Financial Statements

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Independent Auditors' report to the members of Affinity Water Limited

Report on the audit of the financial statements

Opinion

In our opinion, Affinity Water Limited's financial statements:

- Give a true and fair view of the state of the company's affairs as at 31 March 2022 and of its loss and cash flows for the year then ended;
- Have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law); and
- Have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Annual Report and Financial Statements (the "Annual Report"), which comprise: the Statement of financial position as at 31 March 2022; the Income statement, the Statement of comprehensive income, the Statement of changes in equity and the Statement of cash flows for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our audit approach

Context

The terms of the company's licence under the Water Industry Act 1991 require the company to report as if it had issued equity share capital listed on the London Stock Exchange and therefore the opinion below refers to the Listing Rules of the Financial Conduct Authority.

There have been a number of changes to our key audit matters for the year ended 31 March 2022, as set out in further detail below. We have also specifically set out our consideration of the impact of climate change on the audit.

In planning our audit, we have considered the impact that the company has on the environment through its operations and the impact the environment, including the current and potential future impact of climate change, has on the company's business and its financial statements. We did not identify any additional risks of material misstatement in this respect.

Whilst it is acknowledged that the physical and transition risks posed by climate change have the potential to impact the company over the medium to long-term, in particular given the commitment to achieve net zero carbon from operations by 2030, management has assessed that there is no quantitatively material impact arising from climate change on the judgements and estimates made in the financial statements for the year ended 31 March 2022.

However, we have made additional considerations throughout the performance of our audit to address areas which are commonly seen to be impacted by the risks associated with climate change, including the assumptions made as part of the assessment of the company to continue as a going concern, the long term viability of the company and the appropriateness of the useful economic lives of material non-current assets. We have not identified any material exceptions through the procedures performed.

We have also considered and obtained comfort over the consistency of the disclosures in relation to climate change made in the other information within the Annual Report with both the financial statements and the knowledge we obtained from our audit.

Overview

Audit scope

- The company has one finance function, with the audit being carried out by one team.
- In scoping our audit, with reference to our risk assessment, we identified and included all material financial statement line items within the scope of our audit procedures.

Key audit matters

- Accuracy of the measured income accrual.
- Adequacy of loss allowance for trade receivables.
- Assessment of cost capitalisation.

Materiality

- Overall materiality: £3.8 million (2021: £3.9 million) based on 3.5% of the earnings before interest, tax, depreciation and amortisation ('EBITDA') (2021: 3.5% of the three year average EBITDA).
- Performance materiality: £2.9 million (2021: £2.9 million).

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the 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) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, 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.

This is not a complete list of all risks identified by our audit.

'Assessment of cost capitalisation' is a new key audit matter this year. 'Impact of the Covid-19 pandemic', which was a key audit matter last year, is no longer included because the impact of Covid-19 was not considered to be an area of most significance to our audit, with the level of audit effort spent considering and responding to this risk on the financial reporting judgements or estimates, and the execution of the audit, having reduced compared to the prior year. Otherwise, the key audit matters below are consistent with last year.

Key audit matter	How our audit addressed the key audit matter
Accuracy of the measured income accrual Refer to page 148 (Audit, Risk and Assurance Committee Report), page 211 (accounting policies) and page 228 (note 12). A measured income accrual of £41.0 million (31 March 2021: £36.7 million) has been recognised relating to revenue from the provision of water services to metered household customers that had not been billed at the year end date. The determination of the measured income accrual impacts directly on both reported revenue and operating profit. The measured income accrual accounts for the timing difference between the last meter reading and the estimated consumption of water from that point to the year end and is calculated based on the average consumption over the past two years by small geographical groupings of customers. Given the range of factors underlying this estimate, there is a risk that the measured income accrual and associated revenue could be materially misstated.	The measured income accrual is a manual calculation prepared using data from the Hi-Affinity billing system. We understood the methodology and ensured that it had been applied consistently with previous years. We also tested the mechanics of the spreadsheet used to calculate the measured income accrual. In respect of the integrity of the data within Hi-Affinity, we tested the design and operating effectiveness of key controls within the revenue and receivables cycle, including the reconciliation of reports produced from the Hi-Affinity billing system and the revenue journals posted to the general ledger, and the quarterly review of tariff changes made in the Hi-Affinity billing system. We also validated the accuracy of the data within Hi-Affinity by agreeing a sample of meter readings to the system and tracing actual consumption to the bills raised. To assess the overall reasonableness of the accrual, we performed an independent roll forward of the accrual recognised at 31 March 2021 to calculate an expected accrual at 31 March 2022, reflecting the underlying changes in the number of metered customers, pricing tariffs, levels of water consumption and the timing of meter readings. In order to assess the ability of management to prepare appropriate estimates in respect of the measured income accrual, we evaluated the historical accuracy of the estimation process by comparing the bills raised through the year to the amount accrued at 31 March 2021. We also compared the billing subsequent to 31 March 2022 and extrapolated the difference identified against the remainder of the accrual. Based on the procedures performed, we did not identify any material misstatements. We also assessed the disclosures in respect of the measured income accrual and consider these to be appropriate.

Independent Auditors' report to the members of Affinity Water Limited

continued

Key audit matter	How our audit addressed the key audit matter
Adequacy of loss allowance for trade receivables Refer to page 148 (Audit, Risk and Assurance Committee Report), page 211 (accounting policies), page 228 (note 12) and page 245 (note A4). The loss allowance for trade receivables of £33.0 million (31 March 2021: £34.0 million) was calculated by applying a range of different percentages to trade receivables based on their respective ageing, with higher percentages applied to those categories of trade receivables which are considered to be of greater risk. Some customers have difficulty paying their bills or, in certain instances, choose not to pay them. As a result, given there are limited steps that a water company can take to recover debt from household customers, there is an ongoing risk of aged trade receivables not being collected, with this risk being heightened by the economic impact of the increased cost of living being experienced by customers. In order to account for the increased risk of credit loss as a result of the increased cost of living, consistent with the assessment performed in respect of the impact of Covid-19 in the prior year, management have made use of a third-party tool (Acorn consumer classification) to segment their existing customers into demographic segments. These demographic segments were then grouped into three risk buckets (low, medium and high) and allocated a percentage reflecting management's estimate of the likelihood of potential default. The weighted average across the three buckets was then used to calculate an incremental loss allowance for trade receivables to reflect the increased risk caused by the increased cost of living. Given the quantum of trade receivables, and the range of assumptions used in preparing the loss allowance for trade receivables, there is a risk that this estimate could be materially misstated.	We reviewed the methodology for calculating the underlying loss allowance for trade receivables and ensured it had been consistently applied with the prior year. We also understood and tested the mechanics of the spreadsheet used to calculate the initial loss allowance, the measurement basis (measured and unmeasured) and the methodology applied to calculate provision rates and agreed that they are consistent with the prior year. To ensure the appropriate classification of customers into sub-categories to apply the historical expected credit loss methodology, we selected a sample of trade receivables and tested that they have been allocated the appropriate provision rate based on ageing, customer type and measurement basis. In addition, we compared the actual rates used in the calculation of the loss allowance to prior year rates and reviewed the level of bad debt write offs which occurred during the year ended 31 March 2022 to assess the ability of management to prepare appropriate estimates. For the additional loss allowance recognised in relation to the increased cost of living, we assessed management's use of the Acorn consumer classification system and considered this to be a reasonable basis for the assessment performed. We also reviewed the demographic groupings assigned to the household customers and the subsequent risk grouping performed by management. We applied sensitivity analysis on this additional adjustment to consider the risk of this being materially understated or overstated, in light of both cash collection rates and the current economic outlook. Based on the procedures performed, we did not identify any material differences within the loss allowance for trade receivables. We also assessed the disclosures in respect of the loss allowance for trade receivables and consider these to be appropriate.

Key audit matter	How our audit addressed the key audit matter
Assessment of cost capitalisation Refer to page 148 (Audit, Risk and Assurance Committee Report), page 211 (accounting policies), page 224 (note 6) and page 245 (note A4). The additions to assets under construction during the year amounted to £136.0 million (year ended 31 March 2021: £128.1 million). These additions arose as a result of the fact that the company capitalises expenditure with respect to its infrastructure assets where such expenditure enhances or increases the capacity of the network, or relates to material replacements of network components. The allocation of costs between capital and non-capital spend can be judgemental and has a direct on profitability in any given year. The key judgement is management's assessment of what constitutes enhancement compared to maintenance expenditure and the allocation of overheads. Given the magnitude of capital spend, there is a risk that incorrect classification could give rise to a material misstatement.	We reviewed the process for allocating costs to capital projects and are satisfied that this allocation was made on an appropriate basis and is in line with the company's capitalisation policy. We selected a sample of items capitalised in the year and ensured these were consistent with the company's accounting policy and were appropriately capitalised in line with IAS 16. We challenged the assumptions and judgements made in allocating overheads to capital projects, through understanding the nature of activities performed. We also performed a review of a number of capital projects, comparing their current status to that of the approved management plan to understand the nature of the work being performed, whether the status of the project is in line with the initial approved budget and the anticipated timelines set out in the plan. We then used this information to challenge, where appropriate, the accounting treatment of these projects as at 31 March 2022. Overall, we consider the costs capitalised as at 31 March 2022 to be materially appropriate. We also assessed the disclosures in respect of the capitalisation of costs and consider these to be appropriate.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the company, the accounting processes and controls, and the industry in which it operates.

The company has one finance function, with the audit being carried out by one team.

In scoping our audit, with reference to our risk assessment, we identified and included all material financial statement line items within the scope of our audit procedures.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

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

Overall company materiality	£3.8 million (2021: £3.9 million).
How we determined it	Based on 3.5% of the earnings before interest, tax, depreciation and amortisation ('EBITDA') (2021: 3.5% of the three year average EBITDA).
Rationale for benchmark applied	We have used EBITDA as this is the measure that management focus on internally within their reporting. The use of EBITDA is also consistent with the prior year, though a three year average was used in the prior year due to the impact of Covid-19 on profitability.

We use performance materiality to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds overall materiality. Specifically, we use performance materiality in determining the scope of our audit and the nature and extent of our testing of account balances, classes of transactions and disclosures, for example in determining sample sizes. Our performance materiality was 75% (2021: 75%) of overall materiality, amounting to £2.9 million (2021: £2.9 million) for the company financial statements.

In determining the performance materiality, we considered a number of factors - the history of misstatements, risk assessment and aggregation risk and the effectiveness of controls - and concluded that an amount at the upper end of our normal range was appropriate.

We agreed with those charged with governance that we would report to them misstatements identified during our audit above £0.2 million (2021: £0.2 million) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Independent Auditors' report to the members of Affinity Water Limited

continued

Conclusions relating to going concern

Our evaluation of the directors' assessment of the company's ability to continue to adopt the going concern basis of accounting included:

- Testing the mathematical accuracy of the base case going concern model prepared by management and agreeing this to Board approved budgets;
- Assessing the inputs and underlying assumptions of the base case model;
- Assessing the accuracy of the cash flow forecast prepared in the prior year so as to obtain assurance of the ability of management to prepare accurate forecasts;
- Assessing the downside scenario which has been used to sensitise the base case model, including consideration of the underlying assumptions; and
- Reviewing management's analysis of both liquidity and covenant compliance to ensure there is sufficient liquidity and no forecast covenant breaches during the going concern period.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the company's ability to continue as a going concern.

In relation to the directors' reporting on how they have applied the UK Corporate Governance Code, we have nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information, which includes reporting based on the Task Force on Climate-related Financial Disclosures (TCFD) recommendations. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance 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 an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of 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. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' Report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on our work undertaken in the course of the audit, the Companies Act 2006 requires us also to report certain opinions and matters as described below.

Strategic Report and Directors' Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 31 March 2022 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report.

Corporate governance statement

ISAs (UK) require us to review the directors' statements in relation to going concern, longer-term viability and that part of the corporate governance statement relating to the company's compliance with the provisions of the UK Corporate Governance Code, which the Listing Rules of the Financial Conduct Authority specify for review by auditors of premium listed companies. Our additional responsibilities with respect to the corporate governance statement as other information are described in the Reporting on other information section of this report.

Based on the work undertaken as part of our audit, we have concluded that each of the following elements of the corporate governance statement is materially consistent with the financial statements and our knowledge obtained during the audit, and we have nothing material to add or draw attention to in relation to:

- The directors' confirmation that they have carried out a robust assessment of the emerging and principal risks;
- The disclosures in the Annual Report that describe those principal risks, what procedures are in place to identify emerging risks and an explanation of how these are being managed or mitigated;
- The directors' statement in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, 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;
- The directors' explanation as to their assessment of the company's prospects, the period this assessment covers and why the period is appropriate; and
- The directors' 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 its assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Our review of the directors' statement regarding the longer-term viability of the group was substantially less in scope than an audit and only consisted of making inquiries and considering the directors' process supporting their statement; checking that the statement is in alignment with the relevant provisions of the UK Corporate Governance Code; and considering whether the statement is consistent with the financial statements and our knowledge and understanding of the company and its environment obtained in the course of the audit.

In addition, based on the work undertaken as part of our audit, we have concluded that each of the following elements of the corporate governance statement is materially consistent with the financial statements and our knowledge obtained during the audit:

- The directors' statement that they consider the Annual Report, taken as a whole, is fair, balanced and understandable, and provides the information necessary for the members to assess the company's position, performance, business model and strategy;
- The section of the Annual Report that describes the review of effectiveness of risk management and internal control systems; and
- The section of the Annual Report describing the work of the audit committee.

We have nothing to report in respect of our responsibility to report when the directors' statement relating to the company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified under the Listing Rules for review by the auditors.

Independent Auditors' report to the members of Affinity Water Limited

continued

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of directors' responsibilities in respect of the financial statements, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they 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.

Auditors' 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 auditors' 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.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the company and industry, we identified that the principal risks of non-compliance with laws and regulations related to industry regulation, including the requirements of The Water Services Regulation Authority ('Ofwat'), health and safety regulation (including the requirements of The Health and Safety at Work etc Act 1974) and environmental regulation, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the financial statements such as the Listing Rules, UK tax legislation, pensions legislation and the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries to increase revenue or reduce expenditure, in doing so increasing overall profitability, and management bias within accounting estimates, in particular the potential manipulation of the measured income accrual, loss allowance for trade receivables or the extent of costs capitalised. Audit procedures performed by the engagement team included:

- Discussions with management, internal audit and the company's legal team, including inquiring of known or suspected instances of non-compliance with laws and regulation and fraud, and review of board minutes and internal audit reports;
- Discussions with the General Counsel and Head of Ethics & Compliance to discuss both the litigation report and summary of whistleblowing matters arising;
- Challenging assumptions made by management when preparing accounting estimates, in particular those that involve the assessment of future events, which are inherently uncertain – the key estimates determined in this respect are those relating to the measured income accrual and loss allowance for trade receivables; and
- Identifying and testing journal entries posted, such as those with unusual account combinations or those posted by senior management.

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the financial statements. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

Our audit testing might include testing complete populations of certain transactions and balances, possibly using data auditing techniques. However, it typically involves selecting a limited number of items for testing, rather than testing complete populations. We will often seek to target particular items for testing based on their size or risk characteristics. In other cases, we will use audit sampling to enable us to draw a conclusion about the population from which the sample is selected.

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 auditors' report.

Use of this report

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies Act 2006 exception reporting

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

- We have not obtained 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
- Certain disclosures of directors' remuneration specified by law are not made; or
- The financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Other voluntary reporting

Directors' remuneration

The company voluntarily prepares a Remuneration report in accordance with the provisions of the Companies Act 2006. The directors requested that we audit the part of the Remuneration report specified by the Companies Act 2006 to be audited as if the company were a quoted company.

In our opinion, the part of the Remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

Simon Bailey (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Watford

13 July 2022

Income statement
for the year ended 31 March 2022

(Registered Number 02546950)

	Note	2022 £000	2021 (restated) £000
Revenue	1	**319,747**	286,782
Cost of sales		**(258,553)**	(243,634)
Gross profit		**61,194**	43,148
Administrative expenses		**(38,159)**	(40,621)
Impairment losses on financial and contract assets	2.1	**(7,444)**	(8,318)
Other operating income	2.2	**18,972**	17,657
Operating profit	2	**34,563**	11,866
Finance income	4	**16,043**	15,770
Finance costs	4	**(102,873)**	(48,621)
Fair value loss on inflation swaps	4	**(31,295)**	(32,452)
Net finance costs	4	**(118,125)**	(65,303)
Fair value gain on energy swaps		**27,988**	–
Loss before tax		**(55,574)**	(53,437)
Income tax (expense)/credit	5	**(41,331)**	10,311
Loss for the financial year		**(96,905)**	(43,126)

All results of the company in the current year and prior year are from continuing operations.

