Greensands

Annual Report and Financial statements for the year ended 31 March 2017

Contents

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Introduction

Greensands Holdings Limited ('GSH' or 'the company') is the ultimate parent company of Southern Water Services Limited (Southern Water) and all other group companies disclosed in note 33, with no minority interests.

The only operating company in the Group is Southern Water and the information contained in this Strategic Report is therefore mainly based upon the activities of this company only. This information is fully supported by GSH and has been adopted from the Southern Water Annual Report which is published on the Southern Water website. Sections 1 and 2 that follow contain reviews of GSH and Southern Water for the year to 31 March 2017, respectively.

1) Greensands Holdings Limited

Strategic Report:

The Business

GSH acts as a holding company, with the only trading subsidiary being Southern Water.

This section sets out the financial performance and structure of the Group as well as the corporate governance in place at GSH. A summary of the activities, performance and key risks relating to Southern Water are described in section 2 from page 13.

Group financial performance

The accounting policies of the Group, including any changes in accounting policies in the year, are set out on pages 38 to 47.

Consolidated income statement - summary

The consolidated income statement of GSH is summarised in Table 1 below:

Table 1	Years ended 31 March		Change
	2017 £m	2016 £m	%
Revenue	**809.7**	803.7	*0.7*
Other operating income	**1.3**	1.7	*(23.5)*
Operating costs	**(308.3)**	(287.7)	*7.2*
Depreciation, net of amortisation	**(252.6)**	(242.0)	*4.4*
Operating profit	**250.1**	275.7	*(9.3)*
Profit on disposal of fixed assets	**0.4**	0.4	*0.0*
Net finance costs	**(292.8)**	(270.4)	*8.3*
Fair value losses on derivative financial instruments	**(416.8)**	(66.9)	*523.0*
Loss before tax	**(459.1)**	(61.2)	*650.2*
Tax	**109.3**	40.3	*171.2*
Loss for the financial year	**(349.8)**	(20.9)	*1568.9*

Operating profit largely reflects the trading results of Southern Water for the year and additional depreciation from the revaluation of assets on acquisition.

Revenue increased to £809.7 million (2016: £803.7 million). This increase relates to our main water and wastewater income and arises from an increase in customers from new connections and higher levels of consumption billed in the year offset by an overall reduction in tariff.

Operating costs increased by £20.6 million to £308.3 million (2016: £287.7 million). This is largely due to a one-off refund of historic rates charges received in 2015–16 of £13.3 million. Adjusting for this, the increase in our underlying operating costs was £7.3 million. The major reasons for the movement in underlying operating costs are described below and in Table 2.

During the year Southern Water undertook a number of projects to change processes, investing £4.0 million, in order to improve overall customer service performance. These were focused on proactive contact with customers, reducing complaints, providing help and assistance to customers in financial hardship and initiatives to improve our future bad debt performance. While we have continued to see an increase in the level of bad debt charge during this financial year, we are working hard to make improvements and reduce this in the future.

The cold weather over the winter, which followed a dry autumn, resulted in an increased number of bursts and repairs which led to an increase in our level of leakage. In order to tackle this increase, additional costs of £0.9 million were incurred during the year to help find and fix leaks from the water network.

These cost increases were offset by a number of efficiencies and cost reductions, totalling £8.6 million, during the year. These focused on reducing our power consumption, in particular during peak times, improving operational processes, such as reducing chemical usage, waste disposal costs and tankering requirements. It also looked at more efficient ways of using our own teams to make repairs rather than using external contractors. In addition we benefited from improvements to costs in certain contracts and lower costs from dealing with groundwater flooding.

Unfortunately, during 2016–17 we were prosecuted for pollution incidents which occurred at Margate in 2012 and 2014. This prosecution resulted in a fine of £2.0 million, which increased our operating costs in this financial year. Since those incidents, we have also made considerable investment to mitigate the risk of future incidents, improve resilience at the site and to ensure that bathing water in the area is cleaner than ever.

Table 2 **Year-on-year increase/(decrease) in operating costs**	**£m**
Inflation	5.7
Customer services improvement programme	4.0
Increased bad debt charge	3.8
Increased leakage detection and repair activity	0.9
Power efficiencies	(2.4)
Process efficiencies	(4.0)
Procurement savings	(1.4)
Lower costs from dealing with groundwater flooding	(0.8)
Margate – fine	2.0
Other	(0.5)
Movement in operating costs	**7.3**

Depreciation increased to £252.6 million (2016: £242.0 million) as a result of the continuing significant capital investment programme. New schemes commissioned during the year added £11.9 million to the depreciation charge. A further increase for the full year impact of schemes commissioned in the prior year was offset by a reduction for schemes fully written down of £4.3 million.

Operating profit for 2016–17 decreased to £250.1 million (2016: £275.7 million), a 9.3% reduction as a result of the factors set out above.

The profit on disposal of fixed assets of £0.4 million (2016: £0.4 million) mainly relates to the sale of land, buildings and equipment, surplus to operational requirements.

Net finance costs of £292.8 million increased by 8.3% (2016: £270.4 million). This is largely driven by higher Eurobond interest of £11.4 million in Greensands Europe and higher indexation in SWS on inflation-linked bonds of £10.9 million as a result of increasing RPI in 2016–17.

The fair value loss on our derivative financial instruments amounted to £416.8 million (2016: loss £66.9 million). To calculate the fair value of our derivative instruments we discount their forecast future cash flows using UK Government bond yields. These future forecast cash flows are predictable, and match the future forecast movement in our revenues and 'Regulatory Capital Value', but government gilt yields are constantly moving, with the result that the valuation of our derivative instruments can be volatile. There has been a significant reduction in gilt yields during the year which results in a large increase in the liability associated with our derivative instruments for this period, despite there being little change to their future forecast cash flows. The changes in value that are recorded during the lives of derivatives do not represent cash flows.

We have recognised a total tax credit to the income statement of £109.3 million (2016: credit £40.3 million). This differs from the credit that may be expected of £91.8 million, based on the loss before tax of £459.1 million and the current period tax rate of 20%, as described in note 10. This is primarily the result of the treatment of Eurobond interest for which we have not claimed a tax deduction of £14.8 million offset by the announcement of the reduction in the rate of corporation tax from 20% to 19% with effect from 1 April 2017 and 17% from 1 April 2020. A credit of £19.9 million is recognised for the impact of these changes on the deferred tax liability of the company.

The loss after taxation for the year amounted to £349.8 million (2016: loss £20.9 million).

Statement of financial position – summary

The consolidated statement of financial position for GSH is summarised in Table 3 below:

Table 3	As at 31 March	
	2017 £m	2016 £m
Non-current assets	**6,032.1**	5,946.3
Current assets (excluding cash)	**190.7**	194.2
Cash and cash equivalents	**302.3**	38.1
Total assets	**6,525.1**	6,178.6
Current liabilities	**(300.0)**	(237.1)
Non-current liabilities	**(7,021.6)**	(6,219.7)
Total liabilities	**(7,321.6)**	(6,456.8)
Total net liabilities	**(796.5)**	(278.2)
Shareholders' deficit	**(796.5)**	(278.2)

At 31 March 2017 the Group had non-current assets of £6,032.1 million (2016: £5,946.3 million), an increase of £85.8 million from 31 March 2016. Additions to tangible and intangible assets from the capital investment programme of Southern Water, of £341.4 million, were offset by depreciation of £252.6 million. Total non-current assets as at 31 March 2017 include goodwill arising on acquisition of £85.1 million (2016: £85.1 million).

Current assets decreased to £190.7 million (2016: £194.2 million). This decrease mainly results from a lower level of accrued income and net billed debtors at Southern Water, as a result of the impact of raising final bills to non-household customers ahead of their transfer to Business Stream during February and March 2017. This final billing resulted in a transfer from accrued to billed debt and accelerated some cash receipts, which contributed to reducing the overall debt position by £12.3 million. This reduction was offset by increases in prepayments for certain contracts and in VAT recoverable from HMRC.

Current liabilities increased to £300.0 million (2016: £237.1 million). This increase is driven by an increase in capital creditors of £37.5 million, linked to the increase in capital expenditure during the year as a result of a larger number of projects in construction, together with an accrual for the final dividend approved by the Board at the end of March of £54.2 million. These increases were offset by the repayment of a short-term loan of £50.0 million from the drawdown of a term facility in 2015–16.

At 31 March 2017 non-current liabilities totalled £7,021.6 million (2016: £6,219.7 million). The increase of £801.9 million principally resulted from movements on the value of derivative financial instruments (£411.3 million) and pension deficit (£74.6 million) as a result of the significant reduction in gilt yields during the years which are used to value these liabilities together with a net increase resulting from new loans issued of £248.4 million and interest on the Eurobond loan of £106.9 million.

As at 31 March 2017, the Group had net liabilities of £796.5 million (2016: £278.2 million). Excluding the liability associated with the Eurobonds, which are shareholder loans and included within non-current liabilities, of £997.6 million (2016: £890.7 million), the underlying shareholder equity was £201.1 million (2016: £612.5 million).

Cash flow statement – summary

The consolidated cash flow statement for GSH is summarised in Table 4 below:

Table 4	Years ended 31 March	
	2017	2016
	£m	£m
Net cash inflow from operating activities	**524.0**	481.6
Net cash used in investing activities	**(273.6)**	(236.0)
Net cash from/(used in) financing activities	**13.8**	(437.6)
Net increase/(decrease) in cash and cash equivalents	**264.2**	(192.0)

Net cash inflow from operating activities has increased to £524.0 million for 2016–17 from £481.6 million in 2015–16. This increase mainly results from an increase in the level of creditors during 2016–17 compared to a reduction in creditors in the prior year. This movement in the creditor position is driven in part by the timing of payments to suppliers as well as an increase in the value of deposits and deferred revenue held on the Balance Sheet associated with developer activity. In addition in 2015–16 we made a lump sum contribution in respect of our pension deficit of £30.6 million and received a one-off refund of historic rates charges £13.3 million. The net impact of these transactions reduced the cash inflow from operating activities in 2015–16 by £17.3 million.

The net cash used in investing activities increased to £273.6 million for 2016–17 from £236.0 million in 2015–16. This increase mainly results from the profile of our capital investment programme. The period 2016–17 was the second year of the current regulatory period and as a result there was a significant increase in the number of investment projects in construction.

The net cash from financing activities increased to £13.8 million (2016: used in £437.6 million). This increased cash inflow principally results from the net impact of new loans offset by loan repayments which resulted in a cash inflow of £238.3 million in the current year (2016: inflow £110 million). Also the timing of payments of accrued indexation associated with derivatives in place on some of our debt which fell to £2.5 million in the current year (2016: £298.4 million).

Overall these resulted in a net increase in cash and cash equivalents of £264.2 million (2016: net decrease of £192.0 million).

Financial KPIs

Under the Group financial structure there is a comprehensive set of covenanted financial ratios. Of these, two are key ratios, namely the ratio of consolidated net debt to Regulatory Capital Value (RCV) and the ratio of consolidated EBITDA to consolidated net cash interest cost.

The net debt used in the net debt to RCV ratio is calculated as consolidated secured short-term and long-term borrowings less cash and short-term deposits. The RCV of Southern Water is set by Ofwat for five-year periods at periodic reviews and reflects forecast growth in the asset base. It is adjusted at each periodic review for any out-performance, shortfalls in outputs or permitted additional investment and for certain asset disposals. The target for the current five-year regulatory period ending March 2020 is to maintain the ratio of consolidated net debt to RCV at no more than 90%; at 31 March 2017 it was 87%. Lock-up is defined as a restriction on all dividend payments.

The consolidated EBITDA to consolidated net cash interest is targeted to be maintained comfortably above the 2.0 times covenanted level.

Net debt: RCV	%
2015–16 performance:	89
2016–17 performance	87
Covenanted lock-up level	93
Covenanted default level	95

Consolidated EBITDA to cash interest cover	Times
2015–16 performance	3.2
2016–17 performance	2.9
Covenanted default level	2.0

Dividend policy

We aim to deliver a sustainable long-term capital structure, taking into account the interests of all stakeholders. Our shareholders are long-term investors and fully support the strategy adopted.

The Group's dividend policy is to propose dividends having given due consideration to the following financial and performance criteria:

1. Assessment of headroom under debt covenants
2. Assessment of the impact on Southern Water's credit rating
3. Assessment of the liquidity position and ability to Southern Water's fulfil licence conditions
4. Assessment of key areas of business risk
5. Assessment of current year and cumulative distributable reserves
6. Directors' duties under law and Ofwat-administered regulatory arrangements

Distribution proposals submitted to the Southern Water board will also include an assessment of its performance against the business plan, including expected performance over the balance of the regulatory period.

Our dividend policy, and the associated financial and performance criteria, is intended to support the credit ratings of Southern Water and ensure continued access to diversified sources of finance.

Taxation

We manage our tax affairs in an open and transparent way and contribute materially to the Exchequer each year.

All companies within the Southern Water and wider Greensands groups are UK tax resident, ensuring that each company is subject to UK tax. Tax planning is always aligned with our commercial and economic activity. This practice continues to be recognised by HMRC, which assesses us as a 'low-risk' group.

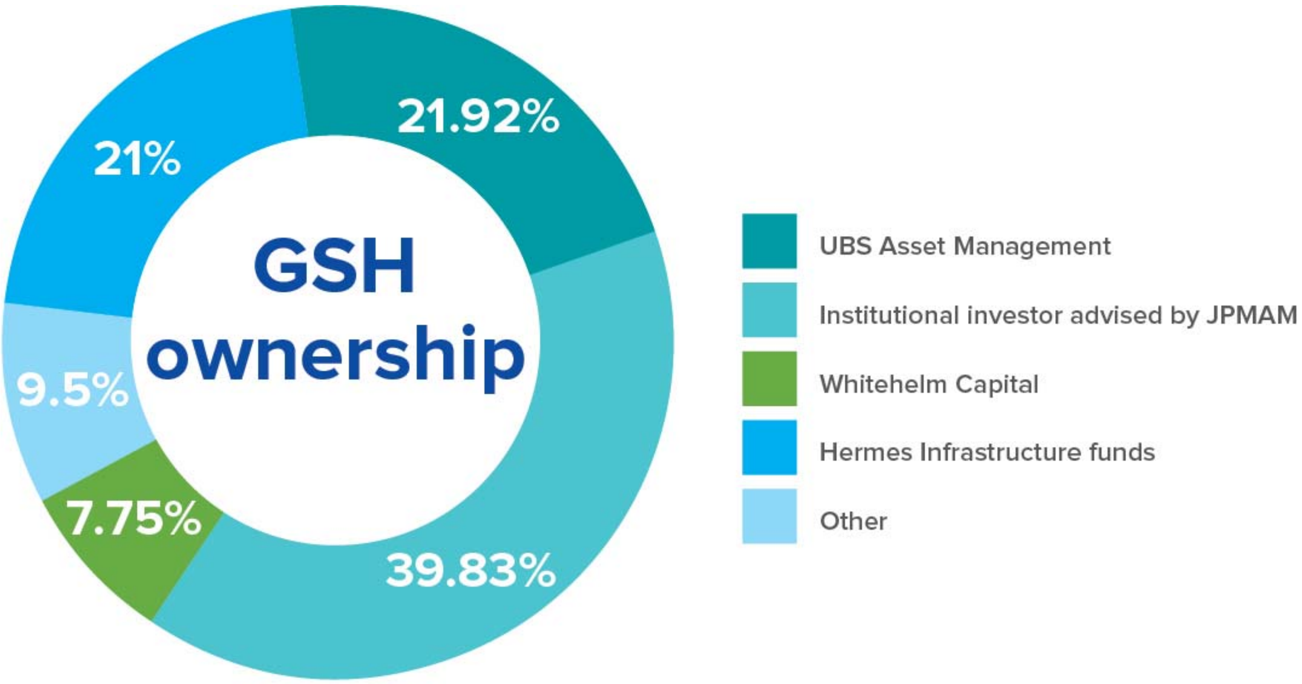
Further information regarding the Southern Water tax position can be found in the Annual Report for Southern Water which is published on its website.

Capital structure, liquidity and other financial matters

Capital structure, ownership and borrowing covenants

Ownership

GSH is owned by a consortium of long-term investors representing infrastructure investment funds, pension funds and private equity and no single shareholder has majority control.

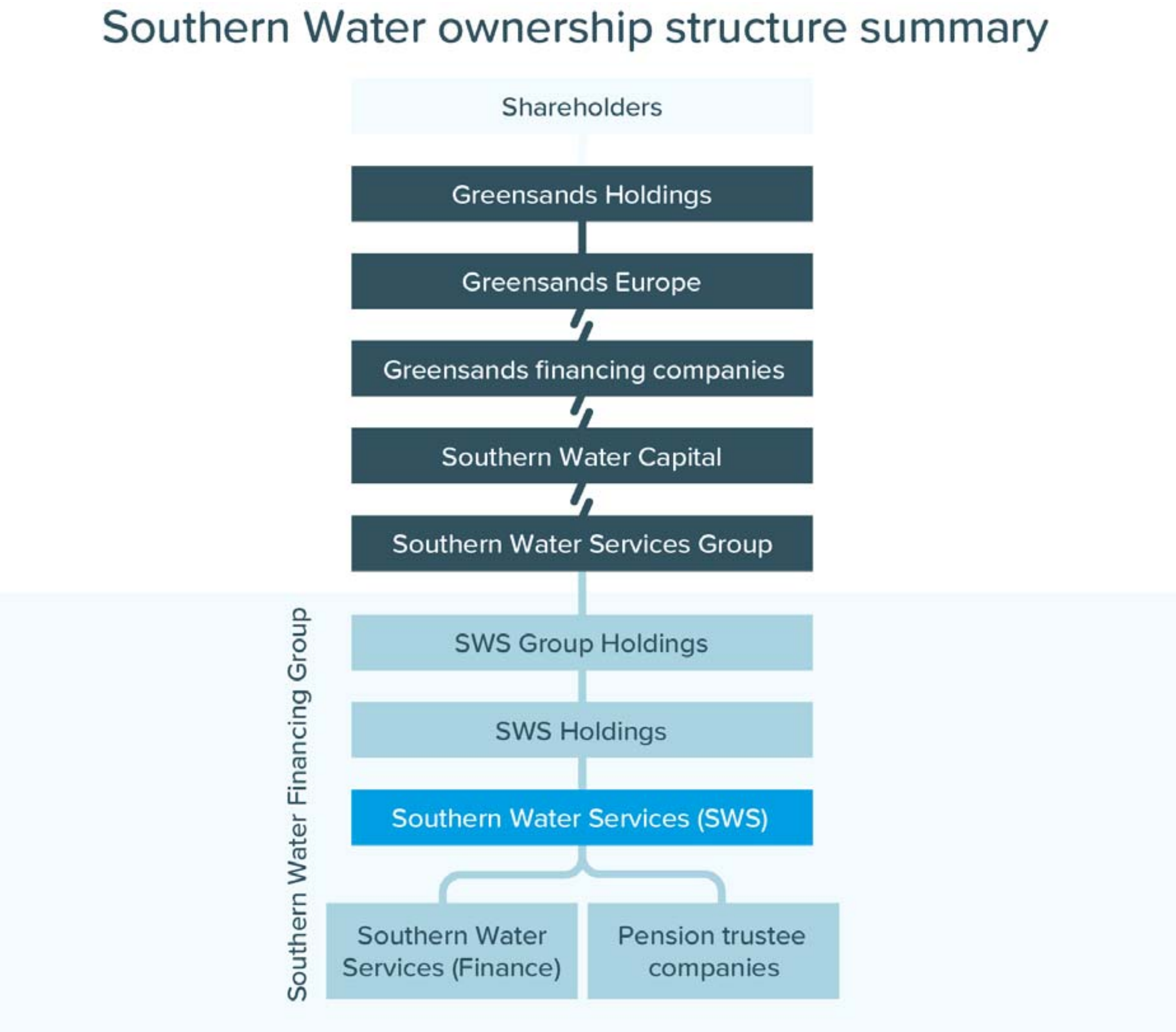


UBS Asset Management – a large-scale global asset manager, offering investment capabilities across all major traditional and alternative asset classes
JP Morgan Asset Management (JPMAM) – a large-scale global asset manager advising institutional investors
Whitehelm Capital – Shareholding managed by Whitehelm Capital on behalf of Motor Trades Association of Australia and Prime superannuation funds
Hermes Infrastructure funds – Hermes Infrastructure is part of Hermes Investment Management and is a specialist infrastructure manager operating a diversified, well-established, UK-focused shared investment platform. With £4.1bn of assets under management, Hermes Infrastructure is one of the UK's largest direct investors
Other – other minor shareholdings held by infrastructure investment companies

Group structure

In September 2007, the Greensands Group of companies was established for the purpose of the acquisition of 100% of the share capital of Southern Water Capital Limited, the then ultimate parent company of Southern Water from the Royal Bank of Scotland (investing £1.9 billion of equity and debt to finance the acquisition).

