Hafren Dyfrdwy Cyfyngedig

Annual report and financial statements for the year ended 31 March 2019

Company number: 03527628

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Hafren Dyfrdwy Cyfyngedig

Company information

Company number	03527628
Directors	J B Coghlan A J Duff J Bowling O R Garfield A Beynon (appointed 1 April 2018) S Jones-Evans (appointed 1 April 2018) M Mehmet (appointed 1 April 2018)
Secretary	H Woodall-Pagan
Registered office	Packsaddle Wrexham Road Rhostyllen Wrexham Clwyd LL14 4EH
Solicitors	Herbert Smith Freehills LLP Exchange House Primrose Street London EC2A 2EG
Auditor	Deloitte LLP Statutory Auditor 4 Brindley Place Birmingham B1 2HZ

Strategic report

What we do

We are one of the 11 regulated water and sewerage companies in England and Wales. The principal activity of the Company is the provision of water and waste water services to customers predominantly in North East Wales, from Wrexham and Bretton in the north to Llanidloes and Knighton in Powys.

The Directors of Hafren Dyfrdwy Cyfyngedig are pleased to present their strategic report on the affairs of the Company, along with the Directors' report, the audited financial statements and the auditor's report for the year ended 31 March 2019.

Key Facts

Turnover	**Litres of drinking water supplied per day**	**Households and businesses served**
£32.0 million	61 million	107,000
(2017/18: £28.2 million)	(2017/18: 66 million)	(2017/18: 128,000)

Loss before interest and tax	**Litres of waste water treated per day**	**Average number of employees**
£2.6 million	3 million	133
(2017/18: £5.9 million profit)	(2017/18: nil)	(2017/18: 137)

Business Model

Running an efficient water business

We provide clean water every time our customers turn on the tap and remove their waste water in an affordable, sustainable and reliable way.

RESOURCES & RELATIONSHIPS WE RELY ON

Resources

Physical assets
A resilient, well maintained network of clean water pipes and reservoirs, sewers and pumping stations.

Natural resources
Water from reservoirs, rivers and underground aquifers are essential to support Severn Trent's operations and value creation.

We look after some of Wales' most impressive natural resources.

Relationships

Our customers and communities
Our customers and communities are at the heart of everything we do. We aim to anticipate and meet changing customers' and wider societal needs.

Our people
We look to attract, develop and retain talented people from all backgrounds, and bring the next generation of water experts into the industry.

Our suppliers and partners
Strong supplier relationships support our business operations in line with our Modern Slavery commitments.

Our regulators
Our industry is regulated by Ofwat and several other regulators and public bodies.

THE WATER CYCLE

Water is collected
We pay the Environment Agency and Natural Resources Wales for the water we collect from reservoirs, rivers and underground aquifers across our region.

Water is cleaned
Our groundwater and surface water treatment works clean raw water to the highest standards, making it safe to drink.

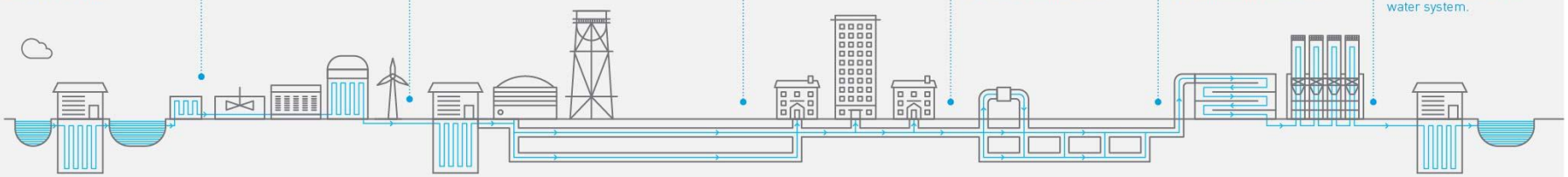
Clean water is distributed
Our network of pipes and our enclosed storage reservoirs bring a continuous supply of clean water right to our customers' taps.

Customers enjoy our services
We provided a safe, reliable supply of water and collect waste water seven days a week, 365 days a year.

Waste water is collected
Our network of sewers and pumping stations collect waste water from homes and businesses and take it to our treatment works.

Waste water is cleaned
Waste water is carefully screened, filtered and treated in our sewage treatment works to meet stringent environmental standards.

Water is recycled to the environment
We pay the Environment Agency and Natural Resources Wales annual consent fees to return the treated water to the water system.



GENERATING & PRESERVING LONG TERM VALUE

Physical assets
Sensible long-term investment.

We completed the replacement of Sygn-y-Pwll reservoir, an investment of £2.8 million.

Natural resources
Over the next five years we'll invest over £2 million to improve biodiversity,

Our customers and communities
Lowest bills in Wales.

We continue to help our customers who are struggling to pay.

Our people
We reward our people by paying fair wages, with a bonus scheme linked to our performance for customers.

Our suppliers and partners
Building sustainable relationships that provide mutual benefit.

Our regulators
We stimulate regulatory debates to improve services for customers across the industry.

Our social purpose

As part of the Severn Trent Group, Hafren Dyfrdwy benefits from the resources and expertise available within the Group – which are being used to drive our social purpose strategy. We are proud to be a pathfinder for a new breed of long-term, socially purposeful companies.

Our commitment is this – every decision we make is based on providing world-class water services at a fair price. We aim to make the most of our contribution to society as a whole and improve the environment. Our social purpose is focused on what our customers want to see from a forward-thinking company. We are certain our efforts will meet our customers' needs now and in the future and we will achieve this through a combination of careful management and sensible long-term investment.

Our social purpose commitments firmly align with Welsh Government's Well-being of Future Generations Act and we constantly strive to operate in a way that considers the long-term impact of our decisions on the people and communities in our region and environmental matters (such as climate change).

The next pages highlight what our social purpose is achieving for customers, the environment and society as a whole as well as our colleagues.

Our social purpose for our Customers

Our social purpose is what drives our ambition to provide world-class services at fair prices.

We continue our unrelenting focus on customer outcomes and we commit to deliver a reliable, consistent service to our customers now and in the future by:

- Ensuring we charge the lowest possible bills that are affordable for all;
- Ensuring water is good to drink and is always there when customers need it;
- Taking waste away safely every day;
- Protecting and creating a thriving environment;
- Engaging with our communities and making a positive difference for the benefit of current and future generations;
- Ensuring customers receive an outstanding customer experience, which is centred around providing a personalised service for everyone whatever their unique needs; and
- Demonstrating that we are a company you can trust who has controls, checks and balances in place to ensure we make the best decisions for our customers. We have made a good start in this area, ensuring that Hafren Dyfrdwy has a strong, independent Board with effective Non-Executive input, but with the added benefit of operating within a strong Group.

Our social purpose for the environment and wider society

Our social purpose means maximising the benefits to the environment and wider society.

Our environmental commitments are also in line with Welsh Government's Water Strategy. In sustainably managing water resources we support healthy communities and biodiversity in Wales.

Over the next five years we will be investing over £2m to improve around 22km of river water quality, which represents the largest statutory environmental programme undertaken in this part of Wales for 20 years. We will also be enhancing biodiversity and well-being by investing around £2m, including at Lake Vyrnwy, where we have a fantastic opportunity to support Wales. The project will:

- enhance the visitor experience so that more people visit the site and stay in the surrounding area thus improving the local economy;
- restore around 450 hectares of upland peat bog to provide greater resilience of our ecosystems; and
- enable local communities to shape the developments and develop a shared sense of ownership.

We're also working with other water companies and partners to explore ways in which water can be traded across water company boundaries. Currently only 4% of water supplies are transferred between water companies. While we've not routinely used water transfers and have no trades currently under development, transfer capacity does exist within the water resource zone for limited, short duration events. Despite our size, we recognise that we could play an important role in water trading so we'll continue working with others where trades make environmental and economic sense, and will be of benefit to Hafren Dyfrdwy's customers.

We are also increasing our contribution to our communities through the Severn Trent Group's community champion programme – an employee volunteering initiative to support community projects.

Our social purpose for our Colleagues

We believe that an expert, highly motivated workforce is vital. And we also believe that a true measure of a company is how it treats its workforce.

Our goals are to:

- Help all our colleagues to succeed;
- Fairly reward people's contributions; and
- Be a company everyone is inspired to work for.

We will achieve these goals by:

- Investing in the best, most relevant apprentice and graduate recruitment schemes in the regions we serve;
- Encouraging everyone to be themselves at work, recognising the widest possible range of talents;
- Encouraging physical and mental wellbeing;
- Paying fair wages, with a bonus scheme for all employees linked to our performance for customers; and
- Giving all employees an opportunity to be part-owners of Severn Trent Plc (60% of our employees take part in our Group Sharesave scheme).

Business overview

Hafren Dyfrdwy is a wholly owned subsidiary of Severn Trent Water Limited, the principal subsidiary of Severn Trent Plc. Severn Trent Water is one of the leading UK water companies, and is committed to enhancing the service offering for Hafren Dyfrdwy's customers.

The Company was launched as Hafren Dyfrdwy on 1 July 2018 for customers in Wales who were previously in Severn Trent Water Limited and Dee Valley Limited. This aligned our operations around the England – Wales border with national boundaries. Hafren Dyfrdwy means 'Severn Dee', representing the coming together of the two companies as represented by the two main rivers in our region.

The boundary alignment involved the following amendments to our region and activities:

- Severn Trent Water's customers in Powys and Monmouthshire were transferred to the Company. This included Severn Trent Water's non-household customers, who had been with different retailers in the English open market, as there is no open market in Wales.
- Our household customers in Chester were transferred to Severn Trent Water.
- Our non-household customers in Chester were transferred to Water Plus to provide retail services. These non-household customers are now eligible to participate in the English open market.
- Our household and non-household customers in North Wales remain as our customers and there was no change to their waste water services provider.

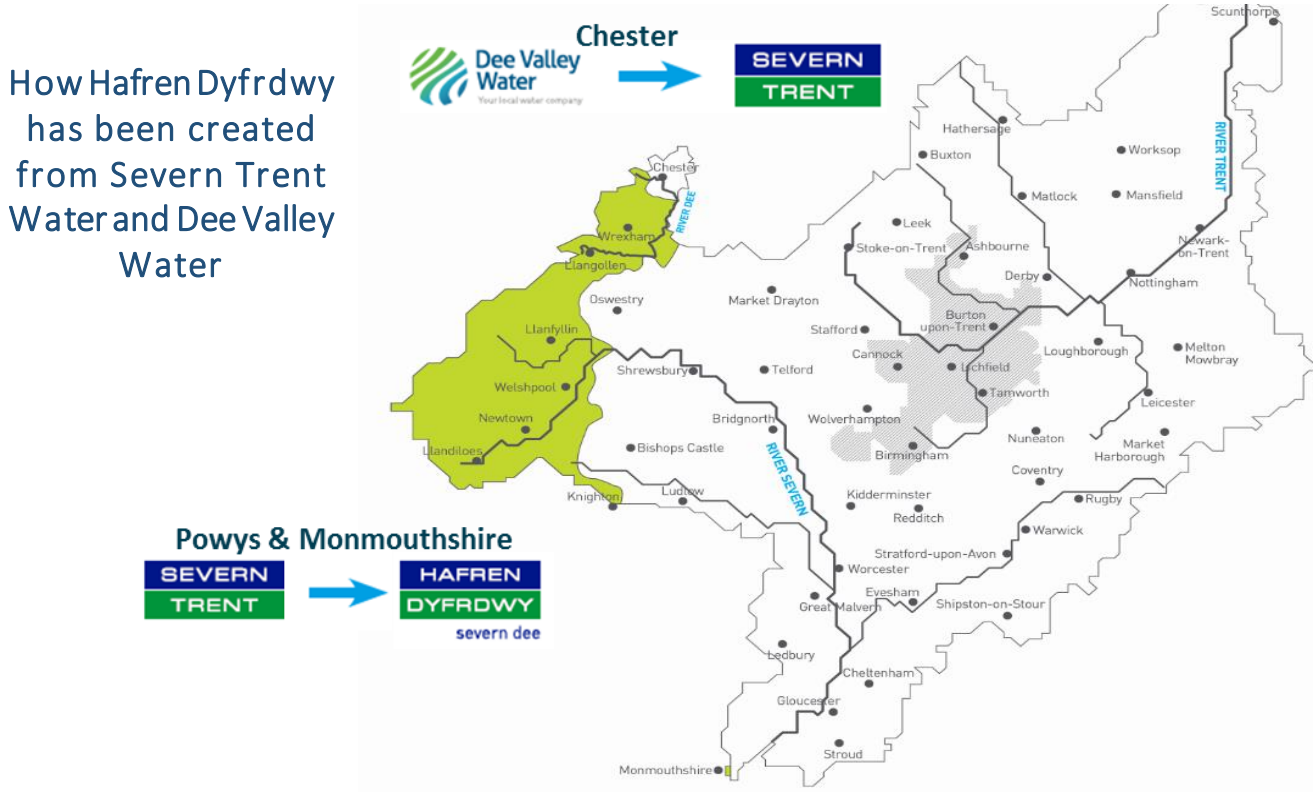
Hafren Dyfrdwy has two Instruments of Appointment (together, our "Licence"): one to supply water services to all of our customers in Wales; the other to provide waste services to customers in Powys and Monmouthshire. We supply drinking water to 105,000 customers in the North East Wales and waste water services to 21,000 customers in Powys and Monmouthshire. We're committed to keeping bills low and providing fresh water to our customers, for generations to come.

This strategic report covers the year ended 31 March 2019. As such, the report reflects performance for our previous Dee Valley Water business, which supplied drinking water to around 128,000 customers in North East Wales, Cheshire and the surrounding areas for the period from April to June 2018, and in the prior year comparatives, with the remainder of the year to 31 March 2019 reflecting the newly launched Hafren Dyfrdwy Company performance.

STRATEGIC REPORT
For the year ended 31 March 2019

Reporting our performance

The licence changes mean that we've had to realign targets previously agreed by Severn Trent Water and Dee Valley Water to the new Company, Hafren Dyfrdwy.



We now have 12 remaining performance commitments with targets reflecting performance levels agreed for customers in Wrexham, and 33 performance commitments with targets reflecting performance levels agreed for our customers in Powys and Monmouthshire. Our performance on outcome delivery incentives (ODIs) in the year is summarised on page 9.

Performance against ODIs

Our performance on our key ODIs in Wrexham and in Powys and Monmouthshire is set out below.

Wrexham

Description	Unit	Actual performance	Target performance
Discoloured water contacts	Number per 1,000 properties	1.02	1.01
Mean zonal compliance	%	99.94	100
Delivery of the outcomes of the service reservoir water quality risk management schemes	Text	Milestone complete	Milestone complete
Average duration of interruptions - 3 hours or longer (planned and unplanned interruptions)	Hours per property per year	0.12	0.2
Sustainable economic level of leakage	Litres per property per day	107.8	90.8
Security of supply index (SOSI)	SOSI	100	100
Number of bursts	Number	185	168
Gross operational greenhouse gas emissions	tCO_2^e	4,987	10,487
Customers' perception based on market research[1]	%	70	Improved
Non-household Service incentive mechanism	Score	83.9	80
Per capita consumption and water efficiency	Litres per capita per day	140.41	128.37
Service incentive mechanism (SIM)[2]	Score	78.4	80

Powys and Monmouthshire

Description	Unit	Actual performance	Target performance
Internal sewer flooding	Number	4	5
External sewer flooding	Number	29	44
Minutes without supply	Minutes	93.74	7.1
Service Incentive Mechanism	SIM	81.45	Upper quartile
Number of Category 3 pollution incidents	Number	1	5
Asset stewardship – coliform failures	Number	nil	nil
Leakage	Ml/d	7.9	5.5

[1] A survey was conducted in 2015/16 to assess satisfaction with our service and establish a baseline for the 'value for money' component. A baseline of 80% was established against which the target was to improve.

[2] Ofwat will determine relative rankings. This information will be published later this year.

Operational review

Our first nine months of operating as Hafren Dyfrdwy have been exciting, challenging and very, very busy. Thanks to the hard work of our teams, we hit the ground running and are now serving all customers in the Wrexham area, as well as those people living in Wales who were previously customers of Severn Trent Water. Our brand new Company is squarely and solely focused on providing a great service to customers living in this beautiful part of Wales.

Above all else, our first year has been a real learning experience. We've met lots of customers and listened closely to their concerns and opinions. And we carried out a huge amount of detailed research on performance, so that we can understand which aspects of our water and waste services are doing well - and where we need to focus more attention.

Our research confirmed that our customers support our long-term plans to improve services while keeping bills down. They want the taps to flow with an abundant supply of clean water and waste water to be taken away quickly, efficiently and safely.

Secondly, our customers want more and better communication from us, including helping them to discover more about the work we're doing to help our communities, or offering them a range of ways to manage their accounts, including online options. It also means providing all of our stakeholders with in-depth detail on our Company's performance. This report, together with our Annual Performance Report, which is available on our website, provides that.

So how's our performance stacking up?

We've summarised our performance during 2018/19 in the following section. Here's a quick summary of the main points:

- Our customers benefited from the lowest bills in Wales (and England) at just 85p per day on average;
- Our waste water performance has been our standout success across the Powys area;
- The prolonged hot, dry weather during the summer put pressure on our supply, and we focussed our resources on protecting supplies to customers and supporting those customers who were at risk of, or experiencing a supply interruption. This was the right thing to do, however, this affected our performance on drinking water quality, speed of response to visible leaks and supply interruptions; and
- We successfully replaced one of the largest clean water reservoirs in the Sugn-y-Pwll area of Wrexham, putting a temporary storage system in place to help minimise the impact on customers while the work was being carried out.

Supporting and listening to our customers

Our customers are at the heart of all we do. We know that keeping bills low is one of their top priorities and so we're proud that our customers benefit from the lowest bills in England and Wales, with an average bill of £311 during 2018/19. Over the next five years, we're increasing investment by 4% per customer to improve services, whilst limiting the increase in customer bills to 1.9% in real terms.

We understand that even though our bills are low, some customers have difficulty paying - so we do everything we can to help those who are struggling to pay. We do this through a range of support initiatives including flexible tariff arrangements and reduced tariff schemes.

