

DAIWATER INVESTMENT LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2023

(Registered Number 10738347)

Daiwater Investment Limited

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Daiwater Investment Limited

Directors and advisers

Directors

Jonathan Carter (appointed 4 October 2022)
Andrew Cox (appointed 15 November 2023)
Michael Osborne
Roxana Tataru
Adam Waddington (appointed 12 May 2023)

Company secretary

Patrick Makoni (appointed 3 April 2023)
Sunita Kaushal (resigned 3 April 2023)

Registered office

Tamblin Way
Hatfield
Hertfordshire
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Independent auditors

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40 Clarendon Road
Watford
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WD17 1JJ

Registered number

10738347

Daiwater Investment Limited

Board's welcome

Highlights

- We met our leakage reduction target for the year and reduced leakage by 15.8%. We are on track to meet a 20% reduction in leakage by 2025.
- We published our draft water resources management plan – setting out how we will provide a sustainable supply of water, while taking care of the environment for the next 50 years.
- We met all obligations under the Water Industry National Environment Programme ('WINEP') through our various schemes to improve the natural environment, completing 23 project units to date for the AMP.
- We improved our approach to ESG reporting, producing a unified ESG policy and establishing an ESG sub-committee at Executive Management team level.
- It is my great pleasure to welcome you to our Annual Report, and also to welcome to the group our new CEO, Keith Haslett, who started in January.

After a rigorous search and selection process, we are confident we have found a great leader who shares our goals and ambitions and is passionate about achieving them. I look forward to working with Keith towards these ends.

I would also like to thank Stuart Ledger for his work as interim CEO while we searched for a permanent appointment. Stuart helped us build strong foundations to meet our demanding commitments for the AMP, and focused the business on the PR24 price review.

As you will see in this report, the past year has been challenging for us. Extreme weather and inflationary pressures affected our operations in a number of key areas. However, underlying performance aside from the extreme weather events was strong, and I am therefore confident we have the right systems in place to be performing strongly by the end of the AMP.

Reducing leakage

Despite the extreme weather, I am very pleased to report that we beat our leakage target this year, a milestone we should celebrate. We have set ourselves one of the toughest leakage reduction targets in the industry. In an area that contains a mix of dense urban populations and rural areas with many interconnections in the network, we

face a greater risk of bursts occurring compared with less-populated areas. We are well on course to achieving our target to reduce leakage by 20% by 2025, and I would like to congratulate our hard-working colleagues throughout the group for this significant achievement.

As we know, alongside reducing demand and bringing online new sources of water, tackling leakage plays an incredibly important part in the long-term sustainable supply of water, and in helping take care of our environment. It is also important to our customers, and is, in fact, a defining issue on how the public perceive their water company and the wider industry.

Public perception

On public perception of the water industry, it could be argued that this is at an all-time low, given frequent reports of environmental concerns, would appear to be attributable in part to sewage discharges. We recognise the environmental impact this has on our rivers and globally rare chalk streams, and that this has affected public confidence in the entire industry. Although we don't manage wastewater and sewage, we are passionate about the health of our rivers and we believe we have an important part to play in returning them to good ecological health. This is not just an issue for the water industry, but a societal one. Which is why we need to continue working with customers, government, the water industry, environmental groups, the agricultural industry and other sectors to increase public understanding on what affects our rivers and what we all need to do to improve them.

Enhancing the environment

We have a great story to tell on our environmental activities and ambitions. In 2022/23, we met all our obligations under the Water Industry National Environment Programme ('WINEP'), through our various schemes to improve the natural environment. These include our river-restoration projects and working with the agricultural community on schemes designed to improve soil fertility and improve the quality of water in the natural environment. We are very much on track to achieve all of WINEP's desired outcomes by the end of this AMP in 2025. However, we know there is much more we need to do, and so we have made some ambitious proposals for environmental improvements in our draft business plan for the next AMP, from 2025 to 2030.

Daiwater Investment Limited

Board's Welcome (continued)

Our future water resources

Over the past year the group, made significant progress in the planning for future water resources. Following the first-ever regional plan for water resources, we published our 50-year plan (known as the Water Resources Management Plan), which aims to address the immense challenges we face from climate change, population growth, demand for water and taking care of the environment.

This is a collaborative approach that represents a fundamental change in how we plan, invest and build a water sector fit for this century and beyond – not just within our company boundaries, but as regions working together across the country. It is an exciting project to be a part of, and one that demonstrates the substantial investment the industry will be making over the next 50 years, through sums unparalleled in the history of the industry. The investment will ensure a sustainable supply of water for a growing population and make our essential public supply resilient to the shocks and stresses of the impacts of climate change.

In the near term, between 2025 and 2030, the group is proposing a much larger investment in our network, services and environmental commitments compared to our current AMP (2020–2025). Over the past few years, our teams have been busy preparing our draft business plan – our most ambitious to date – following extensive research on the issues that matter most to our customers and other stakeholders. We published the draft plan for consultation in May 2023. It represents a significant step in how we achieve our long-term ambitions, as laid out in our Strategic Direction Statement and 50-year action plan for water.

Sustainability

Sustainability is at the very heart of the group's activities and all of our plans. More importantly, it demonstrates how we add value to society. To enhance sustainability within our activities, we use environmental, social and governance ('ESG') themes aligned to the UN's Sustainable Development Goals, to help us understand both the risks for the business and our opportunities to add value. We have established a framework of themes, not just throughout our operations, but

across the group's owners, with regular checks and assurances at Board level.

We continue to improve our approach to ESG reporting and, over the past year, produced a unified ESG policy to help guide and align our teams, while establishing an ESG sub-committee at Executive Management Team level. This committee will monitor the performance of our ESG programmes and balance these with our performance commitments, including overseeing climate-change risks and opportunities and progress towards net zero.

Our ESG initiative also aims to demonstrate the multi-capital value of the group. We recognise it is important to take a deeper view of value, as the services we provide offer broader value creation beyond the financial. We aim to understand how we create value through six capitals – natural, human, social, manufactured, intellectual and financial assets in our business. There is a strong focus on the value we create through natural capital at the group.

Our customer service

Our Customer Measure of Experience ('C-MeX') serves as a metric to incentivise water companies in delivering exceptional customer experiences to households.

Despite a slight improvement in our customer experience scores, which covers overall perception of Affinity Water, we are disappointed to report that our ranking in the water industry C-MeX tables has remained unchanged from the previous year, placing us 14th out of 17 water companies. This has been driven by a decline in the customer service element of our C-MeX score.

We are currently reassessing our strategies to reverse this situation and ensure that prioritising the customer is at the forefront of everything we do. We acknowledge specific areas where we can enhance our service and subsequently improve our C-MeX score. These concerns primarily centre around unresolved customer queries related to billing issues, our metering programme, and visible leaks within our network and on customer properties.

Daiwater Investment Limited

Board's Welcome (continued)

Taking care of our customers

The UK is currently witnessing the highest inflation surge in the past four decades, primarily driven by escalating energy costs and the rising prices of essential household items. We are fully aware of the significant strain this places on many of the households we serve, as some customers may encounter difficulties in paying their bills.

To support our customers, we offer one of the most comprehensive social tariff programmes in the industry, with over 97,000 customers already enrolled. We consistently communicate the availability of this support through our own channels and partnerships with esteemed organisations such as Citizen Advice Bureau, Step Change, and Turn 2 Us, ensuring that individuals are well informed about the assistance we provide.

However, we acknowledge that more needs to be done beyond our social tariffs. Over the past year, we made a commitment to offer a £50 payment towards the bills of over 30,000 customers who require it the most.

Additionally, we have actively explored innovative approaches to pricing water, aiming to enhance both affordability and water demand management. In the 2022/23 financial year, we developed the WaterSave tariff trial in collaboration with our regulator Ofwat, featuring a progressive block charge system with different prices allocated to the initial, middle, and final consumption blocks. This trial, which includes a free allocation of water, will take place in the summer of 2023, involving approximately 1,500 customers from diverse income distributions and both high and low usage metered customers.

A business with people at its heart

Finally, I would like to emphasise the importance of our company culture and values. We believe these have played a significant role in our achievements to date, and we remain committed to supporting a positive, inclusive and productive work environment. We are proud of our employee-engagement initiatives, our diversity and inclusion efforts, our support networks, and other programmes that help us maintain a strong and engaged workforce. I would also like to thank everyone at the group for their continued efforts. We have had to manage some challenging events over the past year, and the hard work and commitment of all our colleagues during these times ensures we can continue to deliver a vital public service to the customers and communities we serve.

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023

Introduction

The directors present their strategic report on Daiwater Investment Limited for the year ended 31 March 2023.

Daiwater Investment Limited invests in and manages long term interests in the water industry in the United Kingdom (UK).

Affinity Water Limited is the only trading subsidiary of the group for the current year and prior year.

Affinity Water Limited owns and manages the water assets and network in an area of approximately 4,500km² split over three regions, comprising eight water resource zones, in the South East of England.

Affinity Water Limited supplies high quality drinking water to communities within the South East of England. It:

- supplies on average 936 million litres of water a day to around 3.89 million people, serving 1.48 million properties;
- operates 91 water treatment works to ensure that water is of the highest quality; and
- distributes water through a network of over 16,900km of mains.

Information on Affinity Water Limited's purpose and business model are detailed in the strategic report of its own Annual Report and Financial Statements for the year ended 31 March 2023 on its website: affinitywater.co.uk/library.

Performance

The group generated a loss for the year of £ 89,047,000 (2022: £99,505,000 loss). The statements of financial position detailed on pages 62 and 63 show shareholders' funds as at 31 March 2023 amounting to £324,365,000 (2022: £452,592,000) for the group and £757,163,000 (2022: £747,907,000) for the company.

The group was acquired by a consortium of investors led by Infracapital Partners II, the infrastructure investment fund managed by M&G (the European Investment arm of Prudential Plc), and Morgan Stanley Infrastructure Partners on 28 June 2012 and has applied acquisition accounting since that date. All company dividends had been made from distributable reverses.

As both the financial and operational results of the group are primarily determined by the results of its trading subsidiary, Affinity Water Limited, the operational and financial performance indicators and targets for the group are those of Affinity Water Limited. These performance indicators, and the performance of Affinity Water Limited for 2022/23 against targets set, are provided in detail in the strategic report of its own Annual Report and Financial Statements for the year ended 31 March 2023 on its website: affinitywater.co.uk/library.

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Risk management

The group has an established framework for identifying, evaluating and managing its key risks. Our main aim is to foster a culture where teams throughout the business manage risks as part of their management of day-to-day operations. The main risks of the group for the year ended 31 March 2023 are those of its trading subsidiary, Affinity Water Limited, and hence this section focuses on the risks and uncertainties of Affinity Water Limited (referred to as the 'subsidiary' throughout the remainder of this section). The subsidiary's Executive Management Team (EMT) also carries out regular assessments of emerging risks, including horizon scanning and monitoring of early warning indicators.

Operational risks are reviewed and prioritised on a quarterly basis in the context of existing controls. Where risks fall outside of risk appetite, action plans are prepared to implement further mitigations and these are carefully monitored to ensure they are completed and provide the desired mitigation. The most significant risks are raised for review by the EMT and may be added to the strategic risk register, which is reviewed by the Board and the Audit, Risk and Assurance Committee. The latter reviews senior management's work on risk management and reports to the Board on the effectiveness of risk management processes.

Emerging risks

The group has defined emerging risks as potential future events or circumstances that could significantly and negatively impact achievement of our strategic objectives and whose likelihood and impact cannot yet be accurately determined.

As part of the group's overall risk management framework, it carries out regular horizon scanning and analysis of various early warning indicators to identify newly emerging risks and determine if any previously identified emerging risks are increasingly likely to become real current operational risks. Where this is the case, such risks will be subject to the same rigorous process described above to evaluate and manage them. The EMT of the subsidiary holds regular sessions to identify and review current and emerging risks. Along with the strategic risks, these are reviewed at least quarterly by the EMT and at least biannually by the Board.

The group's current emerging risks are as follows:

- A. Shifts in societal and political expectations and perceptions, and rising levels of activism
- B. Skills gaps or unavailability due to a tight labour market and increasingly nomadic workforce combined with economic uncertainty
- C. Changes to our supply chain and to the water sector arising from Brexit, ongoing conflict in Europe, changed working patterns, and economic uncertainty
- D. Changes to the power industry, including regional differences in pricing and reliability of service
- E. As the cost of living crisis evolves, it is likely that we will see increasing levels of bad debt which will need to be carefully managed

There is a long-term risk that the value and utility of assets and infrastructure may be reduced as a consequence of environmental change

The group will continue to keep these and other emerging risks under regular and close review.

Climate change

Climate change is one of the greatest challenges for the whole industry and this challenge appears likely to increase in the future. Sustainability and resilience in the light of this challenge is important in maintaining the trust of our customers and regulators.

Climate change can have short and long-term impacts on our assets, operations and the services the group provides. The most recent significant example was the extreme weather the UK experienced in March 2018 the summer of 2022. While we dealt with it effectively and efficiently, we took the opportunity to review and revise our business continuity and emergency response arrangements.

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Climate change

The group has identified climate change as an underlying cause of many of the principal risks listed below, particularly 2, 5 and 7. The group has also documented in its risk registers, where appropriate, controls in place to mitigate as far as possible the potential effects of climate change in elevating those risks. The group will continue to monitor climate change and its impacts on its operations as well as the effectiveness and efficiency of its mitigating controls, with the objective of ensuring our ongoing sustainability and resilience.

On a positive note, the group fully embraces the part it has to play in combating the effects of climate change.

Principal risks

The following have been identified from the risk management analysis as potentially having material adverse effects on the group's business, financial condition, results of operations and reputation. They are managed as described but are not always wholly within the group's control and may still result in material adverse impacts. Factors other than those listed could also have a material adverse effect on the group's business activities.

We have identified 15 principal risks to our business in three categories:

Operational risks

1. Some of the subsidiary's work activities could cause serious harm to its employees, contractors or members of the public
2. The subsidiary may become unable to meet our obligations to provide a sufficient supply of high-quality drinking water
3. The subsidiary may fail to attract, develop and retain employees with the competencies, values and behaviours required to engage with and promote our corporate culture, and deliver our strategic ambition and business outcomes
4. Availability, confidentiality or quality of information or data could become compromised
5. The subsidiary's supply chain may fail to deliver the goods and services it needs to operate its business
6. The subsidiary could cause damage to the environment during its business activities
7. Climate change and other environmental factors could negatively impact the subsidiary's business operations
8. The subsidiary may fail to implement the cultural and operational transformation of its business necessary to deliver its business ambitions
9. A significant disruptive event could impact the subsidiary's ability to deliver normal business activities
10. The health of the subsidiary's assets may deteriorate such that water supply or quality is compromised

Regulatory risks

11. Changes could occur in the regulatory framework, or social or political climate, which could have significant effects on the subsidiary's operational or financial performance
12. The subsidiary may fail to comply with laws and obligations under its instrument of appointment legal, compliance or business obligations
13. Failure to achieve a satisfactory outcome from the price review PR24

Financial risks

14. The subsidiary could fail to maintain or renew appropriate financing for its business activities
15. Macro-economic factors (interest rate, inflation and tax risks) could have a material adverse effect on the subsidiary's financial performance

Daiwater Investment Limited


Strategic report for the year ended 31 March 2023 (continued)

Main changes since 2022/23

A risk relating to a failure to deliver on business plan commitments has been removed this financial year following a review by the business that felt the risk was adequately captured under Risks 2 and 8.







Additionally, we have separated Environmental risk into two separate risks. One relates to the risk that AWL may cause damage to the local environment. The second relates to climate change and extreme weather events impacting upon AWL's ability to meet its objectives. Each is different in nature, with different risk profiles and mitigations.

Operational risks

1 – Injury to staff or 3rd parties	
<p>Risk</p> <p>Failing to manage dangerous working practices may result in a fatal or personal injury, occupational ill-health, disruption to operations, reputational damage, criminal fines, civil damages or regulatory penalties.</p> <p>Link to our customer outcomes:</p> 	<p>Mitigation</p> <p>The subsidiary operates its business using its health and safety management system, which is externally verified and certified to ISO 45001. This encompasses policies, procedures, standards, guidance and risk assessment protocols.</p> <p>The subsidiary provides its employees with appropriate health and safety training to enable them to undertake their tasks and take personal responsibility for their own safety, occupational health and wellbeing, and that of others. This training includes, technical and certificated health & safety training, undertaking regular safety-related communications, safety briefings, toolbox talks, safety stand down days, and promoting safety leadership evaluations and safety conversations across the organisation.</p> <p>Through the subsidiary's procurement strategy and arrangements its contractors and suppliers are required to have externally recognised Health & Safety accreditation, which is verified by bodies such as Achilles, BSI etc. and its health and safety common standards are included as contractual documents, are regularly audited and performance reviews undertaken.</p> <p>The subsidiary has an established governance framework where health and safety-related matters and performance are tracked and monitored, spanning operational, Executive Management Team and Board levels.</p> <p>The subsidiary has an audit and inspection regime and incident review protocols in place to ensure key learnings are captured and any necessary strengthening of controls is actioned appropriately. The subsidiary also has a programme of health surveillance assessments, wellbeing initiatives and an employee assistance programme to help ensure the welfare and wellbeing of its people are effectively managed.</p>



Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

<h3>2 – Service supply to our customers</h3>	
<p>Risk</p> <p>Failure to maintain supply of water for all customers could result in consumers losing confidence in their drinking water, with consequent legal and reputational risks for our business. To measure the subsidiary's delivery, it has performance commitments which carry a penalty and reputational damage to its brand if not met. The subsidiary will deliver these commitments by investment programme and alongside looking to improve its customer experience aiming for high levels of satisfaction.</p> <p>Link to our customer outcomes:  </p>	<p>Mitigation</p> <p>The subsidiary manages this risk through careful supply and demand planning over the short and medium term, and has developed a long-term water resources management plan (WRMP), which identifies, over a 50-year period, how it will balance available supplies and required demand with sufficient headroom for unplanned outage.</p> <p>To support demand management, the subsidiary undertakes extensive education and water saving programmes, including water metering, water saving devices, links to ways to save water along with communications to help customers self-manage usage. The subsidiary undertakes asset maintenance, investment and improving resilience through measures such as removing single points of failure and increasing connectivity of the network. In the event of an emergency, the subsidiary has well-tested contingency and emergency response plans to ensure minimal disruption to our customers.</p> <p>The subsidiary has agreements with neighbouring water companies to both import and export water. Some of these are statutory agreements in use every day whilst others are used only during unplanned incidents. Some of these agreements have been in place for many decades and the subsidiary is currently reviewing them to ensure they remain suitable for its needs. Specific contingency plans exist for key Non-Household Customers who are designated as being critical national infrastructure e.g. Heathrow, Luton and Stansted Airports.</p> <p>The subsidiary continually monitors its performance on a wide range of customer metrics and takes prompt corrective action to address any indicators of dissatisfaction, working closely with regulators, customer groups and independent bodies who advise and challenge it in the development of its plans, to ensure that they reflect customers' priorities.</p>
<h3>3 – Attraction and retention of staff</h3>	
<p>Risk</p> <p>An inability to attract and retain competent and high-performing individuals in the organisation at all levels, who are motivated and engaged to deliver the business objectives.</p> <p>Link to our customer outcomes:</p> <p>   </p>	<p>Mitigation</p> <p>The subsidiary's people strategy is designed to ensure that it can attract, retain, develop and motivate the people within its business to deliver its business objectives.</p> <p>The subsidiary has a dedicated recruitment team that uses direct resourcing methods and works with recruitment suppliers to ensure good quality candidates are sourced. The use of the group's website and new careers site is crucial in providing a strong employee value proposition that will attract talent into the business. The subsidiary also operates a range of apprenticeships to bring in and develop people through its business.</p> <p>Current projects to improve attraction and retention of staff include:</p> <ul style="list-style-type: none"> • Development of a strategic workforce plan to identify the skills that will be needed by the business in the medium to long term, so that appropriate resourcing, talent pipelines and development plans can be implemented; • Improvement of the recruitment experience to provide consistency of role definitions, career pathways to support development and competency frameworks; • Focus on corporate culture, employee engagement, equality, diversity, inclusion and wellbeing, and leadership development; and • Revised and simplified performance management processes to help drive performance levels and achieve business objectives.


Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

4 – Data security / integrity	
<p>Risk</p> <p>In an ever-increasingly connected world, Affinity Water relies on its IT infrastructure and critical third-party suppliers and partners to deliver essential services to its customers. IT Infrastructure or third-party cyber incidents could result in significant disruption to services, which may have a negative impact on customers, colleagues, and business processes. It is, therefore, essential to build Affinity Water’s capability to identify and manage cyber risk, implement protective technology and processes to detect and respond to a security event and maintain plans for resilience.</p> <p>Link to our customer outcomes:  </p>	<p>Mitigation</p> <p>The subsidiary continues to invest in an ongoing programme to build and strengthen its security capability and recognises the security function as a business enabler and driver of Digital Transformation. Investment is planned to continue in the coming financial year to support Affinity Water’s holistic strategy and approach to cyber security. Based on the assumption that cyber breaches are inevitable, the strategy emphasises the need to:</p> <ul style="list-style-type: none"> • to build its capability to identify and manage cyber risks • develop and implement appropriate safeguards to ensure delivery of critical services • implement plans to detect and respond to a cybersecurity event • maintain plans for resilience to restore any lost services <p>The strategy details the objectives, intended outcomes, activities, and supporting plans to deliver a unified framework for cybersecurity and compliance with regulatory requirements and standards, including the Network and Information Systems Regulations (NIS-R) and ISO 27001. Affinity Water continues to embed the security management system and security controls within the business processes. In addition, the security management system’s overall improvement and maturity are validated through an independent assessment to determine progress and continuous improvement opportunities.</p> <p>Since the start of AMP7, significant investment has been made in building the dedicated security function and capability, including the successful deployment of leading Artificial Intelligence and Machine Learning based technologies for immediate detection, alerting and automated response to improve both the resilience to new threats and the response times to incidents.</p> <p>The subsidiary’s ultimate objective is to achieve security by design mindset and approach. This means that the system (or software) has been designed to be secure and trusted from the ground up.</p>



Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

5 – The subsidiary’s supply chain may fail to deliver the goods and services it needs to operate its business	
<p>Risk</p> <p>Global supply chains remain under stress, due to continued pressure on demand and logistics lanes, which are impacted by the sustained impact of high inflation and the Russia/Ukraine conflict. Some markets are also at risk of contraction as the economic landscape puts pressure on smaller suppliers, with acquisitions becoming increasingly common. The subsidiary continues to face challenges regarding the supply of certain chemicals that are essential for its water treatment processes. Much of its capital delivery programme and field activity in its Central region is outsourced to third parties. Existing contractors could have limited capacity to take on additional work due to the volume of large-scale infrastructure projects in and around some of its operational areas.</p> <p>Link to our customer outcomes:</p> 	<p>Mitigation</p> <p>The subsidiary seeks to ensure that its relationship with critical suppliers is secured under long-term agreements, where appropriate. For key activities, the subsidiary may retain more than one supplier to mitigate the risk of supplier failure and frequently qualify multiple suppliers to ensure supply continuity. The subsidiary also undertakes significant due diligence in the selection and ongoing management of suppliers through audit, inspection and verification of performance. The approach has been tested during the recent turbulence in the wider macro-economic climate and other socio-economic upheaval. It has proved resilient with no adverse impact on company objectives.</p> <p>The subsidiary continues to work with other companies in the industry to address the short-term and long-term challenges associated with supply of water treatment chemicals in the UK.</p>

Daiwater Investment Limited


Strategic report for the year ended 31 March 2023 (continued)

6 – The subsidiary could cause damage to the environment during its business activities	
<p>Risk</p> <p>There is a risk that, while operating its business, an incident occurs that inadvertently causes damage to the environment. Such an incident could cause pollution or other environmental damage, impact our EPA scores and cause financial and reputational impacts.</p> <p>Link to our customer outcomes: </p>	<p>Mitigation</p> <p>The subsidiary’s environmental ambition is to leave the environment in a sustainable and measurably improved state. The subsidiary is committed to protection of the environment, prevention of pollution and compliance with environmental legislation, regulations and other requirements that are applicable to us.</p> <p>To deliver on its commitment, the subsidiary has set itself a range of objectives to protect and enhance the environment, which include being certified to ISO 9001 (Quality) and ISO 14001 (Environmental) management systems and always striving for continuous improvement in its processes, systems and activities, minimising the waste it produces and the energy it consumes. The subsidiary works with farmers and communities to control the risk of environmental pollution from third-party activities.</p> <p>The subsidiary has a number of other environmental control systems and processes that include landholdings management plans, catchment management programme, drinking water safety plans, its compliance risk index (CRI) programme, its carbon reduction strategy and biodiversity programme.</p>
7 – Climate change and other environmental factors could negatively impact the subsidiary’s business operations	
<p>Risk</p> <p>The subsidiary is exposed to the possibility of damage to its landholdings, assets and ability to supply wholesome water caused by emerging global issues such as climate change, ecosystem decline, nearby land-use change (e.g. development or agricultural practices), carbon climate and third-party pollution events. Any of these could lead to increased operational costs, damage to its reputation, prosecution, loss of customer trust and/or operational disruption.</p> <p>Link to our customer outcomes: </p>	<p>Mitigation</p> <p>The subsidiary has identified six key climate change risks that without intervention pose an unacceptable risk to our business. The subsidiary’s Climate Change Adaptation Report sets out how it is mitigating and adapting to these risks. In its draft Water Resources Management Plan 2024 the subsidiary has included an assessment of the impact of climate change on its supply-demand balance. This was evaluated using a common approach adopted across the WRSE region to ensure the subsidiary can meet future needs. The subsidiary reviews and responds to planning applications where these could pose a potential risk to its assets and are working with landowners and farmers to improve soil health and water quality through its Catchment Management programme. The subsidiary’s INNS Out scheme is supporting its community to tackle invasive non-native species in its supply area, to help reduce the risk to its landholdings and the wider catchment.</p>


Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

8 – The subsidiary may fail to implement the cultural and operational transformation of its business necessary to deliver its business ambitions