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs, and to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

The notes on pages 211 to 255 are an integral part of these financial statements.

Statement of comprehensive income
for the year ended 31 March 2022

(Registered Number 02546950)

	Note	2022 £000	2021 (restated) £000
Loss for the financial year		**(96,905)**	(43,126)
Other comprehensive income/(expense) for the year which will not be reclassified to profit or loss:			
Re-measurements of post-employment benefit assets	10	**28,749**	(32,162)
Deferred tax (charge)/credit on items that will not be reclassified	5	**(7,187)**	6,111
Other comprehensive income/(expense) for the year, net of tax		**21,562**	(26,051)
Total comprehensive loss for the year		**(75,343)**	(69,177)

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs, and to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

The notes on pages 211 to 255 are an integral part of these financial statements.

Statement of financial position
as at 31 March 2022

(Registered Number 02546950)

	Note	2022 £000	2021 (restated) £000
Assets			
Non-current assets			
Property, plant and equipment	6	**1,615,571**	1,540,949
Right-of-use assets	7	**9,440**	9,508
Intangible assets	8	**43,266**	45,783
Investments	9	**100**	100
Retirement benefit surplus	10	**104,247**	74,532
Derivative financial instruments	11	**7,342**	–
Other receivables	12	**–**	184
		1,779,966	1,671,056
Current assets			
Inventories	13	**4,348**	4,080
Derivative financial instruments	11	**20,646**	–
Trade and other receivables	12	**103,821**	91,793
Short-term investments	9	**70,179**	15,132
Cash and cash equivalents	14	**135,604**	84,766
		334,598	195,771
Total assets		**2,114,564**	1,866,827
Equity and liabilities			
Equity			
Share capital	15	**30,506**	30,506
Share premium	15	**1,400**	1,400
Capital contribution reserve	15	**30,150**	30,150
(Accumulated losses)/retained earnings		**(17,753)**	57,590
Total equity		**44,303**	119,646
Liabilities			
Non-current liabilities			
Trade and other payables	16	**247,074**	150,806
Borrowings	17	**1,275,788**	1,095,079
Lease liabilities	18	**6,329**	6,016
Derivative financial instruments	11	**106,818**	45,925
Deferred tax liabilities	19	**231,530**	183,011
Provisions for other liabilities and charges	20	**3,107**	3,396
		1,870,646	1,484,233
Current liabilities			
Trade and other payables	16	**192,817**	255,492
Lease liabilities	18	**3,317**	3,667
Current tax liabilities		**3,481**	3,611
Provisions for other liabilities and charges	20	**–**	178
		199,615	262,948
Total liabilities		**2,070,261**	1,747,181
Total equity and liabilities		**2,114,564**	1,866,827

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs, and to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

The notes on pages 211 to 255 are an integral part of these financial statements. The statutory financial statements on pages 206 to 255 were approved by the Board of directors and were signed and authorised for issue on 12 July 2022 on its behalf by:

Stuart Ledger
Chief Executive Officer

Ian Tyler
Chairman

Statement of changes in equity
for the year ended 31 March 2022

(Registered Number 02546950)

	Note	Share capital £000	Share premium £000	Capital contribution reserve £000	Retained earnings/ accumulated losses) £000	Total equity £000
Balance as at 1 April 2020 as previously reported		26,506	1,400	30,150	128,918	186,974
Impact of restatement		–	–	–	(1,151)	(1,151)
Balance as at 1 April 2020 (restated)		26,506	1,400	30,150	127,767	185,823
Loss for the year as previously reported		–	–	–	(51,278)	(51,278)
Impact of restatement		–	–	–	8,152	8,152
Other comprehensive loss		–	–	–	(26,051)	(26,051)
Total comprehensive loss (restated)		–	–	–	(69,177)	(69,177)
Issuance of share capital	15	4,000	–	–	–	4,000
Dividends	21	–	–	–	(1,000)	(1,000)
Total transactions with owners recognised directly in equity		4,000	–	–	(1,000)	3,000
Balance as at 31 March 2021 (restated)		30,506	1,400	30,150	57,590	119,646
Balance as at 1 April 2021		**30,506**	**1,400**	**30,150**	**57,590**	**119,646**
Loss for the year		–	–	–	(96,905)	(96,905)
Other comprehensive income		–	–	–	21,562	21,562
Total comprehensive loss		**–**	**–**	**–**	**(75,343)**	**(75,343)**
Dividends	21	–	–	–	–	–
Total transactions with owners recognised directly in equity		**–**	**–**	**–**	**–**	**–**
Balance as at 31 March 2022		**30,506**	**1,400**	**30,150**	**(17,753)**	**44,303**

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs, and to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

The notes on pages 211 to 255 are an integral part of these financial statements.

Statement of cash flows
for the year ended 31 March 2022

(Registered Number 02546950)

	Note	2022 £000	2021 (restated) £000
Cash flows from operating activities			
Cash generated from operations	22.1	**101,280**	98,364
Interest paid		**(41,807)**	(42,337)
Tax (paid)/received		**(130)**	377
Net cash inflow from operating activities excluding capital contributions		**59,343**	56,404
Capital contributions		**25,771**	56,407
Net cash inflow from operating activities		**85,114**	112,811
Cash flows from investing activities			
Investment in short-term deposits		**(55,046)**	10,070
Purchases of property, plant and equipment		**(131,288)**	(125,779)
Proceeds from sale of property, plant and equipment		**435**	1,061
Purchases of intangible assets		**(8,608)**	(11,339)
Interest received		**16,886**	12,986
Net cash outflow from investing activities		**(177,621)**	(113,001)
Cash flows from financing activities			
Proceeds from loan from subsidiary undertaking		**146,994**	–
Principal elements of lease payments	18	**(3,649)**	(3,631)
Issuance of share capital	15	**–**	4,000
Dividends paid	21	**–**	(1,000)
Net cash inflow/(outflow) from financing activities		**143,345**	(631)
Net increase/(decrease) in cash and cash equivalents		**50,838**	(821)
Cash and cash equivalents at the beginning of the year		**84,766**	85,587
Cash and cash equivalents at end of year	14	**135,604**	84,766

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs. Further details are included on pages 211 to 212.

The prior year has also reclassified £6,438,000 of interest received on inflation swaps to interest received. Previously, this was netted off against interest paid. Further details are included on page 212.

The notes on pages 211 to 255 are an integral part of these financial statements.

Notes to the financial statements – accounting policies

Basis of preparation

These financial statements have been prepared under the historical cost convention, modified by revaluation of financial assets and financial liabilities held at fair value through profit and loss, and in accordance with the Companies Act 2006 and Financial Reporting Standard 101: 'Reduced disclosure framework' ('FRS 101') as issued by the Financial Reporting Council.

In preparing these financial statements, the company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards as adopted by the UK (UK-adopted international accounting standards), but makes amendments where necessary in order to comply with the Companies Act 2006 and to take advantage of FRS 101 disclosure exemptions.

On 31 December 2020, EU-adopted IFRS was brought into UK law and became UK-adopted international accounting standards, with future changes to IFRS being subject to endorsement by the UK Endorsement Board. In preparing these financial statements in accordance with FRS 101, the company financial statements transitioned to UK-adopted international accounting standards (as described above) on 1 January 2021. There is no impact on recognition, measurement or disclosure in the period reported as a result of this change.

Going concern

The directors consider it appropriate to adopt the going concern basis of accounting in preparing the financial statements as the company has adequate resources to meet its current operational and financial obligations, and the directors have a reasonable expectation that this will continue for the foreseeable future and for a period of at least 12 months from the date of approval of these financial statements. This is based on assessment of the principal risks of the company and the other matters discussed in connection with the viability statement on page 112 as well as consideration of the company's budgeted cash flows, short and long-term forecasts and ability to generate future revenues, related assumptions and available debt facilities.

While the current economic environment, as a result of the impact of Covid-19, supply chain cost pressures and the energy price crisis, is clearly challenging, the company has in place suitable mitigating actions to ensure that even under a severe but plausible downside scenario, the company is not forecasting any covenant breaches over the going concern period. Details of the company's available liquidity, including undrawn committed borrowing facilities, are included in the liquidity risk section of note A4. There have been no events after the reporting period significantly affecting liquidity headroom.

To assess the severe but plausible downside scenario, management have considered a base case scenario that reflects the current market conditions in the economy and have applied a series of severe downside assumptions. These include both increased costs from the financial impacts of operational events, including the impact of a severe cold weather event over the winter period, and an increase in bad debt representing approximately 6% of debt not currently subject to loss allowance provision.

The base case has taken into consideration the impact of Covid-19, supply chain cost pressures and the energy price crisis on the company, and reprofiled capital expenditure from projects delayed during the first year of AMP7 into later years of AMP7.

Due to the nature of the regulated water company's business, the directors consider it appropriate to place reliance on projected financials.

Principal accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out in note A3. These policies have been consistently applied to all the years presented, unless otherwise stated.

Adoption of new and revised standards

No new standards became applicable for the current reporting year.

Prior year restatements as a result of error and change in presentation

1. Treatment of configuration and customisation costs in a cloud computing arrangement

In April 2021, the IFRS Interpretations Committee ('IFRIC') agenda decision on the treatment of configuration and customisation costs in a cloud computing arrangement was ratified by the International Accounting Standards Board. As such, the company has changed its accounting policy from capitalising all costs directly attributable to configuration and customisation in a cloud computing arrangement, to expensing such costs if the company does not have control of the developed software.

This change in accounting policy due to the IFRIC agenda decision has led to a prior year restatement of the income statement, increasing the loss by £1,464,000, and a reduction in total assets in the statement of financial position as at 31 March 2021 of £2,895,000 as shown in the table on the following page.

The change in accounting policy has also impacted the statement of changes in equity, resulting in a reduction in the opening retained earnings as at 1 April 2020 by £1,151,000, shown in the table on the following page, and a restatement of the loss for the year to 31 March 2021, increasing the loss by £1,464,000, as above.

The change in accounting policy has also impacted the statement of cash flows, decreasing net cash inflow from operating activities by £2,148,000 and decreasing net cash outflow from investing activities by the same amount.

2. Debit Value Adjustment on inflation swap derivative financial instruments

The fair value of derivative financial instrument liabilities now includes a Debit Value Adjustment ('DVA'), which is calculated by discounting the potential future cashflows at a rate that reflects the credit risk of the company, which is consistent with IFRS 13: 'Fair value measurement'.

The omission of the DVA in the prior year was an error and has led to a prior year restatement of the income statement, reducing the loss by £9,616,000, and decreasing the total liabilities in the statement of financial position as at 31 March 2021 by the same amount as detailed on the following page. There has not been a restatement made as at 31 March 2020 as the DVA would not have been material.

This omission has also impacted the statement of changes in equity, to reflect the reduced loss of £9,616,000, but has not had any impact on the statement of cash flows.

Notes to the financial statements – accounting policies continued

Prior year restatements as a result of error and change in presentation continued

3. Trade receivables credit balances

The prior year balance sheet has been restated to reclassify £7,592,000 of credit balances on customers' accounts to 'Payments received in advance' in note 16. Previously this was incorrectly netted off against trade receivables in note 12.

As a result, net assets and net liabilities in the statement of financial position have both increased by £7,592,000, as shown on the following page. The opening position as at 31 March 2020 has not been restated.

This restatement has not had any impact on the income statement, statement of changes in equity or statement of cash flows.

4. Interest receivable on inflation swaps

There has been a reclassification in the statement of cash flows of £6,438,000 net interest received on inflation swaps to interest received. Previously, this was incorrectly netted off against interest paid.

As a result, net cash inflow from operating activities has decreased by £6,438,000, and net cash outflow from investing activities has decreased by the same amount.

This reclassification has not had any impact on the income statement, statement of financial position or statement of changes in equity.

Income statement (extract)	31 March 2021 £000	Increase/ (decrease) due to adjustment 1 £000	Increase/ (decrease) due to adjustment 2 £000	31 March 2021 (restated) £000
Administrative expenses	(38,918)	(1,703)	–	(40,621)
Fair value loss on inflation swaps	(44,218)	–	11,766	(32,452)
Tax credit	12,222	239	(2,150)	10,311
Loss for the financial year	**(51,278)**	**(1,464)**	**(9,616)**	**(43,126)**

The £1,703,000 administrative expenses is made up of £2,148,000 cost of ERP system, less £445,000 write back of depreciation on ERP system.

Statement of financial position (extract)	31 March 2021 £000	Increase/ (decrease) due to adjustment 1 £000	Increase/ (decrease) due to adjustment 2 £000	Increase/ (decrease) due to adjustment 3 £000	31 March 2021 (restated) £000
Intangible assets	48,678	(2,895)	–	–	45,783
Trade and other receivables	84,201	–	–	7,592	91,793
Total assets	**1,862,130**	**(2,895)**	**–**	**7,592**	**1,866,827**
Retained earnings	50,589	(2,615)	9,616	–	57,590
Trade and other payables	247,900	–	-	7,592	255,492
Derivative financial instruments	57,691	–	(11,766)	–	45,925
Deferred tax liabilities	181,141	(280)	2,150	–	183,011
Total equity and liabilities	**1,862,130**	**(2,895)**	**–**	**7,592**	**1,866,827**

Statement of financial position (extract)	31 March 2020 £000	Increase/ (decrease) due to adjustment 1 £000	31 March 2020 (restated) £000
Intangible assets	45,768	(1,192)	44,576
Total assets	**1,840,167**	**(1,192)**	**1,838,975**
Retained earnings	128,918	(1,151)	127,767
Deferred tax liabilities	**198,644**	**(41)**	**198,603**
Total equity and liabilities	**1,840,167**	**(1,192)**	**1,838,975**

New standards, amendments and interpretations not yet adopted

There are no new standards and interpretations, which are not yet effective and have not been early adopted by the company, that will have a material effect on future years.

Disclosure exemptions

As permitted by FRS 101, the company has taken advantage of the following disclosure exemptions available under that standard in the preparation of these financial statements:

- Paragraph 38 of IAS 1: 'Presentation of financial statements' comparative information requirements in respect of:
  - Paragraph 79(a)(iv) of IAS 1: 'Presentation of financial statements';
  - Paragraph 73(e) of IAS 16: 'Property, plant and equipment'; and
  - Paragraph 118(e) of IAS 38: 'Intangible assets' (reconciliations between the carrying amount at the beginning and end of the period)
- The following paragraphs of IAS 1: 'Presentation of financial statements':
  - 16 (statement of compliance with all IFRS); and
  - 38B–D (additional comparative information)
- Paragraphs 40A–D of IAS 1: 'Presentation of financial statements' in respect of prior year restatements
- Paragraph 17 of IAS 24: 'Related party disclosures' (key management compensation)
- The requirements in IAS 24: 'Related party disclosures' to disclose related party transactions entered into between two or more members of a group.

Critical accounting estimates

The preparation of financial statements in conformity with FRS 101 requires the use of certain critical accounting estimates. Estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

Measured income accrual

The company records an accrual for measured consumption of water that has not yet been billed (refer to note 12). The accrual is estimated using a defined methodology based upon weighted average water consumption by tariff, which is calculated based upon historical information. Revenue for the year ended 31 March 2021 included a measured income accrual of £36,719,000. The value of billing recognised in the year ended 31 March 2022 for consumption in the prior year was £39,431,000.

This resulted in a increase of £2,712,000 in the current year's revenue due to the under-estimation of the prior year's revenue. This represented 0.85% of 2021/22 revenue and is within acceptable tolerance for accounting estimates.

Non-household wholesale revenue

The company has contracts with third parties operating in the non-household retail market for the supply of clean water (wholesale supply). The underlying performance obligation is the development and maintenance of the network, and ensuring its continued availability to such third-party retailers on behalf of non-household consumers. Revenue is recognised at the point at which the company has a right to receive the revenue. For non-household retailers, the amount which the company has a right to receive, is determined by non-household consumption volume data.

Loss allowance of trade receivables and contract assets

The company makes an estimate of the recoverable value of trade receivables and contract assets and records a loss allowance based on experience (refer to note A3). This provision is based on, amongst other things, a consideration of actual collection history. At each reporting date, the company takes into consideration any significant economic changes that may impact its credit loss model and future credit losses and resultantly has accounted for an additional bad debt charge given the increase in the cost of living currently impacting our customers. This was calculated by applying an additional loss allowance provision to each segment of our customer base, based on the likely impact to that segment. The actual level of receivables collected may differ from the estimated levels of recovery, which could impact operating results positively or negatively. Each 1% increase in the loss allowance for trade receivables and contract assets across each aged debt bracket would result in an additional bad debt charge of £373,000 (2021: £343,000) and a corresponding reduction in net assets. Each 1% decrease in the loss allowance for trade receivables and contract assets across each aged debt bracket would result in a reduction in the bad debt charge of £373,000 (2021: £343,000) and corresponding increase in net assets.