The holding company structure for SWS is shown in the diagram below and this is followed by an explanation of the principal companies in the structure.



Greensands Holdings (GSH) – Established in 2007, as a single purpose entity for the acquisition of the Southern Water Capital group, GSH is the ultimate parent company of Southern Water and all other group companies, with no minority interests. GSH is a Jersey registered company, but it is UK tax resident and, as such, is liable for tax in the UK. The only operating company in the Group is Southern Water Services. Accordingly, the GSH Board shares and supports the aims of the board of Southern Water for the long-term success of that company. GSH holds 100% of the share capital of Greensands Europe and has no direct holdings in any other entities.

Greensands Europe – Was established as part of the financing for the acquisition of the Southern Water Capital group from RBS in 2007. Greensands Europe has issued debt that is held by our shareholders in proportion to their respective shareholdings.

Greensands financing companies – A number of financing companies were established as part of the acquisition in 2007 to provide additional external financing. Security granted to the lenders of this financing is limited to the share capital of Greensands Holdings Ltd. There are no debt guarantees in place between the Greensands financing companies and the Southern Water Financing group, with the result that SWS is fully protected, and fully isolated, from a default at any Greensands company.

Southern Water Capital (SWC) – Was the previous holding company for the Southern Water group established as part of the sale of Southern Water by Scottish Power in 2002. SWC does not trade and holds preference shares in SWS from which it receives dividends.

Southern Water Services Group (SWSG) – The immediate parent company of the securitised group which acts as a holding company for this group following the financial restructuring on 2003.

Southern Water Financing Group – Southern Water established a financing structure, known as a Whole Business Securitisation (WBS), in 2003 following its sale by ScottishPower. The aim of this refinancing was to reduce SWS's financing costs and gain access to long-term and secure sources of finance. Reducing financing costs ultimately benefits its customers in the form of lower bills. The securitisation structure continues to be in place today.

The financing group, whose immediate parent is SWSG, provides security to finance providers in the form of a charge over the share capital of SWS Group Holdings (SWSGH). No security is provided over SWS's individual regulated operating assets. This structure ensures that, in the unlikely event that either Southern Water or SWSF were to default on their debt obligations, SWS will continue to operate its business as usual. Debt providers are not permitted to either break up or interrupt SWS's business and can therefore only look to a new owner of the financing group to recover their debt in the unlikely event of serious default.

In 2003, a Common Terms Agreement (CTA) between the members of the financing group and its debt investors was established. The CTA sets out arrangements for the ongoing management of SWS's debt issuance programme as well as a number of operating arrangements in order to minimise the company's financial risk and adhere to good industry practice.

One of the CTA arrangements is a limit on the indebtedness of Southern Water and SWSF. This includes precautionary 'early warning' limits which prevent SWS from paying dividends if a limit is breached. The company ensures that it operates with sufficient financial headroom against these limits and has not breached a limit at any time since the implementation of the financing framework in 2003.

Southern Water Services (Finance) (SWSF) – SWS's financing subsidiary, SWSF, was established for the express purpose of raising debt finance on its behalf under the securitisation in 2003.

Due to administrative reasons applicable at the time of the WBS it was necessary for SWSF to be registered in the Cayman Islands in order to raise debt listed on bond markets. This requirement is no longer necessary but the cost of unwinding this structure is considered prohibitive.

SWSF is wholly and exclusively resident for tax in the UK and files tax returns only with HMRC. This means that any profit or loss made by these companies is subject only to UK tax.

Interest rate, liquidity and cash management risk

Southern Water hedges its exposure to interest rate risk on at least 85% of its outstanding debt liabilities in respect of Class A and Class B debt for the period to the next periodic review and at least 70% in the next period (on a rolling basis) into either index-linked or fixed rate obligations.

Additional funds are raised as required, to ensure that sufficient cash and/or facilities are available to fund the business for at least the next twelve months and both Southern Water (Greensands) Financing plc and Southern Water have debt covenants to this effect.

The Group sets exposure and minimum credit rating limits for deposits of cash balances.

The regulatory framework, under which revenues and the RCV are indexed, exposes the Group to inflation risk. This risk is managed through the use of index-linked instruments within the overall debt portfolio.

An analysis of net debt is included in note 29 to the financial statements.

Credit risk

For Southern Water, 82% of the water and wastewater services revenue is received from household customers. The Water Industry Act 1999 prohibits the disconnection of domestic customers for failure to pay water and wastewater charges. An extensive range of collection and recovery methods is employed, as appropriate to the individual circumstances of the customer, to minimise the risk of non-payment.

Following the opening of the competitive market on 1st April 17 non household customers are serviced by water retail companies under licence. Southern Water transacts directly with the water retailers for the Wholesale charges. The new market operates under strict guidelines governed by Ofwat which minimises risk of debt and non-payment. Failure to pay results in the retail company losing its licence.

The level of provision against non-collection of charges is reviewed on an annual basis, based on the age profile of the debt and the likelihood of recovery. A material increase in uncollected revenue, compared with that assumed in the setting of price limits, may provide grounds for an interim price determination by Ofwat.

Financial Risk

See page 30, included within the Directors' report.

Rating

Credit ratings for both Southern Water (Greensands) Financing and Southern Water Services are as follows:

Credit rating	Southern Water (Greensands) Financing	Southern Water Services
Standard & Poor's	BB-	Class A debt: A- Class B debt: BBB
Fitch	BB-	Class A debt: A- Class B debt: BBB
Moody's	Not applicable	Class A debt: Baa1 Class B debt: Ba1 Corporate family rating: Baa2

Fitch has also rated Greensands UK Limited long-term issuer default rating at B+.

During the year the credit rating agencies each reviewed their assessment of the credit ratings for Southern Water. The credit ratings of Standard and Poor's and Fitch remain unchanged and are Stable. Moody's updated the outlook on their credit ratings of Southern Water from Stable to Negative. This change reflects Moody's view of how well Southern Water is currently positioned to withstand a material reduction to the regulatory return on RCV after 2020.

The Group is fully in compliance with all of its covenants and the company has an internal business plan which is expected to stabilise the overall credit rating position.

Corporate Governance

Overview

GSH is a single-purpose entity, being the ultimate holding company for the only operating business in the Group, Southern Water. Accordingly, the GSH Board shares and supports the aims of the board of Southern Water for the long-term success of that company and also its commitment to maintaining high standards of corporate governance. Details of the governance of GSH are listed below, and those of Southern Water can be found in its Annual Report which is published on the Southern Water website.

Board membership and Chairman

The GSH Board comprises five members. Three of those members are appointed by a shareholder represented by JP Morgan Asset Management, one is appointed by shareholders represented by UBS Asset Management and one is appointed by shareholders represented by Hermes Investment Management. Another shareholder appoints an observer to attend and take part, but not vote, at Greensands Board meetings.

The former Chairman of Southern Water Services, Robert Jennings, was also independent Chairman of the GSH Board, which meets four times a year. The purpose of GSH is to act as a single-purpose entity, being the ultimate holding company for Southern Water, providing the financing structure for the Group. As a consequence, the GSH Board complements and supports the aims of the board of Southern Water for its long-term success. In his role as Chairman, Robert united the respective Boards in this common aim. Taking this into consideration it was felt that his cross directorship did not undermine his independence.

Following Robert's resignation in February 2017, Bill Tame was appointed Chairman of Southern Water Services. A chairman of GSH has not yet been appointed. Therefore, from 1 March 2017 no independent members of the SWS board sat on the Board of GSH.

Board operation

GSH is party to the shareholder agreement between the shareholders in the Greensands consortium. Under that agreement, the GSH Board members, apart from the Chairman (if one has been appointed), also comprise the Boards of the six subsidiaries down to Greensands Investments. Two of those directors comprise the board of Southern Water Capital. Apart from the previous Chairman, no director of GSH is also a director of Southern Water, although two were alternate directors for the shareholder-nominated directors on the Southern Water board during the year.

The GSH Board meets at least four times a year on its own. The normal business at such meetings is to agree formally any changes in membership, to note any relevant shareholder activity and to approve formally any transfers of shareholdings. The GSH Board is present with the Southern Water board at the regular monthly meetings of that Board, to consider the operational and financial performance reports of that company. That financial performance does, of course, represent the principal financial performance of the Group.

The GSH Board members are very mindful of the independence of the directors of Southern Water, but can bring additional knowledge, skills and resources of their nominating shareholders and employers, as well as their own personal skills, experience and knowledge of businesses and business sectors similar to that of Southern Water.

For compliance with Condition P of Southern Water's Licence, the shareholders who are considered to be the Joint Ultimate Controllers of Southern Water have given undertakings to provide all necessary information to that company, not to cause Southern Water to breach any of its obligations and to ensure that there are not fewer than three independent non-executive directors on the Southern Water board. Copies of those undertakings are published on Southern Water's website.

GSH does not have any executive directors nor dedicated management employees.

The GSH directors are not remunerated by GSH for their appointments.

Role of the Company Secretary

The Company Secretary is Joanne Statton who is also Company Secretary of Southern Water. All directors have access to the advice and services of the Company Secretariat team. The Company Secretary is responsible for ensuring that the Board operates in accordance with its governance framework and that there are good information flows to the Board. The appointment and removal of the Company Secretary is reserved to the GSH Board.

Director induction, training and development

GSH directors take advantage of the induction and training opportunities available to Southern Water directors as appropriate. On appointment to the Board, a director will discuss and agree induction coverage and then an appropriate comprehensive and individualised induction pack is provided, which will include information on Southern Water and the holding Group structure, the regulatory framework of Southern Water, customer service and the operation of assets, strategic plans, financial reports, business plans and the governance framework. This and further relevant information is summarised in a directors' handbook.

Board meetings

The Board held four scheduled meetings during the year. In addition the GSH Board met to approve the disposal of Southern Water's non-household retail business, the changes to shareholding (disposal by Future Fund) together with associated Director changes, the approval of Southern Water's bonus issue of share capital and capital reduction exercises changes to our Eurobonds and dividend payments. The agenda and papers are sent to the Board members in advance of each meeting. The Board generally holds its meetings where the board of Southern Water is meeting that month.

The Board has no standing committees.

Table of attendance at Board meetings

Attendance at scheduled Board meetings in 2016–17			
Robert Jennings (resigned as Chairman 28 February 2017)	3/3	Michael Nagle	4/4
Andrew Truscott Brian Goodwin as alternate to Andrew Truscott	2/4 1/1	Paul Moy (resigned 20 July 2016) Bronte Somes as alternate to Paul Moy (resigned 20 July 2016)	0/1 1/1
Randy Daniels (appointed 28 June 2016)	3/3	Robert Wall (appointed 15 March 2017)	0/0
Jeff Woodard (resigned 19 May 2016)	2/2	Hamish de Run (appointed 28 June 2016 and resigned 15 March 2017)	3/3
Bronte Somes (appointed 20 July 2016) Jeff Woodard as alternate to Bronte Somes (appointed 20 July 2016 and resigned 26 April 2017)	2/3 1/1		

Annual General Meeting

As a result of changes in Jersey Company Law, to bring it in line with Company Law in England and Wales, GSH, as a private company, is no longer required to hold an AGM. As a result the Board has decided that it will no longer hold an Annual General Meeting.

2) Southern Water Services Limited

Strategic Report summary:

Southern Water Services Limited is the only operating company of the Group. The financial statements of Southern Water, containing a full Strategic Report and Corporate Governance report, are published alongside these financial statements on the Southern Water website. An overview of the performance of the company is provided below.

The Strategic Report, in the following pages, will focus on Southern Water's collective performance over the past year. While it is pleasing to report that the company has achieved a number of successes, it will also be highlighting some of the key challenges the company faces as a business and some of the opportunities for transformation in the future.

Southern Water continues to deliver on the commitments it has made to its customers for 2015–20, maintaining performance in several areas of its operation, such as, preventing pollution and flooding incidents and odour prevention, while sustaining a positive improvement trajectory in customer service. The company intends to build on these areas of good practice as it moves forward, playing to its strengths and performing to its potential in every area of its business.

Southern Water will also be focusing on those areas where it has not performed well, and improving communication with its regulators, customers and stakeholders about the issues that are important to them. By proactively engaging in this way the company will address challenges with its historical performance reporting and data quality so all its stakeholders can have confidence that the company is delivering on its promises and improving its levels of service.

By working collaboratively, sharing ideas and developing innovative solutions, Southern Water will continue to improve in those areas where it is already doing well, while also making the changes necessary to ensure it is seen as a leading company that we can all be very proud of, and that delivers the sustainable service its customers expect.

Serving our customers

Over the past year Southern Water has completed an end-to-end assessment of its customer service processes, working to improve responsiveness and to ensure it is focusing on the individual needs of its customers. The company has looked at how it can make it easier to do business with itself online, over the phone or face-to-face, resulting in improvements to its website and customer contact centre.

Southern Water's new online services portal allows its customers to manage their account, at a time that is convenient to them, while the expansion of proactive and digital teams in its contact centre has increased the number of problems it is able to solve, quickly, before they become an issue for its customers. This new approach has increased customer satisfaction and driven down complaints so the company is confident that these improvements are adding value to its customer experience.

A key focus for Southern Water over the past year has also been improving its contact with some of its most vulnerable customers. The company has been working closely with partner organisations, such as the Citizens Advice Bureau and housing associations to identify those in challenging circumstances so it is then able to apply a more targeted approach to its service. The company plans to continue to build on these partnerships in the year ahead so it is able to extend the reach of its support services to those most in need.

A changing landscape

The water industry is changing, and at pace. Competition has already been introduced this year, with its former non-household customers now able to choose their water provider for the first time. Southern Water decided to sell its non-household retail business to Business Stream, a specialist company in this field. Similar changes are being discussed for household customers too, although ministers have not committed to making a decision on whether or not to introduce household competition until the end of this Parliament.

Increased competition does not mean any differences in regulatory scrutiny, in fact it will lead to a need for more transparency and consistency. The information Southern Water reports to its stakeholders is rightly, constantly under review by its regulator, Ofwat, and this year the company fell short of its requirements. Ofwat assesses companies into one of three categories based on the level of trust it has in the information it receives from them. Its level of trust and confidence in Southern Waters reports, chiefly relating to data quality, transparency, board governance and narrative explanations for stakeholders, had reduced. As such, Ofwat assigned the company an assurance rating of 'prescribed' – lower than its previous rating of 'targeted'.

The Southern Water board responded immediately and, with the company's executive team, instigated an urgent review of the quality measures applied to its published information. As a result, Southern Water has made substantial improvements in a number of areas and will continue to make further improvements in order that its customers and stakeholders can have confidence in the way it presents its information.

These steps were detailed in its revised Final Assurance Plan, published in March of this year. Ofwat's feedback also helped to inform the new structure of this report for 2016–17, with the introduction of a new governance reporting framework, more detailed data quality information and the introduction of more transparent performance reporting and case studies in the Strategic Report.

While Southern Water were pleased to exceed its target level of compliance against the Drinking Water Inspectorate's (DWI) quality measures this year, it raised some concerns regarding the company's monitoring and reporting processes, and its compliance with Water Quality regulations regarding the collection of the required number of samples. While Southern Water has made substantial improvements in some areas, it is recognised that it has further improvements still to make. The company is working closely with the DWI to address these. The DWI's concerns are outlined in Southern Waters updated Statement of Risks, Strengths and Weaknesses, January 2017, and Final Assurance Plan, March 2017, which are available on Southern Waters website – southernwater.co.uk/our-reports.

The company provides a significant amount of data to the EA about the performance of its assets and any wastewater or sewage discharges it makes into what is known as the 'water environment', such as rivers, streams and coastal waters. Southern Water has identified the need to review and improve its end-to-end reporting processes with a view to implementing process and control improvements. Detailed process reviews have continued and a programme of improvements is being developed. The company will establish a programme of rolling audits of its EA reporting and data integrity, starting with the 2017–18 internal audit programme of assurance. In addition, it will complete assurance of the 2015–16 and 2016–17 data. Independent external assurers will be assigned to the review, which will commence in August 2017.

As mentioned previously, Southern Water is also working with Ofwat in relation to the management and operation of its wastewater treatment works and the reporting of relevant information in connection with them.

Innovation and resilience

Southern Water's customers expect a constant supply of safe, clean water and it takes the delivery of this service very seriously. Which is why although the company exceeded its compliance target for water quality, achieving 99.96%, Southern Water was disappointed that in 2016–17 it fell short of its leakage targets. This is an area where historically the company has performed strongly. The company is working hard to continue to improve its performance and it remains on track to hit its five-year target.

Over the past year the company has had a number of operational successes in terms of its management of water pressure on its network and a reduction in the number of complaints about discolouration. The number of properties receiving low pressure dropped during the year to 222, fewer than its target of 257 properties, while just 1,825 of our 2.4 million drinking water customers notified Southern Water of discolouration in 2016.

The performance of Sothern Water's wastewater treatment works was also strong and we are pleased to see a reduction in pollution incidents. The company is also ahead of its promise commitment to increase the amount of renewable energy it uses across its operations.

Southern Water saw a 4% reduction in flooding incidents over the past 12 months as a result of previous flood mitigation work and its planned maintenance activity, and overall, since the start of the current five-year period, external flooding incidents have reduced by 18%. However, there is still more to do and partnerships with customers will help move this work forward.

As a provider of water and wastewater services to an ever-increasing population, Southern Water needs to continue to improve its service offering, providing innovative solutions to ongoing challenges such as climate change, population growth and water scarcity.

Southern Water is already developing these solutions in a number of areas:

- Looking at the opportunity to purchase abstraction licences, which are currently owned but not used by farmers and industries.
- Developing water re-use schemes that allow Southern Water to take highly treated wastewater and put it back into the natural water cycle, before abstracting it again and treating it to drinking water quality standards.
- The company is fitting monitors to its sewer overflows, which help track flows and prioritise areas for investment and improvement to protect the natural environment.
- The company is investing in the development of new drainage systems that manage the impact of

development and increasing amounts of rainfall entering sewers and drains.
- The company is also trialling new technologies that allow it to extract energy from its water and wastewater treatment processes. This includes looking at new nutrient extraction technology to protect its water supply and potentially using extracted materials to generate products that have value elsewhere.

You can read more about the innovative solutions the company is developing to embrace these future challenges in its 'Sustainability and environmental' responsibility section of its annual report.

Working in partnership

In addition to working with its supply chain contractors to deliver day-to-day services to its customers, Southern Water partners with a variety of organisations across its region to further improve its service and resilience levels.

Southern Water is already working with farmers, landowners and environmental organisations to better manage its wider area – catchment management – ensuring the region's natural assets are more secure and viable as a continuing source of water.

To reduce Southern Water's impact on the environment, the company is teaming up with university and technology experts to help it better understand, predict and model changes. The company is also trialling new technologies and processes that limit pollutants being released into the environment, to help maintain higher quality bathing waters.