<p>Risk</p> <p>There is a risk that the changes to the subsidiary’s organisational structure and business processes are insufficient to deliver its business ambitions. The subsidiary has made several performance commitments, which, if not met, may result in it incurring financial penalties and suffering reputational damage in the eyes of its regulators and other stakeholders. In addition, the subsidiary must implement the investment programme set out in its business plan. Failure to do so may lead to the imposition of financial penalties or other enforcement action.</p> <p>Link to our customer outcomes:</p> 	<p>Mitigation</p> <p>The subsidiary is in the midst of a cultural transformation programme to ensure, amongst other things, that it has a culture where its people are comfortable and embrace the significant changes necessary to make the required changes to deliver our Journey to 2025.</p> <p>The subsidiary has implemented a company-wide business excellence programme, utilising Lean/Six Sigma to drive a culture of continuous improvement of all business processes.</p> <p>The subsidiary has a well-established and rigorous project methodology in place to govern how it delivers its programmes and projects. The subsidiary’s Investment Committee reviews all proposed projects before initiation and monitors their delivery to ensure successful outcomes. New projects are approved by reference to available finances, people and other resources as appropriate.</p>
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9 – A significant disruptive event could impact the subsidiary’s ability to deliver normal business activities


<p>Risk</p> <p>The subsidiary’s ability to effectively and efficiently deliver the services that its customers expect could be significantly impacted by an extreme disruptive event, such as catastrophic loss of assets, extreme weather events beyond its current capacity to manage, terrorist attack or extended periods of pandemic or war.</p> <p>Link to our customer outcomes:</p> 	<p>Mitigation</p> <p>The subsidiary maintains an emergency response team to deal with the various issues that put the company or its customers at risk. These high-level procedures are maintained and reviewed on a regular basis. Each event, is subject to a learning review and long-term resilience plans are updated through the outcome of these learning sessions. These improvements are proposed to the investment teams for improvement or corrective actions that add to the company resilience.</p> <p>Business continuity planning is based on the guidance of ISO 22301:2019 and our emergency preparedness is assessed as part of our ISO 9001:2015 certification for assurance purposes. Affinity Water maintains a 24-hour rota to ensure emergency management is available should an event occur.</p> <p>Affinity Water maintains a close working relationship with the relevant local resilience forums (LRFs) organised through local government authorities to meet the requirements of the Civil Contingencies Act (CCA) 2004 and Security and Emergency Measures Direction (SEMD) 2022.</p> <p>Affinity Water regularly engages with Water UK on risks and has representation on the National Incident Management team (NIM) for dealing with tactical responses to national or regional issues, involving DEFRA and other government departments or agencies, and on the Platinum Incident Management team (PIM) for implementing agreed industry strategies in our organisation.</p>
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Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)






<p>10 – The health of the subsidiary’s assets may deteriorate such that water supply or quality is compromised</p>	
<p>Risk</p> <p>The health of the subsidiary’s assets is critical in facilitating the ongoing supply of sufficient quantities of high quality water to its customers and ensuring the operational resilience of the business. The health of its assets is also important in ensuring that they can be operated safely by its employees.</p> <p>Link to our customer outcomes:</p> <p>  </p>	<p>Mitigation</p> <p>The maintenance of the subsidiary’s existing assets to maintain service to customers is funded from the base capital maintenance element of its regulatory settlement; for 2022/23 this was just over £100 million. Unlike some other areas, the subsidiary has autonomy to decide how to allocate funds to best deliver its performance commitments. The subsidiary uses a ‘risk and value’ based approach to inform its decision making, which enables us to prioritise investment to those areas that most need it.</p> <p>This calendar year, the subsidiary is very proud to have delivered one of the best Compliance Risk Index (CRI) scores in the industry – a testament to how the subsidiary has prioritised and delivered water quality-related investments. In support of this, the subsidiary is working on enhancing the accuracy and completeness of its data and the suite of asset health metrics it uses to measure risk. The subsidiary has recently moved its below ground (infrastructure) assets onto the same risk management process as its above ground (non-infrastructure) assets, so it now has a single view of its emerging asset risks in one place.</p>

Regulatory risks

<p>11 – Changes could occur in the regulatory framework, or social or political climate, which could have significant effects on the subsidiary’s operational or financial performance</p>	
<p>Risk</p> <p>Changes to the regulatory framework by Ofwat or the government may have an adverse effect on the subsidiary’s operational or financial performance. The subsidiary is also exposed to risks arising from the general social and political climate, for example, debate around the merits of the current water ownership model, political pressure to restrict price increases, the investment needed by wastewater companies in combined sewer outfalls, and other issues, such as the adequacy of its WRMP and some objections to compulsory water metering. These pressures may lead to a reduction in revenue or have a reputational impact. Nationalisation has fallen down the political agenda, but political risk remains high due to continued scrutiny of the industry.</p> <p>Link to our customer outcomes:</p> <p>  </p>	<p>Mitigation</p> <p>The subsidiary continues to contribute fully to consultations with its regulators and seek to ensure its voice is heard on emerging changes through strong relationships with all its stakeholders.</p> <p>The subsidiary continues to engage with its stakeholders and their representatives to understand and respond to their issues and concerns. The subsidiary regularly engages with stakeholders across the political spectrum to understand and mitigate political risk.</p>

Daiwater Investment Limited


Strategic report for the year ended 31 March 2023 (continued)

12 – The subsidiary may fail to comply with laws and obligations under its instrument of appointment legal, compliance or business obligations	
<p>Risk</p> <p>We need to ensure that the subsidiary’s activities and outputs comply with licence conditions or statutory requirements arising from its appointment, as well as all other applicable laws and standards. Failure to do so may result in an enforcement order, a fine up to 10% of appointed turnover or termination of our appointment and special administration.</p> <p>Link to our customer outcomes:</p> 	<p>Mitigation</p> <p>Priority legal requirements, as set out in the subsidiary’s Licence Conditions and key legislation such as the Water Industry Act 1991, are captured in our Legal Obligations Register which has been introduced in 2023. This register provides a focus on key legal and regulatory obligations and will support future compliance returns, with legal and regulatory focus adapting as risk and circumstances require.</p> <p>The new register provides a reference point and sets clearer accountabilities for high level compliance. It requires directors to provide a statement of compliance that includes all relevant procedures and controls, or otherwise record any risk of non-compliance and provide mitigation and/or an action plan to address that potential non-compliance.</p> <p>All remaining legal or compliance risks will be managed through the application of regular internal reviews, standard operating procedures, training programmes and a risk reporting process where it is appropriate to do so.</p> <p>The subsidiary continues to operate its abstraction, treatment and supply activities to environmental standard ISO 14001 and has adopted the principles of other relevant management systems and standards. The subsidiary’s compliance programme is designed to ensure that:</p> <ul style="list-style-type: none"> • All employees are adequately educated on the legislation and regulations particularly relevant to their specific job roles; and • Appropriate assurance activities are in operation to provide positive evidence of compliance
13 – Failure to achieve a satisfactory outcome from the price review PR24	
<p>Risk</p> <p>The price review process sets the revenue, allowed investment and required performance for the next five-year period – in this case 2025–30. The review includes all aspects of the regulated business and a failure to adequately plan and resource the process could lead to a poor outcome for Affinity Water. The impacts would include insufficient investment allowed in order to meet customer expectations, our obligations and required performance levels.</p> <p>Link to our customer outcomes:</p>    	<p>Mitigation</p> <p>The subsidiary has resourced our PR24 team; planning for the business plan submission in October 2023 is well under way. The subsidiary is fully engaged with Ofwat through the various working groups, consultations and discussion papers that they have issued, and responded to the draft methodology in Autumn 2022. The subsidiary has developed its plans based on its customers’ priorities and will consult with customers on its draft plans in Spring 2023. The subsidiary continues to focus on performance within the current period to ensure it is in the best possible position both to develop and submit its business plan, and also to transition into the next AMP in April 2025.</p>

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Financial risks

14 – The subsidiary could fail to maintain or renew appropriate financing for its business activities	
Risk <p>The subsidiary's business has an ongoing liquidity requirement, driven by the operational costs of the business and its substantial capital investment programme. This results in liquidity risk if the subsidiary is unable to meet its cash flow requirements as and when they fall due. The subsidiary is subject to several covenants in relation to its borrowings. If a covenant is breached, this could lead to a default with any outstanding borrowings becoming immediately repayable. This could also impact the subsidiary's ability to raise funds on sufficiently favourable terms in the future.</p> <p>Link to our customer outcomes:</p> 	Mitigation <p>The subsidiary has undrawn revolving loan facilities, cash balances and standby loan facilities to meet its forecast cash flow needs. The subsidiary's treasury policy requires it to maintain a minimum level of liquidity capable of covering at least 12 months of forecast cash flow requirements. Longer-term financing needs are sourced from the private and public bond markets. As at 31 March 2023, the subsidiary has cash balances of £135.6 million. The subsidiary had £14.2 million of debt maturing in AMP7 and a spread of maturity beyond this. The subsidiary's next major refinancing exercise is scheduled for July 2026 when its £250 million fixed rate bond matures.</p> <p>The subsidiary's policy is to maintain a diverse portfolio of counterparties through which it can access liquidity at all times. This ensures it is not reliant on any single treasury counterparty.</p> <p>The subsidiary has a regular monitoring and certification process of the financial covenants within its Whole Business Securitisation (WBS) documentation. This covers information, financial and general covenants. The subsidiary's treasury policy requires that financial covenants, which include gearing and interest cover ratios, are monitored and reported to the Board on a regular basis. The subsidiary continues to maintain investment grade credit ratings with credit rating agencies.</p>

Daiwater Investment Limited





Strategic report for the year ended 31 March 2023 (continued)

15 – Macro-economic factors (interest rate, inflation and tax risks) could have a material adverse effect on the subsidiary’s financial performance	
<p>Risk</p> <p>Energy costs are a significant part of the subsidiary’s cost base and are subject to market price movements. Since mid-2021, the price of energy in the spot and forward market has increased significantly, which has increased the subsidiary’s costs.</p> <p>Movements in interest rates can result in an increase in the cost of its debt both now and in the future.</p> <p>The subsidiary’s wholesale revenues in a given financial year are explicitly linked to the CPIH published the previous November.</p> <p>An inability to control the subsidiary’s cost inflation on the same basis would lead to a reduction in the company’s profitability. The RCV is also linked to inflation and nominal returns are therefore likely to be further reduced in a low inflation environment.</p> <p>The subsidiary operates a pension plan providing defined benefits based on final pensionable salary. The assets and liabilities within the plan depend on several external factors outside its control, including performance of equity markets, interest rates and future inflation, which may increase the cost of its cash contributions.</p> <p>Customer debt and affordability remain key areas of focus for our business. A downturn in the economy or a reduction in consumer income (real terms) may lead to an increase in unpaid water customer bills. The subsidiary is not permitted to disconnect water supplies to household and certain other types of premises in the event of non-payment, resulting in loss of revenue and increased cost of collection.</p> <p>Link to our customer outcomes:</p> 	<p>Mitigation</p> <p>Energy price fluctuations are mitigated in two ways: firstly, by implementing efficiency programmes to reduce the amount of energy the subsidiary uses. Secondly, by developing self-generating assets (solar) to reduce the subsidiary’s reliance on grid imported energy. The subsidiary has already energised its first solar arrays and aims to have c.10% of its annual energy requirement from solar by 2025.</p> <p>The subsidiary purchases energy in the forward market to achieve cost certainty and reduce the likelihood of needing to purchase during highly volatile periods. The subsidiary has now purchased 100% of its energy requirement until 31 March 2025. Interest rate risk is primarily managed by using a mixture of fixed-rate and inflation linked borrowings, and approved hedging instruments (refer to note A4 to the financial statements for further information). The subsidiary has a financial covenant within its WBS documentation stipulating that at least 85% of its outstanding debt is hedged against movements in interest rates. Interest rate risk is monitored and reported on a regular basis to the Board.</p> <p>Inflation risk in the subsidiary’s costs is managed through undertaking a robust and challenging budgeting process to ensure costs are clearly understood and subsequently controlled during the financial year. The subsidiary also uses inflation-linked debt to ensure a proportion of its interest costs are linked to inflation and, therefore, offsets an element of the movement in revenue and RCV that results from changes in inflation. The subsidiary has inflation-linked swaps with a notional value of £250 million (CPI) and £210 million (RPI). The proportion of debt linked to inflation is now 86.0% (2022: 80.8%).</p> <p>The defined benefit pension plan has been closed to new members since September 2004, and the assets of the plan are held separately from those of the company. The plan is in surplus on an accounting basis (refer to notes 10 and A5 to the financial statements) and the latest actuarial valuation of the defined benefit section of the Affinity Water Pension Plan (AWPP) as at 31 December 2020, determined by an independent qualified actuary, concluded that the pension plan was 96% funded on a self-sufficiency basis. To eliminate the funding shortfall identified, as well as funding the future cost of benefits being accrued within the plan, the group 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. This was formalised in a new schedule of contributions effective from July 2021. 91.5% of the interest rate and inflation risk associated with the plan’s liabilities are hedged by the plan’s assets through liability and cash flow driven investment.</p> <p>The subsidiary has processes and teams dedicated to the efficient collection of customer debt, and outsources to a number of debt collection agencies when the recovery of debt has been unsuccessful. For those customers who struggle to pay their bill, the subsidiary has payment arrangements that are as flexible as possible, and it encourages customers who find themselves in difficulty to contact it as early as possible. The subsidiary also has a social tariff (LIFT) to help support customers who are least able to pay their bills.</p>

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Key

-  Supplying high-quality water you can trust
-  Minimising disruption to you and your community
-  Providing a great service that you value
-  Making sure you have enough water, whilst leaving more water in the environment

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Operational performance

The group has aligned its operational KPIs to its key performance commitments in response to customer expectations. We want customers and stakeholders to be able to assess our track record and hold us to account. The group's principal trading subsidiary is required to report its performance against targets set by Ofwat, the DWI and Defra. These targets include the performance commitments made in its AMP7 Business Plan. The subsidiary's performance in relation to these targets for 2022/23 is analysed in the tables below. For more information on the subsidiary's performance for 2022/23 in relation to all the performance commitments made in its AMP7 Business Plan refer to its own regulatory Annual Performance Report.

Performance key:



increased






decreased - stable



performance met






performance not met

KPI: Water quality	
CRI (Score)	
Actual: 1.092 Target: 2.0 	The Compliance Risk Index (CRI) is a measure to inform the risk arising from treated water compliance failures. Our CRI score, the measure used by the Drinking Water Inspectorate ('DWI') to assess a water company's performance with regards to water quality, was 1.092 for 2022. This was well within the deadband of 2 for our performance commitment and was one of the leading scores across the industry in 2022.
KPI: Leakage	
Average annual water leakage from our network (MI/d)	
Actual: 15.8% (since base year) Target: 14.0% 	This measure is reported as a percentage reduction in a three-year average of leakage against a baseline level of 2019/20. We reduced leakage by 15.8% in 2022/23, surpassing our 14% target.
KPI: PCC	
Average water use (l/p/d)	
Actual: 4.3% increase on a three-year average basis (160.6 l/p/d) Target: 7.3% reduction 	During 2022/23, the subsidiary recorded PCC of 160.6 l/p/d, which is an increase from 159.2 l/p/d recorded in 2021/22. However, we did not achieve the targeted reduction of 7.3% in the three-year average from the 2019/20 baseline. PCC is a measure of water usage in the home. Our three-year average is heavily influenced by the unprecedented demand for water in the home seen in 2020/21. We saw a high-level demand over the summer and were unfortunately still seeing the impact of Covid. Water demand has not returned to pre-pandemic levels, but we remain committed to reducing PCC by the end of AMP. We have continued our water saving initiatives such as our flagship SOS 'Save Our Streams' campaign, home water efficiency checks and innovation projects targeted to water use reduction.

Strategic report for the year ended 31 March 2023 (continued)




Operational performance (continued)

KPI: C-Mex (Score)	
Actual: 14th Target: mid table 	Customer Measure of Experience (C-Mex) is a mechanism to incentivise water companies to provide an excellent customer experience for residential customers, across both the retail and wholesale parts of the value chain. C-MeX is based on a league table comparison of performance by the other 17 water companies in England and Wales.
KPI: D-Mex (Score)	
Actual: 10th Target: mid table 	<p>Developer Measure of Experience (D-MeX) is the measure of levels of service in the developer services area of activity. The index score is made up of both a qualitative and a quantitative element.</p> <p>At the halfway mark for D-MeX, we are currently 10th in the industry league table. For the first nine months of this financial year, the subsidiary achieved 100% compliance against the quantitative element of our D-MeX score. Qualitative scoring for quarter 1 was promising but we then saw a drop in quarter 2 performance.</p> <p>Development Experience have completed a restructure to ensure we are set up to provide our customers with fantastic customer service, as well as working within agreed timescales. We are anticipating seeing the benefits of our restructure in quarter 3 qualitative survey results.</p> <p>The subsidiary is now working on streamlining and improving our processes, so we are about to efficiently meet the needs of our customers and help us achieve our D-MeX goals.</p> <p>Our internal qualitative scoring is tracking very well, and the subsidiary building our strategic to get more real time insight into how we are performing against our customer needs.</p>
KPI: Mains repairs (due to bursts) (Number per 1,000km mains)	
Actual: 169.6 Target: 146.5 	Performance in the year was 169.6 repairs per 1,000km of mains on a target of no more than 146.5 in the year (2021/22: 100.2). Weather is a strong contributing factor in the number of mains repairs needed in a year. The subsidiary experienced an exceptionally hot summer in 2022 with a significant freeze/ thaw event in winter. Figures cannot be compared directly to the previous year's without taking this into account.

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)



Operational performance (continued)

KPI: Water Supply Interruptions > 3 hours (Average minutes per property, water supply interruption)	
Actual: 00:12:53 Target: 00:05:45 	Our overall performance across the year was very strong. We outperformed our monthly target ten out of 12 months. Unfortunately, due to the significant weather events we experienced in the year (Jul-23 hot weather and Dec-23 freeze/thaw), we have failed our performance commitment. We added over ten minutes to the register for these two events (2mins in Jul-23 and 8min in Dec-23). Underlying performance was very strong for the other ten months.
KPI: Properties at risk of low pressure (Number per 10,000 properties)	
Actual: 150.93 Target: 1.381 	The low-pressure KPI definition is properties at risk of receiving low pressure, per 10,000 properties, for which we receive a financial penalty if we fail to achieve the regulatory target. Our performance against the target for year 3 is 150.93 against the target of 1.381. We also have a second performance commitment for low pressure which reflects the average time that a property in our supply area receives pressure or flow below the reference level. Our annual performance against this target is 2.33 hours against a target of 10 hours. It is interesting to note that while we failed to achieve one low pressure measure, we simultaneously outperformed the other. We believe that the 'average property time' measure best represents the overall customer experience with regards to low pressure. There is no doubt that this financial year has been challenging. Record-breaking hot weather in the summer, the freeze/thaw event in December, and unplanned strategic operational issues have all impacted on customer's pressures in ways that have been difficult to mitigate. We have more than 1,100 telemetered pressure monitoring devices installed at critical points across our network, so have a very good understanding and record of mains pressures. The basis of the common reporting guidance for properties at risk of receiving low pressure is now more than 30 years old, and dates to when data and understanding of mains pressures was very limited. Given this, and the number of pressure monitoring points that we now have, it is unlikely we will ever be able to meet the prescribed target for this measure.
KPI: Unplanned interruptions to supply over 12 hours (Number of properties)	
Actual: 6,070 Target: 320 or less 	Our overall performance across the year was very strong. We outperformed our monthly target ten out of 12 months. Unfortunately, due to the significant weather events we experienced in the year (Jul-23 hot weather and Dec-23 freeze/thaw), we have failed our performance commitment. We added over 6,000 properties to the register for these two events. Underlying performance was very strong for the other ten months.

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Financial performance

KPI: Gearing (Ratio of net debt to RCV, %)	
Actual: 73.4% Internal threshold: 80.0% 	The subsidiary's net debt as at 31 March 2023 was £1.257.7m, an increase of £177.9m since last year (2022: £1,079.8m). This increase reflects a net cash outflow of £56.8 million, primarily driven by capital expenditure on our network. In addition, our index linked bonds increase by prevailing RPI and CPI. This non-cash accretion is designed to match growth in nominal RCV and is included within net debt Our gearing is higher than some of our peers in the water industry, however this is only one aspect of our financial resilience. Our gearing of 73.4% is below our internal maximum of 80% of RCV and materially below our trigger level of 90.0%. Our financial policies and capital structure align with our target credit ratings of A3/BBB+/BBB+ for our Class A Bonds with Moody's, Standard & Poor's, and Fitch.
KPI: Cash flow (Net cash flow before tax and financing)	
Actual: -£22.9m outflow Target: -£16.1m outflow 	The subsidiary's net cash flow before tax and financing for the year was a £22.9m outflow, being a £6.8m increase on last year (2022: £16.1m outflow). The increase in the outflow is primarily due to higher net investment in fixed assets in the current financial year in line with our 2020–2025 plan. Cash generated from operations was also lower than in the prior year, with lower operating profits being partially offset by favourable movements in working capital. Our KPI linked to remuneration in the current year relates to totex and working capital within the regulated business, and cash generated from operations from the non-regulated business. Neither of these targets were met, as disclosed in the Remuneration report.

Section 172(1) statement

Daiwater Investment Limited

The principal trading subsidiary Affinity Water Limited accounts for the vast majority of the group; the majority of the directors who sit on the Board of Daiwater Investment Limited sit on the Board of Affinity Water Limited and the day-to-day operation of the group is predominantly managed by employees of Affinity Water Limited. Due to this relationship, the group's values are highly integrated with that of Affinity Water Limited and therefore the statements below relating to Affinity Water Limited should be read on behalf of the group. References to company in the statement below refer to Affinity Water Limited.

Our stakeholders

The group's responsible business approach is the way it does business. It is centred on issues which are of importance to our customers and stakeholders and to the responsible delivery of our business plans. The group has had discussions with stakeholders across all areas of its business to better understand what matters most to them and how it can further involve them in its decision making. The group focused on the following four areas: the environment, supply and demand, water efficiency and vulnerability with the aim of gathering information to inform its current and future strategy.

In the table on the next page, we present a description of the group's and the Board's engagement activities with each key stakeholder group. The information obtained through these engagement activities enables the Board to weigh up all relevant factors when deciding on a course of action that best leads to the long-term success of the group. This can sometimes mean that certain stakeholders are adversely affected, as the group seeks to operate in an ethical and responsible manner in relation to all our stakeholders.

The Board considers, both individually and together, that it has acted in the way it considers, in good faith, would be most likely to promote the success of the group for the benefit of its members and as a whole having regard to its stakeholders and the following matters set out in section 172(1) (a-f) of the Companies Act 2006:

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Our stakeholders (continued)

- a. the likely consequences of any decision in the long term;
- b. the interests of the group's employees;
- c. the need to foster the group's business relationships with suppliers, customers and others;
- d. the impact of the group's operations on the community and the environment;
- e. the desirability of the group maintaining a reputation for high standards of business conduct; and
- f. the need to act fairly between members of the group.

This statement explains how the Board satisfies itself that relationships with each key stakeholder group are managed effectively and that there is sufficient visibility of relevant stakeholder engagement activities in the boardroom to inform decision-making and delivery of strategy.

The Board's approach to section 172(1) and decision making

It is the responsibility of the Chair to enable discussions at Board meetings that lead to decisions being made which are sufficiently informed by section 172 factors. Board minutes record decisions made, and actions agreed in the context of these factors.

The Board's role in stakeholder engagement is to:

- ensure that our purpose, strategy and culture are set in the light of views actively sought from relevant stakeholders;
- set an expectation that all key decisions made take into consideration the views of relevant stakeholders;
- require executive directors and other senior managers to engage with relevant stakeholders in a way that ensures views are understood and taken into consideration when making key decisions;
- encourage executive directors and other senior managers to evolve stakeholder engagement in a way that meets all statutory and regulatory requirements but also embraces the principles on which these are based; and
- undertake direct stakeholder engagement that complements day-to-day stakeholder engagement by management.

In 2020/21, each Board Committee's terms of reference were reviewed by the Board and updated to ensure that consideration of section 172 factors and Ofwat's 2019 Board leadership, transparency and governance principles were appropriately addressed. Directors are reminded of the section 172 requirements at the start of every Board meeting and undertook a training session delivered by external advisors on their responsibilities. During 2022/23, the Board's Schedule of Reserved Matters were reviewed and approved. These can be accessed on our website at <https://www.affinitywater.co.uk/corporate/about/governance-assurance>

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) statement (continued)

The Board's approach to section 172(1) and decision making (continued)

The group's approach to stakeholder engagement is:



The Board undertook a review of its stakeholder engagement during the year and has taken steps to adopt a risk-based approach. Armed with the baseline perception position and policy priorities, a strategic stakeholder engagement plan will be developed based on a mapping exercise and identification of priority stakeholders to focus activity and maximise effective engagement to fulfil objectives within the plan.

We have identified key stakeholders and, using a power and influence model, mapped the stakeholders in terms of our impact on them, and their influence on the company.

Horizon scanning will be used to identify the key trends and emerging issues and assign a priority based on impact and influence. Full horizon scans will be conducted at regular intervals throughout the year to ensure we can adapt our strategic approach to stakeholder engagement as issues, risks and priorities can change quickly. We will use media monitoring, political monitoring, and social listening alongside internal workshops across the business to identify emerging issues for horizon scanning activity and help to define objectives for engagement. We will conduct an annual in-depth horizon scan with regular reviews throughout the year, which will be reported to the Board in the monthly CEO reports and will help the Board effectively manage stakeholder engagement.

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) in action

In the table below, we present a description of the group's and the Board's role in engagement activities with each key stakeholder group.

