

WESSEX WATER SERVICES LTD

Annual Report and Financial Statements
30 June 2016

Registered in England and Wales No. 2366648

CONTENTS

	page
STRATEGIC REPORT	2 to 16
PRINCIPAL RISKS	17 and 18
THE BOARD OF DIRECTORS	19 and 20
GOVERNANCE REPORT	21 to 45
DIRECTORS' REPORT	46 and 47
STATEMENT OF DIRECTORS' RESPONSIBILITIES	48
INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF WESSEX WATER SERVICES LTD	49
INCOME STATEMENT	50
STATEMENT OF OTHER COMPREHENSIVE INCOME	51
BALANCE SHEET	52
STATEMENT OF CHANGES IN EQUITY	53
CASH FLOW STATEMENT	54
NOTES TO THE FINANCIAL STATEMENTS	55 to 80

Strategic Report

Introduction

Overall performance - some indicators are measured for the regulatory year to 31 March 2016

Last year was the first of the new five-year price control period. It brought the introduction of a more risk-based framework with a focus on the outcomes that our customers and local communities want. We have performed well against our performance commitments and achieved industry leading customer service and environmental performance.

Average bills reduced by 5% from April 2015 and through our assistance programme **tap**, we continued to support customers who are financially vulnerable and have difficulty in paying. We are now helping more than 21,000 customers to pay ongoing charges and repay debt, as well as offering additional practical help to reduce water and energy bills.

This year, with the guidance of our expert affordability advisory group, we have introduced a discount of around 20% for pensioners on the lowest incomes who often suffer hardship in silence instead of asking for help.

We are committed to providing the highest quality drinking water to our customers and overall compliance in 2015 was 99.96%. The number of customer contacts we received about acceptability of water reduced significantly, largely because of the beneficial effect of the major mains rehabilitation work we completed in Taunton last year.

Our water supply grid project is making excellent progress and once complete will ensure future demand is met and improve the resilience of supplies to our customers.

Customer excellence

We are a customer centred organisation and believe in putting customers and the communities we serve at the heart of everything we do – our aim is always to achieve the best outcome for them.

We focus on understanding customers' changing needs and responding to the pressures that many continue to be under in these challenging economic times. We are committed to providing help when and where it's needed most because anyone can find themselves vulnerable at any time through illness, unemployment or simply a change in circumstances like a bereavement or divorce.

When we have problems on our network, such as a burst water main, we are using proactive phone calls and text messages to let customers know what the problem is, what we're doing to resolve it and by when, and this is helping improve satisfaction levels.

Our staff need the right skills, confidence and awareness to deal with often quite complex situations, so we make sure we provide specialist training so they can offer the very best support to customers they talk to or meet in their work.

Investing in the community

As a community business and the largest infrastructure investor in the region, we create more than 1,000 jobs directly in constructing new assets and in the regional supply chain. We continue to invest in greater resilience to climate change and supporting economic growth across our region.

We have made good progress on a £39m programme of work to improve bathing water quality at Burnham-on-Sea and we are investing in a number of very innovative projects, some of which are industry firsts. In the Poole Harbour catchment we are working with farmers to reduce nitrate runoff and leaching into the River Frome in the first nitrogen offsetting trial in the UK.

Management of nearly 300 hectares of land designated as Sites of Special Scientific Interest (SSSIs) means that the condition of these vital habitats exceeded government targets. 99.5% of SSSIs were assessed as being in favourable or recovering status.

Innovation and resilience

We must adopt new ways of working and technologies that help improve the services we provide, reduce costs and manage risk. Our employee suggestion scheme, Eureka!, rewards ideas that have been put into practice and is also a way of identifying improvements that can be scaled up.

We run a joint research programme with the University of Bath with whom we've launched a water innovation and research centre based at the university. We have continued to push improvements in efficiency and resource use with more than 95% of the waste we generate diverted from landfill and increasing the value recovery.

We are tackling the reduction of our carbon footprint. In 2015-16 we completed installation of advanced anaerobic digestion and electricity generation at Trowbridge sewage treatment works and installed a large solar photovoltaic array on the roof of our operations centre in Bath.

Strategic Report (continued)

The responsibility for flooding is often complex and we are encouraging partnership working including three partnership schemes to reduce flooding in Somerset at Cannington, Brent Knoll and Wrington.

Working in partnership

This year we have established a new format for our stakeholder liaison through the Wessex Water Partnership, independently chaired by former Water Minister Dan Rogerson.

The Partnership will ensure we deliver the commitments in our current five-year plan and provide advice on customer engagement, customer service, affordability and tariffs in preparation for the next business plan.

Our partnerships with debt advice organisations continue to thrive and we remain convinced that holistic advice is needed to help customers to get back on track and into sustainable payment. In 2013 we set up an affordability action plan and this year the take-up of our schemes and low rate tariffs has increased by 19%.

A focus of the past year has been our work in partnership with our supply chain to remove the very variable investment programme that results from a five-year regulatory cycle. This was assisted by Ofwat's 'early start' programme. As a result, the first year of the current AMP (asset management plan) cycle, from April 2015 to March 2016, has achieved a stable capital programme with expenditure for the year at £200.8m compared to £198.4m for the last year of the previous AMP cycle.

A responsible employer

We can only deliver excellent service to our customers and communities and value to our investors, through the knowledge and skills of our employees and the quality of the assets that we manage and operate.

We are focused on retaining existing and attracting new skills into the business with a commitment to develop staff to their full potential – through leadership and management development, apprenticeship programmes and promotion of diversity and inclusion.

This year we continue to develop our apprenticeship programmes to provide young people with career and skill development opportunities, and to build a strong and skilled workforce for the future – we now have some 51 apprentices and trainees within the business.

We have a strong health, safety and welfare culture embedded in our day-to-day activities that targets zero accidents and supports our aim to be a great place to work in which all employees can work safely and reach their full potential.

Financial results

Turnover for 2015-16 decreased to £521.8m and profit after tax was £166.5m. Operating costs were maintained at the same level as last year and we achieved all our key financial targets in the year.

Dividends were declared in accordance with Board policy which at all times is to preserve our investment grade credit ratings and access to new capital.

We continue to maintain a straightforward corporate structure, pay the expected level of corporation and other taxes and are classed by the Inland Revenue as low risk.

Planning for the future

The water industry is approaching fundamental change with moves to greater competition and more use of markets. We support these changes and are at the forefront of helping shape their delivery. The key to their success will be what they deliver for customers.

Our customer service vision is very simple – we aim to deliver the highest levels of customer satisfaction, make it easy for customers to deal with us and to build trust and loyalty.

We are always looking for improvements and have launched a customer excellence programme which includes improved customer systems, community projects, improved communication and shortened response times.

We take pride in being the best company in the water sector, but that is not enough – we aim to be seen by our customers as the best service provider that they deal with and we are committed to driving the investment, skills and culture that enable us to achieve this ambitious aim.

Strategic Report (continued)

Customers and communities

Introduction

We achieve our customer service vision by delivering what customers say is really important to them:

- excellent and reliable water and sewerage services at a price they can afford
- choice in the way they can communicate and interact with us
- a real person to answer the telephone
- resolving problems quickly and first time
- keeping them informed at all times
- checking they are happy with the outcome if they have a problem
- compensating where things go wrong.

We encourage our staff to go the extra mile (GEM) whenever they can.

We remain the top performer in the water sector for customer service. In the first year of the new look service incentive mechanism (SIM) we have come top of all water and sewerage companies in the satisfaction surveys, showing that however customer service is measured, we continue to be the best.

But we can't stand still. Customer expectations continue to rise and we know that young people today, who will be our customers of tomorrow, will want a very different and increasingly digital customer service experience.

Similarly, we recognise that customers can very often find themselves in vulnerable circumstances for a short or long period of time, so we need increasingly to tailor our service so that we always meet their needs.

Although we take pride in being top of the water sector, our ambition is to be the 'best of the best' and to become a household name for excellent customer service.

To do this we are embarking on a customer excellence programme which includes more than 20 individual projects, ranging from improved customer systems, signage and community projects, to improved communication and shortened response times.

To make sure we get this right we have introduced measures, like net promoter score, that compare us to the best service providers outside the utility sector. And we've become a member of the Institute of Customer Service so we can benchmark ourselves against the UK Customer Service Index.

Reduced leakage

Our leakage strategy has successfully reduced leakage to 68 MI/d, below the Ofwat target of 69.3MI/d.

We plan to operate below target in normal years to maintain a buffer in case severe winter weather causes additional leakage. This year we have planned an enhanced metering programme and a pressure management optimisation project, with the aim of further leakage reduction so we can meet our ambitious target by 2020.

Our target to fix significant leaks on the network reported to us by customers has been met, mainly by improving existing processes and procedures.

Highest quality drinking water

We are committed to providing the highest quality drinking water to our customers.

Our overall compliance with drinking water standards in 2015 was 99.96%. This was marginally below our long-term performance. This is based on the mean zonal compliance for 39 parameters out of approximately 37,000 tests carried out across 88 zones. The calculation is very sensitive to individual failures. In 2015 there were 15 failures of which only two were related to the Company's operation; from a cast iron water main and a tap at a treatment unit that was not representative of the water supplied.

The other 13 can be attributed to domestic plumbing and service pipe issues such as lead service pipes, nickel in taps and taste due to water softeners.

There was a significant reduction in the number of customer contacts about acceptability of water received during the year, largely related to the beneficial effect of the major mains rehabilitation works we completed in Taunton.

We are seeing a downward trend in the number of contacts received and we expect this to continue as we invest in our assets and find new ways of communicating with customers.

During the year we have made significant investment at service reservoirs and treatment works which will improve water quality and protect supplies.

Strategic Report (continued)

Sewage flooding minimised

Sewer flooding is rare but when it does occur it can be devastating so tackling it remains a key objective. We have introduced a new measure which expands the flood register to include internal and external flooding and lowers the likelihood of it happening.

This year we have invested £8m to reduce the risk of flooding at 91 properties or locations. Due to a third party delay one of our projects will finish early in 2016/17, so while we narrowly missed the target for the year, we remain on track to achieve the target in future years.

With regard to internal flooding due to blockages in public sewers, the position for the year is better than our performance commitment at 1.36 incidents per 10,000 properties. This is the result of continued operational improvements and the generally benign weather conditions in the region last winter.

The responsibility for flooding is often complex and we work with local authorities as they produce surface water management plans and strategies to review flood management. There has been a significant change in the number and frequency of liaison meetings and, together with the planning authorities responsible for approving sustainable solutions, we are being consulted more than before. We have contributed towards three partnership schemes to reduce flooding in Somerset at Cannington, Brent Knoll and Wrington.

We are preparing to receive the transfer of private pumping stations to us in October 2016, undertaking sample surveys of these assets and looking to adopt some early where they are causing problems. The latest assessment is that almost 400 pumping stations will be transferred.

Resilient services

Our asset management framework continues to help us develop a more integrated approach to risk and investment decision making. We are certified to the international standard for asset management, ISO55001:2014.

We began work on our major integrated supply grid project in 2010 and it is due to be completed in 2018. Delivery of the project continues and continues to make excellent progress and once complete, will enable us to:

- reduce abstractions from sensitive groundwater sources as agreed with the Environment Agency
- move water more effectively around our region
- ensure future demand is met
- improve the resilience of supplies to customers.

Key sections of the project commissioned and put into service during 2015-16 include:

- new storage tanks at Summerslade (near Warminster) and Littledown (Shaftesbury) and the pumping station at Monkton Deverill (near Warminster), together with all the interconnecting pipelines
- Sturminster Marshall (east Dorset) pumping station and the new storage tank at Snowsdown (Blandford) and the pipelines between the sites.

Together with other related schemes this work has enabled us to meet our commitment to reduce the number of properties supplied by a single source by 28,000.

Mechanical and electrical installation is well under way at Codford and substantial progress has been made on the schemes around Salisbury and in Dorset.

The overarching control system for the grid, called the Optimiser, has been successfully proved on sections of the project that went live this year. The project is on track for completion in 2018.

Good progress has been made with our infiltration reduction plans to reduce the risk of groundwater entering public and private sewers and drains. We inspected more than 107 km of sewers and permanently sealed 4.2 km of them in 2015-16.

Customer service

This was the first year of the new look service incentive mechanism and, once again, we topped the water and sewerage companies' league table for satisfaction surveys.

Complaints also fell again this year, by 19%, and in September the Consumer Council for Water confirmed that we continue to have the lowest number of complaints in the water industry.

We give customers the opportunity to feed-back on our service using whatever communication channel they choose and encourage them to identify staff who have 'gone the extra mile'. Under the guidance of our customer experience group we use this feedback for continuous improvement of policies, processes and training.

Strategic Report (continued)

The feedback shows that 96% of our customers rate our service as very good or good. This is slightly below the long-term average and we continue to work hard to improve the services received by our customers. Both value for money and customer effort scores have improved with 78% of customers rating our service as very good or good value for money and 81% saying it takes little or no effort to resolve their query.

It's important that we continue to evolve and improve our service offering so day to day we are widening our use of alternative communication channels while remaining committed to offering personal telephone answering and, most importantly, choice for our customers. We are seeing a growing number opting for self-service, text messaging and Live Chat and are providing more opportunities for them to send us information using media such as photographs.

Keeping customers informed when we have problems on our network, such as a burst water main, or when we are fixing a problem at their own home or premises, remains one of our key challenges.

Proactive phone calls or text messages from our dedicated customer care team have proved an effective way to let customers know what the problem is, what we're doing to resolve it and by when, and they are helping to drive our satisfaction levels up. The team oversees the whole customer journey and keeps it on track.

This year we re-launched both our Wessex Water Promise and our household leakage policy following feedback from our online customer panel, Have your say. Both are now closer to customers' expectations and easier to understand.

We've also redesigned both our bills and the information we provide with our bills, removing unnecessary duplication and making them easier to follow, because it's essential that customers understand what they are paying for.

Our customer relations staff have been through a new training programme, called Conversation on a page, designed to make our replies to queries and complaints simpler, easier to understand, more personalised and overall more engaging.

We retained our government Customer Service Excellence award for our approach to customer service and have the best overall package of customer guarantees in the industry. We continue to hold the best practice mark of distinction from the Keep me Posted campaign.

Customer engagement

We engage extensively with our customers and stakeholders, both in our day to day business and for specific programmes of work, such as preparation of our five-yearly business plan.

For the business plan covering the five years from April 2015 to March 2020, we consulted more than 24,000 customers and 90 other stakeholders. At the centre of this was the customer scrutiny group which brought together a range of stakeholders to scrutinise our business plan proposals and ensure they truly reflected customers' aspirations for service improvements and ability to pay.

In the last year we have established a new format for our stakeholder liaison for the next five years and in preparation for the 2020-2025 business plan.

The Wessex Water Partnership, independently chaired by Dan Rogerson who was previously Water Minister under the coalition government, is the successor body to the customer scrutiny group.

It held its inaugural meeting in January 2016 and will meet three to four times each year. It will be supported by our new, independently chaired, catchment and futures panels.

We have already developed an engagement strategy for the next business plan – called Your Say, Your Future. We intend to maximise the use of our everyday or continuous engagement with customers, and to carry out specific research projects at key points in the business plan timetable. For instance, developing and testing acceptability of our 25-year vision, currently under way, and our five-year business plan.

We continue to use our Have your say panel to improve our service offering and this year sought its views on:

- the way we communicate with customers if they have a billing query
- our wider information provision and communication channels
- our new home water and energy check service.

We follow up each survey with a newsletter to participants explaining the findings and what we are doing as a result.

Strategic Report (continued)

Customers in vulnerable circumstances

In February this year Ofwat published its vulnerability focus report and practitioners pack for water companies. We featured heavily in the report for offering best practice in this area.

Anyone can find themselves vulnerable at any time due to, illness, unemployment or simply a change in circumstances like a bereavement or divorce. Because our customers are our priority, we are committed to providing help when and where it's most needed.

We pride ourselves on treating customers as individuals and tailoring our customer care and customer service to their needs, making sure we are inclusive and accessible to all. This commitment is demonstrated in our retention of the British Standard for Inclusive Services Provisions (BS 18477) and the Louder than Words charter mark.

We have made sure staff have the right skills, confidence and awareness to deal with often quite complex situations and strengthened this with specialist training, such as GEM and mental health awareness, so they can offer appropriate support to customers they talk to or meet in their work.

We hold registers of customers with longer term disabilities or additional needs and, as they are likely to need the same support from their energy provider, we are doing all we can to signpost customers to other utilities.

Through our assistance programme, **tap**, we continue to support those who are financially vulnerable. We are now helping more than 21,000 customers to pay ongoing charges and repay debt, while offering practical help to reduce water and energy bills.

Around 10,000 customers are in receipt of our main social tariff, Assist, which offers discounts of up to 90% off water charges for those in the greatest financial hardship.

And we're not standing still – this year, under the guidance of our expert affordability advisory group, we've introduced a discount of around 20% for pensioners on the lowest incomes who will often suffer hardship in silence instead of asking for help.

Our partnerships with the debt advice community continue to thrive and we remain strongly of the view that holistic advice is vital to help customers to get back on track and into sustainable payment. It's never just about water debt.

Our affordability action plan has been in place since autumn 2013 and we continue to see an increase in the take-up of our schemes and low rate tariffs. The numbers have increased by 19% over this year.

We are liaising with a growing number of community based organisations outside the debt advice arena to help us engage with customers who are traditionally much harder to reach and likely to be some of the most vulnerable.

Using geographical mapping of deprivation levels and social tariff penetration we've been able to better target our promotional work on areas of most need.

We have also launched two new projects, one with the Department for Work and Pensions and the other with Wiltshire Council. In both cases the organisations will be contacting customers on means tested benefits on our behalf to promote our **tap** programme.

We continue to support financial capability and money management projects in our communities, funding a further four this year through our Money Matters awards. The four projects involve offenders due to leave prison, the over 60s, secondary school children and under 30s, including young families and those with mental health issues.

Preparing for retail market opening

From April 2017 all non-household customers will be able to choose their retailer for water services.

This is a new challenge for the sector and a new opportunity for us, and we need to be ready to operate effectively and compliantly in this new market.

We are in a good starting place with our retail unit costs among the lowest in the industry and our levels of service among the highest, achieved in large part through Water2Business, our joint venture with Bristol Water. We have made good progress and are on course to operate in the shadow market that is due to begin in October 2016.

Water2Business's preparations are focused on ensuring that we meet customers' retail service needs in and out of our existing area of supply so that we can maximise the opportunities to grow our business.

Strategic Report (continued)

Our wholesale readiness programme is being delivered emphasising that we expect to fully comply with our market obligations through the provision of excellent services to both water consumers and to retailers.

Education and water saving

We help customers of all ages to conserve water and prevent blockages in sewers.

Over the last year we have taken our Be Smart love your loo campaign to shows and festivals across our region, including Bristol Harbour Festival.

And our Be Smart save water campaign went to the Royal Bath and West Show at Shepton Mallet and Yeovilton Air Day.

We included information in our bi-annual customer magazine and a range of other leaflets about free water saving devices from our online shop and tips for saving water in the home and garden.

Our three education advisers continued their comprehensive coverage of Bristol, Bath, Somerset, Wiltshire, South Gloucestershire and Dorset.

This year they visited schools, teaching topics ranging from the water cycle to what happens to waste once it has been flushed down the toilet, to students of all ages and community groups.

And they welcomed students to the eight education centres across our region.

During the last year almost 29,500 students benefited from school visits and trips to water and sewage treatment works.

The education advisers also complement our apprenticeship programmes through their interaction and engagement with schools, supporting our mission to highlight career choices. This year we introduced a new initiative with schools to provide a water efficiency audit and help them reduce any waste that was identified. This has saved 80,000 litres of water a day.

Watermark awards

Our Watermark awards continue to support organisations across our region with their environmental projects.

Organisations receiving an award over the last year include the Greater Bedminster Front Garden awards in Bristol.

We provided a grant so organisers can promote sustainable gardening by sharing ways to save water and to use drought tolerant plants.

Environment

We aim to provide high quality, sustainable water and environmental services, while protecting and improving the environment.

Improved bathing waters

Prior to the revised Bathing Water Directive taking effect in 2015, we had identified Burnham Jetty as the only bathing water within our region that would fail to meet the 'satisfactory' standard due to the directive's change of classification and tightening of standards.

The failure at Burnham Jetty as a result of this tightening, rather than any underlying deterioration in water quality, is why our performance commitment for beaches passing EU bathing standards is reported as 98% against our target of 100%.

Outputs from the National Environmental Programme, which we completed during the year thereby achieving 100% performance against target to deliver agreed schemes, include:

- screening an overflow at East Quay in Bridgwater
- installation of 77 event duration monitors
- building an ultraviolet disinfection plant to treat overflows from our storm tanks at Highbridge.

We are active participants in a multi-agency group comprising the Environment Agency, local authority, internal drainage board, catchment sensitive farming team and others to ensure all parties are co-ordinated to deliver water quality improvements.

Strategic Report (continued)

We are supporting a coastal engagement officer who is working with communities in Burnham to raise awareness of water quality and increase ownership of their beach. This includes campaigns on sewer misuse, dog fouling and beach litter.

Rivers, lakes and estuaries protected

Our programme for this asset management plan period (AMP6) includes the reduction of phosphorus concentration in discharges at 47 sewage treatment works.

During the year our in-house engineering team completed outline design on the first group of these schemes – a standardised, modular approach will be adopted, wherever practicable, to ensure procurement and construction is as efficient as possible.

We have been working with the Environment Agency to develop a catchment wide permitting system for phosphorus at our sewage treatment works in the Bristol Avon river catchment. This is an innovative form of permitting which, by assessing the performance of a group of sewage treatment works as a whole, enables a different approach to risk, and delivers greater environmental improvement at a lower overall cost.

During the year we agreed the form of this permit and associated regulatory position statements with the Environment Agency. Work has started on monitoring the 64 sewage treatment works involved.

The agency's National Environment Programme also includes a series of phosphorus technology trials designed to test the performance of new processes to meet future, more stringent concentrations required by the EU Water Framework Directive.

We have completed construction and commissioning of four full-scale trials, including a magnetite assisted settlement process (BioMag), absorptive media (steel slag reed beds) and stretching existing chemical dosing performance on tertiary sand filters and activated sludge plants.

Under this programme we are working with the University of Bath to develop a high-rate algal pond for the removal of phosphorus from sewage effluent.

In addition, design work has begun on eight sewage treatment works which require improved ammonia removal.

Water resources

During 2015-16 the weather was relatively average overall, with 106% of average rainfall across the region. However, there was a distinct seasonal pattern with above average rainfall between January and March and drier than average conditions in the spring and autumn. As a result, groundwater levels were lower than average for most of the year.

This rainfall pattern was also reflected in river flows, with the timing for the start of stream support and flow-led licence restrictions coming earlier in the year than is typical and lasting late into the autumn.

Reservoir storage remained high throughout the year with storage, excluding Wimbleball reservoir, hitting 67% at its lowest point, similar to 2014-15.