Useful economic lives of property, plant and equipment

The annual depreciation charge for property, plant and equipment is sensitive to changes in the estimated useful economic lives and residual values of the assets. The useful economic lives and residual values are re-assessed annually. They are amended when necessary to reflect current estimates, based on management's judgement and experience, which include the knowledge and research of the company's dedicated asset management teams. Refer to note 6 for the carrying amount of property, plant and equipment and note A3 for the useful economic lives for each class of assets.

Based on the current useful lives, the carrying amount of property, plant and equipment at 31 March 2022 is £1,615,571,000 (2021: £1,540,949,000). If the useful lives of the assets were 10% shorter, the carrying amount would instead be £1,164,882,000 (2021: £1,104,713,000) and if they were 10% longer, the carrying amount would be £1,747,322,000 (2021: £1,657,069,000).

Based on the current useful lives, the carrying amount of intangible assets, excluding goodwill, at 31 March 2022 is £28,305,000 (2021 (restated): £30,822,000). If the useful lives of the assets were 10% shorter, the carrying amount would instead be £25,150,000 (2021 (restated): £29,666,000) and if they were 10% longer, the carrying amount would be £31,460,000 (2021 (restated): £37,768,000).

Notes to the financial statements – accounting policies continued

Critical accounting estimates continued

The above estimates have been calculated using the average useful life for each class of asset and assumes that the assets in each category are midway through their useful life.

Defined benefit pension plan

The company has an obligation to pay pension benefits to certain employees. The cost of these benefits and the present value of the obligation depend on a number of factors, including life expectancy, inflation, salary increases, asset valuations and the discount rate on corporate bonds. Management estimates these factors in determining the net pension obligation in the statement of financial position. The assumptions (refer to note A5) reflect historical experience and current trends and may differ from actual results due to changing market and economic conditions and longer or shorter lives of participants. There are no restrictions to the realisability of the surplus relating to the defined benefit section of the pension plan; therefore, no adjustment has been made to the retirement benefit surplus recognised in accordance with International Financial Reporting Interpretations Committee 14: 'The limit on a defined benefit asset, minimum funding requirements and their interaction'. A sensitivity analysis has been performed based on changing different assumptions – see note A5 for the impact of changes in assumptions used.

Critical accounting judgements in applying the entity's accounting policies

The preparation of financial statements also requires management to exercise its judgement in the process of applying the company's accounting policies. The areas involving a higher degree of judgement or complexity are disclosed below.

Revenue recognition

IFRS 15 requires revenue to be recognised in line with the satisfaction of performance obligations identified within contracts between an entity and its customers, at an amount that reflects the transaction price allocated to each performance obligation. Particular challenges exist within the water industry as formal written contracts do not exist for most transactions with customers. Contracts are instead implied through statute and regulation. Judgement is, therefore, required in identifying the services contained within the contract and the customer with whom the contract is entered into, which in turn impacts on how the performance obligations are considered and, therefore, revenue recognised.

Refer to note 1 for the amount of revenue recognised in the income statement.

Grants and contributions

Grants and contributions (consisting of contributions for diversions and requisitioned mains/extensions, and infrastructure charges) are received in respect of property, plant and equipment. Judgement is required in identifying what the performance obligation is for each type of contribution, which in turn impacts on how revenue is recognised.

Contributions received in respect of diversions, requisitioned mains/extensions and infrastructure charges are recognised over a period of time. Contributions received in respect of connections charges are recognised immediately in the income statement. Refer to note A3 for further detail on our accounting policies in relation to these. Refer to note 1 for the amount of revenue recognised in the income statement.

Included within grants and contributions are contributions received relating to the HS2 rail programme, which crosses our supply area. These are shown within capital contributions in the statement of cash flows.

Cost capitalisation

The company capitalises expenditure on its infrastructure assets to property, plant and equipment where such expenditure enhances or increases the capacity of the network, or relates to material replacements of network components. Any expenditure classed as maintenance is expensed in the year it is incurred. Distinguishing between enhancement and maintenance expenditure is a subjective area, particularly when projects have both elements within them. Refer to note 6 for the carrying amount of property, plant and equipment.

Climate change

The natural environment within which the company operates is constantly evolving due to the effects of climate change. This will influence how water is delivered by the company in the future.

The company is continually developing its assessment of the impact that climate change has on the assets and liabilities recognised and presented in its financial statements, such as the valuation of the property, plant and equipment, which could be impacted by either flooding or drought, or management's decision to replace assets as part of the company's net zero strategy. There has been no revaluation of assets during 2021/22 as a result of climate change.

The company established a Green Finance Framework during the year and issued its first green bond in October 2021 to finance projects which will adapt to and mitigate the effects of climate change.

Notes to the financial statements

1. Revenue

1.1 Disaggregation of revenue from contracts with customers

	2022 £000	2021 £000
Timing of revenue recognition – at a point in time		
Unmeasured supplies	**100,115**	96,981
Measured supplies	**155,232**	144,124
Non-household wholesale revenue	**51,111**	34,732
Connection charges	**7,989**	7,904
	314,447	283,741
Timing of revenue recognition – over time		
Requisitioned mains/extensions	**573**	576
Diversions	**3,382**	1,201
Infrastructure charges	**1,145**	1,111
Other	**200**	153
	5,300	3,041
	319,747	286,782

All revenue is derived in the United Kingdom.

1.2 Assets and liabilities related to contracts with customers

The company has recognised the following assets and liabilities related to contracts with customers:

	2022 £000	2021 £000
Net trade receivables	**33,840**	24,505
Contract assets		
Unbilled accrual for metered customers – household customers	**40,847**	36,742
Unbilled accrual for metered customers – non-household customers	**3,506**	2,710
Contract liabilities		
Payments received in advance – household water supplies	**46,746**	41,217
Payments received in advance – non-household water supplies	**–**	2,948
Deferred income – water supplies	**207**	138
Deferred income – other	**622**	1,004
Deferred grants and contributions	**252,772**	154,175
Payments received in advance – grants and contributions	**27,023**	108,100

'Payments received in advance – grants and contributions' in the table above relate to contributions received from developers where the asset is still work in progress and not yet being depreciated. Once the asset is complete, the contribution is moved from 'payments received in advance – grants and contributions' to 'deferred grants and contributions' and amortised, to ensure the accounting treatment is consistent.

Notes to the financial statements continued

1. Revenue continued

1.2 Assets and liabilities related to contracts with customers continued

Significant changes in contract assets and liabilities

Up to 31 March 2022, the company had been reimbursed £154,187,000 (2021: £128,376,000) for its costs incurred in relation to the HS2 rail project, which will cross the Affinity Water supply area. During the year, in line with the company's accounting policy for grants and contributions received in respect of property, plant and equipment, which include contributions received for diversions, £98,478,000 (2021: £14,621,000) relating to costs for assets that have been commissioned was reclassified from payments in advance – grants and contributions to deferred grants and contributions. At 31 March 2022, £14,268,000 (2021: £91,916,000) of payments received were included in payments in advance – grants and contributions.

Recognition of trade receivables, contract assets and contract liabilities

For metered customers, a receivable is recognised when the customer is billed for the usage. At this point, the consideration is unconditional because only the passage of time is required before the payment is due. Where the company has provided the service before payment is due, an accrual for the consumption of water that has not yet been billed is recognised in the income statement and the company discloses this as a contract asset in the statement of financial position (see table on the previous page). Where the company has not provided the service before payment is due, deferred income is recognised and the company discloses this as a contract liability in the statement of financial position (see table on the previous page).

For unmetered customers, the customer pays a fixed amount determined by the transaction prices set out in the company's charging scheme and tariff documents. If the payments received exceed the amount the company has the right to receive, the company recognises a payment received in advance and discloses this as a contract liability in the statement of financial position (see table on the previous page).

Where non-household retailers are billed monthly in advance for wholesale charges, as determined by billing/volume reports created by the market operator, the company recognises deferred income in relation to these accounts and presents this as a contract liability within trade and other payables. Where the company has not provided the service before payment is due, deferred income is recognised and the company discloses this as a contract liability in the statement of financial position (see table on the previous page).

Developers are billed for connection charges and contributions towards diversions and requisitioned mains/extensions in advance of work being performed by the company. The company recognises these payments as being received in advance and discloses them as contract liabilities in the statement of financial position (see table on the previous page).

Developers are billed for infrastructure charges once the connection has been completed; a trade receivable is immediately recognised at this point as the consideration is unconditional. These receivables are included in net trade receivables in the table on the previous page.

The company does not incur any costs to obtain or fulfil contracts that would be recognised as an asset under IFRS 15.

Revenue recognised in relation to contract liabilities

The following table sets out how much of the revenue recognised in the current reporting year relates to carried forward contract liabilities and how much relates to performance obligations that were satisfied in a prior year:

	2022 £000	2021 £000
Revenue recognised that was included in the contract liability balance at the beginning of the year		
Payments received in advance – household water supplies	**41,217**	39,191
Payments received in advance – non-household water supplies	**2,948**	254
Deferred income – water supplies	**138**	72
Deferred income – other	**775**	434
Deferred grants and contributions	**5,300**	3,041
Payments received in advance – grants and contributions	**7,585**	11,320
Revenue recognised from performance obligations satisfied in previous years		
Unbilled accrual for metered customers – household customers	**–**	(264)

Revenue expected to be derived from unsatisfied performance obligations

IFRS 15 requires the disclosure of the aggregate amount of revenue, which is expected to be derived from performance obligations, which are unsatisfied as at the end of the reporting year, i.e. the aggregate amount of future revenues from existing ongoing contracts.

The company has applied the practical expedient, set out in paragraph 121(a) of IFRS 15, not to disclose this amount in relation to water charges as the performance obligation is part of a contract that has an original expected duration of one year or less.

The unbilled accrual for measured income is a contract asset under IFRS 15. Historical information has proved to be an accurate indicator of current consumption and, therefore, the company deems it reasonable to conclude that the measured income accrual is materially correct.

At 31 March 2022, £154,294,000 (2021: £154,175,000) of grants and contributions is expected to be derived from performance obligations which were unsatisfied at the end of the reporting year.

2. Operating profit

2.1 Operating costs

The following items have been charged/(credited) to either cost of sales or administrative expenses in the income statement:

	2022 £000	2021 (restated) £000
Staff costs (note 3.1)	**55,367**	55,189
Profit on disposal of property, plant and equipment	**(244)**	(1,061)
Loss on disposal of infrastructure assets	**728**	1,408
Purchase of bulk water and water supplied under statutory entitlement	**8,440**	10,255
Water abstraction charges	**4,201**	3,984
Business rates	**15,551**	15,448
Chargeable services direct expenditure	**72**	283
Depreciation of infrastructure assets (note 6)	**11,964**	14,868
Depreciation of other property, plant and equipment (note 6)	**48,487**	49,928
Depreciation of right-of-use assets (note 7)	**3,681**	3,684
Amortisation of intangible assets (note 8)	**11,125**	10,132
Impairment of trade receivables and contract assets (note 12)	**7,444**	8,318
Research and development	**133**	126
Short-term lease rentals	**37**	115
Low-value lease rentals	**129**	91
Auditor's remuneration (note 2.3)	**457**	421
Cost of inventories used	**1,334**	714

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs. Further details are included on pages 211 to 212.

Notes to the financial statements continued

2. Operating profit continued

2.2 Other operating income

	2022 £000	2021 £000
Timing of revenue recognition – at a point in time		
Commission and rentals	**18,972**	17,657

The majority of other income relates to commission earned by the company from billing and collecting charges in respect of sewerage and infrastructure within its area on behalf of Thames Water Utilities Limited and Anglian Water Services Limited (refer to note 24).

2.3 Auditors' remuneration

During the year, the company obtained the following services from its Auditor and its associates:

	2022 £000	2021 £000
Fees payable to the company's Auditor and its associates for the audit of the financial statements	**243**	205
Fees payable to the company's Auditor and its associates for other services:		
Audit of the company's associates	**90**	99
Audit-related assurance services		
– regulatory reporting	**61**	56
– Thames Water and Anglian Water annual returns	**10**	10
– audit related assurance service – other	**47**	38
Other assurance services including services related to bond issue	**–**	6
Other non-audit services	**6**	7
Total Auditor's remuneration	**457**	421

3. Employees

3.1 Employee benefit expense (including Executive directors)

	2022 £000	2021 £000
Wages and salaries	**62,408**	59,742
Social security costs	**6,667**	6,168
Other pension costs	**8,399**	8,223
Staff costs	**77,474**	74,133
Staff costs capitalised	**(22,107)**	(18,944)
Staff costs recognised in the income statement	**55,367**	55,189

3.2 Average number of people employed

The average monthly number of full-time equivalent persons (including Executive directors) employed by the company during the year was:

By activity	2022 Number	2021 Number
Operations	**854**	760
Customer service	**257**	240
Administration	**262**	262
	1,373	1,262

Notes to the financial statements continued

3. Employees continued

3.3 Directors' remuneration

Directors' emoluments were as follows:

	2022 £000	2021 £000
Aggregate emoluments	**1,839**	1,390

Aggregate amounts receivable under long-term incentive schemes were £482,000 (2021: £283,000), not included within aggregate emoluments above. For Pauline Walsh, £230,000 relates to the 2019/20 LTIP scheme, which vested in the year ended 31 March 2022, with the remaining amount of £132,000 relating to accrued elements of the 2020/21 and 2021/22 LTIP schemes earned on a pro-rata basis for the period served in office. Both amounts will be fully paid in July 2022. For Stuart Ledger, £120,000 relates to the 2019/20 LTIP scheme, which vested in the year ended 31 March 2022 and will be paid in three equal instalments in the years ending 31 March 2023, 31 March 2024 and 31 March 2025. The prior year total of £283,000 relates to the 2018/19 LTIP scheme, which vested in the year ended 31 March 2021 and will be paid in three equal instalments in the years ending 31 March 2022, 31 March 2023 and 31 March 2024.

Neither the company nor its immediate parent entities has any listed shares and so the directors have not been offered any share incentives.

The Non-Executive directors who were appointed by Allianz Capital Partners on behalf of the Allianz group, DIF and InfraRed Capital Partners Limited on behalf of HICL Infrastructure plc did not receive any emoluments from the company, or any company within the Affinity Water group.

Highest paid director

The highest paid director's emoluments were as follows:

	2022 £000	2021 £000
Aggregate emoluments	**933**	576

Aggregate amounts receivable under long-term incentive schemes were £362,000 (2021: £206,000), not included within aggregate emoluments above. Of this, £230,000 relates to the 2019/20 LTIP scheme, which vested in the year ended 31 March 2022, with the remaining amount of £132,000 relating to accrued elements of the 2020/21 and 2021/22 LTIP schemes earned on a pro-rata basis for the period served in office. Both amounts will be fully paid in July 2022. The prior year total of £206,000 relates to the 2018/19 LTIP scheme, which vested in the year ended 31 March 2021 and will be paid in three equal instalments in the years ending 31 March 2022, 31 March 2023 and 31 March 2024.

The company made no contributions to a pension plan in respect of the highest paid director's qualifying services during the year (2021: £55,000). The highest paid director did not hold any share options during the year.

Further information regarding directors' remuneration during the year can be found within the Remuneration Report on pages 164 to 183.

4. Finance income and costs

	2022 £000	2021 (restated) £000
Finance income:		
Bank interest income	**192**	213
Net interest receivable on RPI linked inflation swaps	**7,434**	6,792
Net interest receivable on CPI linked inflation swaps	**6,929**	6,297
Net income from post-employment benefits	**1,488**	2,468
	16,043	15,770
Finance costs:		
Interest payable on borrowings held at amortised cost from parent company	**(160)**	(160)
Interest payable on borrowings held at amortised cost from subsidiary undertakings	**(37,411)**	(37,510)
Accretion payable in respect of interest on loans from subsidiary undertakings	**(35,047)**	(5,254)
Accretion payable on financial instrument	**(29,574)**	(4,564)
Interest payable on lease liabilities	**(313)**	(315)
Other	**(368)**	(818)
	(102,873)	(48,621)
Fair value gain/(loss) on financial instruments:		
Fair value loss on inflation swaps	**(31,295)**	(32,452)
	(31,295)	(32,452)
Net finance costs	**(118,125)**	(65,303)

The prior year has been restated to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

Notes to the financial statements continued

5. Income tax expense/(credit)

5.1 Income tax expense/(credit) included in the income statement

	2022 £000	2021 (restated) £000
Current tax:		
– UK corporation tax on losses for the year	–	–
– Adjustment in respect of prior years	–	(830)
Total current tax	–	(830)
Deferred tax:		
– Origination and reversal of temporary differences	(10,949)	(9,901)
– Impact of change in tax rate	54,729	–
– Adjustment in respect of prior years	(2,449)	420
Total deferred tax	41,331	(9,481)
Income tax expense/(credit)	41,331	(10,311)

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs, and to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

Tax expense assessed for the year is higher (2021: tax credit is higher) than the standard rate of corporation tax in the UK for the year ended 31 March 2022 of 19% (2021: 19%). The differences are explained below:

	2022 £000	2021 (restated) £000
Loss before tax	(55,574)	(53,437)
Tax calculated at the standard rate of tax in the UK of 19% (2021: 19%)	(10,559)	(10,153)
Tax effects of:		
– Adjustments in respect of prior years	(2,449)	(410)
– Expenses not deductible for tax purposes	(390)	252
– Impact of change in tax rate on deferred tax	54,729	–
Income tax expense/(credit)	41,331	(10,311)

5.2 Income tax expense/(credit) included in the statement of comprehensive income

	2022 £000	2021 £000
Deferred tax:		
– Impact of change in tax rate on deferred tax	1,725	–
– Origination and reversal of temporary differences on retirement benefit surplus	5,462	(6,111)
	7,187	(6,111)

5.3 Factors that may affect future tax charges

In the Spring Budget 2021, the UK Government announced that from 1 April 2023 the corporation tax rate would increase to 25% (rather than remaining at 19%, as previously enacted). This new law was substantively enacted on 24 May 2021. Deferred taxes at the balance sheet date have been measured using these enacted tax rates and reflected in these financial statements.

