hours a day, seven days a week. COVID-19 has tested all industries this year and we have remained fully focused on supporting our employees throughout to ensure we remained resilient and provided our lifesaving product and services for our customers.

We have ensured that none of our employees were furloughed or made redundant as a result of the pandemic and all employees who were shielding, self-isolating or supporting family members were on full pay. We made this decision at the start of the pandemic and remained committed to it throughout the year to protect our employees and ensure we were able to provide the essential services for our customers.

CREATING A GREAT PLACE TO WORK

Responsible and trusted businesses today have a duty to make a positive societal contribution – whether that's through promoting social mobility, addressing racial and gender inequality, or in providing secure and meaningful employment where all employees are paid fairly for the work they do.

At the heart of any great business are the people who work in it. With 1,650 employees, our people strategy is centred around talented people doing great things for customers and each other, and creating the best place to work.

We want to be the best place to work for our employees and we value the expertise, dedication, adaptability, flexibility and commitment of everyone who works with us as one amazing team. We know companies with high trust cultures enjoy better financial results, outperform the market by 2 to 3% a year over a 25-year period, have strong leadership, a talented workforce and are more collaborative and innovative.

This year we asked our employees how it feels to work for South West Water using Great Places to Work Best Workplace Survey™, consistent with other companies across the Pennon Group. We achieved our highest ever participation rate of 81% and have officially passed the threshold to become accredited as a Great Place to Work with a South West Water Trust Index © increasing to 66%. This is a 4% increase on last year and significantly higher than that national average of 53%.

The survey measures effectiveness in a range of categories including Innovation, Maximising Human Potential, Values, Leadership Effectiveness and Wellbeing. Our most improved category was Values, demonstrating that we are becoming a purpose led and value driven organisation. The Company's highest scoring questions for 2021 included people being treated fairly regardless of their race (93%) or their sexual orientation also (93%) in recognition of the Company's approach to diversity, respect and inclusion and my manager takes health & safety seriously (90%) and I understand my safety-related responsibilities (90%) confirming our approach to health & safety being our number one priority.

These results show we have made good progress during the year in embedding the Company's HR strategy but importantly in a year dominated by COVID-19, how we have worked hard to ensure our employees have felt supported.

LISTENING AND ACTING ON EMPLOYEES' VIEWS

Under the Financial Reporting Council's (FRC) code of standards, companies are required to explain how they are incorporating employee views in Board decisions.

Over the course of this year, we have continued to develop and evolve the opportunities for employee's views and input as well as enabling staff forums across the Company to ensure employees are represented and have opportunities to understand and feed into the discussions on matters that impact them and the work they do.

EMPLOYEE FORUMS

The South West Water Employee Engagement Forum has become a well-established forum who meet regularly to create a two-way communication between senior managers of the Company and employees and this year has been chaired by the Group Chief Executive Officer. This forum helps to influence and support business changes and ensures that our employees are front and centre in all that we do, including being the employee voice in the evolving changes to working arrangements in response to COVID-19 during the year. We also have trade union recognition agreements in place for our Craft and Industrial employees and continued to meet frequently across the year to discuss relevant topics including the modernisation of our pension schemes, pay awards, business planning, employee survey and engagement, IT system developments and innovation.

Our Speak Up whistleblowing policy continued to operate throughout 2020/21 providing another engagement channel. Speak Up helps to create an open, transparent and safe working environment, where employees feel able to speak up and are supported if they do so.

Over the course of the year, the Group-wide Pennon Big Chat evolved to become Your Big Chat, moving from a conference call facility to video enabled, enabling all employees access to the Group Executive and creating opportunities to ask questions and suggest topics that employees would like to hear more about. The frequency was also increased to weekly to ensure regular and timely updates are provided to employees. We continued to receive positive feedback from employees who welcome the opportunity to hear from the Directors and ask them question on key business matters. In line with government recommendation, where possible, many of our office-based teams have been working from home, placing greater importance on supporting our employees with timely communications. Discussions have largely focused on health & safety, Coronavirus working arrangements, employee wellbeing, business plan delivery and investments in apprenticeships and future workforce development.

For our remote teams, working tirelessly during the pandemic, we have carried out regular breakfast briefings hosted virtually by the Group Chief Executive Officer and other senior leaders and these have proved to be helpful in promoting more effective two-way communication. Additionally, all employees are invited to pose questions or comments to the Group Chief Executive Officer following the introduction of AskSusan and this has developed into a popular route for further engagement.

DIVERSITY AND EQUAL OPPORTUNITIES

Building a sustainable, agile and diverse workforce is a key pillar of our HR strategy. We have continued to make progress in this area through strong leadership and our gender diversity has improved for the third year running.

Across South West Water, the workforce comprises 1,650 employees with a gender split of 78% male and 22% female, unchanged from the prior year. Our permanent workforce is supported by 114 temporary and agency employees.

Female membership %		
	2020/21	2019/20
The Board	57	25
Executive Management Team	57	43
Senior Management	33	11
Company	22	22

Note: Senior Management includes members of the Executive Management.

South West Water supported International Women's Day on 10 March 2021– an annual worldwide event that celebrates women's achievements, while calling for gender equality. We promoted the day on our social media channels and held a virtual get together for employees to share personal experiences, talk about role models and inspirations and celebrate our employees and their stories.

South West Water largely operates and employs people in the South West of England which traditionally has some of the lowest proportions of ethnic diversity in the country. However, as a responsible business, we believe we have an important role in ensuring we support mobility of all types. Sometimes assumptions can be made, and actions taken, which unintentionally affect certain groups of people in a negative way, leading to a lack of opportunity, difficulty in accessing services or a failure to have a need identified. With less than 1% of employees currently self-identifying as BAME, we want to change this, either by encouraging our existing employees to have the confidence to share their backgrounds, or by encouraging diversity in our recruitment and attraction.

In 2020, South West Water pledged its support to the CBI Change the Race Ratio initiative, a campaign to increase racial and ethnic participation in the senior leadership of companies, as a route to encouraging more diversity at all levels and was the first water company to do so.

One of the ways we intend to achieve this is by become a sponsoring business of the 10,000 black interns initiative. We have signed up to support the programme next year and see this as an important scheme to not only offer black students an opportunity to understand our business but also to improve the levels of ethnic diversity across our industry.

RECRUITMENT

Changing our approach to diversity and inclusion has also changed the way we monitor diversity in all Company job applications. The Company now uses a software gender decoder tool which allows us to check all our job advertising for masculinity to reduce the potential risk of alienating female applicants. In addition, we have refreshed our equal opportunities forms to be included in all onboarding packs. The new version allows us to monitor, analyse and utilise diversity data to inform and shape our business activities to become a more diverse workplace.

TRAINING

We have also commenced a new programme of unconscious bias training and will roll this out to most leadership and all hiring managers during the coming year. Across South West Water we have been undertaking Lived Experience Group sessions to understand what it is like to work at South West Water for employees from minority groups. The outputs have been shared with our Diversity Committee to understand these perspectives and consider appropriate actions when issues are raised.

WOMEN IN WATER NETWORK

South West Water is part of the Women in Water network, supported by Water UK, and aims to encourage women into the water industry, support their development into more senior roles and ensure that their industry voices are heard.

OUR GENDER PAY GAP

This is the fourth year where employers in Great Britain with more than 250 staff have been required by law to publish their gender pay gap on their own website and on a government website. The current national average gender pay gap is 15.5% for all employees. Our gender pay data for 2020/21 improved to 4.9% from 5% last year. In Source Contact Management Limited, our customer facing business which is a subsidiary of South West Water, is now reporting a negative pay gap of -1.4%, a 7% improvement from 5.7%. This means that the average female hourly pay is marginally higher in Source Contact Management than that of their male colleagues for the first time.

According to Energy & Utility Skills, across the water industry workforce, 20% are identified as female which places South West Water, at 22%, ahead of the sector average.

The Board promotes equality of opportunity and diversity across all areas, including gender and ethnicity. The Company has more to do in this area which remains a key focus.

TRAINING AND DEVELOPMENT

We have a strong commitment to investing in the development of our employees and want to build and recognise talent across the Company. Training and development is available for employees at all levels within the organisation. Our aim is to increase productivity, job satisfaction and safety, and to equip the next generation of leaders and employees with appropriate knowledge, skills and the competencies they need to thrive.

We continue to embrace apprenticeships and since 2017, we have started 377 new apprentices across the Company. This has increased by 50 during the past year with greater focus on recruiting operational apprentices to ensure we have the future skills to deliver our essential services. To further demonstrate our ongoing commitment to apprenticeships, we have set a Group target to offer 500 new apprenticeships over the next 5 years. Find out more online at www.southwestwater.co.uk/careers/apprenticeships.

More recently we have launched our 2021 graduate programme and will look to offer 20 new graduates the opportunity to experience a 2-year structured programme of training, work experience and career development before moving into key permanent roles across our group. The programme enables graduates to gain practical experience in our core business areas of Operations; Engineering; Projects; and Customer Service which will be vital in helping them find their ultimate leadership position.

During the year we have delivered 9,905 training days for our 1,650 employees, ensuring that on average each employee has received 44 hours of training.

We have developed a new senior leaders talent development programme to provide structured assessment and development opportunities for our top 50 leaders.

Our Company turnover rate in 2020/21 was 7%. This is significantly lower than the 10.2% seen last year which reflects the lower turnover experience across the country due to Coronavirus.

RESPONSIBLE EMPLOYER

As a responsible employer, South West Water has worked hard during the year to mitigate and minimise the impact of COVID-19 on our business activities and the potential knock on effects for customers and employees. South West Water has not taken any government furlough funding and has not made any COVID-19 related redundancies.

We continued to live our values and demonstrate we are a responsible employer during the year, doing what we can to support communities in the South West. South West Water, as part of the Pennon Group, was therefore one of the first companies to sign up to participate in the government's new Kickstart scheme this year, offering 16-24 years olds, deemed at risk of long-term unemployment, six month paid work placements and have committed to 50 placements.

As part of the Pennon Group, we also continue to be a signatory of the Social Mobility Pledge, the cross-party campaign to improve social mobility in the UK established by the former Rt Hon Justine Greening MP. This pledge reflects our social commitments through our partnerships with local schools, our open-door approach to visitors and our provision of work experience opportunities. As part of our Social Mobility Pledge, we are undertaking a gap analysis to help us develop a detailed action plan to drive further improvements during this year. Our head office and customer call centre are based in Exeter, providing jobs and investment to the local community.

Also, as part of the Pennon Group, we have maintained our membership of the Slave-Free Alliance, which is part of Hope for Justice, the global anti-slavery charity. Our membership demonstrates our commitment to the highest employment standards for both our direct employees and those within our supply chain.

We are fully supportive of the principles set out in the UN Declaration of Human Rights and the Group ethics policy outlines the high standards of employment practice with which everyone in the Company is expected to comply. The Company also supports the International Labour Organization's core conventions for the protection and safety of employees wherever they may work throughout the Company. These standards are also embedded in our sustainable supply chain and documented in our procurement policy and code of conduct for supply chain partners.

HEALTH, SAFETY & WELL-BEING

The health, safety and well-being of our employees is paramount. At South West Water, we believe everyone who works for us and with us, should go home safe to their families and loved ones every day, and this has never had more resonance than in the current climate. Keeping our employees Covid-safe and our work environments Covid-secure has been our top priority throughout 2020/21 and we have worked hard to support employees physically and emotionally.

HOMESAFE

The Company's flagship health & safety programme, HomeSafe, has continued to provide the framework for all health & safety related activities, and in response to COVID-19, a COVID-19 Steering Committee has met weekly supported by a COVID-19 Management Team who have overseen our approach to keeping employees safe including case management of suspected cases, occupational health support, employee communications, approach to testing, facilities management and ongoing policy and guidance. More broadly, through the Local Resilience Forum in the South West, we have continued to play an active role externally, supporting the localised industry response to the pandemic, as well as the transition from the EU.

To better support employee's well-being and mental health, our e-learning module on Mental Health was reissued to all employees and we also extended our Employee Assistance Programme to include family members, allowing families to access trained independent counsellors for support.

E-LEARNING

E-learning has continued to be the main delivery mechanism for continued health & safety awareness during the reporting period and it was pleasing to see the high scores in the recent engagement but we still want to increase these further during the coming year. In response to the higher number of injuries continuing to being related to strains and sprains, we have introduced Olympian manual handling training techniques to its operational teams.

LITFR

LTIFR⁽¹⁾ continues to be the Company's primary measure of performance (1.59) and across the year reported 29 Lost Time Injuries compared to the 23 reported last year. Despite this increase, injuries reported to the HSE were the same as the previous year.

The higher levels of lone-working as a result of the pandemic restrictions may be an influencing factor in the increase of LTIs. The Group has engaged an external partner to embed enhanced training around manual handling techniques to help mitigate against this type of injury. Reports to the HSE were the same as the previous year. With a third of the injuries related to manual handling we have engaged international experts with an Olympic pedigree to carry out additional training for our most vulnerable workforce.

We have additional resources in the field to:

- Embed the HomeSafe behavioural principles
- Deliver quicker asset investment to improve site safety
- Increase volume and quality of reporting to facilitate future analytics
- We are working at a WaterUK level to collaborate on data analytics
- There were no HSE prosecutions

During the year we also carried out independent benchmarking to help us better understand our strengths and development areas and this will be a key underpin for future plans. South West Water will also seek formal certification for its Occupational health & safety Management system to ISO 45001 standards. Our ambition for health & safety is to be the leader for health & safety in the UK water industry by 2025.

⁽¹⁾A lost time injury is defined as any work-related injury that results in a person being unfit for work on any day beyond the day of the incident. Lost time injuries are expressed as a frequency rate (LTIFR) per 200,000 working hours.

OUR OPERATIONS

This is the first year of K7 period (2020-2025) and South West Water has made a strong start in delivering its ambitious New Deal business plan, whilst continuing to deliver outstanding services, safely despite the global pandemic.

KEY FACTS

- 2.3m total population served
- 23 raw water reservoirs
- 653 wastewater treatment works
- 19,049 km wastewater mains network
- 18,433 km of drinking water mains network
- 43 drinking water treatment works
- 150 bathing waters

DELIVERING MORE OF WHAT MATTERS FOR OUR COMMUNITIES

SHARING OUR SUCCESS

Our innovative New Deal business plan, informed by our most extensive engagement programme to date. It sets out our focus to change the nature of our relationship with our customers. WaterShare+, a key aspect of our plan, was launched in October 2020, shared c.£20 million of outperformance from 2015-20 with customers, by offering a choice of a £20 credit to their bill or shares in our parent company, Pennon. We were delighted with the positive response to this trailblazing initiative, which saw one in 16 household customers opting to become Pennon shareholders and giving them a tangible stake in the business.

WaterShare+ also gives customers a greater say in what South West Water does and how the company is run. The independent WaterShare+ Advisory Panel meets in public on a quarterly basis (although held virtually where appropriate), with the panel reviewing South West Water's progress against targets and an opportunity for customers to have a real say in how the business operates.

This year South West Water will hold its first dedicated customer AGM in autumn 2021, designed to be more accessible for all customers who can hear and input into the company's plans.

SUPPORTING OUR COMMUNITIES

We recognise the importance of our role in the communities we serve, and we are committed to delivering more of what matters to them. During the year, we launched dedicated initiatives including our Neighbourhood Fund and the Water-Saving Community Fund.

The Neighbourhood Fund builds on our work to support our communities with funding available for community groups, offering physical activities, education, health and well-being and environmental improvements.

Community groups supported to date include The Hugs Foundation – offering therapeutic and supportive interventions for those suffering from mental ill health, social exclusion, disadvantages and disabilities, and the Cornwall Accessible Activities Programme – supporting families and children with additional needs to access activities during the school holidays.

Our Water-Saving Community Fund promotes ideas to get our customers and communities involved in water conservation projects including support for organisations to create drought tolerant gardens, install water butts in community allotments or provide educational training and displays in schools.

SUPPORT FOR EDUCATION

In partnership with the South West Lakes Trust, an innovative, interactive new education centre is being set up at Roadford Lake informing and promoting water efficiency and the benefits of our work on communities and the environment. It is hoped this centre can explain how we can all reduce water consumption, and the risk of sewerage blockages and pollutions through sewer misuse.

INNOVATIVE AFFORDABILITY AND WATERCARE PROGRAMMES

In our New Deal we made a pledge to eliminate water poverty by 2025 by expanding our toolkit of affordability support to those who need it most. During the year, our WaterCare advisors completed over 3,600 virtual home visits, unlocked c.£2.4 million of financial support ensuring customers are receiving all eligible benefits. We continue to expand our affordability toolkit with over 67,000 customers now benefitting from one or more of our social tariffs, representing an 11% increase compared to 2019/20.

OPERATIONAL DELIVERY – DRIVING PERFORMANCE THROUGH INNOVATION

South West Water has made a strong start to K7, driving performance and efficiency through innovation.

CLEAN, SAFE AND RELIABLE DRINKING WATER

Our focus remains on ensuring the supply of clean, safe and reliable drinking water, whilst protecting the precious natural resources within our region.

IMPROVING WATER QUALITY FOR CUSTOMERS

We continue to target improvements in the quality of water for customers and have seen a c.19% reduction in taste, smell and colour contacts over 2020/21.

During the year, we have introduced a range of innovative raw water management techniques including reservoir mixing at Longham Lake and through the introduction of sonic technology aimed at reducing algae from raw water sources to our treatment sites.

We continue to target further improvements through our planned c.£90 million investment in new treatment works in the Bournemouth Water region which with initial works commencing during the year.

MINIMISING CUSTOMER SUPPLY INTERRUPTIONS

We understand the importance that our customers place on having a reliable supply of drinking water, and the inconvenience that supply interruptions can cause.

During 2020/21, we achieved our best ever performance level of 5 minutes 38 seconds, a 39% year on year reduction for those customers who have an outage for more than three hours. We have also delivered a 80% reduction in supply interruptions over 12 hours.

A key component of our strategy includes a dedicated, in-house supply continuity and alternative water supply team. Alongside this we have introduced innovative technology enabling repairs to the network under pressure. We have also introduced enhanced training and forensic use of data analysis to support our focus on continuous improvement.

DELIVERING A RESILIENT SERVICE

During the year, demand has been higher than the previous year, as a result of the sustained stay at home measures during lockdown, along with a peak in demand driven by the hot, dry period in the spring and an increase in 'staycations' during the summer. Throughout the year, we successfully managed our water resources, balancing supply across the network to maintain safe and resilient supplies at all times, and our reservoir levels remain robust at 97%, broadly in line with the prior year.

2020 was the 24th consecutive year without water restrictions in the South West Water region and maintained Bournemouth Water's track record of no water restrictions ever.

Our customers feel very strongly that we should prevent water from being lost due to leakage, and we continue to invest significantly to prevent and manage leaks on our network. During the last few months of the year, South West Water saw record number of bursts as a result of a unique combination of winter weather and continued high demand due to customer behaviour during the multiple lockdown periods which has led to our leakage target not being achieved. To focus on recovering our performance in this area, we introduced a targeted leakage action plan, focused on leakage hotspots and have returned leakage levels to the level they were this time last year. During the year we also began trialling innovative combined smart meters with acoustic logging capabilities, helping to identify customer leaks and bursts quickly.

RELIABLE WASTEWATER SERVICES

REDUCING SEWER BLOCKAGES

During the year we have delivered a 20% improvement in the number of sewer collapses per 10,000km compared to last year with benefits arising from our K7 early start enhanced sewer cleansing and monitoring programme.

Sewer blockages are a lead indicator for possible flooding and pollution from our network. The reducing trend demonstrates that our programmes of work to reduce blockages in the network through investigating, cleaning and repairing sewers, and publicity campaigns will continue to help reduce the more significant impacts of pollution and flooding on our customers and the environment.

REDUCING INTERNAL FLOODING INCIDENTS

We understand the impact that sewer flooding has on customers, and we continue to do all we can to reduce the likelihood of these events. As a result of our unwavering focus in this area we are pleased to have achieved our stretching 2025 target in 2020/21 – a c.35% improvement from 2019/20. We achieved this through the continuous review of processes and systems to deliver improvements, including a range of initiatives such as educational campaigns aimed at influencing customer behaviours, hydraulic modelling, enhanced CCTV and a dedicated investigation team supporting proactive targeting.

IMPROVED WASTEWATER COMPLIANCE

South West Water has made considerable progress in improving the standard of the water it returns to the environment and over the past five years and we achieved our best ever performance of 99% for the number of compliant wastewater treatment works in 2020 as we work towards a goal of 100%. We have enhanced treatment processes by embedding innovative techniques including the use of I-Phyc's algae-based treatment to

sustainably remove phosphorus and micro-pollutants from sewerage. This nature-based approach is beneficial to the environment whilst reducing costs to operate with lower power and chemical consumption required.

BOOSTING BIODIVERSITY IN OUR REGIONS

Our award winning 'Upstream Thinking' programme has driven an increase in the region's biodiversity since 2005. During 2020/21, we have made improvements covering c.20,000 hectares in key catchments, improving both water quality and natural capital in our region.

We have delivered our commitment to plant 100,000 trees by 2025 and are increasing our target to 250,000. We continue to work closely in partnership with wildlife charities, national parks and farmers to deliver continued environmental benefits.

Our partnership with the North Devon Biosphere Foundation targets further improvement in water quality, quantity and soil health within the catchment. This project seeks to create a UK first landscape scale environmental intelligence programme harnessing artificial intelligence, big data, remote sensing & satellite earth observation to build real-time and predictive models.

The Smart Biosphere triggers a range of economic activity, integrated supply chain development, apprenticeships and jobs in the emerging environment and natural capital economy, whilst also mitigating flood risks, and improving catchment predictability.

ENVIRONMENTAL LEADERSHIP

Our New Deal business plan includes our largest environmental programme in 15 years, recognising that a healthy environment is vital for the long-term sustainability of the services we provide to customers.

BATHING WATER IMPROVEMENTS

We are passionate about protecting and enhancing our region's bathing waters. During the year we delivered capital improvements at four bathing waters, representing 50% of our commitment to 2025. The improvements to date include sustainable solutions such as sewer separation at Seaton in Cornwall with plans for separation at Dawlish and Budleigh Salterton in Devon. These projects help support our commitment to maintaining excellent quality, supporting the region's economy.

DEDICATED POLLUTIONS FOCUS DELIVERING RESULTS

Recognising that our performance for category 1-3 pollutions in the early part of 2020 is not where we had targeted, we launched a Pollution Incident Reduction Plan in the summer of 2020, which has made immediate and sustained improvements with a c.60% reduction in the number of wastewater pollutions on an average monthly basis since the plan was introduced.

We are committed to delivering a step change in our performance in order to achieve the challenging targets set for K7. Our plan centres around the following key initiatives:

- Root cause analysis – enhanced data modelling supporting proactive interventions
- Control systems and early warning – dedicated task force and 24/7 incident recovery
- Asset specific plans – accelerated investments at key hotspot locations
- Influencing customer behaviour – targeted educational campaigns

- Improving our environmental culture – additional training, resources and empowerment for local teams to find and fix issues immediately

LIVING OUR PURPOSE – A SUSTAINABLE FUTURE

Understanding our role in society is crucial to maximising the value we create for stakeholders. We are proud that our ongoing commitment to do the right thing, in the right way, has continued to deliver sustainable results providing essential services to customers and communities

NET ZERO BY 2030

South West Water are committed to achieving Net Zero carbon emissions by 2030 to support the drive for ambitious climate change action. Achieving Net Zero is the building block of our business strategy – enabling us to transform into a different kind of water company. Our plans are driven by a combination of activities, structured through three key pillars – bringing wider benefits to the South West.

- Sustainable living
 - Reducing emissions through operational practices, increasing energy efficiency and using lower carbon fuel sources
 - Meeting our commitments to leak less and help customers to use less - protecting the environment and saving carbon
- Championing renewables
 - Targeting c.50% renewable energy generation at our sites across the South West - working with partnerships and utilising our expertise in this area
 - Where we cannot generate enough ourselves to meet all our needs, 100% of the energy we purchase will be from renewable sources
- Reversing carbon emissions
 - Working in partnership to deliver natural carbon sequestration through peatland restoration and tree planting
 - Supporting the development of innovative solutions to develop low carbon footprint processes through research & development.

REPORT OF THE FINANCE DIRECTOR – FINANCIAL REVIEW

OVERVIEW

Despite the challenges posed by COVID-19 the performance of the business has been resilient. 2020/21 was the start of the new regulatory period and South West Water has made a fast start in delivering our New Deal business plan for customers.

The company has made a strong start to the new regulatory period and has doubled base Returns on Regulated Equity (RoRE) through continued outperformance in respect of totex⁽¹⁾ efficiency and financing, with continued low effective interest rates.

The momentum of totex efficiencies delivered to date in K7 is comparable to those in K6, with c.£70 million recognised during 2020/21 supported by efficient delivery, whilst advancing investments and additional expenditure on areas of focus including pollutions and leakage.

Our efficient financing strategy continues to drive outperformance with South West Water's effective interest rate at 2.5% (2019/20 3.4%), significantly lower than Ofwat's nominal cost of debt of 4.2%. Over half of the 90 basis point reduction from the prior year is linked to active management of our debt portfolio in the current rate environment, whilst the remainder relates to index-linked debt.

Despite the potential future impact of COVID-19, cash collections have remained robust with underlying bad debt costs c.0.5% of revenue, in line with last year and ahead of our K7 target.

Our innovative New Deal business plan set out our focus to change the nature of our relationship with our customers. WaterShare+, a key tenet of our plan, launched in October 2020, shared c.£20 million of outperformance from 2015 to 2020 with customers offering a choice of a £20 credit to their bill or to receive shares in Pennon Group, South West Water's parent company. We were delighted with the positive response to this initiative that saw one in 16 household customers in the region opting to become Pennon Group shareholders and giving them a tangible stake in the business.

Our business plan contained an ambitious programme of capital investment including two new water treatment works in Bournemouth. 2020/21 saw the commencement of these large projects in addition to important upgrades to other water and wastewater treatment work in addition to important improvements to our network.

Our New Deal business plan includes our largest environmental programme in 15 years, recognising that a healthy environment is vital for the long-term sustainability of the services we provide to customers. During the year we delivered capital improvements at four bathing waters, representing 50% of our commitment to 2025.

Following the UK Government's commitment to both build back better and build back greener, we were pleased to have been asked to consider ways in which we could support the green economic recovery. Our Green Recovery Initiative, developed with customers and stakeholders, proposed a set of schemes benefiting our region – delivering significant benefits for customers, society and the environment.

⁽¹⁾total expenditure

STATUTORY FINANCIAL PERFORMANCE

South West Water's statutory results show a decline in profit before tax to £141.8 million (2019/20: £171.1 million). In 2020/21 a non-underlying reduction in revenue of £20.5 million has been recognised due to the Watershare+ rebate scheme and a curtailment charge of £3.5 million in respect of the defined benefit pension scheme being closed to future accrual from 30 June 2021 (see note 6). In 2019/20 there was a non-underlying charge of £0.2 million relating to past service costs on the defined benefit pension scheme and a £2.8m charge relating to a COVID-19 bad debt provision.

REVENUE

Underlying total revenue has decreased by 1.3% to £564.3 million primarily reflecting the transition to the new K7 regulatory period, net of inflationary increases reducing bills and developer services revenue as a result of reduced construction activity during lockdown and subsequent restrictions, partially offset by a net increase in demand from COVID-19 with higher household demand (up by c.9% compared to last year), offsetting the expected reduction in non-household demand (down by c.22% compared to last year).

84% of our household customers in the South West area are now benefitting from a metered supply, with 3,636 customers opting for a meter in 2020/21 (2019/20: 5,065). 74% of households in the Bournemouth Water region are metered with 524 switching in the year (2019/20: 1,197).

EBITDA

Underlying earnings before interest, tax, depreciation and amortisation (EBITDA) were 6.4% lower than 2019/20 at £340.6 million (2019/20: £363.9 million). Underlying operating profit decreased by 9.3% to £222.3 million (2019/20: £245.2 million) and underlying profit before tax decreased by 4.8% to £165.8 million (2019/20: £174.1 million).

Operating costs have increased by £16.5 million (7.8%) compared to 2019/20 due to impacts of price changes on power and wages, volume changes and other one-off costs. South West Water's bad debt performance remains strong with a charge of 0.5% of revenue (2019/20: 0.5%), reduced from 1.7% at March 2015. This continues to be driven by efficient collections as we work with our customers to manage their debt and strive to support those customers in vulnerable situations with affordability challenges.

We continue to look to efficiently manage and optimise value from our estates portfolio, recognising a profit on sale of assets in the year of £0.2 million (2019/20: £0.4 million).

NET FINANCE COSTS

Underlying net finance costs of £56.5 million were £14.6 million lower than last year (2019/20: £71.1 million). This primarily reflects a higher average level of debt during the year offset by lower RPI on index linked debt and a lower Libor rate.

We have secured funding at a cost that is efficient and effective. Index linked funding represents approximately 25% of borrowing; at 2.5% the Company interest rate on average net debt for 2020/21 remains amongst the lowest in the sector (2019/20: 3.3%).

PROFIT BEFORE TAX

South West Water's underlying profit before tax was £165.8 million, a decrease of 4.8% compared with the prior year (2019/20: £174.1 million). On a statutory basis, profit before tax was £141.8 million (2019/20: £171.1 million) reflecting a non-underlying reduction in revenue of £20.5 million has been recognised due to the Watershare+ rebate scheme and a curtailment charge of £3.5 million in respect of the pension scheme being closed to future accrual from 30 June 2021 (see note 6).

TAXATION

The Company's mainstream UK corporation total current tax charge for the year (including prior year adjustments) was £24.3 million (2019/20: £24.9 million), reflective of an effective tax rate of 17.1% (2019/20: 14.6%). The higher effective rate of current tax reflects increased depreciation on qualifying assets relative to capital allowances, a lower prior year credit resulting from the agreement of historic tax liabilities with the tax authorities in the last financial year and a difference in the timing of relief for retirement benefit contributions. The Company had a current tax asset of £3.9 million at 31 March 2021, with current tax due being paid in four quarterly instalments during the year. The company paid tax of £24.7 million during the year in respect of periods 2018/19 to 2020/21, including £20.9 million paid to fellow group entities in respect of group relief.

Underlying deferred tax for the year (including prior year adjustments) was a charge of £3.4 million (2019/20: £9.8 million). This year there is a non-underlying deferred tax credit of £0.7 million (2019/20: £28.3 million charge). The underlying credit reflects additional pension contributions arising on the closure of the pension fund to future accruals, whereas the underlying charge in the prior year was primarily due to the restatement of the deferred tax liability for the change in rate of corporation tax.

Overall the total tax charge for the year was £27.0 million (2019/20: £63.0 million). The reduction being due to reduced profits after non-underlying charges and the absence of a corporate tax rate change restating deferred tax liabilities in the current year.

Although the Chancellor's March 2021 budget announced an increase in the UK corporation tax rate to 25% from April 2023, as this was not enacted at the year end. Current and deferred tax liabilities have continued to be calculated at 19% in these financial statements. The change was substantively enacted on 24 May 2021 and it is anticipated the change in tax rate will increase the tax charge and deferred tax liability by around £85 million next year. The next two financial years will also benefit from the increased super-deduction rates of capital allowances, this will reduce the current tax charge. However, this acceleration of capital allowance tax relief will be offset by a higher deferred tax charge and liability, including the increase in the future corporate tax rate.

DIVIDENDS AND RETAINED EARNINGS

The statutory net profit attributable to ordinary shareholders of £141.8 million has been transferred to reserves.

The Company has established a dividend policy which includes the following components:

- a sustainable level of base dividend growth, determined by a number of factors including the shareholder's investment and the cost of capital
- a further level of growth funded by efficiency outperformance
- comparison with the assumptions made by Ofwat in setting prices for the regulatory period.

Dividend payments are designed to ensure that key financial ratios are not prejudiced, whilst also taking into account balance sheet considerations.

Payments are designed to ensure that the ability of the Appointee to finance its Appointed Business is not impaired. Dividends of £43.5 million were paid to the parent undertaking (2019/20: £249.7 million), representing the base dividend of £42.3 million for 2020/21 and £1.2 million due to the Watershare+ scheme. Payment of the outperformance dividend based on cumulative outperformance for 2019/20 of £58.1 million has been deferred to 2021/22 and recognised as a liability. The dividend was calculated with reference to the projections in the Ofwat 2019 Final Determination and the assumptions for 2020/21 included within the 2020-25 Business Plan.

CAPITAL INVESTMENT

Capital investment was £168.2 million in 2020/21 compared to £161.0 million in 2019/20. Key areas of investment and activity during 2020/21 included:

- Accelerated K7 investment into the shellfish and bathing waters programmes
- Implementation of planned investments and capital solutions driven by the pollutions reduction program
- Year on year increase of c.£4.0 million due to planned and reactive interventions on the wastewater network
- Continued improvements at wastewater treatment works, including flood resilience and at pumping stations to reduce pollution incidents.

CASH FLOW

South West Water's operational cash inflows in 2020/21 at £243.6 million were £26.4 million higher than last year (2019/20: £217.2 million). These funds have been used to finance the Company's capital structure in an efficient way as well as investing in future growth through our substantial continuing capital investment programme.

Corporation tax payments were £24.7 million. Total tax payments reflecting all taxes borne by the Company in 2020/21 are described in more detail in the section on 'Tax Contribution (borne/collected)' on page 40.

LIQUIDITY AND DEBT PROFILE

South West Water has a strong liquidity and funding position with £344.1 million of cash and committed facilities at 31 March 2021. This consists of cash and deposits of £164.1 million (excluding £250.8 million of restricted funds representing deposits with lessors against lease obligations) and undrawn facilities of £180.0 million. At 31 March 2021 the Company's borrowings totalled £2,688.5 million. After the £414.9 million held in cash, this gives a net debt figure of £2,273.6 million, an decrease of £33.6 million during the year (2020: £244.6 million increase).

South West Water has a diversified funding mix of 63% fixed, 12% floating and 25% index-linked borrowings. The Company's debt has a maturity of up to 36 years with a weighted average maturity of 18.6 years matching the asset base. Some of the Company's debt is floating rate, with derivatives being used to fix the rate on that debt. The Company has fixed, or put swaps in place to fix, the interest rate on a substantial portion of the existing debt, in line with the policy to have at least 60% of fixed funding.

£579.4 million of South West Water's debt is index-linked at an overall real rate of under 1.8%. As a result of the aforementioned initiatives, South West Water's cost of finance is among the lowest in the industry. Around two thirds of the net debt is from finance leases, providing a long maturity profile to its debt. Interest payable on them benefits from the fixed credit margins, which were secured at the inception of each lease. A quarter of the net funding for the water business is Retail Price Index (RPI) linked, a level below Ofwat's notional level of 33% leaving headroom for RPI to Consumer Prices Index including owner occupiers' housing costs index (CPIH) transition.

At 31 March 2021 the fair value of the Company's non-current borrowings (excluding leases) was £159.9 million more than its book value (2020: £199.5 million more than book value) as detailed in note 22 to the financial statements. This reflects the continued benefit of securing interest rates below the current market rate, offset by volatility in inflation markets.

CAPITAL STRUCTURE – OVERALL POSITION

The Company's net debt has decreased by £33.6 million to £2,273.6 million. Cash inflow from operations was a strong £243.7 million. Cash outflows relating to the capital programme totalled £161.1 million (2020: £172.2 million), an increase from the prior year due additional capital expenditure to enhance pollutions performance, IT infrastructure to support changing working patterns as a result of COVID-19 and to support services to the Isles of Scilly. The gearing ratio at 31 March 2021, being the ratio of net debt to (equity plus net debt) was 81.2% (31 March 2020: 82.4%).

The combined South West Water and Bournemouth Water debt to Regulated Capital Value (RCV) ratio is 67.1% (31 March 2020: 64.6%). Ofwat's notional gearing target for the K7 (2020-25) regulatory period is set at 60.0.

	2016	2017	2018	2019	2020	2021
Regulatory capital value as at 31 March (£m)	3,150	3,291	3,431	3,505	3,573	3,388

The decrease in RCV reflects an Ofwat policy change in indexation in PR19. From 1 April 2020, 50% of the opening RCV balance was linked to the RPI and 50% to the CPIH. RCV additions from 1 April 2020 onwards are linked to CPIH. At March 2021 RPI was 1.5% and CPIH was 1.1 %. Historically 100% of the RCV balance was linked to RPI, which is generally higher. The balance includes an adjustment for IFRS16 made in line with Ofwat calculations.

South West Water utilises the role of the Pennon Group's treasury function to ensure it has the funding to meet foreseeable needs, to maintain reasonable headroom for future contingencies and to manage interest rate risk. It operates only within policies approved by the Board and undertakes no speculative trading activity.

The Board regularly monitors expected financing needs for at least the following 12 months. These are intended to be met for the coming year from existing cash balances, loan facilities and operating cash flows.

The Pennon Group has considerable financial resources. The Directors therefore believe that South West Water is well placed to manage its business risks in the context of the financial resources available to it.

INTERNAL BORROWING

South West Water's funding is treated for regulatory purposes as ring-fenced. This means that funds raised by, or for it, are not available as long-term funding for other areas of the Pennon Group.

TAXATION STRATEGY

South Water has adopted the Pennon Group plc tax strategy. This means that we will:

- At all times consider the Company's corporate and social responsibilities in relation to its tax affairs
- Operate appropriate tax risk governance processes to ensure that the policies are applied
- Comply with our legal requirements; file all appropriate returns on time and make all tax payments by the due date
- Consider all taxes as part of ongoing business decisions
- Not enter into artificial tax arrangements or take an aggressive stance in the interpretation of tax legislation
- Not undertake transactions which are outside the Company's low risk appetite for tax or not in line with the our Code of Conduct
- Engage with HMRC in a proactive and transparent way and discuss our interpretation of tax laws in real-time, such interpretations following both the letter and spirit of the laws.
- Not have any connections with tax havens unless it is necessary for the purposes of trading within those jurisdictions.

The Company's approach to tax planning, risk management and governance is in line with the Finance Act 2016 requirements; the Company does not expect its tax strategy to change significantly year on year, however it is reviewed and updated annually. Further details are given in the Group's Tax Strategy document which is available on the Pennon Group website.

TAXATION CONTRIBUTION (BORNE/COLLECTED)

The company's total tax contribution extends significantly beyond the UK corporation tax payments.

In addition to corporation tax the most significant taxes involved, together with their profit impact, were:

- Value Added Tax (VAT) of £37.1 million recovered (2019/20: £35.1 million) by South West Water from HMRC. VAT has no material impact upon the profit before tax
- Business rates of £29.5 million (2019/20: £29.1 million) paid to local authorities. This is a direct cost to the Company and reduces profit before tax
- Employment taxes of £17.8 million (2019/20: £16.0 million) including employees' Pay As You Earn (PAYE) and total National Insurance Contributions (NICs). This is a direct cost to the Company and reduces profit before tax
- Fuel Excise Duty of £0.9 million (2019/20: £0.9 million) related to transport costs. This reduces profit before tax
- Payments to the Environment Agency and other regulatory bodies total £11.8 million (2019/20: £11.4 million). This reduces profit before tax

- Carbon Reduction Commitment (CRC) payment for the Company of nil due to be replaced by enhanced climate change levy (2019/20: £0.2 million). This reduces profit before tax.

The corporation tax rate for 2020/21 used to calculate the current year's tax is 19%. During the Chancellor's Budget on 4th March 2021, it was announced that the UK main rate of corporation tax will increase to 25% from 1 April 2023. The change in tax rate was not enacted at the balance sheet date and so is not reflected in these accounts. This change was substantively enacted on 24 May 2021 and deferred tax assets and liabilities will be recalculated and recorded at the tax rate at which they are expected to unwind in the next financial year. It is anticipated the change in tax rate will increase South West Water's tax charge and deferred tax liability by c.£85 million.

To support the fact that we pay our 'fair' share, Pennon Group (including South West Water) again applied to the Fair Tax organisation to seek their independent award and were successful in obtaining certification. The Fair Tax Mark is the UK's accreditation scheme for businesses paying their fair share of corporation tax and reporting on their tax practices transparently.

PENSIONS

The Company is a member of the Pennon Group's defined benefit pension schemes for certain employees of South West Water. The defined benefit schemes were closed to new entrants on or before 1 April 2008. The defined benefit scheme was closed to future accrual from 30 June 2021.

At 31 March 2021 the Company's share of the pension schemes showed an aggregate surplus (before deferred tax) of £14.3 million (2019/20: £7.1 million surplus). The increase in the surplus in 2020/21 primarily driven by remeasurements in financial assumptions during the year.

INSURANCE

South West Water manages its property and third-party liability risks through insurance policies that mainly cover property, motor, business interruption, public liability and employers' liability.

The Company uses three tiers of insurance to cover operating risks:

- self-insurance – pay a moderate excess on most claims
- cover by the Pennon Group's subsidiary (Peninsula Insurance Limited) of the layer of risk between the self-insurance and the cover provided by external insurers
- cover provided by the external insurance market, arranged by our brokers with insurance companies that have good credit ratings.

MANAGING OUR RISKS

The Board and Executive are committed to the effective management of risks and opportunities to ensure the long-term success of the Company.

OUR RISK MANAGEMENT FRAMEWORK



South West Water operates a mature and robust risk management and internal control framework (see diagram above) which are aligned to our strategy and embedded into our processes, culture and ways of working at all levels of the business. These frameworks form a key part of our governance structure ensuring that there is robust review, challenge and assurance over the management of both our current and emerging risks and opportunities.

GOVERNANCE OF THE RISK MANAGEMENT AND INTERNAL CONTROL FRAMEWORKS

The risk management framework encompasses both a 'top down' and 'bottom up' approach. This allows risks and opportunities to be cascaded and escalated effectively, enables a common understanding of the risks and opportunities and their potential impact on the Company's strategic priorities and provides a multi-layered approach to the review and challenge of risk.

A consistent methodology is applied in the identification, assessment and management of the Company's risks, which considers both the likelihood of the risk occurring over a long-term period and formally from a Company perspective, a five-year period as well as the potential impact assessed across a range of categories including financial, safety, environmental and customer service. Principal and business level risks are captured within risk registers and are subject to regular review and challenge, including by the Risk Committee, Executive and Board.

The Company manages its risk exposure, in line with the desired risk appetite and tolerance levels, through the operation of a robust internal control and assurance framework which is aligned to the 'three lines' model. The Executive and the Board obtain assurance over the effectiveness of the internal control environment through a variety of internal and external assurance providers, including an independent Group Internal Audit function.