A number of minor licence changes came into effect on 1 April 2015; more significant changes will be applied from 1 April 2018 in Warminster and Salisbury zones, and our water supply grid project is on track to assist with meeting demands in these areas.

The implementation of our performance measure to limit abstractions at our Mere source has already seen significant reductions in output. The site has only been used as a backup when other sites have been unavailable and where it would be non-cost beneficial to go to another supply. For the year we used 172MI against a target of 100MI. We anticipate this performance improving later in the AMP once the supply grid is commissioned.

Catchment services

Catchment services have continued in 15 high groundwater catchments and five surface reservoirs to tackle pesticide and nutrient issues. The task is to improve raw water quality without having to install additional treatment.

Our experience is that farmers remain willing to engage with our advisers in the majority of cases and the advisers' reputation within the wider agricultural community remains very high. We are currently working with 51 different farmers covering a total of approximately 40,000 hectares.

Nitrate concentrations rose last winter and, at our highest risk sites, Deans Farm and Fonthill Bishop, blending was needed to maintain compliance. However, nitrate concentrations were not as high as previous winters and improvements in nitrate trends at many sites have continued.

Strategic Report (continued)

There were no pesticide failures at any of our high risk reservoirs and catchment work continues to secure and maintain these improvements. Our work to control pesticides, metaldehyde in particular, remains industry leading. The voluntary 'no use' approach that we have championed appears to be the only way to successfully avoid metaldehyde reaching rivers and reservoirs.

Catchment management in the Poole Harbour catchment, with the aim of offsetting the need for nitrogen removal at Dorchester sewage treatment works, has successfully reduced nitrogen across the target area by approximately 20 tonnes against a 2020 target of 40 tonnes.

A new trading platform, EnTrade, will be trialled later in 2016 as an innovative alternative to directly approaching farmers for the funding of cover crops to manage soil quality and fertiliser calibrations.

This is intended to provide an online, reverse auction platform that farmers can bid into for growing cover crops this coming winter. Once the 'proof of concept' trials are complete, we intend to roll this out to a wider set of parameters and issues.

Environmental investigations

We believe investment should be based on sound scientific evidence; by gathering data through investigations we can better understand our impacts and trial solutions.

In AMP6, we will be delivering 40 environmental investigations covering a range of issues including:

- the occurrence and removal of hazardous and emerging substances from sewage effluent
- trialling new, sustainable treatment solutions for phosphorus removal
- understanding the ecological impact of our reservoirs and abstractions
- understanding the impact of our sewage treatment works on the nutrient levels within rivers, compared to other sources, at a catchment scale.

We have started our investigation programme for AMP6 and are including a number of leading edge projects, some of which are industry firsts. These projects will support our proposals for AMP7 to deliver the most cost effective and sustainable solutions for our customers with the best environmental results.

Wildlife and conservation

We have surveyed our key conservation sites extensively over the last five years, making changes to their management for biodiversity. So far, most of our holdings above 10 hectares have been surveyed, amounting to just over 60% of our land area, achieving our performance commitment for the year.

Our management of nearly 300 hectares of land designated as a SSSI ensured that the condition of these vital habitats exceeded government targets; 99.5% of our SSSIs were assessed as being in favourable or unfavourable but recovering status. In 2015, we appointed a part-time conservation, access and recreation (CAR) officer to help improve these elements of our landholding for the public. The role is to oversee and co-ordinate CAR projects at some of our largest and most visited sites, and those of greatest importance for wildlife and heritage.

To date this has included:

- an assessment and improvement plan for the children's play area at Sutton Bingham
- investigating alternative public rights of way at Tucking Mill reservoir
- improvements to the bird hide at Bleadon Levels nature reserve
- evaluating a number of further projects for delivery over the next four years.

We will continue to support wildlife projects funded by our Biodiversity Action Plan Partners Programme up to £80,000 per year and will be supporting the following projects between 2015 and 2020:

- South Wiltshire Farmland Bird project – Cranborne Chase AONB
- Dorset Wild Rivers – Dorset Wildlife Trust
- Wessex Chalk Streams project – Wiltshire Wildlife Trust
- restoring coastal and floodplain grazing marsh in the North Somerset Levels – AvonWildlife Trust.

Reduced carbon footprint

As one of our performance commitments our net greenhouse gas emissions fell to 138 kilotonnes carbon dioxide equivalent in 2015-16 – our lowest since 1999-2000 but still higher than our target of 133. Our emissions are highly sensitive to the carbon intensity of grid electricity; if the carbon intensity had remained at the level forecast in the business plan, our emissions would be better than the target for the year. This reflects the combined effect of the work set out below and the lower carbon dioxide intensity of UK grid electricity compared with 2014-15.

Strategic Report (continued)

One of our long-term sustainability goals is to be carbon neutral in our operations. To do this we need to avoid energy use where possible, improve efficiency and increase renewable energy generation.

While electricity use increased between 1990 and 2010, mainly due to tighter sewage treatment standards, we have now halted this trend, largely through concerted energy efficiency work. This is supported by detailed consumption information, analysed through our energy data hub, that reveals sites using too much electricity and in turn helps focus corrective measures.

This year we trialled Open Energi's dynamic demand system at Ham sewage treatment works; this involves instantaneous, temporary adjustment of the site's energy use to maintain a balance on the local electricity grid. Water management measures such as leakage reductions and catchment management also help avoid unnecessary energy use.

During 2015-16 we completed the installation of advanced anaerobic digestion and associated electricity generation at Trowbridge sewage treatment works. This facility is expected to generate just under seven gigawatt hours of renewable electricity per annum.

Meanwhile, we have installed a 250 kilowatt solar photovoltaic array on the roof of our Bath operations centre which is forecast to supply around 12% of the building's annual electricity demand. Overall we achieved the target of 21% of our energy provided by self-generation.

Our operating division GENeco was a category winner in several awards during the year for schemes such as food waste digestion, gas to grid and the Bio-bus.

These included the Guardian Sustainable Business awards, the UK AD and Biogas Industry awards, the National Recycling awards, the Energy awards, the Low Carbon Vehicle Champion awards, the National Sustainable City awards, the CIWM awards, and the South West Built Environment awards.

Reducing demand for water

In 2015-16 we narrowly missed our performance commitment daily consumption of water per person per day. Consumption was maintained at 138 l/p/day (same as 2014-15) against a target for this year of 135. We attributed being higher than target this year to better than average summer weather, falling water and other utility prices and a return to growth in real incomes.

Ofwat recognises the potential impact of these external factors and actual performance is well within the range that Ofwat have allowed for this. We will continue with our initiatives to promote water efficiency with customers where this year we have exceeded the performance commitment target agreed with Ofwat.

Innovation

It is essential that we are able to adopt new ways of working and technologies that help improve the services we provide, reduce costs and manage risk.

Environmental investigations are carried out to ensure that future capital investment is well-focused. Some of the investigations employ innovative methods and examples from 2015-16 include the following:

- using a biological tracer to establish whether final effluent from Wick St Lawrence sewage treatment works can be found at Sand Bay and Clevedon bathing waters in Somerset
- installing an observation borehole at Compton Durville, Somerset, with vibrating wire piezometers to obtain better detail about groundwater flows
- using magnetite (inert iron oxide) at Bowerhill, Wiltshire, to improve settlement and increase phosphorus removal
- with the University of Bath, trialling high-rate algal ponds at Beckington near Frome – also for phosphorus removal
- controlled release of spate flows downstream of Durleigh, Somerset, reservoir to remobilise phytoplankton that were having an adverse ecological effect in the stream
- monitoring the success of catchment permitting in the Bristol Avon.

Our Eureka! programme rewards staff who have designed projects that save money, improve service to customers, reduce risk and improve our working methods in general.

The most successful ideas in 2015-16 included:

- a central database which documents faults or symptoms and gives possible solutions
- insulation of chemical storage tanks to maintain the life of the chemicals and reduce the run-time of pumps
- installation of variable speed drives for blowers at a sewage treatment works
- a novel reworking of a spindle on a valve to improve the ease and safety of maintenance.

Strategic Report (continued)

We also carry out trials of new products and technology developed by other companies and in the last year these have included:

- waxed hibernation epoxy resin liners which can be used in larger diameter sewers
- manhole sealing in Minehead with polymer modified grouts to prevent saltwater infiltration into sewers
- use of ultrasound to prevent the growth of cyanobacteria in Luxhay reservoir in Somerset
- on-site calibration of water pressure gauges and monitors, reducing the journeys previously involved in bringing them to a single location for recalibration.

Our joint research programme with the University of Bath continued during 2015-16. The main themes are low energy nutrient recovery from sewage; methods for increasing biogas from sewage sludge digesters; emerging pollutants in waste water; and improved techniques for understanding and comparing the whole life costs of water management.

The university's Water Innovation Research Centre, formed in 2014-15 with our assistance, appointed a director and a lecturer in water science and engineering.

And we continue to host one-year industrial placement students from the university who have assisted with energy management, drinking water compliance monitoring and assessment of techniques to lower phosphorus levels in sewage effluent.

Employees

We seek to provide opportunities for our employees to develop, both personally and professionally, equipping them with the skills and expertise they need to be successful in everything they do. In return, they provide an outstanding level of service and performance to our customers, the company and to each other.

This year we have focused heavily on developing our apprenticeship programmes to provide young people with career and skill development opportunities and to build a strong and skilled workforce for the future. Appointing apprentices and expanding our programmes ensure that talent is retained, and secures our stability.

This year there has been a significant expansion in our apprenticeship programmes. There are currently 41 apprenticeship vacancies and we will shortly recruit our 100th modern apprentice. Eleven apprentices have graduated from training and secured permanent positions within the business.

New apprenticeship schemes have been created in finance, information services and property searches, with a water systems apprentice on a brand new training programme. These apprentices complement existing ones in engineering and construction, our laboratory, customer service and operations. We also launched our first ever higher level apprenticeship in engineering and construction.

Promoting diversity and inclusion in our workplace has been a key focus again this year. We recognise that differences in personal characteristics bring richness to our work environment and believe that attracting, developing and retaining employees who reflect the diversity of our customers is essential to our continued success.

We have put in place a range of diversity initiatives including those focused around flexible working, flexible retirement and job share contracts. We have joined the business disability forum to continue our focus on providing all our employees, including those with disabilities, with career development opportunities.

Protecting the health, safety and welfare of our staff, contractors and customers remains the highest priority.

Training

We pride ourselves on the standard and level of learning and development opportunities provided to staff to ensure they have the skills they need to perform their jobs to the highest standards. We promote and encourage progression and ensure that all those looking to build a career with us have the opportunity to do so at a level and pace that suits both them and the Company.

Current and future management and leadership continues to be a priority and along with our accredited level five and level seven management and leadership programmes, we ran a range of management development schemes aimed at supporting our leaders from new manager to senior management level.

We have again held two-day development centres for nominated high potential employees, providing them with routes to further their career development. On average we delivered a ratio of 2.5 days' training for each member of staff per year. The majority of our training schemes are health and safety, technical and craft programmes ensuring our people are highly skilled and competent, keeping themselves, their colleagues and our customers safe at all times.

Strategic Report (continued)

Apprentices

Developing a long-term apprenticeship strategy to secure quality apprenticeship training is fundamental to our recruitment and development processes.

In March 2016, to coincide with National Apprenticeship Week, we held our successful inaugural apprenticeship open day. It was our biggest ever apprenticeship drive. More than 120 potential apprentices visited our operations centre accompanied by guests and parents. Feedback from young people, parents and staff was overwhelmingly positive.

"I just wanted to email you to say you were brilliant on Saturday, my children were very impressed and my 12-year-old daughter now wants to be a civil engineer!! The day did exactly what I wanted it to do for them, which was to open their minds up to all the possibilities that are out there."

Complementing our apprenticeship programmes is our education team. Interacting and engaging with schools supports our mission to highlight career choices and encourage non-traditional employment routes.

We work closely with our leading apprenticeship providers to support local women into engineering and construction campaigns, and ensure our vacancies are promoted to all types of young people across our entire region.

We continue to develop new apprenticeship programmes with the objective of providing young people with career and skill development opportunities and building a strong and skilled workforce for the future. Appointing apprentices and expanding our programmes ensures that talent is retained and secures business stability.

We continue to support staff to complete professional development through a range of accredited professional development bodies relevant to our industry. We currently have 30 employees undertaking study to achieve professional qualifications.

Diversity

We value the differences that a diverse workforce brings and are committed to creating an inclusive workplace for all employees and others who work with the Company as suppliers, contractors, consultants or customers.

Promoting diversity and inclusion has been a key focus again this year. We have implemented a range of diversity initiatives including the promotion of flexible working policies, the introduction of job-share contracts and flexible retirement for those wishing to ease their way into it.

We have developed and piloted a new aspiring leaders' development programme aimed at building confidence in potential leaders of the future. This year, we became a member of the Business Disability Forum and we continue to progress issues for our employees with disabilities.

Diversity scorecard

At March 2016 there were 2,144 employees, of whom 447 were women and 1,667 were men. There were 11 directors, of whom eight were men and three were women, and 40 senior managers of whom eight were women and 32 were men.

Culture

We have a strong, friendly and positive culture and staff enjoy working for the company and with each other. We held a staff survey this year and our employees are highly engaged, with 83% rating Wessex Water a good place to work.

We have launched a new employee appraisal scheme which measures both the performance outcomes that have been achieved and the behaviours that have been demonstrated. Behaviours are assessed against our BEST values of behaviours, excellence, service and teamwork in the way we work and behave with each other, our customers and all our stakeholders.

Health and safety

The potential hazards faced by our industry require the highest standards of health and safety and we are committed to protecting our staff and everyone affected by our operations.

As a responsible employer it is clear to us that the management of health and safety is critical to our success, particularly as we seek to adopt even better ways of delivering services to our customers.

No activity can be totally without risk and we must ensure that our operations are carried out in such a manner as to remove unnecessary risk, and control and manage any residual risk to prevent injury or harm. Where risk cannot be managed and safety assured then work must stop until a safe solution can be found.

Strategic Report (continued)

Protecting the health, safety and welfare of our staff, contractors and customers remains an established and shared responsibility that is essential to our reputation as a leading and trusted employer.

We continue to develop and embed a strong health, safety and welfare culture in our day to day operations that targets zero accidents and supports our aim to be a great place to work in which all employees can work safely and reach their full potential.

We monitor all accidents and incidents reported by employees and, in particular, attention is paid to:

- the annual numbers of total and reportable incidents
- the areas of the company from which these arise
- the proportion of these that fall under each RIDDOR (Reporting of Injuries, Diseases and Dangerous Occurrences Regulations) accident category
- days lost as a result of reportable incidents.

This information is used to evaluate where resources should be allocated to effectively address any problem areas.

Position for the 12 months to 31 December 2015:

- 461 incidents reported
- no fatalities or life changing (permanently disabling) injuries
- no reportable diseases or dangerous occurrences
- seven incidents were notifiable to the Health and Safety Executive
 - five in operations (one specified and four over seven-day injuries)
 - two in engineering and construction (two over seven-day injuries).
- 381 working days lost through notifiable incidents
- two notifiable incidents involving contractors working for us
- no enforcement action from the Health and Safety Executive.

Health and safety awards

Operations were awarded the British Safety Council International Safety award with distinction at the 2016 awards for performance during 2015. Our submission scored 59/60 and it is the sixth year that we've been recognised by the council for demonstrating our commitment to preventing workplace injuries and ill health.

The top submissions in each sector are shortlisted for sector awards and we have again been shortlisted for the power and utilities sector award, one we have won for the last two years.

Engineering and construction have been entering the Royal Society for the Protection of Accidents (RoSPA) annual occupational health and safety awards since 2008 and hold a series of gold and silver awards. In the 2015 awards we were commended in the construction and engineering industry sector awards.

Entrants must be able to demonstrate a robust and high quality safety management system together with a minimum of four years' consistently excellent or continuously improving health and safety performance.

RoSPA recognised our commitment to accident and ill health prevention through Make It Right, endorsing our campaign to promote health, safety and wellbeing as an integral part of our safety culture.

Finance

The UK group ownership structure has remained the same since 2002 with the Company wholly owned by Wessex Water Limited which in turn is wholly owned by YTL Utilities (UK) Limited. Neither of these entities provide any intra-group funding to the Company with virtually all of the debt raised for the UK group sitting within the Company and all borrowings at market rates provided by financial third parties.

Gearing, as measured by net debt to RCV, stood at 66% at March 2016. On a pensions-adjusted basis this figure rises to slightly over 70% which the Board still finds an acceptable level. During the year the Board has continued to pay particular attention to the projected level of the Company's gearing ratio with a view, when declaring dividends, to protect the Company's existing credit ratings.

The next actuarial valuation of the Company's pension scheme is on 30 September 2016. At each triennial valuation the Company agrees with the scheme's trustees a payment recovery plan in respect of any deficit. The Company is committed to honouring any special contribution obligations that it signs up to.

The Company continues to have a healthy liquidity position comprising cash and cash equivalents held on the balance sheet along with undrawn bank facilities giving the Company instant access to funding if needed.

Strategic Report (continued)

Taxation strategy

The Company adopts a prudent approach to its tax affairs, but claims the tax relief to which it is entitled. An independent expert is used to ensure that the correct capital allowances are claimed. The current year corporation tax charge of £27.7m is 17.6% of the profit before tax figure of £157.1m. This is less than the 20% effective tax rate because of the capital allowances the Company is allowed to claim.

The Company does not engage in complicated tax schemes, because it does not believe it is the right thing to do, and because it could endanger its relationship with HMRC. The Company avoids structuring transactions for tax purposes that would give a tax result inconsistent with the underlying economic result.

The Company promotes an open and transparent relationship with HMRC, engaging in an early dialogue with them where there is any uncertainty as to the correct tax treatment of any significant transaction. It thereby ensures that issues are resolved before tax returns are filed, where possible.

HMRC are kept informed as to the structure of the business and in the last year the Company's low risk status with HMRC has been renewed for a further three years.

Financial performance

The first year of the AMP6 price review period saw a reduction in the profitability of the Company, with operating profit falling by £14.8m from £245.4m to £230.6m. The reduction in turnover was £14.7m, with only a £0.1m increase in operating costs.

Turnover

Turnover decreased by £14.7m or 2.7% from £536.5m to £521.8m.

The price reduction imposed by Ofwat at 1 April 2015 was 5.9% offset by November 2014 RPI of 2.05%, a net decrease of 3.85%. At 1 April 2016 there was a price increase agreed by Ofwat of 0.8% increased by November 2015 RPI of 1.1%, a total increase of 1.9%.

The turnover reduction was broadly in line with the weighted average of the two price changes, turnover also being impacted by improving economic conditions in the region which helped generate some growth and the negative impact of customers switching to meters.

Operating costs

Operating costs (excluding depreciation, amortisation and disposal of assets) decreased by £1.5m from £190.8m to £189.3m as savings exceed the general level of inflation. Compared to the previous year there were savings from staff costs, EA charges, bad debts, share option charges and non-tariff basket activities (matched by decreased turnover).

Capital investment

In the year to 31 March 2016 we delivered gross capital expenditure for the first year of the AMP6 programme of £200.8m, which is £2.4m higher than the £198.4m delivered in the previous year.

With the combination of the on-going overlap water supply grid programme, which started in AMP5 and focused early start investment in 2014-15 to mobilise for project delivery in 2015-16, we have achieved a stable transition between the AMPs. Because we deliver a large portion of our investment with our own staff, it is both important to us and our supply chain that we provide this continuity of work.

We have delivered all the regulatory outputs for the year and are well placed to deliver the programme in future.

We have also initiated major technology and business change programmes in preparation for non-household retail market opening, customer excellence and digital transformation.

Our risk-based totex investment planning has resulted in appropriate and timely delivery focusing on those areas that are important to our customers and in particular delivering improvements against our outcomes, such as sewer flooding, river improvements and interruptions to supply.

We are investing more than ever in innovative approaches to solving problems and this will help us continue to improve services throughout the AMP period.

Depreciation and amortisation

Depreciation costs increased by £1.6m, from £100.3m to £101.9m. Under IFRS the infrastructure maintenance charge has been replaced by an IFRS repairs charge and depreciation of underground assets.

Strategic Report (continued)

Interest charges

Interest charges decreased from £76.9m last year to £73.5m this year. The £3.4m decrease was split between an interest payable reduction of £3.3m and a £0.4m increase in interest receivable, reduced by a £0.3m increase in pension related costs.

The £3.4m decrease in base interest costs predominantly arose because of the impact of the fall in the cost of debt from 4.0% to 3.6% in respect of floating rate and index linked borrowings. This was greater than the additional interest on the increase in net debt during the year from £1,862.1m to £1,880.8m.

There is a prudent mix of debt between fixed rate, index linked and floating rate instruments. At the year end the debt split was 48% fixed, 36% index linked and 16% floating, with the index linked debt based on either November or March RPI. The maturity of debt is generally long term with £1,675.0m of debt maturing after 2020.

Taxation charge

The corporation tax charge was £24.6m, an increase of £10.1m over £14.5m last year.

The principal reason for the increase was that last year there was a £14.0m tax credit on first time adoption of IFRS. The credit related to items of infrastructure income taxed in previous years now recognised as profit and taxed in future years under IFRS.

The normal corporation tax rate reduced from 20.75% last year to 20% this year.

The Company has a statutory year end of 30 June and the tax computation is prepared for the 12 months to 30 June each year. Corporation tax is paid quarterly.

Deferred tax has moved significantly from a charge of £18.7m last year to a credit of £34.0m this year, a movement of £52.7m. Both these years have been restated under IFRS which has no deferred tax discounting.

There is a deferred tax credit this year because the rate at which deferred tax is calculated has fallen from 20% at June 2015 to 18% at June 2016. This 2% reduction on the opening deferred tax liability is a credit of £38.1m.

There is a further £14.0m deferred tax reduction this year being the opposite of the corporation tax increase from last year's first time adoption of IFRS.

Dividends

Wessex Water's dividend policy is to declare dividends consistent with the Company's performance and prudent management of the economic risk of the business. The Board has agreed to ensure that gearing stays at or below 70% in order to maintain its current credit ratings and give the Company continued access to the capital markets.

Cashflow and gearing

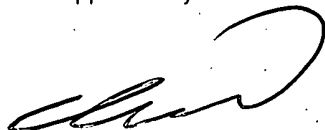
Net debt increased by £18.7m from £1,862.1m to £1,880.8m. This comprised:

- earnings before interest and depreciation of £332.5m, less
- cash outflow from capital investment of £168.3m, less
- interest and tax payments of £73.8m, less
- working capital and bond accrual outflow of £15.1m, less
- dividend payments of £94.0m.

Liquidity at year end was £262.0m comprising £112.0m of short-term bank deposits and £150.0m of facilities not yet drawn down.

The strategic report was approved by the Board of Directors on 9 September 2016 and signed on its behalf by:

Mark Watts
Director



Principal Risks

Despite the challenging economic conditions and growing impact of the changing physical climate we have maintained industry leading customer and environmental performance. This has been achieved through a focus on understanding the risks we face and using innovative approaches to mitigate risks and create opportunities to improve the services we provide.