Following the transition from Dee Valley Water to Hafren Dyfrdwy we've been busy getting out into local towns and villages, making ourselves available to answer any questions customers might have and we've been actively encouraging customers to pop in and see us as we visit locations throughout the region in Dolly, our roadshow vehicle.

Our customers have told us that improving our environment is a key area of focus for them and our plan is not just to protect the environment, it's to significantly improve it. We work hard to make sure that the impact we have is as positive as possible.

We've also been working hard to improve the level of service customers receive when they contact us. Our Customer First initiative, combined with upskilling more of our customer service staff to deal with more complex billing enquiries, has driven an increase in first time resolution on billing contacts. And we're now seeing benefits from the use of technology, with high self-serve rates through our digital channels and improvements through the use of virtual leakage technicians, where customers can use video calls with our leakage experts to improve our diagnosis, and resolution, of the problem.

However, we know we've got more to do in this area. While we met our target for SIM (Ofwat's current measure of customer service) for non-household customers in Wrexham, we were disappointed with our performance for our household customers.

We recognise that during the prolonged hot, dry weather over the summer we focussed the resources of the business on protecting supplies to customers and supporting those customers who were at risk of, or experiencing a supply interruption. This was the right thing to do however, there were associated impacts on our wider service offering, which led to an increase in second stage complaints.

In AMP7 (Asset Management Plan 7) SIM is being replaced by a measure known as C-MeX. This provides a wider view of customer experience of the services we offer and is based partly on customer contact, as with SIM, and partly on customer perception. We're really excited about this as it incorporates all of the activities we do to enrich our customers' lives, such as our visitor experience sites and community

work, alongside our operational activities, which we believe will ensure that the totality of the experience of all our customers is represented.

Supporting our communities

We are increasingly being seen as having a key role in the everyday lives of local communities. Education gives our customers a better appreciation of our, and their role, in achieving social and environmental goals.

Our education programme delivers quality messages directly to our customers and schools. Our school programme continues to focus on three key messages: the importance of using water wisely; helping children understand what they can, and can't, put down the toilet and sink; and the health benefits of staying hydrated. We've complemented this by improving the education section of our website, made use of our social media platforms and provided tips for efficient water use. This approach supports our commitment to Welsh Government's Water Strategy, promoting the efficient, safe and respectful use of water by all that we serve.

We're also delighted to support Refill across our region – a fantastic scheme that promotes the health benefits of tap water, while helping to protect the environment. We are looking to continue this rollout from the 90 refill stations already created throughout our region.

The vast majority of our employees are also customers and members of the communities in our region. Our people don't just serve our local communities, they are an integral part of them. The case study on page 16 demonstrates the passionate support our people have for their friends, family, neighbours and the local environment in volunteering to make a difference.

Standout performance in waste

As of the 1 July 2018, we have provided waste water services to our customers in Powys and Monmouthshire following their transfer from Severn Trent Water. Removing waste water quickly, safely and efficiently is hugely important for our customers and we're pleased to have delivered a standout performance in the period, achieving our targeted level of performance on all waste performance commitments.

Customers quite rightly voice concerns that internal sewer flooding incidents are one of the worst things that can happen. And we are pleased that our performance on internal sewer flooding is amongst the best in the industry. We're driving further performance improvements through targeting proactive work on sewer flooding hotspots across our waste network.

Our focus has been on cluster analysis and prevention of repeat incidents. Using data analytics we are able to better understand high risk areas in our network and proactively cleanse the system – preventing a problem before it occurs. We are committed to improving further, and by continuing to work with fast food outlets we are reducing the amount of fats, oils, and greases that enter our sewers to reduce the risk of sewer flooding.

Focussing on water quality and supply

We've now successfully completed the replacement of one our largest clean water reservoirs in Sugn-y-Pwll, an investment of £2.8 million. This work to modernise the site will ensure that a reliable, low maintenance and efficient supply is maintained for future generations. To minimise the impact on customers while the work was being carried out we constructed a temporary storage system on the adjacent land. We will be continuing our focus on clean water storage, with over £10 million of investment during 2020-25 to carry out ongoing maintenance and to completely rebuild two of our largest reservoirs which feed Welshpool, and Wrexham and one of our smallest storage reservoir feeding rural customers around Hope Mountain. This, combined with the extensive dams programme over the next five years, will improve the resilience of the whole water supply system.

The summer of 2018 saw a period of prolonged hot, dry weather which created unprecedented demand from our customers and pressure on our network. We worked tirelessly during this period and continued to keep taps running for our customers without the need for a hosepipe ban.

In Wrexham we had a really strong year on supply interruptions, coming in well ahead of our commitment for customers. Unfortunately, several major interruptions in the Powys region meant that we've missed our target in this region. We understand that the loss of supply can be difficult for our customers, and have processes in place to ensure customers receive clear and accurate information through the use of our website, social media channels and automated text messaging system. We've also made improvements in the way we respond to such failures and are confident that these improvements will deliver a better level of service for our customers.

Our customers have told us that leakage is another key priority for them, and that we are playing our part to ensure there is enough water to meet future demands. The first half of the year was operationally challenging, with the tail end of freeze-thaw followed by the prolonged hot, dry summer putting pressure on some of our key water measures. We have applied significant focus on our performance commitment for leakage, including:

- maintaining our strong operational focus on leakage recovery and improving processes to reduce known network leaks;
- introducing innovative ways of finding leaks faster, and fixing them more efficiently – including accelerated installation of acoustic loggers, targeted WIP reduction and the use of more innovative solutions such as satellite technology; and
- spending time to better understand our leakage component data – giving us more clarity on how we can best target leakage and providing more accurate reporting going forward.

Despite this significant focus in the second half of the year, we were disappointed to miss our headline leakage targets in both Wrexham and Powys. We continue our focus and are committed to delivering a 15% reduction in leakage over AMP7.

As part of the Severn Trent Group, we are encouraged by the recent launch of the World Water Innovation Fund – where Severn Trent have joined forces with like-minded companies across the globe to find new ways of working – pooling resources and ideas to develop and accelerate new technologies for the benefit of the sector as a whole. Severn Trent Water's £5 million investment in the Fund will make a real difference to peoples' lives across the world. The Fund's initial focus will be on leakage, which is a key issue for all companies.

We have continued to invest in water quality, including proactively flushing distribution mains through the insourcing of our dedicated flushing team and focusing on high risk areas of the network. We were disappointed to miss our drinking water complaints and mean zonal compliance targets. We are applying additional focus to this, and have invested in installing additional treatment processes to ensure that the bulk supply imports maintain the standards needed.

Improving our environment

Our customers are placing an increasingly high value on the natural environment. We share this view and our commitments are aligned with Welsh Government's Well-being of Future Generations Act. Our aim is to operate in a way that considers the impact of our operations on the environment. We are fully committed to protecting and improving our environment and so we're particularly delighted with our performance in this area.

The Severn Trent Group has held the Carbon Trust Standard since 2009 for successfully measuring, managing and reducing carbon emissions. Despite an increase in the overall volume of water service, we have maintained the overall energy used by our water assets year on year. This year we have taken an option to purchase additional green carbon credits to further promote the production of green energy within the UK, as part of our strategy to move towards carbon neutrality.

Our regulatory framework

As a provider of an essential public service we work within a wide-ranging regulatory framework, with strategic and policy direction provided by the Welsh Government in Wales. Ofwat is the industry's economic regulator and sets limits on the prices we can charge our customers over five year Asset Management Plan ('AMP') cycles. This financial year was the fourth of AMP6, which runs from April 2015 to March 2020.

We also work closely with a variety of other regulators and public bodies, including:

- The Drinking Water Inspectorate ('DWI') independently checks that water supplies in England and Wales are safe and that drinking water quality is acceptable to consumers. Its work includes assuring water quality, ensuring companies make the changes necessary to improve, and developing new regulations to further improve water quality.
- The Consumer Council for Water ('CCW') speaks on behalf of water consumers in Wales. It provides advice to consumers and takes up complaints on their behalf.

- Natural Resources Wales ('NRW') is the environmental regulator in Wales. It oversees how the country's natural resources are maintained, improved and used, both now and in the future.

A key year in the regulatory cycle

Every five years, our regulator Ofwat reviews the prices we propose to charge for the forthcoming five year period and what we plan to deliver for customers and the environment. In September 2018, we submitted our Hafren Dyfrdwy business plan for AMP7, which runs from 2020-2025, ('PR19'). This plan is the outcome of over 18 months of development. It takes a long term view; it delivers for customers today and puts the building blocks in place to continuing improving our services and protect them for future generations.

As Hafren Dyfrdwy was a new company with a lack of historical data, it was not unexpected that our business plan was classified as significant scrutiny by Ofwat.

We were pleased however that Ofwat's initial assessment recognised the progress made to reduce our cost base over the last two years and the certainty provided by the total expenditure we submitted in our forecast for the next AMP being approved by Ofwat. We're continuing to work constructively with Ofwat on other parts of the Hafren Dyfrdwy plan to deliver the right outcome for our customers.

In April 2019 we resubmitted our PR19 plan and we look forward to receiving our Draft Determination from Ofwat in July 2019, with our Final Determination expected in December 2019.

Our people make the difference

Our people work tirelessly to keep wonderful water flowing and treating waste for our customers everyday of the year. So they can achieve their best, we work hard to be the best employer we can be. We're constantly looking for new and better ways to help our people do their job more effectively, fulfil their potential and make them feel valued. In doing so, we improve the service we deliver to our customers.

Each member of our team plays an important role in helping us provide excellent services to customers and build a lasting water legacy - and they deserve our wholehearted support at all times. We work hard to create a workplace that's welcoming and safe, where good work is well-rewarded and people are treated with respect. We engage with our employees at every opportunity, helping them progress and enjoy satisfying, rewarding careers. We look after their health, safety and wellbeing and forge strong links with the communities that most of our people call home. We strive to create careers with purpose and meaning. Our aim is to attract and retain talented, hard-working people who want to progress in their careers and provide great customer service. We support the development of all colleagues at all stages of their career and want every employee to feel competent and confident in their everyday work.

Our Employee Forum brings together employee representatives in quarterly meetings and is co-chaired by a member of the Severn Trent Executive Team and a

member of the trade unions. Discussions over the last year included health and safety, the content of our PR19 plan and our social purpose. These discussions have led to practical changes in how we work - such as a full refresh of our induction experience, the education of our workforce on modern slavery and installation of gender neutral changing rooms at all locations - including operational sites - to support our commitment to greater diversity.

Rewarding our employees

As part of being an awesome place to work it is important that our people are properly rewarded. During the year, in response to feedback raised through the Employee Forum and QUEST, we communicated with our teams to make sure that they understand how their pay is set and how they can earn more and progress through the business.

We also ensure we help all employees keep an eye on the future. We offer a market-leading defined contribution pension scheme and double contributions that our employees make (up to a maximum of 15% of salary), regardless of their level or seniority. As our people approach retirement we provide education and support to help them plan for the next stage of their lives.

Promoting health, safety and wellbeing

We believe passionately that no-one should be hurt or become unwell by what we do. With this in mind we provide extensive training on all aspects of health and safety. We have also continued to campaign to remove the stigma associated with mental health and have trained a further 28 employees across the Severn Trent Group as mental health first aiders. We continued our work to help people understand how menopause affects individuals and families and we've shared our approach with other organisations, including Ofwat and the DWI.

Helping our customers to reduce plastic

We're delighted to support Refill– a fantastic scheme that promotes the health benefits of tap water, while helping to protect the environment. There are now over 20,000 refill stations in the UK where you can fill up a water bottle for free, including shops, cafes, restaurants and museums – simply look for the blue sticker in the window. Of these, 90 are within our region in Wales. We are encouraging local businesses to sign up to Refill. All our visitor experience sites have signed up as refill stations too.

Financial performance

Our financial performance reflects a year of organisational change and investment in our business. The licence changes implemented on 1 July 2018 changed our business significantly, bringing in new customers, significant assets and new activities with the waste water business in Powys. With the transfer of the Chester region to Severn Trent Water and the addition of Powys, our region is now more rural and more expensive to serve than previously. However, in line with the commitments made when Severn Trent acquired Dee Valley Water and when the boundary changes were proposed, customer bills were not increased as a result of these increased costs so our revenue did not increase in line with our costs.

During the year we increased our investment in our networks to improve our performance for our customers now and in the future. For example:

- Ensuring we continue to comply with the Security and Emergency Measures Direction, Protective Security Guidance 2020 and the Network and Information Systems Direction.
- Ice-pigging on targeted areas of the network to remove the build-up of silt and chemical residues.
- High velocity flushing in the Legacy zone to remove a key source of manganese from the supply network.
- Installing instrumentation and loggers to give us a better understanding of where and when water is being lost from our network. This investment should enable us to both improve reporting and target improvements in the most efficient way.

This is reflected in our financial results for this year but we expect to see benefits in better customer service and improved financial returns in future.

Turnover was up 13.5% to £32.0 million (2017/18: £28.2 million). The boundary changes increased turnover by £2.9 million. Extra revenue from the supply of waste to new customers in Powys was £2.2 million; and revenue from service agreements relating to reservoir assets transferred from Severn Trent Water £4.5 million was largely offset by the lost revenue from the net reduction in customers following the boundary change £3.8 million. RPI and the K factor increased turnover and other changes increased turnover by £0.9 million.

Operating costs increased by 55.2% to £34.6 million (2017/18: £22.3 million). The boundary changes increased infrastructure maintenance costs by £1.5 million, depreciation by £0.4 million and other operating costs by £6.1 million. The very low population density of our new supply area drives up the asset and operating complexity of our water distribution network and increases the cost of serving customers and of operating and maintaining our network. During the year we aligned the accounting treatment of water mains renewal with that applied by Severn Trent Water. This increased infrastructure maintenance costs by £2.0 million. Aside from the boundary changes, operating costs increased by £2.3 million as a result of increased investment in our networks as set out above.

We incurred £0.4 million exceptional operating costs as a result of the High Court's judgment in the Lloyds Bank case relating to gender equality in Guaranteed Minimum Pension rights that has an impact on the Company's defined benefit pension liabilities. We have obtained independent advice from the Company's actuaries to determine the amount of the additional liability and have made provision for the best estimate in this year's financial statements.

The loss before interest and tax was £2.6 million (2017/18: profit of £5.9 million).

Net finance costs before exceptional costs were up 22% to £3.3 million (2017/18: £2.7 million). The increase is due to higher inter-company debt payable to Severn Trent Water as a result of the asset transfers from the boundary realignment. This debt was repaid via the de-gearing exercise carried out near the end of the year (see below) and we expect lower finance costs in future as a result. On 28 March 2019 as part of the de-gearing exercise (see below) we redeemed £34 million of our index-linked loan from Severn Trent Water. The coupon on this loan is above prevailing market rates and so a premium of £21.9 million was payable on redemption. This charge was settled by issuing new shares to Severn Trent Water and has been treated as an exceptional finance cost in the income statement.

Our full effective tax rate was above the statutory rate at 22%. The impact of disallowable expenditure was more than offset by credits relating to prior years and the impact of the lower tax rate on the deferred tax charge.

We are committed to paying the right amount of tax at the right time. We pay a range of taxes, including business rates, employers' national insurance and environmental taxes such as Climate Change Levy and the Carbon Reduction Commitment as well as corporation tax which is included in our tax charge in the income statement.
The loss for the year was £22.2 million (2017/18: profit of £2.3 million).

We completed the integration of our ERP and billing systems with Severn Trent's systems during the year, bringing our investment in these assets to £9.5 million.

The transfers of assets arising from the boundary changes increased our property plant and equipment by £76 million net.

Our defined benefit pension scheme surplus was £18.6 million (2018: £18.2 million). The funding level remains strong at 139% (2018: 139%).

Receivables increased due to income from reservoir agreements and amounts receivable from Severn Trent Water including group relief of £6.4 million.

On 28 March 2019 we implemented a de-gearing exercise to bring our gearing in line with Ofwat's notional capital structure for AMP7 and to reduce our finance costs to a more sustainable level. We issued 132,810,685 ordinary shares of £1 each at par in exchange for:

- Repayment of £76,861,364 of an inter-company loan with Severn Trent Water Limited at par; and

- Repayment of £34,000,000 of an index-linked loan from Severn Trent Water Limited together with a premium on redemption of £21,949,321.

We finished the year with a strong balance sheet, net assets of £156.2 million (2018: £44.8 million), net current assets of £13.1 million (2018: net current liabilities £0.1 million) and RCV gearing of 66.7% (2018: 67.2%).

Risk management

All of the Company's risks are identified and managed through a continuous corporate risk management process.

During the year the process to adopt the well-established Severn Trent Plc Enterprise Risk Management (ERM) approach has been completed to strengthen the Company's processes to manage and mitigate risks. The Board has overall accountability for ensuring that risk is effectively managed across the Company. The Board's mandate includes defining risk appetite and monitoring risk exposure to ensure significant risks are aligned with the overall strategy of the Company. The management of risk is embedded in our everyday business activities, with employees encouraged to play their part.

On behalf of the Board, the Audit Committee of Severn Trent Plc assesses the effectiveness of the Group's ERM process and internal controls to identify, assess, mitigate and manage risk. The Group Internal Audit function supports the Audit Committee in evaluating the design and effectiveness of internal controls and risk mitigation strategies implemented by management.

Across the Company, we manage risks within the overall governance framework which includes clear accountabilities, delegated authority limits and reward policies. These are designed to provide employees with a holistic view of effective risk management. Our approach reflects our status as a regulated utility providing essential services and operating as part of the Critical National Infrastructure for the UK. The nature of our business is such that there are some significant inherent risks. We aim to have a strong control framework in place to enable us to understand and manage these risks in accordance with our risk tolerance and appetite. The Severn Trent Plc Audit Committee manage risks which are material at a Company level as well as at a Group level, supported by tailored risk reporting and consideration at Hafren Dyfrdwy Board level.

The Directors have carried out a robust risk assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity. The principal risks are summarised on the following pages. For each risk we state what it means for us and what we are doing about it.