Customers <i>Current and future customers, including household and non-household customers, and market participants such as retailers and self-lay providers, developers and NAVs</i>	Communities <i>Communities, non-governmental organisations and civil society, especially environmental organisations and campaigners</i>
Why engagement is important <i>Customers rely on water as an essential service and are at the heart of our business model. We aim to be a positive contributor to, and able to earn fair returns from, a reliable service that is trusted by and represents value for money for customers. Transparent conversations and engagement with the Independent Challenge Group ('ICG'), formerly the Customer Challenge Group ('CCG') will support delivery of our purpose and environmental ambitions</i>	Why engagement is important <i>These groups bring distinctive perspectives and influence on key environmental and social issues on behalf of customers and the public. Engagement will result in us being a progressive, well-regarded company that delivers its purpose and with which communities and civil society want to work in pursuit of common goals</i>
How the company engages <ul style="list-style-type: none"> • <i>Daily contact with customers</i> • <i>Customer research programme</i> • <i>Public meetings</i> • <i>Our website</i> • <i>Media/social media</i> • <i>Through our ICG</i> 	How the company engages <ul style="list-style-type: none"> • <i>Stakeholder Assembly</i> • <i>Joint Forums</i> • <i>Public meetings</i> • <i>Consultation meetings for price review development</i> • <i>Catchment partnerships</i> • <i>Water resources monthly email updates</i> • <i>Volunteering days</i>
How the Board engages <i>Information reported to the Board:</i> <ul style="list-style-type: none"> • <i>The Board receives monthly performance summaries of our AMP7 performance commitments including leakage, PCC, C-MeX and D-MeX and supply interruptions, and other key metrics including customer satisfaction and written complaints</i> • <i>The Board received updates on the impact of customers as a result of the freeze thaw event in December 2022 and the impact of the event on our key performance commitments</i> • <i>The Board received updates on the Save Our Streams campaign and the drive to reduce per capita consumption following the hot weather period over the summer and our draft Drought Management Plan</i> • <i>The Board received updates on the refresh of the Customer Challenge Group, now formally known as the Independent Challenge Group, and reviewed and approved the updated Terms of Reference in September 2022</i> <i>Direct engagement mechanisms:</i> <ul style="list-style-type: none"> • <i>There is a clear reporting line to the CEO and accountability for arrangements regarding handling customer complaints</i> • <i>Chair of the ICG was regularly invited to Board meetings and attended the Board strategy day</i> • <i>Quarterly meeting with the ICG to discuss key performance metrics</i> • <i>Continued engagement with partnership groups to further support customers (Turn2us, CAB, Money Advice) with the ongoing cost of living crisis and customer bill increase for 2023/24</i> <i>Customer protection:</i> <i>The Board considers the group's policies around the protection of customer data through its review of the strategic risk register and our GDPR policy. Customers can access our Privacy Notice website which was made more engaging and user friendly in 2022/23</i>	How the Board engages <i>Information reported to the Board:</i> <ul style="list-style-type: none"> • <i>The Board received updates on the Water Resources Management Plan 2024 and viewed the findings of the stakeholder consultation held during the year</i> • <i>The Board received updates on rainfall and groundwater levels and the risk of having to introduce a Drought Management Plan such as a restrictions on hosepipe use</i> • <i>The Board reviewed the operational working plans to support the national mourning period and ensure operational resources were identified with quick response times if required</i> • <i>The Board receives monthly updates on community projects</i> <i>Direct engagement mechanisms:</i> <ul style="list-style-type: none"> • <i>Our Board-approved Community Engagement Strategy and activities are focused around three core areas:</i> <ul style="list-style-type: none"> ○ <i>Protecting rivers and habitats</i> ○ <i>Investing in science, technology, engineering and mathematics (STEM) and future skills</i> ○ <i>Developing community partnerships</i> <i>Throughout 2022/23, we continued to build on our social purpose and defining the programme of work that will help us meet the growing expectations of our stakeholders and add value to our communities</i> <ul style="list-style-type: none"> • <i>Board members attended key community events in 2022/23 including attending the Rickmansworth Canal festival with our Save our Streams exhibit to talk to invited stakeholders including local councillors and MPs, river groups, Chiltern's Conservation Board, Chiltern's Society, Canal and Rivers Trust and other NGOs</i> • <i>We have arranged several Affinity Water volunteering days with the Chiltern's Society to carry out river improvement works along the River Chess</i>

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) statement (continued)

Section 172(1) in action (continued)

Employees <i>The workforce, including both employees and the wider workforce</i>
Why engagement is important <i>Our success depends on the shared talents, skills and values of the people who work for our company, and our ability to attract and retain a talented and diverse future workforce</i> <i>Successful engagement will mean we are an inclusive employer that retains and attracts people with the talent and skills to achieve our business objectives and whose make-up is aligned with the diversity of the communities we serve</i>
How the company engages <ul style="list-style-type: none">• Senior leadership forums• Engagement “Tap in” surveys and regular pulse survey• Monthly one-to-one meetings and personal best check-ins four times a year• Regular podcasts from the CEO and a welcome to our new CEO• Culture Ambassador forums to gain feedback and progress culture development initiatives• Diversity and Inclusion Steering Group to drive a stronger agenda of inclusiveness• Designated Director for Employee Engagement reporting issues and progress to the Board• Internal communications and monthly team leader briefings communicated to all line managers• Company wide live events giving updates to employees from all areas of the business• Customer delivery roadshows to update front line operational teams on our performance and future plans• Redesigned new starter and training programme developed, with team leader and manager training• Mandatory e-learning sessions including Inclusion and Diversity training
How the Board engages <i>Information reported to the Board:</i> <ul style="list-style-type: none">• We have continued to drive cultural change across the business. Culture Ambassadors represent their departments and report on progress made. The Board received updates from engagement “tap in” surveys and pulse surveys conducted in the year, a focus of which was on diversity, inclusivity, health and wellbeing, and action plans were discussed by the Board. The Board approved a new Policy Statement on Culture & Employee Engagement• Information on productivity, attrition levels, learning participation, training and development plans, wellbeing and output from exit interviews is reported monthly to the Board• Whistleblowing incidents are reported to the Board. All incidents are taken extremely seriously and are thoroughly investigated, working with external reviewers if required• Details on the company’s Hybrid Working Policy and the return to office approach was reviewed <i>Direct engagement mechanisms:</i> <ul style="list-style-type: none">• Chris Newsome, Director of Employee Engagement was responsible for employee liaison in accordance with the Code, having taken over the role from Trevor Didcock in October 2022. The overriding purpose of the role is to ensure that the voice of the workforce is heard and considered at Board level. A key secondary purpose is to improve the transparency of Board activities, discussion and decision-making and in so doing improve alignment between the Board and the workforce. Chris is a member of our Equality, Diversity and Inclusion Committee, established to bring to life our commitment to build a more inclusive culture, allowing all members of our workforce to bring their true selves to work• All of our workforce are entitled to be trade union members. Our interim CFO was a member of the Joint Negotiation and Consultative Committee (‘JNCC’) during the year which, together with employee trade union representatives and other company nominated representatives, meets quarterly to consult on workforce practices and policies and negotiate workforce pay• Keith Haslett as joining CEO met employees across the business to thank them for their work and understand the issues on the ground and the new ways of working• A Safety Stand Down was held to launch the company “Don’t Walk By” campaign, to help us achieve our zero harm ambitions. Presentations were delivered by the Board <i>Workforce policies and practices:</i> <ul style="list-style-type: none">• Refer to the Governance Report for further detail on workforce policies and practice and workforce concerns, and details of what the Board is doing about gender equality and reducing our gender pay gap. The Board approved a new Code of Ethics, Culture and Employee Engagement Policy and our Equality, Diversity and Inclusion strategy during the year.

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) statement (continued)

Section 172(1) in action (continued)

<p>Shareholders <i>Owners of shares in the company</i></p>	<p>Regulators <i>Regulators, including Ofwat, MOSL, EA, DWI, Defra, HSE, Natural England, CCW and CCG/ICG.</i></p> <p><i>Government – central and local government and MPs, highways authorities, Highways England and TfL</i></p>
<p>Why engagement is important <i>Our shareholders have an important role to play and a direct interest in the strong and effective governance and stewardship of our business</i></p> <p><i>We aim to provide a reasonable long-term return on their investment</i></p>	<p>Why engagement is important <i>To ensure we maintain our licence to operate and that our actions are in accordance with the framework determined by the Government and regulators</i></p> <p><i>Engagement will ensure that we are a responsible company which delivers on its purpose</i></p>
<p>How the company engages</p> <ul style="list-style-type: none"> • <i>Board meetings attended by shareholders / nominated directors</i> • <i>Monthly financial and operational updates</i> • <i>Regular meetings and calls</i> • <i>Annual report and financial statements, which gives details of the performance, strategy, viability and company business model, approved by the Board</i> 	<p>How the company engages</p> <ul style="list-style-type: none"> • <i>Industry working groups including committees, panels and forums</i> • <i>Responding to consultations and requests for information</i> • <i>Ongoing dialogue on strategic planning and land disposals</i> • <i>Regular meetings and calls, including meetings with key MPs in our supply area</i>
<p>How the Board engages</p> <ul style="list-style-type: none"> • <i>We explain how the Board engages with our shareholders and involves them in decision-making in our publication: ‘Consulting with our shareholders’, approved by the Board in June 2020 to include the Ofwat 2019 principles, available on the governance pages of our website</i> • <i>In 2022/23 the Board engaged directly with shareholders in setting and approving budgets for 2023/24, discussing the principal trading subsidiary’s viability statement and results of stress testing on our financial covenants</i> • <i>The Board engaged with shareholders following the findings of an Independent Board Evaluation in May 2022, including discussing recommendations, Board composition and actions taken</i> 	<p>How the Board engages</p> <p><i>Information reported to the Board:</i></p> <ul style="list-style-type: none"> • <i>The Board receives monthly updates on regulatory and relevant political developments, and regulatory consultations and requests for additional information</i> • <i>The Board receives monthly updates on correspondence with regulators, including communications with Ofwat regarding our base and enhancement expenditure and plans for expenditure</i> • <i>Updates on the development of our PR24 plan following publication of the PR24 Final Methodology</i> <p><i>Direct engagement mechanisms:</i></p> <ul style="list-style-type: none"> • <i>The Board engaged with Ofwat during the year prior to the recruitment of the new CEO and CFO</i> • <i>The Board engaged with Ofwat during a visit to water treatment works at Iver to understand our plans for the future, WRMP, Water Industry National Environment Programme and PR24</i> • <i>The Board engaged with Ofwat consultations on PR24 draft methodology and Financial Resilience and provided Ofwat with updates on our leakage performance following the missed target in the prior year</i> • <i>Non-Executive and shareholder directors attended regular events with Ofwat, including prior to their appointment and following changes to the Board structure during the year</i> • <i>The Board received updates on proposals to submit to Ofwat for Innovation Competition funding, including the successful innovation award for the Water Neutrality project</i> • <i>The CEO had meetings with the EA, Ofwat and the DWI on operational events, risk assessments and the impact on ODIs and abstraction licences</i> • <i>Delivery Steering Group and monthly performance reviews to drive the achievement of performance commitments in AMP7</i> • <i>Throughout 2022/23 the CEO had meetings with Ofwat representatives on the rising energy costs, financial resilience and hedging for PR24</i> • <i>The Board attended forums held by the CCW</i>

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) statement (continued)

Section 172(1) in action (continued)

Environmental bodies	Providers of finance and credit rating agencies
<p>Why engagement is important <i>We need to manage the impact of taking water from sensitive habitats and to maintain flows in local rivers whilst also ensuring a continuous supply of high-quality water for customers in line with our purpose</i></p> <p><i>Successful engagement will mean we protect water sources and the quality of water supplied and minimise our impact on the environment</i></p>	<p>Why engagement is important <i>It is imperative that we maintain effective relationships and ongoing dialogues with our banks and credit rating agencies to ensure access to financial services as well as capital markets, particularly in the current economic climate. Successful engagement means we will be a responsible company that delivers reliable returns and is transparent in our reporting</i></p>
<p>How the company engages</p> <ul style="list-style-type: none"> • <i>Water Resources Management Plan ('WRMP')</i> • <i>Catchment management</i> • <i>River restoration</i> • <i>Company environmental policy to ensure we meet our purpose to provide high quality drinking water for our customers and take care of the environment</i> 	<p>How the company engages</p> <ul style="list-style-type: none"> • <i>Annual review meetings with credit rating agencies</i> • <i>Regular meetings and calls with banks</i> • <i>Financial reports</i> • <i>Engaged with banking groups and credit rating agencies on the ongoing cost of living crisis</i>
<p>How the Board engages Governance arrangements:</p> <ul style="list-style-type: none"> • <i>The Board is composed of individuals who have appropriate knowledge, skills, experience and background to take decisions informed by an awareness and understanding of environment-related threats and opportunities. Our shareholder directors are focused on environmental issues, as part of our shareholders' wider environmental, social and governance ('ESG') programmes and alignment to the UN's Sustainable Development Goals ('SDGs')</i> • <i>The Safety, Health, Environment and Drinking Water Quality ('SHEDWQ') Committee reviews and monitors, on behalf of the Board, environmental matters arising from our activities and operations, including monitoring performance against targets</i> • <i>Environmental and climate considerations are embedded into our principal risks and the management of these risks, in particular the principal risk 'We may become unable to meet our obligations to provide a sufficient supply of high-quality drinking water', which are monitored by the Board. A full review of risks was undertaken during the year</i> • <i>The Board receives monthly information on our performance in relation to key environmental metrics, including water quality, leakage, sustainable abstraction reductions, average water use and water available for use, to enable it to monitor the success of strategies implemented</i> <p>Climate change:</p> <ul style="list-style-type: none"> • <i>The Board considers climate change in two principal ways:</i> <ol style="list-style-type: none"> 1) <i>The potential impacts of climate change are addressed through long-term planning as part of the statutory WRMP (available on our website: affinitywater.co.uk/water-resources-plan). A Board sub-committee on the WRMP oversaw this work and was advised by external technical experts;</i> 2) <i>Affinity Water has worked closely with other water companies through the WRSE and WRE groups to draft and publish the first ever regional plan for water. Affinity Water's WRMP feeds into the regional plan. As such, a coordinated approach was taken to stakeholder and media engagement to align messaging and demonstrate the industry working together to plan for the future.</i> 3) <i>In 2022/23, we continued to work alongside other water companies and Water UK to develop a route map to reduce carbon emissions to net zero by 2030, an industry-wide target. The SHEDWQ attended a deep-dive session on carbon reduction plans in February 2023.</i> 4) <i>We continued to roll out the solar build programme, with the Board receiving updates on planned delivery, costs and benefits in the current energy market and further investment required.</i> 	<p>How the Board engages Information reported to the Board:</p> <ul style="list-style-type: none"> • <i>A treasury report is provided to the Board on a quarterly basis, which includes details of the company's covenants and gearing headroom, and financial results</i> <p>Direct engagement mechanisms:</p> <ul style="list-style-type: none"> • <i>The interim CFO, on behalf of the Board met with lenders and credit rating agencies during the year and discussed the negative outlook placed on the company by Standard & Poor's</i> • <i>The Board approved a 364 day extension of the revolving credit facilities</i> <p><i>Refer to note A4 of the statutory financial statements for further information on our risk management processes and the Board's role in these.</i></p>

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) statement (continued)

Section 172(1) in action (continued)

Supply chain
<p>Why engagement is important <i>We rely on our supply chain for delivery of operations and capital projects, and partners provide investment and support delivery as well as acting as a source of innovation and new ways of working.</i></p> <p><i>Successful engagement will mean we are a good company to work with, to partner and do business with, ensuring that we and our partners maximise the greatest mutual value in a Zero Harm environment and we can continue to operate in a post-Brexit working environment.</i></p>
<p>How the company engages</p> <ul style="list-style-type: none">• <i>Integration of contractors into our teams</i>• <i>Sharing of reporting and management systems for collaborative and shared learning</i>• <i>Quarterly forums with all our Maintenance and Repair and Traffic Management suppliers, to discuss 'lean' processes and improvements</i>• <i>Regular meetings and calls, including monthly performance meetings with our largest suppliers</i>
<p>How the Board engages <i>Board's involvement in the agreement of supplier terms:</i></p> <ul style="list-style-type: none">• <i>We have a standard set of purchase order terms and conditions and a Supply of Goods and Services Agreement published on our website: affinitywater.co.uk/policies, which is reviewed and amended (where necessary) by our Procurement and Legal teams who report to our Executive members of the Board</i>• <i>We have a Contracts Committee, which approves the award of material contracts</i>• <i>A subset of the wider Board was involved in formulating a strategy for contracting our key Maintenance and Repair suppliers for AMP7, including determining key principles, contract scopes and tender evaluation criteria. The Board monitors supplier spend on a monthly basis.</i>• <i>The Board considers the company's policies around compliance with the Modern Slavery Act and GDPR as they relate to suppliers through the approval of the company's Modern Slavery Statement and review of the appropriateness of mitigation detailed in the strategic risk register in relation to the principal risk: 'Availability, confidentiality or integrity of information or data could become compromised'</i>• <i>The Board receives information on a monthly basis on operational ODI performance and bi-annually on payment practice information to enable it to consider our performance and how it compares to industry peers</i>• <i>The SHEDWQ Committee also reviews and monitors, on behalf of the Board, safety and health matters arising from our activities and operations, including in relation to our supply chain</i>• <i>The Board considers the risk of supply chain failure through its consideration of the strategic risk register</i> <p><i>Direct engagement mechanisms:</i></p> <ul style="list-style-type: none">• <i>Executive directors attend meetings with key members of the supply chain based on a supplier strategy</i>

Priorities ahead

Following a review of direct engagement mechanisms, the Board identified the following priorities for the remainder of AMP7 and into AMP8. These form part of the Journey to 25, the plan approved by the Board to ensure delivery in AMP7 and setting the company up for success in AMP8.

- Deliver the best outcome for this financial year and setting ourselves for success
- Achieve our AMP7 plans and ambitions
- Ensure our plan for AMP8 is robust, credible and stretching with confidence in deliverability
- Ensure we are ready to step into AMP8 and transition seamlessly
- Achieve our AMP8 plans and ambitions

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) statement (continued)

Key decisions made in 2022/23

We set out below key decisions made in 2022/23 and the Board's consideration of section 172 factors in making these.

<p><i>Approved the recruitment of Keith Haslett as CEO</i></p>	<p>A key focus for the Committee since the interim appointment of Stuart Ledger has been the search and appointment process for a permanent CEO. The Committee engaged the services of independent search consultants RRA to evaluate, screen and identify suitable candidates and it led the internal process of assessment and recruitment of Keith Haslett against objective criteria, which protect against discrimination for those with protected characteristics within the meaning of the Equalities Act 2010.</p>
<p><i>Approved the recruitment of Martin Roughead as CFO</i></p>	<p>Upon the departure of the Interim CFO, Mike Thomas in August 2022 who was on a one-year fixed-term contract, Affinity Water Treasurer, Michael Blake, stepped up to fill the CFO position on an interim basis. Since then, the Committee led a robust recruitment process aided by Odgers to appoint Martin Roughead to fill the role of CFO on a permanent basis.</p> <p>For recruitment of both the CEO and CFO, the shareholders were actively engaged as part of the recruitment process as part of their role on the Nomination Committee and Board. RNS' to the LSE (available as a public record) were sent out to inform the markets and other interested stakeholders of the appointments. We also displayed news of the appointments on our Investor Relations (news) pages of our external website to inform our customers and interested stakeholders. All employees were made aware of the appointments through internal communications. Ofwat (the Regulator) was also made aware of the appointments in addition to the Traffic Commissioner.</p>
<p><i>Launch of draft Water Resources Management Plan and regional plans</i></p>	<p>Our Water Resources Management Plan aims to address a significant future shortfall in water resources in our supply area. Population growth, climate change and the demand for water are putting significant pressure on the local environment and water resources in the company's supply area.</p> <p>The group has worked closely with other water companies through the Water Resources South East and Water Resources East groups to draft and publish the first ever regional plan for water, with the company's draft Water Resources Management Plan feeding into the wider regional plan. As such, a coordinated approach was taken to stakeholder and media engagement to align messaging and demonstrate the industry working together to plan for the future. The launch of the plan gained significant media reach highlighting proposed strategic resource options, such as the company's Grand Union Canal Transfer. Two parliamentary events were also held, with company representatives, MPs and interested stakeholders in attendance.</p> <p>The Board received presentations on Executive and Board responsibilities, which included duties of directors under the Companies Act 2006 and the company's statutory duties under the Water Industry Act 1991. The Board also received presentations on the legal requirements of the Water Resources Management Plan Regulations 2007.</p> <p>The Board approved the submission of the draft Water Resources Management Plan to Defra prior to the consultation with stakeholders in November 2022.</p>

Daiwater Investment Limited

Strategic report for the year ended 31 March 2023 (continued)

Section 172(1) statement (continued)

Key decisions made in 2022/23 (continued)

<i>Approved the annual budget and ten-year base case cash flow forecast</i>	<p>The 2023/24 annual budget and ten-year base case cash flow forecast were approved by the Board following a comprehensive review of our strategic priorities and risks to our business in light of Ofwat's Final Determination for AMP7 and our plans to ensure business readiness for AMP8. The Board considered the company viability, stress testing and assumptions made in light of the ongoing energy and cost of living crisis. Our budget process took both a bottom-up approach, which engaged all cost centre managers in the business, and a top-down approach, which engaged our shareholders and considered Ofwat's Final Determination in light of shareholder objectives.</p> <p>The Board considers our plans challenging but that they will position the company well against our longer-term value creation vision whilst honouring our commitments to stakeholders.</p>
<i>Approved the 2023/24 workforce pay settlement</i>	<p>In 2022/23, the Board reviewed progress of pay negotiations with trade unions. The Board considered the importance of creating value for shareholders while balancing the need for investment in the workforce and the ongoing energy and cost of living crisis. Employees were consulted through their trade unions of which all employees are entitled to be a member. The Board concluded that it was in the best interests of the group to support the Chief Executive Officer's decision to approve the proposed pay increase of 7.5% in order to increase employee engagement, retention rates and productivity, leading to increased value creation.</p>

Approval of the strategic report

Approved by the Board and signed on its behalf:

Michael Osborne
Director
21 December 2023

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023

Introduction

The directors present their Annual Report and the audited consolidated Financial Statements of Daiwater Investment Limited ('the company') for the year ended 31 March 2023.

The company was incorporated on 24 April 2017 to acquire the Affinity Water group through the purchase of Affinity Water Acquisitions (Investments) Limited. This transaction completed on 19 May 2017.

The company is a limited liability company registered in England and Wales and it was the ultimate holding and controlling company of the Affinity Water group in the United Kingdom throughout the year. Details of the ownership of the company and the group structure are set out on the following pages and in note 27 of these financial statements. The address of the principal place of business is Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ.

The strategic report from pages 5 to 31 provides information relating to the group, its strategy and its results and financial position for the year ended 31 March 2023. Details of the risks and principal uncertainties facing the group are set out on pages 6 to 18.

Directors

The directors of the company who were in office during the year and up to the date of signing the financial statements except where noted, were as follows:

Jonathan Carter (appointed 4 October 2022)
Andrew Cox (appointed 15 November 2023)
Marissa Dardi (resigned 12 May 2023)
Jaroslava Korpanec (resigned 1 August 2022)

Michael Osborne
Angela Roshier (resigned 15 February 2023)
Roxana Tataru
Adam Waddington (appointed 12 May 2023)

Dividends and dividend policy

The company's dividend policy is to distribute all surplus cash (to the maximum extent permitted by applicable laws and any relevant requirement) subject to there being adequate provision for working capital, approved forecast expenditure and debt servicing (excluding any outstanding shareholder loans). All surplus cash is distributed first, by way of payment of interest on any outstanding shareholder loans and second, by way of interim or, as the case may be, final dividend on the shares in issue. The amount of the dividend is, therefore, subject to the dividend policy of Affinity Water Limited, the group's principal trading subsidiary, which is disclosed in its own Annual Report and Financial Statements for the year ended 31 March 2023 on its website: affinitywater.co.uk/library.

No dividends were paid in the year ended 31 March 2023 from the company. Dividends of £95,000 (2022: £91,000) were paid to non-controlling interests from group subsidiaries.

No final dividend is proposed (2022: £nil).

Significant events during the year

Details of the significant events relating to Affinity Water Limited, that occurred during the year are set out in the performance highlights, Chair's welcome, CEO's introduction and financial review section of its own Annual Report and Financial Statements for the year ended 31 March 2023 on its website: affinitywater.co.uk/library.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Ownership

On 19 May 2017, Affinity Water Acquisitions (Investments) Limited was acquired by a consortium comprising DIF, HICL Infrastructure Company Limited (advised by InfraRed Capital Partners Limited) and Allianz Capital Partners on behalf of the Allianz Group. As part of the transaction, the consortium also acquired Veolia Water UK Limited's 10% equity interest stake in the company. Subsequent to the initial acquisition, HICL Infrastructure Company Limited (advised by InfraRed Capital Partners Limited) sold down 3.4% of its interest to a small group of coinvestors, comprising UK local authority pension funds in June 2017. On 1 April 2019, HICL Infrastructure Company Limited transferred its investment portfolio, assets, and liabilities to HICL Infrastructure plc, a new listed UK registered investment trust, and shareholders of HICL Infrastructure Company Limited became shareholders of HICL Infrastructure plc. 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.

The consortium made its investment through Daiwater Investment Limited, which has been our UK holding company since 19 May 2017.

We consider the following entities to be our ultimate controllers, as they are in a position to exercise material influence over our policy and affairs:

- Allianz Infrastructure Holding I Pte. Limited
- DIF Management Holding BV
- DIF Management UK Limited
- HICL Infrastructure plc
- InfraRed Capital Partners (Management) LLP
- Sun Life Financial Inc.

These entities, have provided the group's principal trading subsidiary, Affinity Water Limited, with legally enforceable undertakings that they will:

- give Affinity Water Limited such information as may be necessary to enable it to comply with its obligations under the Water Industry Act 1991 and Instrument of Appointment;
- refrain from any action which would cause the Affinity Water Limited to breach any of its obligations under the Water Industry Act 1991 or the conditions of its Instrument of Appointment; and
- use their best endeavours to ensure that the Board of Affinity Water Limited maintains three independent non-executive directors, who shall be persons of standing with relevant experience and who shall collectively have connections with and knowledge of the areas for which the group's principal trading subsidiary is a water undertaker and an understanding of the interests of the group's customers and how these can be respected and protected.