The key responsibilities and activities which encompass the Company's risk management framework include:

		Key risk management responsibilities	Key assurance activities
OVERSIGHT	Board	<ul style="list-style-type: none"> Sets the Company's strategic objectives Establishes the Company's risk appetite Determines the Company's principal risks Ensures an effective internal control framework 	<ul style="list-style-type: none"> Quarterly reviews of the Company's principal risks against the determined risk appetite Quarterly reviews of the Company's emerging risk log
	Audit Committee	<ul style="list-style-type: none"> Reviews the effectiveness of the risk management framework Reviews the adequacy of the internal control framework 	<ul style="list-style-type: none"> Perform quarterly deep dive reviews on principal risks Review the Group Internal Audit Plan in respect of South West Water Receive reports on the outcomes of key assurance activities
THIRD LINE OF DEFENCE	Group Internal Audit	<ul style="list-style-type: none"> Provides independent, risk-based assurance on the effectiveness of the internal control framework Coordination of independent assurance activities 	<ul style="list-style-type: none"> Regular reporting to Audit Committee and Executive on the effectiveness of internal controls and the outcomes of key assurance activities
SECOND LINE OF DEFENCE	Executive	<ul style="list-style-type: none"> Day-to-day management of principal and operational risks Establishes the relevant risk management processes and procedures Maintains the internal controls framework 	<ul style="list-style-type: none"> Thorough appraisal of principal and emerging risk profile quarterly Monitor performance against ODIs, other KPIs and financial performance Establish and review policies, procedures and delegated authorities
	Risk Committee	<ul style="list-style-type: none"> Provides review and challenge over principal risks and mitigation strategies Alignment of the 'top down' and 'bottom up' risk management process Performs horizon scanning on emerging risks and opportunities 	<ul style="list-style-type: none"> Quarterly review of principal risks and key functional risks Undertakes deep dive reviews of specific risks.
FIRST LINE OF DEFENCE	South West Water directorate functions	<ul style="list-style-type: none"> The identification and assessment of risks Implementation and execution of appropriate risk mitigation strategies, aligned with the agreed risk appetite Monitor compliance with internal control framework 	<ul style="list-style-type: none"> Review of principal risks on a quarterly basis by senior leadership teams Compliance functions perform second line assurance across regulatory, legal, health & safety, and other key business processes Self-certification of compliance with internal control framework

In addition, the Company also received assurances from a variety of external assessments, including by our regulators, which compliments and further enhances the overall assurance framework.

ENVIRONMENT, SOCIAL AND GOVERNANCE RISK MANAGEMENT

The nature of the Company's operations means that environmental, social and governance (ESG) considerations are inherent in how the Company operates as a responsible business and is a key focus for the Company. The identification, assessment and management of ESG risks and opportunities, including the potential impact of climate change on our business, is integrated into the Company's overall risk management framework and methodology, with the outcomes reflected within the assessment of relevant principal and business level risks. The delivery of the Company's ESG actions and commitments is monitored through our ESG framework.

SOUTH WEST WATER TECHNICAL (NON-FINANCIAL) DATA

In addition to the risk management framework detailed above, recognising the importance of the regulatory ODI framework, South West Water engages an independent, third-party auditor, Jacobs, to audit the accuracy of the technical (non-financial) data reported in its annual performance report (APR), including its performance commitments and environmental data and all other non-financial data required to be reported in line with Regulatory Accounting Guidelines. Their audit opinion on the technical data will be published in the APR available following the publication in July 2021 at www.southwestwater.co.uk/report2021.

CONTINUOUS IMPROVEMENTS TO RISK MANAGEMENT AND INTERNAL CONTROL

A comprehensive review of the Company's risk management processes has been undertaken. Risk management processes have been streamlined, risk reporting has been enhanced and a reconstituted Risk Committee has been established, which includes representation from across key functional areas including operations, health & safety, finance and legal.

Additionally, the following activities have been completed during the year as part of the commitment to continuously improve the Company's risk management framework:

- The Company's risk management policy has been reviewed and updated
- Health & safety governance has been further strengthened with dedicated health & safety committees established during the year
- Key risk indicators and associated metrics have been updated and aligned with strategic priorities, supporting the monitoring of the Company's principal risks against its risk appetite
- An updated telematics system is being rolled out across the Company's fleet, providing improved vehicle and driver monitoring, oversight and reporting
- A programme of second line health & Safety assurance was delivered covering additional safety measures implemented at the Company's operational sites and offices in response to COVID-19
- The Company has further enhanced the resilience of its 24/7 Service Support Centre which provides support to our operational sites and customer contact resolution
- South West Water has continued to progress the replacement programme of operational technology providing further resilience to cyber related risks.

OFWAT'S PRINCIPLES - BOARD LEADERSHIP, TRANSPARENCY AND GOVERNANCE

Ofwat requires that holding companies manage their risks in such a way that the regulated company is protected from risk elsewhere in the Group. Pennon Group's principal risks and uncertainties include those Group-level risks which could materially impact on South West Water.

Pennon's risk management and internal control frameworks ensure that it does not take any action that would cause South West Water to breach its licence obligations. Further, the Group's governance and management structures mean that there is full understanding and consideration of South West Water's duties and obligations under its licence, as well as an appropriate level of information sharing and disclosure to give South West Water assurance that it is not exposed as a result of activities elsewhere within the Group.

Further details of Group-wide principal risks and application of the Group's risk management framework across the Group are provided in the Pennon Group plc annual report (pages 67 to 73).

HORIZON SCANNING

Emerging risks and opportunities are considered to be factors and events which could have a future impact on the achievement of the Company's strategic priorities but lack the required clarity or certainty in order to adequately assess their impact. Horizon scanning of emerging risks and opportunities is embedded within the risk and opportunity review process performed by individual subsidiaries and functions. Emerging risks are also reviewed by the Risk Committee, Executive and Board as part of their regular assessment of the Company's risk profile. Once there is sufficient clarity and certainty over the emerging risk, it is assessed applying the Company's methodology and appropriate mitigating actions are established. Notable emerging risks and opportunities are detailed within the table below:

Risk/opportunity	Comment	Risk category impact	Time horizon
COVID-19 long-term economic implications	Uncertainty remains over the pace and scale of the long-term implications of COVID-19 on the global and UK economy, which could impact our business.	<ul style="list-style-type: none"> Legal, Regulatory and Finance 	Medium Term
Micro-pollutants, plastics and micro-plastics	The continued focus on the impact of micro-pollutants and microplastics could present both risks and opportunities arising from changes to water treatment processes.	<ul style="list-style-type: none"> Operating performance Business Systems and Capital investment 	Medium Term
Biodiversity	Threats to the region's biodiversity, as a result of climate change, may require changes to how we interact with species and habitats in the areas that we operate in.	<ul style="list-style-type: none"> Operating performance 	Long Term
Changes to the demographics within the South West	Increases in population migration to the South West due to the longer-term impact of COVID-19 and climate change could place further demand on our resources and assets.	<ul style="list-style-type: none"> Operating performance 	Long Term

RISK APPETITE

The UK Corporate Governance Code requires companies to determine the risk appetite considered appropriate in achieving the Company's strategic priorities. Striking an appropriate balance between risk and reward is key to the success of the Company's strategy.

The Board has established its risk appetite for each risk category and also for each principal risk. This allows the business to pursue value-enhancing opportunities, whilst maintaining an overall level of risk exposure that the Board considers to be appropriate. The Board's evaluation of the effectiveness of the comprehensiveness of the Company's internal controls in mitigating its principle risks to an acceptable level is considered with due consideration of the relevant risk appetite.

The risk appetite for each risk category is detailed below:

Risk category	Risk appetite statement
Law, regulation and finance	<p>The Board is committed to fully complying with, and being seen to be complying with, all relevant laws, regulations and obligations and has no appetite for non-compliance in this area. This includes (but is not limited to) health & safety, where the Board places the highest level of importance on the welfare of our employees, the public and those who work with, or on behalf of, South West Water. The Company also operates a prudent approach to our financing strategy to ensure our long-term financing commitments are met.</p> <p>The Board acknowledges, however, that South West Water operates in a complex environment influenced by Government policy and regulatory reform. Consequently, there is a greater acceptance of risk in these areas and the Company seeks to mitigate any potential downside and leverage opportunities that may arise from Government policy and regulatory change.</p>
Market and economic conditions	<p>The Board recognises that our activities are exposed to changes in macroeconomic and external market conditions. The Company seeks to take well-judged and informed decisions to mitigate these risks where possible, but accepts that a level of residual risk may remain beyond the Board's control.</p>
Operating performance	<p>The Board has a low appetite for significant operational failure of our assets and seeks to reduce both the likelihood and impact through long-term planning and careful management of our operational assets.</p> <p>There is greater appetite for well-informed risk taking to develop further markets, subject to this not detrimentally impacting on the level of service expected of our regulators, existing customer base and wider stakeholders.</p>
Business systems and capital investment	<p>The Board has a low risk appetite for risk associated with the delivery of capital investment within our regulated business plan. Broader investment decisions are taken on an informed basis with risks weighted against the expected level of return on a case-by-case basis.</p> <p>South West Water seeks to minimise technology and security risk to the lowest possible level without detrimentally impacting on the Company's operations.</p>

PRINCIPAL RISKS AND UNCERTAINTIES

South West Water's business model exposes it to a variety of external and internal risks influenced by the possible impact of macro political, economic and environmental factors.

While the ability of the Company to influence these macro level risks is limited, they continue to be regularly monitored and the potential implications are considered as part of the ongoing risk assessment process. The Company performs a range of scenario planning and analysis exercises to understand the risk exposure of one or a number of these events occurring:

BRITAIN'S TRADE AGREEMENT WITH THE EUROPEAN UNION

On the 31 December 2020 the UK's transition period from leaving the EU ended and was replaced with a new trade agreement. There has been no significant impact or disruption to the operations and activities of the Company either prior to or following the commencement of this trade agreement.

IMPACT OF COVID-19

As a provider of critical services, the Company has continued to operate resiliently throughout the period of COVID-19 to date, demonstrating the strength of the risk management framework. Whilst the UK Government has provided a roadmap for the lifting of current restrictions, this is dependent on a number of factors and there is the potential that specific measures could remain or be reintroduced in the medium term. The Company's principal risks have been assessed giving due consideration to the estimated continued impact of COVID-19 and the mitigating actions that will remain in place.

OVERALL ASSESSMENT OF RISKS

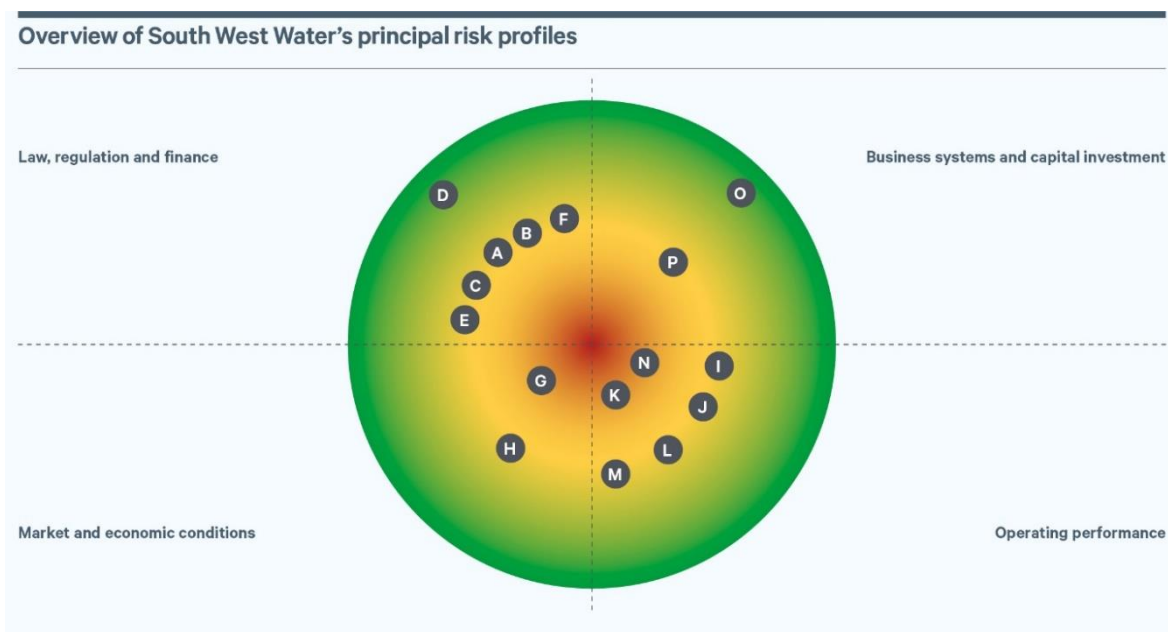
The Directors confirm that during 2020/21 they have carried out a robust assessment of current and emerging risks facing the Company. The assessment of the Company's principal risks has considered the impact on its business model, future performance, solvency and liquidity. These principal risks have been considered in preparing the viability statement on page 59.

STRATEGIC IMPACT AND RISK RANKING

Our principal risks link to the strategic focus areas as described on page 9, and have been assessed on the following scale:

Key	Risk level		
	Low	Medium	High
The low, medium and high risk level is our estimate of the net risk to the Company after mitigation. It is important to note that risk is difficult to estimate with accuracy and therefore the actual risk may be greater or less than our estimate indicates.			
	GREEN	AMBER	RED
Current assessment of direction of travel of risk level	Increasing	Stable	Decreasing
	↑	↔	↓

REPORTING AN OVERVIEW OF THE PRINCIPAL RISK PROFILE



Principal risks	Ref	Strategic priorities	Risk description	Net risk level	Trend
Law, regulation and finance	A	Environment Customer and finance	Changes in Government policy	AMBER	↔
	B	Environment Customer and finance	Regulatory reform	AMBER	↔
	C	Environment Customer and finance	Non-compliance with laws and regulations	AMBER	↑
	D	Customer and finance	Inability to secure sufficient finance and funding, within our debt covenants, to meet ongoing commitments	GREEN	↔
	E	People and community	Non-compliance or occurrence of avoidable health & safety incident	AMBER	↔
	F	Customer and finance	Failure to pay all pension obligations as they fall due and increased costs to the Company should the defined benefit pension scheme deficit increase	AMBER	↔
Market and economic conditions	G	Customer and finance	Non-recovery of customer debt	RED	↔
	H	Customer and finance	Macro-economic risks impacting inflation, interest rates and power prices	AMBER	↔
Operating performance	I	Water Wastewater Environment Resilience	The company's operations and assets are impacted as a result of climate change and extreme weather events	AMBER	↑
	J	Water Service Environment	Failure of operational water treatment assets and processes resulting in an inability to produce or supply clean drinking water	AMBER	↑
	K	Wastewater Service Environment	Failure of operational wastewater treatment assets and processes resulting in an inability to remove and treat wastewater and potential environmental impacts. Including pollutions	RED	↔
	L	Water Wastewater Service Customer and finance	Failure to maintain excellent service or effectively engage with our customers and wider stakeholders	AMBER	↔

	M	People and community	Insufficient skills and resources to meet the current and future business needs and deliver the Company's strategic priorities	AMBER	↔
	N	Water Service Environment People and community Customer and finance	Non-delivery of Regulatory Outcomes and performance commitments	RED	↔
Business systems and capital investments	O	Customer and finance	Inefficient or ineffective delivery of capital projects	GREEN	↑
	P	Water Service Customer and finance	Inadequate technological security results in a breach of the Company's assets, systems and data	AMBER	↑

LAW REGULATION AND FINANCE

Strategic impact	Mitigation and commentary	Risk appetite
Principal Risk A: Changes in Government policy		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, STABLE		AMBER, INCREASING
<p>Environment</p> <p>Customer and finance</p> <p>Changes in Government policy may fundamentally impact our ability to deliver the Group's strategic priorities, impacting shareholder value.</p>	<p>The current UK Government remains supportive of the existing regulatory model and the Company continues to engage with MPs and political stakeholders, both directly and through Water UK, demonstrating the value from our operational performance and continued investment in our network infrastructure.</p> <p>The Company is committed to supporting the South West economy through South West Water's Green Recovery Initiative which focuses on projects that matter most to customers and those that improve public health, protect the environment and address climate change.</p> <p>Broader emerging changes in Government Policy, including restrictions and on-going economic support in response to COVID-19, are regularly monitored in order to assess the potential impact on the Company.</p>	<p>We recognise that Government Policy evolves. The Company seeks to minimise the potential risk and maximise opportunities through regular engagement and robust scenario planning.</p>
Principal Risk B: Regulatory Reform		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, STABLE		AMBER, INCREASING
<p>Environment</p> <p>Customer and finance</p> <p>Reform of the regulatory framework may result in changes to our priorities and the service we provide to our customers. It may have a significant impact on our performance which can impact shareholder value.</p>	<p>Certainty over the regulatory framework for the 2020-25 regulatory period has been provided through South West Water's Final Determination.</p> <p>Ofwat have published initial discussion papers to inform the priorities for the PR24 price review. South West Water have responded to these papers and has proactively commenced planning for the next price review.</p> <p>Specific temporary regulatory changes, in response to COVID-19, remain in place; particularly in respect of the water retail market, including wholesaler support. The Company fully engages with regulators on these changes to minimise the potential impact on the Company's activities.</p>	<p>We accept that regulatory reform occurs and seek to leverage opportunities where possible and minimise the potential risks by targeting changes which are NPV neutral over the longer term to protect customer affordability and shareholder value.</p>

LAW REGULATION AND FINANCE (CONTINUED)

Strategic impact	Mitigation and commentary	Risk appetite
Principal Risk C: Non-compliance with laws and regulations		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, INCREASING.		AMBER, INCREASING
<p>Environment</p> <p>Customer and finance</p> <p>South West Water is required to comply with a range of regulated and non-regulated laws.</p> <p>Non-compliance with one, or a number of these may result in financial penalties negative impact on our ability to operate effectively and reputational damage.</p>	<p>The Company operates within robust and mature regulatory frameworks, ensuring compliance with the requirements of Ofwat, Environment Agency and other relevant regulators. These frameworks are subject to review by South West Water.</p> <p>Legal and regulatory requirements have become more complex with additional legal requirements proposed within the Environmental Bill, as well as additional requirements on water companies to reduce the use of storm overflows.</p> <p>Regular horizon scanning is undertaken to identify potential changes and, where introduced, internal processes, systems and controls are revised, as necessary, to ensure compliance.</p> <p>The Company maintains a comprehensive internal framework to ensure compliance with corporate laws and regulations. This is reinforced through key policies including the Group's Code of Conduct, Anti-Bribery and Corruption, Anti-Facilitation of Tax Evasion and Anti-Modern Slavery and Human Rights, which have been reviewed and endorsed by the Board during the year.</p> <p>South West Water operates a Speak Up whistleblowing process, allowing concerns to be raised confidentially and appropriately investigated. This process has been refreshed and relaunched during the year.</p>	<p>South West Water has the highest standards of compliance and has no appetite for legal or regulatory breaches.</p>
Principal Risk D: Inability to secure sufficient finance and funding, within our debt covenants, to meet ongoing commitments.		
2021 Net risk and direction:		2020 Net risk and direction:
GREEN, STABLE		GREEN, STABLE
<p>Customer and finance</p> <p>Failure to maintain funding requirements could lead to additional financing costs and put our growth agenda at risk. Breach of covenants could result in the requirement to repay certain debt.</p>	<p>South West Water and the entire Pennon Group have well established treasury, funding and cash flow arrangements in place underpinned by a clear Treasury Management policy which has been endorsed by the Board.</p> <p>The impact of political, economic and regulatory risks on the Company's financing commitments and cash flow is regularly reviewed by the Executive and Board.</p> <p>South West Water are fully funded for the 2020-2025 regulatory period.</p> <p>During 2020/21 £90 million of new or renewed funding was entered into through the Sustainable Funding Framework for South West Water.</p>	<p>We operate a prudent approach to our financing strategy in order to ensure our funding requirements are fully met.</p>

LAW REGULATION AND FINANCE (CONTINUED)

Strategic impact	Mitigation and commentary	Risk appetite
Principal Risk E: Non-compliance or occurrence of an avoidable health & safety incident		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, STABLE		AMBER, STABLE
<p>People and community</p> <p>A significant health & safety event could result in financial penalties, significant legal costs and damage to the Company's reputation.</p>	<p>The effective management of health & safety risks continues to be a priority for the Board and Executive.</p> <p>The Company's health & safety governance arrangements have been further enhanced during 2020/21 with dedicated Board and Executive health & safety committees established. Additionally, a new Director of health & safety has been appointed with significant water industry experience.</p> <p>Homesafe training has continued to be delivered to front line and support staff and a new Company-wide Wellbeing strategy has been launched.</p> <p>Enhanced COVID-19 safety measures remain in place to enable the Company's activities to be delivered safely, stringently following the most recent Government guidelines. This includes remote working where appropriate, the provision of COVID-19 testing for those unable to work remotely, social distancing and enhanced hygiene at all of the Company's sites and appropriate personal, protective equipment (PPE).</p> <p>The Long Term Injury Frequency Rate (LTIFR) during the year was 1.59 and the Company remains on track to deliver its LTIFR target of 0.5 by 2025.</p>	<p>We have no appetite for health & safety related incidents and we maintain the highest standards of compliance for our staff, contractors and other third parties.</p>
Principal Risk F: Failure to pay all pension obligations as they fall due and increased costs to the Company should the deferred pension scheme deficit increase		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, STABLE		AMBER, INCREASING
<p>Customer and finance</p> <p>The Company could be called upon to increase funding to reduce the deficit, impacting our cost base.</p>	<p>The Company utilises an experienced in-house Pensions team who also engage with professional advisors to manage the pension scheme's investment strategy.</p> <p>A recovery plan remains in place to return the scheme to a fully funded position on a technical basis by March 2022. During the year £nil million of contributions have been made.</p> <p>Following consultation, the scheme will be closed to future accrual for existing members from 30 June 2021.</p>	<p>The Company will ensure that all obligations are met in full but seeks to manage this without unnecessary increased costs to the Company.</p>

MARKET AND ECONOMIC CONDITIONS

Strategic impact	Mitigation and commentary	Risk appetite
Principal Risk G: Non-recovery of customer debt		
2021 Net risk and direction:		2020 Net risk and direction:
RED, STABLE		AMBER, INCREASING
<p>Customer and finance</p> <p>Reduced customer debt collection would adversely impact on the Company's revenue.</p>	<p>South West Water has continued to review and adapt their debt collection strategies in response to changes in COVID-19 restrictions and the consequential impact on customers. These measures have enabled South West Water to maintain collection rates and debt exposure at levels broadly comparable with the prior year.</p> <p>South West Water have sought to identify those customers most in need and support them in the most appropriate ways; such as automatically extending social tariffs and payment plans.</p> <p>The potential impact on customers arising from the gradual withdrawal of Government economic support measures means a level of risk to collection rates will remain in the medium term.</p>	<p>While seeking to minimise non-recoverable debt, we recognise customer affordability challenges and the inability to disconnect customers results in a residual risk of uncollectable debt remaining.</p>
Principal Risk H: Macro-economic risks impacting on inflation, interest rates and power prices		
2021 Net risk and direction:		2020 Net risk and direction⁽¹⁾:
AMBER, STABLE		AMBER, INCREASING
<p>Customer and finance</p> <p>Lower inflation or deflation could adversely impact on the Company's revenue and significant changes in interest rates and power prices could increase the Company's cost base.</p>	<p>Regulatory revenue controls links the Company's revenue to CPIH.</p> <p>The Company has a diverse portfolio of debt with a manageable debt maturity profile, enabling changes in interest rates to be managed effectively during each regulatory period.</p> <p>South West Water has hedged the majority of its wholesale power costs through to March 2022 and has a new energy purchasing contract in place for future hedging opportunities, to mitigate the risk of volatility in the energy markets. Energy usage is minimised and where possible onsite renewable energy schemes are implemented reducing reliance on purchasing energy from the grid. This remains an important element of the Company's strategy to achieve Net Zero by 2030.</p>	<p>We seek to take well-judged and informed decisions whilst ensuring plans are in place to mitigate the potential impact of macro-economic risks.</p>

⁽¹⁾ The 2021 risk definition has been refocused, although the risks are broadly comparable

OPERATING PERFORMANCE

Strategic impact	Mitigation and commentary	Risk appetite
Principal Risk I: The Company's operations and assets are impacted as a result of climate change and extreme weather events		
2021 Net risk and direction:		2020 Net risk and direction⁽²⁾:
AMBER, INCREASING		AMBER, STABLE
<p>Water</p> <p>Wastewater</p> <p>Environment</p> <p>Resilience</p> <p>Failure of our operations to cope with short term extreme weather or long term implications of climate change may result in an inability to meet customer needs, environmental impacts, increased costs and reputational damage.</p>	<p>A low appetite remains amongst regulators and stakeholders for reduced performance arising from extreme weather and climate change related incidents.</p> <p>Climate change impacts is mitigated through proactive and reactive mitigation strategies. Extensive water resource scenario planning and modelling is undertaken, as outlined in South West Water's 25-year Water Resources Strategy.</p> <p>There has also been significant capital investment to maintain the performance of our assets and pipe network. This has included enhancing the resilience of assets located on or near flood plains or at risk of rising sea levels and costal erosion.</p> <p>South West Water, as part of the Pennon Group is also targeting Net Zero carbon by 2030 and strategies to achieve this are being progressed.</p>	<p>We seek to mitigate the impact of climate change and extreme weather events through long term planning, forecasting and investment.</p>
Principal Risk J: Failure of operational water treatment assets and processes resulting in an inability to produce or supply clean drinking water		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, INCREASING		N/a⁽³⁾
<p>Water</p> <p>Service</p> <p>Environment</p> <p>An inability to produce or supply clean drinking water could result in financial penalties, regulatory enforcement and damage to the Company's reputation.</p>	<p>The potential impact of increased tourism within the region, as a consequence of COVID-19, on water treatment assets increases the potential risk in this area.</p> <p>Additional resilience has been created through the Mayflower Water Treatment Works which replaced Crownhill in November 2020. Further water treatment capital investment is planned during the regulatory period.</p> <p>Asset health is managed through a well established programme of planned and preventative maintenance works and effective stores management.</p> <p>These actions have assisted in delivering further improvements during the year across a number of areas within the Company's drinking water operations.</p> <p>In the event of a significant incident South West Water maintains detailed contingency plans and incident management procedures which are regularly reviewed.</p>	<p>We operate a low tolerance for significant operational failure of our water treatment assets and seek to mitigate these risks where possible.</p>

⁽²⁾ The 2021 risk definition has been refocused, although the risks are broadly comparable

⁽³⁾ In 2020 a combined water and wastewater risk in respect of failure of operational assets and processes was presented and was considered amber and increasing

OPERATING PERFORMANCE (CONTINUED)

Principal Risk K: Failure of operational wastewater assets and processes resulting in an inability to remove and treat wastewater and potential environmental impacts, including pollutions		
2021 Net risk and direction:		2020 Net risk and direction:
RED, STABLE		N/a⁽⁴⁾
<p>Wastewater Service Environment</p> <p>An inability to remove or treat wastewater could result in adverse environment impacts, financial penalties, regulatory enforcement and damage to the Company's reputation.</p>	<p>Wastewater assets are managed through a well established programme of capital investment and planned and preventative maintenance.</p> <p>There have been significant improvements in South West Water's pollutions performance since the launch of the targeted pollutions reduction plan in July 2020.</p> <p>Key enhancements delivered as part of this plan includes governance, training, asset health and technology and there remains continued focus on ensuring this positive trend continues in 2021/22.</p> <p>In the event of a significant incident South West Water maintains detailed contingency plans and incident management procedures which are regularly reviewed.</p>	<p>We operate a low tolerance for significant operational failure of our wastewater processes and assets and maintains the highest level of environmental standards.</p>
Principle Risk L: Failure to maintain excellent service or effectively engage with our customers and wider stakeholders.		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, STABLE		N/a⁽⁵⁾
<p>Water Wastewater Service Customer and finance</p> <p>Failure to maintain an adequate level of service and engagement could lead to financial penalties and reputational damage for South West Water.</p>	<p>The Company continues to invest in training and expanded channels to interact with and support customers. South West Water holds the Institute of Customer Service's ServiceMark accreditation and during 2020/21 also achieved BS 18477 accreditation; a dedicated standard for identifying and responding to customer vulnerability.</p> <p>Following the launch of the Watershare+ scheme an independent Watershare+ advisory panel has been established as a key mechanism for engaging and demonstrating to customers how South West Water is delivering their business plan and Board Pledges.</p> <p>The Company also proactively engages with other key stakeholders including regulators, environmental stakeholders and community groups.</p>	<p>We continually seek to engage with and increase customer and wider stakeholder satisfaction levels.</p>

⁽⁴⁾ In 2020 a combined water and wastewater risk in respect of failure of operational assets and processes was presented and was considered amber and increasing

⁽⁵⁾ This risk was not considered a Principal Risk in 2020

OPERATING PERFORMANCE (CONTINUED)

Principal Risk M: Insufficient skills and resources to meet the current and future business needs and deliver the Companies strategic priorities		
2021 Net risk and direction:		2020 Net risk and direction⁽⁶⁾:
AMBER, STABLE		AMBER, INCREASING
<p>People and community</p> <p>Failure to have a workforce of skilled and motivated individuals will detrimentally impact all of our strategic priorities. We need the right people in the right places to innovate, share best practice deliver synergies and move the Company forward.</p>	<p>Throughout 2020/21, the Company did not furlough any staff or utilise Government COVID-19 support.</p> <p>The Company's HR strategy enables the Company to attract, retain and develop our employees. South West Water has set targets to recruit 500 new apprentices and 100 graduates over the next 5 years; plus 50 kickstart opportunities during 2021. There are currently 106 apprentices and 24 kickstarters across the Company, with the first intake of 20 graduates being recruited.</p> <p>There are also various engagement forums across South West Water which provides opportunities for employees to regularly engage and discuss business priorities with senior management and the Group Executive.</p> <p>The impact of the Company's Employee Benefits and Reward strategy, a focus on talent management and prioritisation of our diversity and inclusion agenda is reflected within the results of the Company's most recent Great Place to Work Best Workplace survey. We achieved our highest ever participation rate at 81% while 71% of respondents believe South West Water is a great place to work; resulting in the Company being accredited as a Great Place to Work.</p>	<p>While turnover of employees does occur, we ensure the appropriate skills and experience is in place with succession plans providing adequate resilience.</p>
Principal Risk N: Non-delivery of regulatory outcomes and performance commitments		
2021 Net risk and direction:		2020 Net risk and direction:
RED, STABLE		RED, INCREASING
<p>Water</p> <p>Service</p> <p>Environment</p> <p>People and community</p> <p>Customer and finance</p> <p>South West Water's Regulatory Outcomes and performance commitments span all of our strategic focus areas.</p> <p>Non-delivery of these could result in financial penalties being applied as well as reputational damage.</p>	<p>Performance against ODIs is subject to regular scrutiny and review by both the Executive and the Board, further supplemented by a comprehensive programme of assurance.</p> <p>Fast track status awarded to South West Water by Ofwat enabled early roll out of key projects and initiatives. This has resulted in c.80% of Outcome Delivery Incentives (ODIs) being on or ahead of target.</p> <p>This includes internal and external sewer flooding and South West Water is achieving its supply interruption target two years ahead of plan.</p> <p>The net penalty position for 2020/21 is largely based on pollutions performance. As outlined in risk K above, the targeted pollutions reduction plan has delivered significant improvements since July 2020 and focus remains on ensuring this positive trend continues into 2021/22.</p>	<p>We are committed to achieving all of our performance commitments over the length of each regulatory period.</p> <p>Where performance in an individual year falls below expectation action plans are implemented and targeted intervention to ensure performance returns to committed levels.</p>

⁽⁶⁾ The 2021 risk definition has been refocused, although the risks are broadly comparable

BUSINESS SYSTEMS AND CAPITAL INVESTMENT

Principal Risk O: Inefficient or ineffective delivery of capital projects		
2021 Net risk and direction:		2020 Net risk and direction:
GREEN, INCREASING		GREEN, INCREASING
<p>Customer and finance</p> <p>Inability to successfully deliver on our capital programme may result in increased costs and delays, detrimentally impacting our ability to provide top class customer service and achieve our growth agenda.</p>	<p>Capital projects are subject to an established and robust business case process, which includes challenge and risk modelling of key assumptions. Projects are delivered utilising skilled project management resource, complemented by Executive level oversight.</p> <p>Projects to be delivered during the current regulatory period are progressing and a number of additional capital projects have been identified as part of South West Water's Green Recovery Initiative submission.</p> <p>There remains a risk that the continued impact of COVID-19 places further strain on the financial health of key contractors and supply chain partners. Regular engagement and communication is maintained with the Company's supply chain, regular monitoring of the financial health of our key partners is undertaken and early intervention is taken where necessary.</p>	<p>The Board has a low risk appetite for risk associated with the delivery of capital investment within our regulated business plan.</p>
Principal Risk P: Inadequate technological security results in a breach of the Group's assets, systems and data		
2021 Net risk and direction:		2020 Net risk and direction:
AMBER, INCREASING		AMBER, INCREASING
<p>Water</p> <p>Service</p> <p>Customer and finance</p> <p>Failure of our technology security, due to inadequate internal processes or external cyber threats, could result in the business being unable to operate effectively and the corruption or loss of data.</p> <p>This could have a detrimental impact on our customers and result in financial penalties and reputational damage to South West Water</p>	<p>During the period of COVID-19 external cyber threats have continued to increase in both volume and sophistication.</p> <p>While there has been an increase in remote working, which has introduced additional capacity challenges, IT systems have remained resilient and have maintained a strong preventative and detective information security framework, aligned to guidance issued by the National Cyber Security Centre. South West Water also continues to hold the ISO27001 accreditation.</p> <p>South West Water has also completed a number of actions during the year as part of the roadmap to meet the requirements of the Network and Information Systems (NIS) directive, with activities aligned to priorities identified by the Drinking Water Inspectorate.</p> <p>Disaster recovery plans are in place for corporate and operational technology and are subject to regular review.</p>	<p>We seek to minimise technology and security risk to the lowest possible level without detrimentally impacting on the Company's operations.</p>

VIABILITY STATEMENT

PERIOD OF ASSESSMENT

The Board regularly considers the appropriate period for the viability assessment to be performed in line with the UK Corporate Governance Code. The Board considers the appropriate period to assess the Company's viability remains unchanged until the end of 2030, which recognises the longer term visibility in the regulatory environment of the South West Water business.

ASSESSMENT OF VIABILITY

The assessment has been made with reference to the Company's current position and prospects, including the ongoing COVID-19 pandemic, its longer-term strategy, the Board's risk appetite and the Company's principal risks and how these are managed, as detailed on pages 42 to 58 of the Risk Report. South West Water is a long-term business characterised by a multi-year investment programmes, with associated revenue streams.

The Company's strategic business plan, including consideration of the ongoing COVID-19 pandemic, principal risks and Ofwat viability scenarios are the foundation of the scenario testing. This assessment has considered the potential impact of arising risks on the business model, future performance, solvency and liquidity over the period in question.

In making their assessment, the Directors reviewed the principal risks and considered which risks might threaten the Company's viability. Over the course of the year the Audit Committee has considered a deep-dive review of the following principal risks to enable a thorough assessment of the impact of these risks on ongoing viability:

Matters considered by the Audit Committee
Retention and development of skills
Working practices response to COVID-19
Cyber Security
Non-payment of customer debt
Brexit readiness
Pollutions Mngement
Climaer Change adaption

In performing this stress testing the following factors have been considered:

- Principal risks have been ascribed a value with reference to risk weighting, factoring in the likelihood of occurrence and financial impact
- Ofwat viability scenarios have been modelled and monetised.

The Ofwat viability scores are as follows:

- Totex underperformance (15% of totex)
- ODI penalty (3% of RoRE) in one year
- Inflation sensitivities (+/-3%)
- Increase in the level of bad debt (20%)

- New debt financed at 2% above forward projections
- Financial penalty – equivalent to 3% of turnover
- Any relevant inter-company financing scenarios.

These scenarios were considered in isolation and in the following combination:

- 10% totex underperformance in each of the years to the end of 2030
- ODI penalty of 1.5% in each of the years to the end of 2030
- A one-off financial penalty of 1% of revenue.

Through this testing, it has been determined that none of the individual principal risks or Ofwat viability scenarios would in isolation, or in aggregate, compromise the Company's viability.

In addition, a reverse engineered scenario that could possibly compromise the Company's viability over the assessment period has been modelled. This scenario builds on the factors above and additionally assumes all the Company's principal risks incurring each year with maximum effect and no probability weightings attached.

The Board considered the likelihood of this scenario on the Company's viability over the period to 2030 and noted the potential mitigating actions which could include a reduction in capital and operational spend and dividends, concluding the Company could remain viable.

In making its assessment of the Company's viability, the Directors have taken account of the Company's robust capital solvency position, the Company's latest assessment of the COVID-19 pandemic, its ability to raise new finance and a key potential mitigating action of restricting any non-contractual payments. In assessing the prospects of the Company, the Directors note that, as the Company operates in a regulated industry which potentially can be subject to non-market influences, such assessment is subject to uncertainty, the level of which depends on the proximity of the time horizon. Accordingly, the future outcomes cannot be guaranteed or predicted with certainty. As set out in the Audit Committee's report on page 83, the Directors reviewed and discussed the process undertaken by management and also reviewed the results of the stress testing performed.

As part of the Board's considerations additional scenarios concerning viability were reviewed. This additional assessment considered South West Water's regulatory financial ring-fence and applied the Ofwat scenarios. These scenarios in isolation and the combination noted above did not compromise the viability of South West Water over the assessment period to 2030.

FORWARD-LOOKING STATEMENTS

This strategic report, consisting of pages 3 to 41, contains forward-looking statements regarding the financial position; results of operations; cash flows; dividends; financing plans; business strategies; operating efficiencies; capital and other expenditures; competitive positions; growth opportunities; plans and objectives of management; and other matters. These forward-looking statements including, without limitation, those relating to the future business prospects, revenues, working capital, liquidity, capital needs, interest costs and income in relation to South West Water, wherever they occur in this strategic report, are necessarily based on assumptions reflecting the views of South West Water as appropriate.

They involve a number of risks and uncertainties that could cause actual results to differ materially from those suggested by the forward-looking statements. Such forward-looking statements should, therefore, be considered in the light of relevant factors, including those set out in this section on principal risks and uncertainties.

The strategic report consisting of pages 3 to 41 was approved by the Board on 30th June 2021.

By Order of the Board

S Davy
Chief Executive Officer
30th June 2021

GOVERNANCE AND REMUNERATION

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CHAIR'S LETTER

On behalf of the Board, I am pleased to introduce the corporate governance report for 2021. This continues to be the Board's principal method of reporting on our governance policies and our application of the principles of good corporate governance.

Strong governance is central to our successful management of the Company and it provides the framework for the effective delivery of our strategy, fulfilment of our purpose, the creation of value for all our stakeholders and the ongoing development of our sustainable business. As Chair of South West Water, one of my overriding responsibilities is to ensure the highest standards of corporate governance. The table on pages 80 and 81 will help you to navigate our reporting and evaluate our performance against the Principles of the 2018 UK Corporate Governance Code.

South West Water is a subsidiary of Pennon Group plc, however as a regulated water and wastewater business, South West Water complies with the requirements of Ofwat. It has its own independent Board of Directors and operates as if it is a publicly listed company in its own right.

The South West Water Board, which includes myself as Chair, two Executive Directors, four Independent Non-Executive Directors convenes on the same day as each Pennon Group Board meeting and considers South West Water strategy, performance and regulatory planning.

ROLE OF THE BOARD AND ITS EFFECTIVENESS

My first role as Chair is to provide leadership to the Board and to provide the right environment to enable each of the Directors and the Board as a whole to perform effectively to promote the success of the Company for the benefit of its stakeholders.

It is my view that the Board continues to be highly effective with a good understanding of the Company's opportunities as well as the threats facing the business. This view is supported by the results of this year's Board and Committee performance evaluations. Further details are provided on page 95.

PURPOSE AND VALUES

The Board was keen that our vision and purpose should reflect the wider social contract we have with our customers and the communities we serve. Our new vision, 'Bringing Water to Life', and our purpose, 'supporting the lives of people and the places they love for generations to come', demonstrate the unique role we play in providing a vital service for the public good. These statements, together with our well-embedded core values (trusted, responsible, collaborative and progressive), guide the Board in all of its activities and decision making.

MONITORING THE COMPANY'S CULTURE

Organisations that embody a clear sense of vision and purpose deliver good results and the most successful workplace cultures are built on trust. The Board relies on employee engagement as a way of monitoring the organisation's culture, most notably our Trust Index © score. This is explained on page 24.

STAKEHOLDER ENGAGEMENT

The Board understands the part South West Water can play in Bringing Water to Life and creating a more sustainable UK. We are committed to carrying out our business in a responsible way and remain focused at improving the provision of water and wastewater services for benefit of all our stakeholders.

Our section 172 statement describes in more detail how the Board has had regard to the interests of all our stakeholders when carrying out its duties. The statement can be found on page 126.

We engage and consult with employees by means of the South West Water employee engagement forum, which, together with regular meetings with particular groups of employees, is used to ensure that employees are kept up to date with the business performance of the Company. We consult regularly with trade union appointment representatives or consultation groups. The Company also cascades information weekly to all employees via The Big Chat, to provide them with important and up to date information about key events and to obtain feedback from them. We will continue to develop and evolve the opportunities for employees' views and input through staff forums, the Big Chat, and through our Speak Up channel.

The Board was disappointed to be prevented from carrying out site visits during 2020/21 due to COVID-19. The Directors did however embrace the opportunities provided by technology and undertook a virtual visit at a major wastewater treatment site where the team showcased our health and safety approaches.

We continue to engage actively with all our stakeholders including our customers, our communities, our people and our suppliers, our regulators and other stakeholders. We are acutely aware that all of our stakeholders are struggling with the challenges posed by an uncertain future and commit to maintaining appropriate and regular dialogue to ensure that the rationale for our strategy and our performance objectives reflects their expectations. Our continuous engagement allows stakeholders to provide feedback on the matters they consider to be important and any issues which they would like to be addressed. Further detail on stakeholder engagement is contained on pages 34 to 37 of the Pennon annual report.

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE AND OTHER REQUIREMENTS

South West Water aims to comply with the UK Corporate Governance Code (the 'UK Code') as fully as possible, within the context of being a subsidiary of a listed company, Pennon Group plc, which itself fully complies with the UK Code. The UK Code is published on the Financial Reporting Council (FRC) website, www.frc.org.uk.

Given the Group structure, there are a limited number of areas in which South West Water does not comply with specific Code provisions. These areas are described on page 81 and 82 alongside any additional mitigations deemed necessary.

In addition, South West Water has complied with Ofwat's revised 'Board leadership, transparency and governance' principles. Further details on our compliance with these principles will be provided in our Annual Performance Report and Regulatory Reporting.