Risk	What Does It Mean	Mitigation	Movement in Net Risk Exposure
Regulation and compliance			
1. Ongoing regulatory reform and the potential increase in policy divergence between the English and Welsh governments	Our operational environment is highly regulated. Our policies and procedures ensure compliance with the regulatory framework. But market reform and the potential for differences in policy between the two governments creates risks. Regulatory changes may increase costs of administration, reduce income and margin and lead to greater variability of returns.	As a Welsh company we are committed to working proactively with the Welsh Government to develop its water strategy for its people. With the alignment of the boundaries of Severn Trent Water and Dee Valley Water to the national boundaries of Wales and England, from 1st July 2018 onwards, the risk to the Company of policy divergence between English and Welsh governments has been removed. Regulatory reform is mitigated through the maintenance of strong relationships, good engagement and open dialogue with the Welsh Government, local and national Welsh Assembly Members, Wales Water Forum, Natural Resources Wales, the Drinking Water Inspectorate and Ofwat.	No change
2. Failure to meet targets for regulatory performance and customer service	The Company has challenging operational performance targets for PR14, with financial penalties and loss of credibility if we fail to meet these. Ofwat's regulatory processes place customers at the heart of the business. Failure to	Our review of processes, systems and equipment is ongoing and investments are being made to deliver significant improvements in the quality of product and service. We have a series of internal measures that enable us to proactively monitor performance and take prompt corrective action when and where necessary. We recognise there is work to do to improve our SIM performance. Work is also underway to prepare for	No change

Risk	What Does It Mean	Mitigation	Movement in Net Risk Exposure
	meet these high standards will lead to customer dissatisfaction and Service Incentive Mechanism (SIM) penalties imposed by Ofwat, all of which will damage the Company's reputation.	Ofwat's new customer measure of performance (C-MeX) in anticipation of SIM being replaced in March 2020.	
Operational			
3. Failure to maintain a constant supply of water that meets Drinking Water Standards	Failure of certain important assets could cause widespread loss of supply to customers with the risk of regulatory sanction, loss of reputation and higher operating costs. Water quality could result in regulatory sanctions, adversely affect our reputation and cause an increase in our costs.	Assets are managed through condition monitoring and maintenance. When appropriate, risk-based asset investment planning identifies assets for replacement, which is a continuing process. Contingency plans provide for major failures. These include bringing in water from other parts of the supply area; providing emergency supplies and mutual aid agreements with other water companies. The Drinking Water Safety Plan addresses the management of water quality risks throughout the supply system from catchment to customer. This ensures there are adequate mitigations in place for all risks, including discolouration, in the form of operational procedures, processes, maintenance, monitoring and appropriately trained staff. Risk-based	No change

Risk	What Does It Mean	Mitigation	Movement in Net Risk Exposure
		investment planning plays an important part by ensuring equipment performs effectively and emerging risks are addressed.	
4. Business interruption and/or data loss resulting from cyber threats	Loss or corruption of computer systems or data is a real and growing threat and potentially, could have far reaching effects, particularly within our administrative and equipment operations.	We continue to commit significant resources and financial investment to maintain the integrity and security of our assets and data. We follow guidance from the National Cyber Security Centre and have defence through multiple layers of software and processes including web gateways, filtering, firewalls, intrusion and advanced threat detection. We have strengthened our security and network operations capability this year and have improved the controls around third party access to our systems and data. We have reviewed our cyber risk methodology and are using this to prioritise future investment to ensure that we protect ourselves in-line with GDPR, Network and Information Systems Regulation and Payment Card Industry Data Security Standard (PCI DSS) best practices. As a precaution, we have robust incident response, business continuity and disaster recovery procedures in place. We have participated in a number of internal cyber security incident exercises to test our response	Increase

Risk	What Does It Mean	Mitigation	Movement in Net Risk Exposure
		capability to cyber-attacks. We also maintain insurance cover for loss and liability. Considering current cyber threat levels we have recognised an overall increase in the net risk exposure.	
5. We are unable to deal with the impact of extreme and unpredictable weather events on our assets and infrastructure and/or are unable to successfully plan for future water resource supply and demand due to climate change.	Climate change (hotter and drier summers, wetter winters and increased storminess) could result in an inability to meet customer demand, lower river levels, decreased raw water quality, flooding of our water or waste works, sewer capacity being exceeded and increased land movement. You	Extreme Weather The extreme weather events of 2018, Freeze Thaw in March 2018 and the prolonged hot, dry summer, have helped to inform our contingency plans. Our PR19 business plan includes investment in the resilience of our assets. Climate Change Our draft Water Resources Management Plan for the next 25 years was consulted on through 2018. The plan includes an assessment of climate change impact. The final plan will be published in summer 2019.	No change

Risk	What Does It Mean	Mitigation	Movement in Net Risk Exposure
Health & Safety			
6. The nature of the activities we undertake creates a potential to cause harm to our employees, contractors and the general public	Our work requires our employees and contractors to use equipment and carry out tasks which have the potential to cause serious harm. In addition, we undertake a lot of work in dynamic public places such as busy streets. We take every precaution to prevent injury, however the failure of a procedure or the breakdown of an asset could lead to injury.	Alignment to the well-established Severn Trent Health, Safety and Wellbeing framework has continued during the year. The framework ensures all our operations and processes are conducted in compliance with Health and Safety legislation and in the interests of the safety of our people and contractors. Our Goal Zero initiative clearly establishes our target that no one should be injured or made unwell as a result of what we do. We recognise that the key to a safer organisation is the behaviour of staff. As such, we encourage near miss reporting across the organisation as we believe this ensures we review incidents to address the root causes of incidents. Our assets are subject to regular monitoring and maintenance though proactive and reactive programmes of work. Our reservoirs are independently inspected and then maintained by our staff to ensure that they remain safe.	No change

Brexit statement

At the time of writing, the terms of the UK's departure from the EU (Brexit) remain uncertain. Brexit does not give rise to a new principal risk for the Company. However, it does have the potential to impact a number of existing risks, such as supply chain, interest rates, availability of funding, regulatory changes and uncertainty for the domestic economy.

Our preparations for a no-deal Brexit are well advanced within the Severn Trent Group and include a Brexit Steering Committee to oversee the contingency and scenario planning necessary to operate effectively if the UK leaves the EU without transition arrangements. The Committee covers; Incident Management, People, Procurement, Security and Resilience, Logistics, Communications, Finance and Capital Delivery. We have been actively engaged with a Water UK coordinated group called the Operations Strategy Group (OSG) at an executive level, focussing on industry preparedness, including industry wide testing of response plans to a 'no deal' scenario. We are also working with a number of Local Resilience Forums to test our approach and plans. We are confident that we are well prepared for the UK's departure from the EU and specifically the risks associated with 'no deal'. The most significant risk identified is associated with the availability of chemicals imported into the UK, we identified this at an early stage and have ensured we have a robust process for maintaining stock levels. This has also been a key focus for the pan-industry group which accordingly has worked with suppliers to increase stock levels chemicals across the UK. Government, Defra and other industry regulators have been kept informed of preparations throughout. We have also increased stock for critical spare parts where a potential risk has been highlighted, by working with our supply chain.

Progress in the Brexit negotiations will continue to be monitored and the risks and uncertainties will be managed through our existing ERM process.

Viability statement

Assessment of current position and long-term prospects

The Directors' assessment of the Company's current financial position is set out in the Financial review on pages 17 to 19.

The Company operates a regulated long-term business characterised by multi-year investment programmes and stable revenues. The water industry in England and Wales is currently subject to economic regulation rather than market competition and Ofwat, the economic regulator, has a statutory obligation to secure that water companies can (in particular through securing reasonable returns on their capital) finance the proper carrying out of their statutory functions. Ofwat meets this obligation by setting price controls for five year Asset Management Periods (AMPs). This mechanism reduces the potential for variability in revenues from the regulated business. The current AMP runs until March 2020 and the Company has submitted its plans for the AMP period 2020 – 2025 (AMP7) to Ofwat. Ofwat will publish its final determination for AMP7 in December 2019. We do not expect the financial outcomes from the determination to be materially different from our business plan.

When considering the Company's prospects beyond 2025, it is necessary to make assumptions about the price review process for the period 2025 – 2030 (PR24),

which will take place in 2024, and has not yet been specified. In making this assessment we have taken account of:

- Ofwat's statutory duty to secure that companies can finance the proper carrying out of their functions;
- The Company's financial structure, which is close to the Ofwat notional capital structure and our plan to retain this; and
- The Company's progress in developing plans for AMP7, the successful execution of which would deliver benefits to all stakeholders and financial incentives that would help to improve our financial resilience in the period beyond 2025.

The Company has significant investment programmes that are largely funded through intra-group borrowing under multi-year agreements and facilities. The tenor of the facilities is set out in note 16 to the financial statements. There are no financial covenants included in these agreements.

The Company's strategic funding objectives reflect the long-term nature of its business and the Company seeks to obtain a balance of secure long-term funding at the best possible economic cost and to maintain financial ratios that would support an investment grade credit rating. The Directors have concluded that at 31 March 2019 the Company could maintain such a rating.

The Severn Trent Group's Treasury Policy requires that it maintains sufficient liquidity to cover cash flow requirements for a rolling period of at least 18 months in order to mitigate the risk of restricted access to capital markets. The Company's refinancing requirements are managed within the Group Treasury department to spread the timing of refinancing requirements and to enable such requirements to be met under most market conditions. The weighted average maturity of debt at the balance sheet date was 7.9 years.

The Company has an established process to assess its prospects. The Board undertakes a detailed assessment of the Company's strategy on an annual basis and the output from this assessment sets the framework for the Company's medium term plan, which is updated annually.

The Company's medium term plan assesses its prospects and considers the potential impacts of the principal risks and uncertainties. Stress tests are performed to assess the potential impact of combinations of those risks and uncertainties. The plan also considers mitigating actions that the Company might take to reduce the impact of such risks and uncertainties, and the likely effectiveness of those mitigating actions.

In considering the Company's prospects the Directors took note of the equity investment of £133 million made by its parent company during the year to reduce its gearing to a level close to the Ofwat notional capital structure by the start of the next AMP in March 2020.

Period of assessment

The Directors considered a number of factors in determining the period to be covered by the assessment. The long-term nature of the Company's principal business, together with relatively stable revenues and a model of economic regulation that places a duty on the regulator to secure that water companies can finance the proper carrying out of their functions, support a longer period of assessment.

However, the changing nature of regulation of the water industry increases the uncertainty that is inherent in the Company's financial projections. The Company has an established planning and forecasting process and the Directors consider that the assessment of the Company's prospects is more reliable if it is based on an established process. The Company's latest medium term plan extends in detail to the end of the next AMP period in 2025 with less detailed projections looking beyond this.

A longer period of assessment introduces greater uncertainty because the variability of potential outcomes increases as the period considered extends.

Bearing in mind the long-term nature of the Company's business; the enduring demand for its services; the nature of the Company's established planning process and the changing nature of the regulation of the water industry in England and Wales, the Directors have determined that seven years is an appropriate period over which to assess the Company's prospects and make its viability statement this year.

Assessment of viability

In assessing its future prospects, the Company has considered the potential effect of risks and uncertainties that could have a significant financial impact under severe but plausible scenarios. The risks and uncertainties considered were identified in the Company's ERM process, which is described on pages 19 to 24, and from the key assumptions in the financial model. The scenarios tested are described below.

Scenario tested	Related principal risk	Mitigating actions
1. *An increase in interest rates for part of the period under consideration* The Company's existing borrowings are at fixed rates or linked to RPI. Higher costs on debt refinanced in the period would adversely impact the Company's profits, cash flows and credit metrics.	N/A – key assumption in financial model	Reduce discretionary expenditure in the short term. Secure additional equity finance from the Severn Trent Group.

Scenario tested	Related principal risk	Mitigating actions
2. The Company underperforms against its performance commitments The Company operates under a regulatory model which encourages companies to deliver what customers want using performance related rewards and penalties. Failure to deliver performance at the committed level can lead to significant penalties.	Risk 2: Failure to meet targets for regulatory performance and customer service	Reduce discretionary expenditure to cover any extra costs resulting from penalties.
3. The Company incurs higher costs than planned that are not funded Significant overspending could result in a deterioration in financial metrics and performance, which might adversely impact the Company's solvency.	Risk 2: Failure to meet targets for regulatory performance and customer service	Reduce discretionary expenditure in the short term. In the medium term implement a cost reduction programme to deliver sustainable cost savings and efficiencies to bring costs back in line with regulated allowances. Secure additional debt or equity finance from the Severn Trent Group.

Scenario tested	Related principal risk	Mitigating actions
4. The Company incurs a financial penalty for non-compliance with legislation The Company operates in a regulatory and legal environment that is complex and changing. Failure to keep pace with changes in legislation or regulation could lead to non-compliance and result in financial penalty.	Risk 1: changes in the regulatory environment for the water industry	Reduce discretionary expenditure to cover any extra costs resulting from penalties.
5. A combination of scenarios 2 – 4	See above	Reduce discretionary expenditure in the short term. Re-profile the Company's capital expenditure programme. Secure additional debt or equity finance from the Severn Trent Group.
6. The Company experiences a severe failure of a key asset The Company's Enterprise Risk Management process has identified a number of risks relating to failure of key assets that might have a significant impact on the Company's operational and financial performance.	Risk 3: Failure to maintain a constant supply of water that meets Drinking Water Standards	Reduce discretionary expenditure to cover any extra costs resulting from the event In the medium term implement a cost reduction programme to deliver sustainable cost savings and efficiencies to bring costs back in line with regulated allowances. Secure additional debt or equity finance from the Severn Trent Group.

The combined scenario represents a situation where several of the severe but plausible scenarios occur simultaneously. In this situation the same mitigating actions would be available to the Company but their application would be deeper.

The Company also tested the following scenarios and found that it remained viable without further mitigating actions:

- Inflation 1 percentage point higher than the base case;
- Inflation 1 percentage point lower than the base case; and
- Bad debt costs increase to 5% of revenues.

The Company has significant funding requirements for the Company's capital programme. Since the Company's principal source of funding is the Severn Trent Group, the Company has considered the outcome of the Severn Trent Group's assessment of viability in making its own assessment. The Company has also considered its parent company's willingness and ability to provide additional funding when required.

Under all scenarios considered, the Company would remain solvent and have access to sufficient funds in normal market conditions. The Group's Treasury Policy requires that it retains sufficient liquidity to meet its forecast obligations, including debt repayments for the next 18 months.

The Company's business plans are based on the current regulatory framework and do not take into account any changes that might arise if a future Government implemented a policy of renationalisation of the water sector.

In making its assessment the Board has made the following key assumptions:

- Any period in which the Severn Trent Group is unable to access capital markets to raise finance during the period under review will be shorter than 18 months; and
- There is no renationalisation of the water sector in the period under review.

On this basis, the stress tests indicated that none of these scenarios, including the combined scenario, would result in an impact to the Company's expected liquidity, solvency or debt covenants that could not be addressed by mitigating actions and are therefore not considered threats to the Company's viability.

Governance and assurance

The Board reviews and approves the medium term plan on which this viability statement is based. The Board also considers the period over which the assessment of prospects and viability statement should be made. The Severn Trent Plc Audit Committee supports the Board in performing this review.

This statement is subject to review by Deloitte, our external auditor. Their audit report is set out on pages 59 to 65.

Assessment of viability

The Directors have assessed the viability of the Company over a seven year period to March 2026, taking into account the Company's current position and principal risks.

Based on that assessment, the Directors have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to 31 March 2026.

Going Concern Statement

These financial statements have been prepared on a going concern basis. The company has considerable financial resources together with a customer monopoly in its area of supply. Consequently, the Directors believe that the Company is well placed to manage its business risks successfully over the forthcoming twelve month period.

The Directors therefore have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future and consider that the going concern basis continues to be appropriate in the preparation of these financial statements.

By order of the Board

James Bowling
Director
9 July 2019

Governance Report

UK Corporate Governance Code Compliance Statement

The Hafren Dyfrdwy Cyfyngedig Board is fully committed to Ofwat's principles for Board leadership, transparency and governance with its emphasis on the importance of strong board leadership and the special responsibilities attached to regulated monopoly companies providing an essential public service. As Hafren Dyfrdwy is not a listed company it is not required to comply with the UK Corporate Governance Code (the "Code"). However, Hafren Dyfrdwy has elected to comply with the 2016 Code, where appropriate and reasonably practicable, to ensure the highest standards of governance.

For the whole of the financial year ended 31 March 2019, Hafren Dyfrdwy was compliant with the Code, with the following exceptions:

1. Audit and Remuneration and Committees at Company level

The Remuneration Committee at Severn Trent Plc Group level operates on behalf of Hafren Dyfrdwy. There have been no Remuneration matters for consideration by Hafren Dyfrdwy Board during the year. In the event such consideration is required, the matters will also be considered at Hafren Dyfrdwy Board level.

The Audit Committee at Severn Trent Plc Group level operates on behalf of Hafren Dyfrdwy, with the Committee providing advice, assurance and recommendations only, ahead of the Hafren Dyfrdwy Board making final decisions.

Any associated assurance in respect of Hafren Dyfrdwy is conducted at a materiality relevant to the size of Hafren Dyfrdwy and risks are considered and managed from an individual Board perspective, with clear and effective governance at individual Board level.

Hafren Dyfrdwy Directors are invited to attend all relevant Severn Trent Plc Audit Committee meetings in respect of Hafren Dyfrdwy matters. Additionally, there is a separate Hafren Dyfrdwy Nominations Committee that comprises Hafren Dyfrdwy Independent Non-Executive Directors only.

In particular the Severn Trent Plc Audit Committee's terms of reference include, but are not limited to, reviewing:

- the integrity of the processes that ensure the quality and reliability of regulatory statements and information to regulatory bodies, including the Annual Regulatory Compliance Statement and Annual Performance Report, submitted to Ofwat; and
- the integrity of the processes that ensure compliance with the requirements of regulatory submissions to regulatory bodies; in respect of Hafren Dyfrdwy.

All Board Committees comprise a majority of Independent Non-Executive Directors. Details of the respective Committees can be found in the Severn Trent Plc Annual Report and Accounts.

2. Provisions relating to relations with shareholders

The Company does not comply with the provisions relating to Relations with Shareholders which covers Dialogue with Shareholders and Constructive use of the AGM, as it would not be appropriate to do so. However, Severn Trent Plc does fully comply with these requirements.