5.4 Reconciliation of current and deferred tax charge

	2022 £000	2022 %	2021 (restated) £000	2021 %
Loss before tax	(55,574)		(53,437)	
Tax calculated at the standard rate of tax in the UK of 19% (2021: 19%)	(10,559)	19%	(10,153)	19%
Tax effect of:				
Depreciation in excess of capital allowances	10,752	(19%)	10,578	(20%)
Pension movements	(183)	0%	(394)	1%
Increase in provisions	(128)	0%	(29)	0%
Expenses not deductible for tax purposes	118	0%	(2)	0%
Adjustment to tax charge in respect of prior years	–	0%	(830)	1%
Reported current tax charge and effective rate	–	0%	(830)	1%
Depreciation in excess of capital allowances	(11,260)	20%	(10,324)	19%
Increase in provisions	128	0%	29	0%
Pension movements	183	0%	394	(1%)
Impact of change in tax rate on deferred tax	54,729	(99%)	–	0%
Adjustments to tax charge in respect of prior years	(2,449)	4%	420	(1%)
Reported deferred tax charge and effective rate	41,331	(74%)	(9,481)	18%
Total tax charge and effective rate	41,331	(74%)	(10,311)	19%

Impact of change in tax rate

In the 2021 Spring Budget the UK Government announced that from 1 April 2023 the Corporation Tax rate will increase to 25%. The deferred tax liability at 31 March 2022 has been recalculated at 25%.

Depreciation in excess of capital allowances

The tax relief on our infrastructure assets is different from the depreciation of these assets in the accounts (although over the total life of the assets the two amounts will be equal). In 2021/22, the amount written off for tax purposes was lower than the depreciation in the accounts, resulting in a higher tax charge for the year.

Pension movements

Tax relief is given for the amount actually paid into the company's pension plan in the year, not the amount charged in the accounts. In 2021/22, the amount paid into the pension plan was higher than the amount charged in the accounts, resulting in a lower tax charge for the year.

Provisions movements

Some provisions charged in the accounts are not deductible until the amounts provided are actually paid. Taxable profits in 2021/22 have been reduced by payments made in respect of provisions charged in previous years.

Expenses not deductible for tax purposes

These will not reverse in future years, therefore, the increase in the tax charge is permanent. Permanent disallowable expenses include fines, business entertaining and certain legal fees.

Adjustment to tax charge in respect of prior years

The tax provision in the accounts is a best estimate at the time. The estimate is corrected when the tax returns are finalised and submitted to HMRC 12 months after the year-end. The correction made to the tax return for the year ended 31 March 2021 resulted in a lower tax charge, mainly as a result of claiming capital allowances.

Notes to the financial statements continued

6. Property, plant and equipment

	Land, buildings and operational structures £000	Potable water distribution mains £000	Raw water pipes £000	Fixed plant £000	Vehicles and mobile plant £000	Assets in course of construction £000	Total £000
Cost or deemed cost							
At 1 April 2021	308,479	904,383	22,765	885,377	84,157	160,058	**2,365,219**
Additions	–	–	–	–	–	136,043	**136,043**
Transfers	1,903	114,816	–	12,014	7,899	(136,632)	**–**
Disposals	(131)	(857)	(4)	–	(427)	–	**(1,419)**
At 31 March 2022	310,251	1,018,342	22,761	897,391	91,629	159,469	**2,499,843**
Accumulated depreciation							
At 1 April 2021	(101,296)	(80,209)	(2,318)	(602,582)	(37,865)	–	**(824,270)**
Charge for the year	(4,596)	(11,643)	(321)	(39,090)	(4,801)	–	**(60,451)**
Disposals	28	83	–	–	338	–	**449**
At 31 March 2022	(105,864)	(91,769)	(2,639)	(641,672)	(42,328)	–	**(884,272)**
Net book amount							
At 1 April 2021	207,183	824,174	20,447	282,795	46,292	160,058	**1,540,949**
Movement in year	(2,796)	102,399	(325)	(27,076)	3,009	(589)	**74,622**
At 31 March 2022	204,387	926,573	20,122	255,719	49,301	159,469	**1,615,571**

All land and buildings are held as freehold.

7. Right-of-use assets

	Buildings £000	Vehicles £000	Other £000	Total £000
Cost				
At 1 April 2021	9,079	7,521	402	**17,002**
Additions	–	3,660	–	**3,660**
Disposals	–	(1,097)	(402)	**(1,499)**
At 31 March 2022	9,079	10,084	–	**19,163**
Accumulated depreciation				
At 1 April 2021	(2,794)	(4,298)	(402)	**(7,494)**
Charge for the year	(1,397)	(2,284)	–	**(3,681)**
Disposals	–	1,050	402	**1,452**
At 31 March 2022	(4,191)	(5,532)	–	**(9,723)**
Net book amount				
At 1 April 2021	6,285	3,223	–	**9,508**
Movement in year	(1,397)	1,329	–	**(68)**
At 31 March 2022	4,888	4,552	–	**9,440**

8. Intangible assets

	Goodwill £000	Software £000	Total £000
Cost			
At 1 April 2021 (restated)	14,961	86,952	**101,913**
Additions	–	8,608	**8,608**
At 31 March 2022	14,961	95,560	**110,521**
Accumulated amortisation			
At 1 April 2021 (restated)	–	(56,130)	**(56,130)**
Charge for the year	–	(11,125)	**(11,125)**
At 31 March 2022	–	(67,255)	**(67,255)**
Net book amount			
At 1 April 2021 (restated)	14,961	30,822	**45,783**
Movement in year	–	(2,517)	**(2,517)**
At 31 March 2022	14,961	28,305	**43,266**

The opening balances have been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs. Further details are included on pages 211 to 212.

Goodwill includes £8,283,000 relating to the unification of the Affinity Water group's regulated businesses on 27 July 2012. The remaining balance of £6,678,000 relates to goodwill arising from the acquisition of the trade and assets of North Surrey Water Limited on 1 October 2000.

Affinity Water Limited is the only cash generating unit ('CGU') due to the fact it constitutes the smallest identifiable group of assets that generate cash inflows for the entity, by means of supplying drinking water to customers. The recoverable amount has been determined using the RCV of Affinity Water Limited at 31 March 2022. Management's assessment has determined that the headroom is such that no reasonable change in any key assumptions is expected to result in impairment of the goodwill recognised.

Included in the computer software asset category above is £12,532,000 of capitalised intangible assets under construction, which is not amortised. £7,366,000 of intangible projects under construction were completed in the year, and amortisation was charged as at the point in time that the software became fit for purpose and ready to use.

There were no individually material computer software development costs in the years ended 31 March 2022 or 31 March 2021.

9. Investments

	2022 £000	2021 £000
Non-current assets		
Investments in subsidiaries (refer to note A6)	**100**	100
Current assets		
Short-term deposits	**70,179**	15,132

The directors confirm that the carrying value of the investments is supported by their underlying net assets.

Notes to the financial statements continued

10. Retirement benefit surplus

Defined benefit section

The net pension expense before taxation recognised in the income statement in respect of the defined benefit plan is:

	2022 £000	2021 £000
Total current service cost of the Affinity Water Pension Plan	**(4,061)**	(3,310)
Contributions from participating employer	**–**	51
Past service cost	**–**	(31)
Pension expense charged to operating profit	**(4,061)**	(3,290)
Net pension interest income credited to finance income (note 4)	**1,488**	2,468
Net pension expense charged before taxation	**(2,573)**	(822)

The opening and closing retirement benefit surpluses included in the statement of financial position are summarised as follows:

	2022 £000	2021 £000
At 1 April	**74,532**	104,619
Principal employer contributions	**3,539**	2,897
Net current service cost (per above)	**(4,061)**	(3,259)
Past service cost	**–**	(31)
Net interest income	**1,488**	2,468
Net re-measurement gain/(loss)	**28,749**	(32,162)
At 31 March	**104,247**	74,532

Re-measurement gains and losses are recognised directly in the statement of comprehensive income and are summarised as follows:

	2022 £000	2021 £000
Re-measurement gains on plan assets	**8,249**	40,649
Re-measurement gains/(losses) on plan liabilities	**20,500**	(72,811)
	28,749	(32,162)

Further analysis and underlying valuation assumptions of the defined benefit plan are provided in note A5.

11. Derivative financial instruments

	2022 £000	2021 (restated) £000
Non-current assets:		
Fair value of energy swaps	**7,342**	–
Current assets:		
Fair value of energy swaps	**20,646**	–
	27,988	–
Non-current liabilities:		
Fair value of RPI linked inflation swaps	**24,224**	6,629
Accretion on RPI linked inflation swaps	**23,702**	7,721
Fair value of CPI linked inflation swaps	**43,729**	30,028
Accretion on CPI linked inflation swaps	**15,163**	1,547
	106,818	45,925

The prior year has been restated to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

A series of power hedging swaps were entered into between May 2021 and February 2022 in order to hedge against wholesale energy prices.

The fair value of energy swaps have been derived from 'Level 2' fair value measurements: directly observable market inputs other than Level 1 inputs. The fair value of energy swaps is calculated by discounting expected future cashflows based on market expectations of energy prices in the future.

An RPI linked inflation swap with a nominal value of £135.0m, which is linked to the maturity of the Class A fixed rate £250.0m bond (maturity July 2026), was entered into in August 2018. A further RPI linked inflation swap with a nominal value of £75.0m, which is also linked to the maturity of the Class A fixed rate £250.0m bond (maturity July 2026), was entered into in October 2020, with an effective date of 1 August 2020.

A CPI linked inflation swap with a nominal value of £25.0m, which is linked to the maturity of the Class A fixed rate £250.0m bond (maturity March 2036), was entered into in March 2020. Further CPI linked inflation swaps with a total nominal value of £225.0m, which are also linked to the maturity of the Class A fixed rate £250.0m bond (maturity March 2036), were entered into between April 2020 and June 2020.

The fair value of RPI and CPI linked inflation swaps have been derived from 'Level 2' fair value measurements: directly observable market inputs other than Level 1 inputs. The fair value of RPI and CPI linked inflation swaps is calculated by discounting expected future cashflows based on market expectations of RPI and CPI. The discount rate used reflects the credit risk of the company, which is consistent with IFRS 13: 'Fair value measurement'.

Notes to the financial statements continued

12. Trade and other receivables

	2022 £000	2021 (restated) £000
Non-current:		
Other receivables	–	184
Current:		
Trade receivables	66,517	66,124
Less: loss allowance for trade receivables	(33,037)	(34,027)
	33,480	32,097
Amounts owed by group undertakings	25	–
Interest receivable from external parties	7,786	7,630
Other receivables	7,964	4,868
Unbilled accrual for metered customers	44,353	39,452
Prepayments and accrued income	10,213	7,746
	103,821	91,793

Trade receivables that were fully provided for were sold in both the current year and prior year, resulting in a reduction to trade receivables of £6,813,000 (2021: £2,213,000) and a corresponding reduction in the loss allowance for trade receivables.

The prior year has been restated to reclassify £7,592,000 of credit balances on customers' accounts to other payables in note 16. Previously, this was netted off against trade receivables. Further details are included on pages 211 to 212.

The carrying amounts of trade and other receivables approximate to their fair value.

12.1 Loss allowance for trade receivables and contract assets

Trade receivables and contract assets do not carry interest and are stated net of a loss allowance, as follows:

	Trade receivables		Unbilled accrual for metered customers		Total	
	2022 £000	2021 £000	2022 £000	2021 £000	2022 £000	2021 £000
At 1 April	34,027	34,585	51	269	34,078	34,854
Provision for receivables impairment charged to income statement	7,394	8,536	50	(218)	7,444	8,318
Sale of trade receivables that were fully provided for	(6,813)	(2,213)	–	–	(6,813)	(2,213)
Receivables written off during the year as uncollectable	(1,571)	(6,881)	–	–	(1,571)	(6,881)
At 31 March	33,037	34,027	101	51	33,138	34,078

See note A4 for details of the nature and the calculation of the loss allowance.

An additional charge to the income statement of £1,413,000 arising as a result of external economic factors including the increase in cost of living currently impacting our customers has been made during the year. This is included within the £7,444,000 total provision for receivables impairment credited to the income statement.

In the prior year, £2,346,000 of the £8,318,000 total provision for receivables impairment charged to the income statement was an additional charge arising as a result of Covid-19.

12.2 Ageing analysis of trade receivables

The aged analysis of receivables at the reporting date is as follows:

	2022 £000	2021 (restated) £000
Aged less than one year	24,157	22,406
Aged between one year and two years	21,884	23,471
Aged greater than two years	20,476	20,247
	66,517	66,124

The prior year has been restated to reclassify £7,592,000 of credit balances on customers' accounts to other payables in note 16. Previously, this was netted off against trade receivables aged greater than two years. Further details are included on pages 211 to 212.

13. Inventories

	2022 £000	2021 £000
Raw materials and consumables	4,348	4,080

Inventories are stated after provisions for impairment of £364,000 (2021: £364,000).

14. Cash and cash equivalents

	2022 £000	2021 £000
Cash at bank and in hand	34,479	43,650
Term deposits	101,125	41,116
	135,604	84,766

The carrying amounts of cash and cash equivalents approximate to their fair value.

15. Share capital, share premium and capital contribution reserve

Allotted and fully paid up	Number of shares (thousands)	Ordinary shares of £0.10 each £000	Share premium £000	Capital contribution reserve £000	Total £000
At 31 March 2021 and 31 March 2022	305,058	30,506	1,400	30,150	62,056

All shares rank pari passu in all respects.

Notes to the financial statements continued

16. Trade and other payables

	2022 £000	2021 (restated) £000
Non-current		
Amounts falling due after more than one year		
Deferred grants and contributions	**25,509**	10,286
Amounts falling due after more than five years		
Deferred grants and contributions	**221,565**	140,520
	247,074	150,806
Current		
Amounts falling due within one year		
Trade payables	**22,166**	23,678
Amounts due to group undertakings	**615**	537
Interest payable to subsidiary companies	**14,052**	13,858
Commitment fees	**63**	55
Social security and other taxes	**1,796**	1,654
Other payables	**5,391**	8,615
Capital accruals	**21,587**	16,833
Deferred grants and contributions	**5,698**	3,369
Payments received in advance	**81,980**	152,911
Deferred income	**843**	1,144
Other accruals	**38,626**	32,838
	192,817	255,492
	439,891	406,298

The prior year has been restated to reclassify £7,592,000 of credit balances on customers' accounts to other payables. Previously, this was netted off against trade receivables in note 12. Further details are included on pages 211 to 212.

The carrying amounts of trade and other payables approximate to their fair value.

Interest payable to subsidiary companies relates to accrued interest on bonds.

17. Borrowings

	2022 £000	2021 £000
Borrowings measured at amortised cost:		
Loan from Affinity Water Finance (2004) PLC financed by bond issue	**252,498**	252,999
Loan from Affinity Water Finance PLC financed by bond issue	**1,019,706**	838,496
Loan from intermediate parent company	**3,550**	3,550
3.5% irredeemable consolidated debenture stock	**–**	–
4% irredeemable consolidated debenture stock	**8**	8
4% irredeemable debenture stock	**1**	1
4.25% irredeemable debenture stock	**–**	–
5% irredeemable debenture stock	**24**	24
5.25% irredeemable debenture stock	**1**	1
	1,275,788	1,095,079

On 13 July 2004, the company's subsidiary Affinity Water Finance (2004) PLC issued a £200,000,000 bond at an interest rate of 5.875% and repayable in July 2026. On 16 July 2014, Affinity Water Finance (2004) PLC completed a tap issue of £50,000,000 on the same terms as the existing £200,000,000 bond.