Another innovative partnership under way is the Integrated Water Resources Plan for the whole of the South East. This goes beyond water companies, to embrace all those who abstract water from the environment and have a role in ensuring water is not wasted. This involves setting up collaborative partnerships with a range of industries, such as agriculture and tourism, in order to look holistically at all the factors influencing water supply, demand and wastewater disposal.

The challenges of water scarcity, population growth and climate change facing the South East will require greater collaboration both within and across sectors. It will be a critical part of achieving outcomes, which deliver long-term resilience with multiple benefits from both the water and wastewater parts of Southern Water's business. It is only by working with partners in this way that the company can really start to make solid plans for the future, looking beyond 2020.

Looking after each other

In order to deliver this step change, Southern Water knows that it needs to look after its employees by fostering a safe working environment, providing continuous professional development, equal opportunities for all and creating a rewarding place to work.

The company wants to encourage a culture where it is collectively responsible, for not just for its own safety, but also and for ensuring it looks after its customers and each other. This year Southern Water launched a new Speak Up policy, which actively encourages all employees to raise concerns about practices or situations that could affect its business.

While Southern Water recorded an increased number of reportable injuries in 2016–17, the company is pleased to report that it achieved the Royal Society for the Prevention of Accidents' gold award for Health and Safety for the 18th consecutive year. The company's aim is to continue to build on its reputation for strong health and safety performance over the coming year, with a particular focus on its wellbeing initiatives, which are designed to encourage good personal physical and mental health.

Good employee engagement is increasingly becoming one of the key differentiators in business. Put simply, engaged employees and high-performing teams help drive safety, productivity, profitability and customer focus.

Over the coming year Southern Water will be renewing its focus in this area, and the company will be taking a fresh look at its company brand and its story. This will help it to align its business priorities with individual team objectives, encouraging local level action planning to help drive positive change and improvements across the company.

The company's commitment to talent management is visible throughout the business. Southern Water continues to safeguard its future by taking on young people as trainees and graduates. The company is among the first in the water industry to train all its operators to NVQ level 3, while it also has a number of its operational leaders undertaking the Level 4 Diploma, ensuring that the company has continued investment in water and wastewater management skills.

Not only are Southern Water encouraging the development of skills within its business, the company continues to lend active support to a variety of initiatives to promote Science, Technology, Engineering and Maths careers to young people so that it is able to recruit from the broadest possible talent pool.

Our community

Over the past year Southern Water has actively contributed to the wellbeing of its customers and its communities. As well as launching a new community grants scheme, its employees gave 4,000 hours – almost 560 days – of their time to help community projects through its company volunteer scheme.

Southern Water's Learn to Swim scheme celebrates its 25th anniversary in 2017. During that time more than 750,000 children across the region have been taught how to stay safe around water. This year the company helped to teach more than 14,000. It is a source of great pride to everyone in the company that it is able to do its bit to keep our children safe.
Southern Water continued its partnerships with local schools, sports clubs and theatre companies to educate customers about how the company can save water and prevent blockages and sewer flooding. And through a variety of fundraising events and local initiatives it also raised a total of more than £139,890 for various regional charities over the course of the year.

Financial results

During 2016–17 Southern Water's operating profit was £258.9 million, a reduction of 9.0% from the previous year.

The 2015–16 operating profit included a one-off benefit from the refund of historical business rates charges of £13.3 million. Taking this into consideration, the company's operating profit reduced by £12.3 million and was principally the result of increased depreciation charges, which result from the continued significant investment in its assets.

In total Southern Water's revenue increased by £6.0 million to £809.7 million reflecting increased customer numbers from new connections and higher levels of billed consumption in part offset by an overall reduction in its tariffs. This increase in revenue was offset by a similar increase in underlying operating costs.

During the year Southern Water has undertaken a number of initiatives specifically targeted at improving its customer service performance. These increased its operating costs by £4.0 million and have focused on reducing complaints, assisting customers in financial hardship and improving its future bad debt performance.

The costs associated with these initiatives together with inflation on its cost base were, in part, offset by the delivery of operating efficiencies totalling £8.6 million. These efficiencies were delivered through a focus on reducing Southern Water's power consumption, in particular minimising usage at peak times and making improvements to operational processes, for example reducing chemical usage and waste disposal costs.

Southern Water believes these initiatives and efficiencies, along with the continuing delivery of its capital investment programme will enable it to continue to make improvements over the coming year and assist in the delivery of the promises it made to customers and stakeholders in its business plan.

The road ahead

Southern Water has had both a successful and challenging year, and the company is determined to build on its strengths and eliminate any weaknesses.

The sector is changing and over the next three years Southern Water intends to embrace these changes and continue to innovate to improve its service levels in order to meet the promises it made to customers in its business plan 2015–20. And, as the company begins its customer consultation and price review process and plan for 2020 onwards, it looks to create a resilient and sustainable business model that will rise to challenges facing the business and the sector as a whole while defining its role in relation to the environment.

Southern Water risks

Risk management is a core component of Southern Water's wider governance and internal control framework, which provides the overarching structure through which the company is managed to achieve its objectives.
The most significant risks facing the company are referred to as 'the principal risks'. These risks are considered by its Executive Leadership Team and board to have the greatest potential to affect the achievement of strategic objectives, based on outputs from the "top down" and "bottom up" risk assessment exercises and its ongoing review and monitoring.

The Southern Water board is responsible for determining the nature and extent of the principal risks it is willing to take in achieving its strategic objectives.

The company's strategy for risk management is that all principal risks are identified, assessed and managed to within acceptable levels. To achieve this, the board and management promote a culture that encourages routine consideration of principal risks in key decisions and supports integration of risk management with its critical processes and ways of working. Risk management and internal control systems are monitored by its board. This covers all material controls including financial, operational and compliance controls.

The purpose of the company's approach to risk management is to support better decisions through an improved understanding of risk.

Figure 1: Southern Water Risk management process

The objectives of the company's risk management strategy are to:

- identify and understand all the principal risks that it faces
- select and proactively take the risks that give it the right returns, and understand their potential impact on the company
- take action to manage the risks the company does not want to be exposed to, ensuring its resources are effectively and efficiently prioritised and used
- monitor and report the risks it is taking against its desired strategic objectives.

Every employee is responsible for helping Southern Water to effectively manage the company's risk exposures and making it a more resilient organisation, able to successfully respond to its changing environment.

Southern Water ensures controls are in place so it can take action to minimise the impact of risks. To do this, risks are managed through a central database where they are ranked and assigned to senior managers who are responsible for implementing mitigation plans. Risks are reviewed each month and the highest are escalated to its Executive Leadership Team, the board and the Audit and Risk Review Committee. Any new risks added to the database with a score above a certain level are passed to a director and Chief Executive Officer for immediate review.

Risk appetite is the Southern Water board's expression of the types and amounts of risk it is willing to take or accept in pursuit of its objectives. The mitigating actions applied to each principal risk are considered by the board against the effectiveness of the existing control environment. This determines the appropriate level of response to ensure compliance with the board's group risk appetite, policies and procedures, and management plans and objectives.

The principal risks Southern Water faces are disclosed below:

Unchanged in the year | Risk reduced in the year | Risk increased in the year

Customer

Customer service

Commentary: Increasing customer expectations and rising standards of customer service across the sector mean that Southern Water may incur financial penalties if the company does not continuously improve its customer service performance.
The Service Incentive Mechanism (SIM) was developed by Ofwat to incentivise improvements in customer service and compares performance across the water sector.

Southern Water's SIM performance for 2016–17 has improved compared to prior years. A continued improvement will be required over the next three years to avoid a financial penalty for this business plan period at the next Price Review.

Southern Water has set challenging targets, including, for example: identifying then reducing our unwanted call volumes and its improvement programmes are working to deliver these for its customers.

Mitigation: Improvements to customer service are being made continually. Southern Water plan to use more insight into customer trends to design a broader range of tailored services and training for its staff.
The company continues to actively engage with its customers and stakeholders in order to strengthen its links with local organisations such as councils and community groups.
Southern Water will continue to improve its customers' experience by providing enhanced online facilities for them to manage their accounts. Where customers do need to speak to the company directly, it has ensured the opening hours of its contact centre are convenient and its bills will be redesigned to make them easier to understand.

Outcomes affected: Responsive customer service; Better information and advice

Bad debt

Commentary: The level of customer bad debt, which cannot be recovered and has to be written off as a loss, continues to be a significant issue for the water industry. In the current economic climate, there is a risk that the number of customers who do not pay their bills will increase. This puts an additional burden on customers who do pay their bills.
Southern Water notes that the ongoing Brexit process may adversely affect the economic climate and customers' ability to pay.
In 2016–17, the bad debt charge to the income statement increased to £25.3 million (2015–16: £21.5 million).

Mitigation: The company understands that some customers may experience financial difficulties, particularly in difficult economic times. Southern Water encourages customers who are struggling to make payments to contact its Affordability Team as early as possible. To assist those in difficulty it offers a range of flexible instalment plans and tariffs, including the introduction of a social tariff from April 2015. Southern Water is proactive in collecting payment from its customers and in helping households to pay their bills and debt. When necessary, the company also uses a leading debt management system, and a panel of Debt Collection Agencies, to recover overdue payments to keep bad debt to a minimum.

In addition Southern Water has partnered with Orbit, a company that provides specialist debt advice to customers in financial difficulty.

This year the company will be enhancing its customer data to enable Southern Water to tailor the experience they receive in order for the company to reach out to those customers who may be in financial hardship, quicker. Southern Water is also looking at new schemes, tariffs and additional services it can offer customers who are in vulnerable circumstances.

Outcomes affected: Responsive customer service; Affordable bills; Having a firm financial footing

Climate

Resilience to drought

Commentary: Some areas of the South East are classified as areas of "severe water stress". Climate change and more variable weather patterns are predicted to pose an increasing challenge for all water companies in the region in future years in terms of the volume of water available.

Given that Southern Water supplies drinking water to more than one million households across Kent, Sussex, Hampshire and the Isle of Wight it is critical that the company is able to ensure it has access to adequate water resources to supply customers and support the economy.

After the lower than average rainfall received during the winter of 2016–17 and subsequent spring, this risk has increased.

Mitigation: Through its investment planning process, Southern Water identifies and then develops those schemes which are necessary to ensure it can meet anticipated demands for water over the next 25 years. The company's long-term investment plan sets out the additional measures that it will take across the region to achieve its target for the Security of Supply Index. These measures include schemes such as: leakage reduction, strategic transfers and the development of new resources. The company has also completed its Universal Metering Programme with nearly 90% of customers now having a meter.

Should a drought occur, as in 2012, the company has a Drought Plan which it would follow to introduce measures to conserve water and secure additional resources through Drought Permits and Drought Orders and by changing the way in which it operates its sources. Southern Water also maintains its Water Resources Management Plan, using an industry-leading approach which allows it to plan to operate under a wider range of droughts than it has seen in the past.

Outcomes affected: A constant supply of high-quality drinking water; Looking after the environment

Preventing flooding of our sites and from our network

Commentary: Changing rainfall patterns, more frequent storms and rising sea levels, could all lead to an increased risk of flooding if volumes overwhelm Southern Water's assets. Excessive rainfall results in high groundwater levels which are not possible to control, causing flooding to private land and property, contamination of water supply, infiltration/inundation of sewers and a breach of flood defences and protection. The serious floods in recent years have also highlighted the need to protect its water and wastewater treatment works and pumping stations from being affected during a flood.

Southern Water has met, or improved upon, its business targets this year for sewer blockages, sewer collapses; external flooding, and internal flooding incidents as a result this risk has reduced.

Mitigation: To help combat this risk, Southern Water has prioritised schemes for investment in 2015–20. It is investing £426 million during this period to provide a reliable and effective wastewater service, part of which will be used to keep its 39,594 kilometres of sewers and 3,243 wastewater pumping stations well maintained. It will also fund the replacement or refurbishment of about 100 kilometres of sewers, with the parts of its network in most need of repair and of most structural use targeted first.

Southern Water is also focusing on reducing the risk of blockages, which are a major cause of flooding from sewers. This will include carrying out targeted surveys of its sewers using cameras, performing regular sewer cleaning work, and putting more resources into keeping its drainage plans up to date to fully understand how much capacity it will need for the years ahead. The company will also provide its customers with better information about the causes of blockages and how they can prevent them. Through investment of £268 million, it intends to ensure there is no increase in the number of blockages in its sewer network.

Outcomes affected: Removing wastewater effectively; Looking after the environment

Operational

Resilient supply of good quality water

Commentary: Southern Water must ensure it can supply enough drinking water to cater for a growing population of more than two million people. Should operational treatment processes fail, the water supply becomes contaminated, or its water distribution network fail:

there is a risk that water could be supplied to customers that is unfit for consumption, and would require a widespread boil water notice in order to protect public health;
large numbers of customers could find their water supply becomes cut off; and
harmful chemicals could be released to the environment.

This could cause damage to its reputation, and lead to prosecution and fines by the Environment Agency or the Drinking Water Inspectorate (DWI).

DWI enforcement actions are referred to in Southern Water's annual report.

The only water quality and supply resilience performance target the company failed to meet or improve upon during the year was leakage. Southern Water achieved a figure of 88.1 million litres per day, which exceeded its target of 87.1 million litres per day.

Mitigation: To avoid such incidents Southern Water prioritises investments in the maintenance of critical assets and technology. It also makes sure its employees follow company processes and procedures. New employees are also trained in these processes and procedures.

In the event of interruption to supply, emergency plans have been developed to ensure continued supply of water to customers, either through use of alternative supply pipes, tankering or provision of bottled water.
The company has provisionally achieved drinking water quality compliance of 99.96%. Its business plan 2015–20 includes schemes to add carbon filters and other more advanced filters at its water treatment works in high risk areas such as Hastings, to help improve the taste and smell of water. The activities to improve water quality include upgrades to wells and boreholes, service reservoirs and water supply works, as well as flushing mains and cleaning service reservoirs, which store water underground before it is pumped to customers' taps.
To avoid problems associated with nitrates and pollutants being washed into rivers from high surface run off after heavy rain, the company has processes to stop water abstraction during and after heavy storms. Drinking Water Safety Plans have been completed which identify where and how problems can arise with drinking water quality and cover the entire supply system, from catchment to customers' taps.

Outcomes affected	A constant supply of high-quality drinking water	Looking after the environment

Operational (continued)

Cyber security

Commentary: Southern Water provides water and wastewater services to customers across its regional infrastructure, which is considered critical national infrastructure.

As a result, the company recognises its operational and enterprise IT systems may be a potential target for cyber threats which could have a significant impact on its business reputation and operational assets.

Additionally, because of the nature of its activities, it holds and process large quantities of data considered sensitive within the meaning of the Data Protection Act, including personal data on its customers and employees. Therefore the protection of the security and integrity of data under its control is of utmost importance.

Mitigation: Southern Water manages this risk through IT security standards, ongoing monitoring of threats to, and activities on, it's IT infrastructure as well as incident management plans.

The company continues to invest in cyber threat mitigation strategies in response to the changing risk landscape and it works with the Centre for Protection of National Infrastructure. Over the past 12 months the company has used industry experts to review its cyber security maturity and help develop an improvement plan.

The company undertakes penetration testing to assure its security measures during the year or when it makes improvements to the IT environment.

Southern Water has clear policies identifying the need to have in place safeguards surrounding the collection, handling, storage and destruction of personal data, and ensuring its compliance with the Data Protection Act (DPA). This policy is supported by Data Protection training which is mandatory for all staff, and assured via the Letter of Compliance process.
The company's data protection policies are currently being updated to ensure it complies with its obligations under the General Data Protection Regulation (GDPR), which replaces the DPA in May 2018.

Outcomes affected	Responsive customer service; Removing wastewater effectively; A constant supply of high-quality drinking water; Having a firm financial footing; Better information and advice; Looking after our assets

Operational (continued)

Wastewater treatment works failures and pollution incidents

Commentary: Southern Water's region benefits from a high quality environment, both inland and coastal. It is fortunate to have some extremely rare habitats, as well as some of the best quality river fishing and coastline in the UK.

One important factor affecting the long-term quality of the environment is the nature, volume and frequency of permitted discharges into them. The company has a number of carefully managed infrastructure assets which are allowed to discharge into the receiving environment.

Reliable wastewater services are essential to maintain public health and protect the environment. Ensuring its assets operate effectively is critical in minimising the risks to public health and/or the environment from pollution and/or sewer flooding.

As well as the potential to cause damage to the environment or distress to customers, incidents like these can also lead to prosecution and fines by the Environment Agency and cause damage to the company's reputation.

The performance of Southern Water's wastewater treatment works continued to be strong during 2016–17 (though this remains subject to further assurance).

As mentioned previously, Southern Water is also working with Ofwat in relation to the management and operation of its wastewater treatment works and the reporting of relevant information in connection with them.

Mitigation: Southern Water continues to operate and maintain its assets effectively.

The company monitors the functionality and performance of its assets on a continuous basis through a central control room. It also monitors any instances when its Combined Sewer Overflow (CSO - back up over flow pipes) are used, to proactively ensure it can identify infrastructure under stress. This, together with its new works management system, has significantly improved the way in which the company dispatches work. It can respond quicker to asset-related events and deliver the required planned preventative maintenance more efficiently.

The majority of the company's £1.8 billion capital investment programme for 2015–20 is targeted to maintain, enhance and extend its wastewater and water sites and networks to reduce the risk of asset failures and asset-related incidents. This investment allows Southern Water to ensure a resilient wastewater service whilst accommodating increases in demand as a result of population growth, meeting new environmental standards and adapting to climate change.

In the last year Southern water has invested £45.2 million at its wastewater treatment works and pumping stations to reduce risks at critical sites, and invested £11.5 million in sewer maintenance and rehabilitation.

In addition, its customer-orientated fats, oils and grease educational programme is targeted at those catchments with blockage hotspots. Southern Water is also increasing customer awareness about how to avoid blocked drains.

Outcomes affected: Removing wastewater effectively; Looking after the environment

Operational (continued)

Health and safety

Commentary: The health and safety of the company's employees and the public in the provision of its services is its highest priority. The nature of its work requires that the employees and contractors undertake activities or use equipment which, if uncontrolled, has the potential to cause significant harm. Southern Water and its contractors have comprehensive processes and procedures to prevent injury and occupational ill-health. Failure to comply with its Health & Safety Management System could result in death, serious injury or adverse health effects. In addition to the personal impact these would have, it could be liable for prosecution under the Health and Safety at Work and Corporate Manslaughter Acts. In addition, there would be a significant reputational risk arising from the adverse publicity.

Mitigation: Southern Water has taken all necessary steps to ensure the potential health and safety risk is suitably mitigated and controlled. It has a clearly defined strategy, safety protocols and standards that are set. Health and safety performance and compliance is monitored and reported to the board on a monthly basis and to the tri-annual board Health and Safety Committee. The Executive Leadership Team monitors health and safety performance via detailed reports at the monthly Health and Safety Management Review meeting. This group ensures there is an adequate system for meeting its responsibilities to its staff, customers and members of the public. These services have been developed and are continuously reviewed to ensure they meet the needs of the business and its employees at work.

All staff receive suitable health and safety training, and the company has a campaign to encourage staff to report 'near misses' or hazards at work to help further reduce the risk of injuries or ill-health. Additionally, every employee has ready access to a copy of the corporate policy statement and health and safety processes and procedures.

Outcomes affected	Having great people	Working in partnership

Financial

Financing our business

Commentary: A significant change in interest rates, a reduction in the availability of credit to the water industry, or a decrease in the company's credit rating, could put its ability to finance its capital investment programme or refinance its existing debt maturities at risk in the future. This is required as a condition of its regulatory licence and its borrowing covenants, where a failure to maintain certain credit ratings could lead to a restriction in dividend payments.

As a minimum, the company intends to maintain its current risk profile. Southern Water only enters into treasury transactions to manage inherent risk and support prudent funding, not to speculate.