LEADERSHIP AND EFFECTIVENESS

Board of Directors

1. Ann Beynon, OBE, BA (Hons)

Independent Non-Executive Director - Appointed to the Board on 1 April 2018

Ann is a Non-Executive Director on the Board of Farmers' Union of Wales Insurance Services, an Independent Advisor to the National Assembly for Wales and a CBI Wales representative for the SE Wales Business Council. Previously, Ann was a Director for BT Wales, S4C's Head of Political and International Affairs and Equality and Human Rights Commissioner for Wales. Prior to this, Ann was a member of the Royal Commission on Reform of the House of Lords.

Other roles

- Independent Advisor to the National Assembly for Wales
- Chair of the Clwstwr Creadigol project for Cardiff University
- Director of Cwmni Ann Beynon CYF
- Director of Digidol CYF
- Director of FUW Insurance Services Limited
- CBI Wales representative for the SE Wales Business Council
- Director of Cardiff French Centre – in liquidation

2. James Bowling, BA (Hons) Econ, ACA

Chief Financial Officer - Appointed to the Board on 17 February 2017

James is a chartered accountant, having started his career with Touche Ross and brings significant financial management, M&A and business transformation expertise to the Board. Prior to joining the Severn Trent Group, James was interim Chief Financial Officer of Shire Plc, where he had been since 2005, first as Head of Group Reporting and from 2008 as Group Financial Controller. Prior to joining Shire, James spent nine years at Ford Motor Company in various finance roles of increasing responsibility.

Other roles

- Executive Director of Severn Trent Water Limited, the Group's licenced entity in England, and Severn Trent Plc

3. John Coghlan, BCom, ACA

Chairman - Appointed to the Board on 17 February 2017

John has a wealth of experience in financial and general management. He spent 11 years at Exel PLC as Chief Financial Officer and ultimately as Deputy Chief Executive Officer until retiring in 2006. Since then, he has been a Director of publicly-quoted and private companies across several sectors. Currently, John is also Non-Executive Director and Audit Committee Chairman of Associated British Ports Holdings Limited and Clarion Housing Group, and is Non-Executive Director of O.C.S. Group Limited.

John has recent and relevant financial experience as a member of the Institute of Chartered Accountants in England and Wales.

Other roles

- Chairman of Freight Transport Association Ireland Limited
- Non-Executive Director of Severn Trent Water Limited, the Group's licenced entity in England, Severn Trent Plc and Chairman of the Audit and Treasury Committees

4. Andrew Duff, BSc, FEI

Independent Non-Executive Director - Appointed to the Board on 17 February 2017

Andrew's extensive experience of international and regulated business, strategic management and customer service in high profile, dynamic environments has equipped him well for the role of Chairman of the Severn Trent Group. Andrew spent 16 years at BP Plc in marketing, strategy and oil trading. He joined National Power in 1998 and the Board of Innogy Plc upon its demerger from National Power in 2000. He played a leading role in its restructuring and transformation through the opening of competition in energy markets culminating in its subsequent sale to RWE in 2003. He became Chief Executive Officer of the successor Company and a member of the RWE Group Executive Committee until his retirement in 2010. He was a Non-Executive Director of Wolseley Plc from July 2004 until November 2013. Andrew was appointed Non-Executive Deputy Chairman of Elementis Plc on 1 April 2014 and became Non-Executive Chairman of Elementis Plc on 24 April 2014. He is the Senior Trustee of Macmillan Cancer Support.

Other roles

- Member of the CBI President's Committee
- Fellow of the Energy Institute
- Senior Trustee of Macmillan Cancer Support
- Chairman of Severn Trent Water Limited, the Group's licenced entity in England, Severn Trent Plc and the Nominations Committee of Severn Trent Plc
- Non-Executive Director - UK Government Investments Limited

5. Olivia Garfield, BA (Hons)

Chief Executive - Appointed to the Board on 17 February 2017

Olivia (Liv) brings to the Board a wealth of experience managing customer service delivery and complex infrastructure and organisations in a regulated environment. Liv was Chief Executive Officer of Openreach, part of the BT Group, where she spearheaded and oversaw the commercial roll-out of fibre broadband to two-thirds of the country. She joined BT in 2002 and held the pivotal roles of Group Director of Strategy and Regulation, Managing Director Commercial and Brands, Global Services and UK Customer Services Director. From 1998 to 2002, Liv worked for Accenture as a consultant in the Communications and High Tech Market Unit, designing and implementing business change solutions across a number of industry sectors.

Other roles

- Member of The 30% Club

- Director of Water UK
- Member of Take Over Panel – Hearings Committee
- Executive Director of Water Plus Limited – joint venture with United Utilities
- Executive Director of Severn Trent Water Limited, the Group's licenced entity in England, and Severn Trent Plc

6. **Sally Jones-Evans,** FCIB, MSC, MBA

Independent Non-Executive Director - Appointed to the Board on 1 April 2018

Sally is a Non-Executive Director of the Principality Building Society where she also chairs the Remuneration Committee and sits on the Audit Committee. She also serves as a Non-Executive Director at the Department for International Development and is a member of the Audit and Risk Assurance Committee, and she is a Trustee Director at Tearfund, the Christian relief and development charity. Sally's executive career was at Lloyds Banking Group for 30 years' where she held a wide range of management roles. Sally has previously served as a Non-Executive Director of Welsh Athletics and the Student Loans Company and a member of the Welsh Government Financial and Professional Services Sector Advisory Panel.

Other roles

- Non-Executive Director at the Department for International Development
- Non-Executive Director of Principality Building Society
- Trustee Director of Tearfund

7. **Dr Mohammed Mehmet,** BSc (Hons), PhD

Independent Non-Executive Director - Appointed to the Board on 1 April 2018

Mohammed was the interim Chief Executive of Powys County Council and had been Chief Executive of Denbighshire County Council until April 2018. Previously he was a member of the Public Services Leadership Panel and the Merthyr Tydfil's Education Recovery Board. Mohammed was the first chair of the National Procurement Board and has led a number of regional programmes including the establishment of the North Wales School Improvement Service. Earlier in his career Mohammed was Assistant Director of Education in the London Borough of Camden and Hackney.

Other roles

- Member of the Advisory Board of Marie Curie in Wales

Board meeting attendance 2018/19

The following table shows the attendance of Directors at scheduled Board meetings during the year:

Director	Position	Board Meetings
Ann Beynon	Independent Non-Executive Director	4/4
James Bowling	Chief Financial Officer	4/4
John Coghlan	Chairman	4/4
Andrew Duff	Non-Executive Director	4/4
Olivia Garfield	Chief Executive Officer	4/4
Sally Jones-Evans	Independent Non-Executive Director	4/4
Mohammed Mehmet	Independent Non-Executive Director	4/4

All meetings are structured to allow open discussion. Minutes of Board and Committee meetings are circulated to all Directors after each meeting.

In the event a Director is unable to attend a meeting, they still receive related papers in advance of the scheduled meeting and any input they have provided is fully considered.

Our Board

As at 31 March 2019, our Board comprised the Chairman, three Independent Non-Executive Directors, one Non-Executive Director and two Executive Directors. The details of their career background, relevant skills, Committee membership, tenure and external appointments can be found within their individual biographies on pages 34 to 36.

The Chairman and Non-Executive Directors are appointed for a three-year term and continuation of Board appointments are conditional on satisfactory performance and recommendation by the Nominations Committee as to reappointment following the annual Board effectiveness evaluation process. This term can be renewed by mutual agreement, up to a maximum total tenure of nine years.

The composition and effectiveness of the Board is subject to regular review by the Nominations Committee which, in particular, considers the balance of skills, experience and independence of the Board, in accordance with the Group's Board Diversity Policy. The Board Diversity Policy Statement is available on the Severn Trent Plc website.

Any new appointments to the Board result from a formal, rigorous and transparent procedure, responsibility for which is delegated to the Nominations Committee (although decisions on Appointments are a matter reserved to the Board). Further information on the work of the Nominations Committee can be found on pages 46 to 49.

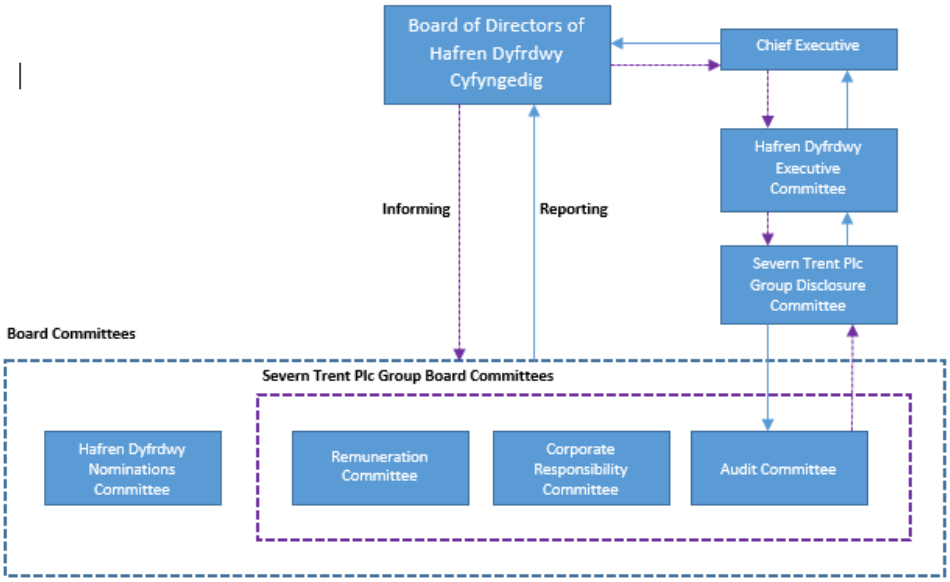
Severn Trent Plc and Hafren Dyfrdwy Cyfyngedig operate as distinct legal entities. The Hafren Dyfrdwy Board's role is to ensure the long term success of Hafren Dyfrdwy. Maintaining the highest standards of governance is integral to the effective delivery of our strategy and ensuring that the Board take decisions that create sustainable long-term value for the mutual benefit of our stakeholders, customers, employees and the communities we serve. The operation of our Board is supported by the collective experience of the Directors and the diverse skills and experience they possess. This enables the Board to reach decisions in a focused and balanced way, supported by independent thought and constructive debate between the Directors. Trust and mutual respect are the cornerstones of relationships between our Directors, with a Board dynamic that supports open and honest conversations to ensure decisions are taken for the benefit of the Company in full consideration of the impact on all stakeholders. Responsibility to all of our stakeholders for the approval and delivery of the Company's strategy and for creating and overseeing the framework to support its delivery sits with the Board.

The requirements of the Board are clearly documented in the Hafren Dyfrdwy Articles of Association and Schedule of Matters Reserved to the Board. They are assisted through the management of agendas, meetings and minutes by Company Secretariat and advised in their meetings by the Company Secretary, where appropriate. There is a clear division of responsibilities between the roles of Chairman and CEO. To allow these responsibilities to be discharged effectively, the Chairman and CEO maintain regular dialogue outside of the Boardroom, to ensure an effective flow of information. The Non-Executive Directors have direct access to senior management at all times. Informal as well as formal contact with the wider business is encouraged to develop a deeper understanding of the Company's operations and requests for further information are welcomed. This broadens the Non-Executive Directors' sources of information and enables them to consider the wider impact of any Board decisions on stakeholders more broadly.

Governance Framework

The Hafren Dyfrdwy Board is supported by a Governance Framework, which is set out below. The Governance Framework comprises the Board, Executive Committee and their respective Committees.

In line with the 2016 UK Corporate Governance Code, the Board delegates certain roles and responsibilities to its various Committees. The Committees assist the Board by fulfilling their roles and responsibilities, focusing on their specific activities, reporting to the Board on decisions and actions taken, and making any necessary recommendations to the Board in line with their terms of reference. They also review whether they have discharged their duties under their terms of reference. The Severn Trent Plc Board regularly reviews the terms of reference of each Committee, with the exception of the Hafren Dyfrdwy Nominations Committee (which were reviewed by the Hafren Dyfrdwy Board during the year). The individual Committee terms of reference are available on the Severn Trent Plc website. The Governance Framework is also subject to periodic review to ensure that it remains appropriate.



Stakeholder engagement

Hafren Dyfrdwy's success depends on the Board taking decisions that deliver mutual benefit to our customers, communities and other stakeholders, as set out in section 172 of the Companies Act. The Board meets with stakeholders throughout the year, a summary of which can be found below:

Customers

- Performance Reports tabled at every Board meeting.
- Extensive customer research considered regularly by the Board in relation to the PR19 plan and submission.
- Board attended some of our PR19 customer research sessions.
- Chair of CCG met the Board.

Communities

- Employees who live and work in our communities meet the Board at site / operational visits.
- Board received updates on the Group's volunteering and educational programmes during the year.
- Board site visit to Lake Vyrnwy Reservoir and Visitor Experience Site.

Employees

- Employee-shareholders had the opportunity to meet the Board at site / operational visits.
- Employee attendance at the Employee Forum, including an opportunity to meet Directors across the Group. Individual Directors provide feedback to the Board following Forum attendance.
- CEO Employee roadshows and senior leader events.
- Board discussion of the QUEST survey results.
- Four Board meetings held at a variety of sites, including operational sites. Directors met a number of employees at these events.

- Board site visits outside of the Board meeting calendar, where Directors met employees and discussed matters with them.
- Internal blogs by Executive Directors.
- Regular senior leader engagement with Executive Directors.

Regulators/ Government

- Regulatory matters regularly considered at Board meetings, including PR19, Water Resources Management Plan and Scheme of Wholesale Charges.
- Regulatory stakeholder attendance at Board meetings during the year.
- Chairman and CEO held regular meetings with Jonson Cox, Ofwat.
- Regulatory consultation updates provided to the Board, including Hafren Dyfrdwy's proposed responses.
- Meetings with the Wales Water Forum.

Suppliers/ Contractors

- Performance Reports tabled at every Board meeting.
- Executive Director attendance at the Employee Forum, including attendance by suppliers, feedback provided to the Board.

The Board in Action

The Board sets the strategy, oversees its delivery and maintains the highest standards of governance which are integral to its delivery. The Board also ensures that, in making its decisions, these create sustainable, long-term value for the mutual benefit of stakeholders. In order for the Company to manage risk effectively, the Board monitors financial performance and reporting and also ensures that appropriate and effective succession planning arrangements and remuneration policies are in place. Below are details of the main topics discussed by the Board during the year.

Main topics discussed by the Board during the year:

Regular Updates

- Performance Review Reports from CEO
- Performance Review Reports from CFO
- Operational Performance Reports
- Reports from the Employee Forum

Financing Strategy

- Budget
- Pension Scheme Update
- Annual Report and Accounts for Hafren Dyfrdwy
- Annual Performance Report for Hafren Dyfrdwy

Governance and Stakeholders

- Board Effectiveness Evaluation
- Review of Committee terms of reference

Regulatory

- PR19
- Annual Report and Accounts
- Annual Performance Report
- Water Resources Management Plan
- Legislation, policy matters and takeover commitments
- Biodiversity Duty for Wales
- Group Data Protection Regulations
- Bribery and Fraud Prevention and Detection Review
- Modern Slavery Act

Strategy

- Review of strategy proposed by executive management
- Water trading opportunities
- Board Strategy day
- Senior Stakeholder Engagement

Culture and Values

- Health, Safety and Wellbeing
- Whistleblowing Reports
- Employee Voice and Workforce Engagement
- Diversity and Inclusion

Risk Management

- Regulatory updates
- Risk reports
- Cyber Review
- Review of Effectiveness of Internal Controls and Risk Management

Board strategy day

In addition to formal meetings at which strategic matters are regularly considered, in December 2018 the Board held a dedicated strategy meeting and visited Nant y Ffrith Reservoir, to focus on Dams and Reservoirs, including managing risk and resilience.

Company purpose and culture

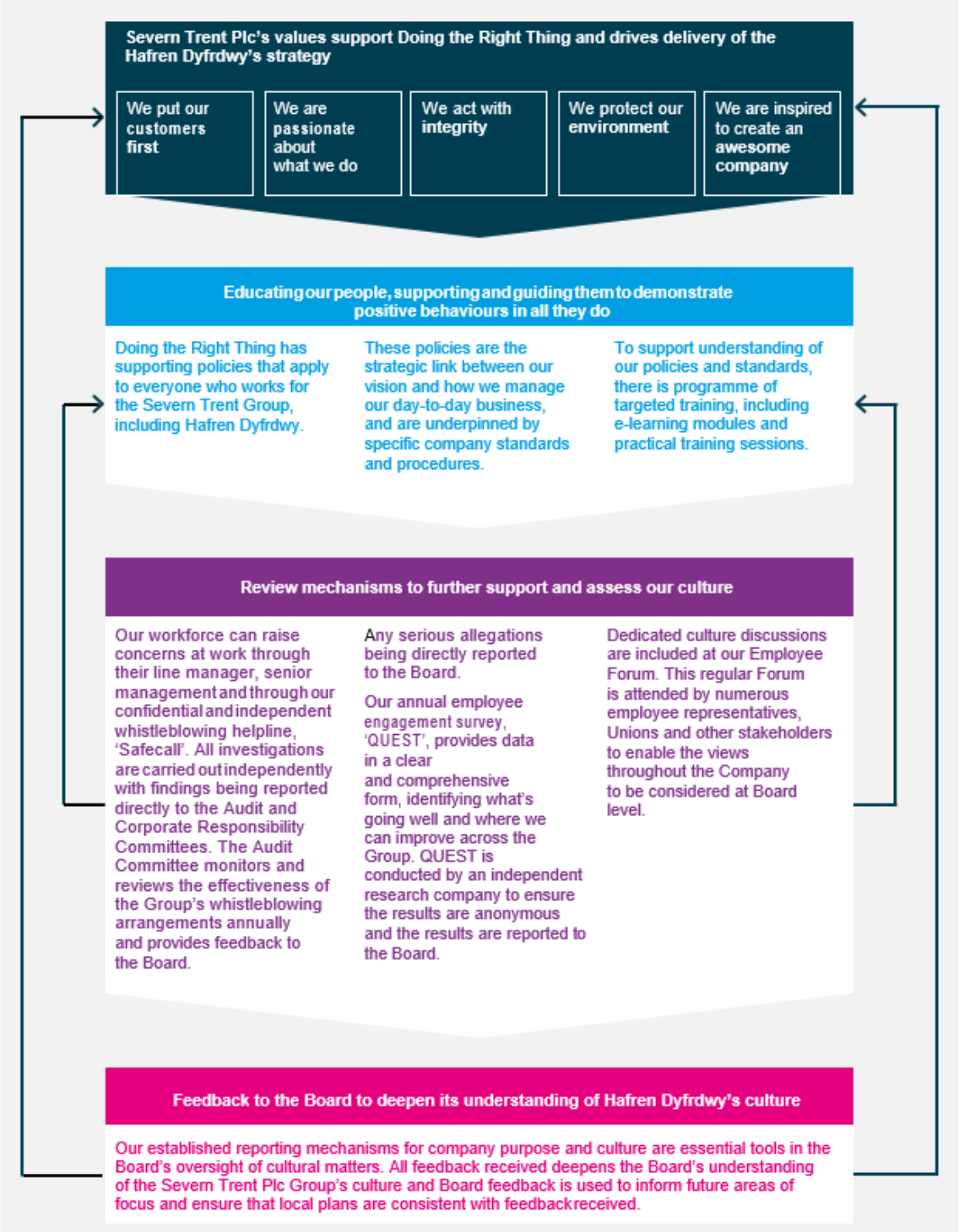
The Board recognises the importance of its role in setting the tone for Hafren Dyfrdwy's culture in line with the culture of the Severn Trent Plc Group. Our Code of Conduct, 'Doing the Right Thing', sets out clearly defined values and standards of behaviour that we expect from everyone who works for, and with, Hafren Dyfrdwy. These values embody the principles by which we operate, and provide a consistent framework for responsible business practices. The supporting policies codify how to identify and deal with suspected wrongdoing, fraud or malpractice; how to ensure that the highest standards of safety are maintained; and how to apply good ethics and sound judgment.