The net proceeds of the bond and tap issue were lent to the company on the same terms.

On 4 February 2013, the company's former subsidiary Affinity Water Programme Finance Limited issued £80,000,000 Class A Guaranteed Notes maturing in September 2022 with a coupon of 3.625%, £250,000,000 Class A Guaranteed Notes maturing in March 2036 with a coupon of 4.500%, £190,000,000 Class A Guaranteed RPI linked Notes maturing in June 2045 with a coupon of 1.548% and £95,000,000 Class B Guaranteed RPI linked Notes maturing in June 2033 with a coupon of 3.249%.

On 29 October 2015, Affinity Water Programme Finance Limited completed a tap issue of its 1.548% RPI linked Notes maturing in June 2045 of £40,000,000 on the same terms as the existing 2045 Notes.

On 19 February 2016, Affinity Water Programme Finance Limited issued £10,000,000 Class B Guaranteed RPI linked Notes maturing in June 2033 with a coupon rate of 1.024%.

On 22 August 2016, Affinity Water Programme Finance Limited exchanged £65,800,000 of its 3.625% Guaranteed Notes due 2022 for a new issue of 3.278% Guaranteed Notes due 2042. An additional £19,200,000 of 3.278% Guaranteed Notes due 2042 were issued at the same time.

On 22 November 2017, Affinity Water Programme Finance Limited issued £60,000,000 Class A Guaranteed Notes maturing in November 2033 with a coupon of 2.699% and £60,000,000 Class A Guaranteed CPI linked Notes maturing in November 2042 with a coupon of 0.230%.

On 22 January 2019, the assets and liabilities of Affinity Water Programme Finance Limited were transferred to the company's subsidiary Affinity Water Finance PLC.

On 20 October 2021, Affinity Water Finance PLC issued £130,000,000 Class A Guaranteed CPI linked Notes maturing in September 2038 with a coupon rate of 0.010%.

The net proceeds of the bond issues and the tap issue were lent to the company on the same terms.

On 4 February 2013, the company borrowed an amount of £3,550,000 from Affinity Water Capital Funds Limited, the company's intermediate parent company. The final repayment date of this loan is 31 March 2036, with interest terms having been set at 4.500%.

The company has unconditionally and irrevocably guaranteed the due and punctual payment of all sums from time to time payable by Affinity Water Finance (2004) PLC and Affinity Water Finance PLC in respect of the bonds issued by these companies. These guarantees constitute direct, general and unconditional obligations of the company, which will at all times rank at least pari passu with all other present and future unsecured obligations. The bonds issued are also guaranteed by Affinity Water Holdings Limited, the company's immediate parent undertaking.

The fair value of the bonds on-lent from the financing subsidiaries at 31 March 2022 is £1,560,813,000 (2021: £1,496,837,000). The fair value of Class A bonds has been derived from 'level 1' fair value measurements: quoted prices (unadjusted) in active markets for identical liabilities. The fair value of Class B bonds has been derived from 'level 2' fair value measurements: directly observable market inputs other than Level 1 inputs. The fair value of Class B bonds is calculated by discounting expected future cashflows at a discount rate which is derived from the yield on comparable instruments which are observable in the market.

The company is subject to a number of covenants in relation to its borrowings, which, if breached, would result in its loans becoming immediately repayable. These covenants specify certain limits in terms of key ratios such as net cash flow to debt interest and net debt to RCV. At the year-end the company was not in breach of any financial covenants.

Notes to the financial statements continued

18. Lease liabilities

	2022 £000	2021 £000
Non-current:		
Lease liabilities	**6,329**	6,016
Current:		
Lease liabilities	**3,317**	3,667

The following amounts in respect of leases are included within these financial statements:

	2022 £000	2021 £000
Depreciation charge of right-of-use assets (refer to note 7)	**3,681**	3,684
Interest expense on lease liabilities (refer to note 4)	**313**	315
Expense relating to short-term leases (refer to note 2.1)	**37**	115
Expense relating to leases of low-value assets (refer to note 2.1)	**129**	91
Principal elements of lease payments included within cash flows from financing activities	**3,649**	3,630
Interest payments included within cash flows from operating activities	**313**	315
Total cash outflow for leases in the statement of cash flows	**3,962**	3,945
Additions to right-of-use assets (refer to note 7)	**3,660**	756
Carrying amount of right-of-use assets (refer to note 7)	**9,440**	9,508

19. Deferred tax liabilities

19.1 Analysis of deferred tax assets and deferred tax liabilities

	2022 £000	2021 (restated) £000
Deferred tax assets:		
– Deferred tax asset to be recovered after more than 12 months	**(585)**	(570)
– Deferred tax asset to be recovered within 12 months	**(38)**	(30)
	(623)	(600)
Deferred tax liabilities:		
– Deferred tax liability to be settled after more than 12 months	**232,153**	183,611
	232,153	183,611
Deferred tax liabilities – net	**231,530**	183,011

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs, and to include a Debit Value Adjustment on the inflation swap derivative instruments. Further details are included on pages 211 to 212

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The gross movement on the deferred tax account is as follows:

	£000
At 1 April 2020 (restated)	198,602
Adjustment to prior year	421
Credited to the income statement (restated)	(9,901)
Credited to other comprehensive income	(6,111)
At 31 March 2021 (restated)	**183,011**
Adjustment to prior year	**(2,450)**
Impact of change in tax rate	**56,456**
Credited to the income statement	**(10,949)**
Charged to other comprehensive income	**5,462**
At 31 March 2022	**231,530**

The adjustment to prior year lines above are due to the tax provision in the accounts being a best estimate at the time. The estimate is corrected when the tax returns are finalised and submitted to HMRC 12 months after the year-end.

Notes to the financial statements continued

19. Deferred tax liabilities continued

The movement in deferred tax assets and liabilities during the year is as follows:

19.2 Deferred tax liabilities

	Accelerated capital allowances £000	Retirement benefit obligations £000	Total £000
At 1 April 2020 (restated)	179,354	19,877	199,231
Adjustment to prior year	421	–	421
Credited to the income statement (restated)	(10,324)	394	(9,930)
Credited to other comprehensive income	–	(6,111)	(6,111)
At 31 March 2021 (restated)	**169,451**	**14,160**	**183,611**
Adjustment to prior year	**(2,449)**	**–**	**(2,449)**
Impact of change in tax rate	**50,351**	**6,255**	**56,606**
Credited to the income statement	**(11,260)**	**183**	**(11,077)**
Charged to other comprehensive income	**–**	**5,462**	**5,462**
At 31 March 2022	**206,093**	**26,060**	**232,153**

19.3 Deferred tax assets

	Provisions £000
At 1 April 2020	(629)
Charged to the income statement	29
At 31 March 2021	(600)
Impact of change in tax rate	**(151)**
Charged to the income statement	**128**
At 31 March 2022	**(623)**

20. Provisions for other liabilities and charges

	Insurance £000	Reorganisation £000	Other £000	Total £000
At 1 April 2020	4,837	607	670	6,114
Charged to the income statement	469	–	–	469
Utilised in the year	(2,580)	(429)	–	(3,009)
At 31 March 2021	2,726	178	670	3,574
(Credited)/charged to the income statement	(105)	2,947	–	2,842
Utilised in the year	(184)	(3,125)	–	(3,309)
At 31 March 2022	**2,437**	**–**	**670**	**3,107**

Insurance

Provisions for insurance represent the amount of the company's liability in respect of individual claims. This is based upon data provided by loss adjusters to insurers and is calculated on settlement experience. The full balance of £2,437,000 is presented as a non-current liability in the statement of financial position.

Included within the provision as at 31 March 2021 is an amount of £184,000, which was recoverable from the company's insurer. The provision above is shown gross, with the corresponding receivable disclosed as a non-current other receivable on the company's statement of financial position in the prior year.

Reorganisation

The reorganisation provision includes £2,947,000 in relation to a corporate reorganisation, which was charged and utilised in the income statement during the year. A provision of £178,000 remaining from a previous reorganisation was also utilised during the year. This was presented as a current liability in the statement of financial position in the prior year.

Other provisions

Other provisions of £670,000 (2021: £670,000) relate to unfunded pension liabilities for a former Non-Executive director, which it is expected will be utilised by January 2051, and, therefore, presented as a non-current liability in the statement of financial position.

21. Dividends

	2022 £000	2021 £000
No first interim dividend paid (2021: 0.38p per share)	**–**	1,000
	–	1,000

Notes to the financial statements continued

22. Notes to the statement of cash flows

22.1 Cash generated from operations

	2022 £000	2021 (restated) £000
Loss before tax	**(55,574)**	(53,437)
Adjustments for:		
Depreciation of property, plant and equipment (note 6)	**60,451**	64,796
Depreciation of right-of-use assets (note 7)	**3,681**	3,684
Amortisation of grants and contributions	**(5,300)**	(3,041)
Amortisation of intangible assets (note 8)	**11,125**	10,132
Profit on disposal of property, plant and equipment	**(244)**	(1,061)
Loss on disposal of infrastructure assets	**728**	1,408
Post-employment benefits	**522**	393
Net finance costs (note 4)	**118,125**	65,303
Net gain on energy swap	**(27,988)**	–
Changes in working capital		
– Inventories	**(268)**	(1,063)
– Trade and other receivables	**(11,844)**	14
– Trade and other payables		
– provision element	**(467)**	(2,540)
– other	**8,333**	13,776
Cash generated from operations	**101,280**	98,364

The prior year has been restated as a result of a change in accounting policy following the IFRIC agenda decision on the treatment of configuration and customisation costs, and to include a Debit Value Adjustment on the inflation swap derivative financial instruments. Further details are included on pages 211 to 212.

Changes in working capital – trade and other receivables of £(11,224,000) in the year (2021: £14,000) primarily relates to an increase in the unbilled accrual for metered customers, VAT receivables and the movement in prepayments and accrued income, as shown in note 12.

Changes in working capital – trade and payables – other of £7,714,000 in the year (2021: £13,776,000) primarily relates to a reduction in other accruals, as shown in note 16.

22.2 Reconciliation of liabilities arising from financing activities

	At 1 April 2021 £000	Cash flow £000	Non-cash flows £000	At 31 March 2022 £000
Loan from Affinity Water Finance (2004) PLC financed by bond issue	**252,999**	**–**	**(501)**	**252,498**
Loan from Affinity Water Finance PLC financed by bond issue	**838,496**	**146,994**	**34,216**	**1,019,706**
Loan from intermediate parent company	**3,550**	**–**	**–**	**3,550**
Lease liabilities	**9,683**	**(3,962)**	**3,925**	**9,646**
Debenture stock	**34**	**–**	**–**	**34**
Total liabilities arising from financing activities	**1,104,762**	**143,032**	**37,640**	**1,285,434**

	At 1 April 2020 £000	Cash flow £000	Non-cash flows £000	At 31 March 2021 £000
Loan from Affinity Water Finance (2004) PLC financed by bond issue	253,462	–	(463)	252,999
Loan from Affinity Water Finance PLC financed by bond issue	833,595	–	4,901	838,496
Loan from intermediate parent company	3,550	–	–	3,550
Lease liabilities	12,559	(3,945)	1,069	9,683
Debenture stock	34	–	–	34
Total liabilities arising from financing activities	1,103,200	(3,945)	5,507	1,104,762

Non-cash flows relate to loan indexation and amortisation of bond issuance costs and net additions of leases.

Notes to the financial statements continued

23. Commitments

23.1 Capital commitments

Capital expenditure contracted for at the end of the reporting year, but not yet incurred, is as follows:

	2022 £000	2021 £000
Property, plant and equipment	**31,985**	19,072
Intangible assets	**2,069**	1,756
	34,054	20,828

23.2 Commitments under leases

The company leases its vehicles and head office building under non-cancellable leases expiring within a maximum of five years. The leases have varying terms, clauses and renewal rights. The company also leased IT server space until 31 December 2021.

The company does not expect to extend any vehicles leases after their lease term has expired. The company will assess closer to the expiry of the lease of the head office building whether another formal agreement will be entered in to.

From 1 April 2019, the company has applied IFRS 16 and recognised right-of-use assets for these leases, (except for short-term and low-value leases, which are not within the scope of IFRS 16), see note 18 for further information.

The future aggregate minimum lease payments for operating leases not within the scope of IFRS 16 are as follows:

	2022 £000	2021 £000
No later than one year	**76**	90
Later than one year and no later than five years	**98**	168
Later than five years	**–**	–
	174	258

24. Billing on behalf of Thames Water and Anglian Water

The company bills and collects charges in respect of sewerage and infrastructure within its area on behalf of Thames Water Utilities Limited and Anglian Water Services Limited. No amounts are included in these financial statements in respect of uncollected sewerage and sewerage infrastructure charges at 31 March 2022 (2021: £nil) and the company incurs no bad debt risk in relation to this service.

25. Events after the reporting period

There were no significant events after the reporting period.

26. Ultimate parent company and controlling party

The immediate parent undertaking of the company is Affinity Water Holdings Limited, a company registered in England and Wales.

Affinity Water Holdings Limited is wholly owned by Daiwater Investment Limited, a company registered in England and Wales. Daiwater Investment Limited is the parent undertaking of the largest group to consolidate the statutory financial statements of the company. These financial statements are also consolidated in the financial statements of Affinity Water Holdco Finance Limited, the smallest group to consolidate the financial statements of the company.

Copies of the group financial statements of Daiwater Investment Limited and Affinity Water Holdco Finance Limited for the year ended 31 March 2022 may be obtained from the Company Secretary, Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ. The directors consider Daiwater Investment Limited as the ultimate holding and controlling company in the United Kingdom.

The directors consider the following entities to be the company's ultimate controllers, as they are in a position to exercise material influence over the company's policy and affairs:

- Allianz Infrastructure Holding I Pte. Limited
- DIF Management Holding BV
- DIF Management UK Limited
- HICL Infrastructure plc
- Sun Life Financial Inc.

Allianz Capital Partners is the Allianz Group's in-house investment manager for alternative equity investments. The investment focus is on infrastructure and renewables as well as private equity funds. Allianz Capital Partners' investment strategy is targeted to generate attractive, long-term and stable returns, while diversifying the overall investment portfolio for the Allianz Group insurance companies.

DIF is an independent and specialist fund management company, which invests in infrastructure assets that generate long-term stable cash flows, including public-private partnerships, regulated infrastructure assets and renewable energy projects in Europe, North America and Australia.

HICL Infrastructure plc is a long-term investor in infrastructure assets, which are predominantly operational and yielding steady returns. HICL Infrastructure plc has a portfolio of infrastructure investments, which are positioned at the lower end of the risk spectrum, in three target market segments: public-private partnerships, regulated assets and demand-based assets. The Investment Manager to HICL Infrastructure plc is InfraRed Capital Partners Limited, a leading international investment manager focused on infrastructure and renewable energy investments. On 1 July 2020, Sun Life Financial Inc acquired an 80% interest in the InfraRed business from InfraRed Capital Partners (Management) LLP and became an ultimate controller.

Notes to the financial statements – appendices

A1. General information

The company owns and manages the water assets and network in an area of approximately 4,500km^2 split over three supply regions, comprising eight separate water resource zones, in the South East of England. The company is the sole supplier of drinking water in these areas.

The company is a private company limited by shares and is incorporated and domiciled in the United Kingdom. The address of its registered office is Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ.

Refer to note 26 for details of the company's parent company and ultimate parent company.

A2. Segmental reporting

In the same way that financial information is reported on a quarterly basis to the Board, the company's chief operating decision maker, during the current and previous financial year on a combined basis, the company presents its results under a single segment for financial reporting purposes.

A3. Accounting policies

Consolidation

The company is a wholly owned subsidiary of its ultimate holding and controlling company, Daiwater Investment Limited, which is the parent undertaking of the largest group to consolidate the statutory financial statements. It is included in the consolidated financial statements of Daiwater Investment Limited, which will be made publicly available. Therefore, the company is exempt by virtue of section 400 of the Companies Act 2006 from the requirement to prepare consolidated financial statements.

Property, plant and equipment

Property, plant and equipment are held at historical cost less accumulated depreciation and impairment charges.

Infrastructure assets comprise a network of mains and associated underground pipe-work. Infrastructure assets are held at deemed cost established through an event-driven valuation on transition to FRS 101 in 2015/16 and subsequent additions are recorded at historical cost less accumulated depreciation and impairment charges.

For accounting purposes, the network is segmented into components based on the material used to construct the pipe concerned. The estimated useful economic lives of infrastructure pipes are based on management's judgement and experience, which includes the knowledge and research of the company's dedicated asset management teams. Where management identifies that the actual useful economic life of an asset significantly differs from the estimate used to calculate its depreciation, the depreciation charge is adjusted prospectively.