My introduction to this corporate governance report and the following sections are made in compliance with the UK Code and cover the work of our Board and its Committees, our internal control systems and procedures including risk management, our corporate governance statements relating to share capital and control, our confirmation of the Company as a going concern and Directors' responsibility statements. Finally, in accordance with reporting requirements, on pages 123 to 125 the Board is able to confirm that the annual report and accounts taken as a whole is fair, balanced and understandable and provides the information necessary to assess the Company's passion, performance, business model and strategy.

SOUTH WEST WATER LIMITED BOARD OF DIRECTORS

The South West Water Board of Directors at the end of the 2020/21 financial year comprises the Chair (a Non-Executive Director), a Senior Independent Director (Non-Executive), two Executive Directors and three further Independent Non-Executive Directors. In addition Paul Boote, Pennon Group Finance Director attends the South West Water Board meetings. The Board considers the Non-Executive Directors to be independent in accordance with the UK Corporate Governance Code. The Board believes its Directors have an appropriate range of skills and experience in their respective disciplines and personality to bring independent and objective judgment to the Board's deliberations.

<p>Gill Rider CB Chair</p>
<p>Appointment Gill was appointed to the South West Water Board on 1 April 2016, having been appointed to the Pennon Group plc board on 1 September 2012.</p> <p>She became Chair of South West Water on 31 July 2020 and is also Chair of Pennon Group plc.</p> <p>She is also Chair of the Nomination Committee and a member of the Remuneration Committee and the Environmental, Social and Governance Committee.</p>
<p>Skills and experience Gill has a wealth of experience in leadership, governance and remuneration across a broad range of sectors including professional services, education, not for profit and government.</p> <p>Gill was the senior independent Director of Charles Taylor plc until its sale in January 2020.</p> <p>Formerly, she was head of the Civil Service Capability Group in the Cabinet Office reporting to the Cabinet Secretary and prior to that held a number of senior positions with Accenture LLP culminating in the post of Chief Leadership Officer for the global firm. She was previously president of the Chartered Institute of Personnel and Development and chair of the council of the University of Southampton.</p>
<p>External appointments Gill is currently a Non-Executive Director of Intertek Group plc where she is also Chair of their Remuneration Committee. In addition to her Plc roles, Gill is the President of the Marine Biological Association.</p>

<p>Susan Davy Pennon Group and South West Water Chief Executive Officer</p>
<p>Appointment Susan was appointed Chief Executive Officer on 31 July 2020. She was appointed to the Board in February 2015 as Chief Financial Officer, having joined the Group as Finance Director of South West Water in 2007.</p> <p>She is a member of the Environmental, Social and Governance Committee, Health and Safety Committee, Pennon Executive and the Pennon Board.</p>
<p>Skills and experience Susan's knowledge of the industry, coupled with her financial and regulatory expertise, has underpinned the development of Pennon's strategy which has included the value creating acquisition of Bournemouth Water in 2015 and the successful Viridor disposal process, both of which she has led. In her 25 years' experience in the utility sector, Susan has also held a number of other senior roles in the water sector, including at Yorkshire Water.</p> <p>Under her guidance South West Water is the only water company to have achieved fast-track status for two consecutive business plans – the first in 2014, the second in 2019.</p> <p>Susan is highly respected in the City and has been instrumental in building Pennon's reputation.</p>
<p>External appointments She is a Non-Executive Director and Audit Chair of Restore Plc, a member of the CBI President's Committee, deputy Chair of the CBI South West, having served as Chair from 2018-2021, a Water UK Board member, member of the Energy & Utilities Skills Partnership Council and was previously a member of the A4S (Accounting for Sustainability) CFO leadership network.</p>

Louise Rowe Finance Director
Appointment Louise was appointed South West Water Finance Director on 1 February 2015. In October 2020 she was also appointed Pennon Sustainability Director.
Skills and experience Louise is a chartered accountant and has been with South West Water for over 12 years. She has held a range of managerial roles within Finance prior to her appointment as Finance Director. Louise holds a number of directorships with South West Water Group companies and is a key member of several Executive subsidiary Committees including the ESG Committee which she chairs. Prior to joining South West Water, she qualified with KPMG, following completion of her physics degree.
External appointments None

Neil Cooper Senior Independent Director (Non-Executive Director)
Appointment Neil was appointed to the Board on 1 April 2016, having joined the Pennon Group plc Board on 1 September 2014. He is chairman of the Audit Committee and a member of the Remuneration, Nomination and Environmental, Social and Governance Committees.
Skills and experience Neil brings to the Board extensive experience in a wide variety of corporate and financial matters. He is currently the Chief Financial Officer of Currencies Direct, a foreign exchange broker and international payment provider. Previously he was Group Finance Director of Barratt Developments plc and, before that, Group Finance Director of William Hill plc and Bovis Homes plc. He also held senior finance positions at Whitbread plc, worked for PricewaterhouseCoopers as a management consultant and held a number of roles with Reckitt & Colman plc. As Chairman of the Audit Committee, Neil has been influential in directing the Company's approach on a number of significant matters including internal control, governance and financial reporting.
External appointments Neil is an Executive Director of Currencies Direct.

Jon Butterworth MBE Independent Non-Executive Director
Appointment Jon was appointed to the Board on 28 September 2017. He is a member of the Audit, Remuneration, Nomination and Environmental, Social and Governance Committees. Jon is also independent scrutineer of health & safety processes across the Group (including within South West Water) to help ensure that these are robust and effective.
Skills and experience Jon has a distinguished track record within the utility industry, having started his career over 40 years ago in British Gas as an apprentice technician and subsequently progressing through a variety of senior leadership roles spanning Construction, Asset Management, Regulation and Operations. As the Managing Director of North West Gas and subsequently the National Operations Director in National Grid, Jon was accountable the United Kingdom Gas Emergency Service, all construction and field operation before taking on the role of Global Director of Safety, Sustainability & Resilience. Jon is currently Chief Executive Officer of National Grid Ventures (NGV) and a member of the National Grid Plc Executive committee, providing direction and leadership to a sizeable portfolio of gas and electricity assets, both onshore and offshore, across the US and Europe in addition to 9 million metering customers applying strategic thinking and commerciality to ensure continued growth and profitability. Jon's utility background provides him with an immense depth of knowledge and experience of the importance of maintaining a balance between profit and safety and constructively challenges the Board and management to constantly raise the bar in this area. Jon is passionate about corporate and social responsibility and was awarded an MBE in 2009 for services to Britain's Gas Industry. He was instrumental in the Government's Rehabilitation of Young Offenders programme and has dedicated over 10 years to Special Olympics Great Britain (SOGB).
External appointments Jon is a Fellow of the Institute of Directors and is also Chairman of CORGI, North Sea Link, NEMO Link, BritNed Netherlands, Ex-Ambassador of the HM Young Offenders Programme, Director of the Gas and Safety Trust and a Trustee of the National Gas Museums Trust.

Iain Evans CBE Independent Non-Executive Director

Appointment Iain was appointed to the Board on 31 July 2020, having served on the Pennon Board since 1 September 2018. He is chairman of the Environmental, Social and Governance Committee and a member of the Audit, Nomination and Remuneration Committees.

Skills and experience Iain has 40 years of extensive global experience in advising companies and governments on issues of complex corporate strategy. In 1983, he co-founded L.E.K Consulting in London and built it into one of the World's largest and most respected corporate strategy consulting firms with a global footprint active in a wide range of industries. Iain was appointed a Non-Executive Director of Welsh Water plc in 1989 and served on the Board for nearly 10 years, including five as Chairman.

As chairman of the ESG Committee for both Pennon Group and South West Water, Iain is leading the development of a sustainability programme that underpins the delivery of Pennon's strategy.

External appointments Iain is a Non-Executive Director of Bologna Topco Limited and also acts as an independent corporate strategy consultant.

Claire Ighodaro CBE Independent Non-Executive Director

Appointment Claire was appointed to the Board on 31 July 2020 having served on the Pennon Board since 1 September 2019. She is chair of the Remuneration Committee and is also a member of the Audit, Environmental, Social and Governance, Nomination and Remuneration Committees.

Skills and experience Claire has held a number of senior roles and directorships of UK and International organisations and has extensive Board experience of serving on audit and governance committees. In May 2019, she stepped down from Bank of America's Merrill Lynch International Board having served the maximum term.

Claire is a past president of CIMA and was the first woman to lead this organisation. She spent most of her executive career with BT plc and has also held Non-Executive directorships across a diverse portfolio including Audit Committee Chair of Lloyd's of London, The Open University and various UK public bodies including UK Trade & Investment and the British Council.

Claire was awarded a CBE in 2008 for services to business. A board level mentor, with Savile Group, from 2009-14, she has also helped executives transitioning into non-executive roles.

As Chair of the Remuneration Committee, Claire will continue to steer the Company's approach on executive remuneration, ensuring that it is aligned with and supports the Company's strategy.

External appointments Claire is Non-Executive chairman of AXA XL UK entities and Non-Executive Director of Flood Re, where she is also chair of the Audit Committee.

IN ATTENDANCE AT THE BOARD

The following attend the Board alongside the Company's Directors:

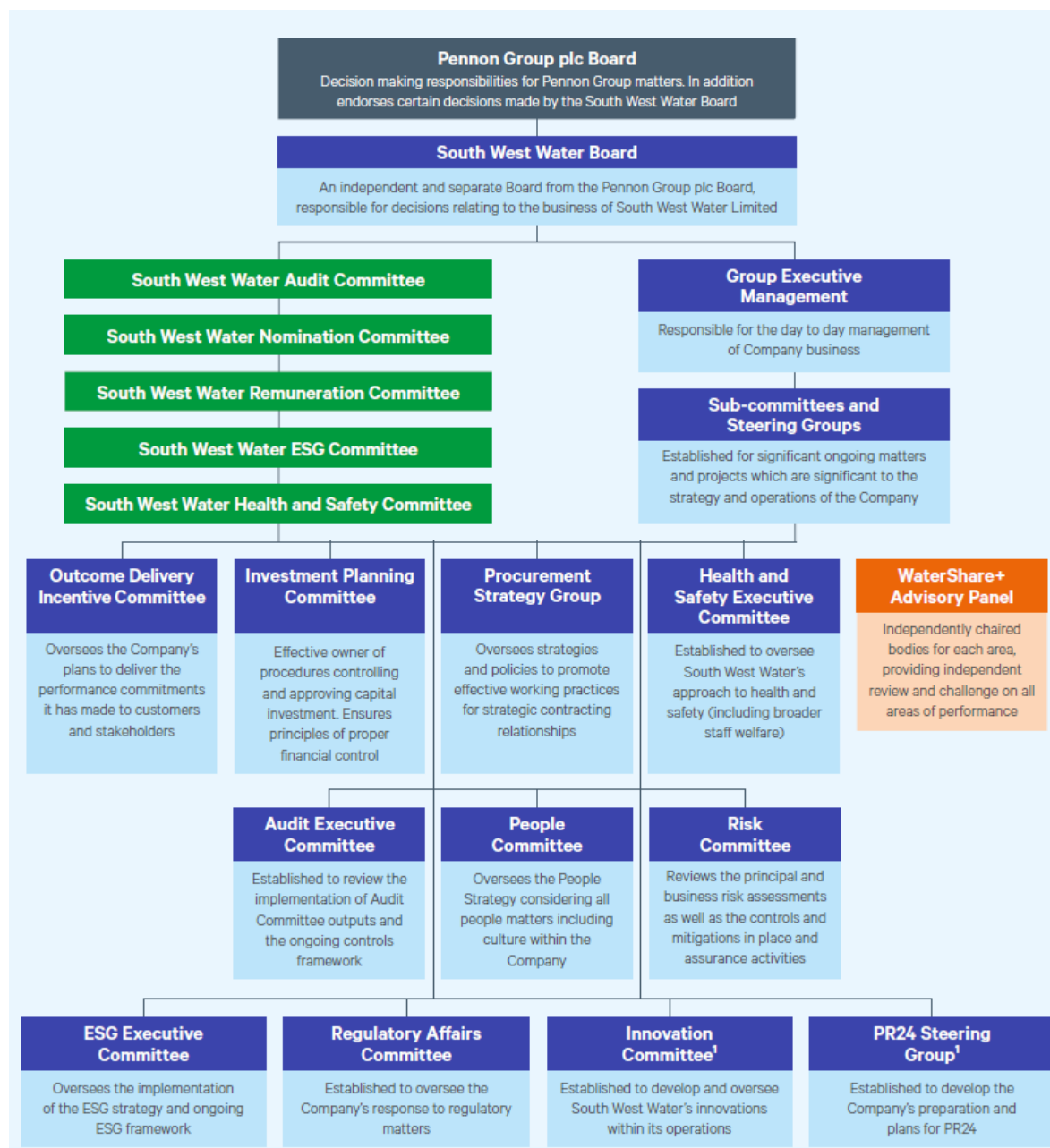
Paul Boote Pennon Group Finance Director
<p>Skills and experience Paul is a chartered accountant with over 20 years' experience in a variety of industries, with the last 10 years of his experience gained at Pennon.</p> <p>Paul has held a number of senior roles at Pennon and most recently has been Pennon's Director of Treasury, Tax and Group Finance. During this time he was responsible for the development of Pennon's sector-leading sustainable debt portfolio, ensuring the Group maintains a responsible approach to tax, as well as leading on financial reporting matters. Over the past year, Paul has been instrumental in the development and successful implementation of the Group's recent strategic review. Since 2014 he has been a regular attendee at Audit Committee meetings, where his support and contribution to discussions is highly valued. Paul holds a number of directorships with Group subsidiary companies and is a key member of the executive Finance Committee which, in his new role, he now chairs.</p> <p>Prior to joining Pennon, Paul held senior finance roles at companies operating in the sport, construction and environmental infrastructure industries.</p> <p>Paul's knowledge of the Group and relationships with key external stakeholders, coupled with his corporate finance and financial reporting experience, provides continuity to the Board as the Group evolves through this strategic review period.</p>
External appointments None

THE BOARD AND ITS GOVERNANCE FRAMEWORK

GOVERNANCE STRUCTURE

BOARD STRUCTURE SUMMARY

The following diagram summarises the context and structure within which the South West Water Board operates aligned with the revised governance approach of Pennon Group plc:



PENNON GROUP PLC BOARD

The Pennon Group Board concentrates on strategic matters for all parts of the Group. Its responsibilities include overall leadership of the Pennon Group, setting the Group's values, policies and standards, approving Pennon's strategy and objectives and providing oversight of the Group's operations and its performance. Without reserving to itself the final decision-making power, the Pennon Group board also endorses certain decisions taken by the South West Water Board, including:

- major capital projects and investments
- long-term objectives and commercial strategy
- the five-year regulatory business plan
- annual budgets
- certain decisions relating to financing.

This approach is compatible with Ofwat's 2019 principles in respect of Board leadership, transparency and governance because such decisions are ultimately reviewed by the South West Water Board.

SOUTH WEST WATER BOARD

As a regulated water and sewerage company which is part of the listed Pennon Group, it is important that South West Water acts as a separate company and that the interests of customers and other stakeholders are protected. South West Water's 'Board, Leadership, Transparency and Governance Code' commits it to acting as if it is a separate Public Listed Company as far as is possible.

The South West Water Board continues to operate as a separate independent Board in accordance with its own schedule of matters reserved to ensure compliance with Ofwat's principles on Board leadership, transparency and governance. As described in more detail on pages 79 to 82, South West Water itself complies with the UK Corporate Governance Code as far as is possible within the context of the Group structure.

The South West Water Board, which includes the Chair, the Chief Executive Officer, one SWW Executive Director and four Non-Executive Directors, convenes before each Pennon Board meeting and considers South West Water strategy, performance and regulatory planning.

Further information on the operations of the Board and Committees are included on pages 65 to 99.

THE SOUTH WEST WATER EXECUTIVE MANAGEMENT

Day-to-day management of South West Water's operations and activities is undertaken by South West Water's Executive Management. It comprises Susan Davy (Chief Executive Officer) and Louise Rowe (Finance Director), who are also members of South West Water's Board and whose experience is described on pages 65 to 67.

There are five further members of the Executive Management, who have responsibilities for key areas of operations of South West Water:

- Matthew Crabtree – Engineering and Supply Chain Director
- Jo Ecroyd – Customer Services Director
- Lisa Gahan – Regulation Director
- Ian Vosper – Operations Director (Wastewater and Networks Water Services)
- Phil Barker – Operations Director (Drinking Water Services)

Group support functions in attendance:

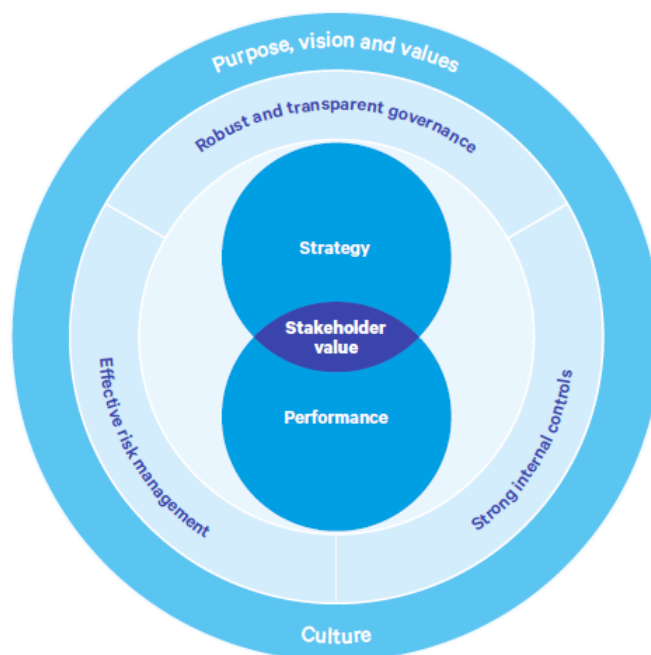
- Digital and IT Director
- Group Chief People Officer
- Group Finance Director
- Group General Counsel and Company Secretary

In addition to the details provided in this report, further information on the structure and operations of the South West Water Executive Management and the sub-committees which support the decision making of the business

is included within the South West Water Annual Performance Report and Regulatory Reporting, published in July 2021 (www.southwestwater.co.uk/report2021).

APPROACH TO GOVERNANCE

The Board acts as the main governing body for the purpose of oversight for the Company. Our approach to governance is an integral part of our culture, guiding how we do business and create value for our stakeholders.



STAKEHOLDER VALUE

We deliver sustainable value for our stakeholders by providing high quality environmental infrastructure and customer services.

STRATEGY

Our strategy is to lead in the UK's water sector, investing for sustainable growth and drive value through efficiency.

PERFORMANCE

Our financial and operational performance is driven by our strategic sustainability objectives.

ROBUST AND TRANSPARENT GOVERNANCE

We are committed to operating to the highest standards of corporate governance.

EFFECTIVE RISK MANAGEMENT

We have a mature integrated risk management framework which is embedded into existing governance structures and ways of working.

STRONG INTERNAL CONTROLS

We keep the effectiveness of our control environment under regular review and seek to continually improve our approach.

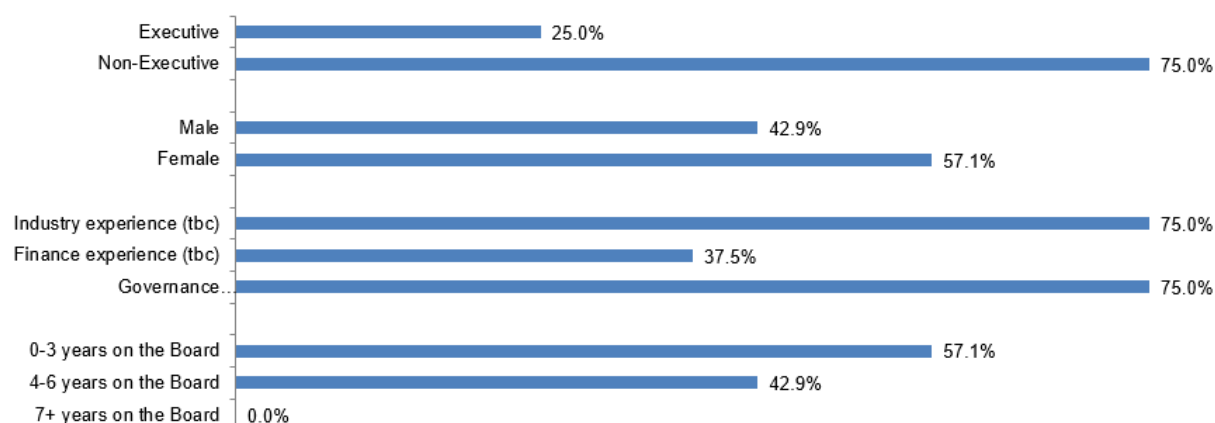
PURPOSE AND VALUES

Our purpose – bringing resources to life, supporting people and the places they love for generations to come – and its supporting values of trusted, responsible, collaborative and progressive will help drive our strategic priorities over the long term.

CULTURE

We are developing a culture that can be lived throughout the Group with integrity and transparency, ensuring we are trusted and valued by all our stakeholders.

BOARD COMPOSITION, INDEPENDENCE, EXPERIENCE AND TENURE (AS AT 31 MARCH 2021)



All of the Non-Executive Directors were considered by the Board to be independent throughout the year. None of the relationships or circumstances set out in Provision 10 of the UK Corporate Governance Code (the UK Code) applied to the Non-Executive Directors listed on page 116.

Notwithstanding their directorship of Pennon Group plc, Gill Rider, Neil Cooper, Jon Butterworth, Iain Evans and Claire Ighodaro are considered to be independent in character and judgement given that they were appointed to the South West Water Board in order to facilitate the Group's revised governance framework, rather than to represent the interests of the shareholder.

All Directors are subject to re-election each year in accordance with provision 18 of the UK Code. At year end, the Board had 57.1% female representation, which exceeds its 33% female representation target. Further details of gender diversity within the Company are described on page 26 and page 96.

All the Non-Executive Directors are considered to have the appropriate skills, experience in their respective disciplines and personality to bring independent and objective judgement to the Board's deliberations. Their biographies on pages 65 to 67 demonstrate collectively a broad range of business, financial and other relevant experience.

BOARD ROLES

During the year there was a clear separation of responsibilities between the Chair and the Chief Executive Officer, divided between managing the Board and the business, while they maintained a close working relationship.

Neil Cooper is chair of the South West Water Audit Committee and in accordance with the UK Code he has recent and relevant financial experience (as set out in his biography on page 66). The Board is satisfied that the Committee as a whole has competence relevant to the sector in which the Company operates.

All the Directors are equally accountable for the proper stewardship of the Group's affairs but they do have specific roles, which include those set out below:

Position	Director	Role
Chair	Gill Rider	<ul style="list-style-type: none"> Leading the Board and setting its agenda Promoting the highest standards of integrity and probity and ensuring good and effective governance

Position	Director	Role
		<ul style="list-style-type: none"> Managing Board composition, performance and succession planning Providing advice, support and guidance to the Executive Directors Representing the Company and being available to stakeholders Discussing separately with the Non-Executive Directors performance and strategic issues
Chief Executive Officer	Susan Davy	<ul style="list-style-type: none"> Managing South West Water and providing executive leadership Leading the operation of the Company in accordance with the decisions of the Board Co-ordinating with the Chair on important and strategic issues of the Company and providing input to the Board's agenda Contributing to succession planning and implementing the organisational structure Managing stakeholder relations
Finance Director	Louise Rowe	<ul style="list-style-type: none"> Supporting the Chief Executive Officer in providing executive leadership and developing strategy Reporting to the Board on performance and developments across the business Implementing decisions of the Board Managing specific business responsibilities
Senior Independent Director	Neil Cooper	<ul style="list-style-type: none"> Assisting the Chair with stakeholder communications and being available as an additional point of contact for stakeholders Being available to other Non-Executive Directors if they have any concerns that are not satisfactorily resolved by the Chair
Non-Executive Directors	Jon Butterworth Iain Evans Claire Ighodaro	<ul style="list-style-type: none"> Critically reviewing the strategies proposed for the Company Critically examining the operational and financial performance of South West Water Evaluating proposals from management and constructively challenging management's recommendations Contributing to corporate accountability through being active members of the Committees of the Board

BOARD MEMBERSHIP AND ATTENDANCE

The Directors and their attendance at the six scheduled meetings of the Board during 2020/21 are as follows:

Board membership		Attendance
Chair		
Gill Rider ⁽¹⁾	Chair	6/6
Sir John Parker ⁽²⁾	Chair	2/2
Non-Executive Directors		
Jon Butterworth	Independent Non-Executive Director	6/6
Neil Cooper	Independent Non-Executive Director	6/6
Iain Evans ⁽³⁾	Independent Non-Executive Director	5/5
Claire Ighodaro ⁽³⁾	Independent Non-Executive Director	5/5
Lord Matthew Taylor ⁽²⁾	Independent Non-Executive Director	2/2
Martin Hagen ⁽²⁾	Independent Non-Executive Director	2/2
Executive Directors		
Susan Davy ⁽⁴⁾	Chief Executive Officer	6/6
Louise Rowe	Finance Director	6/6
Chris Loughlin ⁽²⁾	Managing Director	2/2

⁽¹⁾Appointed as Chair with effect from 31 July 2020.

⁽²⁾Stepped down from the Board on 31 July 2020.

⁽³⁾Appointed to the Board on 31 July 2020.

⁽⁴⁾Appointed as Chief Executive Officer with effect from 31 July 2020

Other than where noted otherwise above, all Directors served during the year. In addition to the six scheduled Board meetings, a Group-wide strategy day is held in September of each year, plus there are other meetings for specific items, as needed.

MANAGING SOUTH WEST WATER

The South West Water Board continues to operate as a separate independent board - albeit with all but one of its Board members also serving on the Board of Pennon Group plc - in accordance with its schedule of matters reserved (see below) to ensure compliance with Ofwat's principles on Board leadership, transparency and governance.

The Pennon Group Board's responsibilities include overall leadership of the Group, setting the Group's values, policies and standards, approving Pennon's strategy and objectives and providing oversight of the Group's operations and its performance.

The Board delegates more detailed consideration of certain matters to the Board Committees and to the Executive Directors as appropriate, the matters reserved to the South West Water Board include:

- All acquisitions and disposals
- Major items of capital expenditure
- Authority levels for other expenditure
- Risk management process and monitoring of risks
- Approval of the strategic plan and annual operating budgets
- Company policies, procedures and delegations
- Appointments to the Board and its Committees
- Approval of the annual reports and financial statements and the Annual Performance Report and Regulatory Reporting.

Without reserving to itself the final decision-making power, the Pennon Group Board also endorses certain decisions taken by the South West Water Board, including major capital projects and investments, long-term objectives and commercial strategy, the five-year regulatory plan, annual budgets and certain decisions relating

to financing. This approach remains compatible with Ofwat's 2019 Board leadership, transparency and governance principles. Approval of South West Water's dividend policy and the declaration of dividends to be paid by South West Water to Pennon remains reserved to the South West Water Board.

OPERATION OF THE BOARD

The Board operates by receiving written reports circulated in advance of the meetings from the Executive Directors on matters within their respective business areas. The Board also receives presentations on key areas of the business and undertakes site visits to meet employees and gain a better understanding of the operation of business initiatives. In light of COVID-19 restrictions in place during the year, no physical site visits took place; Instead the Directors participated in a virtual tour of Brokenbury Wastewater Treatment Works in Torbay in March 2021.

Under the guidance of the Chair, all matters placed before the Board are discussed openly. Presentations and advice are received frequently from other senior executives within the Company and from external advisors to facilitate the decision making of the Board.

In compliance with COVID-19 restrictions, Board and Committee meetings were held online throughout the year. Although this approach presented challenges, it enabled the Company's usual high standards of governance to be maintained.

In arriving at decisions, the Board always considers the impact they might have on stakeholder groups when considering what is in the best interests of stakeholders as a whole.

The Chair and Non-Executive Directors take particular care to ensure that the Board considers the interests of customers in all matters discussed by the Board, reflecting a very real understanding of the particular pressures on South West Water customers. In addition to a monthly review of customer contact and complaint analysis, the Board is regularly updated on customer satisfaction surveys.

South West Water has monitored customer satisfaction with service and value for money quarterly for over 20 years, and has also facilitated focus groups to discuss local and regional investment. Findings from all methods of customer consultation are fed back to the Board and incorporated into Company plans.

All Directors are equally accountable for the stewardship of the Company's affairs with the Non-Executive Directors having a particular responsibility for ensuring that strategies proposed for the development of the business are critically reviewed. The Non-Executive Directors also examine the operational and financial performance of the Company and fulfil a key role in corporate accountability through their membership of the governance Committees of the Board.

SOUTH WEST WATER EXECUTIVE MANAGEMENT

The role of the South West Water Executive is to define and drive the business priorities that will achieve delivery of the strategy. It is responsible for ensuring, to the extent of the authority delegated by the Board, the proper and prudent management of resources to create and maximise shareholder value whilst protecting the interests of the wider stakeholder group.

Chaired by the Chief Executive Officer, the Executive meets regularly to receive reports and refine recommendations to be presented to the Board.

Further details concerning the Executive Management and its sub-groups are provided on pages 69 and 70 and within the South West Water Annual Performance Report and Regulatory Reporting, published in July 2021 (www.southwestwater.co.uk/report2021).

BOARD SUPPORT AND TRAINING

Directors have access to the advice and services of the Company Secretary, and the Board has an established procedure whereby Directors, in order to fulfil their duties, may seek independent professional advice at the Company's expense. The Company Secretary is responsible for ensuring that the Board operates in accordance with the governance framework and that there are good information flows between the Directors, the Board and its Committees.

Newly appointed Directors receive a formal, tailored induction which includes, inter alia, an explanation of the South West Water and Pennon Group structure, regulatory and legal issues impacting the Company, the Pennon Group governance framework and policies, the our approach to risk management and the Company's principal risks (financial and non-financial, including environmental, social and governance (ESG) risks), duties and obligations (including protocols around conflicts of interest and dealing in Pennon Group shares), and the current activities of the Board and its Committees. Newly appointed Directors are also invited to visit different operating facilities and to meet with employees to better understand key processes and systems. Gill Rider received a tailored session as Chair of South West Water which included a refresher on specific ringfenced arrangements.

The training needs of Directors are reviewed as part of the Board's performance evaluation process each year. Training will include attendance at external courses organised by professional advisers and also internal presentations from senior management. During 2020/21, refresher training was provided to the Board on Directors' duties and listing rule obligations (including the Market Abuse Regulation, Class 1 transactions and related party transactions) and the Audit Committee received a technical briefing from the external auditor, which included an update on IFRS changes and an update on financial reporting.

BOARD COMMITTEES' TERMS OF REFERENCE

In accordance with policies, a range of key matters are delegated to the Board's Committees as set out on pages 83 to 99 of this governance report.

The terms of reference of each of the Board's Committees are set out on the Company's website www.southwestwater.co.uk and are also available from the Group Company Secretary upon request. The terms of reference, as well as the Board's schedule of matters reserved, were reviewed during the year to ensure that they remained appropriate and relevant.

DEALING WITH DIRECTORS' CONFLICTS OF INTEREST

In accordance with the Directors' interest provision of the Companies Act 2006 and the Company's Articles of Association, the Board has in place a procedure for the consideration and authorisation of Directors' conflicts or possible conflicts with the Company's interests. This Board consider that this has operated effectively during the year.

Each Director has a duty under the Companies Act 2006 to avoid a situation in which they have, or may have, a direct or indirect interest that conflicts or might conflict with the interests of the Company. This duty is in addition to the existing duty owed to the Company to disclose to the Board any interest in a transaction or arrangement under consideration by the Company.

RISK MANAGEMENT AND INTERNAL CONTROL

The Board is responsible for maintaining the Company's system of internal control to safeguard shareholder investment and the Company's assets and for reviewing its effectiveness. The system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. There is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company that have been in place throughout 2020/21 and up to the date of the approval of this annual report and accounts.

The Company's system of internal control is consistent with the FRC's 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting' (FRC Internal Control Guidance).

The Board confirms that it applies procedures in accordance with the UK Code and the FRC Internal Control Guidance which brings together elements of best practice for risk management and internal control by companies. The Board's risk framework described on pages 42 to 46 in the strategic report provides for the identification of key risks including ESG risks in relation to the achievement of the business objectives of the Company, monitoring of such risks and ongoing and annual evaluation of the overall process.

ESG risks identified and assessed by the Board cover areas such as health & safety, climate change and tax compliance. Details of the key risks affecting the Company are set out in the strategic report (pages 47 to 58).

KPIs are in place to enable the Board to measure the Company's ESG performance, including agreed regulatory performance commitments in respect of Outcome Delivery Incentives (ODIs), and a number of these are linked to remuneration incentives (see pages 101 to 121). A full breakdown of performance during the year against these KPIs is provided in South West Water's Annual Performance Report, which is published in July (see www.southwestwater.co.uk/report2021).

As part of the review of the effectiveness of the system of risk management and internal control under the Company risk management policy, all Executive Directors and senior managers are required to certify on an annual basis that they have effective controls in place to manage risks and to operate in compliance with legislation and Company procedures.

The processes and policies serve to ensure that a culture of effective control and risk management is embedded throughout the Company and that the Company is in a position to react appropriately to new risks as they arise.

CODE OF CONDUCT AND POLICIES

South West Water has adopted the Pennon Group's Code of Conduct and related policies which set out the commitment to promoting and maintaining the highest level of ethical standards. Areas covered in the Code of Conduct include our impact on the environment and our communities, our workplace and our business conduct.

The policy on anti-bribery and anti-corruption strictly prohibits employees from offering or accepting bribes, facilitation payments and kickbacks. The policy requires that due diligence checks of third parties doing business with the Company, including a corruption risk assessment by the relevant unit, to examine the nature of the proposed work or transaction. The policy sets the framework for our clear requirement that everyone who works with or for us must act honestly and with integrity at all times. It has been rolled out comprehensively into all parts of the Company, with ongoing face-to-face and online training provided into business units by the dedicated Pennon Group Legal Compliance team. Enforcement of the policy is achieved through planned and ad hoc checks, the training mentioned, and detailed investigations into allegations or whistleblows received from employees, customers and suppliers around potential wrongdoing.

Specific risk assessments undertaken by the Pennon Group internal audit function identify more vulnerable areas of the Company. In order to try and mitigate risk wherever possible, targeted authorisation and oversight processes apply to the areas identified as being more vulnerable and additional training is provided.

The legal compliance team likewise actively assesses high risk areas based on information gained through their close working with business functions and Pennon Group internal audit. Assessments are undertaken using a number of entry points, including using the output of reviews with the executive teams, during and following face-to-face training, and analysing whistleblowing reports. Foreign trading operations, procurement activities and business development/commercial back-office areas continue to be specifically reviewed for compliance with anti-bribery and anti-corruption requirements. Comprehensive operating procedures are in place to address risks in those areas, with regular reviews taking place to ensure the assessment of risk remains up to date.

The policy also sets out the employment consequences for breach of the policy and potential legal sanctions under bribery laws. Any breaches or failure to adhere to the Company's strict standards of integrity and honesty will be subject to disciplinary action, up to and including dismissal from the Company. All employees are required to read, understand and comply with the policy and report any circumstances or any suspicions of fraud, bribery, corruption or other irregularities, either to a line manager or by using the Company's confidential whistleblowing ('Speak Up') service. There were no confirmed cases of bribery or corruption, and no confirmed business ethics incidents during the year.

The Speak Up service encourages employees to raise concerns about suspected wrongdoing or unlawful or unethical conduct, explains how this should be done and ensures that they are able to do so without fear of reprisals. The Company's whistleblowing policy specifically includes and encourages reporting of:

- Bribery or corruption
- Stealing or fraud
- Corruption or dishonest activity
- Anything else contrary to the law

Allegations of bribery or corruption are reported to the Audit Committee together with investigation outcome and details of any action taken, and will be disclosed to our external auditors. To date there have been no fines, penalties or significant issues reported or found in relation to bribery, corruption or fraud.

A comprehensive review and refresh our Code of Conduct and associated policies was approved by the Board in March 2021. A comprehensive programme of communication and training is now underway. In March 2021, the Board approved an updated version of the Company's Code of Conduct and associated policies following an extensive review and refresh. A comprehensive programme of training and internal communications is now underway with targeted messaging and interactive training sessions. This programme addresses the business' key compliance and principal risk areas and has been designed to increase resilience, heighten awareness and promote a culture of doing the right thing.

The Company also has policies in place covering the acceptance of gifts and hospitality, anti-facilitation of tax evasion and conflicts of interest, which requires our people to disclose any situation which may conflict with their responsibilities as South West Water employees. Our Code of Conduct and our policies are available on our website.

COMPANY AND GROUP COMPLIANCE WITH THE HIGHEST STANDARDS OF BOARD LEADERSHIP AND GOVERNANCE

South West Water Limited is a wholly-owned subsidiary of Pennon Group plc, a FTSE 250 company with a premium listing on the Official List, trading on the main market for listed securities of the London Stock Exchange.

South West Water and its parent company Pennon Group plc, remain committed to operating to the highest standards of Board leadership and governance including transparency of reporting to investors, customers, regulators and other stakeholders. The full range of South West Water's corporate issues including strategy, performance, delivery, compliance and governance are covered within the governance structure shown above.

South West Water adopted its own Board leadership, transparency and governance Code which sets out how South West Water complies with the Ofwat principles from January 2019.

The South West Water Code states that the Company will comply with the UK Corporate Governance Code (the Code) to the extent that it can be applied to South West Water within the context of the Pennon Group structure. The Company will continue to regularly review its governance structures, ensuring it continues to carry out its business in a transparent way, designed to secure the Company's long-term success and profitability. The Company complied fully with the provisions and spirit of the UK Code during the year, subject to the exceptions as described below. Most of the exceptions relate to the Group structure, where certain responsibilities rest with Pennon Group plc (South West Water's parent company) which is fully compliant with the UK Code.

Details of how we have applied the Principles that form the UK Code are provided throughout this annual report and the table below provides some useful signposting. Further the UK Code is published on the Financial Reporting Council (FRC) website, www.frc.org.uk. Exceptions are detailed below.

INDEPENDENCE OF THE CHAIR

Gill Rider (Sir John Parker resigned 31 July 2020) was considered to be independent at the time of her appointment, in accordance with Provision 9 of the Code. At that time, the Board concluded that none of the criteria set out in Provision 10 of the Code applied to Gill; although she was appointed to the position of Chair of Pennon Group plc on the same date, she was not placed on the South West Water Board by Pennon in order to represent Pennon's interests but rather to help the flow of understanding of the issues facing South West Water at Pennon Board level.

In addition, the operation of South West Water and the wider Pennon Group's governance framework is underpinned by the dual South West Water/Pennon Group plc appointments held by Gill Rider and other Non-Executive Directors.

Notwithstanding Gill's Chairship of Pennon Group plc, the South West Water Board believes she continues to demonstrate independence of character and judgement (of Pennon Group plc and its investors, and of management) when leading the Board in debate on South West Water matters.

INDEPENDENCE OF THE NON-EXECUTIVE DIRECTORS

Neil Cooper, Claire Ighodaro, Iain Evans and Jon Butterworth are Non-Executive Directors of our parent entity, Pennon Group plc. In addition, given the longer service of Neil Cooper, a particularly rigorous review was undertaken in respect of his respective re-elections. The Board remains satisfied that, based on the participation at meetings and the contribution outside of the boardroom, Neil Cooper continues to demonstrate independence of character and judgement in the performance of their role.

HOW WE PERFORMED AGAINST THE PRINCIPLES OF THE 2018 UK CODE

	UK code principles	Where
Board leadership and Company purpose	<ul style="list-style-type: none"> • An effective and entrepreneurial Board • Promoting the long-term sustainable success of the Company • Contributing to wider society 	<ul style="list-style-type: none"> • Board information (page 122) • Business model section (page 9) • ESG section (page 16)
	<ul style="list-style-type: none"> • Company's purpose, values and strategy are aligned with its culture • Directors act with integrity, lead by example and promote the desired culture 	<ul style="list-style-type: none"> • Business model (page 9) and throughout the annual report • Our people (page 24)
	<ul style="list-style-type: none"> • Resources, internal controls, risk management 	<ul style="list-style-type: none"> • Risk report (page 42)
	<ul style="list-style-type: none"> • Stakeholder engagement 	<ul style="list-style-type: none"> • Our Stakeholders (page 6) • Our People (pages 24)
	<ul style="list-style-type: none"> • Workforce policies and practices are consistent with the Company's values and support its long-term sustainable success • Workforce is able to raise any matters of concern 	<ul style="list-style-type: none"> • Our People (page 24) • See Code of Conduct information (page 77) • Speak Up information (page 25)
Division of Responsibilities	<p>The role of the Chair is to:</p> <ul style="list-style-type: none"> • Demonstrate objective judgement • Promote a culture of openness and debate • Facilitate constructive Board relations and the effective contribution of all Non-Executive Directors • Ensure the Directors receive timely, accurate and clear information 	<ul style="list-style-type: none"> • The Board and its Governance Framework (page 69) • Operation of the Board section (page 75)
	<ul style="list-style-type: none"> • Board composition – balance of Executive/Non-Executive • Clear division of responsibilities between the Chair and the CEO 	<ul style="list-style-type: none"> • Board composition (page 72) • Nomination Committee report (page 94) • Directors' roles (page 72)
	<ul style="list-style-type: none"> • NED time commitment • NED roles – to provide constructive challenge, strategic guidance, offer specialist advice and hold management to account 	<ul style="list-style-type: none"> • Board of Directors (page 65) • The Board and its Governance Framework (page 69)
	<ul style="list-style-type: none"> • The Board, supported by the Company Secretary, has the policies, processes, information, time and resources it needs to function effectively and efficiently 	<ul style="list-style-type: none"> • Operation of the Board (page 75) • Board support and training (page 76)
Composition, succession and evaluation	<ul style="list-style-type: none"> • Board appointments are subject to a formal, rigorous and transparent procedure • An effective succession plan is maintained for Board and senior management • Appointments and succession plans are based on merit and objective criteria, and should promote diversity 	<ul style="list-style-type: none"> • Nomination Committee report (page 94)
	<ul style="list-style-type: none"> • The Board and Committees have a combination of skills, experience and knowledge • Consideration is given to the length 	<ul style="list-style-type: none"> • Board of Directors (page 65) • Board composition, independence and experience (page 72)

	UK code principles	Where
	<ul style="list-style-type: none"> of service of the Board as a whole and membership regularly refreshed Annual evaluation of the Board considers its composition, diversity and how effectively members work together to achieve objectives Individual evaluation demonstrates that each director continues to contribute effectively 	<ul style="list-style-type: none"> Nomination Committee report (page 94)
Audit, risk and internal control	<ul style="list-style-type: none"> The Board has established policies and procedures to ensure the independence and effectiveness of internal and external audit functions and satisfy itself on the integrity of the financial and narrative statements 	<ul style="list-style-type: none"> Audit Committee report (page 83)
	<ul style="list-style-type: none"> The Board presents a fair, balanced and understandable assessment of the Company's position and prospects 	<ul style="list-style-type: none"> Audit Committee report (page 83) Statement of Directors' Responsibilities (page 129)
	<ul style="list-style-type: none"> The Board has established procedures to manage risk, oversee the internal control framework and determine the nature and extent of the principal risks the Company is willing to take in order to achieve its long-term strategic objectives 	<ul style="list-style-type: none"> Risk report (page 42)
Remuneration	<ul style="list-style-type: none"> Remuneration policies and practices are designed to support strategy and promote long-term sustainable success. Executive remuneration is aligned to the Company's purpose and values, and is clearly linked to the successful delivery of the long-term strategy 	<ul style="list-style-type: none"> Directors' Remuneration report (page 100)
	<ul style="list-style-type: none"> There is a formal and transparent procedure for developing policy on Executive Remuneration and determining director and senior management remuneration. No Director is involved in deciding their own remuneration outcome. 	<ul style="list-style-type: none"> Remuneration Committee report (page 97)
	Directors: <ul style="list-style-type: none"> Exercise independent judgement and discretion when authorising remuneration outcomes; and take account of Company and individual performance, and wider circumstances 	<ul style="list-style-type: none"> Directors' Remuneration report (page 100)

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE

Throughout the year, South West Water complied with its own Board leadership, transparency and governance Code. The South West Water Code states that the Company will comply with the current UK Corporate Governance Code (the UK Code) to the extent it can be applied to the Company in the context of the Pennon Group structure.