The Board is responsible for establishing Hafren Dyfrdwy's purpose, vision and strategy, and satisfying itself that its culture is aligned. Our purpose – to serve our communities and build a lasting water legacy – reflects 'why' we do what we do. Our strategy provides us with 'what' we do. But the 'how' we deliver our purpose and strategy is what differentiates us and sets us apart and that is driven by our culture, values and behaviours.

During the year, the Board spent time deepening its understanding of Hafren Dyfrdwy's culture, through consideration of the results of the Hafren Dyfrdwy employee survey 'QUEST' and other relevant data.

Additionally, the Board interacts with employees as part of their site visit programme. These direct interactions with employees, specifically in relation to culture, allow the Board to understand first-hand the key issues identified by our workforce, and provides an opportunity to feedback specific insights.

The Board continually monitors, assesses and reinforces the Hafren Dyfrdwy's values and culture to satisfy itself that the behaviours throughout the business are aligned with the Company's purpose. Where misalignment is identified by the Board, appropriate corrective action is taken. No instances of misalignment were identified during the year. Additional detail can be found below.



Board evaluation

The effectiveness of the Board is reviewed at least annually, and conducted according to the guidance set out in the Code and FRC Guidance on Board Effectiveness.

The 2018/19 evaluation was internally conducted by the Chairman with support from the Company Secretary through a series of one-to-one meetings in January and February 2019. The Board agreed actions and that six monthly reviews of progress against recommendations in the report would be tabled for Board discussion.

Evaluation Process

Step 1. 2018/19 Process planning - the Company Secretary undertook a detailed review of the Board Effectiveness evaluation process and made revisions to incorporate recommendations and areas of focus highlighted in the 2018 Code and FRC Guidance on Board Effectiveness.

A process for comprehensive one-to-one meetings was developed for the Board and Nominations Committee.

Step 2. One-to-one meetings - Board members participated in comprehensive one-to-one meetings with the Company Secretary, with appropriate time provided to allow detailed discussion to take place.

Step 3. Evaluation and reporting - the Company Secretary compiled the individual responses, including analysis of themes and proposed actions. A detailed report, setting out the findings of the evaluation was provided to the Chairman for consideration. The Company Secretary and Chairman met to discuss the findings, with the resulting report being tabled to the Board in March 2019.

Step 4. Agree actions and monitor progress - the findings of the evaluation exercise were fully considered and included an assessment of Director independence, time commitment and individual performance.

The Evaluation concluded that the Board and Nominations Committee were effective and that all Directors were considered to have demonstrated considerable commitment and time to their roles. The Board is considered to be of the right size and has an appropriately diverse and complementary mix of background, skills and cognitive thought.

The Board noted that PR19 approval and submission had been particularly well managed and that the use of additional Board Committee meetings and briefing papers had ensured that this topic had not distracted the Board from considering other strategic issues and operational performance oversight. It was also agreed that the Board would monitor and review the effectiveness of the Severn Trent Plc Audit Committee in considering Hafren Dyfrdwy matters.

Board development and knowledge

Training and Continuing Professional Development ('CPD')
As well as Board agenda items, training and CPD sessions in relation to specific topics of interest were presented to the Board during the year, as follows:

- Regulatory financing model;
- Asset management, including practical session in respect of Dams and Reservoirs; and
- Enterprise Risk Management.

The aim of the training sessions is to continually refresh and expand the Board's knowledge and skills. In doing so, the Directors can contribute to discussions on

technical and regulatory matters more effectively. The sessions also serve as an opportunity for the Board to discuss strategy and risks with management below Executive Committee level and gain further direct insight into our businesses and management capability.

Directors' resources

An online resource library and Continuing Professional Development ('CPD') repository is available for use by the Directors, which is continually reviewed and updated. The library includes amongst other things a Corporate Governance Manual and details of Board training sessions. It also contains a further reading section which covers updates and guidance on changes to legislation and corporate governance best practice. The Directors also have access to professional development provided by external bodies and our advisers. CPD requirements were considered, through individual performance review meetings as part of the internally facilitated Board effectiveness review in 2018/19.

Induction programme

Any new appointments to the Board result from a formal, rigorous and transparent procedure, responsibility for which is delegated to the Nominations Committee (although decisions on Appointments are a matter reserved to the Board).

We have an established induction programme in place which can be tailored to meet the requirements of individual Directors and includes the following elements/details:

- Ofwat pre-appointment process;
- Our business and how we are regulated, including performance;
- Strategy;
- Key operations and processes including an immersive, practical journey through the water and waste cycles;
- Key stakeholder relationships;
- Customer delivery;
- Capital delivery and commercial;
- How the business is financed and financial performance;
- Our people and how we work, including health, safety and wellbeing, talent and succession, Trade Unions and an overview of our Remuneration Policy;
- Risk and audit, including the Hafren Dyfrdwy risk profile and our approach to risk;
- Face-to-face meetings with key senior colleagues;
- Directors' duties; and
- Governance matters and Group policies.

We continually enhance the Board's induction process, in full consideration of feedback from new appointees and the Board effectiveness evaluation.

Operational and Site Visits

The Board, and individual Directors, undertake site visits during the year, to deepen their understanding of the Company's operations and further inform the Board's decision making in creating sustainable long-term value for the mutual benefit of stakeholders.

Nominations Committee Report

Nominations Committee meeting attendance 2018/19

The following table shows the attendance of Directors at scheduled Nominations Committee meetings during the year:

Director	Position	Board Meetings
John Coghlan	Chairman	1/1
Sally Jones-Evans	Independent Non-Executive Director	1/1
Mohammed Mehmet	Independent Non-Executive Director	1/1
Ann Beynon	Independent Non-Executive Director	1/1
Andrew Duff	Non-Executive Director	1/1

The members of the Committee in 2018/19 were the Non-Executive Directors of the Board. Only members of the Committee have the right to attend Committee meetings. Other individuals such as the Chief Executive, senior management and external advisers may be invited to attend meetings as and when appropriate.

The Committee's terms of reference were updated in March 2019.

Diversity

The Board and Nominations Committee continue to drive the agenda of diversity across the Company and are proud of the progress made, especially in respect of female representation on the Board (now at 42.8%). At an all-employee level, 79.4% of employees are male and 20.6% are female.

The Board remains focused on promoting broader diversity, and creating an inclusive culture in line with the recommendations from the Parker and McGregor-Smith reviews. A diverse organisation benefits from differences in skills, regional and industry experience, background, race, gender, sexual orientation, religion, belief and age, as well as culture and personality.

As part of Board discussions, recognition was given to the importance and benefits of greater diversity, including gender diversity, social and ethnic background and cognitive and personal strengths throughout the organisation, including on the Board itself. Although no targets have been set at present, the benefits that diversity brings to the Board are wholly recognised by the Committee and is evidenced through the commitments made in the Severn Trent Group Board Diversity Policy. The Group Board Diversity Policy was updated and approved by the Severn Trent Plc Board in January 2019 and is available on the Severn Trent Plc website.

The objectives of the Policy, and an update against each of them, are set out on page 83 of the Severn Trent Plc Annual Report. A copy of the Policy Statement is available on the Severn Trent Plc website.

Talent development

We continue to recognise the importance of developing our people and, as such, talent management remains a key topic of discussion. The Group's five year talent plan focuses on building both technical and leadership capability, and creating talent pipelines for the future.

Director conflicts and independence

Severn Trent Plc has a Conflicts of Interest Policy in place for all Group companies, including Hafren Dyfrdwy, and the Hafren Dyfrdwy Board considers potential conflicts at the outset of every meeting. The first agenda item at every Board meeting ensures that actual and potential conflicts are considered, declared and managed. The Board also formally reviews the authorisation of any potential conflicts of interest every six months.

Additionally, the Hafren Dyfrdwy Board conducted an annual review of individual Director conflict authorisations as recorded in our Conflicts of Interest Register in March 2019. The Conflicts of Interest Register sets out any actual or potential conflict of interest situations which a Director has disclosed to the Board in line with their statutory duties and the practical steps that are to be taken to avoid conflict situations. When reviewing conflict authorisations, the Board considers any other appointments held by the Director as well as the findings of the Board effectiveness evaluation.

The policy continues to be applied practically throughout the year, for example in considering the potential conflict presented by Directors having roles on other Group companies. For example, in September 2018 modifications were made to the Severn Trent Plc Group Audit Committee meeting structure to facilitate dedicated Committee focus for Hafren Dyfrdwy regulatory matters and remove a potential conflict of interest scenario in relation to John Coghlan who is a Director of both Severn Trent Water and Hafren Dyfrdwy.

These arrangements are assisted through the management of separate agenda items for Hafren Dyfrdwy matters, with the Independent Non-Executive Directors of Hafren Dyfrdwy being invited to attend all relevant meetings in respect of Hafren Dyfrdwy matters.

The independence of Directors is formally reviewed annually by the Nominations Committee, and as part of the Board evaluation exercise. The Nominations Committee and Board consider that there are no business or other circumstances that are likely to affect the independence of any Non-Executive Director and that all Non-Executive Directors continue to demonstrate independence.

Conflict of interest process in action: Revised Group governance arrangements

Following the integration of Hafren Dyfrdwy, we reviewed our governance arrangements in full consideration of Ofwat's Board leadership, transparency and governance principles. The Board recognise that there is potential for conflicts of

interest to arise from the existence of shared directorships between Severn Trent Water / Severn Trent Plc and Hafren Dyfrdwy. Our Boards and Committees consider conflicts of interest at the outset of every meeting. In addition, the Boards review the authorisation of any potential conflicts of interest every six months. A conflicts of interest register is maintained by Company Secretariat, and sets out any actual or potential conflict of interest situations disclosed by a Director.

Should a conflict or potential conflict materialise, then we have a documented process which provides that the relevant Director(s) may not take part in the subject matters to which the conflict relates and may not vote in respect of any decision taken in relation to it.

The Group has a Conflicts of Interest Policy to formally record our existing process and ensure there is sufficient independent membership in Board discussions and decision making. The Policy promotes independent decision making by the Boards, specifically in respect of any matters where there might be a conflict between the interests of the Boards and the interests of another part of the Group. This ensures that the Boards act in the interests of their respective stakeholders, including customers. A copy of the Policy is available on the Severn Trent Plc website.

To further support the fulfilment of the objectives outlined above, three additional Independent Non-Executive Directors were appointed to the Hafren Dyfrdwy Board on the 1 April 2018. This resulted in the Board comprising a majority of Independent Non-Executive Directors.

The Board Committees at Group level operate on behalf of Hafren Dyfrdwy, with the Audit and Remuneration Committees providing advice, assurance and recommendations only, ahead of the Hafren Dyfrdwy Board making final decisions. The Severn Trent Plc Audit and Remuneration committees comprise a majority of independent members and are independently led. Any associated assurance in respect of Hafren Dyfrdwy is conducted at a materiality relevant to the size of Hafren Dyfrdwy and risks are considered and managed from an individual Board perspective, with clear and effective governance at individual Board level.

Hafren Dyfrdwy Directors are invited to attend all relevant meetings in respect of Hafren Dyfrdwy matters. Additionally, there is a separate Hafren Dyfrdwy Nominations Committee that comprises Hafren Dyfrdwy Independent Non-Executive Directors only.

Human Rights and Modern Slavery

We are committed to protecting the human rights of our employees and contractors as we have clearly set out in our Code of Conduct, ‘Doing the Right Thing’. We have a responsibility to understand our potential impact on human rights and to mitigate or eliminate any potentially negative impacts. Whilst not having a specific human rights policy, we have Company policies on Human Resources, Anti-Bribery and Anti-Fraud, Whistleblowing (‘Speak Up’) and Procurement.

We will always treat people in our business and supply chain fairly and have a clear zero tolerance approach to modern slavery. To date we have had no instances of modern slavery raised, but we are not at all complacent and are fully committed to

taking the steps needed to protect against modern slavery in our business and supply chain and have robust mechanisms in place to report any concerns. The Severn Trent Group Anti-Slavery and Human Trafficking Statement can be found on the Severn Trent Plc Website.

Whistleblowing

Our employees, and wider workforce, can raise concerns at work through their line manager, senior management and through our confidential and independent whistleblowing helpline, 'Safecall'. All investigations are carried out independently and the findings are reported directly through to the Severn Trent Plc Audit and Corporate Responsibility Committees. The Audit Committee monitors and reviews the effectiveness of the Group's whistleblowing arrangements annually and provides feedback to the Board. Additionally, any serious allegations are directly reported to the Board.

Directors' Remuneration report

Remuneration details

Non-Executive Directors' fees

The three independent Non-Executive Directors of Hafren Dyfrdwy Cyfyngedig received an annual fee for the year ended 31 March 2019. All fees were recharged to the Company.

Non-Executive Director fees remain unchanged for the year ahead.

	2018/19	2017/18	Increase %
Fee paid to all Non-Executive Directors	£30,000	n/a – as not appointed	0%

Non-Executive Directors normally serve for terms of three years. The current expiry date of Sally Jones-Evans', Ann Beynon's and Mohammed Mehmet's Letters of Appointment is 1 April 2021. This term of appointment may be extended for a further three year term by mutual agreement of the Board. However, continuation of their reappointment is conditional on satisfactory performance and recommendation by the Hafren Dyfrdwy Nominations Committee.

The total single figure of remuneration below sets out the remuneration received by the Directors for 2018/19:

	Year ended 31 March 2019		Year ended 31 March 2018	
Non-Executive Directors	**Salary and Fees (£'000)**	**Total (£'000)**	**Salary and Fees (£'000)**	**Total (£'000)**
Sally Jones-Evans	**30.0**	**30.0**	**0.0**	**0.0**
Ann Beynon	**30.0**	**30.0**	**0.0**	**0.0**
Mohammed Mehmet	**30.0**	**30.0**	**0.0**	**0.0**

Chairmans' fees

John Coghlan and Andrew Duff are remunerated as Directors of Severn Trent Plc, and received no additional remuneration in respect of their roles as Directors of Hafren Dyfrdwy during 2018/19.

Executive Directors' remuneration

The Executive Directors of Hafren Dyfrdwy mirror those of Severn Trent Plc. A recharge is made to Hafren Dyfrdwy in respect of a proportion of their time for duties carried out by the Executive Directors on behalf of the Company in 2018/19 and this amounts to £37,900 (2.7%) in relation to the Chief Executive and £16,600 (2.0%) in relation to the Chief Financial Officer.

The recharge for Executive Directors time during 2018/19 reflects the fully embedded resource provided by other senior Severn Trent employees in respect of Hafren Dyfrdwy.

The remuneration of the Executive Directors is determined by the Remuneration Committee of Severn Trent Plc ('the Committee'), and any payments made in relation to the annual bonus scheme or LTIP are determined by Group performance and paid out of Group earnings.

The Remuneration Report of Severn Trent Plc (which can be found in the Severn Trent Plc Annual Report and Accounts on the Severn Trent Plc website) sets out the Remuneration Policy for Executive Directors and other senior executive managers, and the total remuneration paid to those Directors.

Summary of the implementation of the Remuneration Policy in 2019/20
Shareholders approved the Severn Trent Remuneration Policy ('the Policy') at the Severn Trent Plc AGM in 2018 (99.18% voted in favour). Full details of the Policy can be found on the Severn Trent Plc website and a summary is contained in the Severn Trent Plc Remuneration Report on page 104.

A key feature of our remuneration package is that it strongly incentivises improvements in service to every single customer, irrespective of whether they are served under the HD or Severn Trent instrument of appointment. For the annual bonus and LTIPs this is achieved by adding performance, such that every customer is treated equally.

The Committee believes that the fundamental architecture of the Executive Directors' remuneration package is appropriate and the policy remains to attract, retain and motivate its leaders and to ensure they are focused on delivering business priorities within a framework designed to promote the long term success of Severn Trent, aligned with shareholder interests.

Annual Bonus 2019/20
As the Company's strategic priorities evolve, the Committee firmly believes that the operation of the bonus must evolve with it, and as a result the Committee has contacted Severn Trent Plc's 30 largest shareholders representing over 50% of its issued share capital, as well as Glass Lewis, The Investment Association and ISS, to inform them of proposed changes to the operation of our annual bonus for 2019/20. Full details are set out on pages 98 and 106 of this year's Severn Trent Plc Remuneration Report.

In summary, the annual bonus performance measures and weightings for 2019/20 financial year will be as follows:

- Group Profit Before Interest & Tax – 49%
- Resilient Service ODIs – 35%
    - Customer Outcomes (15%)
    - Asset Health (10%); and
    - Environment and Social Outcomes (10%)
- Customer Service – 8%
- Health and Safety (Lost Time Incidents) – 8%

The Committee considers the forward looking performance targets to be commercially sensitive and has, therefore, determined not to disclose them in advance. Details of the targets used will be disclosed in next year's Severn Trent Plc Remuneration Report.