The company's policy on risk identification and management is subject to annual review by the Board. The identification and management of risk is delivered through a tiered system of groups from operational staff, senior management, executive directors and the Wessex Water Services Limited Board. The Board reviews and holds ultimate responsibility for the risk process and for the identification and mitigation of risks.

Wherever possible, a risk is measured by its potential financial and service or environmental impact in the next five years, whether direct or indirect, including any possible impact on the price review process. A Risk Group meets twice a year and submits the current corporate risk register and summary report to a Risk Management Advisory Group made up of Executive Directors and senior managers.

The Risk Management Advisory Group scrutinises and challenges the risks included in the register and requires additional work where necessary to better classify the risk or explore other mitigation methods which may be available.

The Chief Executive submits an annual risk review paper to the Board for its review and agreement. This paper details the risk review process, identifies the current principal risks to the business and the mitigation measures in place. It also records the status of emergent risks that have been identified and provides details to the Board of any changes in the National Risk Register (NRR) and the National Resilience Planning Assumptions (NRPAs).

The Board agreed the addition of one principal risk relating to the industry's preparedness for retail non-household market opening, and one change replacing leakage as a principal risk with a wider outcome delivery incentive failure risk which includes leakage. Risk scores have remained static as mitigation works have balanced out a general increasing trend of risk.

The 10 current principal risks agreed at the Board are:

1. Government/regulatory action. Changes to legislation or other regulatory action can adversely affect the way in which the business operates and its profitability. The national audit office and public accounts committee have reported negatively on the sector and tight public finances mean heightened risk of government action on utility taxation, including interest deductibility. Relationships with politicians and regulators are maintained so that the Company's views about the impact of any proposed legislative changes on the Company and its customers are heard.
2. Market opening industry preparedness. A new principal risk reflecting the potential impact if all parties across the industry are not prepared in time for full market opening in April 2017. While our preparations are well advanced there remains the risk that either other companies or Market Operator Services Ltd (MOSL) will not be able to deliver to the very tight programme. This could result in additional cost and general reputational damage across the sector.
3. Major pollution incident. Control of the escape of polluting matter to the environment is central to the Company's business. Recent fines in the industry are now exceeding £1m per incident. Significant effort is made to prevent such an incident occurring through staff adherence to Company processes and procedures. New staff are trained in these processes and procedures and their importance. Local emergency plans are in place to protect the local environment at key installations.
4. Inappropriate staff actions. Considerable damage could be done to the reputation of the Company by a rogue or radicalised employee or contractor. References are obtained for all new starters whether permanent or contract. DBS checks are undertaken for all new permanent and fixed-term staff and for agency staff working in sensitive areas of the business.
5. Health and safety incident. Serious injury or death of a staff member or third party could expose the Company to prosecution under health and safety legislation and the Corporate Manslaughter Act. Health and safety processes and procedures are implemented via staff training and regularly monitored to maintain compliance and protect people from harm. With delivery of a large portion of our investment programme through in-house teams, health and safety is of paramount importance. We do expect to see an increase in fines following the Sentencing Guidelines Council review, just as we experienced on environmental pollutions.

Principal Risks (continued)

6. Availability of new finance. The bond markets are used extensively to fund new investment. The current economic climate has shown the volatility of these markets. Careful management of the relationship with both the ratings agencies and lenders has ensured that, to date, finance has always been available at affordable rates. The relationship with bond markets and rating agencies will be maintained and the Board will continue to ensure that the Company operates within prudent financial parameters. This annual review includes our first published long-term viability statement which includes modelling the main financial risks, and the outcome provides additional confidence in our risk mitigation.
7. Unfit water. A major failure of process or contamination of the water supply is a key risk. Significant effort is made to prevent such an incident occurring through staff adherence to Company processes and procedures. New staff are trained in these processes and procedures and their importance. We have completed a major exercise in documenting and updating our methodology for drinking water safety plans in liaison with the Drinking Water Inspectorate. Risk assessments are now being formally reviewed at the monthly water risk meeting and issues escalated to the Risk Group.
8. Outcome delivery incentive failure. A new principal risk incorporating leakage. As part of the risk-based regulation Ofwat has introduced performance commitments for AMP6. Many of these measures are company specific but some are cross-company measures with stretch targets. As well as reputational risk there are also financial penalties and rewards that can be incurred which will apply in AMP7. This process is new and there are a number of new and trial measures which heighten the risk of financial and reputational impact on the business.
9. Digital security. The Security Service has identified the growing threat of cyber-attack or industrial espionage as a high risk to both businesses and utilities. This is particularly important for Wessex Water assets that are considered part of critical national infrastructure. The Company also holds and processes large quantities of data which are considered sensitive within the meaning of the Data Protection Act. Failure to process and protect the data in the prescribed manner is an offence. Additionally, the information Commissioner can take enforcement action which would require the Company to take prescribed actions for improvements in the future. An annual penetration test is carried out to test our security measures. A quarterly Information Security Forum maintains the focus on mitigating this risk.
10. IS business resilience. Most activities undertaken by the business are reliant on the availability of IT services and facilities and the Company continues to examine ways in which IT resilience can be maintained and, where appropriate, improved. In particular, the IS team have completed a technology enhancement programme enabling real time site to site data replication that will vastly improve the current system recovery times in the event of a disaster situation. The business has committed to Office 365 cloud-based solutions which provide more capacity and improved resilience.

Wessex Water Services Limited Board of Directors

Executive Directors

Colin Skellett – Chief Executive

A chartered chemist and engineer by training, he has worked in the water industry for more than 40 years, holding a number of positions in the management and control of both water supply and sewage treatment.

He joined Wessex Water in 1974 and was appointed its Chief Executive in 1988. Colin oversaw the move from the public to the private sector and the transformation of Wessex Water into a highly rated UK plc. Colin was awarded an OBE for services to business and WaterAid in the 2012 Queen's Birthday Honours and has an Honorary Doctorate in Engineering from the University of the West of England.

Mark Watts – Director of Finance

A qualified treasurer, Mark spent eight years in international banking before joining the treasury department of Wessex Water in 1991. He was appointed Treasury Manager in 1994 before becoming Treasurer in 1999.

Mark is highly experienced in raising finance, from both the capital markets and the banking sector, as well as having a long history in dealing with various corporate finance issues. He was appointed Finance Director and Treasurer on 16 March 2010.

Non-Executive Directors - Independent

David Barclay – Former Vice Chairman of Dresdner Kleinwort and Non-Executive Deputy Chairman of John Lewis plc. Senior Independent Director of Wates Group Limited. Deputy Chairman of the Board of the British Library. Appointed 1 November 2005. Senior Independent Director and Chairman of Audit Committee.

Gillian Camm – Appointed in November 2011 and Chair of the Wessex Corporate Responsibility Committee. Chair of the Board of Governors – University of the West of England, Deputy Lieutenant Gloucestershire, vice president Quartet Community Foundation, member Society of Merchant Venturers, became Chair of the Leadership Foundation for Higher Education in November 2015.

Huw Davies FCA – Appointed in September 2014 and Chair of Pensions Trustees. Former Chief Financial Officer and Company Secretary of the Wates Group. Independent non-executive director of Hydro-International PLC and J Murphy and Sons Ltd. Chairman of the children's communication charity I CAN.

Fiona Reynolds DBE – Appointed in August 2012 and chair of the Futures Panel. Other non-executive roles include the Senior Independent Director on the Executive Board of the BBC, Chair of the Green Alliance, Chair of the International National Trusts Organisation and Chair of the Cathedrals Fabric Commission for England. Director-General of the National Trust from 2001 to 2012. Master of Emmanuel College, Cambridge from September 2013.

Richard Keys - On 1st May 2016 Richard Keys was appointed as an Independent Non-Executive Director. Richard is a chartered accountant with 37 years' experience at Price PricewaterhouseCoopers LLP and was a partner there for 26 years holding a number of senior management positions, most recently that of global chief accountant. In the last six years he has taken on a number of non-executive roles and is also a director at Sainsbury's Bank plc, NATS Holdings Ltd and at the Department for International Development.

Non-Executive Directors - Shareholder

Francis Yeoh CBE – (Chairman) Managing Director of YTL Corporation Berhad, Malaysia since 1988. A founder member of the Malaysia Business Council, member of Malaysia's Capital Markets Advisory Council and Independent Non-Executive Director of The Hong Kong and Shanghai Banking Corporation Limited. Director since May 2002.

Hong Yeoh – Director of YTL Corporation Berhad, Malaysia since 1985, Executive Director of YTL Power International Berhad. Responsible for YTL Group's utilities and construction divisions. Director since May 2002. Chairman of Remuneration Committee.

Wessex Water Services Limited Board of Directors

(continued)

Non-Executive Directors – Shareholder (continued)

Mark Yeoh – Executive Director responsible for the YTL hotels and resorts division. Graduated from King's College, University of London with an LLB (Hons) and was subsequently called to the Bar at Gray's Inn, London in 1988. He joined the YTL Group in 1989 and serves on the Board of YTL Corporation Berhad, YTL Power International Berhad, YTL Land & Development Berhad, YTL Cement Berhad and Wessex Water Limited. Director since October 2003.

Hann Yeoh – Non-Executive Director of Wessex Water since August 2012. Executive Director of YTL Power Generation Sdn Bhd (wholly-owned subsidiary of YTL Power International Berhad) and part of the business development team of YTL Power International Berhad. He also sits on the Board of YTL Power Seraya Pte Limited in Singapore and is a graduate of Oxford University with a Master of Engineering in Engineering Science.

Kathleen Chew – Non-Executive Director of Wessex Water since April 2014. Group Legal Counsel to the YTL Corporation Group. She holds a LLB (Hons) degree from the University of Birmingham and was called to the Bar at Gray's Inn, London in 1982. She joined YTL Corporation Berhad in 1988 to set up its legal department after being in practice at the Malaysian Bar for five years. Prior to joining the YTL Group, she was a partner in the law firm of Abdul Aziz Ong and Co in Kuala Lumpur from May 1987 to January 1988.

Governance Report

Introduction

Wessex Water is committed to high standards of corporate governance. Under Condition F of its Instrument of Appointment as a water and sewerage undertaker (the "Licence") Wessex Water is required to conduct its water and sewerage business as if it were the Company's sole business as a public limited company. The Licence also requires Wessex Water to have particular regard to the UK Corporate Governance Code as approved for the purposes of the Listings Rules of the Financial Services Authority (the "Code"). The Code is not a rigid set of rules and provides general principles of best practice. The Code is made up of "Main Principles", "Supporting Principles" and "Code Provisions". The Code Provisions are subordinate to the Principles. Whilst the Code is generally regarded as embodying best practice in UK Corporate Governance, its main focus is the relationship between a listed company and its shareholders. Wessex Water has a single shareholder and, accordingly, it is able to address some issues more directly and completely than it could if it were a listed company.

Wessex Water's focus is on complying with the Principles and spirit of the Code in its particular context as a private limited company with a single shareholder. In practice, the Company complies with the Code Principles and Code Provisions with only very limited exceptions. In those few areas where we have decided not to follow the precise requirements of the Code we explain why, and how good governance is nevertheless achieved.

The following parts of this Governance Report explain how good governance is at the heart of the Company's business and underpins the Company's relationships with its customers, shareholder, and other stakeholders. The Board regards it as fundamental to the long-term success of the Company to provide excellent customer service and satisfaction. Governance arrangements are kept under constant review. We continue to reflect best practice and maintain our position as the leading water and sewerage company for customer service and satisfaction. We have set out our commitment to best practice in our Code of Practice for Corporate Governance a copy of which is available on our website.

We believe that our governance arrangements ensure that the Company continues to operate effectively and efficiently to the benefit of our customers, shareholder, and other stakeholders with clear accountability for decision making.

Governance Structures - The Board

The affairs of Wessex Water are ultimately the responsibility of the Board, which controls and directs the undertaking of the regulated water and sewerage business. During the reporting year the Board composition was as shown on pages 19 and 20.

The Board annually reviews and approves the Company's Organisation and Control Arrangements (O&CA) which set out the framework for control of the Company's affairs. The O&CA also specify requirements for the competency of members of the Board and its Committees, for effective management of the Company and for the granting of delegated powers and authorisations.

The principal duties of the Board, the matters reserved for its decision and the terms of reference of its Committees are fully documented and copies are available on our website. Matters reserved to the Board include strategy, charges, material changes to the Company's management and control structure, Board appointments, approval of material contracts, risk management, health and safety policies, disposal of material assets, approval of the annual operating budgets, employee pension arrangements, significant changes in accounting policies and defence and settlement of material litigation.

There are no matters specifically reserved to the shareholder. In practice the Board operates (and has operated continuously for more than a decade) without the requirement for shareholder resolutions. As part of its responsibility for the management of risk, the Board has determined criteria which control the extent of dividends paid and consequently the financial gearing of the Company. As with all Board decision making, these criteria were determined with the active involvement of the Independent Non-Executive Directors.

There are two Executive Directors, both appointed on one-year rolling contracts. During the year there were at least four Independent Non-Executive Directors, exceeding by one the requirements of Condition P of the Licence. Five further Non-Executive Directors are appointed by the Company's sole shareholder including the Chairman of the Board.

This balance on the Board ensures a high level of engagement and dialogue with the Company's customers and shareholder. In this way, Wessex Water complies with and exceeds the principles and spirit of the Code without the need for compliance with certain specific Code Provisions (including those in relation to the use of an annual general meeting to communicate with investors and encourage participation) which are not relevant to a company with a single shareholder.

Governance Report *(continued)*

The Non-Executive Directors scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. In addition, the Independent Non-Executive Directors, led by the Senior Independent Director, reviewed the performance of the Chairman. They also form or participate in the various Committees, assessing the integrity of financial information and whether financial controls and systems of risk management are robust and defensible, determining appropriate levels of remuneration for Executive Directors, assisting in appointing and, if necessary, removing Executive Directors, and assisting in succession planning.

The Board ensures that Directors (and in particular the Independent Non-Executive Directors) have access to independent professional advice at the Company's expense where they judge it necessary to discharge their responsibilities as Directors. The Board also ensures that the Committees are provided with sufficient resources to undertake their duties.

The Company arranges appropriate Directors' and Officers' insurance against the usual legal risks faced through holding office.

If Directors have concerns about the running of the Company or a proposed action which cannot be resolved, they are encouraged to ensure that their concerns are recorded in the Board minutes and the Independent Non-Executive Directors are encouraged, on resignation, to provide a written statement to the Chairman highlighting any such concerns.

Due to the Company having a single shareholder, the Code provisions in relation to Directors being subject to annual election by shareholders are of limited relevance and not applied.

Wessex Water complied with the Code's Main Principles and Supporting Principles as to the composition of the Board. Moreover, Wessex Water exceeded the requirements of the Code (designed for listed rather than privately held companies) by having no fewer than four Non-Executive Directors, during the reporting year who are directors or employees of the Malaysian holding company, thus enabling effective dialogue with the shareholder.

While the Board has a majority of Non-Executive Directors, it does not have a majority of Independent Non-Executive Directors as envisaged by the relevant Code Provision. The Ofwat Board Leadership, Transparency and Governance Principles are based on the Code, which applies to UK listed companies. The principal purpose of the Code is to ensure that the interests of a company's members are protected and represented at board level. The preface to the Code states that: "the function should be to help boards discharge their duties in the best interests of their companies." The preamble to the Ofwat Principles states that: "any departures from the Ofwat principles should be by exception in the spirit of corporate governance for listed companies." In the context of a privately held company with a 100 percent shareholder, we consider it to be in accordance with good corporate governance practice for there to be a significant number, if not a majority, of shareholder representatives on the Board. In Wessex Water's case, the shareholder appointed Non-Executive Directors (excluding the Chairman) are not a majority on the Board and are no greater than the number of Independent Non-Executive Directors. Further, Wessex Water has four highly capable and experienced Independent Non-Executive Directors.

The Board considers its current composition ensures an appropriate balance of skills, experience, independence and knowledge so that no single group can dominate decision taking and that the Board does not become too unwieldy.

The search for Board candidates is conducted, and appointments and re-appointments are made, on merit, against objective criteria, and with due regard to the benefits of diversity on the Board, including gender diversity. All directors receive induction training on joining the Board and regularly update and refresh their skills and knowledge.

The following were Directors during the year under review:

Executive Directors	Independent Non-Executive Directors	Shareholder Non-Executive Directors
Colin Skellett	David Barclay	Francis Yeoh CBE
Mark Watts	Gillian Camm	Hann Yeoh
	Huw Davies	Hong Yeoh
	Richard Keys – from 01/05/2016	Mark Yeoh
	Fiona Reynolds	Kathleen Chew

Governance Report *(continued)*

The following directors were appointed after the end of the financial year:

Andrew Pymmer – 01/08/2016

James Ryder – 01/08/2016

Chairman

Throughout the financial year under review Francis Yeoh was the Company's Chairman.

The Chairman leads the Board, ensuring its effectiveness while taking into account the interests of all stakeholders and promoting the highest standards of business ethics and governance. The Chairman is responsible for ensuring that Directors receive accurate, timely and clear information. The Chairman also promotes a culture of openness and debate by facilitating the effective contribution of Non-Executive Directors, in particular ensuring constructive relations between Executive and Non-Executive Directors, and ensuring effective communication with the Company's shareholder. Board agendas are agreed in consultation with other Directors and the Company Secretary.

Any Director or the Company Secretary may request an item be included on the agenda

New Directors receive a full, formal and tailored induction on joining the Board (including an opportunity to meet with representatives of the shareholder). Further training is given as required. In his role as Chief Executive Colin Skellett has responsibility for the day to day business of the Company, making proposals for its strategic direction and communicating with customers and other stakeholders.

Senior Independent Director

The Board has appointed David Barclay as the Senior Independent Director. He chairs the Audit Committee and is a member of the Remuneration Committee and of the Nominations Committee. He would chair Board meetings if the Chairman were unavailable. The Senior Independent Director's role is to act as a sounding board for the Chairman and to serve as an intermediary for the other Directors when necessary. He is also available as an additional point of contact for the shareholder and other stakeholders.

As the Senior Independent Director and appointed in accordance with the Licence, he is well placed to provide an independent link to WSRA, our regulator. His responsibilities during the reporting year included leading the evaluation of the performance of the Chairman. Led by the Senior Independent Director, the Independent Non-Executive Directors met without the other Directors present to appraise the Chairman's performance and to discuss any other relevant matters.

Independent Non-Executive Directors

The Company's Independent Non-Executive Directors are appointed from a range of different backgrounds to bring to the Board external experience and insight. They provide independent thought and challenge to the Board's decision making. The Board has reviewed their status and concluded that they are all independent. In particular, the Board considers these Directors to be independent in character and judgement. The Board are not aware of any relationships or circumstances which are likely to affect, or could appear to affect, any Independent Non-Executive Director's judgement.

Independent Non-Executive Directors are appointed, after consultation with Ofwat and with the agreement of the Company's shareholder, for an initial three-year term (subject to statutory provisions relating to removal) that may be extended. Since 2011 we have seen the appointment of three new Independent Non-Executive Directors and two new shareholder Non-Executive Directors.

Any term beyond six years for an Independent Non-Executive Director is subject to particularly rigorous review and takes into account the need for progressive refreshing of the Board balanced against the requirement for skills, experience, independence and knowledge. The Board considers that David Barclay remained independent and that the Board is refreshed at sufficient intervals, and accordingly the Company is compliant with the spirit of the Code in this respect. Continuity of appointment of some Independent Non-Executive Directors between Ofwat price reviews is desirable to facilitate scrutiny of Company performance against its business plan.

Independent Non-Executive Director	Appointed	Current term expires
David Barclay	01/11/2005	31/10/2016
Gillian Camm	01/11/2011	01/11/2017
Huw Davies	01/09/2014	31/10/2017
Richard Keys	01/05/2016	30/04/2019
Fiona Reynolds	01/08/2012	30/09/2018

Governance Report *(continued)*

All Independent Non-Executive Directors are appointed on written terms setting the time commitments and standards required of them. In accordance with Code Provision B.3.2, terms of engagement are regulated by letters of appointment (copies of which are available on the Company's website). Non-Executive Directors representing the Company's sole shareholder do not have formal terms of appointment and receive no payments from the Company. In accordance with Code Provision B.4.1, all Directors are required to participate in an induction process to familiarise themselves with the Company's governance arrangements, business, regulatory framework and ethos. Introductory meetings are held with all Executive and Non-Executive Directors, the Company Secretary and senior managers across the Company's business.

Visits are made to the Company's principal offices and representative operational sites. The training and development needs of the Executive Directors and Independent Non-Executive Directors are reviewed annually by the Chairman.

Company Secretary

All Directors have access to the Company Secretary and the Company's internal solicitors. The Company Secretary's responsibilities include ensuring good information flows within the Board and its Committees and between senior management and Non-Executive Directors, as well as facilitating induction and assisting with professional development as required. The Company Secretary is responsible for ensuring that the Company's O&CA and Board procedures are followed, and for advising on suggested changes.

The Company Secretary gives legal and regulatory advice as required by the Board or any Director and is responsible for advising the Board through the Chairman on governance matters. The Board is kept informed of major changes to law and regulation affecting the Company's business. The Company Secretary also advises on Directors' duties and conflicts. All Directors are aware that any conflicts of interest must be reported to and registered with the Company Secretary.

The appointment or resignation of the Company Secretary is a matter for consideration by the Board as a whole. Andrew Phillips retired on 30th November 2015 and was succeeded with the agreement of the Board, by Leigh Fisher-Hoyle on the same date.

Board Meetings

The Board meets a minimum of six times a year at approximately bi-monthly intervals, which is considered sufficiently regularly to enable the Board to discharge its duties effectively. It may meet on such further occasions as may be required.

Board attendance in the financial year under review was as follows:

Board Attendance 2015-16			
Colin Skellett	6/6	Kathleen Chew	6/6
David Barclay	6/6	Francis Yeoh	6/6
Gillian Camm	6/6	Hann Yeoh	5/6
Mark Watts	6/6	Hong Yeoh	6/6
Huw Davies	6/6	Mark Yeoh	6/6
Fiona Reynolds	5/6		

Board Committees and Advisory Panels

Four formal committees operated throughout the financial year under review:

- Audit Committee
- Remuneration Committee
- Nominations Committee
- Corporate Responsibility Committee.

These Committees operate under the authority of the Board and assist the Board in carrying out its duties. The Committees report back to the Board on decisions and actions taken together with any specific recommendations. Reports from the Chair of each of the Committees are set out on the following pages.

The Board also receives reports from three liaison panels and a customer partnership panel as part of the Company's commitment to wide stakeholder engagement.

Governance Report *(continued)*

The Futures Panel is chaired by Fiona Reynolds. It keeps under review emerging issues facing all companies today (including sustainability, health and the environment). By invitation a range of external scientific and technical expertise is brought to this panel.