Expenditure on infrastructure assets relating to increases in capacity, enhancements or material replacements of network components is capitalised where it can be reliably measured, and it is probable that incremental future economic benefits will flow to the company. The carrying amount of the replaced part is derecognised. Costs of day-to-day servicing of network components are recognised in the income statement as they arise.

Cost of other property, plant and equipment includes own work capitalised comprising the direct costs of materials, labour and applicable overheads.

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

The estimated useful lives of property, plant and equipment are:

Infrastructure assets	
Potable water distribution mains	50–150 years
Raw water pipes	50–150 years
Other property, plant and equipment	
Buildings	40–60 years
Operational structures	5–85 years
Fixed plant – short life	3–10 years
– other	10–30 years
Vehicles and mobile plant	3–10 years

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in operating profit.

The company is required to evaluate the carrying value of its property, plant and equipment for impairment whenever circumstances indicate, in management's judgement, that the carrying value of such assets may not be recoverable. An impairment review in such circumstances requires management to make subjective judgements concerning the future cash flows, growth rates and discount rates of the asset under review.

Intangible assets

Goodwill

Goodwill represents the excess of the fair value of purchase consideration over the fair value of the net assets acquired. Fair value adjustments based on provisional estimates are amended within one year of the acquisition, if required, with a corresponding adjustment to goodwill.

Goodwill is not amortised but is reviewed for impairment at least annually. Impairment reviews are also carried out if there is an indication that impairment may have occurred, or, where otherwise required, to ensure that intangible assets are not carried above their estimated recoverable amounts. Goodwill is allocated to the CGU that derives benefit from the goodwill for impairment testing purposes. Impairments are recognised immediately in the income statement.

Computer software development costs

Costs associated with maintaining computer software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the company are recognised as intangible assets only if they meet the criteria of IAS 38: 'Intangible Assets', in that it is a separable, identifiable asset and it has a future economic benefit. Other development expenditures that do not meet these criteria are recognised as an expense as incurred, including costs associated with cloud computing arrangements.

Computer software development costs recognised as assets are amortised on a straight-line basis over their estimated useful lives, which does not exceed five years. Amortisation charged on assets with finite lives is recognised in the income statement in operating costs.

Computer software development costs are reviewed for impairment where indicators of impairment exist. Impairments are recognised immediately in the income statement.

Grants and contributions

Grants and contributions received in respect of property, plant and equipment where the performance obligation is deemed to be satisfied over time (consisting of contributions for diversions and requisitioned mains/extensions, and infrastructure charges), are treated as deferred income and released to revenue over the useful economic life of the property, plant and equipment to which they relate once these assets have been commissioned.

The company may be contracted by developers in its statutory supply area to relocate a pipe, which is already in the ground; this is known as a diversion. The company may also be contracted by developers in its statutory supply area to provide a new water main or new sewer; this is known as a requisition/extension. Contributions received in respect of diversions and requisitioned mains/extensions are treated as deferred income and released to revenue over time as the company considers that the obligation to provide these services is highly interrelated with the ongoing obligation to provide water services; therefore, the performance obligation is considered to be satisfied over the period that the property, plant and equipment constructed are in service.

Infrastructure charges are charges levied on developers for network reinforcement, which is not site specific, i.e. to fund expenditure, which will contribute towards wider network reinforcement work away from the development site. Infrastructure charges are treated as deferred income and released to revenue over time as there is an implied ongoing performance obligation to improve and maintain the wider network in order to provide an ongoing supply of water services.

Grants and contributions received in respect of property, plant and equipment where the performance obligation is deemed to be satisfied at a point in time (comprising payments for connection charges) are recognised immediately in the income statement, once the performance obligation is fulfilled. Connection charges are billed to developers for the provision of a connection to an existing water main, laying a pipe to the boundary of customers' properties and connecting to their supply pipes. Connection charges are recognised in revenue in the income statement in the year that they became receivable; the performance obligation has been identified as the connection of a service pipe to the main. Once the connection is made, the performance obligation is fulfilled and the income recognised immediately in the income statement.

Each of these types of grants and contributions (contributions for diversions and requisitioned mains/extensions, infrastructure charges, and connection charges) is not a government grant within the scope of IAS 20: 'Accounting for government grants and disclosure of government assistance' as the contributions are received from developers. While there may not be a written contract with the customer, the legal duties of the company under the Water Industry Act 1991 would seem to constitute a legally enforceable contract based on the transaction prices set out in the company's charges scheme, tariff documents and invoices; accordingly these grants and contributions fall within the scope of IFRS 15.

Investments

Investment in subsidiaries are held at cost, less accumulated impairment losses.

Short-term investments are deposits that cannot be withdrawn prior to maturity and are held at cost.

Trade and other receivables

Trade and other receivables are recognised initially at transaction price. The company holds the trade receivables with the objective of collecting the contractual cash flows, and, therefore, the trade and other receivables are subsequently measured at amortised cost using the effective interest method, less expected credit losses.

Expected credit losses are based on historical recoverability and calculated by applying a range of different percentages to trade receivables of different ages. These percentages also vary between categories of trade receivables. Higher percentages are applied to those categories of trade receivable that are considered to be of greater risk and also to trade receivables of greater age. The historical recoverability of trade receivables is deemed a good estimate of future expected credit losses. At each reporting date, the company takes into consideration any significant economic changes that may impact its credit loss model and future credit losses, for example Covid-19 or the increased cost of living currently impacting our customers. To estimate the impairment to its trade receivables from either of these factors, the company has assessed its debtors based on postcode driven customer demographics. The company has assessed what it believes to be the sensitivity of each demographic to the current and emerging effects of these factors on household finances and ability to maintain payments.

The company applies the IFRS 9 simplified approach for measuring expected credit losses, which uses a lifetime expected loss allowance for all trade receivables and contract assets. To measure expected credit losses, trade receivables and contract assets are grouped based on shared credit risk characteristics and overdue days. Contract assets relate to unbilled metered consumption and have substantially the same risk characteristics as trade receivables for the same types of contract. The company has, therefore, concluded that expected loss rates for trade receivables are a reasonable approximation for loss rates for contract assets.

Inventories

Inventories are valued at the lower of cost or net realisable value after allowance for obsolete and slow-moving items. In accordance with established practice in the water industry, no value has been placed upon the water in reservoirs, mains or in the course of treatment.

Notes to the financial statements – appendices

continued

A3. Accounting policies continued

Cash and cash equivalents

Cash and cash equivalents include cash at bank and in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of 12 months or less. Term deposits with original maturities longer than three months can be redeemed early, subject to the interest income being forfeited or reduced to reimburse any cost incurred by the counterparty. These are classed as cash and cash equivalents if the deposit can be redeemed to meet short-term cash needs and there is no risk of a significant change in value as the result of an early withdrawal. Deposits that cannot be withdrawn prior to maturity are classed as short-term investments.

Current and deferred tax

The tax expense for the year comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in other comprehensive income or directly in shareholder's funds. In this case, the tax is also recognised in other comprehensive income or directly in shareholder's funds, respectively.

The current tax charge is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the date of the statement of financial position.

Deferred taxation is provided in full, using the liability method, on taxable temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. A deferred tax asset is only recognised to the extent that it is probable that sufficient taxable profits will be available in the future to utilise it. Deferred taxation is measured on a non-discounted basis using the tax rates and laws that have been enacted or substantively enacted by the date of the statement of financial position and are expected to apply when the related deferred tax asset is realised, or the deferred tax liability is settled.

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

Trade and other payables

Payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method. Payments received in advance and measured and unmeasured deferred income are contract liabilities under IFRS 15 and relate to advance contributions received in respect of connection charges, diversions and requisitioned mains/extensions and customer payments in advance for measured and unmeasured supplies.

Borrowings

All loans are recognised initially at fair value plus directly attributable transaction costs. The carrying amount of the debt is increased by the amortisation of the finance and transaction costs determined using the effective interest rate in respect of the accounting period and reduced by any payments made in the year. The finance cost recognised in the income statement is allocated to accounting periods over the term of the debt using the effective interest method.

An exchange of debt with substantially different terms is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. At the point of refinancing, all costs relating to the previous debt are written off to the income statement in full.

Financial instruments

Financial instruments, such as derivatives, are initially recognised at fair value on the date the derivative contract is entered into and are subsequently re-measured at their fair value at each reporting year. Gains or losses arising on revaluation are recorded in the income statement in the year in which they arise and are shown within either fair value gain/(loss) on inflation swaps or fair value gain/(loss) on energy swaps on the face of the income statement. Interest received or incurred on these derivative financial instruments is shown within finance income and finance costs on the face of the income statement.

Provisions

A provision is recognised when the company has a legal or constructive obligation as the result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation, and the amount can be reliably estimated.

Ofwat assesses companies' operational performance against agreed performance commitments. Certain performance commitments contain an ODI, which can carry a financial reward or penalty, or both, which will be recognised as a revenue adjustment in the next charging period. The company adjusts future tariffs to reflect such amounts and, therefore, the benefit or cost is linked to the provision of future services as well as future performance. Resultantly, the company does not recognise a provision for penalties or rewards in the financial year in which they are incurred or achieved as these amounts are not an asset or liability at the balance sheet date.

Revenue recognition

The company's core revenue stream is derived from the supply of clean water. The IFRS 15 definition of a contract is met since the UK Government has contracted with the company on behalf of customers by granting the company its water supply licence, where the underlying performance obligation is the development and maintenance of the network, and ensuring its continued availability to customers. Under IFRS 15, revenue is measured at the transaction price and is recognised as the customer receives the benefit of the water supply through consuming the water:

- For metered customers, the amount which the company has a right to receive is variable, determined by the volume of water consumed; and
- For unmetered customers, the amount which the company has a right to receive is determined by the passage of time during which a customer occupies a property to which water is supplied by the company.

The company has contracts with third parties operating in the non-household retail market for the supply of clean water (wholesale supply). The underlying performance obligation is the development and maintenance of the network, and ensuring its continued availability to such third party retailers on behalf of non-household consumers. Revenue is recognised at the point in which the company has a right to receive the revenue. For non-household retailers, the amount which the company has a right to receive is determined by non-household consumption volume data.

For metered household customers, a receivable is recognised when the customer is billed for the usage. At this point, the consideration is unconditional because only the passage of time is required before the payment is due. Where the company has provided the service before payment is due, an accrual for the consumption of water that has not yet been billed is recognised in the income statement offset by a contract receivable within assets. The accrual is estimated using a defined methodology based upon weighted average water consumption by tariff, which is calculated based upon historical information.

Unmetered customers pay a fixed amount determined by the transaction prices set out in the company's charging scheme and tariff documents. If the payments received exceed the amount the company has the right to receive (i.e. unearned income), the company recognises a payment received in advance and discloses this as a contract liability within trade and other payables.

Where non-household retailers are billed monthly in advance for wholesale charges, as determined by billing/volume reports created by the market operator, the company and presents this as a contract liability within trade and other payables.

The recognition of revenue from grants and contributions billed to developers is detailed in the grants and contributions accounting policy.

Revenue is recognised if it is probable that it will be received, considering the customer's ability and intention to pay that amount of consideration when it is due. The company is under a statutory obligation to maintain water services to domestic properties within the areas defined in its water supply licence. As a result, the company may provide water services to customers who are unlikely to pay for these services. The company does not recognise revenue where historical evidence indicates that the company will probably never be able to collect the revenue billed.

The company does not expect to have any contracts where the period between the transfer of the promised goods or services to the customer and the payment terms exceeds one year. The company, therefore, does not adjust any of its transaction prices for the time value of money.

Other income

Other income includes all income derived from sources associated with the ordinary activities of the business, other than revenue derived from the regulatory activities of the business. Other income, including mast rentals and billing and collections services, involves readily identifiable contracts with customers with clearly defined performance obligations to which prices are allocated. Income is recognised as the contracts are completed and the performance obligations satisfied. It is stated net of value added taxes.

Interest income

Interest income is calculated by applying the effective interest rate to the gross carrying amount of a financial asset, except for financial assets that subsequently become credit-impaired. For credit-impaired financial assets, the effective interest rate is applied to the net carrying amount of the financial asset (after deduction of the loss allowance).

Notes to the financial statements – appendices

continued

A3. Accounting policies continued

Leases

The company leases its head office building and most of its vehicles. Rental contracts for vehicles are typically for fixed periods of two to five years. The company has an option to extend its leases; however, no contracts are reasonably certain to be extended after their lease term has expired. The lease contract of the head office building has a remaining period of 3.5 years. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The company's lease agreements do not impose any covenants, but leased assets cannot be used as security for borrowing purposes.

The company also leased some physical IT server space that was accounted for under IFRS 16 up to 31 December 2020. The lease was subsequently renewed to 31 December 2021 and treated as a short-term operating lease until that date. All remaining IT server space has been provided through a hosting service, therefore, it is out of scope of IFRS 16 as there is not a physically distinct identifiable asset. Costs are recognised on a straight-line basis as an expense in profit or loss.

The company applies recognition exemptions to short-term leases and leases of low-value assets. Short-term leases are leases with a term of 12 months or less. Low-value assets comprise small items of office equipment and IT equipment, typically costing no more than £5,000. Costs are recognised on a straight-line basis as an expense in profit or loss.

Leases falling within the scope of IFRS 16 are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the company. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

The company's accounting policy is for assets and liabilities arising from a lease to be initially measured on a present value basis. Lease liabilities include the net present value of one or more of the following lease payments:

- Fixed payments (including in-substance fixed payments), less any lease incentives receivable; and
- Payments of penalties for terminating the lease, if the lease term reflects the lessee exercising that option.

Right-of-use assets are measured at cost comprising one or more of the following:

- The amount of the initial measurement of lease liability;
- Any lease payments made at or before the commencement date, less any lease incentives received;
- Any initial direct costs; and
- Restoration costs.

Lease payments may be discounted using the lessee's incremental borrowing rate if the interest rate implicit in the lease cannot be determined. The incremental borrowing rate is the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions. The company uses an independent third-party to determine the incremental borrowing rate for each class of lease. The weighted average lessee's incremental borrowing rate applied to the lease liabilities during the year was 2.37%. The incremental borrowing rate is re-determined annually and applied to new leases for the subsequent year.

The company enters into agreements with employees to use vehicles that it leases from a third party as a company vehicle. These agreements are considered by the company to be part of the overall compensation package of an employee and, as such, the company has applied IAS 19 'Employee benefits' in accounting for these arrangements rather than considering the arrangements as subleases of vehicles to employees under IFRS 16.

The company does not use sale and leaseback transactions.

Grafham reservoir

Under the Great Ouse Water Act of 1961, the company has an entitlement to water from the Grafham reservoir owned and operated by Anglian Water Services Limited ('Anglian Water'). The company pays Anglian Water a charge for the supply of water, which covers its share of the overall costs of running Grafham reservoir. These costs are recognised as an expense within cost of sales in the income statement as incurred.

Dividend distributions

Dividend distributions to the company's shareholder are recognised as a liability in the company's financial statements in the year in which the dividends are approved.

Retirement benefits

The company operates a pension plan, the Affinity Water Pension Plan ('AWPP'), as the AWPP's Principal Employer, providing defined benefits based on final pensionable salary. The assets of the plan are held separately from those of the company.

Affinity Water Limited was the AWPP's Principal Employer up until 31 August 2020, with former group company Castle Water (Southern) Limited (formerly Affinity for Business (Retail) Limited) being a Participating Employer of the AWPP up until this date. Since this date, Affinity Water Limited has been the sole employer.

The cost of providing benefits under the defined benefit plan is determined using the projected unit method, which attributes entitlement to benefits to the current year (to determine current service cost) and to the current and prior years (to determine the present value of defined benefit obligations) and is based on actuarial advice. Past service costs are recognised immediately in the income statement. When a settlement or a curtailment occurs, the changes in the present value of the plan liabilities and the fair value of the plan assets reflect the gain or loss, which is recognised in the income statement. Losses are measured at the date that the employer becomes demonstrably committed to the transaction and gains when all parties whose consent is required are irrevocably committed to the transaction.

The retirement benefit surplus or deficit in the statement of financial position comprises the present value of the defined benefit obligation (using a discount rate based on high-quality corporate bonds), less any past service cost not yet recognised and less the fair value of plan assets out of which the obligations are to be settled directly. Fair value is based on market price information and in the case of quoted securities is the published bid price.

Re-measurement gains and losses arising from changes in actuarial assumptions are charged or credited to shareholder's funds in other comprehensive income in the year in which they arise.

The amount charged or credited to finance costs is a net interest amount calculated by applying the liability discount rate to the net defined benefit asset or liability.