Directors' report

The Directors present their annual report and the audited financial statements of the Company for the year ended 31 March 2019. Under Section 414C (11) of the Companies Act 2006 the directors have opted to disclose information regarding principal risks and uncertainties and future developments in the Strategic Report. The Governance Report set out on pages 32 to 56 is incorporated by reference into this report and, accordingly, should be read as part of this report.

Matters included in the Strategic report
The following matters are included in the Company's Strategic report on pages 3 to 31:

- Principal activity of the Company
- Future developments in the business
- Principal risks and uncertainties

Directors and Directors' Interests
The Directors who held office during the year were as follows:

J B Coghlan
A J Duff
J Bowling
O R Garfield
A Beynon (appointed 1 April 2018)
S Jones-Evans (appointed 1 April 2018)
M Mehmet (appointed 1 April 2018)

None of the Directors have any beneficial interest in the share capital of the Company. The beneficial interests of the Directors in the share capital of the Company's ultimate holding company, Severn Trent Plc, are disclosed within the accounts for Severn Trent Plc.

No Director has any rights to subscribe for shares in, or debenture of the Company.

Directors' remuneration is disclosed on page 50.

Directors' indemnities
The Company's Articles of Association provide that directors of the Company shall be indemnified by the Company against any costs incurred by them in carrying out their duties including defending any proceedings arising out of their positions as directors in which they are acquitted or judgment is given in their favour or relief from any liability is granted to them by the court. This indemnification has been in force throughout the year and up to the date of signing the financial statements.

Areas of operation
During the course of 2018/19, Hafren Dyfrdwy only had activities and operations in the UK.

Research and development
Innovative use of existing and emerging technologies will continue to be crucial to the successful development of new products and processes for the Company and

our products must continue to deliver value for customers. Expenditure on research and development is set out in the Company financial statements.

Internal controls
Further details of our internal control framework can be found on page 38.

Post balance sheet events
Details of post balance sheet events are set out in the Company financial statements.

Capital structure
Details of the Company's issued share capital and of the movements during the year are shown in note 19 to the Company financial statements. The Company has one class of Ordinary Shares which carries no right to fixed income. Each share carries the right to one vote at General Meetings of the Company. The issued nominal value of the Ordinary Shares is 100% of the total issued nominal value of all share capital.

There are no specific restrictions on the size of a holding nor on the transfer of shares, which are both governed by the general provisions of the Articles and prevailing legislation. The Directors are not aware of any agreements between holders of the Company's shares that may result in restrictions on the transfer of securities or on voting rights.

No person has any special rights of control over the Company's share capital and all issued shares are fully paid.

With regard to the appointment and replacement of Directors, the Company is governed by its Articles, the Code, the Companies Act 2006 and related legislation. The Articles may be amended by Special Resolution of the shareholders. The powers of Directors are described in the Hafren Dyfrdwy Matters Reserved to the Board document, the Articles and the Governance report.

Group Structure
The Company's position within the Severn Trent Plc Group can be found on the Severn Trent Plc website.

Dividends
No dividends (2018: £nil) have been paid in the year. The directors do not recommend the payment of a dividend (2018: nil)

Contributions for political and charitable purposes
During the year the Company did not make any contributions to charitable causes (2018: £12,220). In the event donations are made, they are given to charities whose projects align closely with our aim to promote the responsible use of water resources and waste water services which provide the opportunity for longer-term partnerships. Our policy is not to make any donations for political purposes in the UK, or to donate to EU political parties or incur EU political expenditure.
Accordingly Hafren Dyfrdwy did not make any political donations or incurred political expenditure in the financial year under review.

Employees
The average number of employees within the Company is shown in note 6 to the financial statements on page 77.

Hafren Dyfrdwy believes a diverse and inclusive workforce is a key factor in being a successful business. Through our Diversity and Equal Opportunities Policy, the Company seeks to ensure that every employee, without exception, is treated equally and fairly and that all employees are aware of their responsibilities. This means more than ensuring we don't discriminate in any way – we want to create and maintain a culture open to a diverse population. We believe that no one should be hurt or made unwell by what we do. There were no fatalities during the year.

We are an equal opportunities employer and welcome applications from all individuals, including those with a disability. We are fully committed to supporting applications made by disabled persons, and make reasonable adjustments to their environment where possible (having regard to their particular aptitudes and abilities). We are also responsive to the needs of our employees. As such, should any employee become disabled during their time with us, we will actively re-train that employee and make reasonable adjustments to their environment where possible, in order to keep them in employment with us.

All our training, promotion and career development processes are in place for all our employees to access, regardless of their gender, race, age or disability. The provision of occupational health programmes is of crucial importance to Hafren Dyfrdwy with the aim of keeping our employees fit, healthy and well, including an employee assistance programme.

Employee engagement
We continuously engage with our employees in a number of ways to accommodate different working patterns. This includes:

- all people briefings, 'Team Talk';
- communications event and roadshows held across the Company;
- a dedicated intranet, 'Streamline';
- online news portal and weekly roundup, 'Pipeline News';
- an active employee social media presence, 'Yammer';
- conference calls and email;
- leadership engagement channels – Executive Director blogs, senior management monthly visibility programme and quarterly events;
- Employee Forum; and
- regular meetings with Trade Unions.

We provide opportunities for employees to give their feedback to the Company in a number of ways, from team or shift meetings, our Employee Forum and QUEST. More information on employee engagement can be found in the stakeholder engagement section on page 39.

Internal Controls
The Board is responsible for the Company's Internal Control systems and for reviewing their effectiveness. The Severn Trent Plc Audit Committee regularly monitors and reviews the effectiveness of the Severn Trent Group's systems of

Internal Control, including Risk Management, financial, operational and compliance aspects, in accordance with the requirements of the Code and the Guidance, and appropriate systems have been in place for the year ending 31 March 2019 and up to the date of the Annual Report. This is described in the Severn Trent Plc Audit Committee report on page 89 of the Severn Trent Plc Annual Report. The Internal Control system can provide only reasonable and not absolute assurance against material misstatement or loss, as it is designed to manage rather than eliminate the risk of failure to achieve business objectives.

Annual Performance Report of Hafren Dyfrdwy Cyfyngedig

The Annual Performance Report for Hafren Dyfrdwy Cyfyngedig is prepared and sent to Ofwat. A copy of this will be available on the website of Hafren Dyfrdwy or on request to the Company Secretary. There is no charge for this publication.

By order of the Board

James Bowling
Director
9 July 2019

Directors' responsibilities statement

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 101 "Reduced Disclosure Framework". 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 judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the 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 are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

Responsibility statement

Each of the Directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- the Strategic report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- The Annual Report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

Auditor and disclosure of information to the auditor

In the case of each of the persons who are Directors of the Company at the date when this report is approved:

- so far as each of the Directors is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- each of the Directors has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Relevant audit information means information needed by the Company's auditor in connection with preparing its report. This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

Deloitte LLP has indicated its willingness to continue as auditor.

By order of the Board

James Bowling

Director
9 July 2019

John Coghlan
Chairman
9 July 2019

Independent auditor's report to the members of Hafren Dyfrdwy Cyfyngedig (formerly Hafren Dyfrdwy Limited)

Report on the audit of the financial statements

Opinion

In our opinion:

- **the financial statements of Hafren Dyfrdwy Cyfyngedig (formally Hafren Dyfrdwy Limited) (the 'company') give a true and fair view of the state of the company's affairs as at 31 March 2019 and its loss for the year then ended;**
- **the financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 101 "Reduced Disclosure Framework"; and**
- **the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.**

We have audited the financial statements which comprise:

- the income statement;
- the statement of comprehensive income;
- the balance sheet;
- the statement of changes in equity; and
- the related notes to the financial statements 1 to 22.

The financial reporting framework that has been applied in the preparation of the company financial statements is applicable law and United Kingdom Accounting Standards, including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Summary of our audit approach

Key audit matters	The key audit matters that we identified in the current year were: • Valuation of the provision for trade and other receivables; • Valuation of the retirement benefit surplus; and • Classification and valuation of capital expenditure.
Materiality	The materiality that we used for the current year was £606,000, which was determined on the basis of 2% of revenue.
Scoping	Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

Conclusions relating to going concern, principal risks and viability statement

Going concern

We have reviewed the directors' statement on page 31 to the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them

We confirm that we have nothing material to report, add or draw

and their identification of any material uncertainties to the company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements.

We considered as part of our risk assessment the nature of the company, its business model and related risks including where relevant the impact of Brexit, the requirements of the applicable financial reporting framework and the system of internal control. We evaluated the directors' assessment of the company's ability to continue as a going concern, including challenging the underlying data and key assumptions used to make the assessment, and evaluated the directors' plans for future actions in relation to their going concern assessment.

attention to in respect of these matters.

Principal risks and viability statement

Based solely on reading the directors' statements and considering whether they were consistent with the knowledge we obtained in the course of the audit, including the knowledge obtained in the evaluation of the directors' assessment of the company's ability to continue as a going concern, we are required to state whether we have anything material to add or draw attention to in relation to:

- the disclosures on pages 19 to 24 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation on page 19 that they have carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity; or
- the directors' explanation on pages 25 and 31 as to how they have assessed the prospects of the company, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We confirm that we have nothing material to report, add or draw attention to in respect of these matters.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Valuation of the provision for trade and other receivables	
Key audit matter description	A portion of household customers do not or cannot pay their bills which results in the need for provisions to be made for non-payment of the customer balance. Management makes estimates regarding the expected future loss rate when calculating the provision for trade and other receivables and this process requires the exercise of significant judgement. The bad debt charge of £1.4 million (2018: £1.5 million) represents 3.2% (2018: 2.5%) of household revenue and amounts billed relating to

	customers of Welsh Water and 2.0% (2018: 1.6%) of non-household revenue. The company's provisions against trade and other receivables are included in note 15. We identified a key audit matter relating to the valuation and accuracy of the bad debt provision, in particular the appropriateness of management's use of Severn Trent Water Limited provisioning rates to derive the company's provision. The accounting policy for the provision for trade receivables is disclosed in note 1(l) and management has included this as a key source of estimation uncertainty in note 2 to the financial statements.
How the scope of our audit responded to the key audit matter	We have challenged and critically reviewed the assumptions used in the calculation of the bad debt provision as follows: • Assessed the design and implementation of key management review controls over the bad debt provision model; • Tested the completeness and accuracy of the information used in calculating the bad debt provision to verify the age of debt used within the bad debt model; and • Assessed the rationale for rates used based on current and expected cash collection performance, in particular the appropriateness of the Severn Trent Water collection rates being applied to trade and other receivables.
Key observations	We are satisfied that the assumptions applied in assessing the overall bad debt provision are reasonable and we consider changes to the basis of estimation of the bad debt provision to be appropriate.
Valuation of the retirement benefit surplus	
Key audit matter description	Valuation of the retirement benefit surplus is an area involving significant estimation because the process is complex and requires management (after taking advice from their actuarial advisers) to make a number of assumptions concerning the discount rate, inflation rate, pension increases, and the longevity of current pensioners in order to determine the value of the scheme's liabilities. The key audit matter is focused on the valuation of the pension scheme liabilities and the appropriateness of the actuarial assumptions that are used to calculate it, specifically with reference to the discount rate. The company's retirement benefit surplus as at 31 March 2019 is £18.6 million (2018: £18.2 million) as set out in note 14 to the financial statements. The accounting policy for the provision for retirement benefit schemes is disclosed in note 1(m) and management has included this as a key source of estimation uncertainty in note 2 to the financial statements.
How the scope of our audit responded to the key audit matter	We have challenged the assumptions applied by performing the following procedures: • Evaluated the design and implementation of management's key control over the review of the appropriateness of the actuarial assumptions; • With the support of our pension specialists within our audit team, we challenged the assumptions used in the calculation of the pension scheme surplus as detailed in note 14 specifically challenging the discount rate with reference to comparable market and other third party data; and • Assessed whether there had been any changes in the

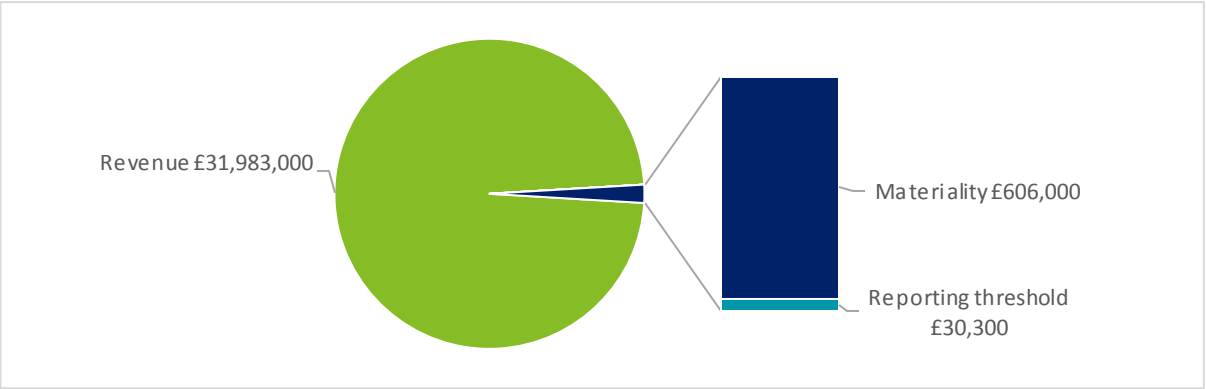
	methodology to determine the assumptions since the prior year.
Key observations	We are satisfied that management's assumptions in the valuation of the retirement benefit obligation are appropriate and apply a consistent valuation methodology to previous periods.
Classification and valuation of capital expenditure	
Key audit matter description	The company has a substantial capital programme which has been agreed with the regulator ("Ofwat") and therefore incurs significant expenditure in relation to the development and maintenance of both infrastructure and non-infrastructure assets. Property, plant and equipment ("PPE") additions in the year which were external to the Severn Trent Plc Group were £12.3 million (2018: £14.1million) of the total additions of £119.7 million (2018: £14.1 million) disclosed in note 13. As the classification of capital expenditure, operating expenditure and infrastructure renewals expenditure directly affects the company's reported financial performance we identified a key audit matter relating to an overstatement of capital expenditure, whether by changing the company's capex implementation guidance and/or incorrect application of these guidelines. Due to the level of judgement involved, we have determined that there was a potential for fraud through possible manipulation of this balance. Management has included this is a critical accounting judgement in note 2 to the financial statements.
How the scope of our audit responded to the key audit matter	We performed the following procedures to respond to the key audit matter: • Reviewed the capitalisation policy and implementation guidance to understand any changes in the current year and to determine compliance with the relevant accounting standards; • Evaluated the design and implementation of controls over the application of the policy to expenditure incurred on projects within the capital programme during the year; • Tested whether there have been any changes in the application of the policy; and • For a sample of capital projects, assessed the application of the capitalisation policy to the costs incurred by reviewing the business cases and invoices, and obtaining further explanations and support for significant changes in capital expenditure from budget.
Key observations	We are satisfied that the classification and valuation of assets capitalised in the year is appropriate.

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Materiality	£606,000 (2018: £547,000)
Basis for determining materiality	Materiality has been determined based on 2% of revenue for the year (2018: 2% of revenue)
Rationale for the benchmark applied	Revenue has been used as the benchmark as it is a key driver of financial performance.



We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £30,300 (2018: £27,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our audit was scoped by obtaining an understanding of the company and its environment, including internal control, and assessing the risks of material misstatement. Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon.

We have nothing to report in respect of these matters.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

In this context, matters that we are specifically required to report to you as uncorrected material misstatements of the other information include where we conclude that:

- *Fair, balanced and understandable* – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy, is materially inconsistent with our knowledge obtained in the auditor

- *Audit committee reporting* – the section describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the company and their environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- the company financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made.

We have nothing to report in respect of this matter.

Use of our report

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

Kate Hadley, FCA (Statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
Birmingham, United Kingdom
9 July 2019

Hafren Dyfrdwy Cyfyngedig (formerly Hafren Dyfrdwy Limited)

Income statement
For the year ended 31 March 2019

	Note	2019 £'000	2018 £'000
Turnover	3	**31,983**	28,209
Operating costs before exceptional items and charge for bad and doubtful debts		**(32,816)**	(20,766)
Charge for bad and doubtful debts		**(1,355)**	(1,501)
Exceptional operating costs	4	**(400)**	–
Total operating costs		**(34,571)**	(22,267)
(Loss)/profit before interest, tax and exceptional items	5	**(2,188)**	5,942
Exceptional operating costs	4	**(400)**	–
(Loss)/profit before interest and tax		**(2,588)**	5,942
Finance income	8	**1,700**	1,700
Finance costs before exceptional items	9	**(5,023)**	(4,420)
Exceptional finance costs	4	**(21,949)**	**–**
Net finance costs		**(25,272)**	(2,720)
(Loss)/profit on ordinary activities before taxation		**(27,860)**	3,222
Current tax	10	**6,772**	(1,617)
Deferred tax	10	**(1,148)**	650
Taxation on loss/profit on ordinary activities		**5,624**	(967)
(Loss)/profit for the year		**(22,236)**	2,255

All results are from continuing operations in both the current and preceding year.