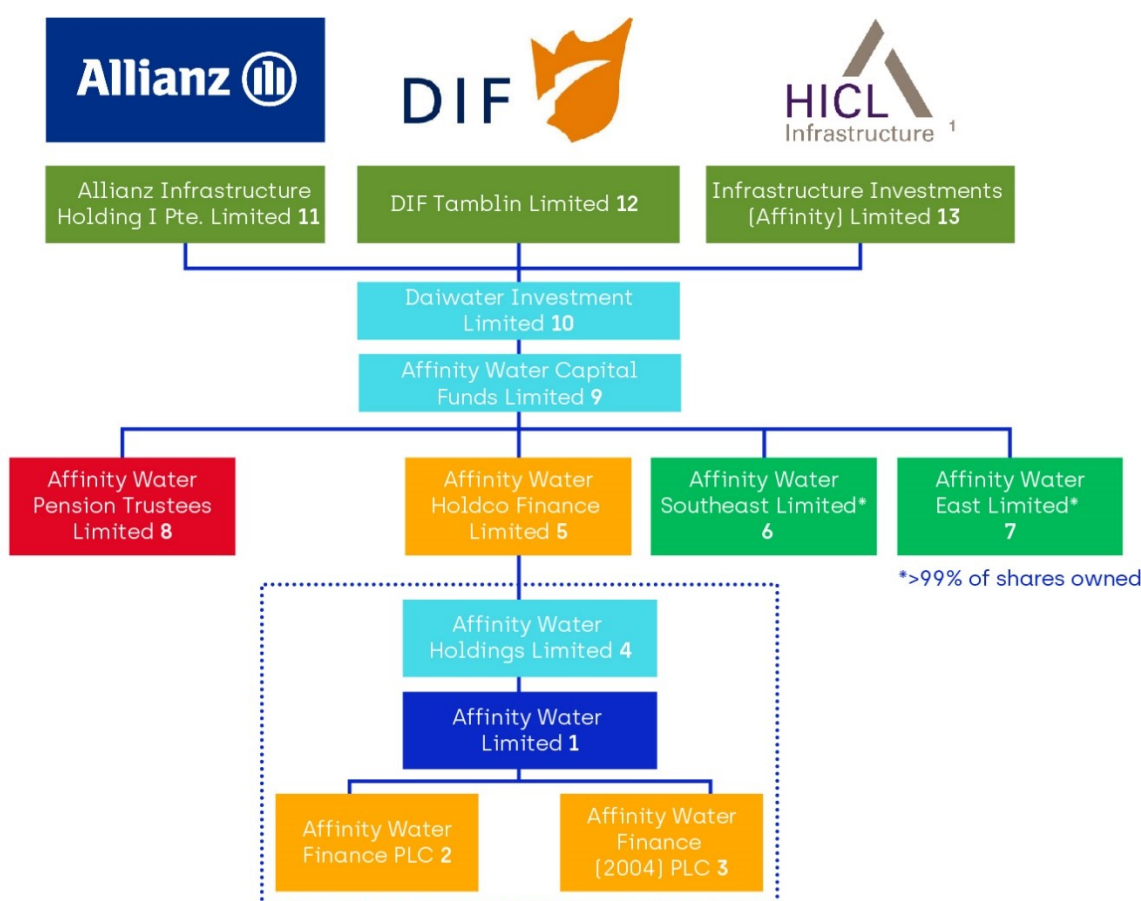
The Board is satisfied that these undertakings are being properly discharged and that Affinity Water Limited is able fully to meet its regulatory obligation to operate its appointed business as if it were substantially its sole business and were a separate listed company. Further, no issues have been identified at the group level which may materially impact on Affinity Water Limited during the year.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Ownership (continued)

The chart below shows the group structure, excluding dormant subsidiaries, as at 31 March 2023. Unless otherwise indicated, all companies are wholly owned by the parent company shown. The numbers listed alongside the companies within the group structure may be cross referenced to the table on pages 35 and 36.



Key

- Shareholder company
- Holding company
- Affinity Water Pension Plan Trustee
- Financing company
- Former regulated water company
- Regulated water company
- ⋯ Whole business securitisation ring fence

¹ HICL Infrastructure sold down 3.4% of its interest to a small group of co-investors, comprising UK local authority pension funds in June 2017

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Group structure

The following table provides further explanation of the group structure

Structure chart ref.	Company	Description	Place of registration
①	Affinity Water Limited	A water undertaker holding an appointment under the Water Industry Act 1991, supplying water to a population of around 3.86 million people in the South East of England. It is the principal trading company of the Group.	England and Wales
②	Affinity Water Finance PLC	A financing subsidiary of Affinity Water Limited established in 2018 to issue bonds under a Euro Medium Term Note (EMTN) programme. It lends monies raised from its bonds to Affinity Water Limited.	England and Wales
③	Affinity Water Finance (2004) PLC	A financing subsidiary of Affinity Water Limited established in 2004 to issue a bond. It lends monies raised from its bond to Affinity Water Limited.	England and Wales
④	Affinity Water Holdings Limited	Affinity Water Limited's immediate holding company. Its equity is provided as security to bondholders in the event of default.	England and Wales
⑤	Affinity Water Holdco Finance Limited	A financing subsidiary of Affinity Water Capital Funds Limited established in 2017. It lends monies raised to Affinity Water Capital Funds Limited.	England and Wales
⑥	Affinity Water Southeast Limited	A company which formerly held an Instrument of Appointment as water undertaker for the Dour community of Affinity Water Limited's water supply area. The appointment was transferred to Affinity Water Limited on 27 July 2012. The company is no longer trading but continues to honour income assurances made to minority shareholders on transfer of its water undertaking to Affinity Water Limited.	England and Wales
⑦	Affinity Water East Limited	A company which formerly held an Instrument of Appointment as water undertaker for the Brett community of Affinity Water Limited's water supply area. The appointment was transferred to Affinity Water Limited on 27 July 2012. The company is no longer trading but continues to honour income assurances made to minority shareholders on transfer of its water undertaking to Affinity Water Limited.	England and Wales
⑧	Affinity Water Pension Trustees Limited	The trustee company of the Affinity Water Pension Plan.	England and Wales
⑨	Affinity Water Capital Funds Limited	The original holding company for Veolia's regulated water businesses, which was acquired by the group in June 2012 through Affinity Water Acquisitions Limited, which provides management services to the company.	England and Wales
⑩	Daiwater Investment Limited	The ultimate holding company of the group in the United Kingdom, paying dividends to the acquisition consortium subsidiaries.	England and Wales

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Group structure (continued)

Structure chart reference	Company	Description	Place of registration
⑪	Allianz Infrastructure Holding I Pte. Limited	A company which holds indirectly Allianz Capital Partners' investment in the Group.	Singapore
⑫	DIF Tamblin Limited	A company established in 2017 to hold indirectly DIF's investment in the Group.	England and Wales
⑬	Infrastructure Investments (Affinity) Limited	A company established in 2017 to hold indirectly HICL Infrastructure plc's investment in the Group, together with the co-investment by certain local authority pension funds.	England and Wales

The following table provides explanation of the Group companies liquidated during the year.

Company	Description	Place of registration
Affinity Water Acquisitions Limited	The company, which bid for and acquired, Affinity Water Capital Funds Limited and its subsidiaries from Veolia Water UK Limited in 2012.	England and Wales
Affinity Water Acquisitions (Midco) Limited	The holding company of Affinity Water Acquisitions Limited.	England and Wales
Affinity Water Acquisitions (Holdco) Limited	The holding company of Affinity Water Acquisitions (Midco) Limited.	England and Wales
Affinity Water Acquisitions (Investments) Limited	The holding company of Affinity Water Acquisitions (Holdco) Limited. It was the ultimate holding company of the Group in the United Kingdom up until 19 May 2017, when it was acquired by Daiwater Investment Limited.	England and Wales
Affinity Water Shared Services Limited	A company which provided administrative and technical services solely to Affinity Water Limited until 31 March 2015. Its employees were transferred over to Affinity Water Limited on that date. Since the transfer, the company has ceased trading.	England and Wales

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Our financing

Affinity Water Limited is the group's principal trading company and is financially and operationally 'ring-fenced' from the rest of the Affinity Water group by way of a WBS. The securitisation further enhances the ring-fencing provisions already in its licence. The sole business of its immediate holding company, Affinity Water Holdings Limited, is holding the shares of Affinity Water Limited.

The group has two financing subsidiaries which have issued bonds which are listed by the UK Listing Authority (UKLA) and the proceeds of which have been lent on to and are guaranteed by the group's principal trading company:

- Affinity Water Finance (2004) PLC has issued an external bond of £250.0m; and
- Affinity Water Finance PLC has issued external bonds totalling £880.0m.

The group believes that the ring-fencing structure provides significant corporate benefits, providing better access to long-term debt markets and an opportunity to reduce the cost of capital employed in the regulated business for the benefit of customers.

Bonds issued by both Affinity Water Finance (2004) PLC and Affinity Water Finance PLC are subject to the Listing Rules and Disclosure and Transparency Rules, being listed by the UKLA.

The bonds issued by the group at 31 March 2023 can be summarised as follows:

Debt	Bond £m	Coupon %	Maturity Date
Class A fixed rate bond 2026*	250.0	5.875%	July 2026
Class A fixed rate bond 2036*	250.0	4.500%	March 2036
Class A RPI linked bond 2045*	190.0	1.548% (real)	June 2045
Class A CPI linked bond 2038	130.0	0.010% (real)	September 2038
Class A fixed rate bond 2042*	85.0	3.278%	August 2042
Class A fixed rate bond 2033*	60.0	2.699%	November 2033
Class A CPI linked bond 2042*	60.0	0.230% (real)	November 2042
Total Class A	1,025.00		
Class B RPI linked bond 2033	95.0	3.249% (real)	June 2033
Class B RPI linked bond 2033*	10.0	1.024% (real)	June 2033
Total Class B	105.0		
Total	1,130.00		

*Listed on the London Stock Exchange

Our next significant debt maturity is in July 2026 when our £250.0m fixed rate bond matures. The maturity profile of all our borrowings is set out in note A4 to our statutory financial statements, and in the graph on the following page.

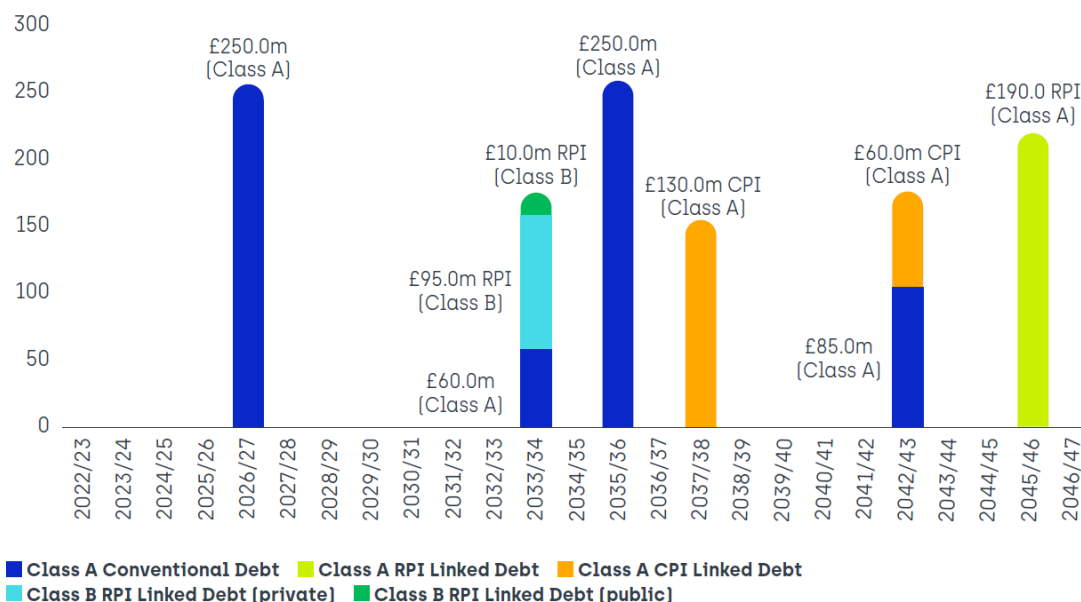
Our net debt¹ as at 31 March 2023 was £1,257.7 million, an increase of £177.9 million since last year (2022: 1,079.8 million), primarily, due to accretion on the index-linked bonds. Our gearing, as measured by net debt to RCV at 31 March 2023, was 73.4% (2022: 73.0%), and remains below our internal maximum gearing level of 80.0% of RCV. The £14.2m Class A fixed rate bond matured in September 2022 and was fully repaid.

¹ This Alternative Performance Measure is calculated as borrowings and accrued interest less loan from intermediate parent company and all company cash and short-term deposits; it is reconciled to our regulatory net debt in table 1E of our Annual Performance Report

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Our financing (continued)



The £14.204 million Class A guaranteed notes matured and were repaid in full in September 2022.

Interest rate exposure is, primarily, managed by using a mixture of fixed rate, floating rate, and index-linked borrowings (refer to note A4 to our statutory financial statements). At the year-end, 49.3% of our gross borrowings were at fixed rates (2022: 52.3%), 32.9% (2022: 33.7%) at rates indexed to RPI and 17.8% (2022: 14.0%) at rates indexed to CPI. Considering our index-linked inflation swaps, the proportion of borrowings at fixed rates decreased to 14.0% (2022: 22.6%), the proportion indexed to RPI increased to 49.5% (2022: 47.4%) and the proportion indexed to CPI increased to 36.6% (2022: 30.0%).

The credit ratings for our subsidiaries' bonds assigned by the rating agencies, Moody's, Standard & Poor's, and Fitch were as follows. Our credit ratings have not changed since March 2022, although in October 2022 our ratings from Standard & Poor's have moved to a negative outlook driven by inflationary pressures impacting industry ratings.

Bonds	Moody's	Standard & Poor's	Fitch
Class A	A3	BBB+	BBB+
Class B	Baa3	BBB-	BBB-
Corporate family rating for Affinity Water Limited	Baa1	Not applicable	Not applicable

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Our financing (continued)

The total value of the issued bonds can be reconciled to the group's net debt position as at 31 March 2023 as follows:

	2023 £000
Nominal value of Class A fixed interest bonds issued	645,000
Nominal value of Class A index linked bonds issued	380,000
Nominal value of Class B index linked bonds issued	105,000
Total nominal value of bonds issued	1,130,000
Accretion on Class A index linked bonds	119,885
Accretion on Class B index linked bonds	48,136
Accretion on financial derivative	98,015
Capitalised bond issue costs and net premium/discount related to Class A bonds	31,230
Capitalised bond issue costs relating to Class B bonds	(1,022)
Capitalised issue costs relating to financial derivative	(271)
Fair value adjustment on acquisition	349,630
Amortisation of fair value adjustment	(138,978)
Bank term loan	41,112
Debentures	34
Cash in hand	(156,563)
Net debt	1,521,208

Net debt as at 31 March 2023 was £1,521,208,000, an increase of £156,391,000 since last year (2022: £1,364,817,000) primarily due to accretion on the index-linked bonds.

Our liquidity is managed through banking arrangements and adequate cash resources, borrowing arrangements and standby facilities. This enables us, at all times, to have the level of funds available that are necessary for the achievement of our business and service objectives. At 31 March 2023, we had cash balances of £78.8 million (2022: £135.6 million) and short-term deposits held as investments of £66.7 million (2022: £70.2 million). The decrease in cash from the prior year is, primarily, due to the proceeds from the issuance of a green bond in the prior year, followed by continued investment in our network in the year to 31 March 2023 and repayment of the £14.204 million bond in September 2022.

To the extent that additional funding is required, as well as our cash balances, Affinity Water Limited has access to two revolving credit facilities totalling £100.0 million (2022: £100.0 million), which were undrawn at 31 March 2023 (2022: undrawn), to finance capital expenditure and working capital requirements.

In addition, we have access to a further £52.0 million of liquidity facilities (2022: £55.0 million), consisting of a 364-day revolving £27.0 million facility to fund any debt service payments in the event of a liquidity shortfall, which would, otherwise, prevent such payments being made and a 364-day revolving facility of £25.0 million to fund operating and capital maintenance expenditure in the event of a liquidity shortfall.

On 2 September 2022, Affinity Water Holdco Finance Limited refinanced its £42,000,000 bank term loan, extending the repayment date from 30 June 2023 to 2 September 2027, with an option to extend for a further two years. The facility also contains an uncommitted accordion feature to increase the loan size to £75,000,000. The carrying amount of the loan at 31 March 2023 was £41,112,000 (2022: £41,429,000).

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Board of directors

The directors of Daiwater Investment Limited who were in office during the year and up to the date of signing the financial statements are disclosed on the directors report on page 32.

Certain Board members are also directors of other group companies. The numbers listed alongside their name in the table below may be cross referenced to the relevant company shown on the structure chart on page 34.

The table below sets out attendance at Board meetings for the year ended 31 March 2023.

	Number of meetings
Michael Osbourne*	2/2
Roxana Tataru*	2/2
Jonathan Carter*	1/1
Adam Waddington*	0/0
Jaroslava Korpanec	0/0
Marissa Dardi	½

* Current directors

There were two Board meetings during the year.

Directors' qualifying third party indemnity provisions

The company has not granted any indemnity to its directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in Section 234 of the Companies Act 2006.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Corporate governance

The group and company benefits from the corporate governance arrangements established by Affinity Water Limited, full details of which can be found in its own Annual Report and Financial Statements for the year ended 31 March 2023, together with more detailed corporate reporting disclosures.

Affinity Water Limited remains committed to the highest standards of governance and supports the principles of good corporate governance set out in the 2018 UK Corporate Governance Code ('the Code'), the UK Stewardship Code and Ofwat's 2019 board leadership, transparency and governance principles. It is ultimately owned by private investors and therefore Affinity Water Limited applies the principles of the Code in this context, having regard to: the Guidelines for Disclosure and Transparency in Private Equity (the Walker Guidelines) and the work of the Private Equity Reporting Group to monitor conformity with the Guidelines; the OECD Principles of Corporate Governance (2004); and Ofwat's revised board leadership, transparency and governance principles.

The trading subsidiary complied with the principles of the Code during 2022/23, except in terms of aligning executive directors' pension contributions with those of its workforce. This is explained in detail in its own Annual Report and Financial Statements on its website: affinitywater.co.uk/library. The reason for the departure is explained within the relevant section of Affinity Water Limited's corporate governance report for the year ended 31 March 2023. The Board of Affinity Water Limited considers its governance arrangements appropriate for a company owned by private investors.

The Board has overall responsibility for the group's and company's systems of internal control and for reviewing the effectiveness of these systems. It is responsible for ensuring the group and company meets its obligations to its shareholders and meets from time to time to facilitate this.

There are certain matters that the Board of Affinity Water Limited has reserved for shareholder approval. These matters are published on Affinity Water Limited's website: affinitywater.co.uk/governance-assurance

Financial and business reporting

Having taken into account all matters considered by the Board and brought to its attention during the year, the directors are satisfied that the Annual Report and Financial Statements taken as a whole are fair, balanced and understandable.

The Board believes that the disclosures set out on pages 5 to 31 of the Annual Report and Financial Statements provide the information necessary for shareholders to assess the group's performance, business model, financial risk management and strategy.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Future developments

It is anticipated the company will continue to invest and manage its long-term interests in the water industry in the United Kingdom for the foreseeable future.

Likely future developments in the business resulting from expected changes in the regulatory and competitive environments that Affinity Water Limited operates in are discussed in the strategic report in its own Annual Reports and Financial Statements for the year ended 31 March 2023 on its website: affinitywater.co.uk/library.

Research and development activities

The development and application of new techniques and technology is an important part of the group's principal trading subsidiary's activities. Affinity Water Limited is a member of UK Water Industry Research (UKWIR), and participates widely in, and benefits from its research programme. The UKWIR programme relating to Affinity Water Limited is currently divided into the following topics: drinking water quality and health; toxicology; water resources; climate change; water mains and services; leakage and metering and regulatory issues.

Affinity Water Limited is also a member of other water industry research and innovation groups: Technology Approval Group, the Water Treatment Technical Working Group, the Sensor for Water Interest Group, the Water Regulations Advisory Scheme and Cranfield Water Network. In addition, Affinity Water Limited carried out more specific research during the year in the fields of process performance and energy optimisation, novel technologies for plumbosolvency control, monitoring of biological risks in the network and risks to water quality when changing sources of supply.

Political contributions

No political contributions were made during the year (2022: £nil), in accordance with the group's policy of not making political contributions.

Financial instruments disclosures

Details of financial instruments risk management are included within risk number 15 on page 17 of the strategic report and in note A4 of the financial statements.

Information required for Affinity Water Limited under the Listing Rules

During the year, no interest was capitalised by Affinity Water Limited.

The remuneration report in Affinity Water Limited's Annual Report and Financial Statements for the year ended 31 March 2023 provides disclosures in relation to relevant requirements of the Listing Rules.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Employee matters

The trading subsidiary maintains a network of trained mental health first aiders within the business and continues to publicise its Employee Assistance Programme.

The subsidiary aims to ensure that each employee or applicant for employment receives the same treatment irrespective of race, gender, disability, sexual orientation, religious belief, creed, marital or parental status. This extends through all company policies including recruitment where the candidate's particular aptitudes and abilities are consistent with the requirements of the job. Opportunities are available to disabled employees for training, career development and promotion. Employees who become disabled whilst employed by the group are actively supported to maintain and/or find appropriate employment within the business.

The subsidiary provides a discretionary company-wide performance bonus scheme for all employees. The discretionary company-wide bonus scheme comprises operational and customer performance measures and a financial performance measure.

Engagement with employees

The trading subsidiary consults and informs its employees on all aspects of business performance through formal and informal consultation bodies, regular team meetings, email and the intranet. It discusses ways to enhance and improve its communications and consultation channels directly with its employees as well as with the Trade Unions to which a number of its employees belong.

Employees are kept informed of changes in the business, and general, financial and economic factors influencing the company together with performance targets. This is achieved through regular briefings or presentations and electronic mailings.

See page 22 for details in our section 172(1) statement on how directors have engaged with employees and taken their interest in accounts.

Engagement with other stakeholders

See pages 22 to 31. for details in our section 172(1) statement on how directors have engaged with suppliers, customers and other stakeholders.

Financial instruments disclosures

Details are included within risk number 14 on page 16 of the strategic report and in note A4 of the financial statements.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Greenhouse Gas Emissions

This section provides information about our greenhouse gas (GHG) emissions and our performance in managing them. For 2022/23, our operational emissions continue to reduce as they have been since 2014/15. We have been confidently reporting our scope 1 and 2 emissions for several years now and have now made significant steps forward in understanding our in-direct emissions (scope 3). For 2022/23, we have developed our first scope 3 inventory, which will enable us to identify key areas for emissions future reductions.

Greenhouse Gas Emission Scopes

The greenhouse gas protocol defines three groups or 'scopes' in which GHG emissions are reported on.

Scope 1 emissions

Scope 1 covers emissions from sources that an organisation owns or controls directly – for example from burning fuel (diesel or petrol) in our fleet of vehicles.

Scope 2 emissions

Scope 2 are emissions that a company causes indirectly from the energy it purchases. For Affinity Water, this relates to the purchase of electricity.

Scope 3 emissions

Scope 3 encompasses emissions that are not produced by the company itself, but by those that it's indirectly responsible for, up and down its value chain. For example, the emissions associated with the goods and services we purchase from suppliers.

Through the development of a scope 3 inventory, we can, for the first time, report our full carbon footprint. For 2022/23, using a market-based approach, we estimate our full carbon footprint to be 91,868 tCO₂e. Following a location-based approach, our footprint is 135,491 tCO₂e.

Market Based and Location Based Reporting

A location-based method reflects the average emissions intensity of the electricity grid on which energy consumption occurs (using mostly grid-average emission factor data). A market-based method reflects emissions from electricity that companies have purposefully chosen. For Affinity Water, this means market-based reporting reflects that our electricity is provided by renewable sources, using a REGO-backed green tariff.

The Renewable Energy Guarantees of Origin (REGO) scheme provides transparency about the proportion of electricity that suppliers source from renewable electricity. The scheme provides certificates called REGOs, which demonstrate electricity has been generated from renewable sources.

How we report our emissions

Our carbon footprint is calculated by converting the main GHGs into a carbon dioxide equivalent (tCO₂e). Emissions are categorised into scopes (based on the GHG Protocol) as follows:

- Scope 1 emissions (direct emissions) are those from activities we own or control, including those from our treatment processes, company vehicles, and burning of fossil fuels for heating.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

How we report our emissions (continued)

- Scope 2 emissions (indirect emissions) result from purchased heat and electricity.
- Scope 3 emissions (indirect emissions) arise from activities we do not own or control, but which we can influence. These include from the products and services we buy. We also report on our emissions based on whether they are considered to be 'operational' resulting from our day-to-day activities or 'embedded' resulting from our wider activities such as the delivery of capital projects.

We use a combination of methods to estimate the emissions associated with our carbon footprint following the principles of the 2015 GHG Protocol Corporate Accounting and Reporting Standard. We also align to the 2019 UK Government Environmental Reporting Guidelines, including the requirements for Streamlined Energy and Carbon Reporting (SECR).

Operational Emissions

Our operational emissions include scope 1, scope 2 and a limited number of scope 3 emissions, all of which are assessed using the latest version of the UKWIR Carbon Accounting Workbook. In 2022/23, the scope of emissions described as 'operational' has increased in line with Ofwat's regulatory reporting requirements. Key changes include the following additions to operational emissions associated with:

- chemicals purchased (previously reported under embedded emissions);
- waste from operations managed by both Affinity Water and third parties; and
- extraction, production, and transportation of fuels in the generation of electricity and heat that is consumed by the reporting company (previously limited to transportation).

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Operational Emissions (continued)

Description	2022/23		2021/22	
	Location Based – Gross (tCO ₂ e)	Market Based – Gross (tCO ₂ e)	Location Based – Gross (tCO ₂ e)	Market Based – Gross (tCO ₂ e)
Scope 1 emissions				
Direct emissions from burning of fossil fuels (including CHP generated onsite)	1,578	1,578	1,870	1,870
Process and fugitive emissions	2,189	2,189	2,417	2,417
Transport: company-owned or leased vehicles	2,147	2,147	1,996	1,996
Total scope 1 emissions	5,914	5,914	6,283	6,283
Scope 2 emissions				
Purchased electricity	43,623	0	46,735	0.000
Total scope 2 emissions	43,623	0	46,735	0
Scopes 1 and 2	49,537	5,914	53,018	6,283
Scope 3 emissions				
Business travel on public transport and private vehicles used for company business	204	204	109	109
Outsourced activities (if not included in Scope 1 or 2)				
Energy and other	156	156	147*	147*
Purchased electricity – transmission and distribution(location based)	3,991	3,991	4,136	4,136
Use of chemicals	10,858	10,858	11,300*	11,300*
Disposal and treatment of waste	2,409	2,409	2,433	2,433
Total scope 3 emissions	17,618	17,618	18,125	18,125
Total Gross Emissions	67,155	23,532	71,143	24,408

Annual operational GHG intensity ratio values	(kgCO ₂ e/MI)	(kgCO ₂ e/MI)	(kgCO ₂ e/MI)	(kgCO ₂ e/MI)
Operational GHG emissions per MI of treated water	195	69	207	71

*This figure has been restated. See below for further detail.