The Wessex Water Partnership including our key organisational stakeholders, scrutinises and assesses the Company's delivery against customer related outcomes and performance commitment. The Partnership is independently chaired by Dan Rogerson who was previously Water Minister under the coalition Government.

The Catchment Panel helps to inform the Company's decision making about sustainable land and water resource use in the context of the Company's services, constructed and natural assets and entitlements. The panel includes representatives of the Environment Agency, Natural England, the Drinking Water Inspectorate, the National Farmers' Union and the Country Landowners Association. The panel is chaired by Dr Richard Cresswell.

Board, Committee and Director Performance

The Board has agreed to review its own performance, and the performance of its Committees, the Chairman, the Executive Directors and the Independent Non-Executive Directors, annually in accordance with the Code. Generally, the Board will engage the services of an external Board evaluation consultant at least one year out of three. Between external evaluations, reviews are facilitated by the Company Secretary.

In accordance with the Code a Board, Chairman and Committee Effectiveness Review was carried out in May 2016. Evaluation of the Board considers the Board's balance of skills, experience, independence and knowledge of the Company and how the Board works together as a unit, and other factors relevant to its effectiveness. A questionnaire was sent by the Company Secretary to all Directors. Individual responses were aggregated and analysed on an anonymized basis, and the results presented to and discussed by the Independent Non-Executive Directors on 17 June 2016. Several improvements were identified, including facilitating wider visibility of activities outside the regulated entity, a greater focus on key topics such as new business models and the newly formed Wessex Water Partnership, and a simpler structure for the regular Board report.

Directors' Remuneration

Details of Directors' remuneration are set out in the Remuneration Committee Report.

Directors' Interests and Conflicts

Directors are aware of the requirement to disclose interests in contracts with the Company and any conflicts of interest. No such interests or conflicts were disclosed during the year.

Whistleblowing

The Company has adopted and publicised to all its employees a whistleblowing policy for reporting instances of malpractice or inappropriate activity across all areas of business, including water regulation, health and safety, bribery, corruption and fraud. All reports are treated on a strictly confidential basis. Reports on whistleblowing are made to the Audit Committee and details are set out in the Audit Committee Report.

Anti-corruption

The Company has adopted a formal policy on business ethics. Directors and employees are expected to commit to the highest standards of professional and ethical conduct in order to protect the Company's reputation and standing. Bribery and corruption is not tolerated. All Directors and employees are made aware of the Company's policy and that breaching it will result in disciplinary action. No instances of a breach of the policy were recorded in the year.

Procurement

The Company has in place procurement rules that ensure awards of contracts for works, services and supplies are made after compliance with the Utilities Contracts Regulations 2006 and for contracts below the relevant thresholds in accordance with clear internal rules. The rules promote fair competition for potential suppliers. All relevant staff are required to certify to internal audit through the year that they have complied with the rules or to disclose non-compliance. No material instances of non-compliance were recorded during the year.

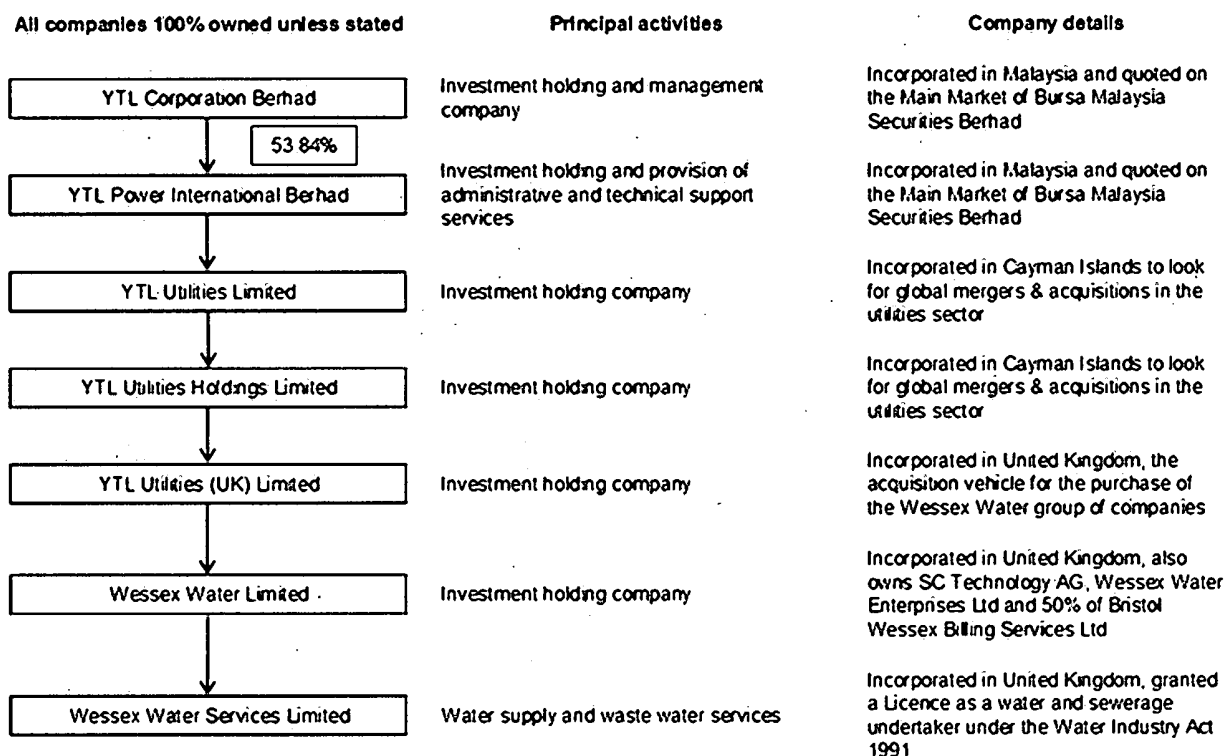
Group Structure

Owat's published document Board Leadership, Transparency and Governance – Holding Company Principles sets out the principles it expects the holding companies of a regulated water company to follow to demonstrate adherence to the highest standards of governance, particularly in its interaction with a regulated water company. The Holding Company Principles build upon and supplement the Company's licence provisions dealing with its relationship with its owners.

The Company's ultimate holding company is a Malaysian company YTL Corporation Berhad, listed on the main market of Bursa Malaysia Securities Berhad. It addresses the Holdco Principles as described below.

Governance Report *(continued)*

A diagrammatic representation of the Group's structure appears below showing ownership of the regulated Company through to YTL Corporation Berhad and each company's country of incorporation and role in the structure. At 30 June 2016, YTL Corporation Berhad was 50.70% owned by third party shareholders and 49.30% owned by Yeoh Tiong Lay & Sons Holdings Sdn Bhd.



The following Directors of the Company are also Directors of the Group companies above:

Colin Skellett and Mark Watts are Directors of Wessex Water Ltd, YTL Utilities (UK) Ltd and YTL Utilities Holdings Ltd.

Francis Yeoh and Mark Yeoh are Directors of Wessex Water Ltd, YTL Utilities (UK) Ltd, YTL Utilities Ltd, YTL Power International Berhad and YTL Corporation Berhad. Hong Yeoh is a Director of Wessex Water Ltd, YTL Utilities (UK) Ltd, YTL Utilities Holdings Ltd, YTL Utilities Ltd, YTL Power International Berhad and YTL Corporation Berhad. Hann Yeoh is a Director of YTL Utilities Holdings Ltd.

YTL Corporation Berhad's consolidated debt and equity are shown in its annual accounts available at its YTL Corporation website. The Company has no borrowings with other Group companies.

The Company operates independently. There are no matters specifically reserved to the shareholder. In practice the Board operates (and has operated continuously for more than a decade) without the requirement for shareholder resolutions. A list of those Directors of the Company who also hold office within the Group structure appears above. Disclosure of the interests of such Directors has been made to the Company.

Governance of YTL Corporation Berhad is in accordance with the requirements of Bursa Malaysia and corporate law in Malaysia which include a requirement to publish statements in its annual accounts on corporate governance, risk, risk management and internal control and the workings of its audit committee.

Governance Report *(continued)*

YTL Corporation Berhad and YTL Power International Berhad gave undertakings to Ofwat in 2002 upon the acquisition of the Company that they and their subsidiaries would comply with the requirements of Licence Condition P. The Condition P undertaking provides that:

- they would give the Company all information as may be necessary to enable the Company to comply with the conditions of its appointments as a water and sewerage undertaker;
- to refrain from any action which would cause or may cause the company to breach any of its obligations under the Water Acts or the conditions of its Licence;
- to ensure that at all times the Company's Board contains not less than three Independent Non-Executive Directors.

YTL Corporation Berhad has confirmed that it:

- fully understands the duties and obligations of the Company arising under statute and its Licence;
- is aware of and is complying with the obligations of Condition P of its Licence;
- discharges these obligations by various means including through its knowledge of the terms of the Licence, the appointments of shareholder directors to the Board of the Company and their involvement in the affairs of the Company and the advice of its UK corporate lawyers;
- will provide the Company with the information it legitimately needs to assure itself that it is not at risk from activities elsewhere in the YTL Group;
- will identify and disclose to the Company promptly in writing any issues, if such should arise, within the YTL Group which may materially impact upon the Company for publication on the Company's website or disclosure in its annual report any relevant announcements made on Bursa Malaysia;
- will facilitate, so far as it is reasonably able, compliance with the Company's Code of Practice for Corporate Governance;
- will support the Company's decision making processes so that it can make strategic and sustainable decisions in the interests of the Company for the long term.

Audit Committee Report

All the independent non-executive directors of the Board as below were members of the Audit Committee throughout the financial year under review:

David Barclay (Chair)
Gillian Camm
Fiona Reynolds
Huw Davies

The Board is satisfied that all members of the Audit Committee are independent and that through David Barclay and Huw Davies, the Committee has relevant financial experience.

Role and Report on Activities

In accordance with Code Provision C.3.2. and C3.3., our Governance Arrangements are available on the Company's website and provide full terms of reference for the Audit Committee.

This report provides details of the role of the Audit Committee and the work it has undertaken during the financial year under review.

The members of the Audit Committee receive updates on financial reporting, the regulatory framework and performance throughout each financial year. In addition to the Committee members the following routinely attend the Committee meetings by invitation: the Director of Finance, senior manager responsible for Regulation and Customer Services, Financial Controller, Head of Internal Audit, and the audit partner from the external auditor KPMG. Other senior management and the Company's external technical auditor are also invited to attend as appropriate.

The technical editor for the Wessex Water Partnership is also invited to the Audit Committee meeting which considers the Annual Review and Performance Report.

Following each meeting the chair of the Audit Committee reports to the subsequent meeting of the Board on the Audit Committee's work.

Governance Report *(continued)*

The Audit Committee met four times in the financial year under review, which it considered sufficient to enable it to discharge its duties effectively. Its work focused on:

- overseeing the Company's financial reporting processes and accounting policies
- ensuring that the Company has adequate internal controls and that they are appropriately reviewed and implemented
- overseeing the internal and external audit programmes
- ensuring compliance with the regulatory reporting obligations of the Company, including the Risk and Compliance Statement and the Company's performance commitments.

In accordance with Code Provision C.3.8, key issues discussed during the financial year under review included:

- detailed review of the Company's preparedness for Open Water with the chair of the Committee signing the first of the three assurance letters required by the Open Water methodology
- detailed review of the Company's Information Assurance Statement and Information Assurance Plan in accordance with Ofwat's Company Monitoring framework – final position and recommending their approval to the Board
- an update of the Company whistleblowing policy following the publication in March 2015 by the Department for Business Innovation and Skills of guidance and a code of practice on whistleblowing
- Company performance on a number of internal processes to deliver regulatory outputs and performance commitment data
- detailed independent consideration of the half year results, the Annual Review documents incorporating the Annual Performance Report prior to their ultimate approval by the Board
- consideration of the material subjective assessments within financial reporting to ensure that the Company's treatment of these matters was properly addressed within the Company's financial statements
- the review and agreement of the annual internal audit programme, the monitoring of internal audit progress and the consideration of 16 internal audit reports in the year.

In reviewing the financial statements, the Audit Committee considered the content, accuracy and tone of the financial statements and the principal risks to the business on pages 17 and 18.

KPMG reported to the Audit Committee on their audit of the year-end financial statements.

Internal Controls

The Audit Committee monitors the effectiveness of the system of internal control assisted by internal audit. It also reviews management reports received from the external auditor.

The Audit Committee receives reports on any whistleblowing allegations made to the Company from either internal or external sources, concerning fraud, bribery or other matters. Reports include the outcomes of resulting investigations and the management action taken. Where appropriate the Audit Committee is asked to approve the proposed management actions. One anonymous whistleblowing allegation was received and investigated in the year. No corroboration of the allegation was found.

Financial Reporting

Material issues considered by the Audit Committee in relation to the financial statements (as also reported by the external auditor) were as follows:

Bad Debt Provision

The Committee considered the key financial risk that arose due to the subjective nature of the provision. It reviewed the methodology of the provision in relation to the different components of the debt and the reasonableness of the differing provision made against each component.

Pension Deficit

The Committee considered the key financial risk that the assumptions made by the Company in association with the independent actuary, in arriving at the pension deficit under IAS 19, could lead to an overly prudent or aggressive position. In particular, the assumptions in relation to inflation, discount rate, pension and salary increases, return on equity and life expectancy were tested against the range of assumptions used by other companies.

Governance Report *(continued)*

Classification of Capital Expenditure

The Committee considered the key financial risk of the degree of judgement involved in the classification of expenditure between operating expenses and capital expenditure. In doing so they considered the level of capital expenditure, the Regulatory Accounting Guidelines and International Financial Reporting Standards, the recharges from overhead to capital projects and the controls of the Company.

Taxation

The Committee also considered the amounts recorded for corporation tax and deferred taxation in the income statement and balance sheet. They reviewed the split between current and prior year taxation, the overall tax reconciliation and current taxation issues as highlighted by the external auditor.

The Committee was satisfied that each of the above issues had been adequately explained and correctly recorded in the statutory accounts of the Company.

Misstatements

Management confirmed to the Audit Committee that they were no material misstatements or immaterial misstatements in the financial statements to achieve a particular presentation. The external auditor reported to the Committee that in the course of their work no misstatements had been found. The Committee was satisfied that the external auditor had fulfilled its responsibilities to the Audit Committee and the Company.

Oversight of Internal Audit and External Audit

The Audit Committee oversees the work of the Company's internal audit function, monitoring and reviewing the effectiveness of the internal audit activities, and manages the relationship with its external auditor. The Audit Committee reviews the performance of the internal and external auditor to ensure that they are effective.

The Audit Committee regularly holds discussions at the end of its meetings with both the internal and external auditor in the absence of executive management.

Internal Audit

The annual programme of planned internal audits is agreed by the Audit Committee prior to the start of each financial year based on a balance of topics which represent major business risks, and internal business processes which affect either financial or regulatory compliance. A total of 16 individual audit reports were submitted to the Committee in the year.

At the request of either Executive Directors, senior managers or the Audit Committee, additional audits are undertaken throughout the financial year to address any issues that arise in the financial year.

The Head of Internal Audit reports back on reviews of performance and the effectiveness of the Company's internal controls and their adequacy in managing business risk and performance. This work is summarised and reported to the Audit Committee on a regular basis.

The audit plans and the level of resources of the internal audit function are reviewed at least annually by the Audit Committee. The Head of Internal Audit is free to raise any issues with the Audit Committee or its Chairman at any time during the financial year.

External Auditor

KPMG were appointed as the Company's auditor in 2002 and the audit contract has not been put out to tender since. Although KPMG's appointment exceeds the normal 10-year period suggested in the FRC UK Corporate Governance Code, it is consistent with the transitional arrangements as published by the FRC, that re-tender can take place at the end of the current audit partner's term of office in 2017. The Committee intends to re-tender the Company's external audit services at that time.

The audit partner attends by invitation meetings of the Committee, and the Committee monitors the effectiveness of the external auditor throughout the year taking into account their own experience of the auditor's effectiveness in the year.

KPMG was paid £156k for audit fees and a total of £9k for advice on tax and other matters. The individual commissions for non-audit work were considered to have no impact on the auditor's objectivity and independence. As a matter of policy, fees paid to the external auditor for non-audit services will not exceed 50% of the annual audit fee unless approved in advance by the Chair of the Audit Committee.

KPMG reports to Ofwat in respect of the Company's Annual Performance Report.

Governance Report *(continued)*

As part of the assurance process for this Annual Review document the Audit Committee also receives a report from its technical auditor on non-financial regulatory performance information provided in the Annual Review including the performance commitment data. The technical auditor services were re-tendered in 2015-16 and a new technical auditor, Mott McDonald, was appointed for the first three years of AMP6.

Audit committee attendance	
David Barclay	4/4
Gillian Camm	4/4
Huw Davies	4/4
Fioria Reynolds	4/4

Nominations Committee Report

The following were members of the Nominations Committee throughout the financial year under review:

Francis Yeoh (Chair)
 David Barclay
 Gillian Camm
 Huw Davies
 Fiona Reynolds
 Colin Skellett
 Hong Yeoh

The Nominations Committee is chaired by a Non-Executive Director appointed by the shareholder, by way of exception to the relevant Code Provision. The relevant Code Provision envisages a majority of the members being Independent Non-Executive Directors and the Chairman or an Independent Non-Executive Director chairing the Committee. This is intended to ensure a formal, rigorous and transparent procedure for the appointment of new Directors to the Board in the case of a listed company with disparate shareholders. However, during the year the Company's Nominations Committee complied with the Principles and spirit of the Code and its composition reflects the requirements of a private company with a sole shareholder.

Nominations committee attendance	
Francis Yeoh	1/1
Hong Yeoh	1/1
David Barclay	1/1
Gillian Camm	1/1
Huw Davies	1/1
Fiona Reynolds	1/1
Colin Skellett	1/1

Role and Report on Activities

The Nominations Committee's full terms of reference are available on the Company's website.

This report provides details of the role of the Nominations Committee and its work over the financial year under review.

The purpose of the Nominations Committee is to ensure that appropriate procedures are in place for the nomination, selection, training and evaluation of Directors. It reviews Board structure, size and composition.

The role of the Nominations Committee is to evaluate the balance of skills, experience, independence and knowledge on the Board.

Governance Report *(continued)*

The Nominations Committee met once during the financial year under review under the chair of Hong Yeoh, in the absence of Francis Yeoh. Its role includes monitoring the independence of Independent Non-Executive Directors, advising the Board on any conflicts of interest and reviewing executive succession planning.

The Committee considered Independent Non-Executive Director changes and the recruitment and appointment process for the appointment of a Managing Director for Wessex Water Services Limited, both of which will take place in 2016-17. The committee also reviewed the executive succession planning process.

Corporate Responsibility Report

The following were members of the Corporate Responsibility Committee throughout the financial year under review:

Gillian Camm (Chair)
Fiona Reynolds.

Chaired by an Independent Non-Executive Director, the principal purpose of this Committee established in 2013 is to make recommendations to the Board about the Company's corporate and social obligations to its employees and other stakeholders. The Committee invited two former executive directors of the Company Andy Pymmer and David Elliott (who stepped down from the Board in April 2014 as part of the Ofwat governance initiative that resulted in the number of executive directors being reduced to two) to attend by invitation.

Role and Report on Activities

The Committee's full terms of reference are available on the Company's website.

Corporate responsibility is central to the values against which our business operates. The Company's long-term success depends on meeting the values of our customers, employees and other stakeholders.

During the year the Committee commented on and endorsed policies on flexible working, flexible retirement and job share contracts, which were launched to complement the Company's diversity strategy. These policies have been presented to the Leadership Forum as part of the wider flexible working approach which the Company is moving towards with respect to employee working and appropriate IT and communication systems.

At each meeting the diversity metrics have been reviewed and challenged by the Committee. It is recognised that progress is being made to attract, develop and retain a more diverse workforce but that it takes time for initiatives to come into effect. An apprenticeship programme has been launched, with a full-time manager, to promote the opportunities available with a network of colleges throughout the region and within the Company. The success of the Open Day was reported along with plans for a Control Room Trailblazer, links to the National Career Services, a Girls Allowed event and wider connections with businesses through our region.

The Committee reviewed a number of reports throughout the year including the use of the Corporate Hospitality Register, charitable giving, health and safety and the Gender Pay Gap reporting. Health and safety has been a key theme throughout the year following the introduction of the five-year health and safety strategy. The Committee has suggested revisions to ensure that well-being is included and to take account of the occupational health and employee assistance service offered.

In addition, the Committee has reviewed the Company's Sustainability Vision, environmental accounting approaches and catchment reporting, all of which are being amended to take account of our longer term plans beyond 2020. The suggestions made by the Committee have been considered and will be reflected within these publications when produced later in 2016.

Corporate responsibility committee attendance	
Gillian Camm	2/2
Fiona Reynolds	2/2

Governance Report *(continued)*

Remuneration Committee Report

Members:

The following were members of the Remuneration Committee throughout the financial year under review:

Hong Yeoh (Chair)
David Barclay
Gillian Camm
Huw Davies
Mark Yeoh.

The Remuneration Committee is chaired by a Non-Executive Director appointed by the shareholder, by way of exception to the relevant Code Provision. The relevant Code Provision envisages at least three Independent Non-Executive Directors on the Remuneration Committee. This is intended to ensure a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual Directors in the case of a listed company with disparate shareholders. However, the Company's Remuneration Committee complies with the Principles and spirit of the Code and reflects the requirements of a private company with a sole shareholder, resulting in a formal and transparent procedure for developing policy on executive remuneration.

Role and Report on Activities

The Remuneration Committee's full terms of reference are available on the Company's website.

The Remuneration Committee determines, on behalf of the Board, the Company's policy on the remuneration (including pension rights and any compensation payments) of Executive Directors, the Chairman and senior executive managers. The Committee seeks to link rewards to performance to promote the long-term success of the Company and does not reward poor performance.

This report sets out the remuneration policy for the Directors of Wessex Water and discloses the amounts paid to them in the financial year ended 30 June 2016. The policy applies to the remuneration of the Company's senior managers.

The Remuneration Committee met twice during the financial year under review, which was considered sufficient to enable it to discharge its duties effectively.

The Remuneration Committee continued to monitor the Company's remuneration policy to take account of evolving best and market practice. The annual bonus plan is designed to promote the success of the Company over the five-year regulatory period, and is based on a portfolio of KPIs linked to the Company's performance scorecard and Ofwat's measures of success.

Salary and bonus levels were benchmarked against the Hay Group Industrial and Service, National Utilities and South West Utilities market sectors with jobs sized in relation to scope, role responsibilities and impact to determine salary.

The Remuneration Committee continued to take a proactive approach to responding to developments in legislation, best practice and the wider market, as well as the corporate strategy, in order to ensure that the Company's senior executive reward policy remained market competitive and fit for purpose.

The Remuneration Committee addressed the need to ensure that changes in senior executive remuneration are proportionate in the context of workforce pay. While it has not set a specific policy on the relationship between Executive Directors' pay and that of the rest of the workforce, it aims to ensure that executive salary movement is appropriately aligned to the rest of the workforce and it specifically considers this aspect as part of its decision making process.