The Company complied fully with the provisions and spirit of the UK Code during the year, subject to the exceptions as described below. Most of the exceptions relate to the Group structure, where certain

responsibilities rest with Pennon Group plc (South West Water's parent company) which is fully compliant with the UK Code.

Provision 25 of the UK Code states that the Audit Committee should make recommendations to the Board in relation to the appointment, re-appointment and removal of the external auditor and to approve the remuneration and terms of engagement of the external auditor. Provision 25 also states that the Audit Committee should develop and implement policy on the engagement of the external auditor to supply non-audit services. As the auditor is appointed on a Group basis, the appointment, re-appointment and removal of South West Water's external auditor is (and has been throughout the year) a matter for the Pennon Group Audit Committee, as is the auditor's remuneration, terms of engagement and non-audit services.

Provision 26 of the UK Code states that a separate section of the annual report should describe the work of the Committee in discharging its responsibilities, in particular an assessment of the effectiveness of the external audit process. Due to the Group structure, the overall assessment as to whether the external audit function is effective (and has been throughout the year) is the responsibility of the Pennon Group Audit Committee, which carries out its assessment in conjunction with the South West Water Audit Committee.

Provision 33 of the UK Code states that the Remuneration Committee should have delegated responsibility for determining the policy for Executive Director remuneration and setting remuneration for the Chair, Executive Directors and senior management. However, the remuneration of the Chair, who is also the Chair of Pennon Group plc and the Pennon Group Chief Executive Officer, who is also a member of the Pennon Group plc Board is the responsibility of the Pennon Group Remuneration Committee.

During the year Pennon Group plc complied fully with the UK Code. Full reports of the Pennon Group plc Board's Committees are contained within the Pennon Group plc annual report and accounts.

THE AUDIT COMMITTEE

The report provides details of the work carried out by the Committee and highlights our focus areas during 2020/21. As in previous years, the principal responsibilities of the Committee continue to be focused on three key areas:

- Ensuring the quality and integrity of the Company's financial reporting; an activity that includes the assessment of the application of accounting policies given underlying standards, probing and testing of accounting judgements made in preparing financial reporting and the assessment of whether the presentation of the Company's activities is fair, balanced and understandable
- Reviewing and challenging the ongoing effectiveness of the internal control environment
- The scope and adequacy of risk management processes across the Company. This encompasses monitoring the Company's risk appetite as well as acting as a forum for carrying out more detailed reviews of higher risk areas of the operation.

These responsibilities are discharged throughout the year in accordance with a schedule of business reflecting the annual reporting cycle of the Company, which is designed to allow sufficient time for their consideration while also permitting time to be spent on related key accounting matters. Monitoring and reviewing the effectiveness of the external auditor and the internal audit function is a further important ongoing element of the Committee's assurance activities.

The Company's executive risk management forum continues to assess risk appetite and monitor key risks and their mitigation, with the Committee subsequently receiving detailed 'deep dive' presentations from senior management on areas impacting our principal risks. During the year, these covered a wide range of topics including recruitment and retention of staff, cyber security, our response to the COVID-19 pandemic, the processes and payment around our customer debt, our performance in relation to pollution and our response to climate change. More detail on our risk management processes, principal risks and their associated mitigation can be found on pages 42 to 58.

Alongside with this risk-orientated activities, we continue to review the output of the Group's financial resilience and health assessments; over a 12 month period through our assessment of the the Company's 'Going Concern' status and over a period until 2030 as it relates to the Company's continuing viability. This year, the viability assessment has considered a range of financial projections given a more complex environment including the ongoing and potential future impacts of the COVID-19 pandemic. South West Water has continued to use a longer assessment period to 2030, noting a greater visibility of future cash flows, being a regulated business. Our viability statement is reported on page 59.

As part of the half-year and year-end reporting review process, we reviewed, probed and challenged the key financial reporting judgements of management as set out on page 85 and 86. Significant matters considered by the Committee both during the year and in relation to the year-end financial statements are laid out in this report.

Looking ahead to 2021/22, as we better understand the full impact of the COVID-19 pandemic, the Committee will remain vigilant and continue to monitor developments and adapt its approach – where necessary - to best support the Company's stakeholders.

SOUTH WEST WATER AUDIT COMMITTEE COMPOSITION AND MEETINGS

Five meetings of the South West Water Audit Committee were held during the year. Membership of the South West Water Audit Committee and their attendance was as follows:

Membership	Position	Attendance
Neil Cooper	Chair	5/5
Gill Rider ⁽¹⁾	Non-Executive Director	2/2
Jon Butterworth	Non-Executive Director	2/3
Iain Evans ⁽²⁾	Non-Executive Director	3/3
Claire Ighodaro ⁽²⁾	Non-Executive Director	3/3
Lord Matthew Taylor ⁽³⁾	Non-Executive Director	2/2
Martin Hagen ⁽³⁾	Non-Executive Director	2/2

⁽¹⁾Gill Rider stood down as a member of the Audit Committee upon her appointment as Chair of the Board on 31 July 2020. She has attended all Audit Committee meetings since that date as an invitee

⁽²⁾Appointed to the Committee with effect from 31 July 2020.

⁽³⁾Stepped down from the Committee with effect from 31 July 2020.

Regular attendees to Committee meetings during the year included: the Chief Executive Officer, Pennon Group Finance Director, the Group General Counsel and Company Secretary, South West Water Finance Director, the Director of Risk and Assurance, Pennon Group Financial Controller and the external auditor.

In addition, the Board Chair has an open invitation to attend the Committee meetings. In the last year her attendance included those meetings at which the Committee reviewed the half-year and full-year financial results of the Company.

The Board is satisfied that all Non-Executive Directors have recent and relevant financial experience and competence in accounting or auditing. Details of their significant current and prior appointments are set out on pages 65 to 67.

The Chair and fellow Committee members are also members of the Remuneration Committee, which allows them to provide input into both Committees on any Group performance matters and on the management of any risk factors relevant to remuneration matters.

SIGNIFICANT MATTERS CONSIDERED BY THE AUDIT COMMITTEE

A calendar of business of the Committee sets in place a framework for ensuring that it manages its affairs efficiently and effectively throughout the year and is able to concentrate on the key matters that affect the Company.

The most significant matters that the Committee considered and made decisions on during the year and, where appropriate, since the year end, are set out below.

Financial reporting	<ul style="list-style-type: none"> • Monitored the integrity of the financial statements of the Company and the half-year and full-year results relating to the Company's financial performance, including reviewing and discussing significant financial reporting judgements contained in the statements • Reviewing the internal assessment of Going Concern and longer term viability on behalf of the Board • After a detailed review in accordance with its established process, advised the Board that the presentation of the annual report & accounts is fair, balanced and understandable in accordance with reporting requirements and recommended their approval for publication • Internal control processes, systems and compliance • Review of internal audit reports on core systems and processes across the Company.
External auditor	<ul style="list-style-type: none"> • Considered auditor's report on its audit of the annual results focusing on key findings • Assessed external auditor effectiveness in respect of the previous year's external audit process • Considered the auditor's report on control themes and observations for the year ended 2020, which did not identify any significant deficiencies. <p>Note, in line with the structure of the Group, certain activities such as recommending reappointment of the statutory financial auditor and assessment of effectiveness of the statutory financial auditor are performed by the Pennon Group Audit Committee. The responsibilities of the Pennon Group Audit Committee are described in the Pennon Group annual report (pages 98 to 101).</p>
Risk management	<ul style="list-style-type: none"> • Reviewed the Company's risk management framework and compliance with that framework during the year and after the year end up until the publication of the Company's annual report • Reviewed the assessment of the risks by the Executive Directors and considered risk appetite • Reviewed the Company risk register and considered appropriate areas of focus and prioritisation for the audit work programme for the year • Assessment of information security across the Company in mitigating key IT risks • As part of the risk management review, considered the annual report on any whistleblowing • Carried out regular deep dives at Committee meetings on principal risk areas.
Governance	<ul style="list-style-type: none"> • Considered and approved Company accounting policies, including the impact of new accounting standards, used in the preparation of the financial statements • Confirmed compliance with the UK Code • Regularly held meetings with the external auditor and the Group Director of Risk and Assurance without members of management being present.

In respect of the monitoring of the integrity of the financial statements, which is a key responsibility of the Committee identified in the UK Code, the significant areas of judgement considered in relation to the financial statements for the year ended 31 March 2021, are set out in the following table, together with details of how each matter was addressed by the Committee.

At the Committee's meetings throughout the year the Committee and the external auditor have discussed the significant matters arising in respect of financial reporting during the year, together with the areas of particular audit focus, as reported on in the independent auditor's report on pages 131 to 140. In addition to the significant matters set out in the table below, the Committee considered presentational disclosure matters including the use on non-underlying performance metrics disclosures, and ensuring a fair presentation of statutory and non statutory performance and financial measures.

During the year, the Committee's areas of focus included:

Area of focus by the Committee: Revenue recognition

How the matter was addressed by the Committee:

Given the nature of the Company's revenue, the areas of judgement for continue to be in respect of revenue recognition relating to income from measured water services and estimates of timing of receipt of unmeasured revenue. Whilst the Committee relied on South West Water's evolving processes for assessment of water into supply, it scrutinised its track record of accuracy looking back at actual outturns versus accruals at previous year ends. The Committee also closely considered the work in respect of these areas at year end by the external auditor as well as reviewing disclosures around revenue recognition accounting policies.

Area of focus by the Committee: Bad and doubtful debts

How the matter was addressed by the Committee:

Regular updates on progress against debt collection targets and other contractual payments due are received by the Board. Performance is monitored regularly against both South West Water's historical collection record and the track record of other companies in the sector. The Committee was particularly mindful of the ongoing impacts of the COVID-19 pandemic on the assessment of expected credit losses (ECLs) in determining the bad debt provision, noting the full impacts of the pandemic on businesses customer bases are unlikely to be fully seen until the UK Government's economic support packages are withdrawn. At the year end the external auditor reported on the work it had performed, which, together with the detailed analysis reported, enabled the Committee to conclude that management's assessment of the year-end position and its provisions for ECL's was reasonable.

Area of focus by the Committee: Going concern basis for the preparation of the financial statements and viability statement

How the matter was addressed by the Committee:

A report from the Pennon Group Finance Director on the financial performance of both the Pennon Group and South West Water, including forward-looking estimates of covenant compliance and funding levels under different scenarios, is provided to the Board on a periodic basis. Rolling five-year strategy projections and the resultant headroom relative to borrowings are also regularly reviewed by the Board, including scenarios to enable the Committee to better understand the potential range of outcomes. At the end of each six-month period the Pennon Group Finance Director prepares for consideration by the Committee a report focusing on the Group's liquidity over the 12-month period from the date of signing of either the annual report or half-year results. The report for 2020/21 included a scenario for the potential impact of the COVID-19 pandemic. The Committee also reviewed a report from the Pennon Group Finance Director on the Company's financial viability over an appropriate period, which the Board considers to be up to 2030, in connection with the UK Corporate Governance Code and Ofwat's requirement for a viability statement to be given by the Board. Similarly, this report also considered the viability of the Company considering the potential ongoing impacts of the COVID-19 pandemic alongside the manifestation of other adverse events modelled from the Company's principal risks and Ofwat's mandated sensitivities for water companies. Consideration of these reports and constructive challenge on the findings of the reports, including the scenario testing carried out by management, has enabled the Committee to form its assessment and satisfy itself that it remains appropriate for the Company to continue to adopt the going concern basis of accounting in the preparation of the financial statements and in addition advise the Board on providing the viability statement set out on page 59.

EFFECTIVENESS OF THE EXTERNAL AUDIT PROCESS

Receiving high-quality and effective audit services is of paramount importance to the Committee. We continue to monitor carefully the effectiveness of our external auditor as well as their independence, whilst recognising that there is a need to use our external auditor's firm for certain non-audit services. We have full regard to the FRC's Ethical Standard and ensure that our procedures and safeguards meet these standards.

The current external auditor, Ernst & Young LLP (EY), was appointed following a comprehensive audit tender process and approval by shareholders at the Company's 2014 AGM. Their reappointment was approved at the 2020 Annual General Meeting. Christabel Cowling is the audit partner and has been in that role since 2019.

The external auditor produced a detailed audit planning report in preparation for the year-end financial statements, which has assisted the auditor in delivering the timely audit of the Company's annual report & financial statements and which was shared with, and discussed by, the Committee in advance.

The effectiveness review of the external auditor is undertaken as part of the Committee's annual performance evaluation which also examines the relationship and communications between the Committee and the external auditor. Further details of the performance evaluation are provided on page 86. No issues were raised during that review and the Committee concluded that the auditor was effective during the year and that the relationship and communications were open and constructive.

The Committee considered that it is appropriate that the external auditor be reappointed and has made this recommendation to the Board. The Committee chair has also met privately, via telephone, with the external auditor to discuss key matters.

AUDITOR INDEPENDENCE

The Committee carefully reviews on an ongoing basis the relationship with the external auditor to ensure that the auditor's independence and objectivity are fully safeguarded.

The external auditor reported on their independence during the year and again since the year end, confirming to the Committee that, based on their assessment, they were independent of the Company.

PROVISION OF NON-AUDIT SERVICES

The Committee continues to have a robust policy for the engagement of the external auditor's firm for non-audit work. The Committee receives a regular report covering the auditor's fees including details of non-audit fees incurred.

Recurrent fees typically relate to agreed procedures in relation to annual regulatory reporting obligations to Ofwat; work which is most efficiently and effectively performed by the statutory auditor. The policy is for non-audit fees not to exceed 70% of the audit fee for statutory work and for the Committee chair to approve all non-audit work performed by the statutory auditor. The Committee carefully reviews non-audit work proposed for the statutory auditor, taking into consideration whether it was necessary for the auditor's firm to carry out such work and would only grant approval for the firm's appointment if it was satisfied that the auditor's independence and objectivity would be fully safeguarded. If there were another accounting firm that could provide the required cost-effective level of experience and expertise in respect of the non-audit services, then such firm would be chosen in preference to the external auditor.

The level of non-audit fees payable to the external auditor for the past year is 23.1% of the audit fee, which is well within the Company's 70% non-audit fee limit.

INTERNAL AUDIT

The internal audit activities of the Company are a key part of the internal control and risk management framework of the Company. There is a long-standing and effective centralised internal audit service at Pennon Group plc which makes a significant contribution to the ability of the Committee to deliver its responsibilities.

Following the establishment in 2019 of a new directorate of Risk and Assurance, encompassing Group risk

reporting and internal audit, the Group's internal audit function has continued to operate effectively. The 2020/21 Group and Company internal audit plan was approved in May 2020 following a thorough review to ensure that the Company was sufficiently flexible to respond to emerging risks, including the impact of COVID-19. In developing the plan, account is taken of the principal risks, the activities to be undertaken by the external auditor, and the Group's annual and ongoing risk management reviews. This approach seeks to ensure that there is a programme of internal and external audit reviews focused on identified key risk areas throughout the Company.

The Director of Risk and Assurance reported regularly through the year to the Committee on audit reviews undertaken and their findings, and there were regular discussions, correspondence and private meetings between the Director of Risk and Assurance and the Committee chair.

The Committee's annual internal assessment of the internal audit function was completed in March 2021 and considered conformance with the Code of Ethics, International Standards and Code of Practice published by the Institute of Internal Auditors, as well as the outputs from stakeholder satisfaction surveys and the resources, skills and experience within the team. The Committee concluded that the Group Internal Audit function continues to be effective. The next cyclical external review of the internal audit function will be undertaken in 2021/22.

FAIR, BALANCED AND UNDERSTANDABLE ASSESSMENT

To enable the Committee to advise the Board in making its statement that it considered that the Company's annual report & accounts is fair, balanced and understandable (FBU) on page 123, the Committee has applied a detailed FBU review framework that takes account of the Company's well-documented verification process undertaken in conjunction with the preparation of the annual report & accounts. This is in addition to the formal process carried out by the external auditor to enable the preparation of the independent auditor's report, which is set out on pages 131 to 140.

In preparing and finalising the 2021 annual report & accounts, the Committee considered a report on the actions taken by management in accordance with the FBU process and an FBU assessment undertaken by the Pennon Executive. This assisted the Committee in carrying out its own assessment and being able to advise the Board that it considered that the annual report & accounts taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's performance, business model and strategy.

STATEMENT OF COMPLIANCE WITH CMA ORDER

Pennon Group plc undertook a competitive audit tender process in 2014, which included the statutory audit engagement for South West Water. The Group is in compliance with the Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014.

Following the rotation of the senior statutory auditor, the Committee considers a full tender for the Pennon Group's external audit services, including the statutory audit of South West Water, subject to its annual reviews, likely in the year ending March 2024. This allows for any potential new audit firm to take up the role for the year ending March 2025. The Committee believes this approach is in the best interest of shareholders, as over this period the Pennon Group will benefit from an efficient and effective audit, while receiving fresh challenge from a new senior statutory auditor.

INTEGRATED ASSURANCE FRAMEWORK

Throughout the year South West Water had in place an effective integrated assurance framework which identifies and monitors all types of assurance to enable a full evaluation of the conclusions drawn by all auditors, inspectors and reviewers from both internal and external providers.

The framework utilises a risk-based approach to ensure an appropriate balance of varied providers of assurance dependent on the assessed risk and complexity of assurance requirements.

(i) Group independent internal audit

South West Water utilises the Pennon Group's independent Internal Audit function, to provide effective risk-based coverage over the internal control environment. The Audit Committee's interactions and engagement into internal audit, including input into the annual plan is summarised above.

(ii) Annual assurance (financial and technical audit)

Alongside the statutory external auditor, South West Water also engages a technical auditor to provide assurance over key areas of regulatory performance reporting. This assurance considers our reported performance against key regulatory outputs and measures.

(iii) Quality assurance and ISO Internal Reviews

The South West Water Audit Committee also considers the resources for carrying out internal audits and reviews in key Company specific areas and endorses and acts on findings from these reviews carried out within the Company. There is a programme of internal audits coordinated by the Risk and Compliance Department as part of the Company's ISO certifications.

South West Water has the following accreditations/certifications:

- ISO 9001: 2015 (quality management)
- ISO 14001: 2015 (environmental management)
- ISO 27001: 2013 (information security)
- ISO 17025: 2005 (laboratories and sampling)
- ISO 50001: 2011 (energy management)
- BS 18477; 2010 (inclusive service provision)

These specific areas are also subject to periodic external reviews (such as ISO external reviews).

SOUTH WEST WATER'S 2020/21 BOARD ASSURANCE STATEMENT

In July 2021, South West Water will publish its annual performance report which will detail assurance work which has been performed in areas which it has identified following consultation as significant areas for assurance, which includes annual reporting. This report will be available as part of South West Waters' – available at www.southwestwater.co.uk/report2021.

THE ENVIRONMENTAL, SOCIAL AND GOVERNANCE COMMITTEE

The role of the ESG Committee is to ensure robust scrutiny of key aspects of environmental, social and governance (ESG) performance and to oversee the Company's performance against its strategic sustainability objectives.

Over the past year we have re-focussed our ESG Strategy, establishing a capitals framework which is uniquely aligned to E, S and G aspects existing Sustainability reporting. This new approach allows clear links between the ESG targets and the impact and benefits of the six core capitals; natural, social, human, manufactured, intellectual and financial.

Alongside our re-focused ESG strategy we have updated our 2021/22 KPIs and associated targets to ensure greater alignment to our emerging capitals strategy and driving ESG assessment improvements. We have also assessed and aligned our objectives and targets against the most relevant of the United Nations Sustainable Development Goals (SDGs) and will increasingly monitor our performance using the SDGs.

The Committee's calendar of business now reflects a focus on performance in each of the capitals in turn and we look forward to reviewing progress against the Company's ambition to be the leader across the South West and the Water Industry. In particular, we're developing how our capitals approach will drive decision making.

A strong performance against our identified SDGs and our own sustainability objectives, ensures high standards of corporate responsibility for the benefit of all our stakeholders – our customers and communities, our people, suppliers and our regulators.

This annual report provides an integrated assessment to show how a responsible approach to sustainability helps us to balance the immediate and longer-term needs of society with the delivery of sustained commercial success.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE (ESG) COMMITTEE COMPOSITION AND MEETINGS

Four meetings of the South West Water Sustainability Committee were held during the year. Members of the Committee and their attendance were as follows:

Membership	Role	Attendance
Iain Evans	Chair	4/4
Gill Rider	Non-Executive Director	4/4
Claire Ighodaro ⁽¹⁾	Non-Executive Director	3/3
Neil Cooper ⁽¹⁾	Non-Executive Director	3/3
Jon Butterworth	Non-Executive Director	3/4
Lord Matthew Taylor ⁽²⁾	Non-Executive Director	1/1
Chris Loughlin ⁽²⁾	Managing Director	1/1
Susan Davy ⁽³⁾	Chief Executive Officer	3/3

⁽¹⁾Appointed to the Committee on 31 July 2020.

⁽²⁾Stepped down on 31 July 2020.

⁽³⁾Appointed to the Committee on 31 July 2020. Also attending the other Committee meeting in role as Pennon Chief Financial Officer.

COMMITTEE REMIT AND ACTIVITIES

During the year, the Committee reviewed its remit and responsibilities and agreed that oversight of health, safety and wellbeing be transferred to a new Health & Safety Committee, with membership comprising all of the Non-Executive Directors and chaired by Jon Butterworth. The Health & Safety Committee provides a 'review and challenge' function to support the Board and the Executive on all matters connected to health & Safety including the deployment of the health & safety strategy, resilience and process safety. It also reviews the extent and effectiveness of the Company's reporting of health & safety performance, as well as comparisons to external benchmarks.

At the same time, it was agreed that the name Environment, Social and Governance Committee would be a better reflection of the nature and breadth of the Committee's responsibilities.

In its new guise, the ESG Committee continues to assess performance against a range of approved targets for the Company, set as part of the business planning process. Progress is reported to the Committee throughout the year.

In addition, it provides assessment and oversight of South West Water's performance against sustainability targets that are core to the successful delivery of its K7 business plan 2020-25. This is consistent with Ofwat's requirement for independent governance of the regulated business.

The Committee ensures challenging targets are set and approved. As at 31 March 2021, South West Water achieved or is on track for 10 of the 12 targets, apart from the number of Category 2 pollution incidents and an increase in our lost time injury frequency rate (LTIFR). We continue to target significant improvements in these areas.

The ESG Committee continues to aim to ensure a transparent approach to conducting business in a responsible manner, within a business focused on delivering robust financial performance and sustainable value for shareholders and stakeholders.

The Committee reviews and approves appropriate strategies, policies, management processes, initiatives, disclosures, targets and performance of South West Water in the areas of environment and compliance, workplace policies, responsible and ethical business practice, supply chain, customer service and engagement, community benefit, and the role and value of the Company in society.

During 2020/21, the Committee has considered a wide range of matters in the course of fulfilling its duties in accordance with its terms of reference:

- The evolution of the Company's sustainability strategy, driven by a new approach to capitals
- Prior to the establishment of the Health & Safety Committee in November 2020, the Company's health and safety performance and the effectiveness of health and safety policies and procedures, including the continued roll-out of the HomeSafe programme
- Environmental leadership, climate change and carbon management
- The Company's biodiversity programme and performance
- Service quality and customer satisfaction
- The Company's approach to community relations, community benefit and investment
- The annual update on people, skills and development
- Sustainable supply chain procurement and practices
- Progress against the sustainability targets for 2020/21 and establishing an updated set of targets for 2021/22 aligned with our ESG strategy
- Sustainability reporting and disclosures for 2020 and the associated verifier's reports and recommendations
- ESG index positions and ratings for 2020
- Approval of the Sustainable Financing Framework Impact Report 2020 and allocation of funds for 2021.

REPORTING AND ASSURANCE

South West Water's sustainability performance and reporting has been audited by Jacobs (a global provider of technical, professional and scientific services, including engineering, architecture, construction, operations and maintenance) as part of its audit of performance data contained within the Annual Performance Report. Jacobs utilise water industry specialists in the audit of our non-financial data.

South West Water considers that Jacobs's method of verification – which includes testing the assumptions, methods and procedures that are followed in the development of data and auditing that data to ensure accuracy and consistency – complements the best practice insight gained through South West Water's membership of Business in the Community.

Jacobs will provide a technical auditor's report within the Annual Performance Report and Regulatory Reporting outlining its opinion and key findings (published in July and available at www.southwestwater.co.uk/report2021).

BENCHMARKING

The Pennon Group (including South West Water) is a constituent within the FTSE4Good Index, Sustainalytics, CDP Climate Change, Dow Jones Sustainability Index and a number of other leading external ESG assessments. FTSE4Good and similar leading indices are designed to facilitate investment in companies that meet globally recognised corporate responsibility standards. These leading indices assess companies on their disclosures relating to stringent environmental, social and governance criteria, and their position to capitalise on

the benefits of responsible business practice.

SOUTH WEST WATER SUSTAINABILITY REPORT

South West Water's sustainability reporting is integrated throughout the strategic report and specifically in the following sections:

- Chair's letter (pages 3 to 4)
- Business model (page 9)
- ESG strategy and performance (pages 16 to 23)
- Our Stakeholders (pages 6 to 8)
- Our people (pages 24 to 29)
- Our operations (pages 30 to 34)

Further details of our operational performance, including in respect of sustainability will be provided in our Annual Performance Report, available at www.southwestwater.co.uk/report2021, published in July.

HEALTH & SAFETY COMMITTEE

An introduction from Jon Butterworth

I believe the key to ensuring we keep employees safe and well in the workplace, is through empowering everyone to take responsibility for the health, safety and wellbeing of each other and for themselves. Simply put, it's about culture, leadership and accountability.

Establishing a new Board Committee focussed purely on Health & Safety in 2020 is an important step forward in the Company's journey as part of our HomeSafe strategy towards zero harm. We aim to be a leader for Health and Safety by 2025, and leadership from the top is critical. The Board now has dedicated time to discuss, review performance, offer support, encourage learning and meet leaders and employees from across the business.

Importantly, the Board also reviews deep dives of High Potential Incidents with a particular focus on lessons learned and in getting to the root cause, encouraging a learning mindset. We have also reviewed externally benchmarking of our performance against water peers, the results from our Engagement survey and employees' perception of health and safety and share good practice.

THE NOMINATION COMMITTEE

There has never been a more important time for responsible business to ensure outstanding leadership and stewardship and to promote diversity.

The Nomination Committee met three times during the year to fulfil the duties set out in its terms of reference.

Only the members of the Committee are entitled to attend the meetings of the Committee. Other regular invitees to the Committee during the year included the Chief Executive Officer, the Chief People Officer and the General Counsel and Company Secretary. Committee members are excluded from participating in Committee discussions where their own positions are under discussion.

Matters considered by the Committee during the year included:

- Overseeing the enactment and implementation of the Board's internal succession plan ensuring an orderly handover and transition of Board and Senior Executive appointments
- Undertaking a review of the Committee structures and review of Non-Executive committee attendance
- Approving revised terms of reference for the Committee in light of changes to the structure and review of the Company's governance framework
- Approval of an emergency succession plan for Board members, following changes made to the Board
- The annual review and approval of the policy on Diversity, Respect and Inclusion and the Company's progress on diversity, the Company position on Gender Pay, and achievement of the Parker Review target for ethnic diversity on Boards ahead of the 2021 target date
- Consideration and approval of the Board becoming a signatory of Change the Race ratio to drive improvements in Ethnic Diversity
- The key themes emerging from a review of the Executive Leadership Review and ongoing development, including a review of the succession plan and flight risk analysis.

The key appointments approved by the Nominations Committee included:

- The appointment of Gill Rider as Chair of the Board and Nomination Committee (previously Senior Independent Director and Chair of the Remuneration Committee) following Sir John Parker's decision to step down on 31 July 2020
- The appointment of Susan Davy (previously Pennon's Chief Financial Officer) as Group Chief Executive Officer, following the decision by Chris Loughlin to step down from the Board on 31 July 2020
- The appointment of Neil Cooper as the Senior Independent Director, in place of Gill Rider following her appointment as Chair
- Claire Ighodaro's appointment as chair of the Remuneration Committee, in place of Gill Rider following her appointment as Chair

It is the usual practice of the Committee to appoint an external search consultancy to assist in non-executive appointments to ensure that an extensive and robust search can be made for suitable candidates. Given the strength and depth of experience of the Board, the Committee concluded that the enactment of the internal succession plan, would best serve the interests of the Company.

No member of the Committee partook in the discussions around their own role. Further information on the Board biographies can be found on pages 65 to 67.

NOMINATION COMMITTEE COMPOSITION AND MEETINGS

Director	Role	Attendance
Gill Rider ⁽¹⁾	Chair	3/3
Neil Cooper	Non-Executive Director	3/3
Claire Ighodaro	Non-Executive Director	3/3
Iain Evans	Non-Executive Director	3/3
Jon Butterworth	Non-Executive Director	2/3

⁽¹⁾Appointed as Chair on 31 July 2020

Also in attendance were the Chief Executive Officer, the Chief People Officer and the Group General Counsel and Company Secretary.

BOARD EFFECTIVENESS REVIEW

The Board undertakes a formal and rigorous review of its performance and that of its Committees and Directors each year. This ensures that they continue to operate effectively and are identifying opportunities for improvement and best practice, as well as helping to inform future agenda items and areas of focus.

Last year's evaluation was externally facilitated with the following actions implemented:

- Appointment of a lead Non-Executive Director for Health & Safety matters
- The importance of the Board in championing Diversity
- A focus on Directors' training and development, further details of which can be found on page 76.

This year the evaluation was carried out in March 2021 via online questionnaire created internally by the Group General Counsel and Company Secretary in consultation with the Chair and respective Committee Chairs.

The questionnaire focused on the ongoing effectiveness of the Board during the year in setting the strategy, promoting the Company's culture and values, ensuring that the Company's obligations to its stakeholders were understood and met, overseeing the use of the Company's resources, managing the risks inherent in the strategy, plans and the operating environment, and ensuring that the Executive had managed all the activities of the Company well.

The outcomes of the review concluded that the Board, its Committees and individual Directors continue to demonstrate a high degree of effectiveness and that the Board had a good understanding of opportunities for growth and risks facing the business. Areas which received positive feedback included the open and co-operative nature of the relationship between the Executive and Non-Executive Directors, the enhanced focus on health & safety and ESG matters respectively, good information flows and the smooth running of remote meetings in the difficult circumstances caused by the COVID-19 pandemic.

Areas identified as meriting ongoing focus included delivering on our commitments, particularly around public value, social purpose and progressing ESG for the benefit of all stakeholders, succession planning, the Directors' training and development needs, and delivery of diversity policy objectives. All of these matters will be included in the respective forward-looking agendas.

TALENT MANAGEMENT AND SUCCESSION PLANNING

During 2020/21, a review was carried out of the capability and potential of the members of the Executive, supported by leadership advisory Heidrick and Struggles.

The Committee, supported by the Group Chief People Officer, reviews both the executive and Non-Executive leadership as part of a regular agenda. Horizon scanning externally has also become a more frequent activity, to ensure that the Board remains flexible to respond to changing priorities.

BOARD DIVERSITY POLICY

The Committee is required by the Board to review and monitor compliance with the Board's diversity policy and report on the targets, achievement against those targets and overall compliance in the annual report each year.

The Board's diversity policy confirms that the Board is committed to:

- The search for Board candidates being conducted, and appointments made, on merit, against objective criteria whilst promoting diversity of gender, social and ethnic backgrounds in this context, the Board with endeavour to achieve and maintain:
 - A minimum of 33% female representation on the Board
 - A minimum of 33% female representation on the Company's senior management team.

Satisfying itself that plans are in place for orderly succession of appointments to the Board and to senior management to maintain an appropriate balance of skills and experience within the Company and on the Board and to ensure progressive refreshing of the Board.

There has never been a more important time for responsible businesses to promote the widest level of diversity in the boardroom and beyond and the Board takes its leadership of this important topic very seriously. The Committee is pleased to report that as at 31 March 2020, 57.1% of the Board's Directors were women, as disclosed on pages 26 and 72 and that the Company's wider leadership team stands at 33% female representation.

Both our Chair and our Chief Executive Officer are members of the 30% Club, a UK campaign that supports the goal of women holding 30% of board seats and promotes initiatives to expand the female talent pipeline at all levels. We also have active membership of 'Women in Water', which promotes female talent across the industry by encouraging networking and the progression of women into more senior roles.

During the year, South West Water was an active proponent of ethnic diversity. In November 2020, we were the first water company to sign up to the Change the Race Ratio, helping society to advance ethnic diversity at all levels and from all backgrounds.

THE REMUNERATION COMMITTEE

The Committee met four times during the year to fulfil the duties set out in its terms of reference. In particular, the Committee is responsible for:

- Ensuring remuneration is aligned with and supports the Company's strategy, reflects our values and optimises performance
- Maintaining and, in every third year, reviewing the remuneration policy and considering any changes necessary to ensure it remains appropriate and fulfils its purpose of attracting and retaining high-calibre people who are able to contribute to the success of the Company
- Advising the Board on the framework of executive remuneration for the Company
- Determining the remuneration and terms of engagement of the Chair, the Executive Directors and senior executives of the Company
- Approving the design and determining targets for any performance-related pay schemes, and approving the payments made, having applied discretion and consideration of the wider circumstances
- Reviewing the wider workforce remuneration, taking these into account when setting the remuneration policy for Executive Directors.

THE COMMITTEE'S ACTIVITIES DURING THE FINANCIAL YEAR

The Committee engaged in the following activities during the year:

- Monitored external developments in remuneration
- Ensured executive remuneration was aligned to PR19 (2020-25) deliverables
- Considered the remuneration arrangements for the outgoing Group CEO and SWW Managing Director
- Considered the remuneration arrangements in respect of the appointment of the new Chair and Chief Executive Officer
- Completed a review of the structure of the fees for the Non-Executive Directors
- Reviewed drafts of the Directors' annual remuneration report and recommended it to the Board for approval for inclusion in the annual report
- Determined performance targets in respect of the Annual Incentive Bonus Plan for 2021/22
- Determined bonuses and deferred bonus awards pursuant to the Company's Annual Incentive Bonus Plan in respect of the year 2020/21
- Approved updates to the rules for the Long-Term Incentive Plan (LTIP), the Annual Incentive Bonus Plan and the all-employee Sharesave scheme to incorporate best practice
- Approving the long-term incentive plan (LTIP) awards for the year
- Reviewed the Group's gender pay gap report
- Approved the release of the 2017 deferred bonus share awards and reviewing the outcome of the 2017 LTIP awards
- Reviewed the Committee's terms of reference and undertook a review of the Committee's performance in the year.

THE COMMITTEE'S FOCUS FOR 2021/22

- Ensure that targets are stretching, so that they act to retain, motivate and incentivise the Executive to deliver the Company's strategic goals and PR19 regulatory commitments (including those relating to

public value, social purpose and ESG), live the Company's values creating long-term value for shareholders

- Monitor on an ongoing basis the alignment of Executive pay and benefits with our strategic direction to ensure these support the long-term success of the Company and promote its values
- Review wider workforce remuneration, taking this into account when setting the remuneration policy for Executive Directors
- Monitoring of the updated remuneration policy to ensure that it is delivering as intended and continues to meet best practice.

REMUNERATION COMMITTEE COMPOSITION AND MEETINGS

In accordance with the Code, all of the Committee members are independent Non-Executive Directors. The Chief Executive Officer also attends meetings when invited except for such part of a meeting when matters concerning her own remuneration are to be discussed.

There were four meetings of the South West Water Remuneration Committee during the year. Members of the Committee and their attendance were as follows:

The Committee is advised by Deloitte, an independent remuneration consultant, to ensure remuneration is determined impartially.

Membership	Position	Attendance
Claire Ighodaro ⁽¹⁾	Chair	3/3
Gill Rider ⁽²⁾		4/4
Neil Cooper	Non-Executive Director	4/4
Iain Evans	Non-Executive Director	4/4
Jon Butterworth ⁽³⁾	Non-Executive Director	3/3
Martin Hagen ⁽⁴⁾	Non-Executive Director	1/1

⁽¹⁾Appointed on 8 July 2020

⁽²⁾Gill Rider stood down as a member of the Remuneration Committee upon her appointment as Chair of the Board on 31 July 2020. She has attended all Remuneration Committee meetings since that date as an invitee. Prior to the announcement on 8 July of her appointment as Chair of the Board, Gill Rider was chair of the Remuneration Committee.

⁽³⁾Appointed to the Committee on 31 July 2020.

⁽⁴⁾Stood down from Committee 31 July 2020

REMUNERATION APPROACH FOR WIDER EMPLOYEES

Consistent with best practice, the Remuneration Committee spends considerable time on matters relating to remuneration arrangements in the wider organisation. Details of remuneration for the wider employee base provide important context when making decisions regarding remuneration for the Executive Directors as well as ensuring that consistent approaches are being adopted across the organisation.

To provide greater transparency of remuneration for colleagues across the Company we have introduced additional information. The Remuneration Committee is kept informed of wider workforce remuneration through the Pennon Group pay dashboard, of which South West Water is part of, which is reviewed twice a year.

Our well-established People Strategy across the Company is centred around talented people doing great things for customers and each other, and creating the best place to work. Responsible and trusted businesses today have a duty to make a positive societal contribution – whether that’s through promoting social mobility, addressing racial and gender inequality, or in providing secure and meaningful employment where all employees are paid fairly for the work they do.

During 2020, a specific Reward framework was created to complement the People Strategy with three aims:

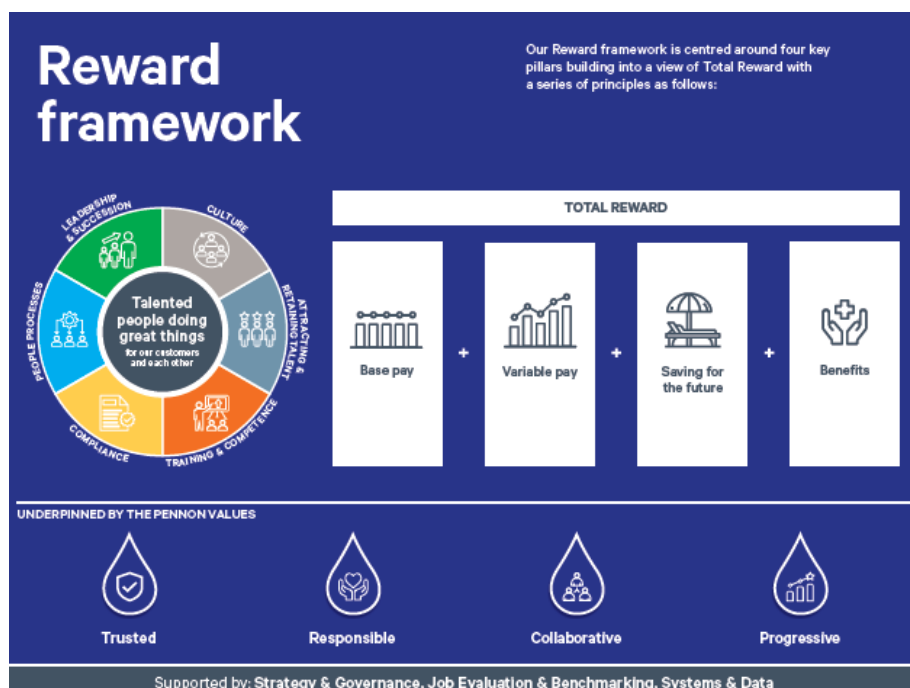
- To communicate to stakeholders our approach to rewarding and recognising employees and their contribution
- To ensure that reward decisions support business delivery and promote long term wealth creation, in line with our People Strategy and values
- To deliver a fair reward package to engage and motivate employees to want to perform at their best.

A critical aspect of the design work was in understanding employees’ views of reward, the benefits most valued and what aspects could be improved. Listening sessions and focus groups were held during this process as well as incorporating themes from the engagement survey.

The Reward framework is centred around four key pillars which build into a Total Reward proposition, ensuring a mix for employees at every stage of their career lifecycle.

The framework was reviewed and endorsed by the People Committee and Remuneration Committee and the success of the strategy measured through the engagement survey and employees’ feedback. This is regularly reviewed and shared with the Remuneration Committee.

As part of creating the strategy, a new online cloud-based Reward Hub, enabling employees to access their reward and benefit options virtually, has been implemented. The Hub also provides the functionality of Total Reward statements, paving the way for the Group to move towards an even more flexible benefits approach. The Reward Hub is an invaluable tool for directly communicating reward elements, helping employees understand and maximise their package.