Using a market-based approach to reporting, our total gross operational emissions (as defined by Ofwat for 2022/23) are estimated to be 23,532 tCO₂e. As expected, this is greater than the operational emissions reported in 2021/22 as the scope of emission considered to be 'operational' has expanded. Comparing against the same basket of emissions for 2021/22 (25,818 tCO₂e) we are reporting a reduction of 3%.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Operational Emissions (continued)

Scope 1

The annual quantity of emissions for 2022/23 in CO₂e resulting from activities for which the company is responsible (scope 1) is 5,914 tCO₂e (2021/22: 6,283 tCO₂e), as shown in Table 1. Sources of direct emissions for the company include fuel emissions from burning of fossil fuels. This is made up of natural gas used for the heating and cooling of our buildings and fuels used, primarily, by generators at our water treatment works. Fugitive and process emissions include ozone used in the disinfection process and waste sludge recycled to our land and refrigerant gases. Also included are fleet fuel emissions, which result from the combustion of purchased fuel for fleet liveried vehicles.

During 2022/23, we saw a small reduction in the use of diesel across our operations. We are also, provisionally, reporting a reduction in natural gas usage. For 2023/24, we expect to see further reductions as we reduce the use of on-site generators and begin to trial the use of biodiesels.

Fleet fuel use increased in 2022/23 compared to 2021/22 by 8%. This resulted from an increase in the number of vehicles we utilise to deliver our operations. The volume of petrol we purchased in 2022/23 has also slightly more than doubled compared to 2021/22 (although still only representing 1% of total fleet fuel purchased).

The majority of our process and fugitive emissions arise from ozone generation, which is used in the water treatment process. For 2022/23, our total ozone generation was similar to 2021/22; however, less ozone was generated using air (rather than liquid oxygen) resulting in fewer emissions being emitted from this process.

Scope 2

In 2022/23, emissions in CO₂e resulting from activities for which the company is responsible (scope 2) is zero, as was the case in 2021/22 when reporting via a market-based approach¹. From October 2020, all our purchased electricity is from 100% REGO-backed renewable energy, which we, primarily, use for the pumping and treatment of water and a small amount for office and operational site use. When reporting using a location-based approach, scope 2 emissions in 2022/23 are 43,623 tCO₂e (2022: 46,735 tCO₂e).

Although we are recording a reduction in scope 2 emissions when taking a location-based approach, our electricity usage increased compared to 2021/22. In 2022/23 we used 225.6GWh, while in 2021/22, we used 220.1GWh.

During the summer of 2022, we experienced prolonged dry weather and an unprecedented heat wave during mid-July. These conditions, significantly, increased demand across our supply area and, in response, we used, significantly, more electricity during June, July and August compared to the same months in 2021/22. Despite the significant increased summer demand, we recorded an improvement in the energy performance of our operations from 631kWh/MI to 630kWh/MI. Several activities have contributed to this increased performance:

- During 2022/23 our solar installation at Chertsey and Walton performed well, in parts as a result of the prolonged dry weather for much of the summer. At Chertsey, the solar arrays produced 1,051,721kWh, which saved approximately 203 tCO₂e when compared to using average grid electricity. At Walton, the solar arrays produced 589,004 kWh, which saved approximately 114 tCO₂e

¹ A location-based method reflects the average emissions intensity of grids on which energy consumption occurs (using mostly grid-average emission factor data). A market-based method reflects emissions from electricity that companies have, purposefully, chosen.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Operational Emissions (continued)

Scope 2 (continued)

- Our energy efficiency and optimisation programme has delivered projects that led to in-year savings of 1,964,000 kWh, which is, approximately, 380 tCO₂e

The reduction in scope 2 emissions resulted from a change in emissions factors for UK average grid electricity. The changed emissions factor is expected to continue as we see a continued decarbonisation of the UK electricity grid (because of reductions in electricity generated from coal and increases in renewable sources).

Scope 3 (Operational Only)

Total scope 3 'operational' emissions in 2022/23 is 17,618 tCO₂e (2021/22: 18,125 tCO₂e). Scope 3 operational emissions arise from a range of activities, including outsourced IT services, business travel, purchase of chemicals for water treatment and fuel and energy-related emissions (not covered in scope 2). For 2022/23 the use of chemicals has been re-defined as operational rather than as embedded emission as we reported in 2021/22.

Chemicals (including Granular Activated Carbon- GAC)

For 2022/23 we have updated the method used to assess the emissions associated with our purchase of chemicals (not including GAC). The method has been updated to better reflect the differences in concentration of the chemicals we purchase compared to those used as a benchmark for understanding associated emissions.

For 2022/23, we estimate that there are 10,858 tCO₂e associated with chemicals we purchase. We have also applied this updated method to recalculate the emissions associated with chemical purchase in 2021/22 and have reassessed this to be 11,300 tCO₂e.

For 2022/23, the emissions associated with our purchase of GAC is assessed to be 4,142 tCO₂e. Our method for calculating GAC emissions remains unchanged from previous years, although we have improved the data used and have updated the emissions for 2021/22.

Business travel in 2022/23 was estimated at 204 tCO₂e, an increase from 2021/22. Increases in business travel were most notable with vehicle mileage increasing by 44% on 2021/22, and increases also recorded in air travel.

In line with UK grid decarbonisation, we have seen a reduction in scope 3 purchased electricity emissions not covered by our green tariff of approximately 4% compared to 2021/22.

Method Used

For scope 1, scope 2 and operational scope 3 GHG emissions, we follow the most common approach to calculate GHG emissions, which is to take activity data (e.g. units of electricity consumed, or distance travelled) and convert the activity data into tCO₂e. We have reported the common intensity metric for the Water Industry, which is Carbon tCO₂e per MI, which is our tCO₂e divided by water into supply (MI).

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

WaterUK Net Zero 2030

In 2019, we joined all UK water companies in pledging to reduce our operational emissions (as defined at the time) to Net Zero by 2030. The emissions included within this target are scope 1, scope 2 and scope 3, where they relate to business travel, outsourced services related to IT and admin, and electricity transmission and distribution.

Our emissions relevant to our Net Zero target continue to reduce (see Figure 1). In 2022/23, we saw a small reduction in emissions of 2% compared to 2021/22. Reductions were associated with reduced diesel and natural gas use and falling transmission and distribution emissions.

For 2023/24, we plan to stay on course to reach our Net Zero by 2030 target through further reductions in the use of fossil fuels, a transition to EVs and by working with our supply chain.

Water UK Net Zero 2030 Emissions (Market Based)

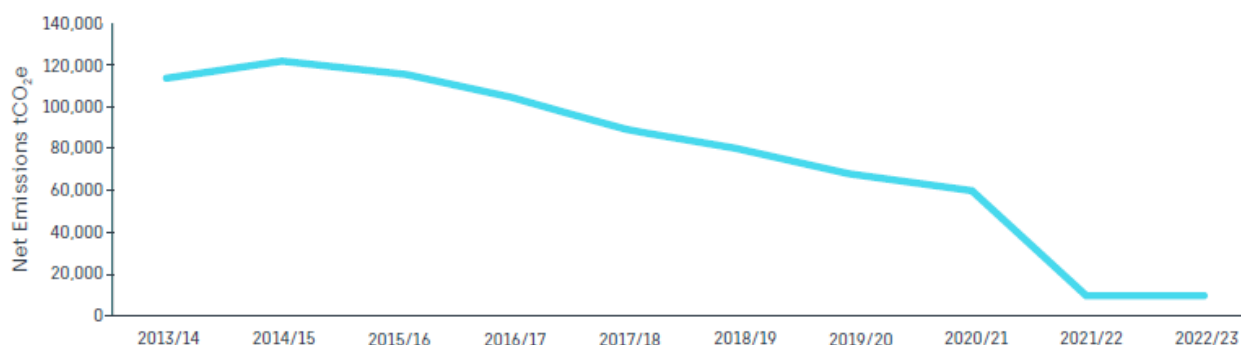


Figure 1 WaterUk Net Zero 2030 net operational emissions

Embedded Emissions

For 2022/23, we undertook two different assessments to understand our embedded emissions. To better understand our full carbon footprint, we worked with specialist provider EcoAct to develop a full scope 3 inventory. To understand in more detail the emissions associated with our capital projects, we used a bespoke asset-based carbon estimation tool to estimate the cradle-to-build emissions associated with our capital projects.

Our capital project emissions fall under the GHG protocol category of 'capital goods'; however, as different methods have been used, the value generated using the asset estimation tool should not be interpreted as a sub-total of the capital good category.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Embedded Emissions (continued)

Capital Projects

In line with Ofwat's reporting requirements, we have calculated the cradle-to-build emissions for our capital programme. This builds on the voluntary reporting undertaken last year. For 2022/23, we estimated that the emissions associated with the delivery of our capital programme were 8,465tCO_{2e}. Although this is an increase on our 2021/22 estimate of 4,350 tCO_{2e}, the scope of projects included within this year's reporting is significantly greater than in 2021/22. In 2022/23, we estimated the emissions associated with 47 projects, an increase from 11 projects in 2021/22.

Within the 47 projects assessed, this included 17 below ground asset (infra) projects with the remainder a mix of above ground (non-infra) projects, storage projects, minor works and lead replacement. We have included both constructing new assets and refurbishment where it is practicable to estimate this value.

For 2022/23, emissions associated with our capital projects were all estimated using the first iteration of our asset carbon estimation tool. Although the tool includes over 400 different process, asset and unit rate models, some assets we construct or install are not included in the tool. We have not been able to estimate the emissions associated with our river restoration projects, some minor works, meter installations or traffic management activities.

Our scope 3 inventory for capital goods enables us to have a high-level overview of this portfolio of activity. This is estimated to be 22,172.6 tCO_{2e} for 2022/23.

Scope 3 inventory

The purpose of our scope 3 inventory is to provide a high-level estimate of all indirect emissions that Affinity Water is responsible for. Where possible, this estimate has used primary data, and where this is not possible, estimates have been derived from spend-based data or other benchmarks. In some cases, scope 3 covers both operational and embedded emissions. For 2022/23, we have not sought to integrate emissions estimates from our assessment of operational emissions; instead, we used the scope 3 inventory as a high-level standalone assessment.

The results of our scope 3 inventory are as expected for a water company. As a provider of infrastructure, we have significant emissions that arise in our supply chain, particularly associated with asset construction and maintenance activities.

Our scope 3 inventory offers insight into how we can better target emissions reduction initiatives and work with our supply chain to reduce emissions.

Scope 3 Category	2022/23 Gross (tCO_{2e})
Category 1: Purchased goods and services	38,406.9
Category 2: Capital goods	22,172.6
Category 3: Fuel- and energy-related activities (not included in scope 1 or scope 2)	16,212.0
Category 4: Upstream transportation and distribution	238.2
Category 5: Waste generated in operations	7,424.5
Category 6: Business travel	227.9
Category 7: Employee commuting	1,063.7
Category 13: Downstream leased Assets	208.7

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Emission Reduction Activities in 2022/23

Our solar installation at Chertsey and Walton performed well during 2022/23, generating 1,051,721 kWh and 589,004 kWh of energy respectively. The electricity generated from solar equated to 0.73% of our total electricity usage during 22/23. This reduced our potential carbon emissions by 317 tCO_{2e}.

During 2022/23, we implemented sixteen energy efficiency schemes including the replacement of borehole and booster pumps. We have completed optimisation schemes improving the overall efficiency of source abstraction and high lift pumping. We have also upgraded control software to optimise booster operations, enabling pumps to maintain maximum efficiency for longer. Additionally, we have continued work on reducing pressure losses on sites through the improvement of our UV treatment processes.

During 2022/23, we started efficiency work on our buildings and offices, with new initiatives to reduce heating and lighting through process and behavioural change. We continue to put focus on changing our culture and have developed the Zapp app which empowers colleagues to raise efficiency ideas to investigation. Energy Management training has continued from last year.

We have developed a mature programme of energy savings opportunities with over 85 named schemes in various stages of implementation. Using this programme, we have set ourselves a £500k energy savings target for 2023/24.

We ordered our first four electric vans in 2022/23 and began installing charging infrastructure at our Stevenage and Staines sites. 2022/23 also saw us launch our salary sacrifice schemes for electric vehicle purchase by our employees.

We are currently piloting ways to reduce whole life emissions (both operational and embodied) of our capital projects. There is significant evidence that to evaluate a project through a carbon lens finds efficiencies in both carbon and costs, which we aim to achieve through the use of the PAS 2080 standard. We are also finding opportunities for wider benefits such as environmental net gain.

Total Gross Emissions (tCO_{2e})

The company supplies water to 3,830,000 consumers in our supply area (2022: 3,780,000). The Covid-19 pandemic developed rapidly in 2020, resulting in an increased demand for water we supply due to the impact of the virus and the hot summer of 2020. The way we operate also had to change with the majority of office-based staff working from home, and just a small number of employees at our office locations. Our front-line delivery teams have continued to work at our operational sites and in the community.

We are currently piloting ways to reduce whole-life emissions (both operational and embodied) of several large capital projects. There is significant evidence that, to evaluate a project through a carbon lens finds efficiencies in both carbon and costs, which we aim to achieve through the use of the PAS2080 standard. We are also finding opportunities for wider benefits such as environmental net gain through our carbon reduction projects.

Our plans include moving to a greener vehicle fleet, to develop significant renewable energy and to be part of the water industry's commitment to plant 11 million trees. In addition to this, we are working closely with our supply chain partners to reduce carbon emissions (scope 3) from our daily activities and planned investment, both from the materials and energy we use.

This financial year has seen a decrease of 79.64%, of our gross greenhouse gas emissions compared to last year. Scope 1 Direct Emissions have increased from 5,003 tCO_{2e} in the prior year to 6,282 tCO_{2e} in 2021/22.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Total Gross Emissions (tCO₂e) (continued)

There has been an increase of 22.58% in natural gas usage from last year. This is due to higher proportion of estimated reads and slight increase of actual consumption, as we see more people working from offices as Covid-19 recedes.

There has been an increase in gas oil consumption against the prior year of 66.57%, due to faulty generators being repaired and increased usage during winter peak load times.

As all our purchased electricity is from a REGO backed Green Tariff, using a market based approach we do not record any scope 2 emissions associated with our operations, include pumping and treating water. Electricity consumption and emissions from outsourced activities, administration services and courier mileage have been included and in line with the Ofwat net zero road map, it is envisaged this will continue to expand.

There have also been increases in the conversion factors across most lines due to changes in government factors; these are in the BEIS 21 methodology paper, which details the revisions due to new/improved data while using existing calculation methodologies, and in the UKWIR CAWv16. The water distributed input has decreased by 1.92%, which is used in the intensity measure (kgCO₂e/MI). We used the WKWIR CAWv16 to calculate emissions.

There has been a 6.36% increase in petrol and diesel consumption relating to transport owned by the company, which contributes to our total emissions.

This compares to an increase in emissions from transport by public transport and private vehicles; this is 0.83% of our total net emissions.

We have also included in our scope 3 emissions:

- Water treatment waste recycled to land
- Water treatment waste sent to landfill
- Other wastes including scrap metals, plastics, cardboard, and glass

During 2022/23, we have implemented energy efficiency schemes including the replacement of borehole and booster pumps. We have completed optimisation schemes improving the overall efficiency of source abstraction and high lift pumping. We have also upgraded control software to optimise booster operations, enabling pumps to maintain maximum efficiency for longer. Additionally, we have continued work on reducing pressure losses on sites through the improvement of our UV treatment processes.

This financial year we have started efficiency work on our buildings and offices, with new initiatives to reduce heating and lighting through process and behavioural change. We continue to put focus on changing our culture and have developed the Zapp app which empowers colleagues to raise efficiency ideas to investigation. Energy Management training has continued from last year.

We have developed a mature programme of energy savings opportunities with over 85 named schemes in various stages of implementation. Using this programme, we have set ourselves a £500k energy savings target for 2023/24.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Going concern

Group

The directors consider it appropriate to adopt the going concern basis of accounting in preparing the financial statements as they believe that the group 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 the assessment of the principal risks of the group and the consideration of the group's budgeted cash flows, short and long-term forecasts and ability to generate future revenues, related assumptions, and to meet the covenants associated with the group's available debt facilities.

To assess a severe but plausible downside scenario, management have considered a base case forecast 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, 20% of debt not currently subject to loss allowance provision. The severe but plausible downside scenario is overlaid on the base case forecast, which has taken into consideration the impact of inflation, interest rates, supply chain cost pressures, the energy price crisis and the cost-of-living crisis.

It is possible both an ICR Trigger and Default Event could occur in the severe but plausible downside scenario, although this is based on the assumption that no mitigating actions would be taken. Management are confident that mitigation actions within their control could be implemented that would prevent a trigger or default event from occurring. Under an ICR Trigger Event, the group would be subject to certain constraints, such as restrictions on dividends and restriction on debt buybacks. However, the directors are satisfied that an ICR Trigger Event would not fundamentally constrain the group's ability to carry out its business, particularly after considering the group's strong cash position, meaning that the group has no further funding requirement in AMP7. Under an ICR Default Event, each finance party may declare all amounts outstanding under the applicable Finance Documents to be immediately due and payable.

The group continues to monitor and manage the risks associated with the ICR covenant through the forecasting and reporting process and continues to monitor potential mitigations, the most prominent of which are working capital management, operating expenditure reviews and fixing energy transactions to align with current market rates.

Details of the group's cash and short-term investment are included in the statement of financial position on page 62, and undrawn committed borrowing facilities are included in notes 17 and A4. Due to the nature of the principal trading subsidiary's regulated business, the directors consider it appropriate to place reliance on projected financials. There have been no events after the reporting financial year significantly affecting liquidity headroom.

Company

The directors consider it appropriate to adopt the going concern basis of accounting in preparing the company 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 at least the next twelve months and the foreseeable future beyond that.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Statement of directors' responsibilities in respect of the financial statements

The directors are responsible for preparing the annual report and financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group and the company financial statements in accordance with UK-adopted international accounting standards.

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

- select suitable accounting policies and then apply them consistently;
- state whether applicable UK-adopted international accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and company will continue in business.

The directors are responsible for safeguarding the assets of the group and company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are also responsible for keeping adequate accounting records that are sufficient to show and explain the group's and company's transactions and disclose with reasonable accuracy at any time the financial position of the group and company and enable them to ensure that the financial statements comply with the Companies Act 2006.

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

Directors' confirmations

The directors consider that the Annual Report and Financial Statements, taken as a whole, are fair, balanced, and understandable, and provide the information necessary for shareholders to assess the company's position and performance, business model and strategy.

In the case of each director in office at the date the directors' report is approved:

- so far as the director is aware, there is no relevant audit information of which the group's and company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the group and company's auditors are aware of that information.

Information required under listing rules

During the year, no interest was capitalised by the company (2022: £nil). For disclosures in relation to relevant requirements of the Listing Rules, refer to the Remuneration Report on Affinity Water Limited Annual Report and Financial Statements for the year ended 31 March 2023 on its website: affinitywater.co.uk/library.

Daiwater Investment Limited

Directors' report for the year ended 31 March 2023 (continued)

Independent auditors

In accordance with Section 485 of the Companies Act 2006, a resolution to reappoint PricewaterhouseCoopers LLP will be proposed at the forthcoming AGM.

On behalf of the Board

Patrick Makoni
Company Secretary
21 December 2023

Registered Office:

Tamblin Way
Hatfield
Hertfordshire
AL10 9EZ

Independent auditors' report to the members of Daiwater Investment Limited

Report on the audit of the financial statements

Opinion

In our opinion, Daiwater Investment Limited's group financial statements and company financial statements (the "financial statements"):

- give a true and fair view of the state of the group's and of the company's affairs as at 31 March 2023 and of the group's loss and the group's and company's cash flows for the year then ended;
- have been properly prepared in accordance with UK-adopted international accounting standards as applied in accordance with the provisions of the Companies Act 2006; 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 Consolidated and Company statements of financial position as at 31 March 2023; the Consolidated income statement, the Consolidated statement of comprehensive income, the Consolidated and Company statements of changes in equity and the Consolidated and Company statements 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 group 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.

Conclusions relating to going concern

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 group's and 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 group's and the company's ability to continue as a going concern.

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

Independent auditors' report to the members of Daiwater Investment Limited

Report on the audit of the financial statements (continued)

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. 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 2023 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 group and company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic report and Directors' report.

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 group's and 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 group or the company or to cease operations, or have no realistic alternative but to do so.

Independent auditors' report to the members of Daiwater Investment Limited

Report on the audit of the financial statements (continued)

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 group 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'), the Water Industry Act 1991, 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 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, the extent of costs capitalised or the impairment assessment of goodwill.. Audit procedures performed by the engagement team included:

- discussions with management, internal audit and the group'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, loss allowance for trade receivables and impairment assessment of goodwill; and
- identifying and testing journal entries posted, such as those with unusual account combinations, and incorporating an element of unpredictability into the audit procedures performed

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.

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.

Independent auditors' report to the members of Daiwater Investment Limited

Report on the audit of the financial statements (continued)

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 company financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

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

21 December 2023

Daiwater Investment Limited

Consolidated income statement for the year ended 31 March 2023 (Registered Number 10738347)

	Note	2023 £000	2022 £000
Revenue	1	323,343	319,747
Cost of sales		(283,958)	(266,764)
Gross profit		39,385	52,983
Administrative expenses	2.1	(38,747)	(38,453)
Impairment losses on financial and contract assets	2.1	(10,779)	(9,389)
Other operating income	2.2	21,929	18,972
Operating profit	2	11,788	24,113
Finance income	4	41,789	38,948
Finance costs	4	(172,535)	(104,495)
Fair value gain/(loss) on swaps	4	49,755	(31,295)
Net finance costs	4	(80,991)	(96,842)
Fair value (loss)/gain on energy swaps		(26,638)	27,988
Loss before tax		(95,841)	(44,741)
Income tax credit/(expense)	5	6,794	(54,764)
Loss for the financial year		(89,047)	(99,505)
(Loss) is attributable to:			
Owners of the group		(89,147)	(99,598)
Non-controlling interests		100	93
		(89,047)	(99,505)

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

The notes on pages 68 to 134 are an integral part of these financial statements.

Daiwater Investment Limited

Consolidated statement of comprehensive income for the year ended 31 March 2023

(Registered Number 10738347)

	Note	2023 £000	2022 £000
Loss for the year		(89,047)	(99,505)
<i>Other comprehensive (expense)/income for the year which will not be reclassified to profit or loss:</i>			
Re-measurements of post-employment benefit assets	10	(52,114)	28,749
Deferred tax credit/(charge) on items that will not be reclassified	5,19	13,029	(7,187)
Other comprehensive (loss)/income for the year, net of tax		(39,085)	21,562
Total comprehensive loss for the year		(128,132)	(77,943)
Total comprehensive loss is attributable to:			
Owners of the group		(128,232)	(78,036)
Non-controlling interests		100	93
		(128,132)	(77,943)

The notes on pages 68 to 134 are an integral part of these financial statements.

Daiwater Investment Limited

Consolidated statement of financial position as at 31 March 2023

(Registered Number 10738347)

	Note	2023 £000	2022 £000
Assets			
Non-current assets			
Property, plant and equipment	6	1,748,160	1,707,172
Right-of-use assets	7	7,649	9,440
Intangible assets	8	645,463	646,964
Investments	9	51	51
Retirement benefit surplus	10	53,615	104,247
Derivative financial instruments	11	3,283	7,342
		2,458,221	2,475,216
Current assets			
Inventories	13	4,833	4,348
Current tax assets		296	308
Trade and other receivables	12	102,739	104,217
Derivative financial instruments	11	6,068	20,646
Short-term investments	9	66,709	70,179
Cash and cash equivalents	14	89,854	150,404
		270,499	350,102
		2,728,720	2,825,318
Total assets			
Equity and liabilities			
Equity			
Called up share capital	15	7,441	7,441
Retained earnings		314,160	442,392
Non-controlling interests		2,764	2,759
Total equity		324,365	452,592
Liabilities			
Non-current liabilities			
Trade and other payables	16	262,074	247,074
Borrowings	17	1,579,932	1,546,535
Lease liabilities	18	4,785	6,329
Derivative financial instruments	11	121,983	106,818
Deferred tax liabilities	19	251,674	271,500
Provisions for other liabilities and charges	20	3,319	3,107
		2,223,767	2,181,363
Current liabilities			
Trade and other payables	16	171,307	188,046
Lease liabilities	18	3,053	3,317
Derivative financial instruments	11	2,128	-
Provisions for other liabilities and charges	20	4,100	-
		180,588	191,363
		2,404,355	2,372,726
Total liabilities		2,404,355	2,372,726
Total equity and liabilities		2,728,720	2,825,318

The notes on pages 68 to 134 are an integral part of these financial statements. The statutory financial statements on pages 60 to 134 were approved by the Board of Directors and were signed and authorised for issue on 21 December 2023 on its behalf by:

Michael Osborne
Director

Daiwater Investment Limited

Company statement of financial position as at 31 March 2023

(Registered Number 10738347)

	Note	2023 £000	2022 £000
Assets			
Non-current assets			
Investments	9	<u>754,027</u>	<u>754,027</u>
		754,027	754,027
Current assets			
Current tax asset		<u>3,126</u>	-
Cash and cash equivalents	14	<u>10</u>	-
		3,136	-
Total assets		<u>757,163</u>	<u>754,027</u>
Equity and liabilities			
Equity			
Called up share capital		<u>7,441</u>	<u>7,441</u>
Retained earnings ¹		<u>749,722</u>	<u>740,466</u>
Total equity		<u>757,163</u>	<u>747,907</u>
Current liabilities			
Current tax liabilities		-	<u>6,120</u>
Total equity and liabilities		<u>757,163</u>	<u>754,027</u>

The notes on pages 68 to 134 are an integral part of these financial statements. The statutory financial statements on pages 60 to 134 were approved by the Board of Directors and were signed and authorised for issue on 21 December 2023 on its behalf by:

Michael Osborne
Director

¹ Result for the year of £9,256,000 (2022: £nil) for the company consisting of dividend income from its subsidiary undertakings is included within retained earnings. This income is from discontinued operations following the liquidation of the subsidiary undertaking during the year to 31 March 2023. Dividends of £nil (2022: £nil) were paid to the company's shareholders.

Daiwater Investment Limited

Consolidated statement of changes in equity for the year ended 31 March 2023 (Registered Number 10738347)

	Note	Attributable to owners of the group			Non-controlling interests £000	Total £000
		Called up share capital £000	Retained earnings £000	Total £000		
Balance as at 1 April 2021		7,441	520,428	527,869	2,757	530,626
(Loss)/profit for the year		-	(99,598)	(99,598)	93	(99,505)
Other comprehensive income		-	21,562	21,562	-	21,562
Total comprehensive (loss)/income		-	(78,036)	(78,036)	93	(77,943)
Dividends	21	-	-	-	(91)	(91)
Total transactions with owners recognised directly in equity		-	-	-	(91)	(91)
Balance as at 31 March 2022		7,441	442,392	449,833	2,759	452,592
Balance as at 1 April 2022		7,441	442,392	449,833	2,759	452,592
(Loss)/profit for the year		-	(89,147)	(89,147)	100	(89,047)
Other comprehensive loss		-	(39,085)	(39,085)	-	(39,085)
Total comprehensive (loss)/income		-	(128,232)	(128,232)	100	(128,132)
Dividends	21	-	-	-	(95)	(95)
Total transactions with owners recognised directly in equity		-	-	-	(95)	(95)
Balance as at 31 March 2023		7,441	314,160	321,601	2,764	324,365

The notes on pages 68 to 134 are an integral part of these financial statements.