To ensure that the Company's remuneration practices are competitive but not excessive, the Remuneration Committee has access to detailed external research on market data and trends from experienced specialist consultants.

Recruitment of Executive Directors

The base salary for any new Executive Director takes into account market data for the relevant role, relativity with the salaries of existing Executive Directors, the individual's experience and current base salary. In the event that an individual is recruited at below market level, their base salary may be aligned over a period of time to the upper quartile position of the relevant market position subject to their performance in the role.

Individual Executive Directors participate in a senior manager bonus scheme, governed by the Remuneration

Governance Report *(continued)*

Committee. Executive Directors have their target bonus set at 50% of base salary and their maximum bonus at 100% of which a proportion is withheld until 2020 under Long Term Incentive Plan (LTIP) arrangements.

During the year, the Remuneration Committee took advice from their independent advisers, Hay Group. Hay Group provided detailed market analysis and advice to the Committee for the senior management group, including Executive Directors and Non-Executive Directors. Hay Group's fee for providing such advice was £14,400 for the year. In line with best practice, the Committee assesses from time to time whether the appointment of its current independent remuneration advisers remains appropriate and whether the role should be put out to tender.

The Remuneration Committee also considers what compensation commitments (including pension contributions and all other elements) Directors' terms of appointment would entail in the event of early termination. The aim is to avoid rewarding poor performance, and the Remuneration Committee would take a robust line on reducing compensation to reflect departing Directors' obligations to mitigate loss.

The Chief Executive (Colin Skellett) and the Group Head of Human Resources (Mark Nicholson) attended the Remuneration Committee meetings to provide advice and respond to specific questions. They did not participate in any discussion concerning their own remuneration.

Remuneration Committee Attendance	
David Barclay	2/2
Gillian Camm	2/2
Huw Davies	2/2
Hong Yeoh	2/2
Mark Yeoh	2/2

The remuneration policy for senior executives is aligned to the Company's four key focus areas, as shown below.

Key Focus	Remuneration Policy
Customer service delivery and business costs	Target annual bonus potential just below the median when compared to industrial and service and national utilities market, supported by competitive base salary at or below market upper quartile. Financial based KPIs within the annual bonus are set with close regard to Ofwat's determination, ensuring that we closely manage our performance within the regulatory limits. Customer focused KPIs form a substantial part of the annual bonus scorecard.
Employee alignment	The Remuneration Committee aims to ensure that the executive salary movement is aligned to the rest of the workforce. The performance scorecard is used for the annual bonus throughout the Company. KPIs within the annual bonus for all employees include health and safety, engagement and training compliance factors.
Environment performance	KPIs within the annual bonus for all employees include environmental factors.
Financial performance	A variety of financial KPIs are used within the annual bonus plan with the aim of delivering a fair return to our shareholder.

The Remuneration Committee continues to monitor variable pay arrangements for the Executive Directors and senior managers. The Remuneration Committee believes that the arrangements are appropriately managed and that the choice of performance measures and targets does not encourage undue risk taking by the executives so that the long-term performance of the business is not put at risk by considerations of short-term value.

Governance Report *(continued)*

The arrangements incorporate a range of internal and external performance metrics, measuring both operational and financial performance providing a rounded assessment of overall company performance to ensure that a significant portion of executive remuneration is performance-related. More details of the remuneration policy for Executive Directors is shown later in this report.

Policy for loss of office

There are no specific provisions for compensation on early termination (except for payment in lieu of accrued but untaken holidays) or loss of office due to a change of ownership of the Company. The Committee will review all contractual obligations and will seek legal advice as and when necessary on the Company's liability to pay compensation in such circumstances. The Committee will seek to reduce the level of compensation payable taking into account, amongst other factors, the Company's and the individual's performance, the Executive Director's obligation to mitigate loss, and length of service.

Relative importance of spend on pay

Note 4 to the accounts shows the total employment costs of the Company, which have been kept under control between 2014-15 and 2015-16.

	2015-16 £m	2014-15 £m	Movement £m	Movement %
Wages and salaries	71.5	71.5	-	-
Social security costs	7.0	6.4	+0.6	+9.4
Pension costs	11.0	11.3	(0.3)	(2.7)
Total employment costs	89.5	89.2	+0.3	+0.3

Charged to:

Capital schemes	33.0	29.8	+3.2	+10.7
Manpower costs	56.5	59.4	(2.9)	(4.9)

The relative importance of total employment costs can be shown as:

Percentage of	2015-16 %	2014-15 %	Source
Turnover	17.2%	16.6%	Profit and loss account
Profit before tax	57.0%	52.9%	Profit and loss account
Profit after tax	53.8%	65.9%	Profit and loss account
Dividends	91.8%	108.1%	Note 8
Capital expenditure	50.1%	48.8%	Cash flow statement

Remuneration Arrangements for Executive Directors 2015-16

Executive Directors' remuneration package, comprises the following elements:

- Basic salary
- Bonus (non-pensionable) subject to individual and company performance
- Long-term incentive plan (LTIP)
- Pension plan
- Company car and private fuel allowance
- Private health insurance and executive medical screening
- Share option scheme of a parent company YTL Power International Berhad.

Governance Report *(continued)*

The table below highlights the key elements of executive remuneration and the link to Company strategy, how executive remuneration is operated in practice and the link to relevant performance metrics.

Element of Pay	Purpose and link to Company strategy
Base Salary	To attract and retain the high calibre Executive Directors and Senior Managers needed to implement the Company's strategy and maintain its leading position in the industry. To provide a competitive salary relative to comparable companies in terms of size and complexity.
Taxable Benefits	To attract and retain high calibre Executive Directors and Senior Managers and to remain competitive in the market.
Pension	To attract and retain high calibre Executive Directors and Senior Managers and to remain competitive in the market.
Annual Bonus	To motivate and reward Executive Directors and Senior Managers for the achievement of demanding financial objectives and key strategic measures (including measures of customer satisfaction, service quality and environmental performance) over the financial year and five-year regulatory period. The performance measures set are stretching in the context of the nature, risk and profile of the Company.
LTIP	To motivate and reward Executive Directors for the achievement of demanding financial objectives and key strategic measures (including measures of customer satisfaction, service quality and environmental performance) over the five-year regulatory period to promote the long term success of the Company.
How operated in practice	
Base Salary	Reviewed annually and takes effect from 1 April. Review takes into consideration; <ul style="list-style-type: none"> • Individual responsibilities, experience and performance • Salary levels for similar sized roles in utilities (south west industrial and service) • The level of pay increases awarded across the Company • Economic and market conditions • The performance of the Company Salaries are paid monthly.
Taxable Benefits	Benefits include: <ul style="list-style-type: none"> • Company car • Private medical insurance • Executive health screening • Private fuel allowance
Pension	All Executive Directors participate in the Company's defined benefit pension scheme. Executive Directors are also insured for a lump sum of up to four times their pensionable salary on death in service.
Annual Bonus and LTIP	The Board of Directors sets annual performance targets for the Company prior to the commencement of each new financial year. Company and individual performance against those targets is measured at the end of the financial year and the level of bonus payable is calculated at that point. Bonuses are paid in April. From 1 April 2015 the Remuneration Committee established a Long-Term Incentive Plan for Executive Directors whereby 20% of any above target bonus element earned will be held back for payment at the end of AMP6 in 2020. The Company will match the value of the retained bonus payment, up to 100%. The long-term incentive payment will be paid to Directors in April 2020. The Committee has the discretion to, and does consider the effect of corporate performance on environmental and governance risks when reviewing Executive Director and senior management bonuses to ensure variable remuneration incentivises and rewards appropriate behaviour. Part of the bonus may be forfeited for under performance in respect of customer service, environmental, regulation and employee related performance targets. Annual bonus is not pensionable.

Maximum opportunity	
Base Salary	There is no prescribed maximum increase. However, Executive Director salary increases are aligned to the increases provided to all Company employees. Such increases are negotiated by the joint staff council involving management and trade union representatives.
Taxable Benefits	N/A
Pension	18.2% of base salary
Annual Bonus	Maximum bonus opportunity is 100% of base salary.
Description of performance metrics	
Base Salary	N/A
Taxable Benefits	N/A
Pension	N/A
Annual Bonus	A combination of 32 key performance indicators relating to financial, customer, environment and assets and employee related measures and targets. An equal weighting is applied to financial, customer, environment and assets and employee related measures (health and safety, training and engagement). The Committee has absolute discretion in making bonus payments.
Change to policy	
Base Salary	No change
Taxable Benefits	No change
Pension	No change
Annual Bonus	No change but the key performance indicators were updated.

A detailed explanation of each of these follows and the table below highlights some of the elements.

Component 2015/16	Colin Skellett Chief Executive	Mark Watts Director
Target bonus (% of salary)	50	50
Maximum bonus (% of salary)	100	100
Actual bonus paid (% of salary)	62	65
Share options (maximum)	Approved 87,000 Unapproved 1,913,000	Approved 87,000 Unapproved 913,000
Pension arrangement	Defined benefit [Pension in payment]	Defined benefit
Benefits	See below	See below

Benefits were company car based on list price and CO2 emissions, fuel £4,310 and private medical insurance £1,775 (family).

Base Salaries and Benefits

Executive Directors' remuneration is reviewed annually by the Remuneration Committee and takes effect from 1 April. Salaries are set with reference to individual performance, experience and contribution, together with development in the relevant employment market (having regard to the upper quartile position for high performers in similar roles in the relevant employment market) and internal relativities.

Differences between Executive Directors' and Employees' Remuneration

The following differences exist between the Company's policy for the remuneration of Executive Directors and its policy for the remuneration of employees:

- Executive Directors pay is benchmarked against the upper quartile position of the South West Utilities market whilst we benchmark median pay and benefits against the South West Industrial and Service market for all fully qualified and experienced employees
- A lower level of target and maximum annual bonus opportunity applies to various employees when compared to Executive Directors. However, all employees, including Executive Directors and Senior Managers were subject to the same negotiated pay award increase
- Executive Directors (and senior managers) participate in a bonus scheme that is not available to other employees to motivate and reward them for achievement of demanding financial objectives and key strategic measures.

Governance Report *(continued)*

In general, these differences arise from the development of remuneration arrangements that are market competitive for the various categories of staff ranging from employees to Executive Directors.

The Remuneration Committee gives due consideration to the current economic climate and current market practice regarding executive salary reviews and the broader employee salary review policy at the Company.

We do not normally link pay levels to company performance measures, as this is done where appropriate through the bonus arrangements.

The Remuneration Committee has reviewed 2015-16 salaries and has determined that salaries for Executive Directors were increased from 1 April 2016 by 1.0% for Colin Skellett and 7.7% for Mark Watts. For Colin Skellett this increase is in line with the agreed increase across the rest of the Company and for Mark Watts the Remuneration Committee considered that a higher increase in salary was warranted as the salary was low compared to the South West Utilities upper quartile.

Executive Directors' bonuses - 2015-16 Scheme

The annual bonus of Executive Directors is performance-related and designed to promote the long-term success of the Company. It is dependent on the achievement of Company and individual targets.

Bonus disclosed is in relation to the performance in the year, and is paid in April following the year end.

The Company targets are 32 key performance indicators covering financial measures, customer service, environmental and asset measures and employee matters, as shown below.

Financial – profit after corporation tax / operational costs / net capital expenditure / cash flow before dividends / dividends declared.

Customers – Service Incentive Mechanism combined score / customers rating service good or very good / customers rating ease of resolution / compliance with drinking water standards / customer contacts about drinking water quality / volume of water saved through water efficiency / properties supplied by a single source of water / properties suffering supply interruptions > 3 hours / volume of water leaked / restrictions on water use / internal flooding incidents per 10,000 properties / flooding risk score.

Environment and Assets – EA's Environmental Performance Assessment / bathing water failures due to WWSL activities / Biodiversity Action Plan landholding assessed and managed / greenhouse gas emissions / proportion of electricity self-generated / all regulatory outputs met / compliance with abstraction licences / water main bursts / monitoring of CSO's presenting a risk to the environment / collapses and bursts on sewerage network.

Employees – RIDDOR incidents per 1,000 employees / employee rating company as a good employer / compliance with training plan / staff turnover / diversity plan progress as assessed by Corporate Responsibility Committee.

The target bonus for the Executive Directors was calculated as follows:

Target Bonus 2015/16	Colin Skellett Chief Executive	Mark Watts Director
Financial		
% of salary	10.0%	10.0%
Amount £	34,992	20,800
Customer		
% of salary	10.0%	10.0%
Amount £	34,992	20,800
Environment and Assets		
% of salary	10.0%	10.0%
Amount £	34,992	20,800
Employees		
% of salary	10.0%	10.0%
Amount £	34,992	20,800
Individual		
% of salary	10.0%	10.0%
Amount £	34,992	20,800
Total		
% of salary	50%	50%
Amount £	174,960	104,000

Governance Report *(continued)*

In the financial year under review, 29 of the 32 Company targets were achieved or bettered. The three company targets not achieved were compliance with drinking water standards, bathing water failures due to Wessex Water activities and employees rating the company as a good employer.

As regards drinking water standards there was only one failure due to Wessex Water operational failures, there was only one bathing water failure which was at Burnham Jetty and the employee rating of the company as a good employer was only a marginal failure at 83% compared to the 85% target.

The actual bonus payments are shown in the Directors' Emoluments table. The detail of how these bonus payments were calculated is shown below.

Actual Bonus 2015/16	Colin Skellett Chief Executive	Mark Watts Director
Financial		
% of salary	12.4%	13.0%
Amount £	43,478	27,200
Customer		
% of salary	12.4%	13.0%
Amount £	43,478	27,200
Environment and Assets		
% of salary	12.4%	13.0%
Amount £	43,478	27,200
Employees		
% of salary	12.4%	13.0%
Amount £	43,478	27,200
Individual		
% of salary	12.4%	13.0%
Amount £	43,480	27,200
Total		
% of salary	62%	65%
Amount £	217,392	136,000

Annual bonus payments to Executive Directors are not pensionable.

Pensions

Executive Directors are members of the Wessex Water defined benefit pension scheme. The scheme is a HMRC registered defined benefit occupational pension scheme. The Executive Directors are members of the WPS section which provides:

- A normal retirement age of 65 years
- A pension at normal retirement age based on 1/60th of completed pensionable service and final pensionable salary
- Life cover of four times basic salary including bonus
- A pension payable in the event of retirement on grounds of ill health
- A dependant's pension on death of two thirds of the member's pension
- Guaranteed increases in line with price inflation (subject to a maximum of 5% each year).

Members' contributions are payable at the rate of 8% of basic salary, with the Company making a further 18.2% contribution. Early payment of pension is available from age 55 with the consent of the Company. Any pension would be subject to a reduction, based on rates the trustees consider appropriate, acting on actuarial advice, to reflect the expected longer payment of the pension. No additional pension will become receivable by a Director if that Director retires early.

In the event of incapacity, an unreduced pension is payable immediately. Incapacity pensions can be paid on either a "partial" or "full ill health" basis depending on the conditions met. A full ill health pension is topped up to give additional service to age 65, subject to a maximum of 20 years.

Under the Trust Deed and Rules, pensions in payment in excess of any guaranteed minimum pension are guaranteed to increase in line with price inflation subject to a maximum of 5% each year. In the calculation of individual cash equivalent transfer values, allowance is made for such increases.

Governance Report *(continued)*

As a result of the changes in pension legislation for high earners, Wessex Water has introduced the following options for individuals under age 55 who are affected by the tax changes:

- continue in the scheme, with individuals meeting any tax liabilities as they fall due; or
- continue in the scheme with a capped pensionable salary which restricts pension growth to the annual allowance limit (£50,000 pa) and receive a cash supplement in lieu of pension entitlement on the excess salary. The cash supplement is based on the employer contribution rate to the scheme, currently 18.2%.

Mark Watts received a cash supplement of 18.2% of excess salary above the capped salary for pension purposes from 1 July 2015 to 8 July 2015.

Executive Directors' Service Contracts

All Executive Directors' service contracts are terminable by either the Company or the Executive Director providing 12 months' notice. There is a theoretical maximum payment in case of redundancy of 100% of salary inclusive of allowances and benefits plus their redundancy entitlement. There are no specific contractual payments or benefits which would be triggered in the event of a change in control of the Company.

Executive Directors	Date of current agreement	Date of appointment as Executive Director	Notice Period
Colin Skellett	01/04/2014	01/09/1989	12 months
Mark Watts	01/04/2014	16/03/2010	12 months

Executive Directors' service contracts are available for inspection during normal office hours at the registered office, Wessex Water, Claverton Down Road, Bath BA2 7WW.

The Remuneration Committee will continue to review the contractual terms for Executive Directors to ensure they reflect best practice and are compliant with employment law. No new Executive Directors were appointed during the financial year under review.

None of the Executive Directors served as a Non-Executive Director for another company.

Non-Executive Directors

The remuneration policy for Independent Non-Executive Directors is determined by the Board. The remuneration reflects the time commitment and responsibilities of the role.

The breakdown of the Independent Non-Executive Directors' fees from 1 July 2015 is shown in the Directors' Emoluments table below. Independent Non-Executive Directors do not participate in share or bonus schemes or any other performance-related scheme, nor is any pension provision made.

Independent Non-Executive Directors are normally appointed for three-year terms (subject to statutory provisions relating to the removal of a Director) that may be renewed. They do not have service contracts but their terms of engagement are regulated by letters of appointment (copies of which are available on the Company's website).

Any term beyond six years for an Independent Non-Executive Director is subject to particularly rigorous review and takes into account the need for progressive refreshing of the Board balanced against the requirement for skills, experience, independence and knowledge.

Non-Executive Directors appointed by the shareholder do not receive any fees or other payments from the Company.

Governance Report *(continued)*

Directors' Emoluments

The table below shows the emoluments for the current year.

2015-16	Salary £000	Bonus £000	LTIP £000	Benefits £000	Pension contributions £000	Total £000
David Barclay	85	-	-	-	-	85
Gillian Camm	66	-	-	-	-	66
Huw Davies	66	-	-	-	-	66
Richard Keys	11	-	-	-	-	11
Fiona Reynolds	66	-	-	-	-	66
Colin Skellett	350	217	11	25	-	603
Mark Watts	213	136	8	17	38	412
Total £000	857	353	19	42	38	1,309

1. No emoluments earned by Francis Yeoh, Hann Yeoh, Hong Yeoh, Mark Yeoh or Kathleen Chew.
2. Richard Keys part year in 2015-16.
3. Benefits comprise private medical insurance, company car and fuel benefits.
4. Two Directors received emoluments for services to other Group Companies, Colin Skellett £291k and Mark Watts £253k. The Audit Committee was satisfied that services provided to other Group Companies do not reduce the effectiveness of the Directors' provision of services to the Company.

The table below shows the emoluments for the prior year.

2014-15	Salary £000	Bonus £000	Benefits £000	Pension contributions £000	Total £000
David Barclay	81	-	-	-	81
Gillian Camm	61	-	-	-	61
Peter Costain	40	-	-	-	40
Huw Davies	52	-	-	-	52
Fiona Reynolds	61	-	-	-	61
Colin Skellett	347	140	23	-	510
Mark Watts	205	96	17	29	347
Total £000	847	236	40	29	1,152

Governance Report *(continued)*

Chief Executive

No remuneration was paid to the Chairman (2015 – £nil). The total remuneration for the Director performing the role of Chief Executive (Colin Skellett) was:

	Remuneration 2015-16 £000	Remuneration 2014-15 £000	% change
WWSL			
Salary	350	347	0.9%
Bonus	217	140	55.0%
LTIP	11	-	-
Benefits	25	23	8.7%
Other group companies			
Salary	88	87	1.1%
Bonus	194	175	10.9%
LTIP	3	-	-
Benefits	6	6	-
Total	894	778	14.9%
All employees WWSL			
Wages and salaries	71,500	71,500	-
Social security costs	7,000	6,400	9.4%
Other pension costs	11,000	11,300	(2.7)%
Total	89,500	89,200	0.3%

Included in the 2015-16 remuneration for the Chief Executive was a bonus of £217k representing 62% of salary, the target bonus being 50% of salary and the maximum 100% of salary.

Comparison with remuneration increase for all employees:

The pay increase awarded to the employees of the Company on 1 April 2015, for the year 2015-16, was a 1.0% increase over the preceding year.

Executive Directors' Defined Benefit Pension Provision

	Pension service completed in years (1)	Normal retirement date at 65	Accrued pension at 30/6/2015 £pa	Increase in accrued pension during the year £pa	Accrued pension at 30/6/2016 £pa
Colin Skellett (2)	41	n/a (2)	169,254	1,998	171,252
Mark Watts	27	19/9/2026	84,443	34,599	119,042

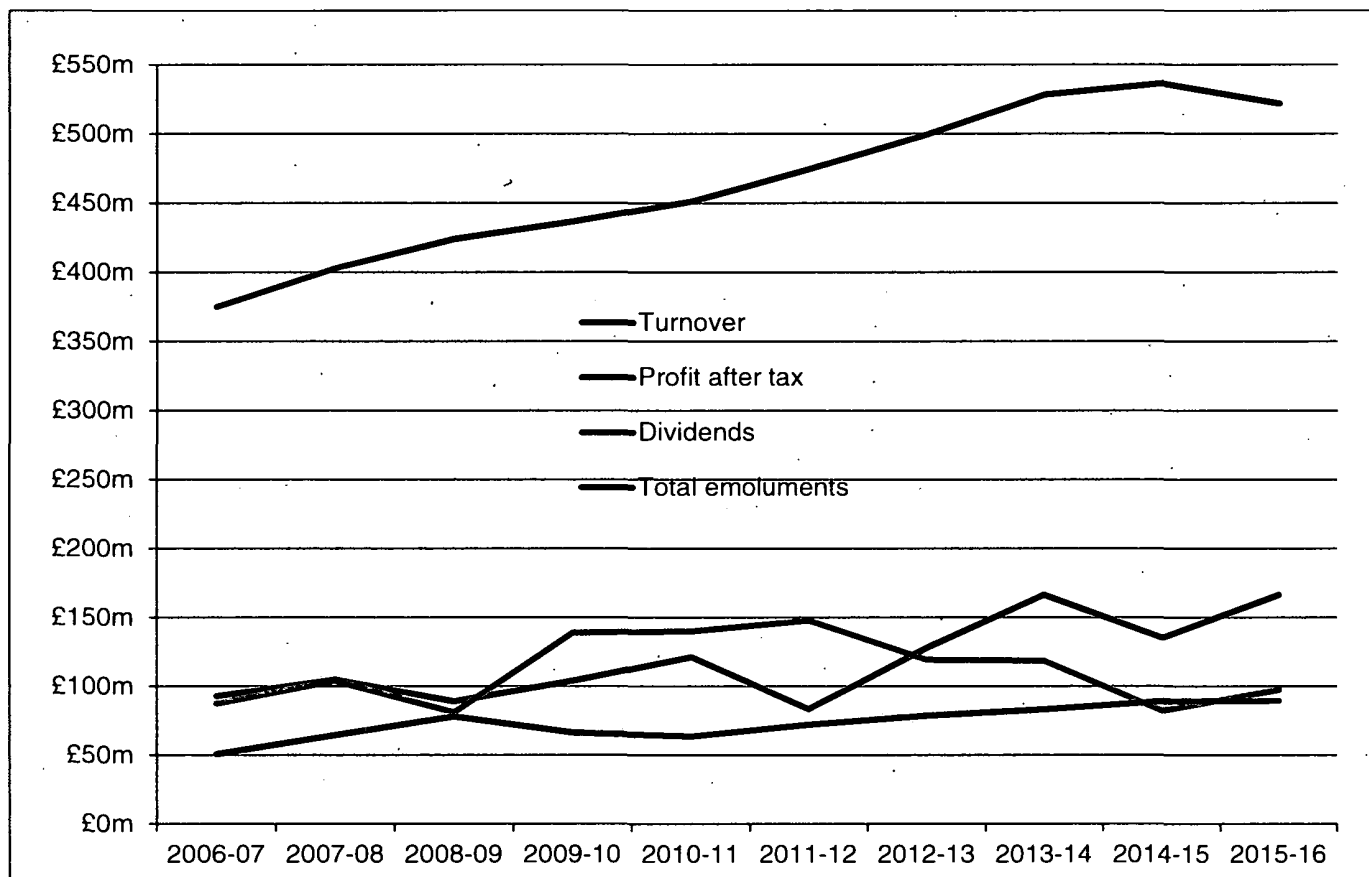
(1) Including transfers in and bonus years

(2) Pension in payment

Governance Report *(continued)*

Remuneration Link to Performance

The table below compares the movement over six years in total emoluments of the Company with the movement in the key financial performance measures of turnover, profit after tax and dividends.