DIRECTORS' REMUNERATION REPORT

PRINCIPLES USED TO DEVELOP REMUNERATION POLICY

Clarity and simplicity	The Committee is committed to providing open and transparent disclosures with regards to executive remuneration arrangements
Risk	Annual bonus deferral, the LTIP holding period and shareholding requirements ensure that Executive Directors are exposed to the long-term performance of the Company
Predictability	For each component of pay, the policy outlines the maximum opportunity levels for Executive Directors. Actual incentive outcomes will vary depending on the level performance achieved against specific measures
Proportionality	Our remuneration framework does not reward poor performance. Payment of the annual bonus and LTIP are subject to the achievement of stretching performance targets
Alignment to culture	The metrics used to measure both short and long-term performance at South West Water are closely aligned to our business strategy. Delivery of awards in shares, in our parent company Pennon Group plc, over three to five years and shareholding guidelines ensure focus on sustainable performance

LINK TO CUSTOMERS

Pay linked to underlying performance	<ul style="list-style-type: none"> ➤ Significant portion of executive remuneration linked to performance of the business
Performance pay – appropriately aligned with customer interests	<ul style="list-style-type: none"> ➤ Annual bonus includes customer and operational measures linked to metrics assessed by our regulator, customers, communities and wider stakeholders
Bonus and long term incentives – substantial link to stretching performance delivery for customers	<ul style="list-style-type: none"> ➤ Stretching targets – motivate management to deliver sustainable performance ➤ Safeguard mechanisms in place to ensure outcomes reflect underlying performance

ANNUAL STATEMENT FROM THE CHAIR OF THE REMUNERATION COMMITTEE

Operationally, we have continued to maintain our focus on and commitment to supporting the environment, customers and colleagues. Our New Deal for the K7 period is seeing us deliver sector leading returns, driving efficiency through innovation and sustainability whilst delivering more of what matters for our communities, with around 80% of ODIs either on track or ahead of target. Year on year we are able to report on improving water quality, reduced customer supply interruptions and a more resilient service.

We have prioritised environmental leadership with our largest environmental programme in 15 years, and a commitment to reduce pollutions by 80% by 2025 alongside our pledge to become Net Zero by 2030.

During the year we also launched our pioneering WaterShare+ share scheme, a key feature of South West Water's 'New Deal' business plan for 2020-25, marking a new relationship between the Company and its customers. This saw 1 in 16 households become shareholders, in our parent Company Pennon, with the remainder receiving their share of South West Water's £20 million of outperformance as a reduction in their bill. We have also helped circa 67,000 customers with our affordability toolkit, representing an 11% increase compared to last year.

The Company has continued to support colleagues during the pandemic without utilising any Government support. We were pleased to announce improvements in benefits arrangements for all employees, which included enhanced income protection terms. Within the Company, we have increased employment levels extending our graduate, apprentice and Kickstart placements, in addition to ongoing recruitment. We also undertook a review of Reward which applies to our wider employee base. Further details of our approach to pay are set out in the main body of the report. We were proud to have been named Britain's Most Admired utility and officially a Great Place to Work as we continue to support our colleagues through COVID-19 and ensure South West Water is a diverse and inclusive place to thrive.

EXECUTIVE CHANGES

During the year the Committee considered the remuneration of the incoming Chief Executive Officer. The Committee sought to adopt a measured approach when setting the salary level. In future years, the Committee will keep arrangements for Directors under review to ensure they suitable reflect their role and experience.

Chris Loughlin stepped down from the post of South West Water Managing Director and Chief Executive Officer with effect from 31 July 2020. Details of his departure terms are provided in the Pennon Annual Report on page 122.

INCENTIVE OUTCOMES

The performance of the Executive Directors has been carefully considered, noting the robust performance despite the pandemic. The progress against financial and operational objectives is reflected in the outcomes against the bonus scorecard. Further details are set out on pages 110 to 121.

Overall, the annual bonus earned in respect of the year is 78.1% of salary for the Chief Executive Officer and 42.1% for the Finance Director. The Committee is satisfied that the bonus outcomes are fully supported by

performance in the year. Careful consideration has been given to the wider context in confirming the level of bonus awarded of which more can be read on page 112.

Half of the bonus earned is deferred into shares which affirms Executives Directors' commitment to creating a long-term, sustainable business.

Share awards granted under the long-term incentive plan (LTIP) in 2018 will be eligible for vesting in 2021. This award was based on Pennon Group metrics: EPS growth (40%), dividend growth (40%) and return on capital employed (20%), as well as an 'underpin' evaluation, including consideration of safety, ESG factors and financial performance.

Awards are expected to vest at 89.9% of maximum, as shown on page 113. This is reflective of financial and operating performance over the performance period. Vested shares for Executive Directors will remain subject to an additional two-year holding period.

POLICY REVIEW

Our current remuneration policy was approved in 2020. We are not proposing to make any changes in the coming year, with incentive levels continuing at the level set out in the remuneration policy.

For 2021/22 annual bonus targets have been refined to incorporate the emergence of ESG goals, ensure alignment with the UK water sector.

Further detail on pay arrangements is provided in the main body of the remuneration report.

ANNUAL REPORT ON REMUNERATION

SUMMARY OF DIRECTORS' REMUNERATION POLICY AND IMPLEMENTATION IN 2021/22

The current remuneration policy was established in 2020. A summary of the policy is set out below alongside detail on how we intend to implement the policy in 2021/22.

Element	Operation	Implementation in 2021/22
Base Salary		
Set at a competitive level to attract and retain high calibre people to meet the Company's strategic objectives in an increasingly complex business environment.	Salaries are generally reviewed annually and any changes are normally effective from 1 April each year. In normal circumstances, salary increases will not be materially different to general employee pay increases.	The salary for the Chief Executive Officer was set on appointment in 2020 and no increases were made in 2021/22. The Finance Director received an 1% increase for 2021/22. Finance Director – £170,650 Chief Executive Officer – £237,500 (50% of Pennon Group recharge)
Benefits		
Benefits provided are consistent with the market and level of seniority to aid retention of key skills to assist in meeting strategic objectives.	Benefits currently include the provision of a company vehicle, fuel, health insurance and life assurance. Other benefits may be provided if the Committee considers it appropriate.	Income protection was introduced for all employees during the year, including Executive Directors.
Pension-related benefits		
Provides funding for retirement and aids retention of key skills to assist in meeting the Company's strategic objectives.	The maximum annual pension contribution or cash allowance is in line with the contribution available to the wider population.	The Chief Executive Officer receives benefits of 10% of salary, which is aligned with the maximum rate available to the wider workforce. The Finance Director receives benefits of 15% of salary.
Annual bonus		
Incentivises the achievement of key performance objectives aligned to the strategy of the Company	The maximum bonus potential for the Finance Director is 75% of base salary and for Chief Executive Officer 125% of base salary. A portion of any bonus is deferred into shares in the Company which are normally released after three years. Normally 50% is deferred. Malus and clawback provisions apply.	Maximum opportunity of 125% of salary for the Chief Executive Officer and 75% for the Finance Director. Deferral of 50% of any bonus into shares for three years. The annual bonus for 2021/22 will continue to be based on a combination of financial, operational and strategic objectives. The bonus structure for the Chief Executive Officer for 2021/22 reflects: <ul style="list-style-type: none"> • 50% financial metrics • 50% customer, operational and ESG metrics

		<p>The bonus structure for the Finance Director for 2021/22 reflects:</p> <p>70% of allowed bonus is linked to:</p> <ul style="list-style-type: none"> • 50% customer and operational metrics ⁽¹⁾ • 20% ESG metrics <p>30% linked to financial delivery targets that support financial sustainability:</p> <ul style="list-style-type: none"> • 20% profit before tax • 10% net debt/gearing <p>Consistent with prior years, a portion of the bonus will be linked to measurable goals that are key to meeting the needs of our customers, our regulator and wider stakeholders. These include measures relating to customer service scores, bathing water failures, leakage and wastewater pollution incidents, interruptions to supply and asset reliability.</p> <p>The element previously based on personal objectives has been removed for 2021/22 and has been replaced with an element linked to specific ESG goals. This will include targets relating to our carbon emissions reduction goals, the working environment for our employees and diversity.</p> <p>The detail of bonus targets are closely aligned to the strategy and are therefore considered to be commercially sensitive. Disclosure of targets will be provided on a retrospective basis in next year's Remuneration Report.</p> <p>Further information for the Chief Executive Officer are disclosed in the Pennon Annual Report of pages 118 and 119.</p>
Long-Term Incentive Plan (LTIP)		
<p>Provides alignment to the achievement of the Company's strategic objectives and the delivery of sustainable long-term value.</p>	<p>Annual grant of conditional shares (or equivalent). Share awards vest subject to the achievement of specific performance conditions measured over no less than three years. In addition, a two-year holding period will apply in respect of any shares which vest at the end of the three-year performance period.</p> <p>An underpin applies which allows the Committee to reduce or withhold vesting if the Committee is not satisfied with the underlying operational and economic performance of the Company. Malus and clawback provisions apply.</p>	<p>Maximum award of 150% of salary for Chief Executive Officer and 100% for Finance Director.</p> <p>The target setting process for the 2021 LTIP grants for the Chief Executive Officer has been delayed in light of the ongoing Pennon strategic review. The Committee is keen to ensure that the targets for the 2021 award reflect the future Pennon Group structure and align with the strategic priorities for the three-year period ending 31 March 2024.</p> <p>Once finalised, the performance measures and targets for the 2021 LTIP awards will be published on the Pennon website.</p> <p>The 2021 LTIP award for the Finance Director will be based on:</p>

		<ul style="list-style-type: none"> • 1/3 Return on Regulated Equity (RoRE) – measure based on outperforming the Final Determination (FD) year on year metric • 1/3 sustainable dividend measures (Pennon) • 1/3 C-MeX (median moving to upper quartile)
<p>Discretion In line with the 2018 Corporate Governance Code, the Remuneration Committee has ensured that it will maintain the ability to override the formulaic outcomes for future awards under the annual bonus and LTIP where the outcomes are not considered by the Committee to be appropriate (e.g. unreflective of underlying performance). The Committee will disclose the use of any such discretion.</p>		
<p>Shareholding requirements</p>		
Create alignment between executives and shareholder and promote long-term stewardship	During the course of their tenure, Executive Directors are expected to build up a shareholding equivalent to a percentage of salary.	Shareholding guideline of 200% of salary for the Chief Executive Officer and 100% of salary for the Finance Director.
<p>All-employees share plans</p>		
Align the interests of all employees with Company share performance.	Executive Directors may participate in HMRC approved all-employee plans on the same basis as employees. The maximum is as prescribed under the relevant HMRC legislation governing the plans.	No changes.
<p>Non-Executive Director fee policy</p>		
Set at a market level to attract Non-Executive Directors who have appropriate experience and skills to assist in determining the Company's strategy.	<p>Non-Executive Directors normally receive a basic fee and an additional fee for any specific Board responsibility such as chair of a Committee or occupying the role of Senior Independent Director.</p> <p>Expenses incurred in the performance of non-executive duties for the Company may be reimbursed or paid for directly by the Company (including any tax due on the expenses). The Chair's benefits include the provision of a driver and vehicle, when appropriate for the efficient carrying out of her duties</p> <p>The Non-Executive Directors fees are set by Pennon Group plc and 50% of these fees are recharged to South West Water through Group recharges. The fee structure was amended in 2020.</p>	<p>2021/22 fee policy will remain unchanged and the below outlines 50% of fees which are recharged from Pennon Group:</p> <p>Chair fee £112,500 Basic Non-Executive fee £30,275</p> <p>Additional fees Senior Independent Director £5,000 Chair of Audit Committee £7,500 Chair of Remuneration Committee £6,500 Chair of ESG Committee⁽²⁾ £6,500 Chair of Health and Safety Committee⁽³⁾ £2,500</p>

(1) This element will only pay out if at least 90% of the basket of other ODIs is met

(2) The ESG Committee used to be called the Sustainability Committee

(3) The Health & Safety Committee was introduced in 2020. The Committee typically holds a minimum of two meetings per annum.

REMUNERATION APPROACH FOR WIDER EMPLOYEES

Consistent with best practice, the Remuneration Committee spends considerable time on matters relating to remuneration arrangements across the wider workforce. This provides important context when making decisions regarding remuneration for the Executive Directors as well as ensuring that consistent approaches are being adopted across the organisation.

To provide greater transparency of remuneration for the wider workforce we have provided expanded disclosure. The Remuneration Committee is kept informed of wider workforce remuneration through the Pennon Group Pay Dashboard, which incorporates South West Water and is reviewed twice a year. This has evolved during 2020/21 to provide oversight of how the Reward Strategy is being implemented and more insight to colleague remuneration.

Our well-established People Strategy across the Group is centred around talented people doing great things for customers and each other, and creating the best place to work. Responsible and trusted businesses today have a duty to make a positive societal contribution – whether that's through promoting social mobility, addressing racial and gender inequality, or in providing secure and meaningful employment where all employees are paid fairly for the work they do.

During 2020 a specific Reward Strategy was created for the Company to complement the people strategy. The Reward Strategy had three aims:

- To communicate to stakeholders our approach to rewarding and recognising employees and their contribution
- To ensure that reward decisions support business delivery and promote long term wealth creation, in line with our people strategy and values
- To deliver a fair reward package to engage and motivate employees to want to perform at their best.

A critical aspect of the design work was in understanding employee's view of reward, the benefits most valued and what aspects could be improved. Listening sessions and focus groups were held during this process as well as incorporating themes from the engagement survey.

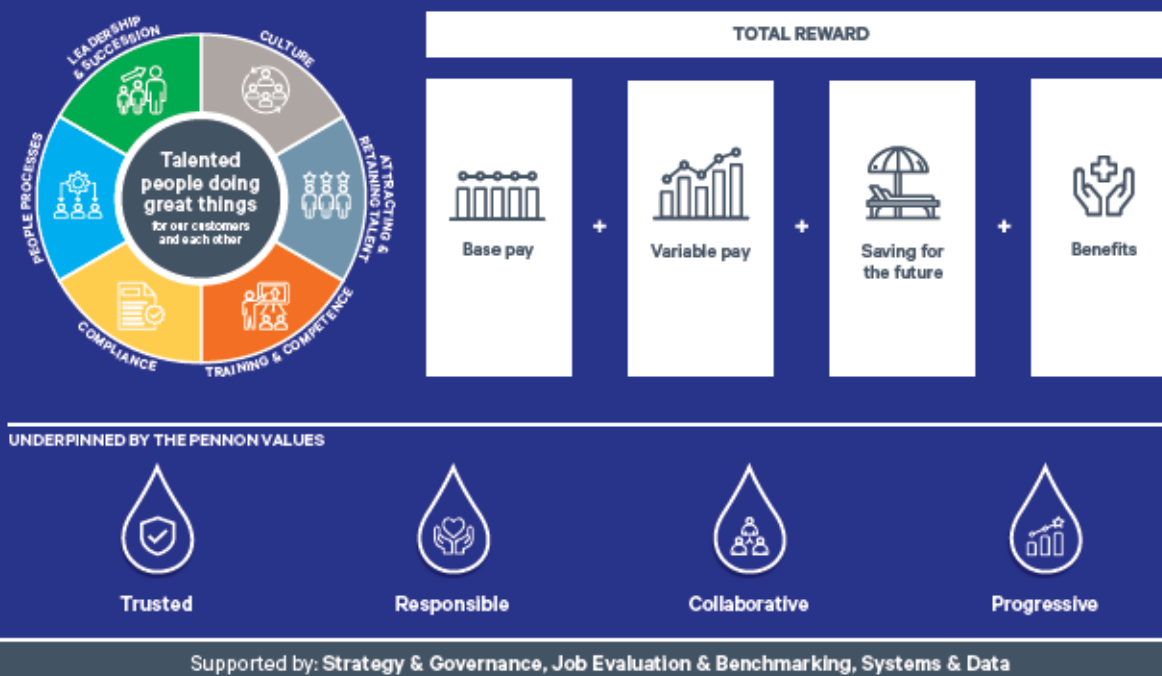
The Reward framework is centred around four key pillars which build into a Total Reward proposition, ensuring a mix for employees at every stage of their career lifecycle.

The framework was reviewed and endorsed by the People Committee and Remuneration Committee and the success of the strategy measured through the engagement survey and colleagues' feedback. This is regularly reviewed and shared with the Remuneration Committee .

As part of creating the strategy, a new online cloud-based Reward Hub enabling employees to access their reward and benefit options virtually, has also been implemented. The Hub also provides the functionality of total reward statements, paving the way for the Company to move towards an even more flexible benefits approach. The Reward Hub is also an invaluable tool for directly communicating reward elements, helping employees understand and maximise their package.

Reward framework

Our Reward framework is centred around four key pillars building into a view of Total Reward with a series of principles as follows:



Pillar	Progress
Base pay	<p>Importantly, the Pennon Group (including South West Water) has formalised its approach to adopting the Living Wage Foundation standards by becoming an accredited employer in April 2021.</p> <p>The Company's overarching principles for basic pay are that it should:</p> <ul style="list-style-type: none"> • Reflect the market and region in which the role operates • Be competitive to support attraction and retention • Be fair, meeting all legislative requirements • Be reviewed annually – we engage with employee Forums and Trade Unions as appropriate <p>The percentage change in salary for Executive Directors in 2021 was 0% compared with general increases of 1% across the Group.</p>
Variable pay	<p>The Company operates a number of variable pay schemes and all employees and temporary workers are eligible to participate. Throughout the main bonus schemes, there is strong correlation in the targets, to align the whole organisation on customer, quality and service.</p> <p>All employees across the Pennon Group (including South West Water) are entitled to participate in annual bonus arrangements. The maximum bonus levels are based on seniority and level of responsibility.</p> <p>In January 2021, we made an exceptional award of £500 to all employees, to recognise the challenges of the COVID-19 pandemic and our colleagues' dedication and fortitude in maintaining essential services to customers.</p> <p>Our Company bonus arrangements for colleagues have a strong focus on customer service. We are revising these for 2021/22 providing colleagues with an increased bonus opportunity of 5% of basic salary.</p>

<p>Saving for the future</p>	<p><i>Modernisation of our pension arrangements</i></p> <p>In 2020 the Pennon Group (including South West Water) consulted with employees on modernising the pension arrangements. The aim of this consultation was:</p> <ul style="list-style-type: none"> • To create a sustainable pension plan for all employees for the future, balancing the cost to employer and employee • To provide greater flexibility for employees to access their pension savings, following the introduction of pensions freedom • Increase the benefit levels within the Defined Contribution (DC) arrangements and reduce scheme administration charges. <p>The proposed changes included increasing the level of employer contributions, providing greater flexibility for employees to choose the most appropriate employee contribution for them, as well being able to make the most of pension freedoms.</p> <p>An extensive consultation programme was managed through Director led, face to face presentations, individual one to ones with pension advisors and dialogue with union representatives and pension trustees. Directors listened closely to the feedback and the new scheme was introduced in July 2020.</p> <p>Importantly these changes have lifted the lowest pension tier to a matching level of twice employee contribution. All tiers have had an increase, with a maximum 10% contribution from the employer.</p> <p>As part of our Saving for the future, all employees are able to participate in HMRC approved Pennon Group Sharesave and Share Incentive Plan, with a strong emphasis on employee buy-in and ownership.</p>
<p>Benefits</p>	<p>The fourth pillar of our framework covers the benefits available to employees. This year, the Company has carefully considered the value individuals place on financial well-being during this difficult year and have implemented the following changes as part of our aspiration to become the best place to work:</p> <ul style="list-style-type: none"> • We have extended our Employee Assistance Programme to immediate family members of our colleagues during the pandemic, providing independent, confidential support • We increased our life assurance plan so that beneficiaries would receive 6x salary • We launched an additional income protection scheme providing greater financial security during long-term sickness absence, for up to three years in addition to the first six months of contractual sick pay. • We are launching our Simply Recognise online tool to allow managers and colleagues to provide positive feedback and thanks to their teams and peers.

In accordance with the 2018 UK Corporate Governance Code, the Committee has also reviewed the level of information provided on pay matters in the wider organisation. Key activity in this regard included:

<p>Pennon Group pay dashboard</p>	<ul style="list-style-type: none"> • The Pennon Group (incorporating South West Water) has established a pay dashboard to help support the Committee in reviewing workforce remuneration and related policies and this has been developed to provide greater insight for 2021 • The dashboard provided an overview of pay arrangements across the business and provides key statistics on pay in different areas of the business and progress on our planned framework implementation • The dashboard covers information on workforce demographics, employee engagement, gender pay, pay ratios, pension and benefits and incentive outcomes in different areas of the business • The Committee intends to keep the content of the dashboard under review to ensure that it continues to provide suitable information for the Committee.
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GENDER PAY GAP

South West Water's Gender Pay Gap has seen an improvement at 4.92% and significantly below the national

average. The Company recognises the need to develop greater gender alignment in middle manager and senior positions and is seeing strong progress in this area. We are also an active supporter of The Women in Water Initiative.

Employee Engagement

Across South West Water we endorse the principle of strengthening opportunities for employees to engage in two-way dialogue at all levels. The South West Water Employee Engagement Forum has become a well-established forum who meet regularly to create a two-way communication between senior managers of the Group and employees and this year has been chaired by the Pennon Group and South West Water Chief Executive Officer.

Over the course of the year, we have evolved our Big Chat to become Your Big Chat, moving from a conference call facility to video enabled enabling all employees access to the Executive and creating opportunities to ask questions and suggest topics that employees would like to hear more about. The frequency was also increased to weekly to ensure regular and timely updates are provided to employees. We continued to receive positive feedback from employees who welcome the opportunity to hear from the Directors and ask them questions on key business matters.

We have been keen to ensure we are able to measure the progress made in this area and were pleased that we achieved our highest ever participation rate of 82% in our annual engagement survey and have officially passed the threshold to become accredited as a Great Place to Work with our Trust Index[©] score increasing to 66%. This is significantly higher than the national average of 53%.

We have welcomed the feedback that has been provided through these routes and employees' openness in participating in these activities.

South West Water Ltd.'s employee participation rate for the 2020 survey was 82%. Survey results included a +11% improvement on our 2019 survey in employees who support the view that we have special and unique benefits, in addition to +10% improvement in rating our overall reward category.

Looking ahead

We plan to develop our employee incentive scheme with increased bonus opportunity retaining our strong alignment to customer service. For 2021/22 we will continue to review and refine our approach to reward, continuing our development of our online Reward Hub with the roll out of Total Reward Statements in the summer and enhancing the Simply Recognise platform functionality.

SINGLE TOTAL FIGURE OF REMUNERATION TABLES (AUDITED INFORMATION)

	Base salary /fees (£000)		Benefits ⁽³⁾ (including sharesave) (£000)		Annual bonus (cash bonus and deferred shares) (£000)		Long-term incentive plan ⁽¹¹⁾ (£000)		Pension ⁽¹²⁾ (£000)		Total remuneration (£000)	
	2020/21	2019/20	2020/21	2019/20	2020/21	2019/20	2020/21	2019/20	2020/21	2019/20	2020/21	2019/20
Executive Directors												
Louise Rowe ⁽¹⁾	169	166	18	18	53	89	156	161	26	25	422	459
Susan Davy ⁽²⁾	228	206	15	15	219	162	361	373	40	59	863	815
Chris Loughlin ⁽⁴⁾	91	269	5	19	72	210	369	489	28	81	565	1,068
Non-Executive Directors												
Sir John Parker, Chair ⁽⁵⁾	47	135	-	-	-	-	-	-	-	-	47	135
Gill Rider, Chair ⁽⁶⁾	88	39	-	-	-	-	-	-	-	-	88	39
Neil Cooper, Senior Independent Director ⁽⁷⁾⁽⁹⁾	40	35	-	-	-	-	-	-	-	-	40	35
Iain Evans ⁽⁹⁾	37	-	-	-	-	-	-	-	-	-	37	-
Claire Ighodaro ⁽⁸⁾⁽⁹⁾	34	-	-	-	-	-	-	-	-	-	34	-
Jon Butterworth ⁽⁹⁾	39	57	-	-	-	-	-	-	-	-	39	57
Martin Hagen ⁽¹⁰⁾	19	57	-	-	-	-	-	-	-	-	19	57
Lord Matthew Taylor ⁽¹⁰⁾	21	61	-	-	-	-	-	-	-	-	21	61

- (1) In 2019/20, the Finance Director received a discretionary bonus for services to the Pennon Group during the year relating to the Strategic Review of 30% of salary. The Committee is satisfied that services provided did not reduce the effectiveness of the Director's provision of services to the Company
- (2) Susan Davy was appointed as Chief Executive Officer of Pennon Group plc and South West Water as of 31 July 2020. This reflects 50% of her remuneration, which is rechargeable to SWW through Group recharges. 50% of her 2019/20 remuneration has been included as a comparative based on her role as Pennon Group Chief Financial Officer. The full single total figure of remuneration tables are shown on page 117 of the Pennon Group plc Annual Report and Accounts 2021.
- (3) Benefits comprise a car allowance, fuel allowance and medical insurance
- (4) Chris Loughlin served as Managing Director of South West Water until he stepped down on 31 July 2020. The disclosure above reflects 50% of full remuneration which is rechargeable to South West Water through group recharges. The full single total figure of remuneration tables are shown on page 117 of the Pennon Group plc Annual Report and Accounts 2021
- (5) Sir John Parker stepped down as Chair on 31 July 2020
- (6) Gill Rider was appointed as Chair on 31 July 2020
- (7) Neil Cooper became Senior Independent Director with effect from 31 July 2020, in addition to his role of Chair of the Audit Committee
- (8) Claire Ighodaro became Remuneration Chair with effect from 31 July 2020
- (9) These directors are also Directors of Pennon Group plc. The disclosures above reflect 50% of their full remuneration which is rechargeable to South West Water through group recharges. The full single total figure of remuneration tables are shown on page 121 of the Pennon Group plc Annual Report and Accounts 2021
- (10) Left the Board on 31 July 2020
- (11) For 2020/21, the 2018/19 LTIP has been valued based on the average Pennon share price during the 3 month period to March 2021 of 946.1p and a vesting outcome of 89.9%, as referred to on page 113 together with an estimate of the accrued dividends payable on the vesting shares. Of the vested amount, 16.49% relates to share price appreciation over the performance period. The 2019/20 LTIP value for 2017/18 reflects the share price at the date of vesting of 1,008.5p, a vesting outcome of 86.6%. The Committee did not exercise any discretion in relation to share price changes. Both LTIP awards are subject to a two-year holding period.
- (12) See page 113 for further information.

NOTES TO THE SINGLE FIGURE TABLE

FIXED PAY

During 2020/21, Susan Davy was appointed as Chief Executive Officer with effect from 1 August 2020. On appointment Susan's salary was set at £237,500.

The Remuneration Committee recognises the market positioning against FTSE peers and intends to keep salary levels for both Executive Directors under review in future years, to ensure that they suitably reflect both development and experience in the role and the evolving size and nature of the Group's operations.

Retirement benefits for the Chief Executive Officer were set at 10% of salary on appointment to her new role. This is aligned to the rate of the wider workforce. Previously, Susan received an overall pension benefit of 25% of salary. Further detail on pension arrangements is set out in the Pennon Group Annual report on page 120. The Finance Director continues to receive 15% of salary.

ANNUAL BONUS OUTTURN FOR 2020/21

The performance targets set and the performance achieved in respect of the annual bonus for 2020/21 is set out below. The Chief Executive Officer's performance can be seen in the Pennon Group Annual report on page 119.

Louise Rowe

For 2020/21, the Finance Director participated in the annual bonus plan which was based on a combination of financial, customer and operational objectives.

In line with the Committee's policy, 50% of any bonus is payable in shares, the release of which is deferred for a three-year restricted period. The performance targets set and performance achieved have been set out below:

South West Water Financial Measures

Financial	Target	Actual	Range	Outcome	Bonus %
PBT	£158.3m	£164.6m	-2% - + 5%	4%	88.2%
Net Debt	£2,200.9m	£2,252.4m	-2% - + 5%	-2.3%	Not achieved
New Deal (Watershare+)				Achieved	Achieved in Full

SWW Customer and Operational Measures

	Target	Actual	Achieved	Bonus outturn
Bathing Waters	0	4	Yes	33.3%
Wastewater pollutions	24.51	130.87	No	
Internal sewer flooding	1.68	1.34	Yes	
EPA	3*	2*	No	
CMeX	Median	Below median	No	
CRI (Water quality)	2	2.06	No	
Supply interruptions	06:30	05:38	Yes	
Water pollutions	0	10	No	
Leakage	120.5	126.8	No	

Susan Davy is Chief Executive Officer of South West Water and Pennon Group plc. Her remuneration is based on the metrics above relating to South West Water Limited as well as additional metrics relating to the performance of other Pennon Group companies in her capacity as Chief Executive Officer of Pennon Group.

Details of her performance and remuneration can be found on pages 117 to 120 of the Pennon Group annual report 2021.

Summary of bonus outcome

	Weighting	Bonus outturn
		Finance Director
South West Water financial measure	20%	8.8%
South West Water service measures	70%	23.3%
New Deal	10%	10%
Total outturn	100%	42.1%

Malus and clawback provisions apply in relation to the bonus awards in respect of the year

LONG-TERM INCENTIVE OUTTURN FOR 2020/21

The awards in the single figure table relate to the 2018/19 share awards granted on 2 July 2018, which are due to vest on 1 July 2021. These share awards were subject to Pennon performance targets previously set as relating to Earnings per Share, a sustainable dividend measure and Return on Capital Employed.

In light of the changes to the Pennon Group, the Remuneration Committee considered the impact of the transaction on the performance criteria applicable to this award. The Committee recognised that the basis of assessment would need to vary to reflect the nature of the Pennon Group prior to and after the transaction. The performance period was therefore split, with the first two years based on the previous Pennon Group structure and the final year based on new Pennon Group structure.

The Remuneration Committee concluded that the sustainable dividends and Return on Capital Employed targets could be largely maintained, with consistent targets applied across the full performance period. However, the EPS targets needed to be adjusted to reflect the shift to a water only business. To simplify the assessment, the underlying EPS growth targets were converted into absolute EPS values, with the period following the sale of Viridor based on targets which reflected the new structure of the Group and the regulated nature of the business. While adjustments of this nature are naturally complex, the Remuneration Committee is satisfied that the approach adopted is consistent with the nature of the targets that were originally set.

The 2018/19 share awards were subject to the satisfaction of EPS growth, a sustainable dividend measure and return on capital employed (RoCE) performance conditions. These conditions were set at the time that the awards were granted.

		Threshold (25% of maximum vests) ⁽²⁾	Maximum (100% of maximum vests)	Achievement ⁽³⁾	Vesting outcome (% of max)
EPS growth (40% of award)	Combined Group (Period to FY20)	57.2p	61.6p	61.7p	100%
	Continuing Group (Period to FY21)	29.6p	30.2p	32.1p	
Sustainable dividend measure (dividend growth and dividend cover) (40% of award)	Combined Group (Period to FY20)	2.6x	3.6x	3.3x	84.9%
	Continuing Group (Period to FY21)			3.7x	
RoCE (average) ⁽¹⁾ (20% of award)	Combined Group (Period to FY20)	8%	10%	9.7%	79.6%
	Continuing Group (Period to FY21)			8.1%	
Total					89.9%

⁽¹⁾ Average of opening and closing capital employed

⁽²⁾ For below threshold performance for any of the performance conditions, 0% vests in respect of that performance condition

⁽³⁾ Straight-line vesting between points.

Vesting of the award is subject to an 'underpin' relating to overall Company performance including environmental, social and governance factors and safety performance, as well as financial performance. The Committee has determined, to the date of this report, that this underpin has been satisfied.

The awards are subject to a two-year holding period during which clawback may be applied if the Committee considers it appropriate in certain circumstances. The holding period ends on 1 July 2023.

RETIREMENT BENEFITS AND ENTITLEMENTS (AUDITED INFORMATION)

Details of Directors' pension entitlements and pension related benefits during the year are as follows. Effective 1 August 2021, the maximum pension contribution made by the Company is 10% of salary:

	Value of defined benefit pension ⁽²⁾	Contributions to defined contribution arrangements (£000)	Cash allowances in lieu of pension (£000)	Total value for the year	Normal retirement age and date (for pension purposes)	Accrued pension at 31 March 2021 ⁽⁴⁾
Susan Davy ⁽³⁾	29	-	50	80	65 (17 May 2034)	29
Louise Rowe ⁽¹⁾	-	13	12	25	65 (15 January 2047)	-
Chris Loughlin ⁽⁵⁾	-	-	55	55	67 (20 August 2019)	-

⁽¹⁾ Louise Rowe is a member of Pennon Group's defined contribution arrangement and received an overall pension benefit from the Company equivalent to 15% of her salary

⁽²⁾ The value of the defined benefit pension accrued over the period comprises the total pension input amount (which has been calculated in line with regulatory requirements) less the pension contributions paid by the Director

⁽³⁾ Susan Davy received an overall pension benefit from the Company equivalent to 25% of her salary for the period 1 April to 31 July 2020, which reduced to 10% of salary from 1 August 2020 on appointment as Chief Executive Officer of Pennon Group plc. For 2020/21 this comprised an employer's contribution of £29,884 and a cash sum of £50,352. She is a member of Pennon Group's defined benefit pension arrangements and is entitled to normal retirement pension payable from age 65 of broadly 1/80th of pensionable remuneration for each year of pensionable service completed. Accrual in this scheme will cease from 1 July 2021.

⁽⁴⁾ Accrued pension is based on service to the year end final pensionable salary at that date

⁽⁵⁾ Chris Loughlin was not a member of any of the Pennon Group's pension schemes during his tenure and received a sum in lieu of pension entitlement equivalent to 30% of salary.

No additional benefits will become receivable by a Director in the event that the Director retires early.

NON-EXECUTIVE DIRECTORS' FEES AND BENEFITS

During the year Sir John Parker stepped down from the Board on 31 July 2020 following five years as Chair of the Pennon Group. No payments were made for loss of office. Sir John's fee prior to this departure was £138,000 (50% recharge through Pennon Group plc).

Gill Rider was appointed to Chair of the Board, having served eight years on the Pennon Board, latterly as Chair of the Remuneration Committee. Her fee was set at £113,000 (50% recharge through Pennon Group plc). When appropriate for the efficient carrying out of her duties, she is provided with a driver and vehicle. She is entitled to expenses on the same basis as the other Non-Executive Directors.

Fees for Non-Executive Directors were initially increased by 1.5% at the start of the financial year. In light of the changes in the Pennon Group, the Non-Executive Director fees were further reviewed. In recognition of the new Board structure, the Committee fees were consolidated into the base fees for Non-Executive Directors (increased from £49,850 50% to £60,550 50%). The additional fees for the Chairs of committees were also reviewed. The revised fee structure is set out in full on page 105.

There is no proposed increase to Non-Executive Director fees for 2021/22.

DIRECTORS' SERVICE CONTRACTS AND LETTERS OF APPOINTMENT

The dates of Directors' service contracts and letters of appointment and details of the unexpired term are shown below:

Executive Directors	Date of Service Contract	Notice Period
Susan Davy	1 August 2020	12 months
Louise Rowe	1 February 2015	12 months
Chris Loughlin ⁽¹⁾	1 January 2016	12 months ⁽¹⁾
Non-Executive Directors	Date of Service Contract	Expiry date of Appointment
Gill Rider ⁽²⁾	22 June 2012	31 August 2024 ⁽²⁾
Sir John Parker ⁽³⁾	19 March 2012	31 March 2021
Neil Cooper	17 July 2014	31 August 2023 ⁽³⁾
Iain Evans	16 June 2018	31 August 2021
Claire Ighodaro	28 May 2019	31 August 2022
Jon Butterworth	1 August 2020	31 July 2023

⁽¹⁾ Stepped down from Board on 31 July 2020 and received payment in lieu of notice as disclosed in the Pennon Group plc annual report and accounts on page 122.

⁽²⁾ Gill Rider was appointed as Chair on 31 July 2020

⁽³⁾ Sir John Parker stepped down from the Board on 31 July 2020.

The policy is for Executive Directors' service contracts to provide for 12 months' notice from either side.

The policy is for Non-Executive Directors' letters of appointment to contain a three-month notice period from either side.

Copies of Executive Directors' service contracts and Non-Executive Directors' letters of appointment are available for inspection at the Company's registered office.

OUTSIDE APPOINTMENTS

Executive directors may accept one board appointment in another company. Board approval must be sought before accepting an appointment. Fees may be retained by the Director. Chris Loughlin was appointed as a Non-Executive Director of Mears Group plc through the year and Susan Davy remained a Non-Executive Director of Restore plc throughout 2020/21. No other outside Company appointments are held by the Executive Directors other than with industry bodies or governmental or quasi-governmental agencies.

ADDITIONAL CONTEXTUAL INFORMATION

HISTORICAL CHIEF EXECUTIVE REMUNERATION

As the Company did not have a Chief Executive Officer until 1 January 2016, the table below provides historical single figure information in the form of the average remuneration of the Executive Directors for years up to and including 2014/15. Their remuneration was considered to be the most appropriate to use as they were the most senior executives in the Company. From 2015/16 onwards, the Chief Executive Officer's remuneration for the year is shown.

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	
							Chris Loughlin	Susan Davy
Chief Executive Officer single figure remuneration (£000)	378	461	553	493	663	1,068	565 ⁽¹⁾	863 ⁽¹⁾
Annual Bonus payout (% of maximum)	89.6%	78.3%	65.8%	85%	90%	78%	79.2%	78.1%
LTIP (PCP) vesting (% of maximum)	0%	34.5%	43.7%	0%	44%	86.6%	89.9%	89.9%

⁽¹⁾ Chris Loughlin stepped down as Chief Executive Officer on 31 July 2020 and was succeeded by Susan Davy. Consistent with the single figure, the figures for Susan Davy relate to the whole of 2020/21, including the portion of the year when she was Chief Financial Officer.

PERCENTAGE CHANGE IN DIRECTORS REMUNERATION
Comparison of Directors' remuneration to employee remuneration

The table below shows the percentage change between 2019/20 and 2020/21 in base salary, benefits and annual bonus of all Directors, including both Executive Directors and Non-Executive Directors, and all employees.

	Percentage change in salary/fees	Percentage change in benefits	Percentage change in pensions	Percentage change in annual bonus
Executive Directors				
Susan Davy ⁽¹⁾	10.7%	0%	-32.2%	34.8%
Louise Rowe	1.5%	0%	2.1%	-40.4%
Chris Loughlin ⁽²⁾	-66.4%	-76%	-65.4%	-65.7%
Non-Executive Directors				
Sir John Parker ⁽³⁾	-66%	0%	-	-
Gill Rider ⁽⁴⁾	126%	0%	-	-
Neil Cooper	16%	0%	-	-
Iain Evans	4%	0%	-	-
Claire Ighodaro	97%	0%	-	-
Jon Butterworth	-	0%	-	-
All Employees				
South West Water	4.28%	4.38%	2.2%	-0.08%
UK employees	1.22%	5.7%	2.5%	-17.8%

⁽¹⁾ Susan Davy appointed as Chief Executive 31 July 2020. Change in remuneration and bonus to reflect this

⁽²⁾ Chris Loughlin stepped down from the Board as Chief Executive Officer 31 July 2020. Change in remuneration, benefits and bonus reflect this.

⁽³⁾ Sir John Parker stepped down from the Board as Chair 31 July 2020

⁽⁴⁾ Gill Rider appointed as Chair 31 July 2020 and received an increase in fees

RELATIVE IMPORTANCE OF SPEND ON PAY

	2020/21 £m	2019/20 £m	Percentage change (%)
Overall expenditure on pay⁽¹⁾	69.8	60.5	15.4%
Distributions to Parent Company (excluding special dividend)⁽²⁾	100.4	119.7	(16.1%)
Net interest charges	56.5	71.1	(20.5%)
Purchase of property, plant and equipment (cash flow)	161.1	172.2	(6.4%)

⁽¹⁾ Excludes employer's social security costs and non-underlying items.

⁽²⁾ Excludes dividend payment of £1.2 million to parent in October 2020 as part of the Watershare+ customer rebate scheme. Includes payment of the outperformance dividend based on cumulative outperformance for 2019/20 of £58.1 million that has been deferred to August 2021.

The above table illustrates the relative importance of spend on pay compared with distributions to shareholders and other Company outgoings. The distributions to Parent Company, interest charges and the purchase of property, plant and equipment (cash flow) have been included as these were the most significant outgoings for the Company in the last financial year.

CHIEF EXECUTIVE OFFICER PAY RATIO

Our CEO pay ratio stands at 69:1 for the median employee. This is not dissimilar to the ratio in 2020 – the demographics of the business have changed considerably with a much larger percentage of apprentices and career entry roles in the Company. We have also supported the Kickstart programme leading to 25 new entrants increasing our population at the lower end of our pay scales.

Year	Method	25th percentile (P25) pay ratio	50th percentile (P50) pay ratio	75th percentile (P50) pay ratio
2020/21	Option A	93:1	69:1	55:1
2019/20	Option A	91:1	64:1	53:1

Option A has been used for the calculations as per the disclosure regulations. The employees at the lower quartile, median and upper quartile (P25, P50, and P75, respectively) have been determined based on a calculation of total remuneration for the financial year 1 April 2020 to 31 March 2021.

- Basic salary for part-time employees and new joiners within the applicable period have been converted to full-time equivalents for the purpose of the calculations.
- Estimated values for employee P11d data have been used in the calculation to establish the ordering of employees, given the timing of publication. This will be validated and amended in due course to account for any variances.

The total remuneration of 2020/21 for the employees identified at P25, P50 and P75 is £28,187, £35,897, and £44,228, respectively.

The base salary of 2020/21 for the employees identified at P25, P50 and P75 is £25,059, £20,724, and £31,306, respectively.

The remuneration arrangements for senior executives, fluctuates year-on-year as a significant portion of the package is linked to performance-related incentive plans. This variation will impact the pay ratios reported in future years.

SHARE AWARD AND SHAREHOLDING DISCLOSURES (AUDITED INFORMATION)

Share awards granted during 2020/21

The table below sets out details of share awards made in the year. Details of the Chief Executive Officer share awards are included in the Pennon Annual Report on page 125.

Executive Director ⁽¹⁾	Type of interest	Basis of Award	Face value £000	Percentage vesting at threshold performance	Performance period end date
Susan Davy	LTIP	150% of salary	684	25% of maximum	2 August 2023
Susan Davy	Deferred bonus	50% of bonus awarded	162	N/A	13 July 2023
Louise Rowe	LTIP	100% of salary ⁽¹⁾	169	25% of maximum	13 July 2023
Louise Rowe	Deferred bonus	50% of bonus awarded	44	N/A	13 July 2023

⁽¹⁾ Exceptionally for 2020, LTIP awards of 100% of salary were awarded

LTIP awards were calculated using the Pennon Group plc share price of £1075.49p (being the average closing price over the five dealing days preceding the date of grant, which was 14 July 2020) for the Finance Director. For the Chief Executive Officer, LTIP awards were based on £1071.9p (being the average closing price over the five dealing days preceding the 3 August 2020). LTIP awards are subject to an additional two-year holding period. Deferred bonus awards were calculated using the average Pennon Group share price at which shares were purchased on the market on 10 July 2020 in order to satisfy the award, which was £1079.47p.

Directors' shareholding and interest in shares

The Remuneration Committee believes that the interests of Executive Directors and senior management should be closely aligned with the interests of Pennon Group plc shareholders.

To support this, the Committee operates shareholding guidelines. For 2020/21, this guideline was 100% of salary for the Finance Director and 200% for the Chief Executive Officer. In line with best practice guidelines, deferred bonuses and LTIP awards subject to a holding period may only count towards the guidelines on a net tax basis. The Executive Directors are expected to build up a shareholding in the Company within the first five years of joining the Company, or appointment to a new role.