Daiwater Investment Limited

Company statement of changes in equity for the year ended 31 March 2023 (Registered Number 10738347)

	Note	Called up share capital £000	Retained earnings £000	Total £000
Balance as at 1 April 2021		7,441	740,466	747,907
Result for the year		-	-	-
Total comprehensive income for the year		-	-	-
Dividends	21	-	-	-
Total transactions with owners recognised directly in equity		-	-	-
Balance as at 31 March 2022		7,441	740,466	747,907
Balance as at 1 April 2022		7,441	740,466	747,907
Profit for the year		-	9,256	9,256
Total comprehensive income for the year		-	9,256	9,256
Dividends	21	-	-	-
Total transactions with owners recognised directly in equity		-	-	-
Balance as at 31 March 2023		7,441	749,722	757,163

The notes on pages 68 to 134 are an integral part of these financial statements.

Daiwater Investment Limited

Consolidated statement of cash flows for the year ended 31 March 2023

(Registered Number 10738347)

	Note	2023 £000	2022 £000
Cash flows from operating activities			
Cash generated from operations	22.1	98,242	102,508
Interest paid		(44,058)	(42,958)
Tax paid		-	(129)
Net cash inflow from operating activities excluding capital contributions		54,184	59,421
Capital contributions		9,637	25,771
Net cash inflow from operating activities		63,821	85,192
Cash flows from investing activities			
Investment in short-term deposits		3,470	(55,046)
Purchases of property, plant and equipment		(122,385)	(131,288)
Proceeds from sale of property, plant and equipment		535	435
Purchases of intangible assets		(5,299)	(8,608)
Interest received		18,390	16,886
Net cash outflow from investing activities		(105,289)	(177,621)
Cash flows from financing activities			
Proceeds from loan from subsidiary undertaking		-	146,994
Principal elements of lease payments		(3,475)	(3,649)
Financing activities		(1,308)	-
Repayment of borrowings		(14,204)	-
Dividends paid to non-controlling interests in subsidiary undertakings	21	(95)	(91)
Net cash (outflow)/inflow from financing activities		(19,082)	143,254
Net (decrease)/increase in cash and cash equivalents		(60,550)	50,825
Cash and cash equivalents at the beginning of the year		150,404	99,579
Cash and cash equivalents at end of year	14	89,854	150,404

The notes on pages 68 to 134 are an integral part of these financial statements.

Daiwater Investment Limited

Company statement of cash flows for the year ended 31 March 2023 (Registered Number 10738347)

	Note	2023 £000	2022 £000
Cash flows from operating activities			
Cash generated from operations	22.1	10	-
Net cash inflow from operating activities		<u>10</u>	<u>-</u>
Net increase in cash and cash equivalents		<u>10</u>	<u>-</u>
Cash and cash equivalents at beginning of year		-	-
Cash and cash equivalents at end of year	14	<u>10</u>	<u>-</u>

The notes on pages 68 to 134 are an integral part of these financial statements.

Daiwater Investment Limited

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.

On 31 December 2020, IFRS as adopted by the European Union at that date was brought into UK law and became UK-adopted International Accounting Standards, with future changes being subject to endorsement by the UK Endorsement Board. This change constitutes a change in accounting framework. However, there is no impact on recognition, measurement or disclosure in the period reported as a result of the change in framework.

The group financial statements and company financial statements have been prepared in accordance with UK-adopted International Accounting Standards and with the requirements of the Companies Act 2006 as applicable to companies reporting under those standards.

Going concern

Group

The directors consider it appropriate to adopt the going concern basis of accounting in preparing the financial statements as they believe that the group 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 the assessment of the principal risks of the group and the consideration of the group's budgeted cash flows, short and long-term forecasts and ability to generate future revenues, related assumptions, and to meet the covenants associated with the group's available debt facilities.

To assess a severe but plausible downside scenario, management have considered a base case forecast 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, 20% of debt not currently subject to loss allowance provision. The severe but plausible downside scenario is overlaid on the base case forecast, which has taken into consideration the impact of inflation, interest rates, supply chain cost pressures, the energy price crisis and the cost-of-living crisis.

It is possible both an ICR Trigger and Default Event could occur in the severe but plausible downside scenario, although this is based on the assumption that no mitigating actions would be taken. Management are confident that mitigation actions within their control could be implemented that would prevent a trigger or default event from occurring. Under an ICR Trigger Event, the group would be subject to certain constraints, such as restrictions on dividends and restriction on debt buybacks. However, the directors are satisfied that an ICR Trigger Event would not fundamentally constrain the group's ability to carry out its business, particularly after considering the group's strong cash position, meaning that the group has no further funding requirement in AMP7. Under an ICR Default Event, each finance party may declare all amounts outstanding under the applicable Finance Documents to be immediately due and payable.

The group continues to monitor and manage the risks associated with the ICR covenant through the forecasting and reporting process and continues to monitor potential mitigations, the most prominent of which are working capital management, operating expenditure reviews and fixing energy transactions to align with current market rates.

Details of the group's cash and short-term investment are included in the statement of financial position on page 62, and undrawn committed borrowing facilities are included in notes 17 and A4. Due to the nature of the principal trading subsidiary's regulated business, the directors consider it appropriate to place reliance on projected financials. There have been no events after the reporting financial year significantly affecting liquidity headroom.

Daiwater Investment Limited

Notes to the financial statements - accounting policies (continued)

Going concern (continued)

Company

The directors consider it appropriate to adopt the going concern basis of accounting in preparing the company 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 at least the next twelve months and the foreseeable future beyond that.

Basis of consolidation

The group financial statements consolidate the financial statements of Daiwater Investment Limited and its subsidiaries from the date of the acquisition of Affinity Water Acquisitions (Investments) Limited, 19 May 2017. The subsidiary companies have been included in the group financial statements using the acquisition method of accounting.

The purchase consideration has been allocated to the assets and liabilities on the basis of fair value at the date of acquisition.

The company was the parent undertaking of the largest group to prepare consolidated financial statements.

As permitted by Section 408 of the Companies Act 2006, the company's income statement has not been included in the financial statements. The parent company's profit (2022: profit) for the year has been included within the company's statement of financial position on page 63 by reference to a footnote.

Principles of consolidation

Subsidiaries are all entities over which the group has control. The group controls an entity when the group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity. Subsidiaries are fully consolidated from the date on which control is transferred. They are deconsolidated from the date that control ceases.

Intercompany transactions and balances between group companies are eliminated on consolidation.

Non-controlling interests in the results and equity of subsidiaries are shown separately in the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of financial position and consolidated statement of changes in equity respectively.

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

There are no amendments to accounting standards, or IFRIC interpretations that are effective for the year ended 31 March 2023 that have a material impact on the group's financial statements.

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 group, that will have a material effect on future years.

Daiwater Investment Limited

Notes to the financial statements - accounting policies (continued)

Critical accounting estimates

The preparation of financial statements in conformity with UK-adopted International Accounting Standards 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 group 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 group 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 2022 included a measured income accrual of £40,757,000. The value of billing recognised in the year ended 31 March 2023 for consumption in the prior year was £41,313,000.

This resulted in an increase of £556,000 in the current year's revenue due to the under-estimation of the prior year's revenue. This represented 0.17% of 2022/23 revenue.

Non-household wholesale revenue

The group 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 group has a right to receive the revenue. For non-household retailers, the amount of revenue which the group has a right to receive is determined by non-household consumption volume data provided by the market operator.

Loss allowance of trade receivables and contract assets

The group makes an estimate of the recoverable value of trade receivables and contract assets and records a loss allowance based on the age of the debt and experience (refer to note 12). This provision is based on, amongst other things, a consideration of actual collection history. At each reporting date, the group 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 and the ongoing energy crisis losses. 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. If the average of the 2021/22 and 2022/23 provision %'s were applied across each aged debt bracket, it would result in a reduction in the loss allowance for trade receivables and contract assets by £2,311,000 and corresponding increase in net assets. For comparison, if the average of the 2020/21 and 2021/22 provision %'s were applied across each aged debt bracket in the prior year, the equivalent sensitivity would have resulted in a £188,000 reduction in the loss allowance for trade receivables and contract assets and corresponding increase in net assets in the prior year.

Daiwater Investment Limited

Notes to the financial statements - accounting policies (continued)

Critical accounting estimates (continued)

Defined benefit pension plan

The group 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.

Impairment of goodwill and the water licence

Determining whether goodwill and the water licence have been impaired requires an estimation of Affinity Water Limited's, the group's main cash generating unit (CGU) constituting the smallest identifiable group of assets that generate cash flows for the group for which the carrying amount of the goodwill and water licence are allocated to, fair value less transaction costs. This fair value has been determined using a discounted cash flow, developed from a detailed business forecast, and applying a terminal value, in addition to an estimate of costs of disposal based on transaction costs paid on acquisition of the group in May 2017. No impairment to goodwill (2022: £nil) has been recognised in the year ended 31 March 2023 (refer to note 8). A 1% decrease in this fair value would lead to a £nil increase to the impairment as at 31 March 2023 (2022: £nil increase) as the fair value sufficiently exceeds the value on acquisition. The fair value would need to decrease by 24% as at 31 March 2023 (2022: 8%) before the value on acquisition exceeded the fair value and an impairment would be necessary. No impairment to the water licence has been recognised in the year ended 31 March 2023 (2022: £nil) (refer to note 8). A 1% impairment of the water licence would result in a charge of £3,008,000 (2022: £3,008,000) and a corresponding reduction in net assets.

Impairment of investment in subsidiary

Determining whether the company's investment in its subsidiary has been impaired requires an estimation of the investment's value in use. The value in use calculation uses an estimate of the enterprise value of Affinity Water Limited, the principal trading direct subsidiary of the company, which is based on its regulatory capital value at the year-end and market premiums paid for UK water supply companies. The carrying amount of investments in subsidiaries at the date of the statement of financial position was £754,027,000 (2022: £754,027,000) with no impairment losses recognised in either 2023 or 2022. If the value in use of Affinity Water Limited were to drop by 10%, an impairment charge of £nil (2022: £nil) would be recognised as the estimated enterprise value would still exceed the carrying amount of the investment.

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 group's dedicated asset management teams and the group's plans to achieve Net Zero carbon emissions by 2030. 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.

Daiwater Investment Limited

Notes to the financial statements – accounting policies (continued)

Critical accounting estimates (continued)

Useful economic lives of property, plant and equipment (continued)

Based on the current useful lives, the carrying amount of property, plant and equipment is £1,748,160,000 at 31 March 2023 (2022: £1,707,172,000). If the useful lives of the assets were 10% shorter, the carrying amount would instead be £ 1,426,248,000 (2022: £1,397,632,000) and if they were 10% longer, the carrying amount would be £2,070,072,000 (2022: £2,016,713,000).

Based on the current useful lives, the carrying amount of intangible assets, excluding goodwill, at 31 March 2023 is £328,457,000 (2022: £329,958,000). If the useful lives of the assets were 10% shorter, the carrying amount would instead be £325,812,000 (2022: £326,634,000) and if they were 10% longer, the carrying amount would be £331,102,000 (2022: £333,281,000).

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.

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 group's accounting policies. The areas involving a higher degree of judgement or complexity are disclosed below.

Revenue recognition

IFRS 15: 'Revenue from contracts with customers' (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 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 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 group 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. The company is seeing increased enhancement and maintenance expenditure due to an increase in extreme weather events arising due to climate change. Refer to note 6 for the carrying amount of property, plant and equipment.

Daiwater Investment Limited

Notes to the financial statements - accounting policies (continued)

Capital risk management policy

The group's capital structure comprises borrowings, derivatives, debentures, cash and liquid resources. Refer to notes 17 and 14 for more details. The main purpose of these financial instruments is to provide finance for the group's operations. The group finances its operations through a mixture of retained profits, borrowings from its subsidiary companies and debentures.

It is the group'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 group's financial instruments are liquidity risk, credit risk, and interest rate and inflation risk. Refer to note A4 for more details.

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 group 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. Management has considered the useful economic lives of assets impacted by climate change and environmental regulation and has considered whether any impairment has arisen as a result of climate change. There has been no revaluation of assets or change in the assessment of assets' useful economic lives during 2022/23 as a result of this review

The group 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. Updates on the proceeds and impact of the Green Funding can be found on our website at affinitywater.co.uk/corporate/investors/library

Daiwater Investment Limited

Notes to the financial statements

1. Revenue

1.1 Disaggregation of revenue from contracts with customers

	2023 £000	2022 £000
Timing of revenue recognition – at a point in time		
Unmeasured supplies	95,859	100,115
Measured supplies	160,210	155,232
Non-household wholesale revenue	54,028	51,111
Connection charges	9,628	7,989
	319,725	314,447
Timing of revenue recognition – over time		
Requisitioned mains/extensions	556	573
Diversions	1,821	3,382
Infrastructure charges	1,178	1,145
Other	63	200
	3,618	5,300
	323,343	319,747

All revenue is derived in the United Kingdom.

1.2 Assets and liabilities related to contracts with customers

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

	2023 £000	2022 £000
Net trade receivables	36,839	33,480
Contract assets		
Unbilled accrual for metered customers – household customers	39,516	40,847
Unbilled accrual for metered customers – non-household customers	3,928	3,506
Contract liabilities		
Payments received in advance – household water supplies	48,500	46,746
Payments received in advance – non-household water supplies	591	-
Deferred income – water supplies	76	207
Deferred income – other	506	622
Deferred grants and contributions	269,039	252,772
Payments received in advance – grants and contributions	15,104	27,023

‘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.

Daiwater Investment Limited

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 2023, the group had been reimbursed £157,631,000 (2022: £154,187,000) for its costs incurred in relation to the HS2 rail project, which will cross the Affinity Water supply area. This project is near completion and the group does not expect to incur significant costs for this in future periods. During the year, in line with the group's accounting policy for grants and contributions received in respect of property, plant and equipment, which include contributions received for diversions, £16,364,000 (2022: £98,478,000) 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 2023, £1,348,000 (2022: £14,268,000) 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 group 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 group discloses this as a contract asset in the statement of financial position (see table on the previous page). Where the group has not provided the service before payment is due, deferred income is recognised and the group 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 group's charging scheme and tariff documents, irrespective of usage. If the payments received exceed the amount the group has the right to receive, the group 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 group recognises deferred income in relation to these accounts and presents this as a contract liability within trade and other payables. Where the group has not provided the service before payment is due, deferred income is recognised and the group 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 group. The group 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 group does not incur any costs to obtain or fulfil contracts that would be recognised as an asset under IFRS 15.

Daiwater Investment Limited

Notes to the financial statements (continued)

1. Revenue (continued)

1.2 Assets and liabilities related to contracts with customers (continued)

Revenue recognised in relation to contract liabilities

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

	2023	2022
	£000	£000
Revenue recognised that was included in the contract liability balance at the beginning of the year		
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	1,091	775
Deferred grants and contributions	3,619	5,300
Payments received in advance – grants and contributions	11,924	7,585
Revenue recognised from performance obligations satisfied in previous years		
Unbilled accrual for metered customers – household customers	-	-

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 group has applied the practical expedient, set out in paragraph 121(a) of IFRS 15, not to disclose the 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 group deems it reasonable to conclude that the measured income accrual is materially correct.

At 31 March 2023, £269,039,000 (2022: £252,772,000) of grants and contributions is expected to be derived from performance obligations which were unsatisfied at the end of the financial year.

Daiwater Investment Limited

Notes to the financial statements (continued)

2. Operating profit/(loss)

2.1 Operating costs

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

	2023	2022
	£000	£000
Staff costs (note 3.1)	55,549	55,367
Energy costs	41,096	35,937
Profit on disposal of property, plant and equipment	(535)	(244)
Loss on disposal of infrastructure assets	890	728
Purchase of bulk water and water supplied under statutory entitlement	11,723	8,440
Water abstraction charges	6,349	4,201
Business rates	15,547	15,551
Chargeable services direct expenditure	(57)	72
Depreciation of infrastructure assets (note 6)	17,430	12,286
Depreciation of other property, plant and equipment (note 6)	55,008	49,704
Depreciation of right-of-use assets (note 7)	3,458	3,763
Amortisation of intangible assets (note 8)	6,800	17,686
Impairment of trade receivables and contract assets (note 12)	10,779	9,389
Research and development	196	133
Short-term lease rentals	24	37
Low-value lease rentals	76	129
Auditors' remuneration (note 2.3)	550	457
Cost of inventories used	1,203	1,334

2.2 Other operating income

	2023	2022
	£000	£000
Timing of revenue recognition – at a point in time		
Commission and rentals	21,929	18,972

The majority of other income relates to commission earned by Affinity Water Limited 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 25).

Daiwater Investment Limited

Notes to the financial statements (continued)

2. Operating profit/(loss) (continued)

2.3 Auditors' remuneration

During the year, the group obtained the following services from its Auditors and their associates:

	2023	2022
	£000	£000
Fees payable to the company's auditors and their associates for the audit of the parent company and consolidated financial statements	22	20
<i>Fees payable to the company's auditors and their associates for other services:</i>		
Audit of the company's subsidiaries	391	313
Audit-related assurance services		
– regulatory reporting	64	61
– Thames Water and Anglian Water annual returns	8	10
– audit related assurance service - other	64	47
Other non-audit services	1	6
Total Auditors' remuneration	550	457

3. Employees

3.1 Employee benefit expense (including Executive directors)

Group

	2023	2022
	£000	£000
Wages and salaries	64,638	62,408
Social security costs	7,160	6,667
Other pension costs	9,476	8,399
Staff costs	81,274	77,474
Staff costs capitalised	(25,725)	(22,107)
Staff costs recognised in the consolidated income statement	55,549	55,367

Daiwater Investment Limited

Notes to the financial statements (continued)

3. Employees (continued)

3.2 Average number of people employed

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

By activity	2023 Number	2022 Number
Operations	875	854
Customer service	250	257
Administration	251	262
	1,376	1,373

The company had no employees during the current year or prior year.

3.3 Directors' remuneration

The disclosure is provided in respect of the directors of Daiwater Investment Limited and their services in respect of the Daiwater Investment Limited group.

All the directors who sat on the Board of Daiwater Investment Limited 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 remuneration from the company, or any company within the group of companies headed by Daiwater Investment Limited. None of the directors of the company participate in the group's pension plans. The company does not have any listed shares and so the directors have not been offered any share incentives.

3.4 Key management personnel compensation

	2023 £000	2022 £000
Short-term employee benefits	736	1,734
Post-employment benefits	30	105
	766	1,839

Key management personnel are considered to be directors of group companies who do not sit on the Board of the company. Only executive directors and independent non-executive directors of Affinity Water Limited receive remuneration for their services as directors. Further information can be found within the remuneration report of Affinity Water Limited's Annual Report and Financial Statements for the year ended 31 March 2023 on its website: affinitywater.co.uk/library.

Daiwater Investment Limited

Notes to the financial statements (continued)

4. Finance income and costs

Group

	2023 £000	2022 £000
Finance income:		
Bank interest income	3,507	192
Net interest receivable on RPI linked inflation swap	6,745	7,434
Net interest receivable on CPI linked inflation swap	6,483	6,929
Fair value gains on bonds	22,215	22,905
Net income from post-employment benefits	2,839	1,488
	<u>41,789</u>	<u>38,948</u>
Finance costs:		
Accretion payable in respect of interest on bonds	(72,096)	(35,047)
Interest payable on bonds	(37,511)	(37,401)
Accretion payable on financial instrument	(59,114)	(29,574)
Interest payable on lease liabilities	(266)	(333)
Other	(3,548)	(2,140)
	<u>(172,535)</u>	<u>(104,495)</u>
Fair value gain/(loss) on financial instruments:		
Fair value gain/(loss) on swaps	49,755	(31,295)
	<u>49,755</u>	<u>(31,295)</u>
Net finance costs	<u>(80,991)</u>	<u>(96,842)</u>

Company

	2023 £000	2022 £000
Interest receivable from subsidiary undertakings	-	-
Total finance income	<u>-</u>	<u>-</u>

Daiwater Investment Limited

Notes to the financial statements (continued)

5. Income tax credit/(expense)

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

	2023 £000	2022 £000
<i>Current tax:</i>		
– UK corporation tax on losses for the year	3	-
– Adjustment in respect of prior years	-	-
Total current tax	3	-
<i>Deferred tax:</i>		
– Origination and reversal of temporary differences	8,266	7,109
– Impact of change in tax rate	2,610	(64,322)
– Adjustment in respect of prior years	(4,085)	2,449
Total deferred tax	6,791	(54,764)
Income tax credit/(expense)	6,794	(54,764)

Tax credit/(expense) assessed for the year is lower (2022: tax expense is higher) than the standard rate of corporation tax in the UK for the year ended 31 March 2023 of 19% (2022: 19%). The differences are explained below:

	2023 £000	2022 £000
Loss before tax	95,841	44,741
Tax calculated at the standard rate of tax in the UK of 19% (2022: 19%)	18,210	8,501
Tax effects of:		
– Adjustment in respect of prior years	(4,085)	2,449
– Other expenses not deductible for tax purposes	(379)	(23)
– Impact of change in tax rate on deferred tax	2,610	(64,322)
– Non-taxable income	-	123
– Derecognition of deferred tax	-	(1,027)
– Unrelieved tax losses carried forward	(9,562)	(465)
Income tax credit/(expense)	6,794	(54,764)

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

	2023 £000	2022 £000
Deferred tax:		
- Impact of change in tax rate on deferred tax	-	(1,725)
- Origination and reversal of temporary differences on retirement benefit surplus	13,029	(5,462)
	13,029	(7,187)

Daiwater Investment Limited

Notes to the financial statements (continued)

5. Income tax expense/(credit) (continued)

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

	2023 £000	2023 %	2022 £000	2022 %
Group loss before tax	(95,841)		(44,741)	
Tax on loss on ordinary activities at standard UK tax rate of 19% (2022: 19%)	(18,210)	19%	(8,501)	19%
Tax effect of:				
Depreciation in excess of capital allowances	12,693	(13%)	10,759	(23%)
Write down of fair value adjustment on acquisition of the Affinity Water Acquisitions (Investments) Limited group	(3,775)	4%	(2,821)	6%
Pension movements	(282)	0%	(183)	0%
Provisions movements	(49)	0%	(128)	0%
Expenses not deductible for tax purposes	64	0%	533	(1%)
Profit on sale of subsidiary	-	0%	(123)	0%
Unutilised tax losses carried forward	9,562	(10%)	465	(1%)
Adjustment in respect of prior years	-	0%	-	-
Reported current tax charge and effective rate	3	0%	1	0%
Depreciation in excess of capital allowances	16,282	(17%)	(11,258)	25%
Write down of fair value adjustment on acquisition of the Affinity Water Acquisitions (Investments) Limited group	(3,775)	4%	2,821	(6%)
Pension movements	(375)	0%	183	(0%)
Impact of change in tax rate on deferred tax	(1,192)	1%	64,321	(145%)
Provisions movements	(64)	(0%)	128	(0%)
Derecognition of deferred tax	-	0%	1,017	(2%)
Unutilised tax losses carried forward	-	0%	-	-
Adjustment in respect of prior years	(4,085)	4%	(2,449)	6%
Reported deferred tax charge and effective rate	6,791	(8%)	54,763	(122%)
Group tax charge and effective rate	6,794	(8%)	54,764	(122%)

Daiwater Investment Limited

Notes to the financial statements (continued)

5. Income tax (credit)/expense (continued)

5.4 Reconciliation of current and deferred tax charge (continued)

Impact of change in tax rate

In the 2021 Spring Budget the Government announced that from 1 April 2023 the Corporation Tax rate will increase to 25%. All significant adjustments to taxable profits for the year ended 31 March 2022 are timing differences. The impact on the tax charge in future years is reflected in the deferred tax account.

Depreciation in excess of capital allowances

The tax relief on our infrastructure assets is different from the depreciation of these assets in the financial statements (although over the total life of the assets the two amounts will be equal). In 2022/23, the amount written off for tax purposes was lower than the depreciation in the financial statements, resulting in a higher tax charge for the year.

Write down of fair value adjustment

The write down of the fair value adjustment in respect of the acquisition of the Affinity Water Acquisitions (Investments) Limited group relates to the gain on revaluation of the assets and liabilities of the companies acquired in 2017/18. It is an accounting adjustment and is not subject to corporation tax.

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 financial statements. In 2022/23, the amount paid into the pension plan was higher than the amount charged in the financial statements, resulting in a lower tax charge for the year.

Provisions movements

Some provisions charged in the financial statements are not deductible until the amounts provided are actually paid. Taxable profits in 2022/23 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.

Unutilised tax losses carried forward

Tax losses that could not be utilised in the year have been carried forward to be offset against future profits. The losses carried forward will reduce tax payable in future years.

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 2022 resulted in a lower tax charge, mainly as a result of claiming capital allowances.