Dividends are as declared in the year. Total emoluments include Directors' emoluments.

Executive Directors' Share Interests Share Options

YTL Power International Berhad (a parent company and itself a subsidiary of YTL Corporation Berhad) operates a share option scheme under which options are granted to employees of the Company. The terms of the scheme are specified under the YTL Power ESOS (2011 UK part) known as the "2011 UK Plan".

The majority of options are issued under terms approved by HMRC (the "Approved" scheme) but some are issued to senior employees under an "Unapproved" scheme. The options are for ordinary shares in YTL Power International Berhad of Malaysian Ringgit RM0.50 each.

The Executive Directors have been granted ordinary share options of Malaysian Ringgit RM0.50 each in YTL Power International Berhad under the 2011 UK Plan. The exercise of share options granted is not subject to any performance criteria, other than continued employment within the group.

Governance Report *(continued)*

Share options held by Executive Directors at the start and end of the financial year, and the exercise price of those share options are shown in the table below:

	Opening number 30/6/2015	Exercise price RM	Date of grant	Exercise date	Expiry date	Closing number 30/6/2016
Colin Skellett	87,000	1.65	1/6/2012	1/6/2015	31/3/2021	87,000
Colin Skellett	1,913,000	1.41	1/6/2012	1/6/2015	31/3/2021	1,913,000
Mark Watts	87,000	1.65	1/6/2012	1/6/2015	31/3/2021	87,000
Mark Watts	913,000	1.41	1/6/2012	1/6/2015	31/3/2021	913,000

Approved options were granted at an exercise price of RM1.65. Unapproved options were granted at an exercise price of RM1.49, which was adjusted to RM1.41 following the distribution to all shareholders of one share for every 20 ordinary shares held as at 13 March 2014.

The share price at 30 June 2016 was RM1.41 or £0.26.

Shares Held

There are no shares held by the Directors in the Company or the UK parent company.

The Executive Directors held the following ordinary shares of Malaysian Ringgit RM0.50 each in YTL Power International Berhad (a parent company), at the start and end of the accounting period. The share price at 30 June 2016 was RM1.41 or £0.26.

	Opening number 30/6/2015	Closing number 30/6/2016
Mark Watts	388,030	388,030

Remuneration Arrangements for Executive Directors 2016-17

Component	Colin Skellett Chief Executive	Mark Watts Director
Target bonus (% of salary)	50	50
Maximum bonus (% of salary) of which a proportion is withheld until 2020 under LTIP arrangements	100	100
Share options (maximum)	Approved 87,000 Unapproved 1,913,000	Approved 87,000 Unapproved 913,000
Pension arrangement	Defined Benefit [Pension in payment]	Defined benefit
Taxable Benefits	Company car, fuel and private medical insurance	

Governance Report *(continued)*

Bonus scheme 2016-17

For 2016-17 there are 29 performance indicators set to reflect the corporate targets in the current regulatory period, as shown below.

Financial – profit after corporation tax / operational costs / net capital expenditure / cash flow before dividends / dividends declared.

Customers – Service Incentive Mechanism combined score / customers rating service good or very good / compliance with drinking water standards / customer contacts about drinking water quality / volume of water saved through water efficiency / properties suffering supply interruptions > 3 hours / volume of water leaked / restrictions on water use / internal flooding incidents per 10,000 properties / flooding risk score.

Environment and Assets – EA's Environmental Performance Assessment / bathing water failures due to WWSL activities / Biodiversity Action Plan landholding assessed and managed / greenhouse gas emissions / proportion of electricity self-generated / all regulatory outputs met / compliance with abstraction licences / monitoring of CSO's presenting a risk to the environment / collapses and bursts on sewerage network.

Employees – RIDDOR incidents per 1,000 employees / employee rating company as a good employer / compliance with training plan / staff turnover / diversity plan progress as assessed by Corporate Responsibility Committee.

Target Bonus 2016-17	Colin Skellett Chief Executive	Mark Watts Director
Financial		
% of salary	10.0%	10.0%
Amount £	35,342	22,400
Customer		
% of salary	10.0%	10.0%
Amount £	35,342	22,400
Environment and Assets		
% of salary	10.0%	10.0%
Amount £	35,342	22,400
Employees		
% of salary	10.0%	10.0%
Amount £	35,342	22,400
Individual		
% of salary	10.0%	10.0%
Amount £	35,342	22,400
Total		
% of salary	50%	50%
Amount £	176,710	112,000

Long-term Incentive Plan from 1 April 2015

In September 2014, the Financial Reporting Council published a revised code of practice of the UK corporate governance code which introduced new provisions relating to executive remuneration, including a change that remuneration policies must be designed to promote the long term success of the Company.

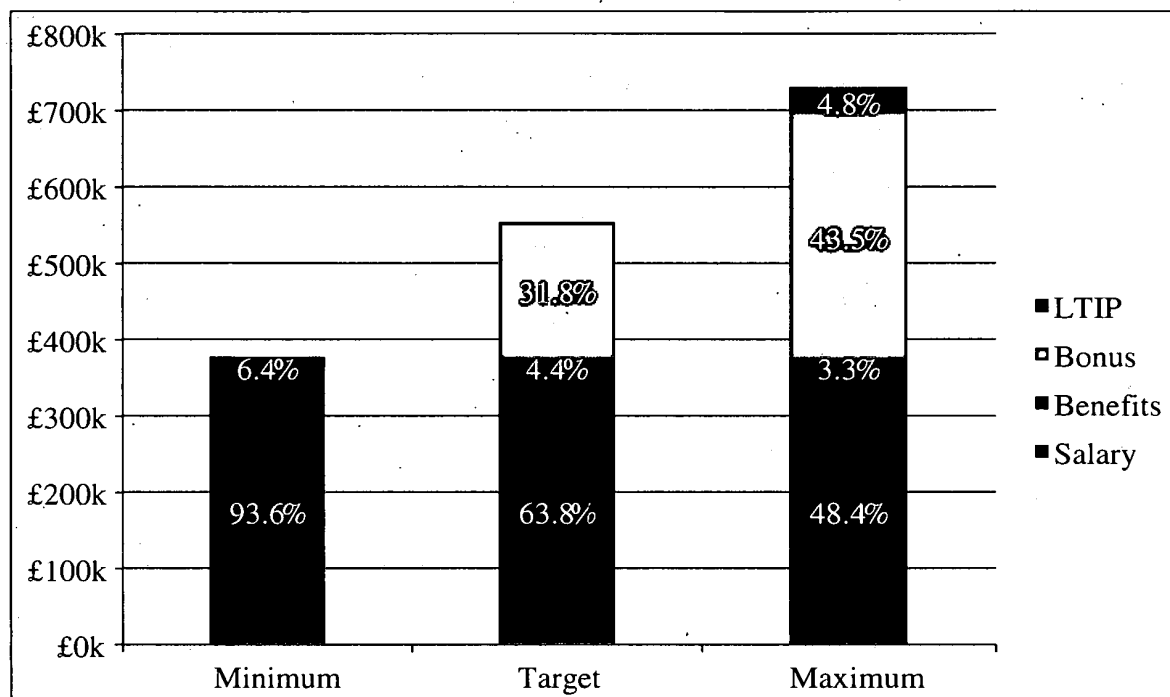
The Remuneration Committee approved the establishment of a long term incentive plan for Directors whereby 20% of any above target bonus element earned will be held back for payment at the end of AMP6 in 2020. The Company will match the value of the retained bonus payment, up to 100%. The long term incentive payment will be paid to Directors in April 2020.

The amount held back from Directors in the first year of the scheme was £10,608 from Colin Skellett and £8,000 for Mark Watts.

Governance Report *(continued)*

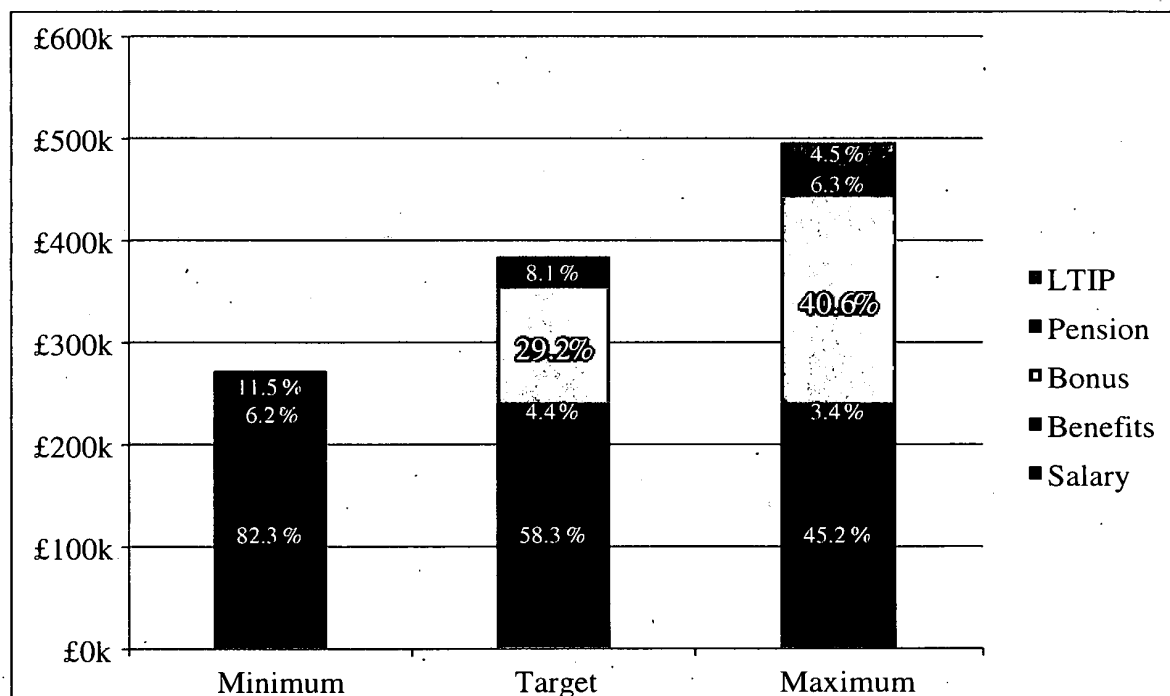
Illustrations of Remuneration Policy

A) Chief Executive Officer – Colin Skellett (using estimated 2016-17 data)



Minimum assumes no bonus earned, target assumes 50% bonus earned and maximum assumes 90% bonus and 10% LTIP earned. No employer pension contributions.

B) Director of Finance – Mark Watts (using estimated 2016-17 data)



Minimum assumes no bonus earned, target assumes 50% bonus earned and maximum assumes 100% bonus earned. No employer pension contributions.

Directors' Report

The Directors have pleasure in presenting their report and the audited statutory accounts (subsequently referred to as accounts) for the year to 30 June 2016.

The Directors consider the annual report and financial statements taken as a whole, to be fair, balanced and understandable and it provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

Principal Activities

The main activities of the Company are the supply of water and the treatment and disposal of waste water.

In December 2014 the industry regulator Ofwat announced the final price control determination for the five-year period to March 2020. The price control for this period has been extended from one price control to four price controls covering wholesale water, wholesale waste water, household retail and non-household retail.

The Directors accepted the price review for the next five years.

There was a price reduction imposed by Ofwat at 1 April 2015 of 5.9% offset by the increase in RPI at November 2014 of 2.05%, a net reduction of 3.85%.

At 1 April 2016 there was a price increase agreed by Ofwat of 0.8% increased by November RPI of 1.1%, a total increase of 1.9%.

Sustainability

Wessex Water Services Ltd has a sustainability vision that guides our progress towards being a sustainable water company. The sustainability vision is reviewed bi-annually.

Ethical Policy

We are determined to maintain our reputation as a Company that observes the highest standards of personal and corporate integrity by adhering to a strict code of business ethics. We aim to be the best and value everyone's contribution in our pursuit of excellence.

We are honest in the way we conduct our business. We treat one another, our customers and the environment with respect.

Employment

Wessex Water Services Ltd is an equal opportunities employer. No person or group of persons applying for a job with the Company is treated less favourably than any other person or groups of persons because of their gender, race, class, colour, nationality, ethnic origin, marital status, sexual orientation, age, trade union membership or activity, religious belief or physical or mental disability.

Selection procedures and criteria ensure that individuals are selected and promoted on the basis of their relevant merits and abilities. These procedures are monitored and regularly reviewed.

Where necessary, the Company provides staff with ongoing professional development to enable them to compete or qualify for positions, or to progress, within the Company.

The Modern Slavery Act 2015

Wessex Water is committed to meeting the aims of the Modern Slavery Act 2015. We strongly oppose slavery and human trafficking in our supply chains and in any part of our business. To be trusted to do the right thing is one of our core values. We would never knowingly engage with suppliers or contractors involved in slavery or human trafficking. In accordance with the requirements of the Act we have published on our website a Slavery and human trafficking statement 2016 signed by the chief executive and we have provided a prominent link to the statement on the home page.

Environmental Policy

Wessex Water Services Ltd protects conserves and improves the environment and operates in a socially responsible manner. Working practices are continually revised as improved techniques and technologies become available. The environment policy is reviewed annually.

Directors' Report (continued)

Research and Development

The Company carried out research and development in support of existing activities to improve the reliability and effectiveness of water and waste water services.

Market Value of Land and Buildings

In the opinion of the Directors, the market value of land and buildings of the Company exceeds the book value of these assets at 30 June 2016.

Supplier Payment Policy

The policy in respect of suppliers is to agree the payment terms for transactions in advance and to make payments in accordance with those terms. At 30 June 2016 trade creditors represented approximately 34 days of trade purchases (2015 – 37 days).

The Company does not follow any specific external code or standard on payment policy.

Charitable Donations


During the year £432,000 was donated to UK charities (2015 – £387,000).

Disclosure of Information to Auditor

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each Director has taken all the steps that ought to have been taken as a Director to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Auditor

A resolution to re-appoint KPMG LLP as auditor of the Company will be put to the forthcoming Board meeting.



By order of the Board
Leigh Fisher-Hoyle – General Counsel
Claverton Down
Bath BA2 7WW
9 September 2016

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE STRATEGIC REPORT, THE DIRECTORS' REPORT AND THE FINANCIAL STATEMENTS

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 they have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU and applicable law.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF WESSEX WATER SERVICES LIMITED

We have audited the financial statements of Wessex Water Services Limited for the year ended 30 June 2016 set out on pages 50 to 80. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 48, 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

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 30 June 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the EU; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or



Andrew Campbell-Orde (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
66 Queen Square,
Bristol, BS1 4BE
9 September 2016

Income Statement

For the year ended 30 June 2016

	<i>Note</i>	2016 £m	2015 £m
Revenue	2	<u>521.8</u>	<u>536.5</u>
Raw materials and consumables used		(31.6)	(32.2)
Staff costs		(56.5)	(59.4)
Depreciation, amortisation and disposal of tangible assets		(101.9)	(100.3)
Other expenses		<u>(101.2)</u>	<u>(99.2)</u>
Total expenses	3	<u>(291.2)</u>	<u>(291.1)</u>
Operating profit	2	<u>230.6</u>	<u>245.4</u>
Financial income	6	0.8	0.4
Financial expenses	6	<u>(74.3)</u>	<u>(77.3)</u>
Net financing expense		<u>(73.5)</u>	<u>(76.9)</u>
Profit before tax		157.1	168.5
Taxation	7	9.4	(33.2)
Profit for the year		<u>166.5</u>	<u>135.3</u>

Statement of Other Comprehensive Income
For the year ended 30 June 2016

	2016 £m	2015 £m
Profit for the year	166.5	135.3
Other comprehensive income		
<i>Items that will not be reclassified to profit or loss:</i>		
Re-measurements of defined benefit liability	(37.8)	(25.2)
Income tax on items that will not be reclassified to profit or loss	6.8	5.0
Other comprehensive income for the year, net of income tax	(31.0)	(20.2)
Total comprehensive income for the year	135.5	115.1

Balance Sheet

At 30 June 2016

	Note	2016 £m	2015 £m
Non-current assets			
Property, plant and equipment	9	3,362.9	3,258.6
Investments in subsidiaries	10	-	-
		<u>3,362.9</u>	<u>3,258.6</u>
Current assets			
Inventories	11	5.1	7.8
Trade and other receivables	12	181.8	183.0
Cash and cash equivalents	13	118.2	81.7
		<u>305.1</u>	<u>272.5</u>
Total assets		<u><u>3,668.0</u></u>	<u><u>3,531.1</u></u>
Current liabilities			
Other interest-bearing loans and borrowings	14	(5.0)	(4.5)
Trade and other payables	15	(181.2)	(164.6)
		<u>(186.2)</u>	<u>(169.1)</u>
Non-current liabilities			
Other interest-bearing loans and borrowings	14	(1,994.0)	(1,939.3)
Other payables	15	(0.4)	(0.4)
Employee benefits	16	(159.9)	(123.3)
Deferred income	17	(251.2)	(218.1)
Provisions	18	(0.2)	(1.7)
Deferred tax liabilities	19	(343.3)	(384.4)
		<u>(2,749.0)</u>	<u>(2,667.2)</u>
Total liabilities		<u><u>(2,935.2)</u></u>	<u><u>(2,836.3)</u></u>
Net assets		<u><u>732.8</u></u>	<u><u>694.8</u></u>
Equity			
Share capital	20	-	-
Retained earnings		<u>732.8</u>	<u>694.8</u>
Total equity		<u><u>732.8</u></u>	<u><u>694.8</u></u>

These financial statements were approved by the Board of Directors on 9 September 2016 and were signed on its behalf by:



Mark Watts - Director

Company registered number: 2366648

Statement of Changes in Equity

For the year ended 30 June 2016

	Note	Share capital £m	Retained earnings £m	Total equity £m
Balance at 1 July 2014		81.3	580.9	662.2
Total comprehensive income for the year				
Profit for the year		-	135.3	135.3
Other comprehensive income		-	(20.2)	(20.2)
Total comprehensive income for the year		-	115.1	115.1
Transactions with owners, recorded directly in equity				
Share capital reduction	20	(81.3)	81.3	-
Dividends	8	-	(82.5)	(82.5)
Total contributions by and distributions to owners		(81.3)	(1.2)	(82.5)
Balance at 30 June 2015		-	694.8	694.8
Balance at 1 July 2015		-	694.8	694.8
Total comprehensive income for the year				
Profit for the year		-	166.5	166.5
Other comprehensive income		-	(31.0)	(31.0)
Total comprehensive income for the year		-	135.5	135.5
Transactions with owners, recorded directly in equity				
Dividends	8	-	(97.5)	(97.5)
Total contributions by and distributions to owners		-	(97.5)	(97.5)
Balance at 30 June 2016		-	732.8	732.8

Included in retained earnings are £561.0m of un-distributable reserves (2015 - £552.5m) created on first time adoption of IFRS when restating infrastructure assets to fair value.

Cash Flow Statement

For the year ended 30 June 2016

	<i>Note</i>	2016	2015
		£m	£m
Cash flows from operating activities			
Profit for the year		166.5	135.3
<i>Adjustments for:</i>			
Depreciation, amortisation and disposal of tangible assets		101.9	100.3
Financial income		(0.8)	(0.4)
Financial expense		74.3	77.3
Taxation		(9.4)	33.2
		<u>332.5</u>	<u>345.7</u>
Decrease / (increase) in trade and other receivables		1.1	(4.5)
Decrease / (increase) in inventories		2.7	(1.1)
(Decrease) / increase in trade and other payables		(1.7)	7.8
(Decrease) in provisions and employee benefits		(7.5)	(5.0)
		<u>(5.4)</u>	<u>(2.8)</u>
Tax paid		(14.2)	(28.3)
Net cash from operating activities		<u>312.9</u>	<u>314.6</u>
Cash flows from investing activities			
Proceeds from sale of property, plant and equipment		1.2	1.0
Interest received		0.7	0.4
Acquisition of property, plant and equipment		(178.8)	(182.6)
Proceeds from infrastructure charges and capital contributions		9.3	6.7
Net cash from investing activities		<u>(167.6)</u>	<u>(174.5)</u>
Cash flows from financing activities			
Proceeds from new loan		50.0	150.0
Interest paid		(60.3)	(59.1)
Repayment of borrowings		-	(100.0)
Payment of finance lease liabilities		(4.5)	(25.6)
Dividends paid		(94.0)	(86.6)
Net cash from financing activities		<u>(108.8)</u>	<u>(121.3)</u>
Increase in cash and cash equivalents		36.5	18.8
Cash and cash equivalents at 1 July		81.7	62.9
Cash and cash equivalents at 30 June	<i>13,14</i>	<u>118.2</u>	<u>81.7</u>

Notes to the financial statements

1. Accounting policies

1.1 Basis of preparation

Wessex Water Services Limited is a Company incorporated and domiciled in the UK.

The Company financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs").

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

Judgements made by the Directors, in the application of these accounting policies, that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 28.

Group accounts have not been prepared as under section 400 of the Companies Act 2006 the Company and its subsidiary are included in the consolidated financial statements of Wessex Water Ltd (see note 26).

1.2 Measurement convention

The financial statements are prepared on the historical cost basis. Non-current assets and disposal groups held for sale are stated at the lower of previous carrying amount and fair value less costs to sell.