Its current credit ratings are:

- Standard & Poor's: Class A debt, A-; Class B debt, BBB
- Fitch: Class A debt, A-; Class B debt, BBB
- Moody's: Class A debt, Baa1; Class B debt, Ba1; Corporate family rating Baa2.

During the year, Moody's updated the outlook on the credit ratings of Southern Water from Stable to Negative. The change to outlook reflects Moody's view of how well Southern Water is currently positioned to withstand a material reduction to the regulatory return on Regulatory Capital Value (RCV) after 2020. It will be considering this as part of our PR19 Business Plan submission.

Mitigation: Southern Water ensures that it maintains sufficient cash reserves and liquidity facilities to finance its operations for at least 18 months.

The company also ensures the aggregate nominal value of debt maturities does not exceed 40% of RCV in any single regulatory period (and 20% of RCV in any 24 months). Exposure to interest rate rises on its current borrowings is also hedged by a subsidiary company, Southern Water Services (Finance) Limited, and current borrowings are at either fixed rates or index-linked. Southern Water ensures that sufficient funds are available for its operational and capital investment programme through ongoing monitoring and forecasting of its cash flow and it take steps to manage this when necessary.

Credit ratings comprise regulatory framework, financial risk and operational risk. Regulatory risk is improving as the company gains clarity of PR19, albeit the key value for the weighted average cost of capital (WACC) is uncertain. Financial risk is stable for the current AMP6 (PR14) period, in part supported by its stated gearing targets. Operational risk is supported by its annual improvement since 2011.

Outcomes affected	Having a firm financial footing	Looking after our assets

Defined benefit pension scheme

Commentary: Southern Water operate a defined benefit pension scheme which has been closed to new entrants from 1 April 2005. The company remains liable for rights earned by past and present members of the scheme. Changes in demographics and fluctuations in investment markets may affect the cost of funding pension promises. Increased scrutiny of deficit recovery proposals by The Pensions Regulator could result in a higher funding requirement for the final salary pension scheme in the future. In addition to the regular dialogue with the Trustees Southern Water is also in ongoing discussions and correspondence with The Pensions Regulator regarding the current deficit and the Southern Water board are keen to agree a reasonable resolution of a long-term funding solution for the scheme.

Mitigation: The company has agreed a long-term funding and risk management strategy with the Trustees. This is monitored regularly by the company and the Trustees, and mitigating actions are reviewed and implemented as appropriate. Southern Water is currently in the process of agreeing the 2016 valuation with the Trustees.

Outcomes affected	Having a firm financial footing	Having great people

Strategy and Regulation

Compliance with regulations and legislation

Commentary: Southern Water is a highly regulated business with three main regulators: Ofwat, the Drinking Water Inspectorate and the Environment Agency. If the company does not meet the standards set by these bodies, it could face fines, legal action and, in the worst case, the loss of its appointment as a water and wastewater company.

This risk has increased since the 2016 Annual Report due to issues with its regulators Ofwat, DWI and the EA.

Last year Ofwat determined that Southern Water fell short in its reporting requirements to its stakeholders. Its level of trust and confidence in the company's reported information reduced, chiefly relating to data quality, transparency, board governance and narrative explanations for stakeholders. Consequently, Ofwat assigned the company an assurance rating of 'prescribed' – lower than its previous rating of 'targeted'.

The DWI has raised enforcement actions against Southern Water regarding its monitoring and reporting processes, and its compliance with Water Quality regulations regarding the collection of the required number of samples.

Southern Water provides a significant amount of data to the EA about the performance of its assets and any wastewater or sewage discharges it makes into what is known as the 'water environment', such as rivers, streams and coastal waters. The company has identified the need to review and improve its end-to-end reporting processes with a view to implementing process and control improvements. Detailed process reviews have continued and a programme of improvements is being developed. Southern Water will establish a programme of rolling audits of its EA reporting and data integrity, starting with the 2017–18 internal audit programme of assurance. In addition, it will complete assurance of the 2015–16 and 2016–17 data. Independent external assurers will be assigned to the review, which will commence in August 2017.

The performance of Southern Water's wastewater treatment works continued to be strong during 2016–17 (though this remains subject to further assurance).

As mentioned previously, Southern Water is also working with Ofwat in relation to the management and operation of its wastewater treatment works and the reporting of relevant information in connection with them.

Note – further details are included in Southern Water's updated statement of Risks, Strengths and Weaknesses, January 2017, available on its website at: southernwater.co.uk/our-reports.

Mitigation: During the year a number of issues were raised by the company's regulators. Southern Water agree that all of its stakeholders, especially its customers, should be able to have full confidence in the integrity of its data and so the company has begun a transformation programme to improve its performance and compliance in information management, project delivery and risk management. Southern Water report regularly on progress of this improvement programme to its regulators.

In relation to the comments raised by Ofwat in its Company Monitoring Framework (CMF) assessment, an internal working group has been formed which met regularly to review progress against the actions identified to improve its reporting for 2016–17. Southern Water has also discussed its proposals with Ofwat to improve its confidence in the company's approach.

Southern Water has procedures in place to comply with legislation and key procedures have been certified to meet relevant industry standards, including ISO 9001 and ISO 14001.

Internal monitoring and assurance is undertaken during the year and annual reporting is supported by external verification through its financial and technical auditors to provide assurance on compliance with its obligations.

Awareness training is provided throughout the company for critical compliance issues, such as the Bribery Act and Competition Law, to ensure everyone understands its legal obligations. All sections of the business review compliance with company procedures through self-assessment every six months, and implement improvement plans, if necessary.

Outcomes affected

Responsive customer service

Removing wastewater effectively

Looking after the environment

Having a firm financial footing

A constant supply of high-quality drinking water

Strategy and Regulation (continued)

Delivery of our capital investment programme

Commentary: Southern Water has a capital investment programme of £1.8 billion between 2015 and 2020. The company has plans in place to ensure it will deliver this and it is working hard to ensure its focus is maintained to complete all works on time.

If the company is unable to deliver significant parts of the programme on schedule, its ability to provide an excellent service to its customers could be compromised. Any failure to deliver would also prevent the company from fulfilling the promises that it has made in its business plan and lead to possible action by the Environment Agency, Drinking Water Inspectorate or Ofwat.

Capital expenditure in the early part of the programme is behind that set out in the business plan, increasing the risk in this area. Southern Water has worked this year to close this shortfall and it remains on track to deliver its required outcomes by the end of the investment programme in 2020.

Mitigation: Southern Water has transformed its capability during the course of the current capital investment programme to bring significant investment capability in house. This includes the establishment of an in-house engineering function, a specialist programme management function and asset planning systems, processes and capabilities. Progress against the capital programme is overseen by its Investment Committee and the company has adapted its monthly reporting procedures to ensure the delivery of the business plan is given the greatest level of focus within the company. The company works closely with its regulators and other interested parties to resolve issues as they arise.

Outcomes affected	Responsive customer service	Removing wastewater effectively	Looking after the environment	Having a firm financial footing
	A constant supply of high-quality drinking water			

Strategy and Regulation (continued)

Regulatory reform

Commentary: During recent years, there has been a significant focus on reform within the water industry, concentrating on the introduction of competition and a greater use of market mechanisms to promote innovation and efficiency. From April 2017, the retail market for non-domestic customers opened, which required structural changes within the company to allow Southern Water to continue to comply with regulatory requirements and to manage the anticipated shift in customer base.

The regulatory framework continues to evolve as it is reviewed to ensure that it is fit for the challenges of the future. This includes assessing the costs and benefits of extending retail competition to all residential customers and proposals to move to CPI instead of RPI as the basis for setting price controls.

The company's current business plan and approved pricing structure, runs until 2020. Southern Water has therefore commenced projects to prepare for Ofwat's next Price Review process in 2019 (PR19) and to plan for 2020 onwards. Its challenge is to present a business plan to Ofwat that will deliver improvements for its customers and its infrastructure according to an equitable pricing structure by the submission deadline at the end of 2018.

Southern Water must also ensure it continues to monitor and adapt to any changes in the assessment criteria it is measured against by the Drinking Water Inspectorate and the Environment Agency.

Mitigation: Throughout the fiscal year Southern Water engaged constructively with Ofwat and Defra on the proposals for market reform. The company actively participated in numerous workshops held by Ofwat, Open Water and Market Operator Services Limited (MOSL). It established a market readiness programme to co-ordinate the changes required in the business, including a steering group chaired by our Director of Strategy attended by its Chief Executive and Chief Financial Officers.

After considering a number of options, Southern Water made the decision to sell its non-household retail business to Business Stream, a specialist company in this field. The market opened successfully on 1 April 2017.

In order to prepare for the PR19 Price Review process, Southern Water has instigated projects to consult with its customers and determine the core values and outcomes that matter most to them and integrate within its next business plan. The company is also initiating projects to prioritise the areas within it that it will focus on from 2020 onwards.

Southern Water continues to closely monitor developments in the requirements from its regulators Ofwat, The Drinking Water Inspectorate and the Environment Agency. To anticipate any such changes the company has proactively initiated programmes of investment in its infrastructure that will help it to be prepared and resilient to their changes.

Outcomes affected	Responsive customer service	A constant supply of high-quality drinking water	Affordable bills	Removing wastewater effectively
	Looking after the environment	Better information and advice	Having a firm financial footing	Looking after our assets

The Strategic Report was approved by the Board of Directors and signed on its behalf by the Company Secretary.

Joanne Statton
Company Secretary
18 July 2017

Directors' report for the year ended 31 March 2017

The directors of Greensands Holdings Limited (Registered Number: Jersey 98700) present their report and the audited financial statements for the year to 31 March 2017.

Group

Greensands Holdings Limited (the company) was incorporated on 28 September 2007 as the parent company of Greensands Europe Limited, whose subsidiaries include Greensands Investments Limited.

On 15 October 2007, the company became the ultimate parent company of the Southern Water group of companies, via the acquisition of Southern Water Capital by Greensands Investments Limited.

Principal activities of the company

The company's principal activity is that of a holding company for Greensands Europe Limited and its subsidiaries. The directors expect the company to continue to carry out these activities in the future.

Principal activities of the Group

The principal activities of the Group are the provision of water supply and wastewater services in the south-east of England.

The trading results reflect the performance of the major trading subsidiary Southern Water Services Limited (Southern Water).

Strategic report

The information that fulfils the requirement of the Strategic Report can be found in the Strategic Report sections on pages 2 to10 and pages 13 to 27.

Future developments

The information regarding future developments of the company can be found in the Strategic Report sections on pages 2 to 10 and pages 13 to 27.

Results and dividends

The consolidated statement of other comprehensive income on page 33 shows the Group's results and loss for the year. Further details are also available in the Strategic Report section on page 2.

Ordinary dividends of £108.2 million were declared during the year ended 31 March 2017 (2016: £82.1 million). Of these dividends £54.0m was paid during the year and the final dividend of £54.2m was paid after the year end.

Directors and their interests

The directors who held office during the year ended 31 March 2017 and up to the date of signing the financial statements, unless otherwise stated, were as follows:

Robert Jennings	Independent non-executive Chairman (resigned 28 February 2017)
Michael Nagle	
Andrew Truscott	
Brian Goodwin	(Alternate to A Truscott)
Bronte Somes	(Appointed as director and resigned as alternate to P Moy 20 July 2016)
Jeff Woodard	(Resigned as director 19 May 2016, appointed alternate to B Somes 20 July 2016). (Resigned as alternate director 26 April 2017)
Robert Wall	(Appointed as director 15 March 2017)
Hamish de Run	(Appointed 28 June 2016 and resigned as director 15 March 2017)
Randy Daniels	(Appointed 28 June 2016)
Paul Moy	(Resigned 20 July 2016)

None of the directors who held office during the financial year had any disclosable interests in the shares of the company or the Group.

Research and development

The improvement of existing services and processes, together with the identification and development of new technology and solutions, are important aspects of the Group's strategy to enhance the quality of service to customers and improve methods of working. Research and development expenditure for the year amounted to £1.0 million (2016: £0.7 million).

Employees

Employee involvement: The Group recognises the importance of its employees and is committed to effective two-way communication and consultation.

The Group has established Business Involvement Groups to facilitate meaningful consultation between management and employees through elected employee representatives. The groups meet regularly at both a functional and company-wide level. An employee survey is also completed on an annual basis to seek input from employees.

The Group recognises the rights of every employee to join a trade union and participate in its activities. Southern Water has a single union agreement with Unison.

The Group publishes its own in-house newspaper, Southern Water News, on a regular basis. General information is posted on the Group intranet and regular team briefing sessions are also held. The information in these publications and briefings covers a wide range of subjects that affect the business, including progress on business and capital projects, the impact of regulatory issues and wider financial and economic issues that may affect the Group.

Equal opportunity: The Group’s policy is to promote equality of opportunity in recruitment, employment continuity, training and career development. The Group takes full account of the needs of people with disabilities and follows set policies and procedures to support reasonable adjustments in the workplace.

Health and safety: The Group recognises its duties to make proper provision for the health, safety and welfare at work of its employees.

Every employee receives a copy of the corporate policy statement on health and safety. There are regular meetings of employee representatives and managers to consider all aspects of health and safety. In addition there is a health and safety management review group which ensures that there is an adequate system for meeting the company’s responsibilities for health and safety to its staff, customers and members of the public.

The Group provides an internal occupational health service for employees, including the provision of physiotherapy. These services have been developed and are continuously reviewed to ensure they meet the needs of the business and our employees at work.

Disabled employees: Applications for employment by disabled persons are always fully considered, bearing in mind the abilities of the applicant concerned. In the event of members of staff becoming disabled every effort is made to ensure that their employment with the Group continues and that appropriate training is arranged. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

Speak Up: Employees are actively encouraged to Speak Up if they see things that are not quite right. This helps us work better as a company and fosters a culture where we ensure that we are always doing the right thing for each other, our customers, the environment and other stakeholders.

Environmental issues

The Group is committed to meeting or improving upon legislative and regulatory environmental requirements and codes of practice, and aims to contain the environmental impact of its activities to a practicable minimum.

The Group recognises its responsibility to operate within a framework that supports sustainable development and has established, where possible, indicator targets which are measurable. Performance against these targets is monitored and reported regularly.

Political donations

No political donations were made in either year.

Land and buildings

In the opinion of the directors, the market value of land is significantly more than its book value. However, it would not be practicable to quantify the difference precisely.

Financial risk management objectives and policies

The Group intends to at least maintain its present risk profile, as measured by its Southern Water investment grade credit rating. The Group does not enter into treasury transactions for the purpose of speculation, but only to manage risk inherent in the business or funding on a prudent basis.

Interest Rate Risk - The Group hedges Southern Water's exposure to interest rate risk on at least 85% of its total outstanding debt liabilities in respect of Class A Debt and Class B Debt for the current year to the next Periodic Review and at least 70% in the next period to the subsequent Periodic Review (on a rolling basis) into either index-linked obligations or fixed rate obligations.

Inflation Risk - The regulatory framework, under which revenues and the RCV are indexed, exposes the Group to inflation risk. The Group manages this risk through the use of index-linked instruments within its overall debt portfolio.

Liquidity risk – The Group raises additional funds, as required, to ensure that it has sufficient cash and/or facilities to fund the business for at least the next twelve months.

Cash management risk – The Group sets exposure limits for, and deposits cash balances with, organisations whose credit ratings are rated a minimum of Moody's P1, Standard & Poor's A1 or Fitch F1.

Going concern

The directors have undertaken a detailed review of the company's liquidity requirements compared with the cash and facilities available, the financial covenant position including projections based on future forecasts, the current ratings and financial risk and have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future, being a period of at least 12 months from the approval of these financial statements.

In forming this assessment the directors have considered the following information:

- The Group's business activities, together with the factors likely to affect its future development, performance and position, which are set out in the Strategic Report on pages 2 to 10 and 13 to 27.
- The financial position of the Group, its cash flows, liquidity position and borrowing facilities, which are described in the Financial Performance reviews on pages 2 to 6.
- The Group has available a combination of cash and committed undrawn bank facilities totalling £880 million at 31 March 2017 (2016: £418.0 million). These funds are sufficient to fund the operating and capital investment activities of the Group for the 12 months from the date of signing the financial statements.
- The Group operates in an industry that is currently subject to economic regulation rather than market competition. Ofwat, the economic regulator, has a statutory obligation to set price limits that it believes will enable the water companies to finance their activities. These limits have been set for the period April 2015 to March 2020.

As a consequence the directors believe that the Group is well placed to manage its business risks successfully.

The directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Qualifying third party indemnity

Following shareholder approval, the Group has provided an indemnity for its directors and the Company Secretary, which is a qualifying third party indemnity provision for the purposes of the Companies Act 2006.

Directors' responsibilities statement

The directors are responsible for preparing the Strategic Report, the Directors' 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 financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. 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 Group and of the profit or loss of the Group for that period. 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 IFRS as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the financial statements comply with the Companies (Jersey) Law 1991. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

The directors consider that the Annual Report and financial statements, 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.

Each of the directors confirm that, to the best of their knowledge:

- The Group financial statements, which have been prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- The Directors' Report and Strategic Report contained in the Annual Report include a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

Responsibility statement

We confirm that to the best of our knowledge:

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

Statement of disclosure of information to auditor

Each of the persons who is a director at the date of approval of this report confirms that:

(1) so far as the director is aware, there is no relevant audit information of which the Group's auditor is unaware; and

(2) he/she has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the Group's auditor is aware of that information.

Auditor

Deloitte LLP has indicated its willingness to continue in office.

Approved by the Board of Directors and signed on its behalf by:

J Statton
Company Secretary
18 July 2017

Financial statements

Consolidated income statement

For the year ended 31 March 2017

	Note	**2017 £m**	2016 £m
Continuing operations			
Revenue	4	**809.7**	803.7
Other operating income	4	**1.3**	1.7
Operating costs			
- before depreciation and amortisation		**(308.3)**	(287.7)
- depreciation and amortisation		**(252.6)**	(242.0)
Total operating costs		**(560.9)**	(529.7)
Operating profit	5	**250.1**	275.7
Profit on disposal of fixed assets		**0.4**	0.4
Finance income	9	**1.3**	2.5
Finance costs	9	**(294.1)**	(272.9)
Fair value losses on derivative financial instruments	22	**(416.8)**	(66.9)
Net finance costs	9	**(709.6)**	(337.3)
Loss before taxation		**(459.1)**	(61.2)
Taxation	10	**109.3**	40.3
Loss for the financial year		**(349.8)**	(20.9)

The notes on pages 38 to 79 form part of these financial statements.