Compliance with the group's tax strategy

All group companies were compliant with the group's published tax strategy during the year ended 31 March 2023. The tax strategy is published on Affinity Water Limited's website: affinitywater.co.uk/investors

Daiwater Investment Limited

Notes to the financial statements (continued)

6. Property, plant and equipment

Group

	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 2022	326,938	1,060,638	23,842	936,226	91,629	159,470	2,598,743
Restatement of opening balance	(1,699)	(100,194)	-	103,530	(1,637)	-	-
Additions	-	-	-	-	-	114,315	114,315
Transfers	2,697	47,849	-	55,405	29,234	(135,185)	-
Disposals	-	(671)	(331)	-	-	-	(1,002)
At 31 March 2023	327,936	1,007,622	23,511	1,095,161	119,226	138,600	2,712,056
Accumulated depreciation							
At 1 April 2022	(106,464)	(93,356)	(2,690)	(646,733)	(42,328)	-	(891,571)
Restatement of opening balance	10	5,693	-	(6,464)	761	-	-
Charge for the year	(5,040)	(17,108)	(322)	(43,299)	(6,669)	-	(72,438)
Transfers	-	-	-	-	-	-	-
Disposals	-	79	34	-	-	-	113
At 31 March 2023	(111,494)	(104,692)	(2,978)	(696,496)	(48,236)	-	(963,896)
Net book amount							
At 1 April 2022	220,474	967,282	21,152	289,493	49,301	159,470	1,707,172
Movement in year	(4,032)	(64,352)	(619)	109,172	21,689	(20,870)	40,988
At 31 March 2023	216,442	902,930	20,533	398,665	70,990	138,600	1,748,160

	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	325,476	946,679	23,846	924,212	84,157	160,059	2,464,429
Additions	-	-	-	-	-	136,043	136,043
Transfers	1,903	114,816	-	12,014	7,899	(136,632)	-
Disposals	(441)	(857)	(4)	-	(427)	-	(1,729)
At 31 March 2022	326,938	1,060,638	23,842	936,226	91,629	159,470	2,598,743
Accumulated depreciation							
At 1 April 2021	(101,802)	(81,483)	(2,360)	(606,591)	(37,865)	-	(830,101)
Charge for the year	(4,761)	(11,956)	(330)	(40,142)	(4,801)	-	(61,990)
Disposals	99	83	-	-	338	-	520
At 31 March 2022	(106,464)	(93,356)	(2,690)	(646,733)	(42,328)	-	(891,571)
Net book amount							
At 1 April 2021	223,674	865,196	21,486	317,621	46,292	160,059	1,634,328
Movement in year	(3,200)	102,086	(334)	(28,128)	3,009	(589)	72,844
At 31 March 2022	220,474	967,282	21,152	289,493	49,301	159,470	1,707,172

Assets were reclassified between land, buildings and operational structures, potable water distribution mains, fixed plant and vehicles and mobile plant in this statutory note, as shown in the line "Restatement of opening balance" within both cost and accumulated depreciation. This is a disclosure adjustment only with no impact on actual depreciation charged to date.

Daiwater Investment Limited

Notes to the financial statements (continued)

6. Property, plant and equipment (continued)

All land and buildings are held as freehold.

Company

The company does not have any property, plant or equipment.

7. Right-of-use assets

Group

	Buildings £000	Vehicles £000	Other £000	Total £000
Cost				
At 1 April 2022	9,079	10,084	-	19,163
Additions	-	1,685	-	1,685
Disposals	-	(680)	-	(680)
At 31 March 2023	9,079	11,089	-	20,168
Accumulated depreciation				
At 1 April 2022	(4,191)	(5,532)	-	(9,723)
Charge for the year	(1,396)	(2,062)	-	(3,458)
Disposals	-	662	-	662
At 31 March 2023	(5,587)	(6,932)	-	(12,519)
Net book amount				
At 1 April 2022	4,888	4,552	-	9,440
Movement in year	(1,396)	(395)	-	(1,791)
At 31 March 2023	3,492	4,157	-	7,649

	Buildings £000	Vehicles £000	Other £000	Total £000
Cost				
At 1 April 2021	10,180	7,521	402	18,103
Additions	-	3,660	-	3,660
Disposals	(1,101)	(1,097)	(402)	(2,600)
At 31 March 2022	9,079	10,084	-	19,163
Accumulated depreciation				
At 1 April 2021	(2,896)	(4,298)	(402)	(7,596)
Charge for the year	(1,479)	(2,284)	-	(3,763)
Disposals	184	1,050	402	1,636
At 31 March 2022	(4,191)	(5,532)	-	(9,723)
Net book amount				
At 1 April 2021	7,284	3,223	-	10,507
Movement in year	(2,396)	1,329	-	(1,067)
At 31 March 2022	4,888	4,552	-	9,440

Company

The company does not have any right-of-use assets.

Daiwater Investment Limited

Notes to the financial statements (continued)

8. Intangible assets

Group

	Goodwill	Billing relationships	Water licence	Computer software development costs	Total
	£000	£000	£000	£000	£000
Cost					
At 1 April 2022	317,006	32,789	300,800	95,571	746,166
Additions	-	-	-	5,299	5,299
Transfers	-	-	-	-	-
At 31 March 2023	317,006	32,789	300,800	100,870	751,465
Accumulated amortisation					
At 1 April 2022	-	(31,947)	-	(67,255)	(99,202)
Charge for the year	-	(842)	-	(5,958)	(6,800)
At 31 March 2023	-	(32,789)	-	(73,213)	(106,002)
Net book amount					
At 1 April 2022	317,006	842	300,800	28,316	646,964
Movement in year	-	(842)	-	(659)	(1,501)
At 31 March 2023	317,006	-	300,800	27,657	645,463

	Goodwill	Billing relationships	Water licence	Computer software development costs	Total
	£000	£000	£000	£000	£000
Cost					
At 1 April 2021	317,006	32,789	300,800	86,962	737,557
Additions	-	-	-	8,609	8,609
At 31 March 2022	317,006	32,789	300,800	95,571	746,166
Accumulated amortisation					
At 1 April 2021	-	(25,386)	-	(56,130)	(81,516)
Charge for the year	-	(6,561)	-	(11,125)	(17,686)
At 31 March 2022	-	(31,947)	-	(67,255)	(99,202)
Net book amount					
At 1 April 2021	317,006	7,403	300,800	30,832	656,041
Movement in year	-	(6,561)	-	(2,516)	(9,077)
At 31 March 2022	317,006	842	300,800	28,316	646,964

Daiwater Investment Limited

Notes to the financial statements (continued)

8. Intangible assets (continued)

Goodwill includes £447,036,000 arising on the acquisition of Affinity Water Acquisitions (Investments) Limited on 19 May 2017, with an impairment of £120,000,000 being recognised in 2018/19, and a £10,030,000 disposal of goodwill relating to Castle Water (Southern) Limited (formerly Affinity for Business (Retail) Limited) in 2020/21. Goodwill is reviewed at least annually for impairment and upon any indication of impairment.

The economic life of the water licence held by Affinity Water Limited has been determined to be indefinite, as the water licence is issued on a perpetual basis with a 25-year notice period. Therefore, the water licence is also reviewed at least annually for impairment and upon any indication of impairment.

No impairment to the water licence has been recognised in the year ended 31 March 2023 (2022: £nil).

Affinity Water Limited, the group's trading subsidiary, is the main cash generating unit (CGU). It constitutes the smallest identifiable group of assets that generate cash flows for the entity, by means of supplying drinking water to customers, for which the carrying amount of the goodwill and water licence are allocated to. The recoverable amount is based on the CGU's fair value less transaction costs, which has been determined using a discounted cash flow, developed from a detailed business forecast, and applying a terminal value, in addition to an estimate of costs of disposal based on transaction costs paid on acquisition of the group in May 2017. This approach has been used as it is an industry-recognised valuation methodology.

An estimate of the terminal value has been determined through an analysis of the current market conditions, taking a prudent approach, using recent transactions in the UK water industry, publicly available share price information for listed water supply companies, and consideration of Affinity Water Limited's risk profile compared to other companies in the sector. This is a subjective area and changes in the conditions for judgements used in estimating a reasonable market premium could significantly affect the assessed value of goodwill in future periods. A 1% decrease in this fair value would lead to a £nil increase to the impairment as at 31 March 2023 (2022: £nil increase) as the fair value sufficiently exceeds the value on acquisition. The fair value would need to decrease by 24% as at 31 March 2023 (2022: 8%) before the value on acquisition exceeded the fair value and an impairment would be necessary.

Included in the software asset category above is £14,419,000 (2022: £12,532,000) of capitalised intangible assets under construction, which is not amortised. £3,408,000 (2022: £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 2023 or 31 March 2022.

Company

The company does not have any intangible assets.

Daiwater Investment Limited

Notes to the financial statements (continued)

9. Investments

Group

	2023	2022
	£000	£000
Non-current assets		
Investments	51	51
Current assets		
Short-term deposits	66,709	70,179

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

Company

	2023	2022
	£000	£000
Investment in subsidiary	754,027	754,027

The investment balance in the company relates to Affinity Water Capital Funds Limited.

The shares of Affinity Water Capital Funds Limited were transferred to Daiwater Investment Limited from Affinity Water Acquisitions Limited on 3 October 2022 for a consideration of £301,413. An application was made to HMRC by Daiwater Investment Limited to claim relief from stamp duty under Section 42 of the Finance Act 1930 (as amended) on this share transfer. HMRC subsequently confirmed acceptance of the stamp duty relief claim.

Determining whether the company's investment in its subsidiary has been impaired requires an estimation of the investment's fair value less transaction costs. This has been determined using the RCV of Affinity Water Limited at 31 March 2023 (being the group's principal trading subsidiary), an estimate of the market premium that a private entity would pay for Affinity Water Limited and an estimate of costs of disposal based on transaction costs paid on acquisition of the group in May 2017. The fair value of remaining debt payments associated with Affinity Water Limited's debt at the year-end has been considered in the impairment assessment. The directors confirm that the carrying value of the investment as at 31 March 2023 and 31 March 2022 is supported by its underlying net assets and that the headroom is such that no reasonable change in any key assumptions is expected to result in impairment of the investment in subsidiary.

Daiwater Investment Limited

Notes to the financial statements (continued)

10. Retirement benefit surplus

Group

Defined benefit section

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

	2023	2022
	£000	£000
Current service cost	(3,236)	(4,061)
Pension expense charged to operating profit/(loss)	(3,236)	(4,061)
Net pension interest income credited to finance income (note 4)	2,839	1,488
Net pension expense charged before taxation	(397)	(2,573)

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

	2023	2022
	£000	£000
At 1 April	104,247	74,532
Employer contributions	1,879	3,539
Current service cost	(3,236)	(4,061)
Net interest income	2,839	1,488
Net re-measurement (loss)/gain	(52,114)	28,749
At 31 March	53,615	104,247

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

	2023	2022
	£000	£000
Re-measurement (losses)/gains on plan assets	(159,088)	8,249
Re-measurement gains on plan liabilities	106,974	20,500
	(52,114)	28,749

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

Company

The company does not have any retirement benefits.

Daiwater Investment Limited

Notes to the financial statements (continued)

11. Derivative financial instruments

Group	2023 £000	2022 £000
Non-current assets		
Fair value of energy swaps	3,283	7,342
Current assets		
Fair value of energy swaps	6,068	20,646
	<u>9,351</u>	<u>27,988</u>
Non-current liabilities		
Fair value of RPI linked inflation swaps	6,937	24,224
Accretion on RPI linked inflation swaps	55,062	23,702
Fair value of CPI linked inflation swaps	10,893	43,729
Accretion on CPI linked inflation swaps	42,953	15,163
Fair value of energy swaps	5,874	-
Fair value of interest swaps	264	-
Current liabilities		
Fair value of energy swaps	2,128	-
	<u>124,111</u>	<u>106,818</u>

A series of power hedging swaps were entered into between May 2021 and January 2023 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'.

In October 2022 the group entered into a swap agreement with nominal value £31,500,000, with effective date 30 September 2022. This transaction swapped interest payable at a SONIA linked floating rate for interest payable at a fixed rate for £31,500,000 of the £42,000,000 bank term loan with maturity 30 September 2024.

The fair value of the interest swaps have been derived from 'Level 2' fair value measurements: directly observable market inputs other than Level 1 inputs. The fair value of the interest swaps is calculated based on market expectations of the interest rate.

Daiwater Investment Limited

Notes to the financial statements (continued)

11. Derivative financial instruments (continued)

Company

The company does not have any derivative financial instruments.

12. Trade and other receivables

Group

	2023	2022
	£000	£000
Current:		
Trade receivables	73,807	66,517
Less: loss allowance for trade receivables	(36,968)	(33,037)
	36,839	33,480
Receivables transferred on sale of subsidiary	9,844	10,264
Less: loss allowance for receivables transferred on sale	(9,844)	(10,264)
	-	-
Interest receivable from external parties	7,404	7,786
Other receivables	8,025	8,385
Unbilled accrual for metered customers	43,444	44,353
Prepayments and accrued income	7,027	10,213
	65,900	70,737
	102,739	104,217

Trade receivables in Affinity Water Limited that were fully provided for were sold in both the current and prior year, resulting in a reduction to trade receivables of £4,397,000 (2022: £6,813,000) and a corresponding reduction in the loss allowance for trade receivables.

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

Daiwater Investment Limited

Notes to the financial statements (continued)

12. Trade and other receivables (continued)

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		Receivables transferred on sale of subsidiary		Unbilled accrual for metered customers		Total	
	2023 £000	2022 £000	2023 £000	2022 £000	2023 £000	2022 £000	2023 £000	2022 £000
At 1 April	33,037	34,027	10,264	8,319	101	51	43,402	42,397
Provision for receivables acquired during the year	-	-	-	-	-	-	-	-
Provision for receivables impairment charged/(credited) to the income statement	10,997	7,394	(420)	1,945	202	50	10,779	9,389
Sale of trade receivables that were fully provided for	(4,397)	(6,813)	-	-	-	-	(4,397)	(6,813)
Receivables written off during the year as uncollectable	(2,669)	(1,571)	-	-	-	-	(2,669)	(1,571)
At 31 March	36,968	33,037	9,844	10,264	303	101	47,115	43,402

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

In the current year, a charge of £10,779,000 to the income statement arose as a result of the ongoing cost of living crisis and a decline in cash collection rates seen in the year.

In the prior year, an additional charge of £1,413,000 to the income statement arose as a result of external economic factors which included the cost of living increases on our customers. This is included within the £9,389,000 total provision for receivables impairment charged to the income statement in the prior year.

12.2 Ageing analysis of trade receivables and receivables transferred on sale of subsidiary

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

	2023 £000	2022 £000
Aged less than one year	27,155	24,157
Aged between one year and two years	23,682	21,884
Aged greater than two years	22,970	30,740
	73,807	76,781

Company

The company does not have any trade or other receivables

Daiwater Investment Limited

Notes to the financial statements (continued)

13. Inventories

Group

	2023	2022
	£000	£000
Raw materials and consumables	4,833	4,348

Inventories are stated after provisions for impairment of £364,000 (2022: £364,000).

Company

The company does not have any inventories.

14. Cash and cash equivalents

Group

	2023	2022
	£000	£000
Cash at bank and in hand	28,170	49,279
Term deposits	61,684	101,125
	89,854	150,404

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

Company

	2023	2022
	£000	£000
Cash at bank and in hand	10	-

Daiwater Investment Limited

Notes to the financial statements (continued)

15. Share capital

Group and company

Allotted, called up and fully paid share capital	2023	2022
	£000	£000
744,133,355 (2022: 744,133,355) ordinary shares of £0.01 (2022: £0.01) each	7,441	7,441

The company was incorporated on 24 April 2017 with a share capital of 3 ordinary £1 shares. There was a further capital injection on 19 May 2017 for an amount of £744,133,352 upon the issuance of 272,070,036 Class B £1 shares, 199,993,280 Class C shares and 272,070,036 Class D £1 shares. On the same date the 3 original ordinary shares were converted into one Class B, one Class C and one Class D share.

Each share class rank pari passu on distribution of profits or capital. Voting rights for each share differs, with Class B carrying 0.92 votes, Class C carrying 1.24 votes and Class D carrying 0.91 votes at a general meeting and on a written resolution of the shareholders.

Allianz Capital Partners owned 272,070,037 of the above Class B shares, DIF owned 199,993,281 of the above Class C shares and HICL Infrastructure plc owned 272,070,037 of the above Class D shares.

On acquisition, each of the parties was granted an option to convert the voting rights attaching to Class B, C and D shares to Class A1, A2, and A3 shares. The option was exercised by Infrastructure Investments (Affinity) Limited via InfraRed Capital Partners Limited, the Investment Manager to HICL Infrastructure plc, on 7 January 2019 and the conversion occurred on 11 February 2019.

On 14 May 2019, InfraRed Capital Partners Limited triggered a further conversion right, which ultimately converted the Class A1, A2 and A3 shares to a single class of ordinary shares. The conversion to ordinary shares occurred on 12 June 2019, under which voting rights become proportional to the shareholders' economic interest.

In March 2021, the company effected a capital reduction by way of solvency statements, reducing the value of each share from £1 to £0.01, with the equity being transferred from share capital to retained earnings.

Daiwater Investment Limited

Notes to the financial statements (continued)

16. Trade and other payables

Group

	2023	2022
	£000	£000
Non-current		
<i>Amounts falling due after more than one year</i>		
Deferred grants and contributions	28,137	25,509
<i>Amounts falling due after more than five years</i>		
Deferred grants and contributions	233,937	221,565
	262,074	247,074
Current		
<i>Amounts falling due within one year</i>		
Trade payables	12,069	22,166
Interest payable to external parties	14,411	14,750
Social security and other taxes	1,847	1,796
Other payables	742	406
Capital accruals	13,519	21,587
Deferred grants and contributions	6,995	5,698
Payments received in advance	73,216	81,980
Deferred income	3,263	843
Other accruals	45,245	38,820
	171,307	188,046
	433,381	435,120

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

Company

The company does not have any trade and other payables.

Daiwater Investment Limited

Notes to the financial statements (continued)

17. Borrowings

Group

	2023	2022
	£000	£000
<i>Borrowings measured at amortised cost:</i>		
Bonds	1,538,786	1,505,072
Bank term loan	41,112	41,429
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
	1,579,932	1,546,535

Affinity Water Finance (2004) PLC

On 13 July 2004, Affinity Water Finance (2004) PLC, a subsidiary of the group, 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 issues and the tap issue were lent to Affinity Water Limited on the same terms.

Affinity Water Finance PLC

On 4 February 2013, the group'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%, £150,000,000 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 group's subsidiary Affinity Water Finance PLC.

Daiwater Investment Limited

Notes to the financial statements (continued)

17. Borrowings (continued)

Group (continued)

Affinity Water Finance PLC (continued)

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%, a Green bond used to fund expenditure outlined in the group's Green Finance Framework.

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

The £14,204,000 Class A Guaranteed Notes with coupon of 3.625% matured in September 2022. The group repaid this amount in full in September 2022.

Affinity Water Limited, a subsidiary of the group, 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 immediate parent undertaking of Affinity Water Limited.

The fair value of the bonds on-lent from the two financing subsidiaries at 31 March 2023 is £1,208,420,000 (2022: £1,560,813,000). 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.

Affinity Water Limited 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 Affinity Water Limited was not in breach of any financial covenants. See additional details on our financial covenants included within the going concern statement in accounting policies.

On 28 September 2017, Affinity Water Holdco Finance Limited borrowed £25,000,000 under a term loan facility with a commercial bank. The initial term of the loan was twelve months, which was subsequently extended to 30 June 2023. The proceeds of this loan were lent to Affinity Water Capital Funds Limited on the same terms. On 2 September 2022, Affinity Water Holdco Finance Limited refinanced its £42,000,000 bank term loan, extending the repayment date from 30 June 2023 to 2 September 2027, with an option to extend for a further two years. The facility also contains an uncommitted accordion feature to increase the loan size to £75,000,000.

On 2 September 2022, the company refinanced its £42,000,000 bank term loan, extending the repayment date from 30 June 2023 to 2 September 2027, with an option to extend for a further two years. The facility also contains an uncommitted accordion feature to increase the loan size to £75,000,000.

Company

The company does not have any borrowings.

Daiwater Investment Limited

Notes to the financial statements (continued)

18. Lease liabilities

Group

	2023 £000	2022 £000
Non-current:		
Lease liabilities	4,785	6,329
Current:		
Lease liabilities	3,053	3,317

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

	2023 £000	2022 £000
Depreciation charge of right-of-use assets (refer to note 7)	3,458	3,763
Interest expense on lease liabilities (refer to note 4)	266	333
Expense relating to short-term leases (refer to note 2.1)	24	37
Expense relating to leases of low-value assets (refer to note 2.1)	76	129
Principal elements of lease payments included within cash flows from financing activities	3,475	3,725
Interest payments included within cash flows from operating activities	266	333
Total cash outflow for leases in the statement of cash flows	3,741	4,058
Additions to right-of-use assets (refer to note 7)	1,685	3,660
Disposals of right-of-use-assets (refer to note 7)	(18)	(964)
Carrying amount of right-of-use assets (refer to note 7)	7,649	9,440

Company

The company does not have any lease liabilities.

Leasing arrangements

The investment properties are leased to tenants under operating leases with rentals payable monthly. Lease income from operating leases where the group is a lessor is recognised in income on a straight-line basis over the lease term. Lease payments for some contracts include CPI increases, but there are no other variable lease payments that depend on an index or rate.

Although the group is exposed to changes in the residual value at the end of the current leases, the group typically enters into new operating leases and therefore will not immediately realise any reduction in residual value at the end of these leases. Expectations about the future residual values are reflected in the fair value of the assets.

Minimum lease payments receivable on leases are as follows:

	2023 £000	2022 £000
Within 1 year	650	654
Between 1 and 2 years	625	643
Between 2 and 3 years	463	624
Between 3 and 4 years	423	463
Between 4 and 5 years	412	423
Later than 5 years	1,080	1,542
	3,653	4,349

Properties are held at cost in line with property, plant and equipment policy provided in note A3.

Daiwater Investment Limited

Notes to the financial statements (continued)

19. Deferred tax liabilities

19.1 Analysis of deferred tax assets and deferred tax liabilities

Group	2023 £000	2022 £000
<i>Deferred tax assets:</i>		
– Deferred tax asset to be recovered within 12 months	(5,569)	(5,764)
– Deferred tax asset to be recovered after more than 12 months	(47,876)	(53,199)
	<u>(53,445)</u>	<u>(58,963)</u>
<i>Deferred tax liabilities:</i>		
– Deferred tax liability to be settled within 12 months	372	587
– Deferred tax liability to be settled after more than 12 months	304,747	329,876
	<u>305,119</u>	<u>330,463</u>
Deferred tax liabilities - net	<u>251,674</u>	<u>271,500</u>

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

	£000
At 1 April 2021	209,548
Charged to the income statement (restated)	54,765
Charged to other comprehensive income	7,187
At 31 March 2022	<u>271,500</u>
Prior year adjustment	4,085
Impact of change in tax rate	1,192
Credited to the income statement	(12,074)
Credited to other comprehensive income	(13,029)
At 31 March 2023	<u>251,674</u>

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.

Daiwater Investment Limited

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

	Fair value adjustment on acquisition £000	Accelerated capital allowances £000	Retirement benefit obligations £000	Total £000
At 1 April 2021	76,247	169,447	14,161	259,855
Impact of change in tax rate (Credited)/charged to the income statement	23,595 (1,531)	50,350 (13,707)	6,255 184	80,200 (15,054)
Charged to other comprehensive income	-	-	5,462	5,462
At 31 March 2022	98,311	206,090	26,062	330,463
Impact of change in tax rate (Credited)/charged to the income statement	(141) (446)	- (12,099)	- 371	(141) (12,174)
(Credited) to other comprehensive income	-	-	(13,029)	(13,029)
At 31 March 2023	97,724	193,991	13,404	305,119

19.3 Deferred tax assets

	Fair value adjustment on acquisition £000	Provisions £000	Unrelieved tax losses £000	Total £000
At 1 April 2021	48,691	599	1,017	50,307
Impact of change in tax rate Credited/(charged) to the income statement	14,002 (4,352)	151 (128)	- (1,017)	14,153 (5,497)
At 31 March 2022	58,341	622	-	58,963
Impact of change in tax rate Credited/(charged) to the income statement	(1,333) (4,220)	- 35	- -	(1,333) (4,185)
At 31 March 2023	52,788	657	-	53,445

Deferred tax balances were recognised on the fair value adjustments made to the assets and liabilities acquired by the group on 19 May 2017.

At 31 March 2023, the group had unused tax losses of £9,562,000 (2022: £7,798,000) available for offset against future profits. No deferred tax asset has been recognised in respect of these losses due to restrictions over accessing these losses in the future.

Company

The company does not have any deferred tax assets or liabilities.

Daiwater Investment Limited

Notes to the financial statements (continued)

20. Provisions for other liabilities and charges

Group	Insurance £000	Reorganisation £000	Tax £000	Other £000	Total £000
At 1 April 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
Charged to the income statement	464	-	4,100	-	4,564
Utilised in the year	(252)	-	-	-	(252)
At 31 March 2023	2,649	-	4,100	670	7,419

Insurance

Provisions for insurance represent the amount of the group'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 £2,649,000 is presented as a non-current liability in the statement of financial position.

Reorganisation

In the prior year, a provision in relation to a corporate reorganisation was charged and utilised in the income statement. A provision of £178,000 remaining from a previous reorganisation was also utilised in the prior year.

Tax provision

A tax provision of £4,100,000 (2022: £nil) has been charged to the income statement. As at 31 March 2023, this is an estimate of an outstanding charge relating to a potential PAYE and NI claim.

Other provisions

Other provisions of £670,000 (2022: £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 group's consolidated statement of financial position.

Company

The company does not have any provision for liabilities and other charges.

Daiwater Investment Limited

Notes to the financial statements (continued)

21. Dividends

	2023 £000	2022 £000
First interim dividend paid of nil per share (2022: nil per share)	95	91
	<u>95</u>	<u>91</u>

Dividends of £95,000 (2022: £91,000) were paid to non-controlling interest from group subsidiaries.

22. Notes to the statement of cash flows

22.1 Cash generated from operations

Group

	2023 £000	2022 £000
Loss before tax from:		
Continuing operations	<u>(95,841)</u>	(44,741)
Loss before tax including discontinued operations	<u>(95,841)</u>	(44,741)
<i>Adjustments for:</i>		
Depreciation of property, plant and equipment (note 6)	72,438	61,990
Amortisation of grants and contributions	(3,619)	(5,300)
Depreciation of right-to-use assets (note 7)	3,458	3,763
Amortisation of intangible fixed assets (note 8)	6,800	17,686
Profit on disposal of property, plant and equipment	(535)	(244)
Profit on disposal of trading subsidiary	-	-
Loss on disposal of infrastructure assets	888	728
Post-employment benefits	1,360	522
Net finance costs (note 4)	80,991	96,842
Net gain on energy swaps	26,638	(27,988)
Changes in working capital		
– Inventories	(485)	(268)
– Trade and other receivables	1,435	(7,931)
– Trade and other payables		
– provision element	4,312	(467)
– other	402	7,916
Cash generated from operations	<u>98,242</u>	<u>102,508</u>

Company

	2023 £000	2022 £000
Profit before tax	<u>-</u>	<u>-</u>
<i>Adjustments for:</i>		
Changes in working capital		
– Trade and other receivables	10	-
Cash used in operations	<u>10</u>	<u>-</u>

Daiwater Investment Limited

Notes to the financial statements (continued)

23. Notes to the statement of cash flows (continued)

23.1 Reconciliation of liabilities arising from financing activities

Group

	At 1 April 2022	Cash flow	Non-cash flows	At 31 March 2023
	£000	£000	£000	£000
Bonds	1,505,072	(14,204)	47,918	1,538,786
Bank term loan	41,429	-	(317)	41,112
Lease liabilities	9,646	(3,741)	1,933	7,838
Debenture stock	34	-	-	34
Total liabilities arising from financing activities	1,556,181	(17,945)	49,534	1,587,770

	At 1 April 2021	Cash flow	Non-cash flows	At 31 March 2022
	£000	£000	£000	£000
Bonds	1,347,268	146,994	10,810	1,505,072
Bank term loan	40,973	-	456	41,429
Lease liabilities	10,692	(4,058)	3,012	9,646
Debenture stock	34	-	-	34
Total liabilities arising from financing activities	1,398,967	142,936	14,278	1,556,181

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

Company

The company has no liabilities arising from financing activities.