Former group company Castle Water (Southern) Limited (formerly Affinity for Business (Retail) Limited) contributed to the AWPP on behalf of its eligible employees up until 31 August 2020. As the Principal Employer, Affinity Water Limited recognised all the remeasurement gains and losses on the plan assets and liabilities. Affinity Water Limited recognised current service costs net of contributions from Castle Water (Southern) Limited (formerly Affinity for Business (Retail) Limited). Since this date, Affinity Water Limited has been the sole employer and, therefore, recognises all the remeasurement gains and losses on the plan assets and liabilities and recognises all current service costs.

Contributions to the defined contribution section of the plan are recognised within cost of sales and administrative expenses in the income statement in the year in which they become payable.

The company also has an obligation to pay pensions to former Non-Executive directors of predecessor companies. A provision in respect of the obligation is included within the net pension asset or liability.

A4. Financial instruments and risk management

Risk management

The company's financial instruments comprise borrowings, derivatives, debentures, cash and liquid resources, lease liabilities, and various items, such as trade receivables and trade payables that arise directly from operations. The main purpose of these financial instruments is to provide finance for the company's operations. The company finances its operations through a mixture of retained profits, borrowings from its subsidiary companies, borrowings from Affinity Water Capital Funds Limited, its intermediate parent, and debentures.

It is the company's policy, and has been throughout the year under review, that no trading in financial instruments shall be undertaken.

The main risks arising from the company's financial instruments are liquidity risk, credit risk, energy risk, interest rate risk and inflation risk. Treasury policies in relation to these risks are agreed in conjunction with the wider Affinity Water group.

The Board reviews and agrees policies for managing each of these risks (refer to our principal risks and uncertainties section beginning on page 98 for further information on management of these risks). These policies have remained unchanged during the year.

Day-to-day responsibility for operational compliance with the treasury policies rests with the treasurer. A treasury report is provided quarterly to the Board, which summarises treasury activities and includes details on the company's position in regard to debt and cash at the end of each quarter.

The company's treasury function does not act as a profit centre and does not undertake speculative transactions.

Liquidity risk

The objective of the company's liquidity risk management policy is to ensure that the company has banking arrangements and adequate, though not excessive, cash balances, revolving credit facilities and standby facilities to enable it at all times to have the level of funds available to it, which are necessary for the achievement of its business and service objectives.

Liquidity risk is primarily managed by maintaining a level of liquidity such that there are sufficient cash balances and committed loan facilities capable of immediate draw down to cover as a minimum the next 12 months' forecast cash requirement ensuring that over-reliance is not placed on any one counterparty, whether through cash holdings or available facilities.

Liquidity is actively monitored by the company's treasury function and reported to the Board on a quarterly basis through the treasury report.

At 31 March 2022, the company had £360,783,000 (2021: £254,898,000) of available liquidity, which comprised £205,783,000 (2021: £99,898,000) of cash and term deposits and £155,000,000 (2021: £155,000,000) of undrawn committed borrowing facilities.

The company entered into RPI linked inflation swaps in August 2018 and October 2020, and between March 2020 and June 2020, entered into a series of CPI linked inflation swaps, as detailed in the interest rate and inflation risk section of note A4.

These transactions lead to a net interest receivable cashflow over the life of the swaps, offset by an accretion payment on maturity (2026 for the RPI swaps and either 2030 or 2036 for the CPI swaps). There is no liquidity risk prior to these dates as there is no requirement to pay collateral prior to maturity. On maturity, a final accretion payment will be made based on the mark to market valuation at that date, resulting in a total forecast cash payment of £110,163,000 (2021: £76,653,000), included in the maturity analysis table. The mark to market valuation is reviewed on a monthly basis and a forecast accretion payment is reviewed annually to ensure sufficient cash balances can be made available if required.

Notes to the financial statements – appendices

continued

A4. Financial instruments and risk management continued

Liquidity risk continued

Undrawn borrowing facilities:

	2022 £000	2021 £000
Floating rate:		
– Expiring within one year	**55,000**	55,000
– Expiring in more than one year	**100,000**	100,000
	155,000	155,000

The facilities expiring within one year comprise two standby facilities with one counterparty (2021: two counterparties) in the event of a liquidity shortfall: a 364 day revolving Debt Service Reserve Facility of £32,000,000 (2021: £32,000,000), which is intended for the purpose of funding any debt service payments, and a 364 day revolving Operations and Maintenance Reserve Facility of £23,000,000 (2021: £23,000,000), which is intended for the purpose of funding operating and capital maintenance expenditure.

The facilities expiring in more than one year comprise two revolving credit facilities, £60,000,000 (2021: £60,000,000) provided by Barclays Bank PLC and £40,000,000 (2021: £40,000,000) provided by Lloyds Bank PLC. The facilities are intended for the purpose of financing capital expenditure and working capital requirements to the extent that additional funding is required and have a maturity date of July 2025 and July 2024 respectively. These facilities were renewed on 24 June 2020 and use SONIA as the reference rate and have sustainability performance measures included.

Maturity analysis

Additional risk may arise if large cash flows are concentrated within particular time periods. The maturity profile in the following table represents the forecast future contractual principal and interest cash flows in relation to the company's non-derivative financial liabilities (borrowings and lease liabilities) with agreed repayment periods on an undiscounted basis.

At 31 March 2022 Non-derivatives	**1 year or less £000**	**1–2 years £000**	**2–3 years £000**	**3–4 years £000**	**4–5 years £000**	**More than 5 years £000**	**Total £000**
Loans from subsidiaries	**53,017**	**38,836**	**39,004**	**39,176**	**289,348**	**1,262,651**	**1,722,032**
Loan from intermediate parent	**160**	**160**	**160**	**160**	**160**	**4,987**	**5,787**
Lease liabilities	**3,545**	**2,849**	**2,469**	**1,161**	**170**	**1**	**10,195**
Total non-derivatives	**56,722**	**41,845**	**41,633**	**40,497**	**289,678**	**1,267,639**	**1,738,014**

At 31 March 2021 Non-derivatives	**1 year or less £000**	**1–2 years £000**	**2–3 years £000**	**3–4 years £000**	**4–5 years £000**	**More than 5 years £000**	**Total £000**
Loans from subsidiaries	38,464	52,561	38,255	38,411	38,571	1,377,401	1,583,663
Loan from intermediate parent	160	160	160	160	160	5,146	5,946
Lease liabilities	3,220	2,689	2,019	1,662	650	–	10,240
Total non-derivatives	41,844	55,410	40,434	40,233	39,381	1,382,547	1,599,849

The maturity profile in the following table represents the forecast future net cash flows in relation to the company's derivatives estimated using the forward rates applicable at the year-end.

At 31 March 2022 Derivatives	**1 year or less £000**	**1–2 years £000**	**2–3 years £000**	**3–4 years £000**	**4–5 years £000**	**More than 5 years £000**	**Total £000**
RPI linked inflation swaps net payment/ (receivable)	**(7,233)**	**(7,131)**	**(7,026)**	**(6,920)**	**38,297**	**–**	**9,987**
CPI linked inflation swaps net payment/ (receivable)	**(6,773)**	**(6,717)**	**(6,660)**	**(6,603)**	**(6,545)**	**24,484**	**(8,814)**
Total derivatives	**(14,006)**	**(13,848)**	**(13,686)**	**(13,523)**	**31,752**	**24,484**	**1,173**

At 31 March 2021 Derivatives	**1 year or less £000**	**1–2 years £000**	**2–3 years £000**	**3–4 years £000**	**4–5 years £000**	**More than 5 years £000**	**Total £000**
RPI linked inflation swap net payment/ (receivable)	(7,439)	(7,575)	(7,479)	(7,382)	(7,283)	15,080	(22,078)
CPI linked inflation swap net payment/ (receivable)	(7,057)	(7,004)	(6,951)	(6,897)	(6,843)	(1,652)	(36,404)
Total derivatives	(14,496)	(14,579)	(14,430)	(14,279)	(14,126)	13,428	(58,482)

Credit risk

Credit risk arises principally from trading (the supply of services to customers) and treasury activities (the depositing of cash).

The financial assets that are subject to the expected credit loss model are trade and other receivables, contract assets relating to the unbilled accrual for metered customers and cash and cash equivalents. While cash and cash equivalents are also subject to the impairment requirements of IFRS 9, the identified impairment loss is nil.

Contract assets and trade and other receivables

The company applies the IFRS 9 simplified approach for measuring expected credit losses, which uses a lifetime expected loss allowance for all trade receivables and contract assets. To measure expected credit losses, trade receivables and contract assets are grouped based on shared credit risk characteristics and overdue days. Contract assets relate to unbilled metered consumption and have substantially the same risk characteristics as trade receivables for the same types of contract. The company has, therefore, concluded that expected loss rates for trade receivables are a reasonable approximation for loss rates for contract assets.

The company manages its credit risk of trade and other receivables through effective management of customer relationships. Concentrations of credit risk with respect to trade receivables are limited due to the company's customer base consisting of a large number of unrelated households and non-household retailers. The Water Industry Act 1991 (as amended by the Water Industry Act 1999) prohibits the disconnection of a water supply and the limiting of supply with the intention of enforcing payment for certain premises, including domestic dwellings. However, allowance is made by Ofwat in revenue limits at each price review for a proportion of receivables deemed to be irrecoverable.

Expected credit losses for household receivables are based on historical recoverability and calculated by applying a range of different percentages to trade receivables of different ages. These percentages also vary between categories of trade receivables. Higher percentages are applied to those categories of trade receivables, which are considered to be of greater risk and also to trade receivables of greater age; these receivables have higher expected credit losses. The company's policy is to write-off closed and live accounts that fall under the following categories: bankruptcy, liquidation, debt relief orders, deceased accounts where there is no estate, failed legal action and receivable amounts from customers who have moved out of the property with no forwarding address or are no longer responsible for payment of a water bill; the company concludes that there is no reasonable expectation of recovery under these circumstances. The historical recoverability of trade receivables is deemed a good estimate of future expected credit losses. At each reporting date the company takes into consideration any significant economic changes that may impact its credit loss model and future credit losses, for example Covid-19 or the increased cost of living currently impacting our customers.

Amounts are also written off on accounts where the company is still supplying the customer and where all reasonable internal and external debt collection activities have been undertaken. Under these circumstances, if the total receivable contains amounts over six years old, the amount over six years old or more is written off. The company's write-off policy on household receivables has remained unchanged and has been consistently applied in the current year compared with the previous year.

Notes to the financial statements – appendices

continued

A4. Financial instruments and risk management continued

Since 1 April 2017, the company has supplied wholesale water to third party retailers operating in the non-household market. Retailers operating in the non-household market have been granted a licence by Ofwat, with the financial resources of the retailer assessed on licence application and monitored on a continual basis. The company uses this assurance and monitors the recoverability of these receivables by assessing cash collection rates since market opening to ensure any uncertain receivables are provided for. At each reporting date, the company takes into consideration any significant economic changes that may impact the recoverability of these debtors and future credit losses.

At each reporting date management takes into consideration any significant economic changes that may impact the model and future credit losses. Therefore, the directors of the company do not believe there is any further credit risk provision required in excess of the expected credit losses of trade receivables (see note 12).

The loss allowance as at 31 March 2022 and 31 March 2021 was determined as follows for both trade receivables and contract assets (unbilled accrual for metered customers):

At 31 March 2022	**Current £000**	**Current £000**	**Less than 1 year £000**	**1–2 years £000**	**2–3 years £000**	**3–4 years £000**	**More than 4 years past due £000**	**Total £000**
Expected loss rate – metered household receivables	**0.28%**	**0.00%**	**3%**	**10%**	**25%**	**49%**	**100%**	
Gross carrying amount – metered household receivables	**–**	**–**	**17,394**	**4,283**	**2,207**	**1,590**	**1,878**	**27,352**
Gross carrying amount – unbilled accrual for metered customers (household)	**40,948**	**–**	**–**	**–**	**–**	**–**	**–**	**40,948**
Gross carrying amount – unbilled accrual for metered customers (non-household)	**–**	**3,505**	**–**	**–**	**–**	**–**	**–**	**3,505**
Provision at expected loss rate	**101**	**–**	**448**	**448**	**545**	**781**	**1,878**	**4,201**
Additional provision	**–**	**–**	**2,177**	**–**	**–**	**–**	**–**	**2,177**
Amounts provided at 100%	**–**	**–**	**1,714**	**3,406**	**2,767**	**2,120**	**2,448**	**12,455**
Loss allowance	**101**	**–**	**4,339**	**3,854**	**3,312**	**2,901**	**4,326**	**18,833**

	Current £000	**Less than 1 year £000**	**1–2 years £000**	**2–3 years £000**	**3–4 years £000**	**More than 4 years past due £000**	**Total £000**
Expected loss rate – unmetered household receivables	–	3%	7%	17%	42%	100%	
Gross carrying amount – unmetered household receivables	–	6,452	2,859	1,686	1,070	1,554	13,622
Provision at expected loss rate	–	175	191	290	451	1,554	2,661
Additional provision	–	857	–	–	–	–	857
Amounts provided at 100%	–	333	2,559	2,377	1,854	2,405	9,527
Loss allowance	–	1,365	2,750	2,667	2,305	3,959	13,045

	Less than 3 months £000	**3–6 months £000**	**6–9 months £000**	**9–12 months £000**	**More than 12 months past due £000**	**Total £000**
Expected loss rate – developer services	**0%**	**34%**	**38%**	**14%**	**86%**	
Gross carrying amount – developer services	**917**	**389**	**230**	**978**	**1,047**	**3,561**
Loss allowance	**–**	**131**	**88**	**140**	**901**	**1,260**
Total loss allowance						**33,138**

At 31 March 2021	Current £000	Current £000	Less than 1 year £000	1–2 years £000	2–3 years £000	3–4 years £000	More than 4 years past due £000	Total £000
Expected loss rate – metered household receivables	0.14%	–	2%	7%	16%	33%	100%	
Gross carrying amount – metered household receivables	–	–	15,679	3,506	2,119	1,344	1,649	24,297
Gross carrying amount – unbilled accrual for metered customers (household)	36,793	–	–	–	–	–	–	36,793
Gross carrying amount – unbilled accrual for metered customers (non-household)	–	2,710	–	–	–	–	–	2,710
Provision at expected loss rate	51	–	236	238	329	443	1,649	2,946
Additional provision	–	–	1,612	–	–	–	–	1,612
Amounts provided at 100%	–	–	3,748	4,192	3,230	1,979	1,614	14,763
Loss allowance	51	–	5,596	4,430	3,559	2,422	3,263	19,321

	Current £000	Less than 1 year £000	1–2 years £000	2–3 years £000	3–4 years £000	More than 4 years past due £000	Total £000
Expected loss rate – unmetered household receivables	–	2%	5%	11%	27%	100%	
Gross carrying amount – unmetered household receivables	–	5,845	3,084	1,630	1,104	1,402	13,066
Provision at expected loss rate	–	114	139	186	297	1,402	2,138
Additional provision	–	734	–	–	–	–	734
Amounts provided at 100%	–	2,635	3,023	2,544	1,850	684	10,736
Loss allowance	–	3,483	3,162	2,730	2,147	2,086	13,608

	Less than 3 months £000	3–6 months £000	6–9 months £000	9–12 months £000	More than 12 months past due £000	Total £000
Expected loss rate – developer services	–	43%	59%	70%	100%	
Gross carrying amount – developer services	1,569	353	184	240	724	3,070
Loss allowance	–	150	108	167	724	1,149
Total loss allowance						34,078

A reconciliation between the opening and closing loss allowances for trade receivables and contract assets for the year ended 31 March 2022 is shown in note 12.

Notes to the financial statements – appendices

continued

A4. Financial instruments and risk management continued

At 31 March 2022 and 31 March 2021, the maximum exposure to credit risk was represented by the carrying amount of each financial asset in the statement of financial position:

	2022 £000	2021 (restated) £000
Cash and term deposits (note 14)	**135,604**	84,766
Short-term deposits (note 9)	**70,179**	15,132
Trade and other receivables (excluding prepayments and amounts recoverable from the company's insurer)	**97,967**	87,164
	303,750	187,062

The company manages its risk from treasury activities by ensuring counterparties meet the minimum credit requirements approved by the Board, which include a maximum peak exposure limit and minimum credit rating. Credit exposure is monitored regularly by the company's treasury function and is reported quarterly to the Board through the treasury report.

The breakdown of cleared cash and cash equivalents and short-term deposits treated as investments exposed to credit risk at each of the credit ratings per Standard & Poor's at 31 March is:

	2022 £000	2021 £000
AAA	**101,125**	41,116
A-1+	**35,048**	–
A-1	**67,212**	52,098
A	**–**	5,084
	203,385	98,298

These are all short-term ratings.