Consolidated statement of other comprehensive income

For the year ended 31 March 2017

	Note	**2017 £m**	2016 £m
Loss for the financial year		**(349.8)**	(20.9)
Other comprehensive loss:			
Items that cannot be reclassified to profit or loss:			
Actuarial loss on pension scheme	24	**(71.4)**	(14.0)
Movement on deferred tax relating to retirement benefit obligations	23	**12.8**	2.8
Deferred tax movement due to rate change	23	**(1.7)**	-
Total other comprehensive loss for the year, net of tax		**(60.3)**	(11.2)
Total comprehensive loss for the year attributable to the owners of the company		**(410.1)**	(32.1)

Consolidated statement of financial position
as at 31 March 2017

	Note	Group 2017 £m	Group 2016 £m
Non-current assets			
Goodwill	12	**85.1**	85.1
Intangible assets	13	**61.1**	42.0
Property, plant and equipment	14	**5,876.4**	5,806.7
Investments	16	**0.1**	0.1
Derivative financial instruments	22	**9.4**	12.4
		6,032.1	5,946.3
Current assets			
Inventories	17	**2.7**	2.4
Trade and other receivables	18	**188.0**	191.8
Cash and cash equivalents	29	**302.3**	38.1
		493.0	232.3
Total assets		**6,525.1**	6,178.6
Current liabilities			
Trade and other payables	19	**(300.6)**	(188.1)
Borrowings	20	**0.6**	(49.0)
		(300.0)	(237.1)
Non-current liabilities			
Borrowings	21	**(5,133.6)**	(4,715.8)
Derivative financial instruments	22	**(1,347.4)**	(936.1)
Deferred tax liabilities	23	**(301.0)**	(421.5)
Retirement benefit obligations	24	**(176.9)**	(102.3)
Provisions for liabilities	25	**(0.5)**	(0.5)
Other non-current liabilities	26	**(62.2)**	(43.5)
		(7,021.6)	(6,219.7)
Total liabilities		**(7,321.6)**	(6,456.8)
Net liabilities		**(796.5)**	(278.2)
Equity			
Called up share capital	27	**921.9**	921.9
Share premium account	28	**4.5**	4.5
Retained earnings	28	**(1,722.9)**	(1,204.6)
Total deficit		**(796.5)**	(278.2)

The financial statements of Greensands Holdings Limited (Registered Number: Jersey 98700) on pages 32 to 79 were approved by the Greensands Holdings Limited Board and authorised for issue on 18 July 2017. They were signed on its behalf by

Michael Nagle
Director

Company statement of financial position
as at 31 March 2017

	Note	**Company 2017 £m**	Company 2016 £m
Non-current assets			
Investments	16	**1.0**	1.0
Other non-current assets	15	**1,016.6**	1,016.6
		1,017.6	1,017.6
Current assets			
Trade and other receivables	18	**54.2**	-
		54.2	-
Total assets		**1,071.8**	1,017.6
Current liabilities			
Trade and other payables	19	**(86.2)**	(32.0)
Non-current liabilities			
Borrowings	21	**(59.2)**	(59.2)
Total liabilities		**(145.4)**	(91.2)
Net assets		**926.4**	926.4
Equity			
Called up share capital	27	**921.9**	921.9
Share premium account	28	**4.5**	4.5
Retained earnings		**-**	-
Total equity		**926.4**	926.4

The company reported a profit for the financial year ended 31 March 2017 of £108.2 million (2016: £82.1 million).

The financial statements of Greensands Holdings Limited (Registered Number: Jersey 98700) on pages 32 to 79 were approved by the Greensands Holdings Limited Board and authorised for issue on 18 July 2017. They were signed on its behalf by

Michael Nagle
Director

Consolidated statement of changes in equity

For the year ended 31 March 2017

	Called up share capital (Note 27) £m	Share premium account (Note 28) £m	Retained Earnings (Note 28) £m	Total £m
Balance at 1 April 2015	**921.9**	**4.5**	**(1,090.4)**	**(164.0)**
Loss for the financial year	-	-	(20.9)	(20.9)
Other comprehensive loss for the year			(11.2)	(11.2)
Total comprehensive loss for the year	-	-	(32.1)	(32.1)
Equity dividends paid (note 11)	-	-	(82.1)	(82.1)
Balance at 31 March 2016	**921.9**	**4.5**	**(1,204.6)**	**(278.2)**
Loss for the financial year	-	-	(349.8)	(349.8)
Other comprehensive loss for the year			(60.3)	(60.3)
Total comprehensive loss for the year	-	-	(410.1)	(410.1)
Equity dividends paid (note 11)	-	-	(108.2)	(108.2)
Balance at 31 March 2017	**921.9**	**4.5**	**(1,722.9)**	**(796.5)**

Company statement of changes in equity

For the year ended 31 March 2017

	Called up share capital (Note 27) £m	Share premium account (Note 28) £m	Retained earnings £m	Total £m
Balance at 1 April 2015	**921.9**	**4.5**	**-**	**926.4**
Profit for the financial year	-	-	82.1	82.1
Other comprehensive income for the year	-	-	-	-
Total comprehensive income for the year	-	-	82.1	82.1
Equity dividends paid (note 11)	-	-	(82.1)	(82.1)
Balance at 31 March 2016	**921.9**	**4.5**	**-**	**926.4**
Profit for the financial year	-	-	108.2	108.2
Other comprehensive income for the year	-	-	-	-
Total comprehensive income for the year	-	-	108.2	108.2
Equity dividends paid (note 11)	-	-	(108.2)	(108.2)
Balance at 31 March 2017	**921.9**	**4.5**	**-**	**926.4**

Consolidated statement of cash flows

For the year ended 31 March 2017

	Note	**2017 £m**	2016 £m
Cash from operating activities		**524.1**	481.6
Tax paid		**(0.1)**	-
Net cash from operating activities	29	**524.0**	481.6
Investing activities			
Interest received		**1.1**	2.9
Purchase of property, plant and equipment		**(246.7)**	(237.9)
Purchase of intangible assets		**(31.1)**	(6.8)
Receipt of grants and contributions		**3.1**	5.2
Sale of property, plant and equipment		**-**	0.6
Net cash used in investing activities		**(273.6)**	(236.0)
Financing activities			
Equity dividends paid		**(54.0)**	(82.1)
Interest paid		**(167.7)**	(163.2)
Payment of derivative accretion		**(2.5)**	(298.4)
Repayment of short-term borrowings		**(80.0)**	(200.0)
Repayments of obligations under finance leases		**(0.3)**	(0.2)
Issue costs of new loans		**-**	(0.2)
Proceeds of new loans		**318.3**	310.0
Swap break costs		**-**	(3.5)
Net cash from/(used in) financing activities		**13.8**	(437.6)
Net increase/(decrease) in cash and cash equivalents		**264.2**	(192.0)
Cash and cash equivalents at beginning of the year		**38.1**	230.1
Cash and cash equivalents at end of the year		**302.3**	38.1

Notes to the consolidated financial statements
For the year ended 31 March 2017

1 Accounting policies

The principal accounting policies, which have been applied consistently throughout the current and preceding year, are set out below.

Basis of preparation

Greensands Holdings Limited is a company incorporated in Jersey (JE98700) under the Companies Act. The address of the registered office is given on page 1. The principal activities of the company and its subsidiaries (the Group) and the nature of the Group's operations are set out in the Strategic Report on pages 2 to 10.

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs). The financial statements have also been prepared in accordance with IFRSs adopted by the European Union and therefore the Group financial statements comply with Article 4 of the EU IAS Regulation

The financial statements have been prepared on a going concern basis under the historical cost convention, except for the revaluation of financial instruments, which occurs at the end of each reporting period as explained in the accounting policies below.

Historical cost is generally based on the fair value of the consideration given in exchange for the goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement purposes in these consolidated financial statements is determined on such a basis, except for leasing transactions that are within the scope of IAS 17 'Leases', and measurements that have some similarities to fair value but are not fair value, such as net realisable value in IAS 2 'Inventories' or value in use in IAS 36 'Impairment of Assets'.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

Basis of consolidation

The Group financial statements include the financial statements of the company and all entities controlled by the company (its subsidiaries) made up to 31 March each year.

Control is achieved when the company: has the power over the investee, is exposed, or has rights, to variable return from its involvement with the investee; and has the ability to use its power to affects its returns. The company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of these three elements of control.

The company considers that it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally.

Consolidation of a subsidiary begins when the company obtains control over the subsidiary and ceases when the company loses control of the subsidiary. Specifically, the results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the date the company gains control until the date when the company ceases to control the subsidiary.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with the Group's accounting policies. All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between the members of the Group are eliminated on consolidation.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

1 Accounting policies (continued)

Adoption of new and revised accounting and financial reporting standards

The amendments to the following revised accounting standard have been adopted in the current year.

Amendments to IAS 1 Disclosure Initiative	The Group has adopted the amendments to IAS 1 *Disclosure Initiative* for the first time in the current year. The amendments clarify that an entity need not provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material, and give guidance on the bases of aggregating and disaggregating information for disclosure purposes. However, the amendments reiterate that an entity should consider providing additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users of financial statements to understand the impact of particular transactions, events and conditions on the entity's financial position and financial performance. The amendments also address the structure of the financial statements by providing examples of systematic ordering or grouping of the notes. The adoption of these amendments has not resulted in any impact on the financial performance or financial position of the Group.

The Group has not applied the following new and revised accounting standards that have been issued but are not yet effective and, in some cases, had not yet been adopted by the EU.

IFRS 9	Financial Instruments
IFRS 15	Revenue from Contracts with Customers
IFRS 16	Leases
IFRS 2 (amendments)	Classification and Measurement of Share-based Payment Transactions
IAS 7 (amendments)	Disclosure Initiative
IAS 12 (amendments)	Recognition of Deferred Tax Assets for Unrealised Losses
IFRS 10 and IAS 28 (amendments)	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The directors do not expect that the adoption of the standards listed above will have a material impact on the financial statements of the Group in future periods, except as noted below:

- IFRS 9 will impact both the measurement and disclosures of financial instruments;
- IFRS 15 may have an impact on revenue recognition and related disclosures; and
- IFRS 16 will require extensive disclosure and the effect on the financial statements has not yet been quantified as this is subject to further review.

Beyond the information above, it is not practicable to provide a reasonable estimate of the effect of these standards until a detailed review has been completed.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

1 Accounting policies (continued)

Going concern

The Group's and company's business activities, together with the factors likely to affect the future development and position, are set out in the Strategic Report on pages 2 to 27.

The directors have undertaken a detailed review of the Group's and company's liquidity requirements compared with the cash and facilities available, the financial covenant position including projections based on future forecasts, the current ratings and financial risk and have a reasonable expectation that the Group and company have adequate resources to continue in operational existence for the foreseeable future, being a period of at least 12 months from the approval of these financial statements. For this reason they continue to adopt the going concern basis of accounting in preparing the annual financial statements; further details can be found in the Directors' Report on page 28.

Business combinations

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquiree and the equity interest issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in profit or loss as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognised at their fair value at the acquisition date, except that:

- deferred tax assets or liabilities and assets or liabilities related to employee benefit arrangements are recognised and measured in accordance with IAS 12 'Income Taxes' and IAS 19 'Employee Benefits' respectively; and
- assets (or disposal groups) that are classified as held for sale in accordance with IFRS-5 'Non-current Assets Held for Sale and Discontinued Operations' are measured in accordance with that Standard.

Goodwill arising in a business combination is recognised as an asset at the date that control is acquired (the acquisition date). Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the acquirer's previously held equity interest (if any) in the entity over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after reassessment, the Group's interest in the fair value of the acquiree's identifiable net assets exceeds the sum of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the acquirer's previously held equity interest in the acquiree (if any), the excess is recognised immediately in profit or loss as a bargain purchase gain.

Goodwill is not amortised but is reviewed for impairment at least annually.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period. On disposal of a cash-generating unit, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

1 Accounting policies (continued)

Segmental reporting

The Group's revenue arises from the provision of services within the United Kingdom. It has a large and diverse customer base and is not reliant on any single customer.

The Southern Water board and management team review all internal management information on a single segment basis and accordingly no segmental information is provided in this report.

Revenue recognition

Revenue represents the income receivable (net of value added tax) in the ordinary course of business for goods and services provided. In respect of unbilled charges, revenue includes an estimate of the consumption between the date of the last meter reading and the period-end. The revenue accrual is estimated using a defined methodology based upon historical billing, consumption information and the applicable tariff.

Revenue from the supply of services represents the value of services provided under contracts to the extent that there is a right to consideration and is recorded at the fair value of the consideration due. Revenue is recognised when the amount of revenue can be measured reliably and it is probable that the economic benefits associated with the transaction will flow to the Group. Revenue is not recognised when it is considered probable that economic benefits will not be received. In these circumstances revenue is only recognised when collectability is reasonably certain. Payments received in advance of revenue recognition are recorded as deferred income.

Unmetered income is based on either the rateable value of the property or on an assessed volume of water supplied. Metered income is based on actual or estimated water consumption.

Interest income is recognised on a time proportionate basis using the effective interest method.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established (provided that it is probable that the economic benefits will flow to the company and the amount of revenue can be measured reliably).

Provision for impairment of trade receivables

The bad debt provision is calculated by applying estimated recovery rates to various categories of debt, reflecting past collections experience and expectations of future recovery of outstanding receivables at the date of the statement of financial position.

Taxation

The taxation charge in the income statement represents the sum of the tax currently payable and deferred tax.

Current taxation is based on the result for the year as adjusted for disallowable and non-taxable items and items of income or expense which are taxable or deductible in other years. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the statement of financial position date.

Deferred taxation is tax expected to be payable on temporary differences between the treatment of certain items for taxation and accounting purposes. Deferred taxation is provided on all temporary differences that have originated but not reversed by the end of the reporting period. It is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised based on tax laws and rates that have been enacted or substantively enacted at the reporting date.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is regarded as probable that taxable profits will be available against which deductible temporary differences can be utilised.

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

Goodwill

Goodwill is initially recognised and measured as set out on page 54 with the carrying value being reviewed for any indicators of impairment on an annual basis.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

1 Accounting policies (continued)

Intangible assets

Intangible assets are measured at cost less subsequent amortisation and any impairment. Amortisation of intangible assets is calculated on a straight-line basis over the estimated useful lives, which are primarily three to ten years. The estimated useful life and amortisation method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

Property, plant and equipment

Property, plant and equipment comprises:

- i. Freehold land and buildings – comprising land and non-operational buildings
- ii. Infrastructure assets – comprising a network of systems consisting of mains and sewers, impounding and pumped raw water storage reservoirs, sludge pipelines and sea outfalls
- iii. Plant and machinery – comprising structures at sites used for water and wastewater treatment; pumping or storage where not classed as infrastructure along with associated fixed plant
- iv. Other assets – comprising vehicles, computers, mobile plant and meters
- v. Assets under construction.

All property, plant and equipment is stated in the statement of financial position at cost or at deemed cost on transition to IFRS, less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

The difference between depreciation based on the fair valued carrying amounts of assets and depreciation based on the asset's original cost is transferred annually from the revaluation reserve to retained earnings through equity. The costs of repairs to the infrastructure network are recognised in the income statement as they arise.

Expenditure which results in replacement or renewal of infrastructure or enhancements to the operating capability of the infrastructure network is capitalised.

Items of property, plant and equipment that are transferred to the Group from customers or developers are initially recognised at fair value in accordance with IFRIC 18 'Transfers of Assets from Customers'. The corresponding credit is recorded as deferred income and released to other income over the expected useful lives of the related assets.

Borrowing costs directly attributable to the construction of qualifying assets, that necessarily take a substantial period of time to get ready for their intended use, are capitalised during the period of time that is required to complete and prepare the asset for its intended use. The commencement of capitalisation begins when both finance costs and expenditures for the asset are being incurred and activities that are necessary to get the asset ready for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to get the asset ready for use are complete. Other borrowing costs are expensed.

Subsequent costs are included in the asset's carrying amount or recognised as separate assets, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the income statement as incurred.

Freehold land is not depreciated, nor are assets in the course of construction until they are commissioned. Commissioning is deemed to occur when a new works is officially taken over from the contractor following completion of performance and take-over tests.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

1 Accounting policies (continued)

Property, plant and equipment (continued)

Other assets are depreciated on a straight-line basis over their estimated operating lives which are principally as follows:

Non-infrastructure assets	Years	*Infrastructure assets*	Years
Buildings	10–60	Water mains	100–120
Operational structures	15–80	Sewers	80–200
Fixed plant	10–40	Reservoirs	200
Vehicles, computers and mobile plant	3–10	Ancillary structures	10–70

Operational structures are assets used for wastewater and water treatment purposes. These include water tanks and similar assets.

The estimated useful lives and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

Impairment of tangible and intangible assets

At the end of each reporting period, the Group reviews the carrying amounts of its tangible and intangible assets, to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised immediately in the income statement, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised immediately in the consolidated income statement, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Grants and contributions

Grant and contributions received are treated as either revenue or deferred income in line with IFRIC 18 as defined by the nature of the receipt.

Infrastructure receipts, contributions received following new connections towards enhancing the network, are recognised as revenue when they are receivable.

Grants and contributions receivable in respect of non-current assets are treated as deferred income and released to other income over the useful economic life of those fixed assets.

Grants and contributions received in respect of new connections to the water and sewerage networks are treated as deferred income and released to revenue in line with the expected expenditure they are intended to compensate.

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

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

1 Accounting policies (continued)

Leased assets

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

(i) The Group as lessee

Where the Group enters into a lease which entails taking substantially all the risks and rewards of ownership of an asset, the lease is treated as a 'finance lease'. Assets held under finance leases are recognised as assets of the company at their fair value or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. The asset is recorded in the statement of financial position as a non-current asset and is depreciated over its estimated useful life or the term of the lease, whichever is shorter. Future liabilities to the lessor under such leases, net of finance charges, are included within creditors. Rentals payable are apportioned between the finance element, which is charged to the income statement, and the capital element, which reduces the outstanding obligation for future instalments.

Leases where the lessor retains substantially all the risks and rewards of ownership are classified as operating leases. Rentals payable under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

Sale and leaseback transactions occur when an asset is sold but use is immediately re-acquired by entering into a lease with the buyer. Where the new lease is an operating lease, the transaction is treated as the disposal of an asset and the operating lease accounted for in accordance with existing policies.

(ii) The Group as lessor

The sale of income rights relating to aerial masts and sites owned by the Group to third parties is treated as an operating lease. Income received from such sales is received entirely in advance and is therefore taken to deferred revenue and credited to other operating income in the income statement over the life of the lease.

Non-current asset investments

Investments held as non-current assets, including investments in subsidiaries, are stated at cost, less, where appropriate, provision for any impairment in value. The carrying values of non-current asset investments are reviewed for impairment in periods if events or changes in circumstances indicate the carrying value may not be recoverable.

Inventories

Inventory is held for use in the production of water supply and treatment of wastewater. Raw materials and work in progress are valued at the lower of cost and net realisable value. Net realisable value is the estimated selling price, less further costs expected to be incurred to completion and costs to be incurred in marketing, selling and distribution.

Deferred revenue

Deferred revenue includes monies received from customers where the related service has not yet been provided.

Amounts are deferred to the statement of financial position and released to the consolidated income statement in line with the period of the service provided.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

1 Accounting policies (continued)

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle that obligation and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

An environmental provision is made for the costs relating to decommissioned or dormant assets which have been identified as having an environmental impact.

Retirement benefits

The Group operates a defined benefit pension scheme, the assets of which are held separately from those of the Group in independently administered funds. An independent actuary conducts a valuation of this pension scheme every three years.

The liability recognised in the statement of financial position in respect of the defined benefit pension scheme is the present value of the defined benefit obligation at the end of the period less the fair value of plan assets. The current service cost, which is the increase in the present value of the liabilities of the Group's defined benefit pension scheme expected to arise from employee service in the period, is charged to operating costs. The net interest on the scheme's net assets/(liabilities) is included in other finance charges. Actuarial gains and losses are recognised in the consolidated statement of other comprehensive income.

The pension cost under IAS 19 'Employee Benefits' is assessed in accordance with the advice of a firm of actuaries based on the latest actuarial valuation and assumptions determined by the actuary. The assumptions are based on information supplied to the actuary by the Group, supplemented by discussions between the actuary and management. The assumptions are disclosed in note 24.

Loss before taxation and net liabilities are affected by the actuarial assumptions used. The key assumptions include: discount rates, pay growth, mortality and increases to pensions in payment and deferred pensions, and may differ from actual results due to changing market and economic conditions and longer or shorter lives of participants.

The Group also operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the Group in an independently administered fund. Group contributions to the scheme are charged to the income statement in the period to which they relate. Differences between contributions actually paid are shown as either accruals or prepayments in the statement of financial position.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

1 Accounting policies (continued)

Financial instruments

Financial assets and financial liabilities are recognised in the Group's statement of financial position when the Group becomes a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss (FVTPL)) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at FVTPL are recognised immediately in the consolidated income statement.

Financial assets

(i) Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as 'loans and receivables'. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

(ii) Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each statement of financial position date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

For financial assets carried at amortised cost, the amount of the impairment is the differences between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate. The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account.