1.3 Going concern

The Directors have considered the financial position of the Company and have concluded that they will be able to meet their liabilities as they fall due for the foreseeable future. For these purposes the foreseeable future is taken to mean a period of at least 12 months from the date of approval of these accounts.

1.4 Foreign currency

Transactions in foreign currencies are translated into sterling at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are retranslated to the functional currency at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are retranslated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined.

1.5 Financial instruments

Investments

Investments held as fixed assets are stated at cost less any provision for impairment. Those held as current assets are stated at the lower of cost and net realisable value.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and bank deposits. Bank overdrafts that are repayable on demand and form an integral part of the Company's cash management are included as a component of cash and cash equivalents for the purpose only of the cash flow statement.

Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost using the effective interest method, less any impairment losses.

Notes to the financial statements

1. Accounting policies *(continued)*

1.6 *Property, plant and equipment*

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses.

Infrastructure assets have been revalued to fair value on 1 July 2013, the date of transition to Adopted IFRSs, and are measured on the basis of deemed cost, being the revalued amount at the date of that revaluation.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

Leases in which the Company assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. Where land and buildings are held under leases the accounting treatment of the land is considered separately from that of the buildings. Leased assets acquired by way of finance lease are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and less accumulated impairment losses.

Under IFRIC 18 sewers adopted at nil cost to the Company are included in fixed assets at a fair value, which is cost of construction and depreciated at the same rate as infrastructure assets.

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Land is not depreciated. The estimated useful lives are as follows:

- Buildings and operational assets 15 to 80 years
- Infrastructure assets 108 years
- Plant, machinery and vehicles 3 to 30 years
- Other assets 4 to 15 years

Infrastructure assets comprise 8 components whose weighted average life is 108 years:

Impounding reservoirs 150 years, raw water mains 100 years, treated water mains 100 years, communication pipes 60 years, sewers 125 years, sewage pumping stations 60 years, combined sewer overflows 80 years and sea outfalls 60 years.

Depreciation methods, useful lives and residual values are reviewed at each balance sheet date.

1.7 *Intangible assets and goodwill*

Goodwill

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is not amortised but is tested annually for impairment.

Research and development

Expenditure on research activities is recognised in the income statement as an expense as incurred.

1.8 *Investment property*

Investment properties are properties which are held either to earn rental income or for capital appreciation or for both. Investment properties are stated at cost less accumulated depreciation.

1.9 *Inventories*

Inventories are stated at the lower of cost and net realisable value. Cost is based on the first-in first-out principle and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads based on normal operating capacity.

Notes to the financial statements

1. Accounting policies *(continued)*

1.10 Impairment excluding inventories and deferred tax assets

Financial assets (including receivables)

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Non-financial assets

The carrying amounts of the Company's non-financial assets, other than inventories and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill, and intangible assets that have indefinite useful lives or that are not yet available for use, the recoverable amount is estimated each year at the same time.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

1.11 Employee benefits

Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Company's net obligation in respect of defined benefit pension plans and other post-employment benefits are calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets are deducted. The Company determines the net interest on the net defined benefit liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability.

The discount rate is the yield at the reporting date on bonds that have a credit rating of at least AA that have maturity dates approximating the terms of the Company's obligations and that are denominated in the currency in which the benefits are expected to be paid.

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which the Company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement in the periods during which services are rendered by employees.

Re-measurements arising from defined benefit plans comprise actuarial gains and losses and the return on plan assets. The Company recognises them immediately in other comprehensive income and all other expenses related to defined benefit plans in employee benefit expenses in profit or loss.

When the benefits of a plan are changed, or when a plan is curtailed, the portion of the changed benefit related to past service by employees, or the gain or loss on curtailment, is recognised immediately in profit or loss when the plan amendment or curtailment occurs.

The calculation of the defined benefit obligations is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Company, the recognised asset is limited to the present value of benefits available in the form of any future refunds from the plan or reductions in future contributions and takes into account the adverse effect of any minimum funding requirements.

The Company's employees are members of the Wessex Water Ltd Group pension scheme. The Company recognises a cost equal to its contribution payable for the period. The assets of the scheme are held separately from those of the Group. The scheme has been closed to new members since 2009.

Notes to the financial statements

1. Accounting policies *(continued)*

1.11 Employee benefits *(continued)*

Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Company has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

Share-based payment transactions

YTL Power International Berhad operates an equity settled share-based payment scheme for the employees of the group. The fair value of the share-based payment awards is recognised as an expense over the period of the award. The amount recognised is adjusted to reflect the actual number of awards for which service and performance conditions are met at the vesting date. Where YTL Power International Berhad grants rights to its equity instruments to the Company's employees, they are accounted for as equity settled in the consolidated accounts. In the Company accounts they are accounted for as a charge to the profit and loss account and an inter-company liability.

1.12 Provisions

A provision is recognised in the balance sheet when the Company has a present legal or constructive obligation as a result of a past event, that can be reliably measured and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects risks specific to the liability.

1.13 Revenue

Turnover represents income receivable in the ordinary course of business, excluding VAT, for services provided. Turnover is recognised to the extent that it is probable that economic benefits will flow to the Company. For measured customers turnover includes an estimate of the sales value of units consumed between the last meter reading and the end of the period. Where premises are unoccupied or where no services are provided, charges are not raised and no turnover is recognised.

1.14 Deferred income

Grants and contributions in respect of specific expenditure on non-infrastructure fixed assets are treated as deferred income and recognised in the profit and loss account over the expected useful economic lives of the related assets.

Grants and contributions relating to infrastructure assets are amortised over 108 years.

Under IFRIC 18 sewers adopted at nil cost to the Company are shown in deferred income at a fair value, which is cost of construction, and amortised at the same rate as infrastructure assets are depreciated.

1.15 Bad debt policy

Debt is written off for one of four reasons;

- It is considered or known to be uncollectible
- It is considered uneconomic to collect
- Older debt is written off by agreement with the customer in return for the receipt of monthly payments to pay-off current year debt as part of our "Restart" and "Restart Plus" policies
- Write off is ordered by the County Court. In these cases the Court may set payment at a proportion of the outstanding debt. When this level of payment is reached the Court will instruct that the rest is to be written off.

The policy for calculating the bad debt provision is to analyse the outstanding debt between payment categories and to make provision according to the historical non collection rate for that payment category. The categories selected are direct debit, instalments, standing orders, DSS, bankruptcy and all other. The profile of provision differs between categories, but for all categories debt that is 4 years old is fully provided.

Notes to the financial statements

1. Accounting policies *(continued)*

1.16 Expenses

Operating lease payments

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

Finance lease payments

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Financing income and expenses

Financing expenses comprise interest payable, finance charges on shares classified as liabilities and finance leases recognised in profit or loss using the effective interest method, unwinding of the discount on provisions, and net foreign exchange losses that are recognised in the income statement (see foreign currency accounting policy). Borrowing costs that are directly attributable to the acquisition, construction or production of an asset that takes a substantial time to be prepared for use, are capitalised as part of the cost of that asset. Financing income comprises interest receivable on funds invested, dividend income, and net foreign exchange gains.

Interest income and interest payable is recognised in profit or loss as it accrues, using the effective interest method. Dividend income is recognised in the income statement on the date the entity's right to receive payments is established. Foreign currency gains and losses are reported on a net basis.

1.17 Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit other than in a business combination; and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised.

1.18 Non-current assets held for sale and discontinued operations

A non-current asset or a group of assets containing a non-current asset (a disposal group) is classified as held for sale if its carrying amount will be recovered principally through sale rather than through continuing use, it is available for immediate sale and sale is highly probable within one year.

A discontinued operation is a component of the Company's business that represents a separate major line of business or geographical area of operations that has been disposed of or is held for sale, or is a subsidiary acquired exclusively with a view to resale. Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier. When an operation is classified as a discontinued operation, the comparative income statement is restated as if the operation has been discontinued from the start of the comparative period.

1.19 Dividends

Dividends are proposed by the board and immediately afterwards are authorised by the shareholder, and are therefore recognised as a liability in the accounts until paid.

Notes to the financial statements

1. Accounting policies *(continued)*

1.20 *Adopted IFRS not yet applied*

The following Adopted IFRSs have been issued but have not been applied in these financial statements:

- IFRS 9 Financial Instruments (mandatory for years commencing on or after 1 January 2018)
- IFRS 14 Regulatory Deferral Accounts (mandatory for years commencing on or after 1 January 2016)
- IFRS 15 Revenue from Contracts with Customers (mandatory for years commencing on or after 1 January 2017)
- IFRS 16 Leases (Mandatory for years commencing on or after 1 January 2019)
- Amendments to IAS 16 and IAS 28 Clarification of Acceptable Methods of Depreciation and Amortisation
- Amendment to IFRS 11 Accounting for Acquisitions of Interests in Joint Operations
- Annual improvements to IFRS's 2012-14 Cycle (mandatory for years commencing on or after 1 January 2016)
- Disclosure initiative – Amendments to IAS 1 (mandatory for years commencing on or after 1 January 2016).

The Company does not currently expect that adoption of these standards will have a significant effect on the results or financial position of the Company, but may affect disclosure requirements.

Notes to the financial statements

2 Segmental analysis

	2016 £m	2015 £m
<i>Turnover</i>		
Regulated	513.8	529.2
Unregulated	8.0	7.3
	<u>521.8</u>	<u>536.5</u>
 <i>Operating profit</i>		
Regulated	230.6	245.4
Unregulated	-	-
	<u>230.6</u>	<u>245.4</u>
 <i>Net assets</i>		
Regulated	732.8	694.8
Unregulated	-	-
	<u>732.8</u>	<u>694.8</u>

3 Expenses and auditor's remuneration

Included in profit are the following:

	2016 £m	2015 £m
Impairment loss on other trade receivables and prepayments	11.7	12.0
Research and development expensed as incurred	0.1	0.1
	<u>11.8</u>	<u>12.1</u>
 <i>Auditor's remuneration:</i>		
Audit of these financial statements	156	156
Taxation compliance services	9	10
AMP6 price review services	-	18
Other costs	-	182
	<u>165</u>	<u>366</u>

Notes to the financial statements *(continued)*

4 Staff numbers and costs

The average number of employees (including Directors) during the year was as follows:

	Number of employees	
	2016	2015
Average number of employees	<u>2,012</u>	<u>1,921</u>

The aggregate payroll costs of these employees was:

	2016	2015
	£m	£m
Wages and salaries	71.5	71.5
Social security costs	7.0	6.4
Pension costs	11.0	11.3
	<u>89.5</u>	<u>89.2</u>

These costs were allocated as follows:

Capital schemes	33.0	29.8
Operating expenses	56.5	59.4
	<u>89.5</u>	<u>89.2</u>

5 Directors' remuneration

	2016	2015
	£'000	£'000
Total Directors' remuneration including benefits in kind	<u>1,309</u>	<u>1,152</u>
Remuneration of highest paid Director	<u>603</u>	<u>510</u>

Details of Directors' remuneration can be found in the Governance Report. Directors' remuneration is in respect of two Executive Directors, five Non-Executive Directors and five YTL appointed Directors (2015 - two Executive Directors, five Non-Executive Directors and five YTL appointed Directors).

Notes to the financial statements *(continued)*

6 Finance income and expense

Recognised in the income statement

	2016	2015
	£m	£m
<i>Finance income</i>		
Interest receivable on short-term bank deposits	0.8	0.4
Total finance income	<u>0.8</u>	<u>0.4</u>
<i>Finance expense</i>		
To fellow subsidiary undertakings	(64.3)	(68.6)
Net interest on net defined benefit pension plan liability	(4.6)	(4.3)
On bank loans and leases	<u>(5.4)</u>	<u>(4.4)</u>
	<u>(74.3)</u>	<u>(77.3)</u>
Net interest payable	<u>(73.5)</u>	<u>(76.9)</u>

In accordance with IAS 23 borrowing costs of £1.5m (2015 - £2.2m) associated with the funding of eligible capital projects have been capitalised at an interest rate of 3.9% (2015 – 4.0%).

7 Taxation

Recognised in the income statement

	2016	2015
	£m	£m
<i>Current tax expense</i>		
Current year	27.7	16.4
Adjustments for prior years	<u>(3.1)</u>	<u>(1.9)</u>
Current tax expense	<u>24.6</u>	<u>14.5</u>
<i>Deferred tax expense</i>		
Origination and reversal of temporary differences	2.0	18.1
Reduction in tax rate	(38.1)	-
Adjustments for prior years	<u>2.1</u>	<u>0.6</u>
Deferred tax (credit) / expense	<u>(34.0)</u>	<u>18.7</u>
Tax (credit) / expense in income statement	<u>(9.4)</u>	<u>33.2</u>

Notes to the financial statements *(continued)*

7 Taxation *(continued)*

Income tax recognised in other comprehensive income

	2016 £m	2015 £m
Re-measurements of defined benefit liability	6.8	5.0
Change in tax rate	-	-
Tax credit	<u>6.8</u>	<u>5.0</u>

Reconciliation of effective tax rate

	2016 £m	2015 £m
Profit for the year	166.5	135.3
Total tax (credit) / debit	<u>(9.4)</u>	<u>33.2</u>
Profit excluding taxation:	157.1	168.5
Tax using the UK corporation tax rate of 20% (2015 - 20.75%)	31.4	35.0
Reduction of tax rate on deferred tax balances	(38.1)	-
Non-deductible expenses	0.1	0.4
(Over) provided in prior years	(0.9)	(1.4)
Group relief for nil consideration	(1.3)	(1.4)
Other	<u>(0.6)</u>	<u>0.6</u>
Total tax (credit) / debit	<u>(9.4)</u>	<u>33.2</u>

Reductions in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017) and 18% (effective from 1 April 2020) were substantively enacted on 26 October 2015. A further reduction to the UK Corporation Tax rate was announced in the 2016 Budget to further reduce the tax rate to 17% (effective from 1 April 2020). These reductions will reduce the company's future current tax charge accordingly. The deferred tax liability at 30 June 2016 has been calculated based on the rate of 18% substantively enacted at the balance sheet date.

8 Dividends

The dividend policy is to declare dividends consistent with the Company's performance and prudent management of the economic risk of the business.

	2016 £m	2015 £m
Interim dividends for the current year	76.5	65.0
Final dividend for the current year	<u>21.0</u>	<u>17.5</u>
	<u>97.5</u>	<u>82.5</u>

Notes to the financial statements *(continued)***9 Property, plant and equipment**

	Land & buildings £m	Infra- structure assets £m	Plant, equipment & vehicles £m	Office & IT equipment £m	Company total £m
Cost					
Balance at 1 July 2014	827.6	1,835.8	1,436.4	30.0	4,129.8
Additions	21.7	95.6	82.7	3.0	203.0
Disposals	(0.5)	(1.5)	(25.2)	(8.0)	(35.2)
Balance at 30 June 2015	848.8	1,929.9	1,493.9	25.0	4,297.6
Balance at 1 July 2015	848.8	1,929.9	1,493.9	25.0	4,297.6
Additions	15.3	74.0	118.8	1.8	209.9
Disposals	(1.0)	(1.5)	(11.3)	-	(13.8)
Balance at 30 June 2016	863.1	2,002.4	1,601.4	26.8	4,493.7
Depreciation and impairment					
Balance at 1 July 2014	(243.2)	(15.6)	(692.7)	(19.4)	(970.9)
Depreciation charge for the year	(14.2)	(16.6)	(68.5)	(1.0)	(100.3)
Disposals	0.3	-	23.9	8.0	32.2
Balance at 30 June 2015	(257.1)	(32.2)	(737.3)	(12.4)	(1,039.0)
Balance at 1 July 2015	(257.1)	(32.2)	(737.3)	(12.4)	(1,039.0)
Depreciation charge for the year	(14.2)	(17.6)	(68.1)	(2.7)	(102.6)
Disposals	0.4	-	10.4	-	10.8
Balance at 30 June 2016	(270.9)	(49.8)	(795.0)	(15.1)	(1,130.8)
Net Book Value					
At 1 July 2014	584.4	1,820.2	743.7	10.6	3,158.9
At 30 June 2015	591.7	1,897.7	756.6	12.6	3,258.6
At 30 June 2016	592.2	1,952.6	806.4	11.7	3,362.9

Notes to the financial statements

9 Property, plant and equipment (continued)

Infrastructure assets comprise a network of systems of mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines, sea outfalls and infrastructure investigations and studies.

Included in infrastructure assets at 1 July 2014 is £703.5m fair value adjustment on first time adoption of IFRS.

There is no impairment loss recognised in these financial statements.

At 30 June 2016 the net book value of leased plant and machinery was £13.5m (2015 - £17.4m). The leased equipment secures lease obligations (see note 14).

Assets under construction included in the values above were £193.1m (2015 - £110.8m).

Cumulative borrowing costs capitalised and included above were £5.0m (2015 - £3.5m).

Included in freehold land and buildings above is an amount of £12.3m (2015 - £12.2m) in respect of land which is not depreciated.

10 Investments in subsidiaries

The Company has an investment of £13,000 (2015 – £13,000) in 100% of the ordinary share capital of a subsidiary company Wessex Water Services Finance Plc.

11 Inventories

	2016 £m	2015 £m
Raw materials and consumables	3.0	3.3
Work in progress	2.1	4.5
	<u>5.1</u>	<u>7.8</u>

Raw materials, consumables and work in progress recognised as "Other expenses" in the year amounted to £3.2m (2015 - £4.3m). There was no write-down of inventories to net realisable value in either year.

12 Trade and other receivables

	2016 £m	2015 £m
Trade receivables	62.5	66.7
Owed by fellow subsidiary company	38.2	35.1
Prepayments and accrued income	76.3	76.1
Other debtors	4.8	5.1
	<u>181.8</u>	<u>183.0</u>

13 Cash and cash equivalents

	2016 £m	2015 £m
Short-term bank deposits	112.0	71.6
Cash at bank	6.2	10.1
	<u>118.2</u>	<u>81.7</u>

Notes to the financial statements (continued)

14 Other interest-bearing loans and borrowings

This note provides information about the contractual terms of the Company's interest-bearing loans and borrowings, which are measured at amortised cost. For more information about the Company's exposure to interest rate and foreign currency risk, see note 21.

	2016 £m	2015 £m
Non-current liabilities		
Bank loans	415.0	365.0
Finance lease liabilities	6.9	11.9
Inter-company loans	<u>1,572.1</u>	<u>1,562.4</u>
	<u>1,994.0</u>	<u>1,939.3</u>
Current liabilities		
Bank overdraft	-	-
Current portion of finance lease liabilities	<u>5.0</u>	<u>4.5</u>
	<u>5.0</u>	<u>4.5</u>

Terms and debt repayment schedule

	Currency	Nominal interest rate	Year of maturity	Face value 2016 £m	Carrying amount 2016 £m	Face value 2015 £m	Carrying amount 2015 £m
Bank loans	Sterling		2018-2024	415.0	415.0	365.0	365.0
<i>Inter-company loans</i>							
Bond	Sterling	5.375%	2028	198.7	198.3	198.6	198.3
Bond	Sterling	5.75%	2033	346.9	345.9	346.7	345.7
Bond	Sterling	4.00%	2021	198.6	198.6	198.3	198.3
Bond	Sterling	4.00%	2021	104.8	104.8	105.8	105.8
Index Linked Bond	Sterling	3.52%	2023	74.4	74.4	73.2	73.2
Index Linked Bond	Sterling	2.186%	2039	61.0	61.0	60.0	60.0
Index Linked Bond	Sterling	1.75%	2046	100.1	100.1	98.5	98.5
Index Linked Bond	Sterling	1.75%	2051	100.0	100.0	98.5	98.5
Index Linked Bond	Sterling	1.369%	2057	100.0	100.0	98.5	98.5
Index Linked Bond	Sterling	1.374%	2057	100.0	100.0	98.4	98.4
Index Linked Bond	Sterling	1.489%	2058	63.0	63.0	62.4	62.4
Index Linked Bond	Sterling	1.495%	2058	63.0	63.0	62.4	62.4
Index Linked Bond	Sterling	1.499%	2058	63.0	63.0	62.4	62.4
				<u>1,988.5</u>	<u>1,987.1</u>	<u>1,928.7</u>	<u>1,927.4</u>

Notes to the financial statements

14 Other interest-bearing loans and borrowings (continued)

Finance lease liabilities

Finance lease liabilities are payable as follows:

	Minimum lease payments	Interest	Principal	Minimum lease payments	Interest	Principal
	2016	2016	2016	2015	2015	2015
	£m	£m	£m	£m	£m	£m
Less than one year	5.4	(0.4)	5.0	5.3	(0.8)	4.5
Between one and five years	7.3	(0.4)	6.9	12.8	(0.9)	11.9
	<u>12.7</u>	<u>(0.8)</u>	<u>11.9</u>	<u>18.1</u>	<u>(1.7)</u>	<u>16.4</u>

15 Trade and other payables

	2016	2015
	£m	£m
Current		
Amounts payable to subsidiary company	31.1	30.9
Amounts payable to other group companies	0.6	0.6
Amounts owed to associate companies	0.7	-
Trade payables	14.8	16.0
Dividend	21.0	17.5
Other creditors	2.5	2.6
Corporation tax	14.0	3.6
Taxation and social security	2.3	2.0
Accruals and deferred income	<u>94.2</u>	<u>91.4</u>
	<u>181.2</u>	<u>164.6</u>
Non-current		
Other payables	<u>0.4</u>	<u>0.4</u>
	<u>181.6</u>	<u>165.0</u>

Notes to the financial statements *(continued)*

16 Employee benefits

Pension plans

	2016 £m	2015 £m
Fair value of scheme assets	544.1	516.1
Present value of defined benefit obligations	(702.8)	(638.2)
Net (liability) for defined benefit obligations	(158.7)	(122.1)
Unfunded and compensatory added years pension	(1.2)	(1.2)
Total employee benefits	(159.9)	(123.3)

The Company sponsors a funded defined benefit pension plan for qualifying UK employees. The plan is administered by a separate board of Trustees which is legally separate from the Company. The Trustees are composed of representatives of both the employer and employees. The Trustees are required by law to act in the interest of all relevant beneficiaries and are responsible for the investment policy with regard to the assets plus the day to day administration of the benefits.

Under the plan, employees are entitled to annual pensions on retirement using an accrual rate, final pensionable salary and service. Benefits are also payable on death and following other events such as withdrawing from active service.

No other post-retirement benefits are provided to these employees.

Liabilities for an unfunded arrangement and a compensatory payment for added years' service are held outside the defined benefit scheme. The Company also operates a defined contribution section within the main pension scheme.

a. Profile of the Scheme

The defined benefit obligation includes benefits for current employees, former employees and current pensioners. Broadly, about 38% of the liabilities are attributable to current employees, 16% to former employees and 46% to current pensioners. The Scheme duration is an indicator of the weighted-average time until benefit payments are made. For the Scheme as a whole, the duration is around 18 years reflecting the approximate split of the defined benefit obligation between current employees (duration of 25 years), deferred members (duration of 25 years) and current pensioners (duration of 12 years).

b. Funding requirements

UK legislation requires that pension schemes are funded prudently. The last funding valuation of the Scheme was carried out by a qualified actuary as at 30 September 2013 and showed a deficit of £94.6 million. The Company is paying deficit contributions of:

- £8.6M by 31 March 2014 and 31 March 2015;
- £7.6M by each 31 March, from 31 March 2016 to 31 March 2020 inclusive;
- £10.2M by each 31 March, from 31 March 2021 to 31 March 2024 inclusive;

which, along with investment returns from return-seeking assets, is expected to make good this shortfall by 31 March 2024.