Statement of comprehensive income

For the year ended 31 March 2019

	2019 £'000	2018 £'000
(Loss)/profit for the year	**(22,236)**	2,255
Other comprehensive income for the year		
Items that will not be reclassified to the income statement:		
Net actuarial gains	**400**	8,100
Tax on net actuarial gains	**(68)**	(1,385)
	332	6,715
Total comprehensive (loss)/income for the year	**(21,904)**	8,970

Hafren Dyfrdwy Cyfyngedig (formerly Hafren Dyfrdwy Limited)

Balance sheet

At 31 March 2019

	Note	**2019 £'000**	2018 £'000
Non-current assets			
Other intangible assets	12	**8,772**	4,548
Property, plant and equipment	13	**192,369**	110,168
Retirement benefit surplus	14	**18,644**	18,205
		219,785	132,921
Current assets			
Inventory		**522**	434
Trade and other receivables	15	**30,819**	23,080
Current tax receivable		**258**	–
Cash and cash equivalents		**328**	908
		31,927	24,422
Current liabilities			
Borrowings	16	**(612)**	(478)
Trade and other payables	17	**(17,994)**	(23,213)
Current tax payable		**–**	(877)
		(18,606)	(24,568)
Net current assets/(liabilities)		**13,321**	(146)
Non-current liabilities			
Borrowings	16	**(49,158)**	(62,482)
Trade and other payables	17	**(11,837)**	(11,162)
Deferred tax	18	**(15,675)**	(14,296)
		(76,670)	(87,940)
Net assets		**156,436**	44,835
Equity			
Called up share capital	19	**133,051**	240
Other reserves		**614**	614
Fair value reserve		**11,685**	11,685
Retained earnings		**11,086**	32,296
Equity attributable to owners of the Company		**156,436**	44,835

The financial statements were approved by the Board of Directors on 9 July 2019. They were signed on its behalf by:

James Bowling
Director
9 July 2019
Company Number: 03527628

Hafren Dyfrdwy Cyfyngedig (formerly Hafren Dyfrdwy Limited)

Statement of changes in equity
For the year ended 31 March 2019

	Equity attributable to owners of the Company				
	Share capital	Other reserves	Fair value reserve	Retained earnings	Total
	£'000	£'000	£'000	£'000	£'000
At 1 April 2017	240	614	11,685	23,326	35,865
Profit for the year	–	–	–	2,255	2,255
Net actuarial gains	–	–	–	8,100	8,100
Tax on net actuarial gains	–	–	–	(1,385)	(1,385)
Total comprehensive income for the year	–	–	–	8,970	8,970
At 1 April 2018 as previously reported	240	614	11,685	32,296	44,835
Restatement (note 1 b)ii))	–	–	–	694	694
At 1 April 2018 restated	240	614	11,685	32,990	45,529
Loss for the year	–	–	–	(22,236)	(22,236)
Net actuarial gains	–	–	–	400	400
Tax on net actuarial gains	–	–	–	(68)	(68)
Total comprehensive loss for the year	–	–	–	(21,904)	(21,904)
Share issue	132,811	–	–	–	132,811
At 31 March 2019	**133,051**	**614**	**11,685**	**11,086**	**156,436**

Other reserves represent reserves arising from previous Schemes of Arrangement accounted for under the principles of merger accounting.

The fair value reserve arose on the revaluation of infrastructure assets to fair value on transition to FRS 101.

Notes to the financial statements

1. Accounting policies

a) Accounting convention

The financial statements have been prepared on the going concern basis (see Strategic report) under the historical cost convention as modified by the revaluation of certain financial assets and liabilities (including derivative instruments) at fair value, and in accordance with applicable United Kingdom Accounting Standards and comply with the requirements of the United Kingdom Companies Act 2006 ('the Act'). The principal accounting policies, which have been applied consistently in the current and preceding year are set out below.

Hafren Dyfrdwy Cyfyngedig (the Company) is a private company limited by shares incorporated in the United Kingdom under the Companies Act 2006 and is registered in Wales.

b) Basis of preparation

i) General

The Company is a wholly owned subsidiary of Severn Trent Plc and is included in the consolidated financial statements of Severn Trent Plc.

The Company meets the definition of a qualifying entity under FRS 100 Application of Financial Reporting Requirements. Accordingly, the Company has elected to apply FRS 101 Reduced Disclosure Framework. Therefore the recognition and measurement requirements of EU-adopted IFRS have been applied, with amendments where necessary in order to comply with the Companies Act 2006 and The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) as these are Companies Act 2006 accounts.

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available under that standard in relation to share based payment, financial instruments, capital management, presentation of comparative information in respect of certain assets, presentation of a cash flow statement, standards not yet effective, impairment of assets and related party transactions.

Where required, equivalent disclosures are given in the group financial statements of Severn Trent Plc. The group financial statements of Severn Trent Plc are available to the public and can be obtained as set out in note 22.

ii) New accounting policies

In the current financial year the Company has adopted IFRS 9 "Financial Instruments" and IFRS 15 "Revenue from Contracts with Customers".

IFRS 9 replaces the provisions of IAS 39 that relate to the recognition, classification and measurement of financial assets and financial liabilities.

Provisions against trade receivables were calculated under the previous accounting policy using historical collection information and losses expected as a result of future events were not recognised. Under IFRS 9 the Company recognises a provision for the lifetime expected credit losses for trade receivables. In accordance with the transitional provisions in IFRS 9, comparative figures have not been restated.

The total impact on the Company's retained earnings as at 1 April 2018 is as follows:

	£'000
Closing retained earnings 31 March 2018 – IAS 39	32,296
Decrease in provision for trade receivables	857
Deferred tax on above adjustment	(163)
Adjustment to retained earnings from adoption of IFRS 9 on 1 April 2018	694
Opening retained earnings 1 April 2018 – IFRS 9	**32,990**

1. Accounting policies (continued)

b) Basis of preparation (continued)

ii) New accounting policies (continued)

Under IFRS 15, there was no change to the recognition of revenue from charges for water or waste water services. The policy for recognition of charges for water and waste water services is set out in note 1 c). The performance obligations are satisfied by the provision of water and waste water services and this was also the basis for recognising revenue under the previous accounting standard.

There was no change to the recognition of contributions from developers. The policy for recognition of contributions from developers is set out in note 1 i). The performance obligations for this income are satisfied through the ongoing supply of water and waste water services to the relevant property and this was also the basis for recognising revenue under the previous accounting standard.

c) Revenue

Revenue includes turnover and interest income.

Turnover represents the fair value of consideration receivable, excluding value added tax, trade discounts and inter-company sales, in the ordinary course of business for goods and services provided.

Turnover is not recognised until the service has been provided to the customer or the goods to which the sale relates have either been despatched to the customer or, where they are held on the customer's behalf, title has passed to the customer and it is probable that it will be received.

Water and waste water revenue is recognised when the service is provided and includes an estimate of the amount of mains water and waste water charges unbilled at the year end. The accrual is estimated using a defined methodology based upon a measure of unbilled water consumed by tariff, which is calculated from historical billing information.

Commission income is earned on amounts billed on behalf of other water companies for the sewerage services they provide to the Company's customers. Commission is recognised when the bill is sent to the customer.

Interest income is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable.

d) Exceptional items

Exceptional items are income or expenditure, which individually or, if of a similar type, in aggregate s hould, in the opinion of the directors, be disclosed by virtue of their size or nature if the financial statements are to give a true and fair view.

e) Taxation

Current tax payable is based on taxable profit for the year and is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred taxation is provided in full on taxable temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred taxation is measured on a non-discounted basis using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred tax liability is settled.

Current and deferred tax are recognised in profit or loss, except where they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income or directly in equity, respectively. Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

A deferred tax asset is only recognised to the extent it is probable that sufficient taxable profits will be available in the future to utilise it.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets

against current tax liabilities.

1. Accounting policies (continued)

f) Borrowings

All borrowings are initially recognised at fair value less issue costs. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest rate method whereby interest and issue costs are charged to the income statement and added to the carrying value of borrowings at a constant rate in proportion to the capital amount outstanding.

Index-linked debt is adjusted for changes in the relevant inflation index and changes in value are charged to finance costs.

g) Other intangible non-current assets

Intangible assets acquired separately are capitalised at cost. Following initial recognition, finite life intangible assets are amortised on a straight-line basis over their estimated useful economic lives as follows:

	Years
Software	3 - 10

Amortisation charged on intangible assets is taken to the income statement through operating costs.
Finite life intangible assets are reviewed for impairment where indicators of impairment exist (see j) below).
Intangible assets with indefinite useful lives are carried at cost less accumulated impairment losses. Such assets are reviewed for impairment at least annually and where indications of impairment exist in accordance with the policy set out in j) below.

Development expenditure is capitalised as an intangible asset and written off over its expected useful economic life where the following criteria are met:

- it is technically feasible to create and make the asset available for use or sale;
- there are adequate resources available to complete the development and to use or sell the asset;
- there is the intention and ability to use or sell the asset;
- it is probable that the asset created will generate future economic benefits; and
- the development costs can be measured reliably.

Research expenditure is expensed when it is incurred.

h) Property, plant and equipment

Property, plant and equipment is held at cost (or at deemed cost for infrastructure assets on transition to IFRS/FRS 101) less accumulated depreciation. Expenditure on property, plant and equipment relating to research and development projects is capitalised and depreciated over the expected useful life of those assets.

The costs of like for like replacement of infrastructure components are recognised in the income statement as they arise. Expenditure which results in enhancements to the operating capability of the infrastructure networks is capitalised.

Where items of property, plant and equipment are transferred to the Company from customers or developers, the fair value of the asset transferred is recognised in the balance sheet. Fair value is determined based on estimated depreciated replacement cost. Where the transfer is in exchange for connection to the network and there is no further obligation, the corresponding credit is recognised immediately in turnover. Where the transfer is considered to be linked to the provision of ongoing services the corresponding credit is recorded in deferred income and released to operating costs over the expected useful lives of the related assets.

Where assets take a substantial period of time to get ready for their intended use, the borrowing costs directly attributable to the acquisition, construction or production of these assets are added to their cost.

Property, plant and equipment is depreciated, using the straight-line method, to its estimated residual value over its estimated useful life, with the exception of freehold land which is not depreciated. Assets in the course of construction are not depreciated until commissioned.

1. Accounting policies (continued)

h) Property, plant and equipment (continued)

The estimated useful lives are:

Fixed asset category	Type of asset	Estimated useful life
Freehold land and buildings	Buildings and service reservoirs	30 – 80 years
Infrastructure assets	Impounding reservoirs	250 years
	Raw water aqueducts	250 years
	Water mains	80 – 150 years
Fixed plant and equipment	Fixed plant	20 – 40 years
	Equipment	20 – 40 years
	Water meters	10 – 20 years
	Mobile plant and vehicles	2 – 15 years

i) Grants and contributions

Grants and contributions received in respect of non-current assets, including certain charges made as a result of new connections to the water and sewerage networks, are treated as deferred income and released to operating costs over the useful economic life of those non-current assets.

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

j) Impairment of non-current assets

At each balance sheet date, the Company reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs of disposal and value in use at the date the impairment review is undertaken. 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 for which the estimates of the future cash flows have not been adjusted.

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

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

k) Inventory

Inventory is stated at cost less provision for surplus or obsolete inventory.

1. Accounting policies (continued)

l) Trade and other receivables

Trade receivables and accrued income are measured at fair value on initial recognition. If there is objective evidence that the asset is impaired, it is written down to its recoverable amount and the irrecoverable amount is recognised as an expense in operating costs.

The Company applies the simplified approach permitted by IFRS 9 for estimating expected credit losses on trade receivables. For trade receivables that are assessed not to be impaired individually, expected credit loss es are estimated based on the Company's historical experience of trade receivable write-offs.

m) Retirement benefits

(i) Defined benefit schemes

The difference between the value of defined benefit pension scheme (the scheme) assets and defined benefit pension scheme liabilities is recorded on the balance sheet as a retirement benefit asset or obligation.

The scheme assets are measured at fair value using bid price for assets with quoted prices. For scheme assets with no quoted price, the fair value is derived by using quotations from independent third parties or by using applicable valuation techniques at the end of each reporting period. The scheme liabilities are measured at the balance sheet date by an independent actuary using the projected unit method and discounted at the current rate of return on high quality corporate bonds of equivalent term and currency to the liability.

Service cost, representing the cost of employee service in the period, is included in operating costs. Net finance cost is calculated by applying the discount rate used for the scheme liabilities to the net obligation. Finance income and cost is disclosed separately in the income statement. In previous periods these amounts were shown net and have been represented to be shown separately.

Changes in the retirement benefit obligation that arise from:

- differences between the return on scheme assets and interest income included in the income statement;
- actuarial gains and losses from experience adjustments; and
- changes in demographic or financial assumptions,

are classified as re-measurements, charged or credited to other comprehensive income and recorded in the statement of comprehensive income in the period in which they arise.

(ii) Defined contribution scheme

Contributions to defined contribution pension schemes are charged to the income statement in the period in which they fall due.

2. Critical accounting judgments and key sources of estimation uncertainty

In the process of applying the Company's accounting policies, the Company is required to make certain judgments, estimates and assumptions that it believes are reasonable based on the information available. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results may ultimately differ from those estimates.

Critical accounting judgments

i) Classification of costs between operating expenditure and capital expenditure

Hafren Dyfrdwy's business involves significant construction and engineering projects. Assessing the classification of costs incurred on such projects between capital expenditure and operating expenditure requires judgments to be made. The judgments are made based on objective criteria that the Company has developed to facilitate the consistent application of its accounting policies.

During the year, the Company has reassessed the classification of costs in relation to the water mains renewal programme. We have deemed costs in relation to the programme not be an enhancement to the operating capability of the asset and therefore have recognised costs of £2.0m in the income statement in the current financial year.

Sources of estimation uncertainty

i) Depreciation and carrying amounts of property, plant and equipment

Calculating the depreciation charge and hence the carrying value for property, plant and equipment requires estimates to be made of the useful lives of the assets. The estimates are based on engineering data and the Company's experience of similar assets. Details are set out in note 1 h). A five year change in the average remaining useful lives of property, plant and equipment would result in a £1.1 million change in the depreciation charge.

ii) Retirement benefit obligations

Determining the amount of the Company's retirement benefit obligations and the net costs of providing such benefits requires assumptions to be made concerning long-term interest rates, inflation and longevity of current and future pensioners. Changes in these assumptions could significantly impact the amount of the obligations or the cost of providing such benefits. The Company makes assumptions concerning these matters with the assistance of advice from independent, qualified actuaries. Details of the assumptions made and associated sensitivities are set out in note 14 to the financial statements.

iii) Provision for impairment of trade receivables

Determining the expected credit losses for trade receivables requires estimates of the future collection performance based on past experience and expected future developments as a result of conditions at the balance sheet date. Details of the amounts provided and charged to the income statement are set out in note 15. A change of 200 basis points in the expected credit loss rate would change the amount charged to the income statement by £607,000.

3. Revenue

	2019	2018
	£'000	£'000
Water and waste water services	**30,280**	25,051
Commission	**1,703**	3,156
Other services	**–**	2
Turnover	**31,983**	28,209
Finance income	**1,700**	1,700
	33,683	29,909

4. Exceptional items

	2019 £'000	2018 £'000
GMP equalisation costs	**400**	–
Exceptional finance costs	**21,949**	–
	22,349	–

On 25 October 2018, the High Court issued a judgment in the Lloyds Bank case in relation to gender equality in Guaranteed Minimum Pension rights that has an impact on the Company's defined benefit pension liabilities. An exceptional charge of £0.4 million was incurred for the provision following this judgment.

The exceptional finance cost of £21.9 million arose from the premium payable on the redemption of £34.0 million of the Company's index-linked loan in exchange for the issue of ordinary shares.

5. (Loss)/profit before interest and tax

	2019 £'000	2018 £'000
(Loss)/profit before interest and tax is stated after charging/(crediting):		
Depreciation - infrastructure assets	**1,112**	477
Depreciation - non-infrastructure assets	**4,891**	4,927
Amortisation of intangible assets	**733**	39
Profit on disposal of property, plant and equipment	**–**	(204)
Staff costs (see note 6)	**6,274**	7,344
Hired and contracted services	**7,986**	1,735
Infrastructure maintenance expenditure	**4,152**	789

During the year the following fees were charged by the auditor:

	2019 £'000	2018 £'000
Fees payable to the Company's auditor for:		
- the audit of the Company's annual accounts	**45**	51
Total audit fees	**45**	51
Fees payable to the Company's auditor and its associates for other services:		
- other assurance services	**26**	20
Total non-audit fees	**26**	20

No other fees were payable to the auditor (2018: nil).

6. Staff numbers and costs

The average number of persons employed by the Company (including Directors) during the year was as follows:

	2019 number	2018 number
Direct staff	**133**	137

The aggregate payroll costs of these persons was as follows:

	2019 £'000	2018 £'000
Wages and salaries	**5,049**	6,180
Social security costs	**462**	468
Pension costs defined benefit plans (note 14)	**600**	488
Pension costs defined contribution plans (note 14)	**163**	208
Total staff costs	**6,274**	7,344

7. Directors' remuneration

The amounts paid to Non-Executive Directors in respect to their services to the Company was £90,000 (2018: nil) which was paid by other group companies.

The Executive Directors do not receive remuneration for their services within the Company. The emoluments of the Executive Directors are paid by other companies within Severn Trent Group.

Amounts paid to past Directors in respect of loss of office was nil (2018: £137,612).

8. Finance income

	2019 £'000	2018 £'000
Interest income on defined benefit scheme assets (note 14)	**1,700**	1,700
Total finance income	**1,700**	1,700

9. Finance costs

	2019 £'000	2018 £'000
Interest charged on:		
Amounts payable to group companies	**3,685**	2,960
Finance leases	**18**	–
Bank and other loans	**120**	60
Interest cost on defined benefit scheme assets (note 14)	**1,200**	1,400
Total finance costs before exceptional items	**5,023**	4,420

Borrowing costs of £1,808,000 (2018: £1,056,000) incurred funding eligible capital projects have been capitalised at an interest rate of 4.0% (2018: 6.0%). Tax relief of £344,000 (2018: £201,000) was claimed on these costs, which was credited to the income statement, offset by a related deferred tax charge of £307,000 (2018: £180,000).

10. Taxation

a) Analysis of tax (credit)/charge in the year

	2019 £'000	2018 £'000
Current UK corporation tax at 19% (2018: 19%)		
Current year	**(6,627)**	288
Prior year adjustment	**(145)**	1,329
Total current tax	**(6,772)**	1,617
Deferred tax		
Origination and reversal of temporary differences:		
- current year	**1,302**	333
- prior year adjustment	**(154)**	(983)
Total deferred tax	**1,148**	(650)
Total tax (credit)/charge	**(5,624)**	967

b) Factors affecting the tax (credit)/charge in the year

The tax assessed for the current year is lower (2018: higher) than the standard rate of corporation tax in the UK of 19% (2018: 19%).