(iii) Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. On derecognition of a financial asset the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

Financial liabilities

Fixed rate interest-bearing borrowings are initially measured at fair value, net of transaction costs, and are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Issue costs in relation to index-linked and variable rate bonds are separately disclosed within creditors.

The carrying value of index-linked debt instruments is adjusted for the annual movement in the retail price index. The change in value arising from indexation is charged or credited to the income statement in the year in which it arises.

Premiums and proceeds from gilt lock agreements received on issue of debt instruments are credited to the income statement over the term of the debt at a constant rate on the carrying amount.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

1 Accounting policies (continued)

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

Derivative financial instruments

The Group enters into a variety of derivative financial instruments to manage its exposure to inflation risk in line with the Group's risk management policy and no speculative trading in financial instruments is undertaken. Further details of derivative financial instruments are disclosed in note 22.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently re-measured to their fair value at the end of each reporting period. The resulting gain or loss is recognised in the income statement immediately.

Certain derivative instruments, principally index-linked swaps, do not qualify for hedge accounting, and as such, the Group does not currently apply hedge accounting.

Derivatives with a positive fair value and derivatives with a negative fair value are set-off against each other with the net position being presented as either a financial liability or financial asset. A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be realised or settled within 12 months. Other derivatives are presented as current assets or current liabilities.

Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value through profit and loss.

An embedded derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the hybrid instrument to which the embedded derivative relates is more than 12 months and is not expected to be realised or settled within 12 months. Other derivatives are presented as current assets or current liabilities.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

2 Critical accounting judgements and key sources of estimation uncertainty

In the application of the Group's accounting policies, which are described in note 1 above, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements

Critical judgements, apart from those involving estimations, that are applied in the preparation of the financial statements are discussed below:

(i) Revenue recognition

The Group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured. When the Group considers that the criteria for revenue recognition are not met for a transaction, revenue recognition is delayed until such time as collectability is reasonably assured. Payments received in advance of revenue recognition are recorded as deferred income.

(ii) Property, plant and equipment

The Group recognises property, plant and equipment (PPE) on its water and wastewater infrastructure assets where such expenditure enhances a significant length of the network or increases the capacity of the network, whereas any expenditure classed as maintenance is expensed in the period it is incurred. Determining enhancement from maintenance expenditure is a subjective area, particularly when assessing whether the length of network replaced enhances the network. In addition, management capitalise time and resources incurred by the Group's support functions on capital programmes based on judgments made in respect of the proportion of capital work performed by these functions.

The assessment of useful economic lives is also a key judgment in determining the carrying value of property, plant and equipment.

(iii) Provisions and contingent liabilities

The Group exercises judgement in recognising provisions and the exposures to contingent liabilities related to pending litigation or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation, as well as other contingent liabilities. Judgement is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and the point of recognition for the associated liability.

Sources of estimation uncertainty

The key assumptions about the future, and other key sources of estimation uncertainty at the reporting period end that may have a risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed below:

(i) Measured income accrual

The measured income accrual is an estimation of the amount of water and wastewater unbilled at the period end. The accrual is estimated using a defined methodology based upon historical billing and consumption information and the applicable tariff. The calculation is sensitive to estimated consumption for measured customers.

(ii) Allowance for doubtful receivables

At each reporting date, the Group evaluates the recoverability of trade receivables and records an allowance for doubtful receivables based on experience. This allowance is based on, amongst other things, a consideration of actual collection history. The actual level of receivables collected may differ from the estimated levels of recovery, which could impact future operating results positively or negatively.

(iii) Retirement benefit obligations

The Group operates a defined benefit scheme as well as a defined contribution scheme. Under IAS 19 'Employee Benefits' the Group has recognised an actuarial loss of £71.4 million for the year to 31 March 2017 (2016: loss of £14.0 million).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

2 Critical accounting judgements and key sources of estimation uncertainty (continued)

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 2015 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 of the financial statements.

(iv) Provisions and contingent liabilities

The Group evaluates its exposures to contingent liabilities relating to pending litigation or other outstanding claims and recognises provisions using estimates to quantify the possible range of the financial settlement. Because of the inherent uncertainty in this evaluation process, actual losses may be different from the originally estimated provision.

(v) Goodwill

An impairment review on goodwill is conducted at least annually. The net asset value of the subsidiaries is used in the impairment review. Therefore any estimations or judgements used in respect to the value of the assets or liabilities of the subsidiaries may affect the outcome of the impairment review.

3 Segmental analysis

The directors believe that the whole of Group's activities constitute a single class of business. The Group's revenue is generated wholly from within the United Kingdom. The Greensands Holdings Board and management team review all internal management information on a single segment basis and accordingly no segmental information is provided in this report.

4 Revenue

An analysis of the Group's revenue is as follows:

Continuing operations	**2017 £m**	2016 £m
Water and sewerage services	**764.8**	759.0
Other services	**44.9**	44.7
Total turnover	**809.7**	803.7
Other operating income	**1.3**	1.7
Finance income (note 9)	**1.3**	2.5
Total revenue	**812.3**	807.9

Other operating income includes rents receivable.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

5 Group operating profit for the year

Group loss for the year has been arrived at after charging/(crediting):	**2017 £m**	2016 £m
Depreciation on		
- owned assets	**237.0**	232.0
- assets held under finance leases	**0.7**	1.3
	237.7	233.3
Amortisation of intangible assets included in other operating expenses:		
- other	**14.9**	8.7
Profit on disposal of property, plant and equipment	**0.4**	0.4
Research and development expenditure	**1.0**	0.7
Rentals under operating leases		
- Properties	**1.7**	1.7
- Vehicles	**2.2**	2.2
Employee costs (note 7a)	**46.0**	56.3
Amortisation of grants and contributions (see note 26)	**(1.2)**	(1.1)
Rates rebate (see note (i) below)	**-**	(13.3)
Fees payable to the company's auditor in respect of:		
- statutory audit of the company's financial statements	**0.3**	0.2
- other services pursuant to legislation	**0.1**	0.1
- all other services	**0.2**	0.7
Total audit and non-audit fess	**0.6**	1.0

Audit related and non-audit services primarily relate to regulatory assurance fees, and other taxation and professional fees.

Notes:

(i) The rates rebate of £13.3 million received in the year ending 31 March 2016 relates to a refund of historic rates charges following a successful appeal.

6 Profit of the parent company

The profit for the financial year dealt with in the financial statements of the parent company is £108.2 million (2016: £82.1 million). Consequently, this sum was paid to the shareholders of the company as ordinary dividends (see note 11).

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

7 Employee information

		2017 £m	2016 £m
(a) Group employee costs			
Wages and salaries		**81.9**	77.4
Social security costs		**8.3**	7.1
Pension costs	- Defined contribution	**2.6**	2.3
	- Defined benefit	**5.1**	6.3
Total employee costs		**97.9**	93.1
Less: charged as capital expenditure		**(41.4)**	(36.8)
Charged to the income statement		**56.5**	56.3

Employee costs that are charged as capital expenditure are those directly related to the construction or acquisition of assets.

(b) Average number of persons employed by activity
The average monthly numbers of persons (including executive directors) employed by the Group during the year was:

	2017 Number	2016 Number
Operations	**1,298**	1,239
Customer services	**317**	378
Corporate centre	**505**	502
	2,120	2,119

8 Directors' emoluments

During the year there were no payments made to directors by the Group in return for services as a director of Greensands Holdings Limited. In 2016 one director received £10,459. However, one other director received £15,000 (2016: £15,000) paid by one of the ultimate shareholders.

9 Net finance costs

	2017 £m	2016 £m
Finance income		
Interest receivable	**1.3**	2.5
	1.3	2.5
Finance costs		
Interest payable on loans	**(320.2)**	(300.2)
Interest rate swap receipts	**43.3**	43.7
Indexation	**(20.9)**	(10.0)
Amortisation of issue costs	**(2.0)**	(5.5)
Amortisation of gilt lock proceeds	**0.1**	0.1
Amortisation of bond premium	**0.7**	0.6
Swap break costs	**-**	(3.4)
Other finance expense (note 24)	**(3.7)**	(3.9)
	(302.7)	(278.6)
Amounts capitalised on qualifying assets	**8.6**	5.7
	(294.1)	(272.9)
Fair value losses on derivative financial instruments		
Derivative financial instruments not designated as hedges	**(416.8)**	(66.9)
Net finance costs	**(709.6)**	(337.3)

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

9 Net finance costs (continued)

A large proportion of the payment of interest payable on loans falls due on 31 March. Where this date is not a business day, the interest is paid on the next following business day.

Borrowing costs included in the cost of qualifying assets during the year arose on the general borrowing pool and are calculated by applying a capitalisation rate of 4.23% to expenditure on such assets (2016: 4.00%).

10 Taxation

	2017 £m	2016 £m
Current tax:		
Current year	**0.1**	0.1
Adjustments in respect of prior years	**-**	-
Total current tax charge	**0.1**	0.1
Deferred tax:		
Origination and reversal of temporary differences	**(89.5)**	6.9
Adjustment in respect of prior years	**-**	(0.4)
Effect of corporation tax rate change	**(19.9)**	(46.9)
Total deferred tax	**(109.4)**	(40.4)
Total tax credit on loss	**(109.3)**	(40.3)

The tax assessed for the year is different to the standard rate of corporation tax in the UK due to the following factors:

	2017 £m	2016 £m
Loss before tax	**(459.1)**	(61.2)
Current tax:		
Tax at the UK corporation tax rate of 20% (2016: 20%)	**(91.8)**	(12.2)
Permanent differences	**8.9**	7.9
Deferred tax assets not recognised	**(14.8)**	11.3
Differences between current and deferred tax rates	**8.3**	-
Impact of tax rate changes	**(19.9)**	(46.9)
Adjustment in respect of prior years – deferred tax	**-**	(0.4)
Tax credit for year	**(109.3)**	(40.3)

Factors that may affect future tax charges:

Reductions in the main rate of corporation tax to 19% from 1 April 2017 and to 18% from 1 April 2020 were enacted in the Finance Bill 2015, and deferred tax balances at 31 March 2016 are calculated based on these reduced rates. It was subsequently announced in the 2016 UK Budget that the corporation tax rate would instead reduce to 17% from 1 April 2020. This further reduction has been substantively enacted in Finance Bill 2016 at the reporting date, and deferred tax balances at 31 March 2017 have been calculated using this reduced rate. A £19.9 million credit has been recognised in the consolidated income statement in the year to reflect the reduction in the deferred tax liability as a result of the rate change. In addition, charges of £1.7 million have been recognised in the consolidated statement of other comprehensive income to reflect the reduction in the deferred tax asset relating to the pension deficit.

Based on current capital investment plans, the company expects to continue to be able to claim capital allowances in excess of depreciation in future years at a similar level to the current year.

Note 23 Deferred Tax Liability shows that the balance is made up of a deferred tax liability arising on accelerated capital allowances, and deferred tax assets arising on the fair value revaluation of financial instruments, the pension deficit and other short-term timing differences.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

10 Taxation (continued)

At the reporting date the Group has unused tax losses of £45.2 million (2016: £5.6 million) available for offset against future profits. A deferred tax asset has been recognised in respect of £39.7 million (2016: £nil) of such losses. No deferred tax asset has been recognised in respect of the remaining Group losses of £5.6 million (2016: £5.6 million), with a deferred tax asset of £0.9 million (2016: £1.0 million), due to the uncertainty of suitable taxable profits in the foreseeable future on which to utilise these losses.

Future tax relief of £131.7 million (2016: £215.4 million) is expected to be available for accrued interest that will be deductible for tax purposes on a paid basis. No deferred tax benefit has been recognised in respect of these interest deductions, as it is probable that they will not reverse in the foreseeable future and there is uncertainty over the availability of suitable taxable profits against which these may be offset.

The total amount of deferred tax asset un-provided is £23.3 million (2016: £39.7 million). At present it is not envisaged that the unwinding of the underlying temporary differences will give rise to a tax benefit in the foreseeable future.

Deferred tax liabilities have not been discounted.

In addition to the amount charged to the consolidated income statement, the following amounts relating to tax have been recognised in the consolidated statement of other comprehensive income:

	2017 £m	2016 £m
Deferred tax		
Arising on income and expenses recognised in other comprehensive income:		
Tax credit on actuarial losses on defined benefit pension scheme	**(12.8)**	(2.8)
Deferred tax movement due to rate change	**1.7**	-
Total income tax recognised in other comprehensive income	**(11.1)**	(2.8)

11 Dividends

	2017 £m	2016 £m
Amounts recognised as distributions to equity holders in the year:		
Current year interim dividend of £0.059 (2016: £0.032) per share	**54.0**	29.2
Current year final dividend of £0.059 (2016: £0.057) per share	**54.2**	52.9
	108.2	82.1

The current year interim dividend of £54.0 million was paid in October 2016 and the final dividend of £54.2 million was paid in April 2017.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

12 Goodwill

Group	£m
Carrying amount at 1 April 2016	85.1
Impairment at 31 March 2017	-
Net book value at 31 March 2017	**85.1**

Goodwill is reviewed annually for impairment by comparing the underlying statement of financial position value of the Group, having adjusted for net debt, with the Regulatory Capital Value (RCV) of Southern Water Services. The excess of value over the RCV is then compared to recent transactions in the water industry to assess whether the book value of the Group is supportable.

Other indicators considered are, the financial performance, operating performance and future changes to the operating environment of our only operating company Southern Water Services.

To date no indicators of impairment have been identified.

13 Intangible assets

	Externally generated		
	Assets under construction £m	**Computer software £m**	**Total £m**
Cost			
At 1 April 2016	11.7	64.5	**76.2**
Additions	16.9	17.1	**34.0**
Transfers	(8.5)	8.5	**-**
At 31 March 2017	20.1	90.1	**110.2**
Amortisation			
At 1 April 2016	-	34.2	**34.2**
Charge for the year	-	14.9	**14.9**
At 31 March 2017	-	49.1	**49.1**
Net book amount			
At 31 March 2017	**20.1**	**41.0**	**61.1**
At 31 March 2016	11.7	30.3	42.0

The Group currently does not have any internally generated intangible assets.

Included within additions above is £1.3 million of interest that has been capitalised on qualifying assets in accordance with IAS 23 ‘Borrowing costs’. The cumulative net book value of the borrowing costs capitalised amount to £1.8 million (2016: £0.7. million). The company has elected to apply IAS 23 from 1 April 2003, as permitted by the standard.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

14 Property, plant and equipment

The Group tangible assets are shown below. The company has no tangible assets.

	Land & buildings £m	Plant & machinery £m	Infra-structure assets £m	Assets under construction £m	Other £m	Total £m
Cost						
At 1 April 2016	1,572.7	2,983.8	2,490.5	252.9	615.7	**7,915.6**
Additions	1.6	87.9	35.9	167.3	14.7	**307.4**
Transfers	(1.4)	36.2	71.8	(106.4)	(0.2)	**-**
Disposals	-	(5.5)	(0.3)	-	(1.4)	**(7.2)**
At 31 March 2017	1,572.9	3,102.4	2,597.9	313.8	628.8	**8,215.8**
Depreciation						
At 1 April 2016	643.4	1,054.0	59.1	-	352.4	**2,108.9**
Charge for the year	41.0	120.4	29.7	-	46.6	**237.7**
Disposals	-	(5.5)	(0.3)	-	(1.4)	**(7.2)**
At 31 March 2017	684.4	1,168.9	88.5	-	397.6	**2,339.4**
Net book amount						
At 31 March 2017	**888.5**	**1,933.5**	**2,509.4**	**313.8**	**231.2**	**5,876.4**
At 31 March 2016	929.3	1,929.8	2,431.4	252.9	263.3	5,806.7

Freehold land is stated at a cost of £51.7 million at 31 March 2017 and 31 March 2016 and is not depreciated.

The Group's interest in land and buildings are almost entirely freehold.

Included within additions above is £7.3 million (2016: £5.7 million) of interest that has been capitalised on qualifying assets in accordance with IAS 23 'Borrowing Costs'. The cumulative net book value of the borrowing costs capitalised amount to £167.4 million (2016: £167.0 million). The Group has elected to apply IAS 23 from 1 April 2003, as permitted by the standard.

Assets held under finance leases

Included in the amounts shown above are the following amounts in relation to property, plant and equipment held under finance leases:

	2017 £m	2016 £m
Net book amount at 31 March	**5.3**	5.9

In accordance with IFRS 1 'First-time Adoption of International Financial Reporting Standards', the Group has elected to measure its infrastructure and operational assets at 1 April 2014, being the date of transition to IFRS, at their fair value and to use that fair value as their deemed cost at that date.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

15 Other non-current assets

	Company 2017 £m	Company 2016 £m
Amounts owed by group undertakings	**1,016.6**	1,016.6

All amounts due from group undertakings are unsecured, interest free and repayable on demand.

16 Investments

	Group 2017 £m	Group 2016 £m
Other external investments		
At 1 April	**0.1**	0.1
Additions	**-**	-
Total investments as at 31 March	**0.1**	0.1

The investment above represents a non-controlling interest of 7.17% in a private limited company called, Landlord TAP Limited. The company owns a national web portal set up as part of a Water UK initiative to improve data on tenants and thereby increase collections with the aim of reducing customer bad debt.

	Company 2017 £m	Company 2016 £m
Greensands Europe Limited		
At 1 April and 31 March	**1.0**	1.0
Total subsidiary investments	**1.0**	1.0

A full list of subsidiaries is disclosed in note 33.

17 Inventories

	Group 2017 £m	Group 2016 £m
Raw materials	**2.0**	1.5
Work in progress	**0.7**	0.9
	2.7	2.4

The company does not hold any inventory.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

18 Trade and other receivables

	Group 2017 £m	Group 2016 £m
Trade receivables	**224.6**	198.5
Provision for impairment	**(123.3)**	(111.9)
Net trade receivables	**101.3**	86.6
Accrued income	**53.1**	80.1
Prepayments	**19.7**	14.6
Other receivables	**13.9**	10.5
	188.0	191.8

Accrued income as at 31 March 2017 includes water and sewerage income not yet billed of £50.2 million (2016: £73.1 million).

The directors consider that the carrying values of trade and other receivables are reasonable approximations of their fair values.

	Company 2017 £m	Company 2016 £m
Greensands Investments Limited		
Other receivables	**54.2**	-
	54.2	-

Provision for impairment

Movements on the doubtful debts provision were as follows:

	Group 2017 £m	Group 2016 £m
At 1 April	**(111.9)**	(110.5)
Charge for bad and doubtful debts	**(25.3)**	(21.5)
Amounts written off during the year	**13.9**	20.1
At 31 March	**(123.3)**	(111.9)

At each reporting date, the Group evaluates the recoverability of trade receivables and records allowances for doubtful receivables based on experience.

The following table provides information regarding the ageing of receivables that are specifically provided for:

	Group 2017 £m	Group 2016 £m
Current	**0.7**	0.7
1-2 years	**2.4**	0.9
2-3 years	**11.8**	9.9
3-4 years	**14.1**	7.0
more than 4 years	**39.8**	37.5
	68.8	56.0

A collective provision is recorded against assets which are past due but for which no specific provision has been made. This is calculated based on historical experience of levels of recovery.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

18 Trade and other receivables (continued)

The aged analysis of receivables that were overdue at the reporting date but not individually provided for is as follows:

	Group 2017 £m	Group 2016 £m
Current	**59.7**	56.5
1-2 years	**32.1**	30.3
2-3 years	**13.7**	19.5
3-4 years	**8.6**	12.5
more than 4 years	**6.4**	6.7
	120.5	125.5

The amounts above are reconciled to gross and net debtors in the tables below:

At 31 March 2017	**Gross £m**	**Provision £m**	**Group Net £m**
Not due	**35.3**	**-**	**35.3**
Overdue not specifically provided	**120.5**	**(54.5)**	**66.0**
Overdue and specifically provided	**68.8**	**(68.8)**	**-**
	224.6	**(123.3)**	**101.3**

At 31 March 2016	Gross £m	Provision £m	Group Net £m
Not due	17.0	-	17.0
Overdue not specifically provided	125.5	(55.9)	69.6
Overdue and specifically provided	56.0	(56.0)	-
	198.5	(111.9)	86.6

Trade receivables neither past due or impaired relate to domestic and retail customers whose history of payments supports no impairment being made.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

19 Trade and other payables

	Group 2017 £m	Group 2016 £m
Trade payables	**18.9**	13.7
Capital creditors and capital accruals	**96.8**	59.3
Corporation tax	**0.1**	0.1
Other taxation and social security	**3.0**	2.8
Other payables	**54.2**	-
Other accruals and deferred revenue	**127.6**	112.2
	300.6	188.1

	Company 2017 £m	Company 2016 £m
Other payables	**54.2**	-
Amounts owed to group undertakings	**32.0**	32.0
	86.2	32.0

The directors consider that the carrying values of trade and other payables are not materially different from their fair values.