The next funding valuation is due no later than 30 September 2016 at which progress towards full-funding will be reviewed.

The Company also pays contributions of 18.2% of pensionable salaries in respect of current accrual and non-investment related expenses, with active members paying a further 7.3% of pensionable salaries on average. A contribution of £7.6m is expected to be paid by the Company during the year ending on 30 June 2017.

c. Risks associated with the Scheme

Asset volatility - The liabilities are calculated using a discount rate set with reference to corporate bond yields; if assets underperform this yield, this will create a deficit. The Scheme holds a significant proportion of growth assets (equities, diversified growth fund and global absolute return fund) which, though expected to outperform corporate bonds in the long-term, create volatility and risk in the short-term. The allocation to growth assets is monitored to ensure it remains appropriate given the Scheme's long term objectives.

Notes to the financial statements

16 Employee benefits (continued)

Changes in bond yields - A decrease in corporate bond yields will increase the value placed on the Scheme's liabilities for accounting purposes, although this will be partially offset by an increase in the value of the Scheme's bond holdings.

Inflation risk - The majority of the Scheme's benefit obligations are linked to inflation and higher inflation will lead to higher liabilities (although, in most cases, caps on the level of inflationary increases are in place to protect against extreme inflation). The majority of the assets are either unaffected by or only loosely correlated with inflation, meaning that an increase in inflation will also increase the deficit.

Life expectancy - The majority of the Scheme's obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the liabilities.

The Trustees insure certain benefits payable on death before retirement.

A contingent liability exists in relation to the equalisation of Guaranteed Minimum Pension ("GMP"). The UK Government intends to implement legislation which could result in an increase in the value of GMP for males. This would increase the defined benefit obligation of the plan. At this stage, it is not possible to quantify the impact of this change.

d. Reporting at 30 June 2016

The results of the latest funding valuation at 30 September 2013 have been adjusted to the balance sheet date taking account of experience over the period since 30 September 2013, changes in market conditions, and differences in the financial and demographic assumptions. The present value of the defined benefit obligation, and the related current service cost, were measured using the Projected Unit Cost Method.

The principal assumptions used to calculate the liabilities under IAS 19 are set out below:

The major assumptions used by the actuary were:

	30.06.16	30.06.15
Rate of increase in salaries – year 1	1.6%	0.75%
Rate of increase in salaries – years 2 to 3 (2015 years 2 to 4)	2.8 %	2.50%
Rate of increase in salaries – long term	3.3 %	3.70%
Rate of increase in pensions in payment	1.8 % or 2.7 %	2.2% or 3.1%
Rate of increase in pensions in payment - reduced level members	2.0 %	2.3%
Discount rate	2.9 %	3.8%
Inflation assumption – RPI	2.8 %	3.2%
Inflation assumption – CPI	1.8 %	2.2%

The mortality assumptions are based upon the recent actual mortality experience of Scheme members, and allow for expected future improvements in mortality rates. The assumptions are that a member currently aged 60 will live, on average, for a further 27.0 years (2015 – 27.2 years) if they are male, and for a further 29.3 years (2015 – 29.5 years) if they are female. For a member who retires in 2036 at age 60 the assumptions are that they will live, on average, for a further 28.4 years (2015 – 28.8 years) after retirement if they are male, and a further 30.9 years (2015 – 31.1 years) after retirement if they are female.

The mortality table adopted is based upon 95% of standard tables S1P(M/F)A adjusted to allow for individual years of birth. Future improvements are assumed to be in line with the CMI 2015 core projection, with a long term improvement rate of 1.0% p.a. for all members.

Sensitivity analysis:

The key assumptions used for IAS 19 are: discount rate, inflation and mortality. If different assumptions are used, this could have a material effect on the results disclosed. The sensitivity of the results to these assumptions are set out below. For the purposes of these sensitivities it has been assumed that the change in the discount rate and inflation has no impact on the value of Scheme assets.

- A reduction in the discount rate of 0.1% from 2.9% to 2.8% would increase the scheme liabilities by £13.2 m from £702.8m to £716.0m, increasing the scheme deficit to £171.9m
- An increase in the inflation assumption of 0.1% (from 1.8% to 1.9% for CPI and 2.8% to 2.9% for RPI) would increase the scheme liabilities by £11.4m from £702.8m to £714.2m, increasing the scheme deficit to £170.1m
- An increase in life expectancy of 1 year would increase the scheme liabilities by £25.1m from £702.8m to £727.9m, increasing the scheme deficit to £183.8m.

Notes to the financial statements

16 Employee benefits (continued)

e. The value of the assets as follows:

	2016	2015
	£m	£m
Equities	251.9	261.2
Property	28.8	27.0
Government Bonds	145.1	129.4
Corporate Bonds	117.4	98.3
Other	0.9	0.2
	<u>544.1</u>	<u>516.1</u>

f. The amounts recognised in comprehensive income are set out below:

	2016	2015
	£m	£m
Operating cost – service cost		
Current service cost	10.9	10.1
Administration expenses	0.5	0.4
Past service cost	0.1	1.2
Financing cost		
Interest on net benefit liability	4.6	4.3
Pension cost recognised in profit and loss	<u>16.1</u>	<u>16.0</u>
Re-measurements in Other Comprehensive Income (OCI)		
Return on plan assets in excess of that recognised in net interest	(12.0)	(30.1)
Actuarial losses due to changes in financial assumptions	64.0	62.2
Actuarial gains due to changes in demographic assumptions	(7.8)	-
Actuarial gains due to liability experience	(6.4)	(6.9)
Pension cost recognised in OCI	<u>37.8</u>	<u>25.2</u>
Total amount recognised in profit and loss and OCI	<u>53.9</u>	<u>41.2</u>

g. Changes to the present value of the defined benefit obligations during the year:

	2016	2015
	£m	£m
Opening defined benefit obligation	638.2	566.5
Current service cost	10.9	10.1
Interest expense on defined benefit obligation	24.1	24.8
Contributions by scheme participants	0.2	0.2
Actuarial gains due to changes in demographic assumptions	(7.8)	-
Actuarial losses due to changes in financial assumptions	64.0	62.2
Actuarial gains due to liability experience	(6.4)	(6.9)
Net benefits paid out	(20.5)	(19.9)
Past service cost	0.1	1.2
Closing defined benefit obligation	<u>702.8</u>	<u>638.2</u>

Notes to the financial statements

16 Employee benefits (continued)

h. Changes to the fair value of scheme assets during the year:

	2016 £m	2015 £m
Opening fair value of scheme assets	516.1	467.7
Interest income on scheme assets	19.5	20.4
Re-measurement gains on scheme assets	12.0	30.1
Contributions by employer	17.3	18.0
Contributions by scheme participants	0.2	0.2
Net benefits paid out	(20.5)	(19.9)
Administration costs incurred	(0.5)	(0.4)
Closing fair value of scheme assets	<u>544.1</u>	<u>516.1</u>

i. Additional analysis:

Actual return on scheme assets

Interest income on scheme assets	19.5	20.4
Re-measurement gains on scheme assets	12.0	30.1
Actual return on scheme assets	<u>31.5</u>	<u>50.5</u>

Analysis of amounts recognised in Other Comprehensive Income

Total re-measurement losses	<u>(37.8)</u>	<u>(25.2)</u>
Total loss	<u>(37.8)</u>	<u>(25.2)</u>

History of asset values, defined benefit obligations, deficit in the scheme and experience gains and losses

	30.06.16 £m	30.06.15 £m	30.06.14 £m	30.06.13 £m	30.06.12 £m
Fair value of scheme assets	544.1	516.1	467.7	422.1	380.8
Defined benefit obligation	(702.8)	(638.2)	(566.5)	(536.0)	(516.6)
Deficit in the scheme	<u>(158.7)</u>	<u>(122.1)</u>	<u>(98.8)</u>	<u>(113.9)</u>	<u>(135.8)</u>
Experience gains on scheme assets	12.0	30.1	26.0		
Experience gains / (losses) on scheme liabilities	6.4	6.9	(9.7)		

Defined contribution plans

The Group also operates a defined contribution pension plan.

The total expense relating to this plan in the current year was £2.0m (2015 - £1.8m).

Notes to the financial statements

16 Employee benefits (continued)

Share-based payments

YTL Power International Berhad (a subsidiary of the ultimate parent company YTL Corporation Berhad) operates share option schemes under which options are granted to employees of the Company. The current scheme the "YTL Power International Berhad Employees Share Option Scheme 2011" first issued share options to employees on 1 June 2012. The terms of the 2011 scheme are specified under the YTL Power International Berhad Employees Share Option Scheme 2011 (2011 UK part) known as the "2011 UK Plan".

The majority of options have been issued under terms approved by the Inland Revenue, the "Approved" scheme, but some have been issued to senior employees under an "Unapproved" scheme. The options are for ordinary shares of YTL Power International Berhad of Malaysian Ringgit RM0.50 each.

2011 UK Plan

The exercise price and fair value of the share options are as follows:

Granted – Ordinary shares of RM0.50 each	Vesting date	Expiry date	Exercise price RM	Fair value RM
01/06/2012 Unapproved	01/06/2015	31/03/2021	1.41	0.22
01/06/2012 Approved	01/06/2015	31/03/2021	1.65	0.16

Under IFRS 2 equity settled share-based payments are measured at the fair value at the date of the grant, and the fair value is expensed on a straight line basis over the vesting period. There was no charge recognised in the profit and loss account for IFRS 2 as the share options have passed their vesting date. The key assumptions were as follows:

Scheme	Weighted ave. share price at grant RM	Expected volatility %	Expected option life years	Risk free rate %	Dividend yield %
01/06/2012 Unapproved	1.63	21.2	3	3.14	5.6
01/06/2012 Approved	1.63	21.2	3	3.14	5.6

The following options were outstanding at 30 June 2015 and 30 June 2016:

Granted – Ordinary shares of RM0.50 each	Outstanding at 30 June 2015	Granted	Forfeited	Exercised	Outstanding at 30 June 2016
01/06/2012 Unapproved	7,947,000	0	(39,000)	(13,000)	7,895,000
01/06/2012 Approved	39,041,000	0	(985,000)	(20,000)	38,036,000
TOTAL	46,988,000	0	(1,024,000)	(33,000)	45,931,000

The share price at 30 June 2016 was RM1.41 or £0.26.

Notes to the financial statements *(continued)*

17 Deferred income

	Above ground grants £m	Below ground grants £m	Sewer adoptions £m	Total £m
Balance at 1 July 2014	8.1	147.0	31.2	186.3
Received during the year	0.5	8.0	25.5	34.0
Amortisation	(0.3)	(1.4)	(0.5)	(2.2)
	<u>8.3</u>	<u>153.6</u>	<u>56.2</u>	<u>218.1</u>
Balance at 30 June 2015	8.3	153.6	56.2	218.1
Received during the year	1.0	8.7	25.9	35.6
Amortisation	(0.3)	(1.5)	(0.7)	(2.5)
	<u>9.0</u>	<u>160.8</u>	<u>81.4</u>	<u>251.2</u>
Balance at 30 June 2016	9.0	160.8	81.4	251.2

18 Provisions

	Restructuring £m	Total £m
Balance at 1 July 2015	1.7	1.7
Provisions made during the year	-	-
Provisions used during the year	(1.5)	(1.5)
	<u>0.2</u>	<u>0.2</u>
Balance at 30 June 2016	0.2	0.2
Non-current	-	-
Current	0.2	0.2
	<u>0.2</u>	<u>0.2</u>
Balance at 30 June 2016	0.2	0.2

The restructuring provision is in respect of a reorganisation announced before the prior year-end, delivering efficiencies in the first year of the AMP 6 price review period. Full consultation has taken place and termination dates are in the first quarter of the new financial year.

Notes to the financial statements *(continued)*

19 Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Liabilities		Assets		Net	
	2016 £m	2015 £m	2016 £m	2015 £m	2016 £m	2015 £m
Property, plant and equipment	542.0	571.3	(169.8)	(162.1)	372.2	409.2
Employee benefits	-	-	(28.8)	(24.7)	(28.8)	(24.7)
Provisions	(0.1)	(0.1)	-	-	(0.1)	(0.1)
Tax liabilities / (assets)	541.9	571.2	(198.6)	(186.8)	343.3	384.4
Net of tax liabilities / (assets)	-	-	-	-	-	-
Net tax liabilities / (assets)	541.9	571.2	(198.6)	(186.8)	343.3	384.4

Movement in deferred tax during the year

	1 July 2015 £m	Recognised in income £m	Recognised in equity £m	30 June 2016 £m
Property, plant and equipment	409.2	(37.0)	-	372.2
Employee benefits	(24.7)	2.7	(6.8)	(28.8)
Provisions	(0.1)	-	-	(0.1)
	384.4	(34.3)	(6.8)	343.3

Movement in deferred tax during the prior year

	1 July 2014 £m	Recognised in income £m	Recognised in equity £m	30 June 2015 £m
Property, plant and equipment	391.0	18.2	-	409.2
Employee benefits	(20.1)	0.4	(5.0)	(24.7)
Provisions	(0.2)	0.1	-	(0.1)
	370.7	18.7	(5.0)	384.4

Notes to the financial statements *(continued)***20 Capital and reserves**

	2016	2015
	£	£
Issued at 1 April	1	81,350,000
Share capital reduction	-	(81,349,999)
	<hr/>	<hr/>
Issued at 31 March	1	1
	<hr/>	<hr/>
<i>Allotted, called up and fully paid</i>		
Ordinary shares of £1 each	1	1
	<hr/>	<hr/>
	1	1
	<hr/>	<hr/>
Shares classified as liabilities	-	-
Shares classified in shareholders' funds	1	1
	<hr/>	<hr/>
	1	1
	<hr/>	<hr/>

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

On 30 March 2015 the Directors of the Company approved a capital reduction of 81,349,999 £1 ordinary shares which increased retained earnings. To enable the capital reduction to be undertaken the Directors prepared a Solvency Statement declaring that following the capital reduction the Company would be able to meet its debts / liabilities as they fell due over the next 12 months.

21 Financial instruments**(a) Fair values of financial instruments**

Fair value is the amount at which a financial instrument could be exchanged in an arms-length transaction between informed and willing parties, other than a forced or liquidation sale. The fair value of short term and floating rate borrowings approximate to book value. The fair value of long term fixed rate borrowings has been calculated using market values or discounted cash flow techniques.

The fair value of long term fixed rate inter-company loans are classified as level 1 in the IFRS 13 fair value hierarchy and have a carrying value of £1,572.1m and a fair value of 1,955.3m. Short term and floating rate borrowings have a carrying value and fair value of £308.7m.

The IFRS 13 fair value hierarchy is a categorisation relating to the extent that the fair value can be determined by reference to comparable market values. The hierarchy ranges from level 1 where instruments are quoted on an active market through to level 3 where the assumptions used to derive fair value do not have comparable market data.

It is the Company's policy to recognise all the transfers into the levels and transfers out of the levels at the date of the event or change in circumstances that caused the transfer. No liabilities are classified as level 2 or level 3.

Notes to the financial statements

21 Financial instruments (continued)

The fair values of all financial assets and financial liabilities by class together with their carrying amounts shown in the balance sheet are as follows:

	Carrying amount	Fair Value	Level 1	Carrying amount	Fair Value	Level 1
	2016	2016	2016	2015	2015	2015
	£m	£m	£m	£m	£m	£m
Loans and receivables						
Cash and cash equivalents (note 13)	(118.2)	(118.2)	(118.2)	(81.7)	(81.7)	(81.7)
Total financial assets	(118.2)	(118.2)	(118.2)	(81.7)	(81.7)	(81.7)
Other interest-bearing loans and borrowings (note 14 current)	5.0	5.0	5.0	4.5	4.5	4.5
Other interest-bearing loans and borrowings (note 14 non-current)	1,994.0	2,377.2	2,377.2	1,939.3	2,217.8	2,217.8
Total financial liabilities	1,999.0	2,382.2	2,382.2	1,943.8	2,222.3	2,222.3
Total financial instruments	1,880.8	2,264.0	2,264.0	1,862.1	2,140.6	2,140.6

(b) Credit risk

Financial risk management

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers and investment securities.

Cash and cash equivalents are short term deposits with counterparties that have a credit rating of A1+/P1 or A1/P1, and hence there is no exposure to credit risk for these values.

	2016	2015
	£m	£m
Cash and cash equivalents	118.2	81.7
	118.2	81.7

The concentration of credit risk for trade receivables (see note 12) at the balance sheet date by geographic region was:

South West England	62.5	66.7
	62.5	66.7

Notes to the financial statements

21 Financial instruments (continued)

Trade receivables are from domestic and business customers. No individual customer or industrial sector has a material balance outstanding at either year end.

The aging of trade receivables at the balance sheet date was:

	Gross 2016 £m	Impairment 2016 £m	Gross 2015 £m	Impairment 2015 £m
Less than 1 year	40.5	(4.3)	45.2	(4.9)
1 to 2 years	20.4	(7.5)	20.8	(7.5)
2 to 3 years	16.5	(7.6)	15.5	(7.1)
3 to 4 years	12.0	(7.5)	12.4	(7.7)
More than 4 years	17.8	(17.8)	16.8	(16.8)
	<u>107.2</u>	<u>(44.7)</u>	<u>110.7</u>	<u>(44.0)</u>

The movement in the provision for bad debts in respect of trade receivables during the year was as follows:

	2016 £m	2015 £m
Balance at 1 July	(44.0)	(37.1)
Written off	11.0	5.1
Charge to profit and loss	<u>(11.7)</u>	<u>(12.0)</u>
Balance at 30 June	<u>(44.7)</u>	<u>(44.0)</u>

The bad debt policy is shown in the accounting policies (note 1).

(c) Cash flow hedges

The Company does not have any cash flow hedges.

(d) Liquidity risk

Financial risk management

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due.

The Company is a regulated utility with a five-year settlement with the industry regulator, which allows it to plan to a certain degree of accuracy the financial obligations in the medium term. The Company has also secured long-term funding through bonds issued by its subsidiary company. This means that the need to obtain additional finance has been spread over future years and is not considered onerous in any one regulatory period.

Notes to the financial statements

21 Financial instruments (continued)

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the effect of netting agreements:

	Carrying amount	Contractual cash flows	Year 1	Years 2 to 5	Over 5 years
	2016	2016	2016	2016	2016
	£m	£m	£m	£m	£m
Non derivative financial instruments					
Finance lease liabilities	11.9	12.8	5.5	7.3	-
Secured bank loans	415.0	449.9	5.6	159.1	285.2
Inter-company loans	1,572.1	3,053.2	56.1	226.3	2,770.8
Total financial instruments	1,999.0	3,515.9	67.2	392.7	3,056.0
	Carrying amount	Contractual cash flows	Year 1	Years 2 to 5	Over 5 years
	2015	2015	2015	2015	2015
	£m	£m	£m	£m	£m
Non derivative financial instruments					
Finance lease liabilities	16.4	18.1	5.3	12.8	-
Secured bank loans	365.0	397.5	4.8	157.1	235.6
Inter-company loans	1,562.4	3,298.2	56.1	226.5	3,015.6
Total financial instruments	1,943.8	3,713.8	66.2	396.4	3,251.2

(e) Market risk

There is no exposure to equity or foreign currency risk, the interest rate risk is shown below.

Interest rate risk

At the year end the interest rate profile of the Company's interest-bearing financial instruments was:

	2016	2015
	£m	£m
Fixed rate instruments	947.6	948.1
Floating rate instruments	326.9	281.4
Index linked instruments	724.5	714.3
	1,999.0	1,943.8

The Company policy is to keep a significant proportion of total financial instruments in each of the three categories.

Sensitivity

The floating rate instruments are sensitive to interest rate movements. If there was a 1% increase in interest rates on those floating rate instruments at the balance sheet date, there would be an additional interest charge to the income statement of £2.8m.

Notes to the financial statements (continued)

22 Operating Leases

There were no non-cancellable operating lease rentals payable by the Company.

During the year £1.8m was recognised as an expense in the income statement in respect of operating leases (2015 - £1.7m) and £1.0m (2015 - £0.9m) was recognised as rental income by the Company.

23 Commitments

Capital expenditure contracted but not provided at 30 June 2016 was £108.6m (2015 - £152.3m).

The Company has guaranteed Bonds of £1,572.1m (2015 - £1,562.4m) issued by its wholly owned subsidiary company Wessex Water Services Finance Plc.

24 Contingencies

There are no material contingent liabilities at 30 June 2016 for which provision has not been made in these accounts.

25 Related parties

There were no transactions with key management personnel. Directors' emoluments have been disclosed in the Governance Report.

There have been no transactions with the holding companies described in note 26.

26 Ultimate parent company and parent company of larger group

The smallest group into which the financial statements of the Company are consolidated is that headed by Wessex Water Ltd, a company incorporated in England whose registered address is Wessex Water Operations Centre, Claverton Down, Bath, BA2 7WW.

The pre-penultimate, penultimate and ultimate holding companies are YTL Power International Berhad, YTL Corporation Berhad and Yeoh Tiong Lay & Sons Holdings Sdn Bhd respectively, all registered in Malaysia.

The largest group in which the results of the Company are consolidated is that headed by YTL Corporation Berhad incorporated in Malaysia. The consolidated financial statements of these groups are available to the public and can be obtained from Yeoh Tiong Lay Plaza, 55 Jalan Bukit Bintang, 55100 Kuala Lumpur, Malaysia.

27 Subsequent events

There are no subsequent events requiring disclosure in these financial statements. The final dividend for the year was declared in June 2016 and paid in July 2016.

28 Accounting estimates and judgements

In preparing the financial statements and applying the accounting policies, the Company is required to make reasonable estimates and judgements based on the available information, the most significant of which are;

a) Defined benefit pension scheme deficit

In recognising the deficit on the balance sheet there are a number of assumptions concerning inflation, rate of increase of salaries and pensions, mortality rates and interest rates that can have a significant effect on the deficit recorded. These assumptions are discussed with independent qualified actuaries and disclosed in note 16 to the financial statements.

b) Bad debt provision

The methodology behind the provision is based upon the age of the debt and the method of payment of the debt. Historical evidence is used to determine a percentage of debt to be provided according to the age and payment type.

c) Classification of capital expenditure

Due to the high value of capital expenditure the judgements made on the classification of expenses as operating or capital, and within capital between maintenance and enhancement, are key to the preparation of the accounts. The Company follows both accounting standards and guidelines issued by Ofwat in making these judgements.