Interest rate and inflation risk

The company seeks to manage its interest rate risk by maintaining its exposure within a Board approved range, primarily through using a mixture of fixed, inflation linked and floating rate borrowings. An RPI linked inflation swap with a nominal value of £135.0m, which is linked to the maturity of the Class A fixed rate £250.0m bond (July 2026), was entered into in August 2018 as this was the most efficient way to switch to a higher proportion of index linked debt. A further RPI linked inflation swap with a nominal value of £75.0m, also linked to the maturity of the Class A fixed rate £250.0m bond (July 2026), was entered into in October 2020, although backdated to 1 August 2020. A series of CPI linked inflation swaps with a total nominal value of £250.0m, linked to the maturity of the Class A fixed rate £250.0m bond (March 2036), were entered into between March 2020 and June 2020.

These swaps will lead to net interest receivable cashflow over the life of the swaps, which is expected to increase the headroom against our covenant limits, offset by an accretion payment on maturity. Movements in RPI/CPI forward rates create fair value profits or losses, which will flow through the income statement.

The company earns an economic return on its RCV, comprising a real return through revenues and an inflation return as an uplift to its RCV. To the extent that nominal debt liabilities finance a proportion of the RCV, there is an asset liability mismatch, which potentially exposes the company to the risk of economic loss where actual inflation is lower than that implicitly locked in through nominal debt. The company's index-linked borrowings, which are linked to inflation, form a partial economic hedge of the company's regulatory assets, which are also linked to inflation.

Interest rate and inflation risks are reported quarterly to the Board through the treasury report.

The interest rate profile of the company's debt is as follows:

As at	Fixed rate debt £000	RPI linked debt £000	CPI linked debt £000	Total £000
31 March 2022	**671,752**	**387,649**	**216,387**	**1,275,788**
31 March 2021	672,411	360,188	62,480	1,095,079

Sensitivity analysis

Sensitivity analysis has not been performed on movements in interest rates as the company's fixed rate debts had no exposure to interest rates as at 31 March 2022. The following table details the sensitivity of profit before taxation to changes in RPI and CPI on the company's index-linked borrowings, RPI linked inflation swap and CPI linked inflation swap. The analysis relates to the position at the reporting date and is not indicative of the years then ended, as these factors would have varied throughout the year.

Impact on profit before taxation	2022 £000	2021 £000
1% increase in RPI	**(3,872)**	(3,559)
1% decrease in RPI	**3,872**	3,640
1% increase in CPI	**(2,406)**	(630)
1% decrease in CPI	**1,600**	631

Energy price risk

The company is allowed a fixed amount of revenue by the regulator, in real terms, to cover electricity costs for each five-year regulatory pricing period. To the extent that electricity prices remain floating over this period, this exposes the company to volatility in its operating cash flows. The company has mitigated this risk by fixing the price on a proportion of its anticipated electricity usage out to the end of AMP7 through entering into electricity swap contracts.

Currency risk

The company has no material net exposure to movements in currency rates.

Capital risk management

The gearing policy approved by the Board is a target measured as net debt (as defined in the company's WBS documentation, refer to table 1E of the company's regulatory Annual Performance Report) to RCV, of 80%. This allows sufficient headroom within the company's financial covenants, which are triggered at a level of more than 90%. The company's gearing on this basis was 73.0% at 31 March 2022 (76.0% at 31 March 2021).

Assuming no significant changes to existing credit rating agencies' methodologies or sector risk assessments, the company aims to maintain its existing credit ratings of A3 with Moody's, BBB+ with Standard & Poor's and BBB+ with Fitch for the Class A bonds issued by its financing subsidiaries. These ratings are used by the industry's economic regulator, Ofwat, to assess the company's ability to comply with its licence requirement to maintain an investment grade credit rating.

The company looks to manage its risk by monitoring and maintaining the relevant key financial ratios used by the credit rating agencies to determine the credit ratings given. Further detail on the precise measures and methodologies used to assess water companies' credit ratings can be found in the methodology papers published by the rating agencies. Gearing and credit ratings are reported quarterly to the Board through the Treasury Report.

Notes to the financial statements – appendices

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A5. Retirement benefits

Defined benefit section

The company's pension plan providing benefits based on final pensionable salary is closed to new members (the two precursor plans closing in April 1996 and September 2004). The assets of the AWPP are held separately from those of the company. The plan's corporate trustee (the 'Trustee') is a subsidiary of Affinity Water Capital Funds Limited, an intermediate parent of the company.

The risks of the plan are as follows:

Asset volatility

The plan liabilities are calculated using a discount rate set with reference to high-quality corporate bond yields. If plan assets underperform this yield, this will create a deficit.

The assets of the plan include a proportion of equities, which are expected to outperform corporate bonds in the long term, while providing volatility and risk in the short term. As the plan has matured, the Trustee has commenced reducing the level of investment risk and will be investing more in assets that better match the liabilities of the plan and expected cash outflows based on the plan's maturity profile.

The company believes that due to the strength of its business and the long-term nature of the plan liabilities, a level of continuing equity investment is an appropriate element of the Trustee's long-term strategy to manage the plan efficiently.

Changes in bond yield

A decrease in corporate bond yields will increase plan liabilities, although this will be partially offset by an increase in the value of the plan's bond holdings.

Life expectancy

The majority of the plan's obligations are to provide benefits for the life of its members, so increases in life expectancy will result in an increase in the plan's liabilities.

Inflation risk

The pension obligations are linked to inflation, and higher inflation will lead to higher liabilities (although, in most cases, caps on the level of inflationary increases are in place to protect the plan against extreme inflation).

Investment strategy

Following a Trustee investment strategy review in 2018/19, and the focus towards a 'cashflow driven investment' strategy, the Trustee implemented the following changes to the plan's portfolio at that time:

- Increased the level of interest rate and inflation hedging provided by the plan's assets from 90% to 92.5%, subsequently rebalanced to 90% in December 2021; and
- Introduced a new segregated actively managed investment 'liability driven investment/cashflow driven investment' portfolio managed by Insight Investment Management Limited, which is expected to provide stable returns and regular income to meet the plan's outgoings.

The latest actuarial valuation of the AWPP, determined by an independent qualified actuary, was at 31 December 2020, which concluded that the pension plan was 96% funded on a self-sufficiency basis. This actuarial valuation was made on the 'attained age' funding method, based on the following assumptions:

RPI inflation:	measured by reference to the Bank of England gilt inflation curve
CPI inflation:	measured by reference to the RPI inflation curve described above less 1.0% per annum pre-2030 and less 0% per annum post-2030
Pre-retirement discount rate:	measured by reference to the Bank of England gilt yield curves plus 0.25% per annum
Post retirement discount rate:	measured by reference to the Bank of England gilt yield curves plus 0.25% per annum
Salary increases:	measured by reference to the CPI inflation curve described above plus 0.5% per annum
Deferred pension increases:	measured by reference to the CPI or RPI inflation curves described above with an appropriate adjustment for any caps and collars
Pension increases:	measured by reference to the CPI or RPI inflation curves described above with an appropriate adjustment for any caps and collars

Defined benefit section – employer contributions

Based on the latest actuarial valuation at 31 December 2020, and to eliminate the funding shortfall identified, as well as funding the future cost of benefits being accrued within the plan, the company agreed to pay contributions of £1,250,000 prior to 31 July 2021, £1,600,000 prior to 31 December 2021, and £1,600,000 per annum commencing from 1 January 2022 onwards.

The contributions expected to be paid by the company into the AWPP for the year ending 31 March 2023 are, therefore, £1,600,000 (£5,000,000 in the year ended 31 March 2022, based on the former Schedule of Contributions and dependent on the outcome of the actuarial valuation as at 31 December 2020 being undertaken at the time).

The weighted average duration of the defined benefit obligation is 16.5 years (2021: 17.5 years).

Defined benefit section – financial and demographic assumptions

Adjustments to actuarial valuations have been made based on the following assumptions:

	2022	2021
Discount rate	**2.70% pa**	1.95% pa
Salary growth	**3.60% pa**	3.25% pa
RPI	**3.65% pa**	3.25% pa
CPI	**3.10% pa**	2.75% pa
Life expectancy for a male pensioner from age 65 (years)	**22**	22
Life expectancy for a female pensioner from age 65 (years)	**24**	24
Life expectancy from age 65 (years) for a male participant currently aged 45 (years)	**24**	23
Life expectancy from age 65 (years) for a female participant currently aged 45 (years)	**26**	26

Deferred pensions are revalued to retirement age in line with the CPI assumption, of 3.10% per annum (2021: 2.75% per annum) unless otherwise prescribed by statutory requirements or the plan rules.

Defined benefit section – sensitivity analysis

The below sensitivity analyses are based on a change in an assumption, while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit asset to significant actuarial assumptions, the same method (present value of the defined benefit asset calculated using the projected unit credit method at the end of the reporting year) has been applied as when calculating the pension asset recognised within the statement of financial position.

	Change in assumption	Impact on defined benefit obligation	Change in assumption	Impact on defined benefit obligation
2022				
Discount rate	**0.5% decrease**	**8.6% increase**	**0.5% increase**	**7.6% decrease**
Salary growth	**0.5% increase**	**0.8% increase**	**0.5% decrease**	**0.7% decrease**
Pension growth rate	**0.5% increase**	**6.8% increase**	**0.5% decrease**	**6.1% decrease**
Life expectancy	**1 year increase**	**4.0% increase**	**1 year decrease**	**4.0% decrease**
2021				
Discount rate	0.5% decrease	9.2% increase	0.5% increase	9.2% decrease
Salary growth	0.5% increase	0.9% increase	0.5% decrease	0.9% decrease
Pension growth rate	0.5% increase	7.5% increase	0.5% decrease	7.5% decrease
Life expectancy	1 year increase	4.0% increase	1 year decrease	4.0% decrease

Notes to the financial statements – appendices

continued

A5. Retirement benefits continued

Defined benefit section – net retirement benefit surplus

At 31 March, the fair values of the plan's assets recognised in the statement of financial position were as follows:

	Plan assets %	2022 £000	Plan assets %	2021 £000
Equity securities	**7%**	**37,244**	6%	33,415
Debt securities	**71%**	**391,678**	73%	392,829
Property	**–**	**156**	–	266
Infrastructure	**1%**	**3,388**	2%	9,575
Liability driven investments	**15%**	**80,555**	13%	70,344
Cash and cash equivalents	**6%**	**34,481**	6%	33,941
Total fair value of the plan's assets	**100%**	**547,502**	100%	540,370
Present value of defined benefit obligations		**(443,255)**		(465,838)
Net retirement benefit surplus		**104,247**		74,532

The total of assets that are quoted is £441,737,000 (2021: £416,456,000) and the total of assets that are unquoted is £105,765,000 (2021: £123,914,000).

Defined benefit section – fair value of plan assets

Movements in the fair value of the plan's assets were as follows:

	£000	£000
At 1 April 2021 / 1 April 2020	**540,370**	501,251
Benefits paid	**(15,301)**	(16,395)
Principal employer contributions	**3,539**	2,897
Contributions by plan participants	**215**	552
Interest income	**10,430**	11,416
Re-measurement gains	**8,249**	40,649
At 31 March 2022 / 31 March 2021	**547,502**	540,370

Defined benefit section – present value of plan liabilities

Movements in the present value of the defined benefit liabilities are as follows:

	£000	£000
At 1 April 2021 / 1 April 2020	**(465,838)**	(396,632)
Benefits paid	**15,301**	16,395
Contributions by plan participants	**(215)**	(552)
Net current service cost	**(4,061)**	(3,259)
Past service cost	**–**	(31)
Interest expense	**(8,942)**	(8,948)
Re-measurement gains/(losses)	**20,500**	(72,811)
At 31 March 2022 / 31 March 2021	**(443,255)**	(465,838)

Defined contribution section

At the same time that the defined benefit section became closed to new entrants, the company established a defined contribution section to provide pension benefits to qualifying employees.

The total pension charge for the defined contribution section of the AWPP for the year ended 31 March 2022 was £3,677,000 (2021: £3,573,000). There are no amounts prepaid or outstanding in respect of the defined contribution section at 31 March 2022 (2021: £nil).

A6. Subsidiaries

Name of company	Country of registration/ incorporation	Registered address	Nature of business	Type of holding	Proportion of voting rights and shares held
Affinity Water Finance (2004) PLC	United Kingdom	Tamblin Way, Hatfield, Hertfordshire AL10 9EZ	Financing company	Ordinary shares	100%
Affinity Water Finance PLC	United Kingdom	Tamblin Way, Hatfield, Hertfordshire AL10 9EZ	Financing company	Ordinary shares	100%
Three Valleys Water Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire AL10 9EZ	Dormant company	Ordinary shares	100%
Tendring Hundred Water Services Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire AL10 9EZ	Dormant company	Ordinary shares	100%
Folkestone and Dover Water Services Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire AL10 9EZ	Dormant company	Ordinary shares	100%
White Cliffs Water Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire AL10 9EZ	Dormant company	Ordinary shares	100%

The company has an investment of £50,000 in 100% of the £1 ordinary shares of a subsidiary company, Affinity Water Finance (2004) PLC. The principal activity of Affinity Water Finance (2004) PLC, incorporated in the United Kingdom, is to raise finance for the company. It made a profit of £1,000 for the year ended 31 March 2022 (2021: £1,000), relating to bond management fees charged to Affinity Water Limited.

The company also has an investment of £50,000 in 100% of the £1 ordinary shares of another subsidiary company, Affinity Water Finance PLC. The principal activity of Affinity Water Finance PLC, incorporated in the United Kingdom, is to raise finance for the company. It made a profit of £7,000 for the year ended 31 March 2022 (2021: £6,000), relating to bond management fees charged to Affinity Water Limited.

The four dormant subsidiaries listed above file accounts at Companies House.

A7. Related party transactions

Purchases of goods and services

			2022		2021	
Related party	Nature of relationship	In respect of	Value £000	Balance £000	Value £000	Balance £000
Allianz Global Corporate & Speciality	Common ownership	Insurance	**1,701**	**(616)**	2,093	(1,084)
Allianz Insurance	Common ownership	Insurance	**539**	**(539)**	–	–
Allianz Engineering	Common ownership	Insurance	**–**	**–**	1	–
SSE plc	Shared director (up until 29 January 2021)	Electricity	**–**	**–**	21,965	–

Sales of goods and services

			2022		2021	
Related party	Nature of relationship	In respect of	Value £000	Balance £000	Value £000	Balance £000
Vistry Group plc	Shared director	Connection charges	**4**	**–**	2	–

See note 3.3 for disclosure of the directors' remuneration.

Glossary of terms

Glossary of key abbreviations and definitions used within this report and the water industry

AMP – Asset Management Plan

The five-year price control period covered by a company's Business Plan. AMP6 ran from 2015 to 2020. AMP7 runs from 2020 to 2025.

C-MeX – Customer Measure of Experience

A measure of customer service levels being used by Ofwat in AMP7.

CCG – Customer Challenge Group

An independent group of individuals who hold us to account on how we are performing against our Performance Commitments.

CRI – Compliance Risk Index

A measure of water quality compliance designed to illustrate the risk arising from treated water compliance failures.

D-MeX – Developer Measure of Experience

A measure of developer service levels being used by Ofwat in AMP7.

Ml/d – Megalitres per day

A measure of consumption. One megalitre is equal to one million litres.

MOSL – Market Operator Services Limited

The market operator of England's non-household water market.

MZC – Mean Zonal Compliance

A measure of water quality compliance derived from monitoring samples taken from customers' taps.

ODI – Outcome Delivery Incentive

Mechanism for financial rewards or penalties that underpins the Performance Commitments submitted in a company's Business Plan (the "Plan").

PCC – Per Capita Consumption

The amount of water used by each person, usually measured in litres per person per day ('l/p/d').

PR – Periodic Review

The price determination process undertaken by Ofwat ahead of each new AMP. The PR19 process set the price controls for AMP7.

R-MeX – Retailer Measure of Experience

A measure of retailer service levels being used by Ofwat in AMP7.

RCV – Regulatory Capital Value

The economic value of the regulated business, as determined by the price control regime.

RORE – Return on Regulated Equity

A financial metric used by Ofwat to determine the profitability of the regulated company.

Totex – Total expenditure

The sum of operational expenditure and capital expenditure.

WINEP – Water Industry National Environment Programme

A set of actions that water companies must complete in order to meet their environmental obligations.

WRMP – Water Resources Management Plan

A long-term plan detailing how a water company will maintain a sustainable balance between future demand and supply of water.

Our regulators

CCW – Consumer Council for Water

The regulator tasked with investigating customer complaints relating to service, price and value for money.

Defra – Department for the Environment,

Food and Rural Affairs

The UK Government department responsible for water policy.

DWI – Drinking Water Inspectorate

The regulator ensuring compliance with drinking water quality regulations.

EA – Environment Agency

A non-governmental organisation that controls, inter alia, how much water we can abstract from the environment.

Ofwat – Water Services Regulation Authority

The economic regulator of the water industry.

Consultancy, design and production by: jonesandpalmer.co.uk