20 Current borrowings

	Group 2017 £m	Group 2016 £m
Current		
Obligations under finance leases	**0.5**	-
Loans and other borrowings	**-**	50.0
Premium deferred on issue	**0.7**	0.7
Deferred gilt lock proceeds	**0.1**	0.1
Debt issue costs	**(1.9)**	(1.8)
	(0.6)	49.0

Further descriptions about the above items are given in note 21 ‘Non-current borrowings’.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

21 Non- current borrowings

An analysis of the external loans is shown below:

Loans and other borrowings:	**Notes**	**Group 2017 £m**	Group 2016 £m
Class A £350m 6.192% fixed rate 2029	(i), (ii), (iii)	**378.7**	380.4
Class A £150m 3.706% index linked 2034	(iii), (iv)	**259.2**	253.9
Class A £35m 3.706% index linked 2034	(iii), (iv)	**60.4**	58.5
Class A £350m 6.640% fixed rate 2026	(i), (ii)	**375.3**	377.4
Class A £150m 3.816% index linked 2023	(iii), (iv)	**235.2**	232.0
Class A £350m 5.000% fixed rate 2021	(i), (ii)	**348.2**	347.8
Class A £150m 5.000% fixed rate 2041	(i), (ii)	**145.7**	145.6
Class A £200m 4.500% fixed rate 2052	(i), (ii)	**197.1**	197.1
Class A £300m 5.125% fixed rate 2056	(i), (ii)	**292.7**	292.6
Class A £300m 6.125% fixed rate 2019	(i), (ii)	**299.2**	298.8
Class A £175m 2.780% fixed rate 2031	(ii)	**173.9**	-
Class A £75m 2.960% fixed rate 2036	(ii)	**74.5**	-
Class A £60m – 0.000% index linked 2025	(iv), (x)	**62.1**	60.5
Class A £40m - 0.000% index linked 2026	(iv), (xi)	**41.0**	-
Artesian £165m 4.076% index linked 2033	(iii), (iv)	**290.5**	285.0
Artesian £156.5m 3.635% index linked 2032	(iv)	**225.8**	221.7
Total Class A debt		**3,459.5**	3,151.3
Class B £250m 4.50% fixed rate 2038	(ii), (v)	**248.3**	247.8
£250m 8.500% Guaranteed Secured Fixed Rate Notes 2019	(ii)	**248.9**	248.2
£125m Facility Agreement 2016 – Libor plus 3.25% 2022	(vi)	**122.0**	123.0
£75m Facility Agreement 2016 – Libor plus 4% 2025	(vi)	**73.2**	73.8
Eurobonds 12% 2038 (note 32)		**997.6**	890.7
Term Facility Agreement 2014 £150m - 6-month Libor plus 1.95% 2021		**150.0**	150.0
Term Facility Agreement 2016 £50m – 6-month Libor plus 0.5% 2016		**-**	50.0
Debt issue costs	(vii)	**(183.2)**	(187.6)
Premium deferred on issue	(viii)	**10.2**	10.9
Deferred gilt lock proceeds	(ix)	**5.0**	5.2
Obligations under finance leases		**1.5**	1.5
Total borrowings		**5,133.0**	4,764.8
Current borrowings		**(0.6)**	49.0
Non-current borrowings		**5,133.6**	4,715.8

Non-current borrowings	**Group 2017 £m**	Group 2016 £m
Repayments fall due as follows:		
Between one and two years	**548.6**	-
Between one and five years	**1,617.8**	1,046.3
After five years not by instalments	**2,966.6**	3,669.5
	5,133.0	4,715.8

	Company 2017 £m	Company 2016 £m
Loans from group undertakings	**59.2**	59.2

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

21 Non-current borrowings (continued)

Class A and Class B loans are guaranteed and secured pursuant to a guarantee and security agreement (the Security Agreement). The agreement is over the entire property, assets, rights and undertaking of each of Southern Water Services Limited, Southern Water Services (Finance) Limited (SWSF), SWS Holdings Limited, and SWS Group Holdings Limited. In the case of Southern Water Services Limited, this is to the extent permitted by the Water Industry Act 1991 and the Licence to own and operate water assets.

Notes:

(i) The Group has entered into swap agreements that convert Class A fixed rate debt into either floating or index-linked debt in accordance with the Group's financial risk management policy.

(ii) Fixed rate bonds are recognised net of issue costs, discounts and inclusive of premiums (where applicable) on issue and are carried at amortised cost using the effective interest rate method.

(iii) The bond premiums referred to in note (ii) above also apply to various index-linked bonds. The premiums date back to 2003 when the related bonds were issued and arose when a number of the Group's swap instruments were effectively closed out and the resulting loss was rolled forward into the pricing of these bonds. The premiums are carried at amortised cost using the effective interest rate method.

(iv) The value of the capital and interest elements of the index-linked loans is linked to movements in the Retail Price Index. The increase in the capital value of index-linked loans during the year of £20.9 million (2016: £10.0 million) has been taken to the income statement as part of finance costs.

(v) The interest rate on the Class B £250 million is fixed at 4.50% until March 2022 when it reverts to Libor plus a margin to be determined.

(vi) The £200 million funds have been recognised net of associated issue costs amounting to £3.5 million combined. Both loans are being carried at amortised cost using the effective interest rate method.

(vii) Debt issue costs represent issue fees paid by SWSF and SWC that are not otherwise accounted for within the amortised cost of specific loans. Where these costs are attributable to a specific instrument they are being amortised over the life of that instrument. The remaining costs are being amortised over the weighted average life of the loans advanced at the time the costs were incurred. As at 31 March 2017 debt issue costs amounted to £183.2 million of which £1.9 million represents the short-term amount which is disclosed separately in note 20.

In addition to the above, swap break costs are included within this balance. These costs originated prior to securitisation when a swap was entered into, to act as a hedge for the future issue of bonds under securitisation. The swap was closed out and break costs were incurred when the bonds were issued in July 2003. The accounting treatment of these costs mirror the amortised cost value of opposing related bonds referred to in note (iii) above. These bonds are inclusive of premiums that compensate the swap break costs suffered.

(viii) The deferred bond premium represents the additional book value of the Class A Artesian £156.5 million loan issued in 2004. The premium is being amortised over the life of the bond.

(ix) Prior to the issue of the Class A £300 million bond in the year to 31 March 2008, SWSF entered into a gilt lock agreement, resulting in the receipt of £6.3 million, which was advanced to SWS along with the proceeds of the bond issue. The proceeds have been deferred and are being released to the income statement over the life of the loan.

(x) The Class A £60 million loan is index-linked with an interest rate of 0.00% until 2025.

(xi) The Class A £40 million loan is index-linked with an interest rate of 0.00% until 2026.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

21 Non-current borrowings (continued)

Repayments fall due as follows:	2017 £m	2016 £m
Borrowings excluding finance leases:		
Between one and two years not by instalments	**548.1**	-
Between two and five years not by instalments	**1,617.8**	1,044.8
After five years not by instalments	**2,966.7**	3,669.5
	5,132.6	4,714.3
On demand or within one year not by instalments	**(1.1)**	49.0
	5,131.5	4,763.3
Finance leases:		
Between one and two years not by instalments	**0.6**	1.3
Between two and five years not by instalments	**0.4**	0.2
After five years not by instalments	**-**	-
	1.0	1.5
On demand or within one year not by instalments	**0.5**	-
	1.5	1.5
Borrowings including finance leases:		
Between one and two years not by instalments	**548.7**	1.3
Between two and five years not by instalments	**1,618.2**	1,045.0
After five years not by instalments	**2,966.7**	3,669.5
	5,133.6	4,715.8
On demand or within one year not by instalments	**(0.6)**	49.0
	5,133.0	4,764.8

Obligations under finance leases comprise optional residual value balloon payments due on vehicle leases at the end of the lease period, where the minimum lease payments (including finance charges) have been prepaid at the start of the lease. If the company opts not to pay the balloon payment, it must return the vehicle to the lessor.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

22 Financial instruments

The following table provides a comparison by category of the carrying amounts of the Group's financial assets and financial liabilities at 31 March 2017 and 31 March 2016.

Financial assets and liabilities by category	Group 2017 £m	Group 2016 £m
Financial assets		
Derivative financial instruments designed as FVTPL*		
- Non-current	**9.4**	12.4
Held to maturity investments		
- Non-current	**0.1**	0.1
Trade and other receivables		
- Current (excluding prepayments)	**168.4**	177.2
Cash and cash equivalents		
- Current	**302.3**	38.1
Total financial asset	**480.2**	227.8
Financial liabilities		
Derivative financial instruments designed as FVTPL*		
- Non-current	**1,347.4**	936.1
Borrowings		
- Current	**(0.6)**	49.0
- Non-current	**5,133.6**	4,715.8
Trade and other payables		
- Current	**300.7**	188.1
Total financial liabilities	**6,781.1**	5,889.0

*Fair value through profit and loss.

The below table analyses derivative financial instruments held on the statement of financial position.

Derivative financial instruments	Group 2017 Assets £m	Group 2017 Liabilities £m	Group 2016 Assets £m	Group 2016 Liabilities £m
Derivative financial instruments not designated as hedges:				
Interest rate swaps	**9.4**	**(15.0)**	12.4	(16.1)
RPI swaps	**-**	**(1,332.4)**	-	(920.0)
Total derivative financial instruments	**9.4**	**(1,347.4)**	12.4	(936.1)
Derivative financial instruments can be analysed as follows:				
Current	**-**	**-**	-	-
Non-current	**9.4**	**(1,347.4)**	12.4	(936.1)
	9.4	**(1,347.4)**	12.4	(936.1)

The notional principal amount of the outstanding interest rate swap contracts at 31 March 2017 was £1,513.2 million (2016: £1,513.2 million).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

22 Financial instruments (continued)

In accordance with IAS 39 the Group has reviewed all contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard. None were identified during the year or previous year.

i) Financial risk management objectives and policies

The principal financial risks to which the Group is exposed are interest rate, liquidity and RPI risks. The Board has approved policies for the management of these risks.

Interest rate risk

The Group's interest rate risk is primarily in relation to its fixed rate borrowings (fair value risk) and floating rate borrowings (cash flow risk). Interest rate derivatives are used to manage the overall interest rate profile within the Group policy, which is to maintain a higher proportion of net debt at fixed rates of interest having regard to the prevailing interest rate outlook.

The weighted average effective interest rates at the statement of financial position dates by class of debt were as follows:

	Group 2017 %	Group 2016 %
By class of debt (all classed as financial liabilities)		
Class A	**4.68**	4.97
Class B	**4.74**	4.74
Artesian	**2.13**	2.21
Greensands £250m bond	**8.75**	8.67
Greensands £125m facility	**3.95**	4.54
Greensands £75m facility	**4.46**	4.97

The weighted average interest costs at the statement of financial position dates were as follows:

	Group 2017 %	Group 2016 %
Fixed	**8.43**	8.97
Floating	**3.47**	3.29
Indexed	**4.50**	4.57

Liquidity risk

The Group raises funds, as required, to ensure that it has sufficient cash and/or facilities to fund the business of Southern Water Services Limited for the next twelve months.

RPI risk and sensitivity analysis

The principal market risks are interest rates and movements in RPI. Interest rates on the Group’s loans are currently either fixed or fully effective swap instruments are in place to swap floating rates for fixed. RPI impacts indexation charged on index-linked loans and swaps. These instruments form an economic hedge with the Group’s revenues and regulatory assets, which are also linked to RPI inflation.

The Group also notes that the result of the recent EU referendum will increase uncertainty around these risk areas in the short term.

For further details about Group financing matters please refer to the ‘Capital structure, liquidity and other financial matters’ section of the Strategic Report contained within these financial statements on page 7.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

22 Financial instruments (continued)

ii) Maturity of financial liabilities and financial instruments

The maturity profile of the Group's financial liabilities at 31 March 2017 and 31 March 2016 is disclosed within note 21.

The table below analyses the Group's derivative financial instruments into relevant maturity profiles based on the remaining period at the reporting date.

	Within one year £m	**Within two to five years £m**	**Within five to 25 years £m**	**After 25 years £m**	**Total £m**
At 31 March 2017					
Derivative financial instruments – asset	**-**	**9.4**	**-**	**-**	**9.4**
Derivative financial instruments – liability	**-**	**(178.7)**	**(516.1)**	**(652.6)**	**(1,347.4)**
	-	**(169.3)**	**(516.1)**	**(652.6)**	**(1,338.0)**

	Within one year £m	Within two to five years £m	Within five to 25 years £m	After 25 years £m	Total £m
At 31 March 2016					
Derivative financial instruments – asset	-	12.4	-	-	12.4
Derivative financial instruments – liability	-	(127.5)	(368.4)	(440.2)	(936.1)
	-	(115.1)	(368.4)	(440.2)	(923.7)

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

22 Financial instruments (continued)

iii) Fair values of financial assets and financial liabilities

The following table provides a comparison by category of the carrying amounts and the fair values of the Group's financial assets and financial liabilities at 31 March 2017 and 2016.

	Group 2017 Book value £m	**Group 2017 Fair value £m**	Group 2016 Book value £m	Group 2016 Fair value £m
Cash and cash equivalents	**302.3**	**302.3**	38.1	38.1
Non-current asset investments	**0.1**	**0.1**	0.1	0.1
Non-current derivative financial instruments	**9.4**	**9.4**	12.4	12.4
	311.8	**311.8**	50.6	50.6
Current borrowings	**0.6**	**0.6**	(49.0)	(49.0)
Non-current borrowings	**(5,133.6)**	**(6,166.7)**	(4,715.8)	(5,373.0)
Non-current derivative financial instruments	**(15.0)**	**(15.0)**	(16.1)	(16.1)
Non-current RPI swaps	**(1,332.4)**	**(1,332.4)**	(920.0)	(920.0)
	(6,480.4)	**(7,513.5)**	(5,700.9)	(6,358.1)

Derivative activity is undertaken by subsidiaries in the Group, Greensands Senior Finance Limited, Southern Water (Greensands) Financing Plc and Southern Water Services (Finance) Limited (SWSF), as determined by the Board, which considers the overall risk profile of the Group and enters into derivatives to mitigate or hedge any risks identified, as appropriate. No derivatives are undertaken for trading purposes, or to benefit from price fluctuations.

No derivative activity is undertaken by the company.

The SWSF business consists of lending to other group companies and raising external finance.

All fair values are based on arm's length transactions in normal market conditions. Where available, market values have been used to determine fair values.

The fair value of the Group's long-term borrowings has been estimated based on quoted market prices for the same or similar debt where possible. Where prices did not exist, the fair value has been estimated based on the calculations of the present value of future cash flows using the appropriate discount rates in effect at the statement of financial position dates.

For interest rate swap agreements the fair value has been estimated based on market valuations at the statement of financial position dates.

The Group has no material un-hedged monetary assets and liabilities denominated in a currency different from the local currency of the particular operation.

Fair values of other non-current liabilities, current trade and other payables, provisions and current trade and other receivables have been estimated as not materially different from book value and have been excluded from the table above. The same can be said for non-current asset investments; however, this balance has been displayed in the table above.

In accordance with IFRS 13 'Fair Value Measurement', the financial instruments carried at fair value on the statement of financial position have been classified as level 2 for fair valuation purposes, being valued by reference to valuation techniques using observable inputs other than quoted prices in active markets for identical assets and liabilities. The future cash flows have been discounted at a rate that reflects credit risk.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

23 Deferred tax liabilities

Deferred tax is provided as follows:

	Accelerated tax depreciation £m	Revaluation of financial instruments £m	Retirement benefit obligations £m	Losses and other timing differences £m	Total £m
At 1 April 2015	631.5	(173.9)	(25.3)	32.2	464.5
(Credit)/charge to income statement	21.6	(9.9)	6.1	(11.1)	6.7
Credit to other comprehensive income	-	-	(2.8)	-	(2.8)
Effect of change in tax rate –income statement	(65.3)	18.4	2.2	(2.2)	(46.9)
At 1 April 2016	587.8	(165.4)	(19.8)	18.9	421.5
(Credit)/charge to income statement	(12.4)	(67.5)	0.1	(9.7)	(89.5)
Credit to other comprehensive income	-	-	(12.8)	-	(12.8)
Effect of change in tax rate –income statement	(32.0)	12.9	0.1	(0.9)	(19.9)
-other comprehensive income	-	-	1.7	-	1.7
At 31 March 2017	**543.4**	**(220.0)**	**(30.7)**	**8.3**	**301.0**

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to do so. The following is the analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2017 £	2016 £
Deferred tax liabilities	**543.4**	609.7
Deferred tax assets	**(242.4)**	(188.2)
	301.0	421.5

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

24 Retirement benefit obligations

The deficit associated with retirement benefit obligations has increased to £176.9 million (2016: £102.3 million) as a result of a decrease in corporate bond yields which decrease the discount rate used to calculate the value of pension scheme liabilities, offset by asset returns.

Pension schemes operated

The Group principally operates one defined benefit pension scheme (final salary) and one defined contribution scheme, details of which are shown below:

1. Southern Water Pension Scheme (SWPS), a funded defined benefit scheme, was closed to new members on 31 December 1998, re-opened in July 2003 and closed once more to new entrants on 1 April 2005. This scheme has nine trustee directors. The Southern Water Services Executive Pension Scheme (SWEPS) was also closed to new entrants and merged with the SWPS on 1 April 2005.

   The Trustees are responsible for administrating the Fund which is held separately from the company. Legal and General and Blackrock are unit registrars for Southern Water Pension Scheme unit holdings, and appoint custodians at individual pooled fund level (not client holding level). The directors of SWS are responsible for setting the accounting assumptions for the fund for inclusion in these financial statements.

   The main risks of the scheme are as follows:

   a) Asset volatility

      For the purpose of setting the contribution requirements, the calculation uses a discount rate set with reference to government bond yields, with allowance for additional return to be generated from the investment portfolio – whereas under FRS 101, the defined benefit obligation is calculated using a discount rate set with reference to corporate bond yields.

      The schemes hold a significant proportion of their assets in growth assets. The returns on these assets may be volatile and are not correlated to the value placed on the liabilities. This means that the deficit may be volatile in the shorter term, which may result in an increase in the contribution requirements and an increase in the net defined benefit liability recorded on the statement of financial position.

      However, the company believes that return-seeking assets offer an appropriate level of return over the long term for the level of risk that is taken. Furthermore, the scheme's other assets are well-diversified by investing in a range of asset classes, including liability-driven investments, government bonds and corporate bonds.

   b) Changes in bond yields

      A fall in bond yields increases the value placed on the liabilities for reporting purposes and for setting the company's contribution requirements. However, in this scenario the scheme's investment in corporate and government bonds is expected to increase and therefore offset some of the increase in the value placed on the liabilities.

   c) 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 scheme's liabilities. This is particularly significant where the longer duration and inflation-linked nature of the payments result in higher sensitivity to changes in life expectancy. The scheme does not contain a hedge against increases in future life expectancy.

   d) Inflation risk

      The majority of the scheme's benefit obligations are linked to inflation and higher out-turn inflation will lead to a higher benefit obligation (although in most cases caps on the level of inflationary increases are in place to protect the plan against extreme inflation). The majority of the schemes' assets do not provide a direct hedge against changes in inflation as they are either fixed-interest in nature, e.g. corporate bonds and government bonds, or have an indirect link to inflation, e.g. equities.