Daiwater Investment Limited

Notes to the financial statements (continued)

24. Commitments

24.1 Capital commitments

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

Group	2023	2022
	£000	£000
Property, plant and equipment	28,481	31,985
Intangible assets	885	2,069
	29,366	34,054

Company

The company does not have any capital commitments.

24.2 Commitments under leases

The group leases two buildings and most of its vehicles under non-cancellable operating leases expiring within a maximum of five years. The leases have varying terms, clauses and renewal rights. The group also leased IT server space until 31 December 2021.

The group does not expect to extend any vehicles leases after their lease term has expired. The lease of the head office building will expire in September 2025. The group will assess closer to the expiry of the lease of the buildings whether further formal agreements will be entered in to.

From 1 April 2019, the group 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:

Group	2023	2022
	£000	£000
No later than one year	59	76
Later than one year and no later than five years	39	98
	98	174

Company

The company does not have any commitments under operating leases.

Daiwater Investment Limited

Notes to the financial statements (continued)

25. Billing on behalf of Thames Water and Anglian Water

The group's principal trading subsidiary, Affinity Water Limited, 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 2023 (2022: £nil), and the group incurs no bad debt risk in relation to this service.

26. Events after the reporting financial year

Martin Roughead was appointed to the board as Chief Financial Officer on 17 April 2023.

Patrick Makoni was appointed as Secretary on 3 April 2023.

27. Ultimate parent company and controlling party

Daiwater Investment Limited, a company registered in England and Wales, is the parent undertaking of the largest group to consolidate the statutory financial statements of this group for the year ended 31 March 2023, and only group to consolidate the company.

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 (up until 1 July 2020, InfraRed Capital Partners (Management) LLP).

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.

Daiwater Investment Limited

Notes to the financial statements – appendices

A1. General information

The group owns and manages the water assets and network in an area of approximately 4,500km² split over three supply regions, comprising eight separate water resource zones, in the South East of England. Affinity Water Limited, the group's principal trading indirect subsidiary, is the sole supplier of drinking water in these areas.

The company manages an investment in Affinity Water Capital Funds Limited.

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 27 for details of the company's controlling company.

A2. Segmental reporting

In the same way that financial information is reported on a quarterly basis to the Board, the group's chief operating decision maker, during the current and previous financial year on a combined basis, the group and company present their results under a single segment for financial reporting purposes. Management do not consider climate change to have had an impact on reporting results under a single segment.

A3. Accounting policies

Property, plant and equipment

Property, plant and equipment are held at the fair value on acquisition on 19 May 2017 less accumulated depreciation and impairment charges.

Infrastructure assets comprise a network of mains and associated underground pipework. Infrastructure assets are held at deemed cost established through an event-driven valuation on acquisition by Daiwater Investment Limited 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 group'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 group. 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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

Property, plant and equipment (continued)

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	3-15 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 group 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.

Goodwill

Goodwill represents the excess of the fair value of purchase consideration over the fair value of the net assets of the subsidiary 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.

Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

Intangible assets

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 group 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.

Water licence

The remaining economic life of the water licence has been determined to be indefinite, as the water licence is issued on a perpetual basis with a 25-year notice period.

Billing relationships

A remaining economic life of five years has been determined for the billing relationships based on the length of the revenue stream forecast used in calculating the fair value of the billing relationships on acquisition. Amortisation charged is recognised in the income statement in operating costs.

Impairment

Intangible assets are reviewed for impairment where indicators of impairment exist. Impairments are recognised immediately in the income statement.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

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 group 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 group 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 group 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 group under the Water Industry Act 1991 would seem to constitute a legally enforceable contract based on the transaction prices set out in the group's charges scheme, tariff documents and invoices; accordingly, these grants and contributions fall within the scope of IFRS 15.

Investments

The company's investments 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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

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 group takes into consideration any significant economic changes that may impact its credit loss model and future credit losses, for example the increased cost of living and energy crisis currently impacting its customers. To estimate the impairment to its trade receivables from either of these factors, the group has assessed its receivables based on postcode driven customer demographics. The group 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 group applies the IFRS 9: 'Financial Instruments' (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 group 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.

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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

Current and deferred tax

The tax credit for the year (and expense in the prior 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 credit 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 group'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 group 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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

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 date. 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 consolidated income statement. Interest received or incurred on these derivative financial instruments is shown within finance income and finance costs on the face of the consolidated income statement.

The fair value of derivative financial instruments 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 principal trading subsidiary of the group, consistent with IFRS 13: 'Fair value measurement'.

Provisions

A provision is recognised when the group 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 the principal trading subsidiary's operational performance against agreed performance commitments. Certain performance commitments contain an Outcome Delivery Incentive, which can carry a financial reward or penalty, or both, which will be recognised as a revenue adjustment in the next charging period. The principal trading subsidiary 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 group 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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

Revenue recognition

The group'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 group on behalf of customers by granting the group 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 group has a right to receive is variable, determined by the volume of water consumed; and
- for unmetered customers, the amount which the group 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 group.

The group 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 group has a right to receive the revenue. For non-household retailers, the amount which the group has a right to receive is determined by non-household consumption volume data provided by the market operator.

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 group 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 group's charging scheme and tariff documents. If the payments received exceed the amount the group has the right to receive (i.e., unearned income), the group 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 recognises deferred income in relation to these accounts 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 group 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 group may provide water services to customers who are unlikely to pay for these services. The group does not recognise revenue where historical evidence indicates that the group will probably never be able to collect the revenue billed.

The group 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 group therefore does not adjust any of its transaction prices for the time value of money.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

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 most 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).

Leases

The group leases one building, and most of its vehicles. Rental contracts for vehicles are typically for fixed periods of two to five years. The group 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 building has a remaining period of 2.5 years. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The group's lease agreements do not impose any covenants, but leased assets cannot be used as security for borrowing purposes.

The group 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. 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 group 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 group. 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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

Leases (continued)

The group'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 group 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 group to be part of the overall compensation package of an employee and, as such, the group 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 group does not use sale and leaseback transactions.

The Group as a lessor

The investment properties are leased to tenants under operating leases with rentals payable monthly. Lease income from operating leases where the group is a lessor is recognised in income on a straight-line basis over the lease term.

Lease payments for some contracts include CPI increases, but there are no other variable lease payments that depend on an index or rate.

Although the group is exposed to changes in the residual value at the end of the current leases, the group typically enters into new operating leases and therefore will not immediately realise any reduction in residual value at the end of these leases. Expectations about the future residual values are reflected in the fair value of the assets.

Grafham reservoir

Under the Great Ouse Water Act of 1961, the group has an entitlement to water from the Grafham reservoir owned and operated by Anglian Water Services Limited (Anglian Water'). The group 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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A3. Accounting policies (continued)

Retirement benefits

The group operates a pension plan, the Affinity Water Pension Plan (AWPP) providing defined benefits based on final pensionable salary. The assets of the plan are held separately from those of the group. The plan's corporate trustee is a subsidiary of the group.

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 group bears all the risks and rewards associated with the scheme and therefore recognises all the remeasurement gains and losses on the plan assets and liabilities.

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.

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 group 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.

Dividend distributions

Dividend distributions to the group's shareholders are recognised as a liability in the group's financial statements in the year in which the dividends are approved, until they are paid.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management

Risk management

The group'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 group's operations. The group finances its operations through a mixture of retained profits, borrowings from its subsidiary companies and debentures.

It is the group'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 group'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 group of companies headed by Daiwater Investment Limited.

The Board reviews and agrees policies for managing each of these risks (refer to page 5 of the strategic report 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 group's position in regard to debt and cash at the end of each quarter.

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

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Liquidity risk

Group

The objective of the group's liquidity risk management policy is to ensure that the group 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 group's treasury function and reported to the relevant company's Board on a quarterly basis through the treasury report.

At 31 March 2022, the group had £308,563,000 (2022: £375,583,000) of available liquidity, which comprised £156,563,000 (2022: £220,583,000) of cash and term deposits and £152,000,000 (2022: £155,000,000) of undrawn committed borrowing facilities.

The group 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 £209,145,000 (2022: £110,163,000), 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.

In October 2022 the company also entered into a swap agreement with nominal value £31,500,000, with effective date 30 September 2022. This transaction swapped interest payable at a SONIA linked floating rate for interest payable at a fixed rate for £31,500,000 of the £42,000,000 bank term loan with maturity 30 September 2024.

Undrawn borrowing facilities:

	2023	2022
	£000	£000
<i>Floating rate:</i>		
– Expiring within one year	52,000	55,000
– Expiring in more than one year	100,000	100,000
	152,000	155,000

The facilities expiring within one year comprise two standby facilities with one counterparty (2022: two counterparties) in the event of a liquidity shortfall: a 364 day revolving Debt Service Reserve Facility of £27,000,000 (2022: £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 £25,000,000 (2022: £23,000,000), which is intended for the purpose of funding operating and capital maintenance expenditure.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Liquidity risk (continued)

Group (continued)

The facilities expiring in more than one year comprise two revolving credit facilities, £60,000,000 (2022: £60,000,000) provided by Barclays Bank PLC and £40,000,000 (2022: £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.

The facility, expiring in 2027 with the option to extend to 2029, comprises of a committed lending of £42m, which is fully drawn, and a further £33m uncommitted accordion facility. The facility is provided by ING Bank N.V. with HSBC Bank Plc acting as agent. The purpose of this facility is to fund operations outside of the ringfenced entity. The facility references SONIA.

Company

At 31 March 2023 and 31 March 2022, the company had no available liquidity and no available undrawn borrowing facilities.

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 group's non-derivative financial liabilities (borrowings and lease liabilities) with agreed repayment periods on an undiscounted basis.

Group

At 31 March 2023	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
Non-derivatives							
Bonds	39,751	39,980	40,225	290,468	26,030	1,331,002	1,767,456
Bank term loan	3,804	3,737	3,601	3,484	43,693	-	58,319
Lease liabilities	3,238	2,857	1,541	501	131	1	8,269
	46,793	46,574	45,367	294,453	69,854	1,331,003	1,834,044
At 31 March 2022	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
Non-derivatives							
Bonds	53,017	38,836	39,004	39,176	289,348	1,262,651	1,722,032
Bank term loan	697	42,172	-	-	-	-	42,869
Lease liabilities	3,545	2,849	2,469	1,161	170	1	10,195
	57,259	83,857	41,473	40,337	289,518	1,262,652	1,775,096

On 2 September 2022, Affinity Water Holdco Finance Limited refinanced its £42,000,000 bank term loan, extending the repayment date from 30 June 2023 to 2 September 2027, with an option to extend for a further two years. The facility also contains an uncommitted accordion feature to increase the loan size to £75,000,000.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Liquidity risk (continued)

Maturity analysis (continued)

Covenant risk

The group's compliance with its lending covenants is a risk. Both an ICR Trigger and Default Event would occur in a number of severe but plausible downside scenarios detailed in the principal trading subsidiary's viability statement for the year ended 31 March 2023. However this is on the assumption that no mitigating actions would be taken. Management are confident that mitigation actions within their control could be implemented that would prevent a trigger or default event from occurring should one of these scenarios arise. The group is able to withstand the financial impacts of a severe but plausible downside scenario without the occurrence of an Event of Default under its borrowing covenants. However, an ICR Trigger Event would occur in the severe but plausible downside scenario (excluding any mitigating action).

Under an ICR Trigger Event, the group would be subject to certain constraints such as restrictions on dividends and restriction on debt buybacks. However, the directors are satisfied that an ICR Trigger Event would not fundamentally constrain the group's ability to carry out its business, particularly after considering the group's strong cash position meaning that the group has no further funding requirement in AMP7. The group continues to monitor and manage the risks associated with the ICR covenant through the forecasting and reporting process and has identified mitigations, the most prominent of which are working capital management, operating expenditure reviews and fixing energy transactions. The group was not in breach of its financial covenants as at 31 March 2023 or up to the date of signing these financial statements.

Company

The company has no non-derivative financial liabilities.

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

Group

At 31 March 2023	1 year or less	1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years	Total
	£000	£000	£000	£000	£000	£000	£000
Derivatives							
RPI linked inflation swaps net payment/ (receivable)	(6,427)	(6,249)	(6,067)	81,592	-	-	62,849
CPI linked inflation swaps net payment/ (receivable)	(6,486)	(6,390)	(6,293)	(6,194)	(3,037)	88,196	59,796
SONIA to fixed interest rate swap net payment/ (receivable)	(338)	(144)	-	-	-	-	(482)
Total derivatives	(13,251)	(12,783)	(12,360)	75,398	(3,037)	88,196	122,163

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Liquidity risk (continued)

Maturity analysis (continued)

At 31 March 2022	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
Derivatives							
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	<u>(14,006)</u>	<u>(13,848)</u>	<u>(13,686)</u>	<u>(13,523)</u>	<u>31,752</u>	<u>24,484</u>	<u>1,173</u>

Company

The company has no derivative instruments.

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 group 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 group has therefore concluded that expected loss rates for trade receivables are a reasonable approximation for loss rates for contract assets.

The group 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 group'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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Credit risk (continued)

Contract assets and trade and other receivables (continued)

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 group'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 group 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 group takes into consideration any significant economic changes that may impact its credit loss model and future credit losses, for example the increased cost of living currently impacting the group's customers and the current energy crisis.

Amounts are also written off on accounts where the group 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 group's write-off policy on household receivables has remained unchanged and has been consistently applied in the current year compared with the previous year.

Since 1 April 2017, the group 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 group 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 group takes into consideration any significant economic changes that may impact the recoverability of these receivables and future credit losses.

The group has concluded that, given the nature of its financing arrangements, the procedure currently in place to assess the impairment of financial instruments detailed above is deemed sufficient under the expected credit loss model; historical recoverability of trade receivables has shown to be a good indicator of future expected losses, both in the next 12 months and across the lifetime of the instrument.

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 group 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 2023 and 31 March 2022 was determined as follows for trade receivables, receivables transferred upon sale of subsidiary and contract assets (unbilled accrual for metered customers):

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Credit risk (continued)

Contract assets and trade and other receivables (continued)

Group

At 31 March 2023 (£000)	Current	Current	Less than 1 year	1 – 2 years	2 – 3 years	3 – 4 years	More than 4 years past due	Total
Expected loss rate – metered household receivables	0.76%	0.00%	7%	27%	45%	64%	100%	
Gross carrying amount – metered household receivables	-	-	19,930	4,706	2,530	1,579	2,202	30,947
Gross carrying amount – unbilled accrual for metered customers (household)	39,819	-	-	-	-	-	-	39,819
Gross carrying amount – unbilled accrual for metered customers (non-household)	-	3,927	-	-	-	-	-	3,927
Provision at expected loss rate	303	-	1,339	1,262	1,149	1,002	2,202	7,257
Amounts provided at 100%	-	-	1,970	4,075	2,973	2,214	2,923	14,155
Loss allowance	303	-	3,309	5,337	4,122	3,216	5,125	21,412
Expected loss rate – unmetered household receivables		0.00%	17%	37%	56%	68%	100%	
Gross carrying amount – unmetered household receivables		-	7,588	3,202	1,901	1,385	1,792	15,868
Provision at expected loss rate		-	1,253	1,194	1,066	945	1,792	6,250
Amounts provided at 100%		-	1,100	845	2,043	1,787	2,464	8,239
Loss allowance		-	2,353	2,039	3,109	2,732	4,256	14,489
Expected loss rate – non-household receivables				0%	0%	0%	100%	
Gross carrying amount – non-household receivables				-	-	-	9,844	9,844
Loss allowance				-	-	-	9,844	9,844
Expected loss rate – developer services			0.00%	30%	41%	21%	46%	
Gross carrying amount – developer services			1,102	220	223	804	2,250	4,599
Loss allowance			-	67	91	170	1,042	1,370
								<u>47,115</u>

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Credit risk (continued)

Contract assets and trade and other receivables (continued)

At 31 March 2022 (£000)	Current	Current	Less than 1 year	1 – 2 years	2 – 3 years	3 – 4 years	More than 4 years past due	Total
Expected loss rate – metered household receivables	0.28%	0%	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	Less than 1 year	1 – 2 years	2 – 3 years	3 – 4 years	More than 4 years past due	Total
Expected loss rate – unmetered household receivables		0%	3%	7%	17%	42%	100%	
Gross carrying amount – unmetered household receivables		-	6,453	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%		-	332	2,559	2,377	1,854	2,405	9,527
Loss allowance		-	1,364	2,750	2,667	2,305	3,959	13,045
					Less than 1 year	1-2 years	More than 2 years past due	Total
Expected loss rate – non-household receivables					0%	0%	100%	
Gross carrying amount – non-household receivables					-	-	10,264	10,264
Loss allowance					-	-	10,264	10,264
			Less than 3 months	3 – 6 months	6 – 9 months	9 – 12 months	More than 12 months past due	Total
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
								43,402

A reconciliation between the opening and closing loss allowances for trade receivables and contract assets for the year ended 31 March 2023 is shown in note 12.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Credit risk (continued)

Contract assets and trade and other receivables (continued)

Company

The company has no loss allowance for trade receivables and contract assets.

At 31 March 2023 and 31 March 2022, the maximum exposure to credit risk was represented by the carrying amount of each financial asset in the statement of financial position:

Group	2023	2022
	£000	£000
Cash and term deposits (note 14)	89,854	150,404
Short-term deposits (note 9)	66,709	70,179
Trade and other receivables (excluding prepayments and amounts recoverable from the group's insurer)	96,569	98,363
	253,132	318,946

The prior year has been restated to reclassify trade receivables credit balances to payments received in advance.

Company

The company has no such financial assets.

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

Group	2023	2022
	£000	£000
AAA	61,683	101,125
A-1+	35,883	35,048
A-1	47,177	82,012
	144,743	218,185

These are all short-term ratings.

Company

The company has no cash and cash equivalents.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Interest rate and inflation risk

The group 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. A series of RPI linked inflation swaps with a total nominal value of £210.0m, linked to the maturity of the Class A fixed rate £250.0m bond (July 2026), were entered into between August 2018 and October 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 and impact the Group's retained earnings or accumulated losses.

In October 2022 the company also entered into a swap agreement with nominal value £31,500,000, with effective date 30 September 2022. This transaction swapped interest payable at a SONIA linked floating rate for interest payable at a fixed rate for £31,500,000 of the £42,000,000 bank term loan with maturity 30 September 2024.

The group 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 group to the risk of economic loss where actual inflation is lower than that implicitly locked in through nominal debt. The group's index-linked borrowings, which are linked to inflation, form a partial economic hedge of the group's regulatory assets, which are also linked to inflation.

Interest rate and inflation risks are reported quarterly to the Affinity Water Limited Board through the Treasury Report.

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

	Fixed rate debt £000	RPI-linked debt £000	CPI-linked debt £000	Total £000
As at				
31 March 2023	780,246	563,287	236,399	1,579,932
31 March 2022	809,387	520,761	216,387	1,546,535

The company had no debt at 31 March 2023 or 31 March 2022 however in October 2022 the company also entered into a swap agreement with nominal value £31,500,000, with effective date 30 September 2022. This transaction swapped interest payable at a SONIA linked floating rate for interest payable at a fixed rate for £31,500,000 of the £42,000,000 bank term loan with maturity 30 September 2024. . .

Sensitivity analysis

Sensitivity analysis has not been performed on movements in interest rates as the group's fixed rate debts had no exposure to interest rates as at 31 March 2023. Given the large movements in inflation and the current high levels, the following table details the sensitivity of (loss)/profit before taxation to changes in RPI and CPI on the group'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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A4. Financial instruments and risk management (continued)

Sensitivity analysis (continued)

Impact on loss before taxation	2023
	£000
2%/1% increase in RPI	(4,389)
2%/1% decrease in RPI	4,391
2%/1% increase in CPI	(2,209)
2%/1% decrease in CPI	2,209
Impact on loss before taxation	2022
	£000
1% increase in RPI	(3,872)
1% decrease in RPI	3,872
1% increase in CPI	(2,406)
1% decrease in CPI	1,600

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 group has no material net exposure to movements in currency rates.

Capital risk management

The gearing policy approved by the Board of Affinity Water Limited is a target, measured as net debt (as defined in Affinity Water Limited's WBS documentation) to RCV, of 80%. This allows sufficient headroom within the group's financial covenants, which are triggered at a level of more than 90%. Affinity Water Limited's gearing on this basis was 73.4% at 31 March 2023 (73.0% at 31 March 2022).

Assuming no significant changes to existing credit rating agencies' methodologies or sector risk assessments, the group 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 group's ability to comply with its licence requirement to maintain an investment grade credit rating.

The group 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 of Affinity Water Limited through the Treasury Report.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A5. Retirement benefits

Defined benefit section

The group'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 group. The plan's corporate trustee (the 'Trustee') is a subsidiary of the group.

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 group 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 91.5% in November 2022, with the Investment Guidelines allowing a range from 87.5% to 100%); 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.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A5. Retirement benefits (continued)

Defined benefit section (continued)

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 group 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 group into the AWPP for the year ending 31 March 2024 are therefore £1,600,000 (£1,600,000 in the year ended 31 March 2023, 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 13.4 years (2022: 16.5 years).

Defined benefit section - financial and demographic assumptions

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

	2023	2022
Discount rate	4.75% pa	2.70% pa
Salary growth	3.20% pa	3.60% pa
RPI	3.20% pa	3.65% pa
CPI	2.70% pa	3.10% 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	24
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 2.70% per annum (2022: 3.10% per annum) unless otherwise prescribed by statutory requirements or the plan rules.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A5. Retirement benefits (continued)

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
2023				
Discount rate	0.5% decrease	6.8% increase	0.5% increase	6.1% decrease
Salary growth	0.5% increase	0.6% increase	0.5% decrease	0.6% decrease
Pension growth rate	0.5% increase	5.7% increase	0.5% decrease	4.9% decrease
Life expectancy	1 year increase	4.0% increase	1 year decrease	4.0% decrease
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

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 %	2023 £000	Plan assets %	2022 £000
Equity securities	1%	2,535	7%	37,244
Debt securities	68%	266,081	71%	391,729
Property	0%	42	0%	156
Infrastructure	1%	2,692	1%	3,388
Liability driven investments	28%	108,353	15%	80,555
Cash and cash equivalents	2%	8,047	6%	34,481
Total fair value of the plan's assets	100%	387,750	100%	547,553
Present value of defined benefit obligations		(334,135)		(443,306)
Net retirement benefit surplus		53,615		104,247

The total of assets that are quoted is £330,095,000 (2022: £441,737,000) and the total of assets that are unquoted is £57,604,000 (2022: £105,765,000).

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A5. Retirement benefits (continued)

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 2022 / 1 April 2021	547,553	540,421
Benefits paid	(17,337)	(15,301)
Employer contributions	1,879	3,539
Contributions by plan participants	170	215
Interest income	14,573	10,430
Re-measurement (losses)/gains	(159,088)	8,249
At 31 March 2023 / 31 March 2022	387,750	547,553

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 2022 / 1 April 2021	(443,306)	(465,889)
Benefits paid	17,337	15,301
Contributions by plan participants	(170)	(215)
Current service cost	(3,236)	(4,061)
Past service cost	-	-
Interest expense	(11,734)	(8,942)
Re-measurement gains	106,974	20,500
At 31 March 2023 / 31 March 2022	(334,135)	(443,306)

Defined contribution section

At the same time that the defined benefit section became closed to new entrants, the group 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 2023 was £4,043,000 (2022: £3,677,000). There are no amounts prepaid or outstanding in respect of the defined contribution section at 31 March 2023 (2022: £nil).

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

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 Capital Funds Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Holding and investment company	Ordinary shares	100%
Affinity Water Holdco Finance Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Finance company	Ordinary shares	100%
Affinity Water Holdings Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Holding company	Ordinary shares	100%
Affinity Water Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Water supply	Ordinary shares	100%
Affinity Water Finance (2004) PLC	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Finance company	Ordinary shares	100%
Affinity Water Finance PLC	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Finance company	Ordinary shares	100%
Affinity Water East Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Investment company	Ordinary shares	99%
				Ordinary non-voting shares	88%
				10% preference shares	98%
Affinity Water Southeast Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Investment company	Ordinary shares	99%
				Ordinary non-voting shares	92%
				14% preference shares	98%

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A6. Subsidiaries (continued)

Name of company	Country of registration/ incorporation	Registered address	Nature of business	Type of holding	Proportion of voting rights and shares held
Affinity Water Pension Trustees Limited	United Kingdom	Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ	Pension trustee	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%

A7. Related party transactions

Group

Purchases of goods and services and dividends paid

Related party	Nature of Relationship	In respect of	2023		2022	
			Value £000	Balance £000	Value £000	Balance £000
Allianz Global Corporate & Speciality	Common ownership	Insurance	616	-	1,701	(616)
Allianz Insurance	Common ownership	Insurance	565	(26)	539	(539)

See notes 3.3 and 3.4 for directors' remuneration and key management personnel compensation disclosures respectively.

Daiwater Investment Limited

Notes to the financial statements – appendices (continued)

A7. Related party transactions (continued)

Group (continued)

Sales of goods and services

Related party	Nature of relationship	In respect of	2023		2022	
			Value £000	Balance £000	Value £000	Balance £000
Vistry Group plc	Shared director	Connection charges	88	-	4	-

Company

Purchases of goods and services and dividends paid

Related party	Nature of Relationship	In respect of	2023		2022	
			Value £000	Balance £000	Value £000	Balance £000
Allianz Capital Partners, DIF and HICL Infrastructure plc	Shareholders	Dividend	-	-	-	-

Sales of goods and services and dividends received

Related party	Nature of Relationship	In respect of	2023		2022	
			Value £000	Balance £000	Value £000	Balance £000
Affinity Water Capital Funds Limited	Subsidiary undertaking	Loans receivable and interest	-	-	-	-