The differences are explained below:

	2019 £'000	2018 £'000
(Loss/)profit on ordinary activities before tax	**(27,860)**	3,222
Tax at the standard rate of corporation tax in the UK 19% (2018: 19%)	**(5,293)**	612
Tax effect of depreciation on non-qualifying assets	**140**	46
Non-deductible expenses	**–**	2
Adjustment in respect of prior years	**(298)**	346
Current year impact of rate change	**(173)**	(39)
Total tax (credit)/charge	**(5,624)**	967

The exceptional operating costs generated a deferred tax credit of £68,000 and the exceptional finance costs generated a current tax credit of £4,170,000.

c) Tax charged directly to equity

In addition to the amount charged to the income statement, the following amounts have been charged directly to equity:

	2019 £'000	2018 £'000
Deferred tax		
Tax on actuarial gains	**(68)**	(1,385)

11. Dividends

Dividends paid in the year were nil (2018: nil).

12. Other intangible assets

	Computer software £'000
Cost	
At 1 April 2017	–
Additions	4,587
At 1 April 2018	4,587
Additions	4,957
At 31 March 2019	**9,544**
Amortisation	
At 1 April 2017	–
Amortisation for the year	(39)
At 1 April 2018	(39)
Amortisation for the year	(733)
At 31 March 2019	**(772)**
Net book value	
At 31 March 2019	**8,772**
At 31 March 2018	4,548

13. Property, plant and equipment

	Land and buildings £'000	Infrastructure assets £'000	Fixed plant and equipment £'000	Assets under construction £'000	Total £'000
Cost					
At 1 April 2017	74,077	68,744	19,904	–	162,725
Additions	–	–	–	14,042	14,042
Disposals	(9,273)	–	(7,700)	–	(16,973)
Reclassifications	(60,228)	9,255	50,891	82	–
At 1 April 2018	4,576	77,999	63,095	14,124	159,794
Additions	20,196	64,317	14,657	20,481	119,651
Disposals	(2,109)	(22,373)	(21,620)	(2,287)	(48,389)
At 31 March 2019	**22,663**	**119,943**	**56,132**	**32,318**	**231,056**
Depreciation					
At 1 April 2017	(27,350)	(19,398)	(14,447)	–	(61,195)
Charge for the year	(89)	(477)	(4,838)	–	(5,404)
Disposals	9,273	–	7,700	–	16,973
Reclassifications	16,120	(2,729)	(13,391)	–	–
At 1 April 2018	(2,046)	(22,604)	(24,976)	–	(49,626)
Charge for the year	(597)	(1,112)	(4,294)	–	(6,003)
Disposals	1,258	7,078	8,606	–	16,942
At 31 March 2019	**(1,385)**	**(16,638)**	**(20,664)**	**–**	**(38,687)**
Net book value					
At 31 March 2019	**21,278**	**103,305**	**35,468**	**32,318**	**192,369**
At 31 March 2018	2,530	55,395	38,119	14,124	110,168

In the current year, a number of assets were transferred between Severn Trent Water Limited and the Company as part of of the boundary alignment discussed in the Strategic report. These assets were transferred at book value. Included in additions above are assets of £107 million which were transferred from Severn Trent Water Limited and disposals at cost of £48 million with accumulated depreciation of £17 million transferred to Severn Trent Water Limited. This resulted in a net increase of £76 million in property, plant and equipment.

14. Retirement benefit schemes

a) Defined benefit pension scheme

(i) Background

The Company participates in the Water Companies Pension Scheme, a defined benefit pension scheme in the UK. This is a sectionalised scheme and the Company participates in the Dee Valley Water Limited section of the scheme. The scheme funds are administered by trustees and are independent of the Company's finances. Contributions are paid to the scheme in accordance with recommendations of an independent, qualified actuarial advisor. The section has a history of raising pensions in line with inflation, and these increases are reflected in the measurement of the obligation. The section is closed to new entrants.

The trustees are required to act in the best interests of the schemes beneficiaries. A formal actuarial valuation of the scheme is carried out on behalf of the trustees at triennial intervals by an independent, professionally qualified actuary. Under the defined benefit pension scheme, members are entitled to retirement benefits calculated by reference to their pensionable service and pensionable salary history, with inflationary pension increases applying in line with the scheme rules.

The UK defined benefit pension scheme and the date of the last completed formal actuarial valuation as at the accounting date is as follows:

	Date of last formal actuarial valuation
Water Companies Pension Scheme – Dee Valley Water Limited Section (DVWS)	31 March 2017

(ii) Amount included in the balance sheet arising from the Company's obligations under the defined benefit pension scheme

	2019	2018
	£'000	£'000
Fair value of assets	**66,644**	65,005
Present value of the defined benefit obligations	**(48,000)**	(46,800)
Net asset recognised in the balance sheet	**18,644**	18,205

	2019	2018
	£'000	£'000
Fair value of scheme assets		
Equities	**–**	10,005
Diversified growth funds	**–**	5,300
Liability-driven investment funds (LDI)	**33,000**	42,400
Emerging markets multi-asset funds	**–**	3,900
High-yield bonds	**31,305**	3,400
Cash	**2,339**	–
	66,644	65,005

The majority of the assets have quoted prices in active markets, but there are small proportions of the equity and LDI investments which are unquoted.

14. Retirement benefit schemes (continued)

Movements in the fair value of the scheme assets were as follows:

	2019	2018
	£'000	£'000
Fair value at 1 April	**65,005**	70,854
Interest income on scheme assets	**1,700**	1,700
Contributions from the sponsoring companies	**339**	597
Contributions from scheme members	**100**	203
Return on plan assets (excluding amounts included in finance income)	**1,700**	(400)
Expenses paid	**(200)**	(149)
Benefits paid	**(2,000)**	(7,800)
Fair value at 31 March	**66,644**	65,005

Movements in the present value of the defined benefit obligations were as follows:

	2019	2018
	£'000	£'000
Present value at 1 April	**(46,800)**	(61,009)
Service cost	**(200)**	(488)
Exceptional past service cost	**(400)**	–
Interest cost	**(1,200)**	(1,400)
Contributions from scheme members	**(100)**	(203)
Actuarial gains arising from changes in demographic assumptions	**900**	4,000
Actuarial (losses)/gains arising from changes in financial assumptions	**(2,200)**	4,700
Actuarial losses arising from experience adjustments	**–**	(200)
Benefits paid	**2,000**	7,800
Present value at 31 March	**(48,000)**	(46,800)

(iii) Amounts recognised in comprehensive income in respect of defined benefit pension scheme

The amounts recognised in the income statement are as follows:

	2019	2018
	£'000	£'000
Current service cost	**(200)**	(488)
Exceptional past service cost	**(400)**	–
Administrative expenses	**(200)**	–
Interest income on scheme assets	**1,700**	1,700
Interest cost	**(1,200)**	(1,400)
Total amount charged to the income statement	**(300)**	(188)

14. Retirement benefit schemes (continued)

The amounts recognised immediately in other comprehensive income are as follows:

	2019	2018
	£'000	£'000
Net actuarial gains/(losses) in the year due to:		
- Changes in financial assumptions	**(2,200)**	4,700
- Changes in demographic assumptions	**900**	4,000
- Experience adjustments on defined benefit obligations	**–**	(200)
Actuarial gains/(losses) on assets relative to interest on assets	**1,700**	(400)
Gain recognised in other comprehensive income	**400**	8,100

Actuarial gains and losses have been reported in the statement of comprehensive income.

(iv) Actuarial risk factors

The scheme typically exposes the Company to actuarial risks such as investment risk, inflation risk and longevity risk.

Investment risk

The Company's contributions to the scheme are based on actuarial calculations which make assumptions about the returns expected from the scheme's investments. If the investments underperform against these assumptions in the long-term, then the Company might need to make additional contributions to the scheme in order to fund the payment of accrued benefits.

Each plan's investment strategy seeks to balance the level of investment return sought with the aim of reducing volatility and risk. In undertaking this approach reference is made to both the maturity of liabilities and the funding level of that plan. A number of further strategies are employed to manage underlying risks, including liability matching asset strategies, diversification of asset portfolios and interest rate hedging.

The Section does not invest directly in property occupied by the Company or in financial securities issued by the Company. The investment strategy is set by the Trustee of the Section. Currently the plan has a balanced approach, investing in lower risk assets (e.g. liability driven instruments, which respond to factors such as changes in interest rates) alongside higher risk assets (e.g. high-yield bonds).

Inflation risk

The benefits payable to members of the scheme are linked to inflation measured by the RPI or CPI, subject to caps. The Company's contributions to the scheme are based on assumptions about the future level of inflation. If inflation is higher than the levels assumed in the actuarial calculations then the Company may need to make additional contributions to the Scheme in order to fund the payment of accrued benefits.

The scheme uses Liability Driven Investment ("LDI") within the asset portfolio to hedge against the value of liabilities changing as a result of movements in long-term interest rate and inflation expectations. This structure allows the scheme to both hedge against these risks and retain capital investment in assets that are expected to generate higher returns.

Longevity risk

The Company's contributions to the scheme are based on assumptions about the life expectancy of scheme members after retirement. If scheme members live longer than assumed in the actuarial calculations then the Company may need to make additional contributions to the scheme in order to fund the payment of accrued benefits.

14. Retirement benefit schemes (continued)

(v) Actuarial assumptions

The major financial assumptions used in the accounting valuation of the obligations for the Company were as follows.

	2019	2018
	% pa	% pa
Price inflation – RPI	**3.2**	3.1
Price inflation - CPI	**2.2**	2.1
Discount rate	**2.5**	2.7
Pension increases in payment	**3.2**	3.1

The assumption for price inflation is derived from the difference between the yields on longer term fixed rate gilts and on index-linked gilts.

In setting our discount rate, we construct a yield curve. Short-dated yields are taken from market rates for AA corporate bonds. Long-dated yields for the curve are based on the average yield available on all long-dated AA corporate bonds. We project the expected cash flows of the schemes and adopt a single equivalent cash flow weighted discount rate based on this constructed yield curve.

The mortality assumptions are based on those used in the latest triennial funding valuation. The mortality assumptions adopted at the year end for accounting purposes and the life expectancies at age 65 implied by the assumptions are as follows:

	2019		2018	
	Men	**Women**	Men	Women
Mortality table used	**S2NMA**	**S2NFA**	S2NMA	S2NFA
Mortality table compared with standard table	**95%**	**99%**	95%	99%
Mortality projections	**CMI 2018**	**CMI 2018**	CMI 2017	CMI 2017
Future improvement per annum	**1.0%**	**1.0%**	1.0%	1.0%
Remaining life expectancy for members currently aged 65 years	**21.9**	**23.6**	22.4	24.1
Remaining life expectancy at age 65 for members currently aged 45 years	**22.9**	**24.8**	23.4	25.3

The calculation of the scheme obligations is sensitive to the actuarial assumptions and in particular to the assumptions relating to discount rate, price inflation (capped, where relevant) and mortality. The following table summarises the estimated impact on the Company's obligations from changes to key actuarial assumptions whilst holding all other assumptions constant.

Assumption	**Change in assumption**	**Impact on disclosed obligations**
Discount rate[1]	Increase/decrease by 0.1% pa	Decrease/increase by £0.7/£0.8 million
Price inflation[2]	Increase/decreased by 0.1% pa	Increase/decrease by £0.6 million
Mortality[3]	Increase in life expectancy by 1 year	Increase by £2.1 million

1 A change in discount rate is likely to occur as a result of changes in bond yield and as such would be expected to be offset to a significant degree by a change in the value of the bond assets held by the plans.
2 The projected impact resulting from a change in RPI reflects the underlying effect on pensions in payment, pensions in deferment and resultant increases in salary assumptions.
3 The change in assumption is based on triennial valuations and reflect the fact that life expectancy rates are expected to increase.

14. Retirement benefit schemes (continued)

(vi) Effect on future cash flows

Additional deficit contributions ceased in March 2018. Contribution rates are set in consultation with the trustees for the Section and each participating employer.

The weighted average duration of the expected benefit obligation from the Section at the end of the year is 15 years (2018: 16 years).

b) Defined contribution pension schemes

The Company also operates a defined contribution scheme. The pension cost charge for the period represents contributions payable by the Company to the scheme and amounts to £163,179 (2018: £208,000).

There were no outstanding or prepaid contributions either at the beginning or end of the financial year.

15. Trade and other receivables

	2019	2018
	£'000	£'000
Current assets		
Trade receivables	**8,195**	5,038
Bad debt provision	**(1,847)**	(2,882)
Net trade receivables	**6,348**	2,156
Amounts receivable from parent and fellow subsidiary undertakings	**17,229**	9,850
Other amounts receivable	**2,773**	7,514
Prepayments	**275**	66
Accrued income	**4,194**	3,494
	30,819	23,080

The carrying values of trade and other receivables are reasonable approximations of their fair values .

Doubtful debt provision

The Company has a statutory obligation to provide water and sewerage services to customers within its region. Therefore there is no concentration of credit risk with respect to its trade receivables and the credit quality of its customer base reflects the wealth and prosperity of all of the commercial businesses and domestic households within its region.

Movements on the doubtful debts provision were as follows:

	2019	2018
	£'000	£'000
At 1 April as previously reported	**3,739**	2,875
Restatement (note 1 b)ii))	**(857)**	–
At 1 April restated	**2,882**	2,875
Provision against trade receivables	**696**	644
Increase in provision against other amounts receivable	**597**	857
Provision against accrued income	**62**	–
Amounts transferred to Severn Trent Water due to boundary change	**(382)**	–
Amounts written off during the year	**(870)**	(637)
At 31 March	**2,985**	3,739

15. Trade and other receivables (continued)

The aged analysis of trade receivables that are specifically provided for is as follows:

	2019	2018
	£'000	£'000
Up to 1 year	**–**	998
1 - 2 years	**–**	859
2 - 3 years	**–**	510
More than 3 years	**438**	515
	438	2,882

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

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

	2019	2018
	£'000	£'000
Up to 1 year	**1,003**	857
1 - 2 years	**1,130**	–
2 - 3 years	**273**	–
More than 3 years	**141**	–
	2,547	857

The provision as a % of aged gross debt is as follows:

	2019	2018
	%	%
Up to 1 year	**9**	10
1 - 2 years	**34**	–
2 - 3 years	**40**	–
More than 3 years	**80**	–

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

			2019			2018
	Gross	**Provision**	**Net**	Gross	Provision	Net
	£'000	**£'000**	**£'000**	£'000	£'000	£'000
Accrued income – not due	**4,256**	**(62)**	**4,194**	3,494	–	3,494
Other amounts receivable	**3,849**	**(1,076)**	**2,773**	8,371	(857)	7,514
Trade receivables						
Not due	**–**	**–**	**–**	–	–	–
Overdue not specifically provided	**7,496**	**(1,409)**	**6,348**	2,156	–	2,156
Overdue and specifically provided	**699**	**(438)**	**–**	2,882	(2,882)	–
	16,300	**(2,985)**	**13,315**	16,903	(3,739)	13,164

16. Borrowings

	2019 £'000	2018 £'000
Current		
Bank overdrafts	**612**	478
Non-current		
Other loans	**107**	108
Loans due to parent company	**49,051**	62,374
	49,158	62,482
	49,770	62,960

Loans due to parent company comprises of the following:

	2019 £'000	2018 £'000
Index-linked loan	**22,861**	55,084
Floating rate loan	**26,190**	7,290
	49,051	62,374

The loan principal on the index-linked loan is adjusted annually by changes in the Retail Prices Index. Interest on the loan is charged on the indexed principal at 3.635% per annum. The loan matures on 29 September 2032. This loan has decreased due to a part repayment of £34 million of the principal in the form of shares as part of the debt for equity arrangement with Severn Trent Water Limited.

Interest on the floating rate loan is charged interest at LIBOR + 1.5%. The loan facility of £30 million matures on 8 March 2022.

17. Trade and other payables

	2019 £'000	2018 £'000
Current liabilities		
Trade payables	**668**	369
Amounts owed to ultimate parent undertaking	**84**	4,258
Amounts owed to parent and fellow subsidiary undertakings	**8,988**	1,032
Social security and other taxes	**118**	341
Other payables	**5,075**	15,528
Deferred income	**176**	194
Accruals	**2,885**	1,491
	17,994	23,213
Non-current liabilities		
Deferred income	**11,837**	11,162
	29,831	34,375

18. Deferred tax

	Accelerated tax depreciation	Retirement benefit surplus	Other	Total
	£'000	£'000	£'000	£'000
At 1 April 2017	(11,913)	(1,674)	26	(13,561)
Credit/(charge) to income	677	(36)	9	650
Charge to equity	–	(1,385)	–	(1,385)
At 1 April 2018 as previously reported	(11,236)	(3,095)	35	(14,296)
Restatement (note 1 b)ii))	–	–	(163)	(163)
At 1 April restated	(11,236)	(3,095)	(128)	(14,459)
(Charge)/credit to income	(1,270)	(6)	128	(1,148)
Charge to equity	–	(68)	–	(68)
At 31 March 2019	**(12,506)**	**(3,169)**	**–**	**(15,675)**

19. Share capital

	2019	2018
	£'000	£'000
Total issued and fully paid share capital		
133,051,089 (2018: 240,404) ordinary shares of £1 each	**133,051**	240

On 28 March 2019, the Company increased its issued and fully paid share capital by allotting 132,810,685 shares for the nominal share value of £1 each as a result of the debt for equity exchange between Hafren Dyfrdwy Cyfyngedig and Severn Trent Water Limited.

20. Capital commitments

At 31 March 2019 the Company had capital commitments as follows:

	2019	2018
	£'000	£'000
Contracted for but not provided in the financial statements	**3,690**	3,156

21. Related party transactions

In accordance with the exemption allowed by FRS 101, no disclosure is made of transactions with other wholly owned companies which are consolidated into the Severn Trent Plc Group.

There were no other related party transactions.

22. Ultimate parent undertaking

The immediate parent undertaking is Severn Trent Water Limited, a company registered in England and Wales.

Severn Trent Water Limited is the parent undertaking of the smallest group to consolidate these financial statements. Financial statements for Severn Trent Water Limited can be obtained from The Company Secretary, Severn Trent Water Limited, P.O. Box 5309, Coventry, CV3 9FH.

The Directors regard Severn Trent Plc, a company registered in England and Wales, as being the Company's ultimate holding company and controlling party. Severn Trent Plc is the largest group for which group accounts are drawn up and of which the Company is a member. Financial statements for Severn Trent Plc can be obtained from Severn Trent Plc's registrars at Equiniti, Aspect House, Spencer Road, Lancing, West Sussex, BN99 6DA.