The beneficial interests of the Executive Director in the ordinary shares (40.7p each) of Pennon Group plc as at 31 March 2021 and 31 March 2020 and interest are shown in the table below:

	Share interests (including connected parties) at 31 March 2021	Share interests (including connected parties) at 31 March 2020	Unvested awards				Vested LTIP awards in holding period ⁽¹⁾	Shareholding guideline (to be accrued over five years)	Shareholding guideline met?
			Performance shares (subject to performance conditions)	SAYE	Deferred Bonus shares				
Susan Davy	90,010	78,834	222,527	2,834	62,206	89,602	200%	Yes	
Louise Rowe	15,799	13,759	49,921	2,834	18,222	20,428	100%	Yes	

⁽¹⁾ These share awards are not subject to further performance criteria and may therefore count towards the guideline on a net-of-tax basis.

Since 31 March 2021, 28 additional ordinary shares in Pennon Group have been acquired by Louise Rowe as a result of participation in the Pennon Group's Share Incentive Plan.

The interests of the outgoing Chief Executive Officer can be seen on page 125 of the Pennon Annual Report.

Non-Executive Directors' shareholding

The beneficial interests of the Non-Executive Directors, including the beneficial interests of their spouses, civil partners, children and step-children, in the ordinary shares (40.7p) of the Pennon Group, are shown in the table below:

Director	Shares held at 31 March 2021	Shares held at 31 March 2020
Sir John Parker ⁽¹⁾	27,027	27,027
Gill Rider	3,612	2,500
Neil Cooper	-	-
Iain Evans	-	-
Claire Ighodaro	-	-
Jon Butterworth	-	-

⁽¹⁾ Stepped down from the Board on 31 July 2020.

There have been no changes in the beneficial interests or the non-beneficial interests of the above Directors in the ordinary shares of the Company between 1 April 2021 and 1 June 2021. There is no formal shareholding guideline for the Non-Executive Directors; however, they are encouraged to purchase shares in the Company.

Details of share awards

The Chief Executive Officer's share awards can be seen on pages 125 to 128 in the Pennon Annual Report.

(a) Long-term incentive plan

In addition to the above beneficial interests, the following Directors has or had a contingent interest in the number of ordinary shares (40.7p each) of Pennon Group plc shown below, representing the maximum number of shares to which they would become entitled under the plan should the relevant criteria be met in full:

Director and date of award	Vested awards held at 1 April 2020 ⁽ⁱ⁾	Conditional awards held at 1 April 2020	Conditional awards made in year	Market price of each share upon award in year	Vesting in year ⁽ⁱⁱ⁾	Value of shares upon vesting (before tax) £000	Vested awards held at 31 March 2021 ⁽ⁱⁱⁱ⁾	Conditional awards held at 31 March 2021	Date of end of restricted period	Expected date of release ^(iv)
Susan Davy										
01/07/16	15,567	-	-	920.00p	-	115	15,557	-	30/06/19	30/06/21
25/08/17	-	73,972	-	802.70p	74,045	747	74,045	-	24/08/20	24/08/22
02/07/18	-	76,653	-	790.12p	-	-	-	76,653	01/07/21	01/07/23
04/07/19	-	82,062	-	752.72p	-	-	-	82,062	03/07/22	03/07/24
03/08/20	-	-	63,812	1071.9p	-	-	-	63,812	02/08/23	02/08/25
Louise Rowe										
01/07/16	4,467	-	-	920.00p	-	33	4,467	-	30/06/19	30/06/21
25/08/17	-	15,946	-	802.70p	15,961	161	15,961	-	24/08/20	24/08/22
02/07/18	-	16,524	-	790.12p	-	-	-	16,524	01/07/21	01/07/23
04/07/19	-	17,692	-	752.72p	-	-	-	17,692	03/07/22	03/07/24
03/08/20	-	-	15,705	1075.49p	-	-	-	15,705	13/07/23	13/07/25

(i) 32% of the award shares granted on 1 July 2016 vested on 1 July 2019 at a market price of £741.2p per share.

(ii) 86.6% of the award shares granted on 25 August 2017 vested on 25 August 2020 at a market price of £10.085 per share. In respect of (i) and (ii) above, the total number of shares that vested included additional shares equivalent in value to such number

(iii) Vested award; no longer subject to performance conditions

(iv) Awards granted from 2015 onwards are subject to a two year holding period following vesting

(b) Annual incentive bonus plan – deferred bonus shares (long- term incentive element)

The following Director has or had a contingent interest in the number of ordinary shares (40.7p each) of Pennon Group plc shown below, representing the total number of shares to which they have or would become entitled under the deferred bonus element of the annual incentive bonus plan (the bonus plan) at the end of the relevant restricted period:

Director and date of award	Restricted awards held at 1 April 2020	Restricted awards made in year	Market price of each share upon award in year	Released in year	Value of shares upon vesting (before tax) £000	Restricted awards held at 31 March 2021	Date of end of restricted period
Susan Davy							
30/08/17	20,503	-	808.691p	20,503 ⁽¹⁾	205	-	29/08/20
25/07/18	22,746	-	761.36p	-	-	22,746	24/07/21
24/07/19	24,449	-	755.5386p	-	-	24,449	23/07/22
14/07/20	-	15,011	1,079.47p	-	-	15,011	13/07/23
Louise Rowe							
30/08/17	5,929	-	808.691p	5,929 ⁽¹⁾	59	-	29/08/20
25/07/18	6,803	-	761.36p	-	-	6,803	24/07/21
24/07/19	7,317	-	755.5386p	-	-	7,317	23/07/22
14/07/20	-	4,102	1,079.47p	-	-	4,102	13/07/23

⁽¹⁾ These shares were released on 1 September 2020 at 1000.5p per share

During the year the Directors received dividends on the above shares in accordance with the conditions of the bonus plan as follows: Louise Rowe £8,775.

(c) Sharesave scheme

Details of options to subscribe for ordinary shares (40.7p each) of Pennon Group plc under the all-employee sharesave scheme were:

Director and date of grant	Options held at 1 April 2020	Granted in year	Exercised /lapsed in year	Exercise price per share	Market price of each share on exercising	Market value of each share at 31 March 2021	Options held at 31 March 2021	Exercise period/maturity date
S.Davy 03/07/18	2,834	-	-	635.00p	-	975.00p	2,834	01/09/21- 28/02/22
L. Rowe 03/07/18	2,834	-	-	635.00p	-	975.00p	2,834	01/09/21- 28/02/22

THE REMUNERATION COMMITTEE AND ITS ADVISERS

Claire Ighodaro replaced Gill Rider as Chair of the Remuneration Committee on 8 July 2020. Gill Rider continued to serve as a member of the Committee. Neil Cooper and Iain Evans were members of the Remuneration Committee throughout the year. Jon Butterworth joined the Committee from 31 July 2020.

During the year the Committee received advice or services which materially assisted the Committee in the consideration of remuneration matters from Sir John Parker (Chair of the Board), Adele Barker (Pennon Group Chief People Officer) and from Deloitte LLP. During 2018/19, Deloitte LLP was reappointed directly by the Committee with a refreshed advisory team, following a comprehensive retendering process. Deloitte LLP is a member of the Remuneration Consultants Group and as such voluntarily operates under the code of conduct in relation to executive remuneration consulting in the UK. The Committee is satisfied that the advice it has received from Deloitte LLP has been objective and independent.

DIRECTORS' REMUNERATION REPORT COMPLIANCE

This Directors' remuneration report has been prepared in accordance with the provisions of the Companies Act 2006 and the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. The UK Corporate Governance Code also sets out principles of good governance relating to directors' remuneration, and this report describes how these principles are applied in practice. The Committee confirms that throughout the financial year the Company has complied with these governance rules and best practice provisions. The external auditor is obliged to state whether, in its opinion, the relevant sections have been prepared in accordance with the Companies Act 2006. The external auditor's opinion is set out on page 131 and the audited sections of the annual report on remuneration are identified in this report.

BOARD OF DIRECTORS AND COMPANY INFORMATION

CHAIR	G Rider CB
CHIEF EXECUTIVE OFFICER	S Davy
FINANCE DIRECTOR	L F Rowe
SENIOR INDEPENDENT DIRECTOR	N Cooper (Non-Executive)
NON-EXECUTIVE DIRECTORS	C Ighodaro CBE I Evans CBE J Butterworth MBE
COMPANY SECRETARIES	S Pugsley
REGISTERED OFFICE	Peninsula House Rydon Lane Exeter Devon EX2 7HR
INDEPENDENT AUDITOR	Ernst & Young LLP 1 Bridgewater Place Water Lane Leeds LS11 5QR
COMPANY'S REGISTERED NUMBER	02366665
PRINCIPAL ACTIVITIES	The principal activities of the Company are the provision of water and sewerage services. The Company holds the water and sewerage appointments for Cornwall and Devon and parts of Somerset and Dorset. It also provides water supply services to parts of Dorset, Hampshire and Wiltshire.

DIRECTORS' REPORT – OTHER STATUTORY DISCLOSURES

INTRODUCTION

This Directors' report is prepared in accordance with the provisions of the Companies Act 2006 and regulations made thereunder. It comprises pages 62 to 99 and 123 to 128 as well as the following matters which the Board considers are of strategic importance and, as permitted by legislation, has chosen to include in the strategic report rather than the Directors' report:

- risk management systems (page 42 to 45 of the strategic report)
- likely future developments of the Company (page 9 of the strategic report)
- certain employee matters (pages 24 to 29 of the strategic report), as well as the disclosures below.

In addition, there are a number of disclosures which are included in the Directors' report by reference, including:

- financial risk management (note 3 of the financial statements)
- financial instruments (pages 35 to 41 of the strategic report and notes 15 to 19 of the notes to the financial statements).

BOARD OF DIRECTORS

The Directors in office as at the date of this report are named on page 122. Sir John Parker, the previous Chair, and Chris Loughlin, the previous Chief Executive Officer, served during the year until their retirement from the Board on 31 July 2020. Lord Matthew Taylor and Martin Hagen also left the South West Water Board on 31 July 2020.

FINANCIAL RESULTS AND DIVIDEND

A total dividend for the year of £43.5 million was paid during the year (2019/20: £249.7 million). A further £58.1m was declared and approved during the year and payment is being deferred to 2021/22. The Report of the Finance Director on pages 35 to 41 analyses the Company's financial results in more detail and sets out other financial information.

DIRECTORS' INSURANCE AND INDEMNITIES

The Company has maintained throughout the year Directors' and officers' liability insurance for the benefit of the Company, the Directors and its officers. The Company has entered into qualifying third party indemnity arrangements for the benefit of all its Directors in a form and scope which comply with the requirements of the Companies Act 2006 and which were in force throughout the year and remain in force.

EMPLOYMENT POLICIES AND EMPLOYEE INVOLVEMENT

South West Water has a culture of continuous improvement through investment in people at all levels within the Company. It is committed to pursuing equality and diversity in all its employment activities including recruitment, training, career development and promotion and ensuring there is no bias or discrimination in the treatment of people. In particular, applications for employment are welcomed from persons with disabilities, and special arrangements and adjustments as necessary are made to ensure that applicants are treated fairly when attending for interview or for pre-employment aptitude tests. Wherever possible the opportunity is taken to retrain people who become disabled during their employment in order to maintain their employment within the Company.

The Company has policies in place covering health & safety, equal opportunities, diversity and inclusion, ethics and employee relations. In addition, the Board has a diversity policy, details of which are set out in the report of the Nomination Committee on page 94. Information regarding the diversity of the workforce is provided on pages 24 to 27.

South West Water respects the right to freedom of association and employees are consulted regularly about changes which may affect them either through their trade union-appointed representatives, through consultation groups or by means of their elected representatives at the Employee Engagement Forum. These forums, together with regular meetings with particular groups of employees, are used to ensure that employees are kept up to date with the business performance of their employer and the financial and economic factors affecting the performance of the Company and the Pennon Group as a whole. South West Water also cascades information monthly to all employees to provide them with important and up to date information about key events and to obtain feedback from them. Further information about workforce engagement and employment matters relating to the Company is set out on pages 24 to 29 of the Strategic report.

South West Water and the Pennon Group as a whole encourages share ownership among its employees in Pennon Group plc by operating an HM Revenue & Customs approved Sharesave scheme and Share Incentive Plan. Following Pennon shareholder approval at the 2014 AGM, these were amended to provide for the increased savings limits approved by Government. At 31 March 2021, approx. 56% of South West Water's employees were participating in these plans.

MODERN SALVERY ACT

We have in place policies and procedures to assess, monitor and reduce the risk of forced labour and human trafficking occurring in our businesses and supply chains. Risk assessments of any high-risk supply partners have been completed to ensure compliance with the Modern Slavery Act across the Company and our anti-slavery and human trafficking web-based statement for the year, which is completed at a Group level, is available at www.southwestwater.co.uk.

GREENHOUSE GAS EMISSIONS

The Company has taken advantage of the exemption offered under the Companies Act 2006 and has not reported details of Greenhouse gas emissions during the financial year. Details of South West Water's greenhouse gas emissions can be found in the Annual Performance Report and Regulatory Reporting, published in July 2021 (www.southwestwater.co.uk/report2021).

RESEARCH AND DEVELOPMENT

The development and testing of innovative techniques and processes will continue to play a role in the further improvement and provision of cost effective services.

Research and development expenditure amounted to £0.1 million during the year (2019/20: £0.2 million).

OVERSEAS BRANCHES

The Company has no overseas branches.

DONATIONS

During 2020/21 the Company provided a total of £291,000 in charitable donations (2019/20: £200,000).

No political donations were made or political expenditure incurred and no contributions were made to a non-EU political party (2019/20: nil).

GOING CONCERN

The going concern basis has been adopted in preparing the financial statements as stated by the Directors on page 123. At 31 March 2021, the Company had access to undrawn committed funds and cash and cash deposits totalling £389.0 million (£293.2 million excluding restricted cash). Having considered the Company's strong funding position and prudent financial projections, which take into account a range of possible impacts, as described in this report, from the COVID-19 pandemic, the Directors have a reasonable expectation that the Company has adequate resource to continue in operational existence for a period of at least 12 months from the date of approval of the financial statements and that there are no material uncertainties to disclose. For this reason they continue to adopt the going concern basis in preparing the financial statements.

ENGAGING WITH STAKEHOLDERS - SECTION 172 STATEMENT

The decision making principles within Section 172 of the Companies Act 2006 (s.172) are embedded throughout our processes and within all that we do as a company.

All decisions are considered against the need to ensure we act in a sustainable, ethical and collaborative way, understanding the views of our different Stakeholders and weighing their competing interests. Our Board leads and sets the tone by carefully noting the priorities of our Stakeholders during its discussions and when it takes decisions. We also know the importance of continually assessing the long-term impacts of our decisions. This helps us meet our Purpose, our Values, and our aspirations to be a responsible, trusted and sustainable business acting in a way which benefits all our Stakeholders as much as possible. Properly understanding the impacts of what we are doing has become part of how we operate and it permeates everything we want to achieve here at South West Water.

OUR s.172 APPROACH

When we make decisions, we always take into proper account all of the following:

- The long-term consequences of any decision
- The interests of the company's employees
- The importance of having excellent business relationships with suppliers, customers and anyone else who we impact
- The impact our operations have on our on our community and environment
- Ensuring we maintain our reputation for the highest standards of business conduct

As part of every decision we make, we will look at how we will impact our Stakeholders. To enable us to understand the points of view of our Stakeholders and where our decisions could affect them, we have a Stakeholder engagement programme. We see Stakeholder engagement both as fundamental to development and delivery of our Purpose and Strategy and as critical for our long-term sustainable success. Although there are often competing interests and priorities involved, being clear on what matters to our Stakeholders, allows our Board to weigh-up all relevant factors.

MATTERS CONSIDERED BY THE BOARD

Below are examples of decisions taken by the Board during the year and how Stakeholder views and inputs, as well as other s.172 considerations, were considered.

Matter	Section 172 Considerations	Our Engagement	The Board's Role
Board changes and governance framework	The enactment of the Board's internal succession plan and new governance framework required to position South West Water favourably for the next phase of its growth strategy and focus on UK Water was considered by the Board to be essential for	The new Company Purpose and culture were developed following consultation with regulators, employees and customers.	Key stakeholders were identified, feedback reviewed and the succession plan modified as appropriate. A number of Board and Board committee meetings followed, including a review by the Nomination Committee. Throughout the process of enacting the succession plan

	<p>long-term success.</p> <p>Noting these objectives, the following stakeholders were identified as key:</p> <ul style="list-style-type: none"> • Regulators • Employees • Customers 		<p>and new governance framework, the Board oversaw and challenged management's engagement with stakeholders and had regard to the need to foster the Company's business relationships with shareholders, regulators and customers.</p>
Green Recovery Initiative	<p>We recognise our vital role in the region and our stewardship of essential resources, to ensure that we are supporting our communities and the places they love for generations to come.</p> <p>Noting these objectives, the following stakeholders were identified as key:</p> <ul style="list-style-type: none"> • Regulators • Employees • Customers • Suppliers 	<p>In line with our Strategic Plan, a significant part of which is focused on our environmental and social impacts, we developed our Green Recovery Initiative following discussion with our regulators and government, presentations to customer focus groups including the WaterShare+ Advisory Panel and reviews with suppliers.</p> <p>We engaged with our employees via the Big Chat and the Employee Survey, which indicated strong support from employees for our approach.</p>	<p>The Board's decision-making process was based on its objective to ensure that the business is environmentally and socially sustainable in the long-term. The Board reviewed the Green Recovery Initiative throughout its development taking into account the engagement with all those whose interests would be affected by its plans.</p> <p>The Board approved the Green Recovery Initiative for submission to our regulators in January 2021.</p>
Watershare+	<p>The WaterShare+ scheme was developed to build a closer relationship with South West Water's customers by offering customers the opportunity to become shareholders in their water company, giving them a voice and a financial stake in our business.</p> <p>Noting these objectives, the following stakeholders were identified as key:</p> <ul style="list-style-type: none"> • Customers • Regulators • Shareholders. 	<p>During our engagement in the leadup to our Business Plan for 2020-25, we consistently received feedback that customers would like to have a greater say in their water company and share in financial outperformance.</p> <p>Watershare+ affords customers the opportunity to become a different type of stakeholder - a shareholder with a financial stake in their water company.</p> <p>WaterShare+ was an innovative component of our PR19 Business Plan and was positively received and supported by Ofwat. The WaterShare+ share scheme was designed to ensure that there was no dilution of existing shareholdings or existing voting rights so that our existing shareholders were unaffected.</p>	<p>The Board had an active role in the development of the WaterShare+ scheme from its inception and continues to provide oversight of the scheme.</p> <p>Implementation of the scheme in 2020 was overseen by the Board and it continues to monitor the scheme through the WaterShare+ Advisory Panel and a separate customer Annual General Meeting to be held annually with the first meeting being held in Autumn 2021.</p>
Pension scheme changes	<p>Our people are fundamental to our success and our ability to deliver our long-term aims. To ensure the retention of our valued employees and to attract new talent, South West Water is committed to providing appropriate and attractive employee benefits and being a</p>	<p>As part of the Company's long-term pensions strategy, the business engaged in an extensive consultation process with employees and trade unions on the plans to modernise its pensions arrangements.</p> <p>The business simultaneously consulted with the Group's Pension Trustees regarding</p>	<p>The Board provided regular input to the development of the Company's plans to modernise its pensions arrangements. The outcome of the consultation and allied reviews, resulted in a decision to close the main defined benefit scheme to future accrual with effect from 1 July</p>

	<p>responsible employer, including by providing modern, equitable and suitably managed pensions arrangements.</p> <p>Noting these objectives, the following stakeholders were identified as key:</p> <ul style="list-style-type: none"> • Customers • Pension Trustees • Regulators 	<p>these plans as well as the Pensions Regulator.</p>	<p>2021 - with all employees transitioning to a new and bespoke defined contribution scheme offered through a master trust arrangement.</p>
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STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for preparing the annual report, the Directors' remuneration report and the financial statements in accordance with applicable law and regulations. Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Company financial statements in accordance with International Financial Reporting Standards (IFRSs) in conformity with the Companies Act 2006.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for the year.

In preparing these financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently
- Make judgements and accounting estimates that are reasonable and prudent
- State whether applicable International Financial Reporting Standards (IFRSs) in conformity with the Companies Act 2006 have been followed, subject to any material departures disclosed and explained in the financial statements. The Directors confirm that they have complied with the above requirements in preparing the financial statements.

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

The Directors have voluntarily opted to comply with the UK corporate Governance Code (the Code) to the extent required, within the context of being a subsidiary of a listed company. The Directors have prepared the Strategic Report, Directors' Report, Directors' Remuneration Report and Corporate Governance Statement in compliance with the Code.

Each of the Directors, whose names and functions are listed on page 74, confirms that, to the best of his or her knowledge:

- i) The financial statements, which have been prepared in accordance with IFRSs in conformity with the Companies Act 2006, give a true and fair view of the assets, liabilities, financial position and profit of the Company.
- ii) The strategic report (pages 3 to 41) and the Directors' report (62 to 99 and 123 to 128) include a fair review of the development and performance of the business during the year and the position of the Company at the year end, together with a description of the principal risks and uncertainties they face.
- iii) Following receipt of advice from the Audit Committee, that the annual report, taken as a whole, is fair, balanced and understandable, and provides the information necessary for the shareholders to assess the Company's performance, business model and strategy.

The Directors are responsible for the maintenance and integrity of the Company's website www.southwestwater.co.uk. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

STATEMENT AS TO DISCLOSURE OF INFORMATION TO THE COMPANY'S AUDITOR

a) So far as each of the Directors in office at the date of signing of the report is aware, there is no relevant audit information of which the Company's auditor is unaware; and

b) each of the Directors has taken all the steps that each Director ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

The Directors' report consisting of pages (62 to 99 and 123 to 128) was approved by the Board on 30th June 2021.

By Order of the Board

SIMON A F PUGSLEY

Group General Counsel and Company Secretary

30th June 2021

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SOUTH WEST WATER LIMITED

OPINION

We have audited the financial statements of South West Water Limited for the year ended 31 March 2021 which comprise the Income Statement, the Statement of Comprehensive Income, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes 1 to 36, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Accounting Standards in conformity with the requirements of the Companies Act 2006.

In our opinion, the financial statements:

- ▶ give a true and fair view of the company's affairs as at 31 March 2021 and of its profit for the year then ended;
- ▶ have been properly prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006; and
- ▶ have been prepared in accordance with the requirements of the Companies Act 2006.

BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

CONCLUSIONS RELATING TO GOING CONCERN

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate. Our evaluation of the directors' assessment of the company's ability to continue to adopt the going concern basis of accounting included the following procedures:

- ▶ We have obtained management's going concern assessment, including the cash forecast, liquidity requirements and forecast covenant calculations for the going concern period which covers the period from approval of the 2021 financial statements through to 30 June 2022, and have tested this for arithmetical accuracy. Management has modelled a downside scenario in their cash forecasts and covenant calculations in order to incorporate unexpected changes to the forecasted liquidity of the company.
- ▶ We have considered the forecasts used for the going concern assessment period for reasonableness, in the context of our knowledge of the business gained during the audit, and, where applicable, corroborated the data with audit information from other areas. We have evaluated the appropriateness of the key assumptions in management's forecasts including revenue growth, by comparing these to year to date performance and through consideration of historical forecasting accuracy.

- ▶ The company has an agreed business plan with Ofwat for the five year price period from 1 April 2020 to 31 March 2025, setting out the basis of allowed tariff changes. We have compared the key assumptions in the company forecasts to the agreed business plan for consistency.
- ▶ We have evaluated management's stress test modelling including management's downside scenario, to understand the impact on the company's liquidity and covenant ratios.
- ▶ We have compared facilities assumed in the forecasts to supporting documentation.
- ▶ We have compared the risks identified in management's assessment to the company risk register and evaluated the quantification by management. We have considered whether there are other alternative risks based on our knowledge of the business.
- ▶ We tested the extent of changes in assumptions required to give rise to a reduction in liquidity or breach in covenants.
- ▶ We have read the company's going concern disclosures included in the annual report in order to assess whether the disclosures were appropriate and in conformity with the reporting standards.

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 company's ability to continue as a going concern for a period to 30 June 2022.

In relation to the company's reporting on how they have applied the UK Corporate Governance Code, we have nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the company's ability to continue as a going concern.

OVERVIEW OF OUR AUDIT APPROACH

Key audit matters	<ul style="list-style-type: none"> • Revenue recognition in respect of accrued income • Valuation of the expected credit loss provision for customer balances
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AN OVERVIEW OF THE SCOPE OF OUR AUDIT

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for the Company. This enables us to form an opinion on the financial statements. We take into account size, risk profile, the organisation of the Company and effectiveness of controls, including controls and changes in the business environment when assessing the level of work to be performed.

Changes from the prior year

There were no changes to the scope of the audit from the prior year.

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) that we identified. These matters included 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 our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Revenue recognition, specific to accrued income £543.8 million (PY comparative £571.6million) of which £77.6 million is accrued at 31 March (PY comparative £71.6 million)</p> <p><i>Refer to the Audit Committee Report (page 86); Accounting policies (pages 146-147); and Note 5 of the Financial Statements (page 156)</i></p> <p>The company's material revenue streams relate to the provision of water and sewerage services. ISAs (UK & Ireland) presume there is a risk of fraud relating to revenue recognition. For the company, given the targets associated with financial performance and potential pressures to meet market expectations, there is an incentive to overstate revenue. This risk over revenue recognition specifically arises in relation to income from measured water services, which requires an estimation of the amount of unbilled charges at the</p>	<p>We obtained an understanding of the process for the supply of measured services, meter reading and related billing in order to assess the completeness of the accrual for revenue at the year end;</p> <p>We tested key controls linked to system generated information and around the estimation process for measured revenue;</p> <p>We obtained internal and external data on factors that influence demand from customers, such as weather patterns and leaks in infrastructure networks and formed an expectation of the impact of these matters on revenue to compare to assumptions used in management's estimate;</p> <p>Given the changes in customer consumption patterns (increase in household consumption and decreased in non household consumption) arising from the impact of Covid-19, we used</p>	<p>We concluded that the estimation process undertaken by management to calculate the measured income accrual reflected latest operational factors in the key assumptions and that the income accrual was appropriately determined.</p>

<p>year end. This is calculated using a combination of system generated information, based on previous customer volume usage, together with management judgement as to the likely impact on usage of factors such as recent weather patterns. In the current year, management's estimation has also taken into account the impact of Covid-19 on consumption patterns by customers, which has seen increased consumption by household customers and decreased consumption by non household customers.</p>	<p>evidence from actual meter readings throughout the year to compare to the assumptions used to estimate revenue recognised for metered customers without a recent reading;</p> <p>We obtained a system report of invoices raised post year end based on actual meter readings taken since the year end. We selected a sample of items from the report to compare to supporting evidence. We compared this report to the year end assumptions used to accrue income for these customer accounts, to assess the reliability of the assumptions used to determine accrued income;</p> <p>We performed analytical procedures by comparing revenue balances for the year against expectations and obtained support for significant variances; and</p> <p>In performing our journal testing, we paid increased attention to entries impacting revenue, focusing on non-system postings and those raised in the last two weeks of the year.</p>	
<p>Valuation of the expected credit loss provision for customer balances (£88.4 million, PY comparative £91.6 million)</p> <p><i>Refer to the Audit Committee Report (page 86); Accounting</i></p>	<p>We performed a walkthrough of the process for calculating the bad debt provision and assessed the design effectiveness of the relevant key controls;</p> <p>We tested the operating effectiveness of key controls over</p>	<p>We have concluded that the provision of £88.4 million is within an acceptable range and appropriately reflects the recent history of collection of outstanding debts and considerations of the impact on future collections of the</p>

<p><i>policies (page 149); Note 18 of the Financial Statements (page 164)</i></p> <p>The South West Water credit loss provision is calculated using a combination of system generated information on historic debt recovery rates and management's judgement of the future likely recovery rates.</p> <p>Management's key assumptions include:</p> <ul style="list-style-type: none"> • that the historic level of collections is indicative of the ability to collect at the same levels in the future; • that the risk of non recovery from customers varies, depending on factors such as whether the household customer no longer occupies a property in the area, has previously paid/not paid, is/is not on a payment plan etc; and • that the collection processes implemented in response to the Covid-19 pandemic will enable management to maintain the current level of collection performance <p>There is a risk that the assumptions used by management in calculating the provision, may be susceptible to management bias and the valuation of the provision against trade receivables may be misstated. We have therefore focused on this key audit matter.</p>	<p>the integrity of data and the report utilised to generate the ageing and categorisation of debt within each component's billing systems;</p> <p>We tested historic data on collection rates and evaluated how this data was used in the preparation of the provision;</p> <p>We assessed the assumptions used by management in determining the amounts provided against the different categories and age of debt, by comparing these assumptions to historic collection rates and by considering the impact of changes in the methods adopted operationally by management to collect debt, and in the external environment;. We considered whether the historic collection performance evidenced the behaviour patterns assumed by management depending on categorisation of household customers;</p> <p>We utilised collection information over previous periods, with sensitivities to consider the impact of a deterioration which might arise from a downturn in the economy, post removal of Government support packages, to determine an acceptable range of the likely ultimate collection of debts existing at the balance sheet date and compared this to the provision recorded by management; and</p> <p>We tested the appropriateness of journal entries and adjustments</p>	<p>economic environment arising from Covid-19.</p>
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	impacting the doubtful debt provision, particularly those raised close to the balance sheet date.	
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In the prior year, our auditor's report included a key audit matter in relation to the impact of COVID-19 pandemic and the impact on going concern. In the current year, our considerations are covered in the Conclusions relating to going concern section above.

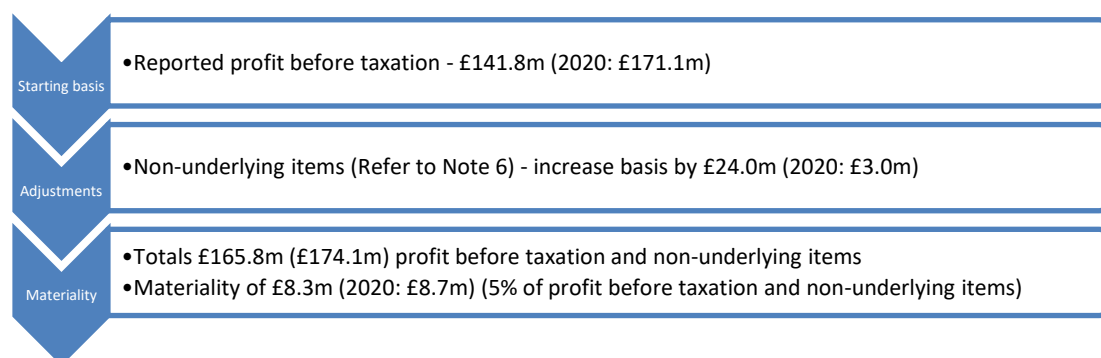
Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Company to be £8.3 million (2020: £8.7 million), which is 5% (2020: 5%) of profit before taxation and non-underlying items. We believe that profit before taxation and non-underlying items provides us with an appropriate measure of the underlying performance of the company. We excluded non-underlying items on the basis that profit before taxation after non-underlying items is not indicative of the underlying performance of the company. We also note that market and analyst commentary on the performance of the company uses the same measure.



Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Company's overall control environment, our judgement was that performance materiality was 75% (2020: 75%) of our planning materiality, namely £6.2m (2020: £6.5m). We have set performance materiality at this percentage based on our assessment of the company's internal control environment and the extent and nature of audit findings identified in the prior period. This basis is consistent with the prior year.

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.4m (2020: £0.4m), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read 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 there is a material misstatement in the financial statements themselves or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- ▶ the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- ▶ the strategic report and directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or directors' report.

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

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

Voluntary reporting matters

Directors' remuneration report

The Company voluntarily prepares a Report of the directors on remuneration in accordance with the basis of preparation set out in the Directors' Remuneration Report. The directors have requested that we audit the part of the Report of the directors on remuneration specified by the Companies Act 2006 to be audited as if the Company were a quoted company.

In our opinion, the part of the directors' remuneration report to be audited has been properly prepared in accordance with the basis of preparation set out in the Directors' Remuneration Report.

Corporate Governance Statement

ISAs (UK) require us to review the directors' statement in relation to going concern, longer-term viability and that part of the Corporate Governance Statement relating to the company's compliance with the provisions of the UK Corporate Governance Code specified for our review.

Based on the work undertaken as part of our audit, we have concluded 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:

- Directors' statement with regards to the appropriateness of adopting the going concern basis of accounting and any material uncertainties identified set out on page 125;
- Directors' explanation as to its assessment of the company's prospects, the period this assessment covers and why the period is appropriate set out on pages 59 to 61;
- Directors' statement on fair, balanced and understandable set out on page 88;
- Board's confirmation that it has carried out a robust assessment of the emerging and principal risks set out on page 47;
- The section of the annual report that describes the review of effectiveness of risk management and internal control systems set out on page 43; and;
- The section describing the work of the audit committee set out on pages 83 to 89.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 129, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors 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 directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

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 economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the company and management.

Our approach was as follows:

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the company and determined that the most significant are:
 - Companies Act 2006
 - Financial Reporting Council (FRC) and the UK Corporate Governance Code
 - Tax legislation (governed by HM Revenue & Customs)
 - Health and Safety legislation
 - Environment Agency environmental permits
 - Ofwat regulations
- We understood how South West Water Limited is complying with those frameworks by reading internal policies and codes of conduct and assessing the entity level control environment, including the level of oversight of those charged with governance. We made enquiries of the company's legal counsel, regulatory team and internal audit of known instances of non-compliance or suspected non-compliance with laws and regulations. We corroborated our enquiries through review of correspondence with

regulatory bodies. We designed our audit procedures to identify non-compliance with such laws and regulations identified in the paragraph above. As well as enquiry and attendance at meetings, our procedures involved a review of the reporting to the above committees and a review of board meetings and other committee minutes to identify any non-compliance with laws and regulations. Our procedures also involved journal entry testing, with a focus on journals meeting our defined risk criteria based on our understanding of the business.

- We assessed the susceptibility of the company's financial statements to material misstatement, including how fraud might occur by making enquiries of senior management, including the Chief Executive Officer, Chief Financial Officer, Head of Internal Audit and Audit Committee Chair. We planned our audit to identify risks of management override, tested higher risk journal entries and performed audit procedures to address the potential for management bias, particularly over areas involving significant estimation and judgement. Further discussion of our approach to address the identified risks of management override are set out in the key audit matters section of our report.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved making enquiries of key management and legal counsel, reviewing key policies, inspecting legal registers and correspondence with regulators and reading key management meeting minutes. We also completed procedures to conclude on the compliance of significant disclosures in the Annual Report and Accounts with the requirements of the relevant accounting standards, UK legislation and the company's voluntary compliance with the UK Corporate Governance Code.
- We communicated regularly with the component teams and attended key meetings with the component teams, management and legal counsel in order to identify and communicate any instances of non-compliance with laws and regulations.
- The company operates in the water sector which is highly regulated. As such the Senior Statutory Auditor reviewed the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of an expert where appropriate

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/auditorsresponsibilities>. This description forms part of our auditor's report.

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Christabel Cowling (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
Leeds
30th June 2021

INCOME STATEMENT

FOR THE YEAR ENDED 31 MARCH 2021

	Notes	Before non- underlying items 2021 £m	Non-underlying items (note 6) 2021 £m	Total 2021 £m	Before non- underlying items 2020 £m	Non-underlying items (note 6) 2020 £m	Total 2020 £m
Revenue	5	564.3	(20.5)	543.8	571.6	-	571.6
Operating costs	7						
Employment costs		(53.9)	(3.5)	(57.4)	(50.0)	(0.2)	(50.2)
Raw materials and consumables		(18.1)	-	(18.1)	(14.9)	-	(14.9)
Other operating expenses		(151.7)	-	(151.7)	(142.8)	(2.8)	(145.6)
Earnings before interest, tax, depreciation and amortisation		340.6	(24.0)	316.6	363.9	(3.0)	360.9
Depreciation and amortisation	7	(118.3)	-	(118.3)	(118.7)	-	(118.7)
Operating profit		222.3	(24.0)	198.3	245.2	(3.0)	242.2
Finance income	8	0.7	-	0.7	2.3	-	2.3
Finance costs	8	(57.2)	-	(57.2)	(73.4)	-	(73.4)
Net finance costs		(56.5)	-	(56.5)	(71.1)	-	(71.1)
Profit before tax		165.8	(24.0)	141.8	174.1	(3.0)	171.1
Taxation (charge)/credit	9	(31.6)	4.6	(27.0)	(34.7)	(28.3)	(63.0)
Profit/(loss) for the year		134.2	(19.4)	114.8	139.4	(31.3)	108.1

The notes on pages 146 to 177 form part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 MARCH 2021

	Notes	Before non- underlying items 2021 £m	Non-underlying items (note 6) 2021 £m	Total 2021 £m	Before non- underlying items 2020 £m	Non-underlying items (note 6) 2020 £m	Total 2020 £m
Profit /(loss) for the year		134.2	(19.4)	114.8	139.4	(31.3)	108.1
Other comprehensive income/(loss)							
Items which will not be reclassified to profit or loss							
Re-measurement of defined benefit obligations	24	13.9	-	13.9	2.7	-	2.7
Income tax on items that will not be reclassified	9, 26	(2.6)	-	(2.6)	1.6	-	1.6
Total items that will not be reclassified to profit or loss		11.3	-	11.3	4.3	-	4.3
Items that may be reclassified subsequently to profit or loss							
Cash flow hedges		8.9	-	8.9	(11.2)	-	(11.2)
Income tax credit on items that may be reclassified	9, 26	(1.6)	-	(1.6)	2.5	-	2.5
Total items that may be reclassified subsequently to profit or loss		7.3	-	7.3	(8.7)	-	(8.7)
Other comprehensive Income for the year net of tax		18.6	-	18.6	(4.4)	-	(4.4)
Total comprehensive income for the year		152.8	(19.4)	133.4	135.0	(31.3)	103.7

The notes on pages 146 to 177 form part of these financial statements.

BALANCE SHEET

AS AT 31 MARCH 2021

	Notes	2021 £m	2020 £m
Assets			
Non-current assets			
Property, plant and equipment	13	3,138.8	3,089.0
Goodwill	14	51.3	51.3
Derivative financial instruments	19	1.5	-
Investment in subsidiary undertakings	16	3.3	3.3
Retirement benefit asset	24	14.3	7.1
		3,209.2	3,150.7
Current assets			
Inventories	17	5.4	4.9
Derivative financial instruments	19	0.2	-
Trade and other receivables	18	164.3	145.2
Current tax asset	25	3.9	3.4
Cash and cash deposits	20	414.9	284.1
		588.7	437.6
Liabilities			
Current liabilities			
Borrowings	22	(91.5)	(57.9)
Derivative financial instruments	19	(6.1)	(6.2)
Trade and other payables	21	(159.1)	(85.5)
Provisions	27	(0.3)	(0.6)
		(257.0)	(150.2)
Net current assets			
		331.7	287.4
Non-current liabilities			
Borrowings	22	(2,597.0)	(2,533.4)
Other non-current liabilities	23	(128.2)	(122.9)
Derivative financial instruments	19	(17.4)	(24.4)
Deferred tax liabilities	26	(271.2)	(263.8)
		(3,013.8)	(2,944.5)
Net assets			
		527.1	493.6
Equity			
Called up share capital	28	250.9	250.9
Retained earnings and other reserves	30	276.2	242.7
Total Equity		527.1	493.6

The notes on pages 146 to 177 form part of these financial statements.

The financial statements on pages 141 to 177 were approved and authorised for issue by the Board of Directors on 30th June 2021 and were signed on its behalf by:

S Davy
Chief Executive Officer

Registered office: Peninsula House, Rydon Lane, Exeter, Devon, England EX2 7HR
Registered Number: 02366665

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 MARCH 2021

	Notes	Called up share capital (note 28) £m	Retained earnings and other reserves (note 30) £m	Total Equity £m
At 31 March 2019		250.9	389.2	640.1
Opening adjustment on adoption of IFRS 16		-	(1.8)	(1.8)
At 1 April 2019 (adjusted for IFRS 16)		250.9	387.4	638.3
Profit for the year		-	108.1	108.1
Other comprehensive income for the year		-	(4.4)	(4.4)
Total comprehensive income for the year		-	103.7	103.7
<i>Transactions with owners</i>				
Dividends paid	10	-	(249.7)	(249.7)
Share based payments (net of tax)		-	1.3	1.3
Total transactions with owners		-	(248.4)	(248.4)
At 31 March 2020		250.9	242.7	493.6
Profit for the year		-	114.8	114.8
Other comprehensive income for the year		-	18.6	18.6
Total comprehensive income for the year		-	133.4	133.4
<i>Transactions with owners</i>				
Dividends paid	10	-	(43.5)	(43.5)
Dividends deferred	10	-	(58.1)	(58.1)
Share based payments (net of tax)		-	0.5	0.5
Watershare+ reserves adjustment		-	1.2	1.2
Total transactions with owners		-	(99.9)	(99.9)
At 31 March 2021		250.9	276.2	527.1

The notes on pages 146 to 177 form part of these financial statements.

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 MARCH 2021

	Notes	2021 £m	2020 £m
Cash flows from operating activities			
Cash generated from operations	31	314.6	319.1
Interest paid		(46.3)	(58.3)
Tax paid		(24.7)	(43.6)
Net cash generated from operating activities		243.6	217.2
Cash flows from investing activities			
Interest received		0.2	0.6
Purchase of property, plant and equipment		(161.1)	(172.2)
Receipt of grants and contributions		3.3	3.6
Proceeds from sale of property, plant and equipment		0.2	0.6
Net cash used in investing activities		(157.4)	(167.4)
Cash flows from/(used in) financing activities			
Deposit of restricted funds	20	(24.3)	(21.5)
Proceeds from new borrowing		130.0	241.5
Repayment of borrowings		(35.0)	(35.0)
Repayments of intercompany borrowings		(3.7)	(50.0)
Finance lease sale and lease back		15.0	115.0
Finance lease principal repayments		(18.8)	(118.7)
Dividends paid	10	(43.5)	(249.7)
Net cash used in financing activities		19.7	(118.4)
Net increase/(decrease) in cash and cash equivalents		105.9	(68.6)
Cash and cash equivalents at beginning of the year		58.2	126.8
Cash and cash equivalents at end of the year	20	164.1	58.2

The notes on pages 146 to 177 form part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. GENERAL INFORMATION

South West Water Limited is a company registered in the United Kingdom under the Companies Act 2006. The address of the registered office, the nature of the Company's operations and its principal activities are set out on page 122.