Notes to the financial statements (continued)
For the year ended 31 March 2017

24 Retirement benefit obligations (continued)

2. A second company stakeholder scheme, which is a defined contribution scheme, is also available to all employees.

   Contributions made to the defined contribution scheme for the year ended 31 March 2017 amounted to £2.6 million (2016: £2.3 million). No contributions were outstanding at either year-end.

   Members of all schemes receive an annual statement of their accrued benefits.

   The latest actuarial valuation of the SWPS was carried out as at 31 March 2013 using the projected unit method. For closed schemes under this method the current service cost will increase as the members of the schemes approach retirement. The assumptions that have the most significant effect on the results of the valuation are those relating to the rate of return on investments, and the level of inflation, which drives pension increases in the SWPS.

The principal assumptions in the valuation were as follows:

	2013 SWPS % per annum (pa)
Return on investments: pre-retirement Return on investments: post-retirement (pensioner/non-pensioner)	FI Gilt curve + 65 bps
Salary growth	2.50%
Pension increases on the excess over guaranteed minimum pensions (where capped at 5% pa)	2.75%

The term ‘FI Gilt curve’ refers to the generally available fixed interest gilt yield curve agreed by the Trustees and the company for the purposes of the 2013 actuarial valuation.

The assets of the scheme had a market value of £574.5 million at 31 March 2013. This was sufficient to cover 77% of the scheme’s benefits. The duration of the scheme liabilities is 21 years.

Expected employer and employee contributions to the defined benefit scheme for 2017-18 are £5.6 million and £0.2 million respectively under the current Schedule of Contributions.

Notes to the financial statements (continued)

For the year ended 31 March 2017

24 Retirement benefit obligations (continued)

IAS 19 – assumptions, asset, liability and reserves disclosures

The formal actuarial funding valuation was carried out as at 31 March 2013 and updated to 31 March 2016 by a qualified independent actuary. The major assumptions used by the actuary are set out in the table below.

	2017	2016
	% pa	% pa
Price inflation (RPI)	3.3	3.0
Price inflation (CPI)	2.3	2.0
Rate of increase in salaries (plus an age-related promotional scale)	2.4	2.5
Rate of increase of pensions in payment (MIS* members only)***	2.3	2.0
Rate of increase of pensions in payment (Old section** members only)***	3.3	3.0
Rate of increase of pensions in payment (all other members)***	3.2	2.9
Rate of increase for deferred pensions (MIS* members only)***	2.3	2.0
Rate of increase for deferred pensions (all other members)***	3.2	2.9
Discount rate	2.8	3.6

* MIS refers to the Southern Water Mirror Image Pension Scheme. Pensions in payment and deferment for this section will be indexed in line with the Consumer Price Index.

** For this section the Trustee will endeavour to meet any indexation of excess pension above the 5% per annum cap on increases that apply to other sections of the Scheme.

*** In excess of any Guaranteed Minimum Pension (GMP) element.

Assumptions regarding future mortality experience are set based on advice, published statistics and experience. For 2016–17, the company has used the post-retirement mortality assumptions based on the standard SAPS mortality tables together with future improvements in line with CMI 2014 improvements with a long-term improvement rate of 1.25% per annum.

	2017	2016
	Years	Years
Longevity at age 65 for current pensioners		
Male	**22.7**	23.0
Female	**24.8**	25.1
Longevity at age 65 for future pensioners		
Male	**24.4**	24.8
Female	**26.7**	27.0

Notes to the financial statements (continued)

For the year ended 31 March 2017

24 Retirement benefit obligations (continued)

The assets and liabilities in the schemes and the expected rates of return at 31 March 2017 and 31 March 2016 were:

	Value at 2017 £m	Value at 2016 £m
Equities	**186.1**	171.5
Government bonds	**190.3**	196.2
Non-government bonds	**355.5**	266.3
Cash	**11.0**	40.1
Total market value of plan assets	**742.9**	674.1
Total value of plan liabilities	**(919.8)**	(776.4)
Accrued deficit in the plan	**(176.9)**	(102.3)
Related deferred tax asset	**30.7**	19.8
Net retirement benefit obligations	**(146.2)**	(82.5)

The equity investments and bonds which are held in plan assets are quoted and are valued at the current bid price.

Reconciliation of the present value of the scheme liabilities	**2017 £m**	2016 £m
At 1 April	**776.4**	789.3
Current service cost	**5.1**	5.4
Interest expense	**27.5**	26.4
Member contributions	**0.2**	0.2
Experience gain on liabilities	**(12.0)**	-
Actuarial (gain)/loss on liabilities:		
- due to changes in demographic assumptions	**(11.0)**	10.0
- due to changes in financial assumptions	**165.6**	(27.1)
Benefits paid	**(32.0)**	(27.8)
Scheme liabilities at 31 March	**919.8**	776.4

Sensitivity analysis of the scheme liabilities

The sensitivity of the present value of the scheme liabilities to changes in the principal assumptions used is set out below.

	Change in assumption	Impact on scheme liabilities (%)	Impact on scheme liabilities (£m)
Discount rate	+/- 1%	-/+ 15	-/+ 116
Rate of inflation*	+/- 1%	+/- 13	+/- 101
Rate of increase in pensions in payment	+/- 1%	+/- 11	+/- 85
Mortality	+/- 1yr	+/- 3	+/- 23

*A change in inflation is assumed to be reflected in a change in the assumed rates of deferment revaluation and pension increase (on pension in excess of GMP).

The above sensitivity analysis is based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. The methods and types of assumptions used in preparing the sensitivity analysis did not change compared to the previous period.

Notes to the financial statements (continued)
For the year ended 31 March 2017

24 Retirement benefit obligations (continued)

Reconciliation of the value of the scheme assets	**2017 £m**	2016 £m
At 1 April	**674.1**	674.0
Interest income	**23.8**	22.5
Gain/(loss) on assets above interest	**71.2**	(31.1)
Employer contributions	**5.6**	37.2
Member contributions	**0.2**	0.2
Benefits paid	**(32.0)**	(27.8)
Administrative expenses	**-**	(0.9)
Bid value of scheme assets at 31 March	**742.9**	674.1

The total return on scheme assets was £95.0 million (2016: loss of £9.5 million).

Total cost recognised as an expense	**2017 £m**	2016 £m
Current service cost	**5.1**	5.4
Net interest cost	**3.7**	3.9
Administration expenses	**-**	0.9
Total income statement expense before deduction for tax	**8.8**	10.2

Analysis of the amounts recognised in other comprehensive income	**2017 £m**	2016 £m
Actual return less expected return on pension scheme assets	**71.2**	(31.1)
Experience gain arising on scheme liabilities	**12.0**	-
Gain/(loss) due to changes in demographic assumptions	**11.0**	(10.0)
(Loss)/gain due to changes in financial assumptions	**(165.6)**	27.1
Total loss recognised in OCI before adjustment for tax	**(71.4)**	(14.0)

The cumulative amount of actuarial losses recognised in other comprehensive income is £264.9 million (2016: £193.5 million).

Analysis of the movement in the scheme's deficit during the year	**2017 £m**	2016 £m
Deficit in the scheme at 1 April	**(102.3)**	(115.3)
Employer's contributions	**5.6**	37.2
Employer's current service cost	**(5.1)**	(5.4)
Financing charge	**(3.7)**	(3.9)
Administration expenses	**-**	(0.9)
Actuarial loss	**(71.4)**	(14.0)
Deficit in the scheme at end of year	**(176.9)**	(102.3)

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

25 Provisions for liabilities

	Group 2017 £m	Group 2016 £m
Environmental obligations		
Provision as at 1 April	**0.5**	0.5
Utilised in year	**-**	-
Provision at 31 March	**0.5**	0.5

The environmental provision relates to costs for the decommissioning of abandoned sites. No reimbursement is expected. The period over which the provision will be utilised cannot be determined thus the provision is not discounted. Discounting the provision would not materially affect its value.

26 Other non-current liabilities

	Deferred revenue £m	Grants & contributions £m	Group Total £m
At 1 April 2016	14.5	29.0	43.5
Receivable in year	-	20.2	20.2
Released to income statement	(0.3)	(1.2)	(1.5)
At 31 March 2017	**14.2**	**48.0**	**62.2**

These grants and contributions relate to property, plant and equipment.

Deferred revenue of £14.2 million (2016: £14.5 million) relates to the proceeds from the sale of income rights relating to aerial masts and sites owned by the Group. The income will be credited to the income statement evenly over the life of the lease.

27 Called up share capital

	Group and Company 2017 £m	Group and Company 2016 £m
Authorised, allotted, called up and fully paid		
921,874,025 Ordinary shares of £1 each	**921.9**	921.9

The company has one class of ordinary share which carries no right to fixed income. The holders of ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at meetings of the company.

28 Other reserves

	Group and Company 2017 £m	Group and Company 2016 £m
Share premium account	**4.5**	4.5
Retained earnings	**(1,722.9)**	(1,204.6)
	(1,718.4)	(1,200.1)

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

29 Notes to the cash flow statement

Cash generated by operations	2017 £m	2016 £m
Continuing operations		
Operating profit	**250.2**	275.7
Adjustments for:		
Depreciation of property, plant and equipment	**237.6**	233.3
Amortisation of intangible assets	**14.9**	8.7
Difference between pension charge and cash contributions	**(0.4)**	(31.0)
Amortisation of grants and contributions	**(1.2)**	(1.1)
Operating cash flows before movements in working capital	**501.1**	485.6
Increase in inventories	**(0.4)**	(0.2)
Decrease in receivables	**3.3**	12.7
Increase/(decrease) in payables	**20.1**	(16.5)
Cash from operating activities	**524.1**	481.6
Tax paid	**(0.1)**	-
Net cash generated from operating activities	**524.0**	481.6

Cash and cash equivalents	2017 £m	2016 £m
Cash and bank balances	**302.3**	38.1

Cash and cash equivalents comprise cash and short-term bank deposits with an original maturity of three months or less, net of outstanding bank overdrafts. The carrying amount of these assets is equal to their fair value.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

29 Notes to the cash flow statement (continued)

Analysis of net debt	**At 1 April 2016 £m**	**Cash flow £m**	**Other non-cash changes £m**	**At 31 March 2017 £m**
Cash and cash equivalents	38.1	264.2	-	**302.3**
Derivative financial instruments	(923.7)	2.5	(416.8)	**(1,338.0)**
Debt issue costs	187.6	-	(4.4)	**183.2**
Gilt lock proceeds	(5.2)	-	0.2	**(5.0)**
Borrowings due within one year	(50.7)	50.0	-	**(0.7)**
Borrowings due after one year	(4,895.0)	(288.3)	(125.7)	**(5,309.0)**
Finance leases	(1.5)	0.3	(0.3)	**(1.5)**
Net debt	(5,650.4)	28.7	(547.0)	**(6,168.7)**

Balances at 31 March 2017 comprise:	**Current assets £m**	**Current liabilities £m**	**Non-current liabilities £m**	**Total £m**
Cash and cash equivalents	302.3	-	-	**302.3**
Derivative financial instruments	-	-	(1,338.0)	**(1,338.0)**
Debt issue costs	-	1.9	181.3	**183.2**
Gilt lock proceeds	-	(0.1)	(4.9)	**(5.0)**
Borrowings due within one year	-	(0.7)	-	**(0.7)**
Borrowings due after one year	-	-	(5,309.0)	**(5,309.0)**
Finance leases	-	(0.5)	(1.0)	**(1.5)**
Net debt	302.3	0.6	(6,471.6)	**(6,168.7)**

The non-cash movement of £547.0 million relates to an increase in debt as a result of indexation, fair value losses on derivative financial instruments, Eurobond interest, plus the amortisation of loan issue costs, gilt lock proceeds, and deferred proceeds.

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

30 Contingent liabilities

Contractors submit claims to Southern Water for the estimated final cost of their works. These claims are reviewed to assess where the liability for the costs rests and the amount that will actually be settled. The expected amount is included within capital creditors and a further sum is identified as a contingent liability, representing a proportion of the difference between the contractor's claim and Southern Water's valuation.

Neither the company nor the Group had any contingent liabilities for capital claims at the year-end (2016: £nil).

Southern Water is subject to a number of claims, disputes and potential litigation as is normal for a company of its size and nature. These include investigations by regulatory bodies, the EA and DWI, as well as a claim in respect of property search income. The directors of the company and Group consider that an appropriate position has been taken in reflecting such items in these financial statements. It is not currently possible to estimate the financial effect and likely timing of any associated outflow given the early stage of these investigations and claims.

31 Financial commitments

(a) Capital commitments are as follows:

	2017 £m	2016 £m
Contracted for but not provided for in respect of contracts placed in respect of property, plant and equipment	**354.8**	183.9
Contracted for but not provided for in respect of contracts placed in respect of intangible assets	**9.7**	9.9

(b) The Group as lessee

	2017 £m	2016 £m
Lease payments under operating leases recognised as an expense in the year	**3.9**	3.9

As at 31 March 2017 and 2016, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases in respect of vehicles and land and buildings for which the payments fall due as follows:

	Land and buildings		Other	
	2017 **£m**	2016 £m	**2017** **£m**	2016 £m
Within one year	**1.7**	1.7	**0.2**	0.2
In the second to fifth years inclusive	**6.2**	6.3	**0.3**	0.4
After five years	**13.0**	14.5	**0.1**	0.1
	20.9	22.5	**0.6**	0.7

Operating leases are charged to the income statement over the lease term.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

32 Related party transactions

Balances and transactions between the company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note. Transactions between the Group and its associates are disclosed below.

Greensands Holdings Limited is owned and controlled by a consortium of investors. At 31 March 2017, the largest shareholder in Greensands Holdings Limited is an institutional investment company advised by JP Morgan Asset Management.

The transactions and balances with the Group's related parties (i.e. the shareholders) are summarised below.

	2017 £m	2016 £m
Eurobond interest		
IIF Int'l SW UK Investment Ltd	**33.4**	29.8
Phildrew Nominees Ltd	**21.8**	15.0
National Nominees Ltd	**8.3**	7.4
The Northern Trust Company	**-**	22.4
Sky Brace Investments Ltd	**5.1**	4.5
Sumaya Investments Ltd	**5.1**	4.5
Falkirk Council - Falkirk Council Pension Fund	**0.4**	-
The City of Edinburgh Council – Lothian Pension Fund and Lothian Buses Pension Fund	**1.2**	-
Hermes GPE Infrastructure Fund LP	**22.4**	3.7
SW Holdings LP	**2.1**	1.9
Simcoe Yeoman Water Ltd	**7.1**	6.3
Total Eurobond interest payable to related parties	**106.9**	95.5
Loans and other borrowings greater than one year:		
Eurobonds – Shareholder loans		
IIF Int'l SW UK Investment Ltd	**112.4**	112.4
Phildrew Nominees Ltd (UBS IIF)	**20.1**	20.1
Phildrew Nominees Ltd (UBS IINF)	**2.8**	2.8
Phildrew Nominees Ltd (UBS II4F)	**22.2**	22.2
Phildrew Nominees Ltd (UBS IIUSTEF)	**11.1**	11.1
Phildrew Nominees Ltd (UBS IIF (A) LP)	**5.2**	-
Phildrew Nominees Ltd (UBS IIF (B) LP)	**6.9**	-
Phildrew Nominees Ltd (UBS IIF (C) LP)	**5.0**	-
National Nominees Ltd - Motor Trades Association of Australia Super Fund	**21.4**	21.4
National Nominees Ltd – Prime Super	**6.5**	6.5
The Northern Trust Company (as custodian for Future Fund Investment Company No.2 Pty Ltd)	**-**	84.2
Sky Brace Investments Ltd	**17.1**	17.1
Sumaya Investments Ltd	**17.1**	17.1
Falkirk Council - Falkirk Council Pension Fund	**1.4**	-
The City of Edinburgh Council – Lothian Pension Fund and Lothian Buses Pension Fund	**4.1**	-
Hermes GPE Infrastructure Fund LP	**14.0**	14.0
Hermes GPE Infrastructure Fund Spring I LP	**7.8**	-
Hermes GPE Infrastructure Fund Spring II LP	**46.0**	-
Hermes GPE Infrastructure Fund Spring III LP	**7.8**	-
SW Holdings LP	**7.0**	7.0
Simcoe Yeoman Water Ltd	**23.9**	23.9
Accrued interest	**637.8**	530.9
Total Eurobonds – Shareholder loans	**997.6**	890.7

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2017

33 Subsidiaries

As at 31 March 2017 the company held 100% of the ordinary share capital of Greensands Europe Limited. Greensands Europe Limited's principal subsidiaries are listed below and are included within these consolidated financial statements.

Company	Registered address	Activity
Greensands UK Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water (Greensands) Financing plc	Southern House, Yeoman Road, Worthing	To raise debt finance
Greensands Junior Finance Limited	Southern House, Yeoman Road, Worthing	To raise debt finance
Greensands Senior Finance Limited	Southern House, Yeoman Road, Worthing	To raise debt finance
Greensands Investments Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water Capital Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water Investments Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water (NR) Holdings Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water (NR) Limited	1 Exchange Crescent, Conference Square, Edinburgh	Non-trading activities
SWS Group Holdings Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
SWS Holdings Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water Limited	Southern House, Yeoman Road, Worthing	Intermediate parent company for Southern Water(NR) Group
Southern Water Services Limited	Southern House, Yeoman Road, Worthing	Supply of Water and Wastewater Services
Southern Water Services Finance Limited*	Ugland House, PO Box 309, George Town, Grand	To raise debt finance
Southern Water Services Group Limited	Southern House, Yeoman Road, Worthing	Non-trading activities
Southern Water Industries Limited	Southern House, Yeoman Road, Worthing	Dormant
Bowsprit Holdings Limited	Southern House, Yeoman Road, Worthing	Dormant
Monk Rawling Limited	Southern House, Yeoman Road, Worthing	Dormant
Bowsprit Property Development Limited	Southern House, Yeoman Road, Worthing	Property development
EcoClear Limited	Southern House, Yeoman Road, Worthing	Dormant
Southern Water Executive Pension Scheme Trustees Limited	Southern House, Yeoman Road, Worthing	Dormant
Southern Water Pension Trustees Limited	Southern House, Yeoman Road, Worthing	Dormant
Southern Water Retail Services Limited	Southern House, Yeoman Road, Worthing	Dormant

*The country of incorporation for this company is the Cayman Island.
All of the above subsidiary companies are wholly-owned by ordinary shares.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2017

34 Post balance sheet events

Following careful consideration of the options available to Southern Water regarding the opening of the non-household retail market, the company disposed of its non-household retail business function with effect from 1 April 2017. It is estimated that this disposal will have an immaterial impact on operating profit.

Independent auditor's report to the members of Greensands Holdings Limited

We have audited the financial statements of Greensands Holdings Limited for the year ended 31 March 2017 which comprise the Consolidated Income Statement, the Consolidated Statement of Other Comprehensive Income, the Consolidated and Company Statements of Financial Position, the Consolidated and Company Statements of Changes in Equity, the Consolidated Statement of Cash Flows and the related notes 1 to 34. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB).

This report is made solely to the company's members, as a body, in accordance with Article 113A of the Companies (Jersey) Law 1991. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

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

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Group's and the company's affairs as at 31 March 2017 and of the Group's loss for the year then ended;
- have been properly prepared in accordance with IFRSs as issued by the IASB; and
- have been properly prepared in accordance with the Companies (Jersey) Law 1991.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies (Jersey) Law 1991 requires us to report to you if, in our opinion:

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

Anthony Matthews

Anthony Matthews
for and on behalf of Deloitte LLP
London, United Kingdom
21 July 2017