2. PRINCIPAL ACCOUNTING POLICIES

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

(a) Basis of preparation

These financial statements have been prepared on the historical cost accounting basis (except for fair value items, principally transfers of assets from customers and certain financial instruments as described in accounting policy note (u) and (n) respectively and in accordance with International Financial Reporting Standards (IFRS) in conformity with the requirements of the Companies Act 2006. A summary of the principal accounting policies is set out below, together with an explanation where changes have been made to previous policies on the adoption of new accounting standards and interpretations in the year.

The going concern basis has been adopted in preparing the financial statements as stated by the Directors on page 123. At 31 March 2021, the Company had access to undrawn committed funds and cash and cash deposits totalling £389.0 million (£293.2 million excluding restricted cash). Having considered the Company's strong funding position and prudent financial projections, which take into account a range of possible impacts, as described in this report, from the COVID-19 pandemic, the Directors have a reasonable expectation that the Company has adequate resource to continue in operational existence for a period of at least 12 months from the date of approval of the financial statements and that there are no material uncertainties to disclose. For this reason they continue to adopt the going concern basis in preparing the financial statements.

New standards or interpretations which were mandatory for the first time in the year beginning 1 April 2020 did not have a material impact on the net assets or results of the Group. Although the IASB's interest rate benchmark reform amendments IFRS 7 'Financial Instrument (FI) disclosures' and IFRS 9 'FI recognition and measurement' came into effect from 1 January 2020, these had already been early adopted by the Group in its 2020 financial statements as explained in the accounting policy for financial instruments.

New standards or interpretations due to be adopted from 1 April 2021 are not expected to have a material impact on the Group's net assets or results. Existing borrowing covenants are not impacted by changes in accounting standards.

(b) Exemption from consolidation

The Company is exempt under the provisions of section 400 of the Companies Act 2006 from the requirement to produce group financial statements as it is a wholly-owned subsidiary of Pennon Group plc which is registered within the European Economic Area and which itself produces consolidated financial statements. Accordingly consolidated financial statements have not been prepared and the financial information presented is for the Company as an individual undertaking. Group financial statements are included in the Annual Report of Pennon Group plc which is available from Peninsula House, Rydon Lane, Exeter, EX2 7HR.

(c) Revenue recognition

Revenue is recognised following delivery of performance obligation and an assessment of when control over the product or service is transferred to the customer. Revenue is only recognised when collection of consideration is highly probable.

Revenue is recognised either when the performance obligation in the contract has been performed (point in time) or 'over time' as the performance obligations to the customer are satisfied. For each obligation satisfied over time, the Company applies a revenue recognition method that accurately reflects performance in transferring control to the customer.

Where a contract with a customer includes more than one performance obligation, revenue is allocated to each obligation in proportion to a fair value assessment of the total contract sales value split across the services provided.

At the inception of a contract, the total transaction price is estimated, being the fair value to which the Company expects to be entitled under the contract, including any variable consideration. Variable consideration is based on the most likely outcome of the performance obligations.

Revenue excludes value added tax, trade discounts and revenue arising from transactions between Group companies.

For most of the services provided to domestic customers, contract terms are implied through statute and regulation in the absence of formal, written contracts. South West Water has a duty under legislation to provide domestic customers with services regardless of payment and is not permitted to disconnect domestic customers for non-payment of bills. Charges are set via the periodic review price-setting process, regulated by Ofwat.

In respect of ongoing, continuous services to customers, such as the provision of drinking water and wastewater services, revenue is recognised over time in line with customer usage of those services.

2. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

(c) Revenue recognition (continued)

Customers with an unmeasured supply are billed at the start of the year for the full amount of the annual charge but typically take advantage of a choice of payment arrangements to pay by regular instalments.

Customers with a metered supply are sent up to four bills per year, based either on actual meter readings or estimated usage. For these customers, revenue includes an estimation of the amount of unbilled usage at the period end. Payment options for domestic customers include an annual Meter Payment Plan where customers agree to pay a fixed amount per month which is adjusted to reflect actual consumption at the end of the year.

A range of regulated services is offered to property developers and owners who require connection to the water and sewerage networks or need the networks to be extended or altered. Typically, these customers pay an estimate of the charges in advance as a deposit, which is treated as a contract liability and are billed or refunded the difference between the estimate and actual costs on completion of the work.

Where the performance obligation relates solely to a connection to the network, revenue is recognised at the point of connection when the customer is deemed to obtain control.

Where assets are constructed or provided by the Company or assets transferred to the Company, it is considered that there is an explicit or implied performance obligation to provide an ongoing water and / or wastewater service, with the result that revenue is recognised over a time no longer than the economic life of assets provided by or transferred to the Company.

Contract assets and liabilities

A trade receivable is recognised when the Company has an unconditional right to receive consideration in exchange for performance obligations already fulfilled. A contract asset is recognised when the Company has fulfilled some of its performance obligations but has not yet obtained an unconditional right to receive consideration. The amounts of contract assets is disclosed within note 18 (Trade and other receivables - current) if applicable. A contract liability is recognised when consideration is received in advance of the Company performing its performance obligations to customers, including, when appropriate, transfers of assets from customers (per paragraph (u) below). The value of contract liabilities is disclosed within note 21 (Trade and other payables - current) and note 23 (Other non-current liabilities) as appropriate.

(d) Segmental reporting

The Directors believe that the whole of the Company's activities constitute one single segment. Operating segments are reported in the manner consistent with internal reporting to the Chief Operating Decision Maker, which has been identified as the Board of Directors.

The Company's country of domicile is the United Kingdom and is the country in which it generates all of its revenue. The Company's non-current assets are all located within the United Kingdom.

In accordance with IFRS 15, revenue has been disaggregated based on the services of supplying clean water, removal and treatment of wastewater and retail and other services. Further details are contained in note 5.

(e) Goodwill

Goodwill arising on consolidation from the acquisition of subsidiary undertakings represents the excess of the purchase consideration over the fair value of net assets acquired, less any subsequent impairment charges.

Goodwill is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed. For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash generating units (CGUs) or group of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal reporting purposes. Goodwill is allocated and monitored at the reportable operating segment level. Further details are contained in accounting policy (i).

When a subsidiary undertaking is sold, the profit or loss on disposal is determined after including the attributable amount of goodwill.

(f) Other intangible assets

Other intangible assets include assets acquired in a business combination and are capitalised at fair value at the date of acquisition. Following initial recognition, finite life intangible assets are amortised on a straight-line basis over their estimated useful lives, with the expense charged to the income statement through operating costs.

(g) Property, plant and equipment

Infrastructure assets were included at fair value on transition to IFRS and subsequent additions at cost, less accumulated depreciation. Expenditure to increase capacity or enhance infrastructure assets is capitalised where it can be reliably measured and it is probable that incremental future economic benefits will flow to the Company. The cost of day to day servicing of infrastructure components is recognised in the income statement as it arises.

2. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

(g) Property, plant and equipment (continued)

Infrastructure assets are depreciated evenly over their estimated useful economic lives and are principally:

Dams and impounding reservoirs	200 years
Water mains	40 – 120 years
Sewers	40 – 120 years

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

ii) Other assets (including property, overground plant and equipment)

Other assets are included at cost less accumulated depreciation.

Freehold land is not depreciated. Other assets are depreciated evenly over their estimated useful economic lives to their residual value and are principally:

Land and buildings - freehold buildings	30 – 60 years
Land and buildings - leasehold buildings	Over the estimated useful life or the finance lease period, whichever is shorter
Operational properties	40 – 80 years
Fixed plant	20 – 40 years
Vehicles, mobile plant and computers	4 – 10 years

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

The cost of assets includes directly attributable labour and overhead costs which are incremental to the Company. Borrowing costs directly attributable to the construction of a qualifying asset (an asset necessarily taking a substantial period of time to be prepared for its intended use) are capitalised as part of the asset. Assets transferred from customers are recognised at fair value as set out in accounting policy (u).

The assets residual value and useful lives are reviewed annually.

Gains or losses on disposals are determined by comparing the proceeds of sale with the carrying amount and are recognised within the income statement.

(h) Leased assets

All are accounted for by recognising a right-of-use-asset and a lease liability except for:

- Low value assets; and
- Leases with a duration of 12 months or less.

Contracts are initially measured at the present value of contractual payments due to the lessor over the lease term, with the discount rate determined by reference to the rate inherent in the lease unless this is not readily determinable, in which case the Group's incremental borrowing rate on commencement of the lease is used. After initial measurement, lease payments are allocated between the liability and finance cost. The finance cost is charged to profit and loss over the lease period to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The interest element of cash payments in respect of these leases is included within interest payments in determining net cash generated from operating activities. The capital element of the cash payment is included within cash flows from financing activities. Right-of-use assets are amortised on a straight line basis over the remaining term of the lease or the remaining economic life of the asset if shorter. When the Group revisits its estimate of lease term (because, for example, it reassesses an extension option), it adjusts the carrying amount of the lease liability to reflect the payments to make over the revised term, which is discounted at the same discount rate that applied on lease commencement. In these circumstances an equivalent adjustment is made to the carrying value of the right-of-use asset, with the revised carrying amount being amortised over the remaining (revised) lease term.

Assets are included as property, plant and equipment as right-of-use assets at the lower of their fair value at commencement or the present value of the minimum lease payments and are depreciated over their estimated economic lives or the finance lease period, whichever is the shorter. The corresponding liability is recorded as borrowings. The interest element of the rental costs is charged against profits using the actuarial method over the period of the lease.

The Company regularly uses sale and lease back transactions to finance its capital programme. A sale and leaseback transaction is where the Company sells an asset and immediately reacquires the use of the asset by entering into a lease with the buyer. Each transaction is assessed as to whether it meets the criteria within IFRS 15 'Revenue from contracts with customers' for a sale to have occurred. As a result, a lease liability is recognised, the associated property, plant and equipment asset is derecognised, and a right-of-use asset is recognised at the proportion of the carrying value relating to the right retained. Any gain or loss arising relates to the rights transferred to the buyer.

2. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

(i) Impairment of non-financial assets

Assets with an indefinite useful life are not subject to amortisation and are tested annually for impairment, or whenever events or changes in circumstance indicate that the carrying amount may not be recoverable.

Assets subject to amortisation or depreciation are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which an asset's carrying amount exceeds its recoverable value. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (CGUs). Value in use represents the present value of projected future cash flows expected to be derived from a CGU, discounted using a pre-tax discount rate which reflects an assessment of the market cost of capital of the CGU. Impairments are charged to the income statement in the year in which they arise.

(j) Grants and contributions

Grants and contributions receivable in respect of property, plant and equipment are deducted from the cost of those assets. Grants and contributions receivable in respect of expenditure charged against profits in the year have been included in the income statement.

(k) Investment in subsidiary undertakings

Investments in subsidiary undertakings are initially recorded at cost, being the fair value of the consideration paid, including associated acquisition costs. Subsequently, investments are reviewed for impairment on an individual basis annually or if events or changes in circumstances indicate that the carrying value may not be fully recoverable.

(l) Inventories

Inventories are stated at the lower of cost and net realisable value. The cost of finished goods and work in progress includes raw materials and the cost of bringing stocks to their present location and condition. It excludes borrowing costs. Net realisable value is the estimated selling price less cost to sell. The costs of items of inventory are determined using weighted average costs.

(m) Cash and cash deposits

Cash and cash deposits comprise cash in hand and short-term deposits held at banks. Bank overdrafts are shown within current borrowings.

(n) Financial instruments

Financial instruments are recognised and measured in accordance with IFRS 9. The Company classifies its financial instruments in the following categories:

i) Debt instruments at amortised cost

All loans and borrowings are initially recognised at fair value, net of transaction costs incurred. Following initial recognition interest-bearing loans and borrowings are subsequently stated at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when the instruments are derecognised or impaired. Premia, discounts and other costs and fees are recognised in the income statement through amortisation.

Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

ii) Trade receivables

Trade receivables do not carry any interest receivable and are recognised initially at fair value and subsequently at amortised cost using the effective interest method, less provision for expected credit losses (ECLs). In accordance with the terms and conditions of IFRS 9, the Company performs an impairment analysis at each reporting date to measure the ECLs. The Company does not track changes in credit risk but instead recognises a loss allowance based on lifetime ECLs at each reporting date. The Company has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the receivables and the economic environment.

iii) Receivables due from fellow subsidiary undertakings

Amounts owed by fellow subsidiaries are classified and recorded at amortised cost and reduced by allowances for ECLs. Estimated future credit losses are first recorded on initial recognition of a receivable and are based on estimated probability of default. Individual balances are written off when management deems them not to be collectible.

iv) Trade payables

Trade payables are not interest-bearing and are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

(n) Financial instruments (continued)

v) Derivative financial instruments and hedging activities

The Company uses derivative financial instruments, principally interest rate swaps, to hedge risks associated with interest rate and exchange rate fluctuations. Derivative instruments are initially recognised at fair value on the date the derivative contract is entered into and subsequently remeasured at fair value for the reported balance sheet.

The Company designates certain hedging derivatives as either:

- a hedge of a highly probable forecast transaction or change in the cash flows of a recognised asset or liability (a cash flow hedge); or
- a hedge of the exposure to change in the fair value of a recognised asset or liability (a fair value hedge).

The gain or loss on re-measurement is taken to the income statement except for cash flow hedges which meet the conditions for hedge accounting, when the portion of the gain or loss on the hedging instrument which is determined to be an effective hedge is recognised directly in equity, and the ineffective portion in the income statement. The gains or losses deferred in equity in this way are subsequently recognised in the income statement in the same period in which the hedged underlying transaction or firm commitment is recognised in the income statement.

To qualify for hedge accounting, the Company is required to document in advance the relationship between the item being hedged and the hedging instrument. The Company is also required to document and demonstrate an assessment of the relationship between the hedged item and the hedging instrument which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed at the end of each reporting period to ensure that the hedge remains highly effective.

The full fair value of a hedging derivative is apportioned on a straight-line basis between non-current and current assets or liabilities based on the remaining maturity of the hedging derivative.

Derivative financial instruments deemed held for trading which do not qualify for hedge accounting are classified as a current asset or liability with any change in fair value recognised immediately in the income statement.

The Company uses cross-currency swaps for some of its foreign currency denominated private placement borrowings. The swaps either have the effect of (i) converting variable rate foreign currency borrowings into fixed rate sterling borrowings, (ii) converting fixed rate foreign currency borrowings into fixed rate sterling borrowings, or (iii) converting fixed rate foreign currency borrowings into floating rate sterling borrowings.

In January 2020, the IASB's interest rate benchmark reform amendments to IFRS 7 'Financial Instrument (FI) disclosures' and to IFRS 9 'FI recognition and measurement' (the 'Phase 1 amendments') were endorsed by the EU. The amendments modify hedge accounting requirements to allow hedge accounting to continue for affected hedges during the period of uncertainty before the hedged items or hedging instruments are affected when current interest rate benchmarks are amended due to the ongoing interest rate benchmark reforms. The Company chose to early adopt the Phase 1 amendments, which are mandatory for annual reporting periods commencing after 1 January 2020, for its reporting period ended 31 March 2020.

The Phase 1 amendments are relevant to the Company given that it applies hedge accounting to its benchmark interest rate exposures.

The application of the Phase 1 amendments impacts the Company's accounting policies in the following ways:

The Company has floating rate debt, linked to the UK's benchmark rate GBP London Inter-Bank Offered Rate (GBP LIBOR), which it fixes through cash flow hedges using interest rate swaps. The Phase 1 amendments permit continuation of hedge accounting even though there is uncertainty about the timing and amount of the hedged cash flows due to the interest rate benchmark reforms.

The Company uses cross-currency interest rate swaps to hedge the foreign currency risk, where applicable, within its financial instruments. The Phase 1 amendments permit continuation of hedge accounting even though there is uncertainty about the replacement of the floating interest rates included in its cross-currency interest rate swaps.

The Company will retain the cumulative gain or loss in the hedging reserve for designated cash flow hedges that are subject to interest rate benchmark reforms even though there is uncertainty arising from the reform with respect to the timing and amount of the cash flows of the hedged items. If the hedged future cash flows are no longer expected to occur due to reasons other than interest rate benchmark reform, the cumulative gain or loss will be immediately reclassified to profit or loss.

The IASB published its Phase 2 amendments on interest rate benchmark reform in August 2020. These amendments deal with issues that might arise during the reform of an interest rate benchmark. The Phase 2 amendments are applicable to periods commencing after 1 January 2021, with early adoption permitted. The Company will adopt the Phase 2 amendments at the appropriate time.

2. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

(o) Taxation including deferred tax

The tax charge for the year comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in the statement of comprehensive income or directly in equity. In this case the tax is also recognised in the statement of comprehensive income or directly in equity as appropriate.

Current tax is calculated on the basis of tax laws enacted or substantively enacted at the balance sheet date. Management periodically evaluates tax items subject to interpretation and establishes provisions on individual tax items, where in the judgement of management, the position is uncertain.

The Company is part of the Pennon Group for tax purposes and accordingly may use the tax group relief provisions whereby current tax liabilities can be offset by current tax losses arising in other Group companies. Payments for group relief are included within the current tax disclosures.

Deferred tax is provided in full on temporary differences between the carrying amount of assets and liabilities in the financial statements and the tax base, except where they arise from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the assets can be realised. Deferred tax is determined using the tax rates enacted or substantively enacted at the balance sheet date, and expected to apply when the deferred tax liability is settled or the deferred tax asset is realised.

(p) Provisions

Provisions are made where there is a present legal or constructive obligation as a result of a past event and it is probable that there will be an outflow of economic benefits to settle this obligation and a reliable estimate of this amount can be made. Where the effect of the time value of money is material, the current amount of a provision is the present value of the expenditures expected to be required to settle obligations. The unwinding of the discount to present value is included as notional interest within finance costs.

Provisions for restructuring costs are recognised when a detailed formal plan for the restructuring has been communicated to affected parties.

(q) Contingent liabilities

The Company is subject to litigation from time to time as a result of its activities. The Company establishes provisions in connection with litigation where it has a present legal or constructive obligation as a result of past events and where it is more likely than not an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

There are contingent liabilities that arise in the normal course of business which, if realised, are not expected to result in a material liability to the Company.

(r) Dividend distributions

Dividend distributions are recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholder. Interim dividends are recognised when paid; final dividends when approved by the shareholder at the Annual General Meeting.

(s) Employee benefits

i) Retirement benefit obligations

The Company operates defined benefit and defined contribution pension schemes through its parent company.

Defined benefit pension schemes

The liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the year less the fair value of plan assets. If the value of the plans assets exceeds the present value of its obligations, the resulting surplus is only realised if the Company has an unconditional right to that surplus.

The defined benefit obligation is calculated by independent actuaries who advise on the selection of Directors' best estimates, using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high quality corporate bonds, and that have terms to maturity approximating to the terms of the related pension obligation. The increase in liabilities of the Company's defined benefit pension schemes, expected to arise from employee service in the year, is charged against operating profit.

Changes in benefits granted by the employer are recognised immediately as past service cost in the income statement.

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

Defined contribution scheme

Costs of the defined contribution pension scheme are charged to the income statement in the period in which they arise. The Company has no further payment obligations once the contributions have been paid.

2. PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

ii) Share-based payment

The Company participates in a number of equity-settled share-based payment plans for employees operated by its parent company Pennon Group plc. The fair value of the employee services acquired in exchange for the grant is recognised as an expense over the vesting period of the grant.

Fair values are calculated using an appropriate pricing model. Non market-based vesting conditions are adjusted for in assumptions as to the number of shares which are expected to vest.

At each balance sheet date, the Company revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to equity.

(t) Fair values

The fair value of the interest rate swaps is based on the market price to transfer the asset or liability at the balance sheet date in an ordinary transaction between market participants.

The fair values of short-term deposits, loans and overdrafts with a maturity of less than one year are assumed to approximate to their book values. In the case of non-current bank loans and other loans, the fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate available to the Company for similar financial instruments.

(u) Transfers of assets from customers

Where an item of property, plant and equipment that must be used to connect customers to the network is received from a customer, or where cash is received from a customer for the acquisition or construction of such an item, that asset is recorded and measured on initial recognition at its fair value. The credit created by the recognition of the asset is recognised as a contract liability on the balance sheet. The contract liability reduces and revenue is recognised in the income statement as the performance obligations are satisfied. The period over which the credit is recognised depends upon the nature of the service provided, as determined by the agreement with the customer. Where the service provided is solely a connection to the network, the credit is recognised at the point of connection. If the agreement does not specify a period, revenue is recognised over a period no longer than the economic life of the transferred asset used to provide the ongoing service.

The fair value of assets on transfer from customers is determined using a cost valuation approach allowing for depreciation.

(v) Non-underlying items

Non-underlying items are those that in the Directors' view should be separately disclosed by virtue of their size, nature or incidence to enable a full understanding of the Company's financial performance.

3. FINANCIAL RISK MANAGEMENT

(a) Financial risk factors

The Company's activities expose it to a variety of financial risks; market risk (interest rate risk), liquidity risk and credit risk.

The Company receives treasury services from the treasury function of Pennon Group plc, the parent company, which seeks to ensure that sufficient funding is available to meet foreseeable needs and to maintain reasonable headroom for contingencies and manages inflation and interest rate risk.

The principal financial risks faced by the Company relate to interest rate and credit counterparty risk.

These risks and treasury operations are managed in accordance with policies established by the Board. Major transactions are individually approved by the Board. Treasury activities are reported to the Board and are subject to review by internal audit.

Financial instruments are used to raise finance, manage risk, optimise the use of surplus funds and manage overall interest rate performance. The Company does not engage in speculative activity.

i) Liquidity risk

The Company actively maintains a mixture of long-term and short-term committed facilities which are designed to ensure the Company has sufficient available funds for operations and planned expansions equivalent to at least one year's forecast requirements at all times. Details of undrawn committed facilities and short-term uncommitted facilities are provided in note 22.

The Company has entered into covenants with lenders. While terms vary, these typically provide for limits on gearing (primarily based on the business's regulatory capital value and unregulated EBITDA plus interest receivable on service concession arrangements) and interest cover. Existing covenants are not impacted by subsequent changes to accounting standards.

3. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial risk factors (continued)

Contractual undiscounted cash flows including interest payments, at the balance sheet date were:

31 March 2021

	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 5 years £m	Over 5 years £m	Total £m
Non-derivative financial liabilities					
Borrowings excluding finance lease liabilities	40.1	40.2	135.8	965.2	1,181.3
Interest payments on borrowings	26.7	28.3	89.4	595.7	740.1
Lease liabilities including interest	55.3	37.8	267.3	1,543.1	1,903.5
Trade and other payables	159.1	-	-	-	159.1
Derivative financial liabilities					
Derivative contracts – net payments	9.3	6.7	3.9	(2.4)	17.5

31 March 2020

	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 5 years £m	Over 5 years £m	Total £m
Non-derivative financial liabilities					
Borrowings excluding finance lease liabilities	38.8	42.7	127.9	943.5	1,152.9
Interest payments on borrowings	27.7	27.0	78.9	564.5	698.1
Lease liabilities including interest	39.5	94.4	150.9	1,750.6	2,035.4
Trade and other payables	85.5	-	-	-	85.5
Derivative financial liabilities					
Derivative contracts – net payments	6.4	6.6	18.8	0.4	32.2

ii) Market risk

The Company has both interest bearing assets and interest bearing liabilities. The Company has a policy of maintaining, after the effect of interest rate swaps, at least 60% of interest bearing liabilities at fixed rates. At the year end, 63% (31 March 2020: 52%) of net borrowings were at fixed rates and 25% (31 March 2020: 25%) were index-linked. The Company uses a combination of fixed rate and index-linked borrowings and fixed rate interest swaps as cash flow hedges of future variable interest payments to achieve this policy. The notional principal amounts of the interest rate swaps are used to determine settlement under those swaps and are not, therefore, an exposure for the Company. These instruments are analysed in more detail in note 19.

The interest rate for index-linked debt is based upon a CPI or an RPI measure provides an approximation to the index used in determining the amount of income from customers.

The Company is primarily exposed to the UK's benchmark interest rate, GBP LIBOR, within its hedge accounting relationships, which are subject to interest rate benchmark reform.

The Company has closely monitored the market and the output from the various industry working groups managing the transition to new benchmark interest rates. The Financial Conduct Authority (FCA) has made clear that, at the end of 2021, it will no longer seek to persuade or compel, the banks to submit to LIBOR.

During 2019/20 the Company converted a LIBOR revolving credit facility (RCF) to a Sterling Overnight Index Average (SONIA) linked RCF, this was to address the documentary changes and allow the Company to test the changes in the Treasury management system. Further work continues to ensure the Company is well placed to amend the debt portfolio before the December 2021 transition, the Company has updated some of its documentation to include SONIA switch language and is looking now looking to address the derivative book.

Below are the details of the hedging instruments and hedged items in scope of the amendments to IFRS 7 and 9 due to interest rate benchmark reform, by hedge type. The terms of the hedged items listed match those of the corresponding hedging instruments.

3. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial risk factors (continued)

Hedge type	Instrument type	Maturing	Nominal £m	Hedged item
Cash flow hedges	Receive three-month UK benchmark rate (GBP LIBOR), pay GBP fixed interest rate swap	2024-2030	701	UK benchmark rate (GBP LIBOR) issued financial instruments of the same nominals as the swaps
	Receive six-month UK benchmark rate (GBP LIBOR), pay GBP fixed interest rate swap	2025	100	UK benchmark rate (GBP LIBOR) issued financial instruments of the same nominals as the swaps

The Company will continue to apply the amendments to IFRS 9 until the uncertainty arising from the interest rate benchmark reforms with respect to the timing and the amount of the underlying cash flows that the Company is exposed ends. The Company has assumed that this uncertainty will not end until alternate language has been agreed with the counterparties and is dependent on the outcome of the introduction of fallback provisions and the clauses negotiated with lenders.

The Company has no significant interest-bearing assets upon which the net return fluctuates from market risk. Deposit interest receivable is expected to fluctuate in line with interest payable on floating rate borrowings. Consequently the Company's income and cash generated from operations (note 31) are independent of changes in market interest rates.

For 2021 if interest rates on variable net borrowings had been on average 0.5% higher/lower with all other variables held constant, post-tax profit for the year and equity would have increased/decreased by £1.9 million (2020: £0.6 million), for the equity sensitivity fair value, derivative impacts are excluded.

For 2021 if RPI on index-linked borrowings had been on average 0.5% higher/lower with all other variables held constant, post-tax profit for the year and equity would have decreased/ increased by £2.0 million (2020: £2.0 million).

iii) Credit risk

Credit counterparty risk arises from cash and cash deposits, derivative financial instruments and exposure to customers, including outstanding receivables. Further information on the credit risk relating to trade and other receivables is given in note 18.

Counterparty risk arises from the investment of surplus funds and from the use of derivative financial instruments. The Board has agreed a policy for managing such risk, which is controlled through credit limits, counterparty approvals, and rigorous monitoring procedures.

The Company has no other significant concentration of credit risk. Surplus funds of the Company are usually placed in short-term fixed interest deposits or the overnight money markets. Deposit counterparties must meet a board approved minimum criteria based on their short-term credit rating.

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to minimise the cost of capital.

The Company's policy is to have a minimum of 12 months pre-funding of projected capital expenditure. At 31 March 2021 the Company had cash and committed facilities excluding restricted funds of £389 million (31 March 2020: £293 million), meeting this objective.

The Company monitors capital on the basis of the gearing ratio, which is calculated as net borrowings divided by total capital. Net borrowings is analysed in note 32 and is calculated as total borrowings less cash and cash deposits. Total capital is calculated as equity plus net borrowings.

(b) Capital risk management

The gearing ratios at the balance sheet date were:

	Note	2021 £m	2020 £m
Net borrowings	32	2,273.6	2,307.2
Total equity		527.1	493.6
Total capital		2,800.7	2,800.8
Gearing Ratio		81.2%	82.4%

Consistent with the industry peer group, the Company is also monitored on the basis of the ratio of its net debt to Regulated Capital Value (RCV). South West Water's net debt to RCV has increased to 67.1%. Ofwat's notional gearing target for the K7 (2020-25) regulatory period is set at 60.0%.

3. FINANCIAL RISK MANAGEMENT (CONTINUED)

(b) Capital risk management (continued)

	Note	2021 £m	2020 £m
Regulatory Capital Value		3,387.5	3,572.5
Net borrowings	32	2,273.6	2,307.2
Net borrowings / Regulatory Capital Value		67.1%	64.6%

The Company has entered into covenants with lenders and, whilst terms vary, these typically provide for limits on gearing and interest cover. The Company has been in compliance with its covenants during the year. Existing covenants are not impacted by subsequent changes to accounting standards.

(c) Determination of fair values

The Company uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

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

The Company's financial instruments are valued principally using level 2 measures as analysed in note 19.

The fair value of financial instruments traded in active markets (such as trading and available-for-sale securities) is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Company is the current bid price.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. A variety of methods and assumptions are used based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values.

4. CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES

The Company's principal accounting policies are set out in note 2. Management is required to exercise significant judgement and make use of estimates and assumptions in the application of these policies. Estimates are based on factors including historical experience and expectations of future events that management believe to be reasonable. However, given the judgemental nature of such estimates, actual results could be different from the assumptions used:

Estimates

Provision for expected credit losses

The Company has a material level of exposure to collection of trade receivables. Provisions in respect of these balances are calculated based on assumptions of historical credit loss experience, adjusted for forward-looking factors which by their nature are subject to uncertainty. Analysis of actual recovery compared with provisioning levels have not, to date, resulted in material variances.

Under its regular review procedures, at the balance sheet date, the Company applies a simplified approach in calculating expected credit losses (ECLs) for trade receivables and contract assets. Therefore, the Company does not track changes in credit risk but instead recognises a loss allowance based on lifetime ECLs at each reporting date. South West Water has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the receivables and the economic environment.

In the prior year, at the onset of the COVID-19 pandemic, an additional assessment of ECLs was focused on the potential impact from the pandemic. Considerations in this assessment have included the type of customers, whether they conduct essential business operations, are linked to central or regional government and past experience of behaviours in challenging economic times. This additional level of assessment continues. The precise quantum of the impact of the pandemic on both the Company's business and household customers remains uncertain as the Group's assessment anticipates that the ongoing financial support from government will potentially delay the full impact on expected credit losses.

4. CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES (CONTINUED)

Provision for expected credit losses (continued)

The actual level of debt collected may differ from the estimated levels of recovery. As at 31 March 2021 the Company's current trade receivables were £216.2 million (2020: £208.4 million), against which £88.4 million (2020: £91.6 million) had been provided for ECLs (note 18). The provision for ECLs includes a non-underlying charge of £nil (2020: £2.8 million) in relation to the impact of COVID-19. The additional amounts provided in the previous year continue to be required based on the Group's ongoing assessment of the impact of the pandemic.

Retirement benefit obligations

The Company operates defined benefit pension schemes, through its parent company, for which actuarial valuations are carried out as determined by the trustees at intervals of not more than three years. The most recent triennial valuation of the main scheme was as at 31 March 2019.

The pension cost and liabilities under IAS 19 are assessed in accordance with Directors' best estimates using the advice of an independent qualified actuary and assumptions in the latest actuarial valuation. The assumptions are based on member data supplied to the actuary and market observations for interest rates and inflation, supplemented by discussions between the actuary and management. The mortality assumption uses a scheme-specific calculation based on CMI 2019 actuarial tables with an allowance for future longevity improvement. The principal assumptions used to measure schemes' liabilities, sensitivities to changes in those assumptions and future funding obligations are set out in note 24.

Judgements

Non-underlying items

In establishing which items are disclosed separately as non-underlying, to enable a full understanding of the Group's financial performance, the Directors exercise their judgement in assessing the size, nature or incidence of specific items. See note 6 for further details.

Other estimates

During the year, management reassessed the critical estimates and resolved that the level of estimation for revenue recognition of accrued revenue is still not considered critical as the estimates are largely calculated on a systematic basis and have not, to date, resulted in a material adjustment within the following 12-month period. However, management consider the total level of estimation of accrued revenue relating to water, waste and sale of electricity to be material and highlight this as a material other estimate.

Management have also concluded that taxation is no longer an area of critical estimation in preparation of the financial statements.

5. REVENUE

In accordance with IFRS 15, revenue has been disaggregated based on the services of supplying clean water, removal and treatment of wastewater and other services.

	2021 £m	2020 £m
Water	257.0	255.6
Wastewater	261.4	281.4
Other services	25.4	34.6
Total	543.8	571.6

6. NON-UNDERLYING ITEMS

Non-underlying items are those that in the Directors' view are required to be separately disclosed by virtue of their size or incidence to enable full understanding of the Company's financial performance in the year and business trends over time.

	Note	2021 £m	2020 £m
Revenue			
Watershare+ ¹		20.5	
Operating Costs			
Pension curtailment charge ²	24	3.5	-
Pensions past service cost ³	24	-	0.2
COVID-19 provision for expected credit losses ³		-	2.8
Earnings before interest, tax, depreciation and amortisation		24.0	3.0
Tax credit arising on non-underlying items	9	(4.6)	(0.6)
Deferred tax change in rate ⁴	9	-	28.9
Net non-underlying charge		19.4	31.3

6. NON-UNDERLYING ITEMS (CONTNUED)

1. In September 2020, the Group offered its WaterShare+ scheme to its customers whereby customers could choose to accept a credit on their bill or take shares in Pennon Group plc. The value of the rebate equates to £20 per customer and the total value of £20.5 million (2020 £nil) has been recognised in full as a non-underlying reduction to revenue. £19.3 million of the WaterShare+ credits were taken as credits on customers' bills, with the balance of £1.2 million being taken as shares in Pennon Group Plc. This item is non-underlying in nature given its individual size and its non-recurring nature.
2. Pennon Group completed its employee consultation to modernise its ongoing pension arrangements. The outcome of the consultation resulted in a decision to close Pennon's principal defined benefit pension scheme to future accrual with effect from 30 June 2021. This resulted in a curtailment charge for South West Water of £3.5 million (2020 Nil).
3. In 2020 £0.2 million of past service costs relating to the Defined Benefit pension scheme were classified as non-underlying due to their nature. In response to the COVID-19 pandemic a detailed expected credit loss review was undertaken in 2020. Economic and credit conditions were worsening, however the UK Government continued to implement economic measures to support the wider economy. As a result of the review, a provision of £2.8 million has been recognised. The charge is considered non-underlying due to its size and nature.
4. Following the Chancellor's budget on 11 March 2020, the UK headline corporation tax rate will remain at 19%. It was previously set to reduce to 17% from 1 April 2020 and that change has now been cancelled. All deferred tax assets and liabilities have therefore been recalculated to crystallise at 19%, resulting in a non-underlying deferred tax charge in the year of £28.9 million. The change was substantively enacted on 17 March 2020. This charge is considered non-underlying due to it arising from a material legislative change, and its treatment is consistent with that applied in relation to previous changes in the corporation tax rate.

7. OPERATING COSTS BEFORE NON-UNDERLYING ITEMS

	Note	2021 £m	2020 £m
Employment costs before non-underlying items	11	53.9	50.0
Raw materials and consumables		18.1	14.9
<i>Other operating expenses include</i>			
Profit on disposal of property, plant and equipment		(0.2)	(0.4)
<i>Operating lease rentals payable:</i>			
Short term/low value asset lease expense		1.4	1.1
Research and development expenditure		0.1	0.1
Provision for expected credit losses before non-underlying items	18	2.8	2.9
<i>Depreciation of property, plant and equipment:</i>			
Owned assets		86.6	72.3
Under leases		31.7	45.9
		<u>118.3</u>	<u>118.2</u>
Amortisation of other intangible assets		-	0.5
Total Depreciation		<u>118.3</u>	<u>118.7</u>

Fees payable to the Company's auditor's in the year were:

	2021 £000	2020 £000
Fees payable to the Company's auditors and its associates for the audit of the financial statements	307	233
Fees payable to the Company's auditors and its associates for other services:		
Audit related assurance	39	35
All other services	32	67
Total fees	<u>378</u>	<u>335</u>

Expenses reimbursed to the auditors in relation to the audit of the Company were £nil (2019/20: £15,000).

A description of the work of the Audit Committee is set out in its report on page 83 to 89 which includes an explanation of how the auditor's objectivity and independence are safeguarded when non-audit services are provided by the auditor's firm.

8. NET FINANCE COSTS

	Finance cost £m	2021 Finance income £m	Total £m	Finance cost £m	2020 Finance income £m	Total £m
Cost of servicing debt						
Bank borrowings and overdrafts	(13.9)	-	(13.9)	(17.0)	-	(17.0)
Interest element of finance lease rentals	(24.5)	-	(24.5)	(34.5)	-	(34.5)
Interest element of operating lease rentals	(1.2)	-	(1.2)	(1.2)	-	(1.2)
Other finance costs	(3.4)	-	(3.4)	(2.6)	-	(2.6)
Interest receivable	-	0.7	0.7	-	2.3	2.3
Intercompany interest to subsidiaries	(13.8)	-	(13.8)	(17.9)	-	(17.9)
Working capital adjustment	(56.8)	0.7	(56.1)	(73.2)	2.3	(70.9)
Notional interest						
Retirement benefit obligations (note 24)	(0.4)	-	(0.4)	(0.2)	-	(0.2)
Finance (costs)/income	(57.2)	0.7	(56.5)	(73.4)	2.3	(71.1)

In addition to the above, finance costs of £0.9 million (2019/20: £2.0 million) have been capitalised on qualifying assets included in property, plant and equipment.

9. TAXATION

	Before non- underlying items 2021 £m	Non- underlying items (note 6) 2021 £m	Total 2021 £m	Before non- underlying items 2020 £m	Non- underlying items (note 6) 2020 £m	Total 2020 £m
Analysis of charge in year						
Current year tax charge/(credit)	28.2	(3.9)	24.3	24.9	-	24.9
Deferred tax charge/(credit)	3.4	(0.7)	2.7	9.8	(0.6)	9.2
Deferred tax arising on change of rate of corporation tax	-	-	-	-	28.9	28.9
Total deferred tax charge/(credit)	3.4	(0.7)	2.7	9.8	28.3	38.1
Tax charge/(credit) for year	31.6	(4.6)	27.0	34.7	28.3	63.0

UK Corporation tax is calculated at 19% (2019/20 19%) of the estimated assessable profit for the year.

UK corporation tax is stated after a credit relating to prior year current tax of £0.2 million (2019/20 credit of £2.1m) and a prior year deferred tax charge of £0.3 million (2019/20 charge of £3.7 million).

The tax for the year differs from the theoretical amount that would arise using the standard rate of corporation tax in the UK of 19% (2019/20: 19%). The differences are explained below:

	2021 £m	2020 £m
Reconciliation of total tax charge		
Profit before tax	141.8	171.1
Profit before tax multiplied by the standard rate of corporation tax in the UK of 19% (2019/20: 19%)	26.9	32.5
<i>Effects of:</i>		
Expenses not deductible for tax purposes	-	0.3
Profit on the disposal of non-qualifying assets	-	(0.1)
Change in rate of corporation tax	-	28.9
Adjustments to tax charge in respect of prior years	0.1	1.6
Depreciation charged on non-qualifying assets	0.4	0.3
Other	(0.4)	(0.5)
Tax charge for year	27.0	63.0

9. TAXATION (CONTINUED)

The average effective tax rate excluding non-underlying items for the year was 19% (2019/20 20%).

The current tax charge for the year differs from the theoretical amount that would arise using the standard rate of corporation tax in the UK of 19% (2019/20: 19%). The differences are explained below:

	2021 £m	2020 £m
Reconciliation of current tax charge		
Profit before tax	141.8	171.1
Profit before tax multiplied by the standard rate of corporation tax in the UK of 19% (2019/20: 19%)	26.9	32.5
<i>Effects of:</i>		
Relief for capital allowances in place of depreciation	(21.4)	(21.6)
Disallowance of depreciation charged in the accounts	20.1	19.4
Expenses not deductible for tax purposes	-	0.2
Adjustments to tax charge in respect of prior years	(0.2)	(2.1)
Depreciation charged on non-qualifying assets	0.4	0.3
Relief for capitalised interest and foreign exchange gains/losses	(0.2)	(0.4)
Other timing differences	(1.3)	(3.4)
Current Tax charge for year	24.3	24.9

South West Water's current tax charge is lower than the UK headline rate of 19%, primarily due to the availability of capital allowances. Capital allowances provide tax relief when a business incurs expenditure on qualifying capital items such as plant and machinery used by the business. As an infrastructure business, these allowances help the Company to plan major investment and consequentially to maintain lower customer bills, as corporation tax relief is given against the investments made.

The adjustment to the tax charge in respect of prior years represents a current tax credit of £0.2 million and a deferred tax charge of £0.3 million. These adjustments reflect the true-up of the previous year's provision to the tax computations filed with HMRC.

In addition to the amounts recognised in the income statement the following tax charges and credits were also recognised:

	2021 £m	2020 £m
Amounts recognised directly in other comprehensive income		
Deferred tax charge/(credit) on defined benefit pension schemes	2.6	(1.6)
Deferred tax charge/(credit) on cash flow hedges	1.6	(2.5)
Amounts recognised directly in equity		
Deferred tax charge/(credit) on share based payments	0.4	(0.6)

Factors affecting future tax charges

In the Chancellor's March 2021 Budget, it was announced the rate of UK corporation tax will remain at 19% for the next two years before increasing to 25% from April 2023. As the future increase in the tax rate was not enacted at the balance sheet date, all current and deferred tax assets and liabilities continued to be calculated and stated at the 19% rate. This change was substantively enacted on 24 May 2021 and deferred tax assets and liabilities will be recalculated and recorded at the tax rate at which they are expected to unwind in the next financial year. It is anticipated the tax rate increase will increase the tax charge and dererred tax liability by around c.£85 million.

The budget also introduced an acceleration of capital allowances for expenditure on new qualifying assets in the period April 2021 to April 2023, with a 130% super-deduction for plant and machinery and a 50% first year allowance for other qualifying assets. This is expected reduce the current tax charge in the next two financial years, however it will be offset by an increase in deferred tax charges and liabilities for the acceleration of tax relief and the higher corporate tax rate applicable to future timing differences.

10. DIVIDENDS

	2021 £m	2020 £m
Amounts recognised as distributions to equity holders in the year:		
Base dividend of 24.1p per ordinary share in respect of 2019/20 paid 30 August 2019	-	60.5
Outperformance dividend of 23.6p per ordinary share in respect of 2018/19 paid 30 August 2019	-	59.2
Special dividend of 51.8p per ordinary share in respect of 2019/20 paid 30 August 2019	-	130.0
Base dividend of 16.9p per ordinary share in respect of 2020/21 paid 29 March 2021	42.3	-
Watershare+ dividend	1.2	-
Declared and approved:		
Outperformance dividend of 23.2p per ordinary share in respect of 2019/20	58.1	-
	101.6	249.7

A dividend payment of £1.2m was made to Pennon Group Plc in October 2020 as part of the Watershare+ customer rebate scheme (see note 6). Payment of the outperformance dividend based on cumulative outperformance for 2019/20 of £58.1m has been deferred to August 2021. The Company is obligated to pay the dividend therefore £58.1m has been recognised as a transaction with owners during the year ended 31 March 2021.

11. EMPLOYMENT COSTS

The average number of persons (including Executive Directors) employed by the Company was 1,567 (2020: 1,452).

	Note	2021 £m	2020 £m
Wages and salaries		56.2	52.1
Social security costs		5.6	5.2
Pension costs	24	12.6	7.4
Share-based payments		1.0	1.0
Total employment costs		75.4	65.7
Charged as follows:			
Employee costs		53.9	50.0
Capital schemes		18.0	15.5
Non-underlying pension past service cost	6	-	0.2
Non-underlying pension curtailment charge	6	3.5	-
Total employment costs		75.4	65.7

Details of Directors' emoluments are set out in note 12. There are no personnel other than Directors, who as key management exercise authority and responsibility for planning, directing and controlling the activities of the Company.

12. DIRECTORS' EMOLUMENTS

	2021 £000	2020 £000
Executive Directors:		
Salary	488	456
Performance-related bonus paid or payable	208	149
Share-based payments	541	359
Other emoluments, including payments in lieu of pension provision	113	147
Non-Executive Directors (including Chairman)	325	384
Total emoluments	1,675	1,495

More detailed information concerning Directors' emoluments (including pensions and the highest paid Director) and share interests is shown in the Annual Report on Remuneration on pages 103 to 121. This report also details arrangements with Pennon Group plc for the payment and recharging of emoluments relating to Directors who serve as Directors of both Pennon Group and South West Water. One of the directors received compensation for loss of office which has been borne in full by Pennon Group plc. The cost of share-based payments represents the amount charged to the income statement, as described in note 29.

The aggregate gains on vesting of Directors' share-based awards amounted to a total of £87,000 (2020: £nil). Total gains made by Directors on the exercise of share options were £nil (2020: £nil).

12. DIRECTORS' EMOLUMENTS (CONTINUED)

At 31 March 2021 there were no Directors accruing retirement benefits under defined benefit pension schemes (2020: nil) At 31 March 2021 there was one Director accruing benefits under defined contribution pension schemes with contributions of £3,000 made during the year (2020: £12,693).

13. PROPERTY, PLANT AND EQUIPMENT

	Freehold land and buildings £m	Infrastructure assets £m	Operational properties £m	Fixed and mobile plant, vehicles and computers £m	Construction in progress £m	Total £m
Cost:						
At 31 March 2019	52.5	1,894.2	748.7	1,832.2	148.6	4,676.2
IFRS 16 transition adjustment	31.1	-	-	0.8	-	31.9
At 1 April 2019 (adjusted for IFRS 16)	83.6	1,894.2	748.7	1,833.0	148.6	4,708.1
Additions	0.1	27.8	1.8	53.9	77.4	161.0
Assets adopted at fair value	-	8.1	-	-	-	8.1
Grants & contributions	-	(1.8)	-	-	(0.9)	(2.7)
Disposals	-	(0.6)	-	(1.3)	-	(1.9)
Transfers/reclassifications	1.7	17.3	19.1	68.0	(106.1)	-
At 31 March 2020	85.4	1,945.0	769.6	1,953.6	119.0	4,872.6
Additions	0.1	17.0	2.7	49.1	99.2	168.1
Assets adopted at fair value	-	7.5	-	-	-	7.5
Grants & contributions	-	-	-	-	(3.7)	(3.7)
Disposals	-	-	-	(0.7)	-	(0.7)
Transfers/reclassifications	0.4	13.5	12.6	70.2	(96.7)	-
At 31 March 2021	85.9	1,983.0	784.9	2,072.2	117.8	5,043.8
Accumulated depreciation:						
At 31 March 2019	13.0	273.6	271.9	1,104.4	-	1,662.9
Charge for year	2.9	23.0	13.6	83.0	-	122.5
Disposals	-	(0.6)	-	(1.2)	-	(1.8)
At 31 March 2020	15.9	296.0	285.5	1,186.2	-	1,783.6
Charge for year	2.9	23.2	13.8	82.2	-	122.1
Disposals	-	-	-	(0.7)	-	(0.7)
At 31 March 2021	18.8	319.2	299.3	1,267.7	-	1,905.0
Net book value:						
At 31 March 2019	39.5	1,620.6	476.8	727.8	148.6	3,013.3
At 31 March 2020	69.5	1,649.0	484.1	767.4	119.0	3,089.0
At 31 March 2021	67.1	1,663.8	485.6	804.5	117.8	3,138.8

Out of the total depreciation charge for the Company of £122.1 million (2019/20: £122.5 million), the sum of £1.7 million (2019/20: £2.6 million) has been charged to capital projects, £2.1 million (2019/20: £1.7 million) has been offset by deferred income and £118.3 million (2019/20: £118.2 million) against profits.

Asset lives and residual values are reviewed annually.

During the year borrowing costs of £0.9 million (2019/20: £2.0 million) have been capitalised on qualifying assets, at an average borrowing rate of 2.7% (2019/20: 3.4%).

13. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Right of use assets held under leases included above were:

	Freehold land and buildings £m	Infrastructure assets £m	Operational properties £m	Fixed and mobile plant, vehicles and computers £m	Construction in progress £m	Total £m
Cost:						
At 31 March 2020	35.1	404.8	481.5	518.8	-	1,440.2
Additions	0.2	8.8	0.7	5.6	-	15.3
Disposals	-	-	-	-	-	-
At 31 March 2021	35.3	413.6	482.2	524.4	-	1,455.5
Accumulated depreciation:						
At 31 March 2020	1.4	78.2	135.0	281.3	-	495.9
Charge for year	1.3	(0.3)	7.8	22.9	-	31.7
At 31 March 2021	2.7	77.9	142.8	304.2	-	527.6
Net book value:						
At 31 March 2020	33.7	326.6	346.5	237.5	-	944.3
At 31 March 2021	32.6	335.7	339.4	220.2	-	927.9

During 2021 the depreciation on leased infrastructure assets included a credit of £5.1 million in respect of depreciation on owned assets which had been treated as relating to leased assets in the 2020 financial statements. There was a corresponding charge to depreciation on owned infrastructure assets in 2021.

14. GOODWILL

	2021 £m	2020 £m
Cost		
At 1 April	51.3	51.3
At 31 March	51.3	51.3

The goodwill of £51.3 million was recognised on acquisition of Bournemouth Water in 2016/17. It is attributable to synergies and outperformance arising from the merger of operating activities.

Impairment testing of goodwill

The Group tests goodwill for impairment annually or more frequently if there are any indications that impairment may have arisen. The recoverable amount, for which goodwill was recognised on the acquisition of Bournemouth Water in 2016, is assessed using level 2 fair value hierarchy techniques, with reference to the market value of the merged water business, using a market based observable premium to Regulated Capital Value.

15. FINANCIAL INSTRUMENTS BY CATEGORY

The accounting policies for financial instruments have been applied to the line items as below:

	Note	Fair value Derivatives used for cash flow hedging £m	Amortised cost Loans and receivables £m	Trade receivables and trade payables £m	Total £m
31 March 2021					
Financial assets					
Trade and other receivables	18	-	10.7	127.8	138.5
Cash and cash deposits	20	-	414.9	-	414.9
Derivatives	19	1.7	-	-	1.7
		1.7	425.6	127.8	555.1
Financial liabilities					
Borrowings	22	-	(2,688.5)	-	(2,688.5)
Derivative financial instruments	19	(23.5)	-	-	(23.5)
Trade and other payables	21	-	(62.2)	(62.1)	(124.3)
		(23.5)	(2,750.7)	(62.1)	(2,836.3)

15. FINANCIAL INSTRUMENTS BY CATEGORY (CONTINUED)

		Fair value Derivatives used for cash flow hedging £m	Loans and receivables £m	Amortised cost Trade receivables and trade payables £m	Total £m
	Note				
31 March 2020					
Financial assets					
Trade and other receivables	18	-	14.4	116.8	131.2
Cash and cash deposits	20	-	284.1	-	284.1
		-	298.5	116.8	415.3
Financial liabilities					
Borrowings	22	-	(2,591.3)	-	(2,591.3)
Derivative financial instruments	19	(30.6)	-	-	(30.6)
Trade and other payables	21	-	(5.3)	(52.3)	(57.6)
		(30.6)	(2,596.6)	(52.3)	(2,679.5)

16. INVESTMENTS

	2021 £m	2020 £m
At 31 March:		
Subsidiary undertakings	3.3	3.3

The Company has three wholly-owned trading subsidiaries, Peninsula Properties (Exeter) Limited, South West Water Finance plc and Source Contact Management Limited. The Company also has eight wholly-owned dormant subsidiaries, Bournemouth Water Investments Limited and its subsidiaries, BWH Enterprises Limited, Bournemouth Water Limited, Alderney Water Limited, West Hampshire Water Limited, Avon Valley Water Limited and Aquacare (BWH) Limited.

All of these subsidiaries are registered at Peninsula House, Rydon Lane, Exeter, Devon, England, EX2 7HR and are also incorporated and operate in England. The Company also has a minority shareholding in Landlord Tap Limited, which is incorporated, registered and operates in England.

Consolidated financial statements have not been prepared, as explained in note 2(b).

In the opinion of the Directors, the total value of the investments in subsidiaries is not less than the amount at which they are shown in the balance sheet.

17. INVENTORIES

	2021 £m	2020 £m
Raw materials and consumables	5.4	4.9

18. TRADE AND OTHER RECEIVABLES – CURRENT

	2021 £m	2020 £m
Amounts receivable from customers	216.2	208.4
Less: provision for expected credit losses	(88.4)	(91.6)
Net trade receivables	127.8	116.8
Amounts owed by fellow subsidiary companies	10.7	14.4
Other receivables	16.9	8.6
Prepayments and accrued income	8.9	5.4
Trade and other receivables – current	164.3	145.2

Trade receivables include accrued income relating to customers with metered budget plans.

18. TRADE AND OTHER RECEIVABLES – CURRENT (CONTINUED)

The Directors consider that the carrying amounts of trade and other receivables approximate to their fair value. There is no concentration of credit risk in trade receivables. The Company has a large number of customers who are dispersed and there is no significant loss on trade receivables expected that has not been provided for. The Company applies the simplified approach in calculating the expected credit losses for trade receivables allowing a provision matrix to be used which is based on the expected life of trade receivables, default rates for different customer categories within the collection process and forward looking information. As at 31 March, an analysis of the aging of gross trade receivables is as follows:

	2021 £m	2020 £m
Not due	31.6	33.1
Past due 1 - 30 days	12.3	8.2
Past due 31 - 120 days	11.9	12.0
More than 120 days	160.4	155.1
Total trade receivables	216.2	208.4

The aged trade receivables above are taken directly from the Company's sales ledger records before the deduction of credit balances and other adjustments.

The Company specifically reviews separate categories of debt to identify an appropriate allowance for expected credit losses as outlined in note 2(n). South West Water has a duty under legislation to continue to provide domestic customers with services regardless of payment. The expected credit loss rate applied ranges from 0% (not due) to 100% (<120 days and untraced previous occupier). No expected credit loss provision has been recognised in respect of amounts owed by fellow subsidiary undertakings.

The movement in the allowance for expected credit losses in respect of trade receivables was:

	2021 £m	2020 £m
At 1 April	91.6	86.8
Provision for expected credit losses	2.8	5.7
Net Receivables written-off during the year as uncollectable	(6.0)	(0.9)
At 31 March	88.4	91.6

Receivables in respect of wholesale water and wastewater services retailed by fellow group subsidiaries are included as amounts owed by fellow subsidiary companies.

19. DERIVATIVE FINANCIAL INSTRUMENTS

	2021 £m	2020 £m
Derivatives used for cash flow hedging:		
Assets		
Current assets	0.2	-
Non-current assets	1.5	-
Total assets	1.7	-
Liabilities		
Current liabilities	(6.1)	(6.2)
Non-current liabilities	(17.4)	(24.4)
Total liabilities	(23.5)	(30.6)

The Group's financial risks and risk management policies are set out in note 3. The fair value of hedging derivatives is split between current and non-current assets or liabilities based on the maturity of the cash flows. The ineffective portion recognised in the income statement arising from cash flow hedges was £nil (2019/20 £nil).

Interest rate swaps and fixed rate borrowings are used to manage the mix of fixed and floating rates to ensure at least 60%, after the effect of interest rate swaps, of net borrowings is at fixed rate. At 31 March 2021, 63% (31 March 2020: 52%) of net borrowings were at fixed rates.

At 31 March 2021 interest rate swaps to swap from floating to fixed rate and hedge financial liabilities with a notional value of £801 million existed, with a weighted average maturity of 4.4 years (31 March 2020: £1,063.0 million, with 4.0 years). The weighted average interest rate of the swaps was 1.29% (31 March 2020: 1.42%).

19. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

The periods for which cash flow hedges are expected to affect future profit or loss as follows:

	<1 year £m	1-2 years £m	2-5 years £m	Over 5 years £m	Total £m
31 March 2021					
Assets	0.2	0.2	0.6	0.7	1.7
Liabilities	(6.1)	(6.1)	(11.3)	-	(23.5)
31 March 2020					
Liabilities	(6.2)	(6.2)	(17.8)	(0.4)	(30.6)

Valuation hierarchy

The amounts of financial instruments carried at fair value by valuation method were:

	2021 £m	2020 £m
Level 2 inputs		
Assets		
Derivatives used for cash flow hedging	1.7	-
Liabilities		
Derivatives used for cash flow hedging	23.5	30.6

The Company uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2)
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3)

The fair value of financial instruments not traded in an active market (level 2, for example over-the-counter derivatives) is determined by using valuation techniques. A variety of methods and assumptions are used based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

20. CASH AND CASH DEPOSITS

	2021 £m	2020 £m
Cash at bank and in hand	17.1	33.2
Short-term bank deposits	147.0	25.0
Other deposits	250.8	225.9
Cash and cash deposits	414.9	284.1

Overnight deposits have an average maturity of one working day. Other short-term bank deposits have an average maturity of 79 days.

Other deposits include £250.8 million (31 March 2020: £225.9 million) of restricted funds to settle long-term lease liabilities (note 22).

For the purposes of the cash flow statement, cash and cash equivalents comprise:

	2021 £m	2020 £m
Cash and cash deposits as above	414.9	284.1
Less: deposits with a maturity of three months or more (restricted funds)	(250.8)	(225.9)
Cash and cash equivalents	164.1	58.2

21. TRADE AND OTHER PAYABLES – CURRENT

	2021 £m	2020 £m
Trade payables	62.1	52.3
Amounts owed to subsidiary companies	6.1	4.2
Amounts owed to parent undertaking	56.1	1.1
Other tax and social security	1.8	2.0
Other payables	9.9	11.2
Accruals	21.1	12.7
Contract liabilities	2.0	2.0
	159.1	85.5

The Directors consider that the carrying amount of trade and other payables approximates to their fair value.

Included in amounts owed to parent undertaking is £58.1m relating to payment of the outperformance dividend based on cumulative outperformance for 2019/20 that has been deferred to August 2021.

The movement in the current and non-current contract liabilities was:

	2021 £m	2020 £m
At 1 April	124.9	118.1
Revenue recognised in the year	(1.0)	(1.3)
Consideration received in advance of completion of performance obligations	6.3	8.1
At 31 March	130.2	124.9

The analysis of contract liabilities between current and non-current is:

	2021 £m	2020 £m
Current	2.0	2.0
Non-current (note 23)	128.2	122.9
	130.2	124.9

Performance obligations related to the current contract liabilities closing balance above are expected to be satisfied, and revenue will be recognised, within the financial year ended 31 March 2022.

Payment of the outperformance dividend based on cumulative outperformance for 2019/20 of £58.1m has been deferred to August 2021.

22. BORROWINGS

	2021 £m	2020 £m
Current		
European Investment Bank	32.4	27.0
Other external loans	7.7	7.5
Loan from subsidiary company (note 35)	3.2	4.2
	43.3	38.7
Leases	48.2	19.2
Total current borrowings	91.5	57.9
Non-current		
European Investment Bank	205.0	237.4
Other external loans	506.3	382.4
Loan from subsidiary company (note 35)	494.6	494.3
	1,205.9	1,114.1
Leases	1,391.1	1,419.3
Total non-current borrowings	2,597.0	2,533.4
Total borrowings	2,688.5	2,591.3

22. BORROWINGS (CONTINUED)

The loan from subsidiary company represents loans from South West Water Finance plc, a UK company whose purpose is to raise borrowings for South West Water Limited. The fair value of the non-current borrowings were:

	2021	2021	2020	2020
	Book	Fair	Book	Fair
	value	value	value	value
	£m	£m	£m	£m
European Investment Bank	205.0	188.8	237.4	220.9
Other external loans	506.3	573.8	382.4	435.5
Loan from subsidiary company	494.6	603.2	494.3	657.2
	1,205.9	1,365.8	1,114.1	1,313.6
Leases	1,391.1	-	1,419.3	-
	2,597.0	1,365.8	2,533.4	1,313.6

Under IFRS 16 the disclosure relating to the fair value of leases is not required.

Where market values are not available, fair values of borrowings have been calculated by discounting expected future cash flows at prevailing interest rates.

The maturity of non-current borrowings was:

	2021	2020
	£m	£m
Between 1 and 2 years	68.7	113.4
Over 2 and less than 5 years	362.4	206.1
Over 5 years	2,165.9	2,213.9
	2,597.0	2,533.4

The weighted average maturity of non-current borrowings was 18.6 years (31 March 2020: 20.4 years).

The Company has leases for various assets as shown in note 13.

The maturity of lease liabilities was:

	2021	2020
	£m	£m
Within 1 year	48.2	19.2
Over 1 year and less than 5 years	243.2	148.9
Over 5 years	1,147.9	1,270.4
	1,439.3	1,438.5

For the purposes of calculating debt or borrowings under the Company's financing agreements, all of which were negotiated under IFRS prior to the implementation of IFRS 16, borrowings that were previously categorised as operating leases under IAS 17 are excluded from the definition of debt. As at 31 March 2021 the carrying value of leases previously categorised as IAS 17 operating leases was £35.4 million (2020: £36.1 million).

The Company does not face a significant liquidity risk with regard to its lease liabilities. Lease liabilities are monitored by the treasury function.

The discount rate used to calculate the lease liabilities above involves estimation. Where the Group cannot readily determine the rate implicit in the lease the Group uses an estimated incremental borrowing rate (IBR). At 31 March 2021, the range of IBRs used was between 2.9% and 4.5% (2020 between 2.93% and 4.50%) and the weighted average IBR across all leases was 3.8% (2020 3.8%). If the weighted average rate used increased or decreased by 10bps this would result in a c.1.2% increase or reduction in the present value of lease liabilities recognised at 31 March 2021 (2020 1.2%).

The period for repayment of certain leases includes an agreement to deposit with the lessor group amounts equal to the difference between the original and revised payments due. The accumulated deposits, £250.8 million at 31 March 2021 (2020 £225.9 million), are currently being held to settle the lease liability subject to rights to release by negotiation with the lessor. The deposits are subject to a registered charge given as security to the lessor for the balance outstanding.

Other information required to be disclosed under IFRS 16 is included in note 13.

22. BORROWINGS (CONTINUED)

Undrawn committed borrowing facilities at the balance sheet date were:

	2021 £m	2020 £m
Floating rate:		
Expiring after one year	180.0	235.0
	180.0	235.0

In addition, the Company has undrawn uncommitted short-term bank facilities of £nil (31 March 2020: £nil).

23. OTHER NON-CURRENT LIABILITIES

	2021 £m	2020 £m
Contract liabilities	128.2	122.9

Non-current contract liabilities relate to consideration received in advance of the Company performing its performance obligations to customers where performance obligations will not be completed within twelve months of the balance sheet date. The overall movement in total contract liabilities is disclosed in note 21. Contract liabilities reflect the fair value of assets transferred from customers. The majority of the contract liabilities included above are expected to unwind after five years.

24. RETIREMENT BENEFIT OBLIGATIONS

The Company's employees are eligible to participate in a defined contribution scheme, operated by the parent company, Pennon Group plc. The Company is also a member of the Pennon Group defined benefit scheme which was closed to new members on or before 1 April 2008.

The assets of the Pennon Group's pension schemes are held in separate trustee-administered funds. The trustees of the funds are required to act in the best interest of the funds' beneficiaries. The appointment of the schemes' trustees is determined by the schemes' trust documentation. The Pennon Group has a policy for the main fund that one-half of all trustees, other than the Chairman, are nominated by members of the schemes, including pensioners.

Defined contribution schemes

Pension costs for defined contribution schemes were £3.3 million (2019/20: £1.5 million).

Defined benefit schemes

The principal actuarial assumptions at 31 March were:

	2021 %	2020 %	2019 %
Rate of increase in pensionable pay	3.2	2.7	3.3
Rate of increase for current and future pensions	2.0	2.0	2.0
Rate used to discount schemes' liabilities and expected return on scheme assets	2.05	2.30	2.40
Inflation	3.2	2.7	3.3

Mortality

Assumptions regarding future mortality experience are set based on actuarial advice in accordance with published statistics and experience. The mortality assumption uses a scheme-specific calculation based on CMI 2019 actuarial tables with an allowance for future longevity improvement.

The average life expectancy in years of a member having retired at age 62 on the balance sheet date is projected at:

	2021	2020	2019
Male	24.7	24.7	23.9
Female	27.0	26.9	26.3

The average life expectancy in years of a future pensioner retiring at age 62, 20 years after the balance sheet date, is projected as:

	2021	2020	2019
Male	25.5	25.4	25.0
Female	27.9	27.9	28.1

24. RETIREMENT BENEFIT OBLIGATIONS (CONTINUED)

The sensitivities regarding the principal assumptions used to measure the schemes' liabilities are:

	Change in assumption	Impact on schemes' liabilities
Rate of increase in current and future pensions	+/- 0.5%	+/- 6.6%
Rate used to discount schemes' liabilities	+/- 0.5%	+/- 9.3%
Inflation	+/- 0.5%	+/- 6.3%
Life expectancy	+/- 1 year	+/- 4.1%

The sensitivity analysis shows the effect of changes in the principal assumptions used for the measurement of the pension liability. The method used to calculate the sensitivities is approximate and has been determined taking into account the duration of the liabilities and the overall profile of each scheme's membership. This is the same approach as has been adopted in previous years. The sensitivity in respect of changes in pensionable pay has been removed from the analysis this year as it is no longer relevant as the scheme is closing to future accrual on 30 June 2021.

The amounts recognised in the balance sheet were:

	2021 £m	2020 £m
Present value of financial obligations	(695.9)	(636.0)
Fair value of plan assets	710.2	643.1
Net asset recognised in the balance sheet	14.3	7.1

The movement in the net defined benefit obligation over the accounting period is as follows:

	2021		Present value of		2020	
	Present value of obligation £m	Fair value of plan assets £m	Total £m	Present value of obligation £m	Fair value of plan assets £m	Total £m
At 1 April	(636.0)	643.1	7.1	(659.4)	637.5	(21.9)
Current service cost	(5.8)	-	(5.8)	(5.7)	-	(5.7)
Interest (expense)/income	(12.5)	12.1	(0.4)	(16.2)	16.0	(0.2)
Past service cost and gains and losses on settlements	(3.5)	-	(3.5)	(0.2)	-	(0.2)
	(21.8)	12.1	(9.7)	(22.1)	16.0	(6.1)
Remeasurements:						
(Loss)/return on plan assets excluding amounts included in interest expense	-	83.0	83.0	-	(14.9)	(14.9)
(Loss)/gain from change in demographic assumptions	-	-	-	(3.5)	-	(3.5)
Gain/(loss) from change in financial assumptions	(73.9)	-	(73.9)	28.2	-	28.2
Experience gain/(loss)	4.8	-	4.8	(7.1)	-	(7.1)
	(69.1)	83.0	13.9	17.6	(14.9)	2.7
Contributions:						
Employers	-	3.0	3.0	-	32.4	32.4
Payments from plans:						
Benefit payments	29.2	(29.2)	-	27.9	(27.9)	-
Administration costs	1.8	(1.8)	-	-	-	-
	31.0	(28.0)	3.0	27.9	4.5	32.4
At 31 March	(695.9)	710.2	14.3	(636.0)	643.1	7.1

Employer contributions are made into the scheme by South West Water and other companies within the Pennon Group based upon pensionable pay of employees in each section of the scheme. Full details of the scheme are included within the Pennon Group plc financial statements (see note 30).

24. RETIREMENT BENEFIT OBLIGATIONS (CONTINUED)

The Group completed its employee consultation to modernise its ongoing pension arrangements. The outcome of the consultation resulted in a decision to close the Pennon's principal defined benefit pension scheme to future accrual with effect from 30 June 2021. This resulted in a curtailment charge of £3.5 million, which has been included within non-underlying items for the Company (see note 6).

The assets in the schemes and the expected long-term rates of return at year end were:

	2021		2020	
	Quoted prices in active market £m	Fund %	Quoted prices in active market £m	Fund %
Equities	131.1	19	100.8	16
Property	49.7	7	51.2	8
Bonds	369.1	52	337.5	52
Diversified Growth Fund	109.9	15	99.1	15
Insurance linked securities	41.6	6	44.3	7
Other	8.8	1	10.2	2
	710.2	100	643.1	100

Other assets principally represent cash contributions received from the Company towards the year-end which are invested during the subsequent financial year.

Through the Pennon Group defined benefit pension plan, the Company is exposed to a number of risks, the most significant of which are detailed below:

Asset volatility: The liabilities are calculated using a discount rate set with reference to corporate bond yields; if assets underperform this yield, this will create a deficit. The scheme holds a significant proportion of growth assets (equities, diversified growth funds and property) which are expected to outperform corporate bonds in the long-term while providing volatility and risk in the short-term. The allocation to growth assets is monitored such that it is aligned with the scheme's long-term objectives.

Changes in bond yields: A decrease in corporate bond yields will increase the value placed on the scheme's liabilities for accounting purposes, although this will be partially offset by an increase in the value of the scheme's bond holdings.

Inflation risk: The majority of the scheme's benefit obligations are linked to inflation, and higher inflation will lead to higher liabilities (although, in most cases, caps on the level of inflationary increases are in place to protect against extreme inflation). The majority of the assets are either unaffected by or loosely correlated with inflation, meaning that an increase in inflation will also increase the deficit.

Life expectancy: The majority of the scheme's obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the liabilities.

In conjunction with its investment advisors, the trustees have structured the scheme's investments with the objectives of balancing investment returns and levels of risk. The asset allocation has three principal elements:

- holding of cash funds and bonds which is expected to be less volatile than most other asset classes and reflects market movements in the scheme's liabilities;
- A proportion of assets with fund managers having freedom in making investment decisions to maximise returns
- Investment of a proportion of the schemes' assets in alternative asset classes which give the potential for diversification (currently property, insurance linked securities and diversified growth).

The liabilities of the defined benefit schemes are measured by using the projected unit credit method which is an accrued benefits valuation method in which the scheme liabilities make allowance for projected increases in pensionable pay.

The future cash flows arising from the payment of the defined benefits are expected to be settled primarily in the period between 15 and 40 years from the balance sheet date.

The 2019 triennial actuarial valuation of the principal defined benefit scheme was agreed in the previous financial year with an actuarial valuation deficit of £53 million. The Company made a deficit recovery contribution of £nil (2020 £28.5 million reflecting three years of contributions for 2020-22) to the main scheme. This is in line with our regulatory commitments. Pennon Group plc monitors funding levels on an annual basis and expects to pay total contributions of around £0.4 million during the year ending 31 March 2022, with this amount being adjusted for inflation.

25. CURRENT TAX ASSET

	2021	2020
	£m	£m
Current year (liability)/asset	(0.8)	0.3
Prior year tax items	4.7	3.1
At 31 March	3.9	3.4

26. DEFERRED TAX LIABILITIES

Deferred tax is provided in full on temporary differences under the liability method using enacted tax rates. Movements on deferred tax were:

	2021	2020
	£m	£m
Liabilities at 1 April	263.8	230.8
Opening adjustment on adoption of IFRS 16	-	(0.4)
Charged to the income statement	3.5	9.8
Charged/(credited) to equity/other comprehensive income	4.6	(2.5)
Change of rate in equity/other comprehensive income	-	(2.2)
Change of rate in income statement – non-underlying	-	28.9
Non underlying (credit) to the income statement	(0.7)	(0.6)
Liabilities at 31 March	271.2	263.8

Deferred tax assets have been recognised in respect of all temporary differences giving rise to deferred tax assets because it is probable that these assets will be recovered.

The majority of the Company's deferred tax asset is expected to be recovered over more than one year. All deferred tax assets and liabilities within the same jurisdiction are offset.

The movements in deferred tax assets and liabilities were:

Deferred tax liabilities

	Accelerated tax depreciation	Retirement benefit obligations	Total
	£m	£m	£m
At 31 March 2019	240.7	(5.1)	235.6
Opening adjustment on adoption of IFRS 16	(0.4)	-	(0.4)
Charged to the income statement	6.8	2.9	9.7
Non-underlying charge to the income statement	27.3	1.6	28.9
(Credited) to other comprehensive income/equity	-	(1.6)	(1.6)
At 31 March 2020	274.4	(2.2)	272.2
Charged to the income statement	2.0	1.0	3.0
Non-underlying (credit) to the income statement	-	(0.7)	(0.7)
Charged to other comprehensive income/equity	-	2.6	2.6
At 31 March 2021	276.4	0.7	277.1

Deferred tax (assets)

	Provisions	Derivatives	Share based payments	Total
	£m	£m	£m	£m
At 31 March 2019	(1.0)	(3.3)	(0.5)	(4.8)
Charged/(credited) to the income statement	0.2	-	(0.1)	0.1
Non-underlying (credit)/charge to the income statement	(0.6)	-	-	(0.6)
Charged/(credited) to other comprehensive income/equity	-	(2.5)	(0.6)	(3.1)
At 31 March 2020	(1.4)	(5.8)	(1.2)	(8.4)
Charged/(credited) to the income statement	0.5	-	-	0.5
Charged/(credited) to other comprehensive income/equity	-	1.6	0.4	2.0
At 31 March 2021	(0.9)	(4.2)	(0.8)	(5.9)

26. DEFERRED TAX LIABILITIES (CONTINUED)

Deferred tax (charged)/credited to other comprehensive income/equity during the year was:

	2021	2020
	£m	£m
Remeasurement of defined benefit obligations	(2.6)	1.6
Share-based payments	(0.4)	0.6
Cash-flow hedges	(1.6)	2.5
	(4.6)	4.7

Capital allowances are available when a business incurs qualifying expenditure on capital items such as infrastructure assets. Capital allowances provide tax relief on these items in place of accounting depreciation which is not tax deductible. Over the period of ownership of an asset, cumulative depreciation and capital allowances will equalise. Capital allowance rates are set by the UK Government and every business receives the same rate of allowance. Capital allowance rates vary from 3% up to 100% in certain instances, with most items qualifying for relief in the current year at either 6% or 18% per annum. Given the Company's continued capital investment programme, it is unlikely that the deferred tax liability resulting from the acceleration of tax relief on qualifying capital expenditure will crystallise in the foreseeable future.

The different accounting treatment of property, plant and equipment for tax and accounting purposes means that the taxable income of the Company is not the same as the profit reported in the financial statements. The adjustments for this are reflected in the current tax reconciliation. As explained in Taxation note 9, the government has introduced capital expenditure super-deduction allowance incentives for the two year period to April 2023 which increases the rate of capital allowance to up to 130% for expenditure on qualifying plant and machinery. This is expected to provide an increase in current tax relief to the Company with a consequently higher deferred tax liability and charge due to the additional capital allowance deductions and the increase in the rate of corporation tax rate to 25% from April 2023.

Short term temporary differences also arise on items such as provisions, retirement benefit obligations and derivatives because the treatment of such items is different for tax and accounting purposes. These differences reverse over future years following that in which they arise, as is reflected in the deferred tax charge in these financial statements. Specifically, retirement benefit obligations will crystallise over the life of the pension scheme and/or the period when spreading applies (which can be up to three years), short term liabilities including provisions will typically crystallise in the following year and share based payments will crystallise over the period of the share schemes which is up to 5 years.

Where interest charges and other costs are capitalised in the accounts, tax relief is either given as the charges are incurred or when the costs are taken to the income statement.

Derivatives reflect the fair value movements on treasury derivatives, these can fluctuate considerably each year. The balance will crystallise when derivative items are either terminated or mature, the life of these items can be up to ten years.

27. PROVISIONS

	2021	2020
	£m	£m
Restructuring		
At 1 April	0.6	1.1
Utilised during year	(0.3)	(0.5)
At 31 March	0.3	0.6

The restructuring provision is expected to be utilised within one year.

28. CALLED UP SHARE CAPITAL

	2021	2020
	£m	£m
Authorised		
500,000,000 Ordinary shares of £1 each	500.0	500.0
Allotted and fully paid		
250,923,000 Ordinary shares of £1 each	250.9	250.9

29. EMPLOYEE SHARE SCHEMES

The Company participates in a number of share plans for the benefit of employees operated by Pennon Group plc. Details of each plan are:

i) Sharesave Scheme

An all-employee savings related plan is operated that enables employees to invest up to a maximum of £500 per month for three or five years. These savings can then be used to buy Ordinary shares, at a price set at a c.17% discount to the market value at the start of the savings period, at the third, fifth or seventh year anniversary of the option being granted. Options expire six months following the exercise date and, except for certain specific circumstances such as redundancy, lapse if the employee leaves the Pennon Group before the option exercise period commences.

Outstanding options to subscribe for Pennon Group plc Ordinary shares of 40.7p each under the Sharesave scheme are:

Date granted	Subscription price fully paid	Period when options normally exercisable	Thousands of shares in respect of which options outstanding at 31 March	
			2021	2020
14 July 2014	611p	2017 – 2019	-	-
24 June 2015	683p	2018 – 2020	2	98
29 June 2016	709p	2019 – 2021	34	36
28 June 2017	767p	2020 – 2022	30	161
03 July 2018	635p	2021 – 2023	593	624
09 July 2019	620p	2022 – 2024	429	436
16 July 2020	928p	2023 – 2025	229	-
			1,317	1,355

The number and weighted average exercise price of Sharesave options are:

	2021		2020	
	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	1,355	651	1,290	669
Granted	245	928	450	620
Exercised	(230)	729	(230)	674
Expired	(53)	730	(155)	675
At 31 March	1,317	686	1,355	651

The weighted average share price at the date of exercise of Sharesave options during the year was 1,021p (2019/20: 820p). The options outstanding at 31 March 2021 had a weighted average exercise price of 686p (31 March 2020: 651p) and a weighted average remaining contractual life of 1.5 years (31 March 2020: 1.9 years).

The aggregate fair value of Sharesave options granted during the year was £0.4 million (2019/20: £0.5 million), determined using the Black-Scholes valuation model. The significant inputs into the valuation model, at the date of issue of the options, were:

	2021	2020
Weighted average share price	1,089p	765p
Weighted average exercise price	928p	620p
Expected volatility	21.0%	20.0%
Expected life	3.5 years	3.4 years
Risk free rate	0.1%	0.5%
Expected dividend yield	4.0%	5.2%

Expected volatility was determined by calculating the historical volatility of the Pennon Group's share price over the previous three years.

29. EMPLOYEE SHARE SCHEMES (CONTINUED)

ii) Performance and Co-investment Plan

Executive Directors and Senior Management receive a conditional award of Ordinary shares in Pennon Group plc, and are also required to hold a substantial personal shareholding in Pennon Group plc. The eventual number of shares, if any, which vest is dependent upon the achievement of conditions of the plan over the restricted period, being not less than three years. From 2017/18, no further awards have been made under this plan as it has been superseded by a Long-Term Incentive Plan (see iii below).

The number and price of shares in the Performance and Co-investment Plan are:

	2021		2020	
	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	-	-	68	920
Vested	-	-	(21)	920
Lapsed	-	-	(47)	920
At 31 March	-	-	-	-

iii) Long Term Incentive Plan

Executive Directors and Senior Management receive a conditional award of Ordinary shares in Pennon Group plc. Share awards vest subject to the achievement of specific performance conditions measured over a performance period of not less than three years.

The number and price of shares in the LTIP are:

	2021		2020	
	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	136	780	140	797
Granted	78	1,074	52	753
Lapsed	(12)	803	(56)	796
At 31 March	202	743	136	780

The awards outstanding at 31 March 2021 had a weighted average exercise price of 743p (31 March 2020: 780p) and a weighted average remaining contractual life of 2.9 years (31 March 2020: 1.3 years).

The aggregate fair value of awards granted during the year was £0.3 million (2020: £0.2 million), determined from market value. No option pricing methodology is applied since the vesting of the shares depend on non-market performance vesting conditions.

iv) Annual Incentive Bonus Plan – Deferred Shares

Awards under the plan to Executive Directors and Senior Management involve the release of Ordinary shares in Pennon Group plc to participants. There is no performance condition since vesting is conditional upon continuous service with the Pennon Group for a period of three years from the award.

The number and weighted average price of shares in the Incentive Bonus Plan are:

	2021		2020	
	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)	Number of Ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	126	775	140	830
Granted	31	1,079	45	755
Vested	(44)	809	(38)	950
Lapsed	(1)	755	(21)	782
At 31 March	112	845	126	775

29. EMPLOYEE SHARE SCHEMES (CONTINUED)

The awards outstanding at 31 March 2021 had a weighted average price of 845p (31 March 2020: 775p) and a weighted average remaining contractual life of 1.3 years (31 March 2020: 1.5 years). The Group's share price at the dates of the awards ranged from 762p to 1,079p (2020: 761p to 950p).

The aggregate fair value of awards granted during the year was £0.3 million (2019/20: £0.3 million), determined from market value. No option pricing methodology is applied since dividends declared on the shares are receivable by the participants in the scheme.

Further details of the plans and options granted to Directors, included above, are shown in the Directors' remuneration report.

30. RETAINED EARNINGS AND OTHER RESERVES

	Note	Hedging reserve £m	Retained earnings £m	Total £m
At 31 March 2019		(16.1)	405.3	389.2
Profit for the year		-	108.1	108.1
Other comprehensive loss for the year		(8.7)	4.3	(4.4)
Dividends paid	10	-	(249.7)	(249.7)
Share-based payments (net of tax)		-	1.3	1.3
IFRS16 opening reserves adjustment (net of tax)		-	(1.8)	(1.8)
At 31 March 2020		(24.8)	267.5	242.7
Profit for the year		-	114.8	114.8
Other comprehensive loss for the year		7.3	11.3	18.6
Dividends paid/payable	10	-	(101.6)	(101.6)
Watershare+ reserves adjustment		-	1.2	1.2
Share-based payments (net of tax)		-	0.5	0.5
At 31 March 2021		(17.5)	293.7	276.2

The hedging reserve is used to record the portion of the gain or loss on a hedging instrument in a cash flow hedge that is determined to be an effective hedge.

The Watershare+ reserves adjustment relates to the shares in Pennon issued through Company's rebate scheme (see note 6).

31. CASH FLOWS FROM OPERATING ACTIVITIES

Reconciliation of profit for the year to cash generated from operations:

	2021 £m	2020 £m
Continuing operations		
Profit for the year	114.8	108.1
Adjustments for:		
Share based payments	1.0	1.0
Profit on disposal of property, plant and equipment	(0.2)	(0.4)
Depreciation charge	118.3	118.3
Amortisation of intangible fixed assets	-	0.4
Finance income	(0.7)	(2.3)
Finance costs	57.2	73.4
Taxation	27.0	63.0
Non-underlying pensions past service cost	-	0.2
Non-underlying provision charge	-	2.8
Non-underlying Pension curtailment charge	3.5	-
Non-underlying Watershare+ rebate revenue adjustment	20.5	
Non-underlying Watershare+ rebate retained earnings adjustment	1.2	
Changes in working capital:		
Increase in inventories	(0.5)	-
Increase in trade and other receivables	(39.6)	(8.0)
Increase/(Decrease) in trade and other payables	9.3	(10.5)
Decrease in retirement benefit obligations	3.1	(26.5)
Decrease in provisions	(0.3)	(0.4)
Cash generated from operations	314.6	319.1

32. NET BORROWINGS

	2021 £m	2020 £m
Cash and cash deposits	414.9	284.1
Borrowings – current		
Other current borrowings	(43.3)	(38.7)
Lease obligations	(48.2)	(19.2)
Total current borrowings	(91.5)	(57.9)
Borrowings – non-current		
Other non-current borrowings	(1,205.9)	(1,114.1)
Lease obligations	(1,391.1)	(1,419.3)
Total non-current borrowings	(2,597.0)	(2,533.4)
Total net borrowings	(2,273.6)	(2,307.2)

33. CONTINGENT LIABILITIES

	2021 £m	2020 £m
Guarantee of borrowings of subsidiary undertaking	443.4	439.8

Guarantees in respect of performance bonds, the last of which expire in 2057 and which will be reduced in line with repayments of the borrowings of the subsidiary undertaking, are entered into in the normal course of business.

The Company is subject to litigation from time to time as a result of its activities. The Company establishes provisions in connection with litigation where it has a present legal or constructive obligation as a result of past events and where it is more likely than not an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

34. CAPITAL COMMITMENTS

	2021 £m	2020 £m
Contracted but not provided	76.2	72.0

35. RELATED PARTY TRANSACTIONS

	2021 £m	2020 £m
Parent company		
Purchase of goods and services		
– Group expenses	7.0	7.6
Payment for provision of finance		
- Loan interest	-	0.3
Sale of goods and services		
– Administrative services	3.3	0.6
Dividends paid	43.5	249.7
Subsidiaries of the Company		
Purchase of goods and services		
– Property consultancy	0.1	0.2
– Billing and collection services	11.2	10.5
Payment for provision of finance		
– Loan interest	13.8	17.6
Sale of goods and services (administrative services)	1.3	1.3

35. RELATED PARTY TRANSACTIONS (CONTINUED)

	2021 £m	2020 £m
Fellow subsidiaries of the Pennon Group		
Purchase of goods and services		
– Management charges	0.3	0.9
– Waste disposal	0.2	0.5
Sale of goods and services		
– Non-household services	81.6	106.4
– Tankered waste and trade effluent charges	-	1.7
Year end balances		
Borrowings		
– Loan from subsidiary	497.8	498.5
Receivables		
– Fellow subsidiaries	10.7	14.4
Payables		
– Parent company	56.1	1.1
– Subsidiaries	6.1	4.2

36. PARENT COMPANY

The parent company, and ultimate controlling party, is Pennon Group plc which is registered in England. Group financial statements are included in the Annual Report of Pennon Group plc which is available from Peninsula House, Rydon Lane, Exeter, Devon, England, EX2 7HR.