SCOTTISH WATER
Water Industry Commission for Scotland (WICS) ANNUAL RETURN 2022/23

Contents

Section M – Regulatory Accounts Commentary

1 Overview

The financial performance of Scottish Water's regulated activities is measured on a regulatory accounting basis, which includes items subject to a long-term normative charge (LTNC)[1]. The following tables and commentary have therefore been presented on that basis. Reconciliations to Scottish Water's performance on a statutory accounting basis is set out in Table M3 (Tier 1 statement to statutory P&L) tables.

The Regulated Income & Expenditure Statement and Capital Investment for the year to 31 March 2023 compared to the Final Determination[2] is presented below.

<table>
<tr><th>SW Regulated Income & Expenditure Statement</th><th>Actual 2022/23 £m</th><th>WICS financial model underpinning FD 2022-23 £m</th><th>Inc/(dec) 2022/23 £m</th><th>Cumulative inc/(dec) 2021-23 £m</th></tr>
<tr><td>Total revenue</td><td>1,385</td><td>1,411</td><td>(26)</td><td>(39)</td></tr>
<tr><td>Regulatory operating costs</td><td>(416)</td><td rowspan="2">(609)</td><td rowspan="2">16</td><td rowspan="2">14</td></tr>
<tr><td>PFI costs</td><td>(177)</td></tr>
<tr><td>Interest charges</td><td>(136)</td><td>(175)</td><td>39</td><td>55</td></tr>
<tr><td>Costs before items subject to LTNC</td><td>729</td><td>784</td><td>55</td><td>69</td></tr>
<tr><td>Total available to support investment before LTNC items</td><td>656</td><td>627</td><td>29</td><td>30</td></tr>
<tr><td>Responsive repair & refurbishment costs</td><td>(215)</td><td>(263)</td><td>48</td><td>75</td></tr>
<tr><td>Developer contributions</td><td>(30)</td><td>(34)</td><td>4</td><td>4</td></tr>
<tr><td>Tax paid</td><td>(30)</td><td>(5)</td><td>(25)</td><td>(45)</td></tr>
<tr><td>Total LTNC Items</td><td>(275)</td><td>(302)</td><td>27</td><td>34</td></tr>
<tr><td>Surplus after charging LTNC items</td><td>381</td><td>325</td><td>56</td><td>64</td></tr>
</table>

Revenue

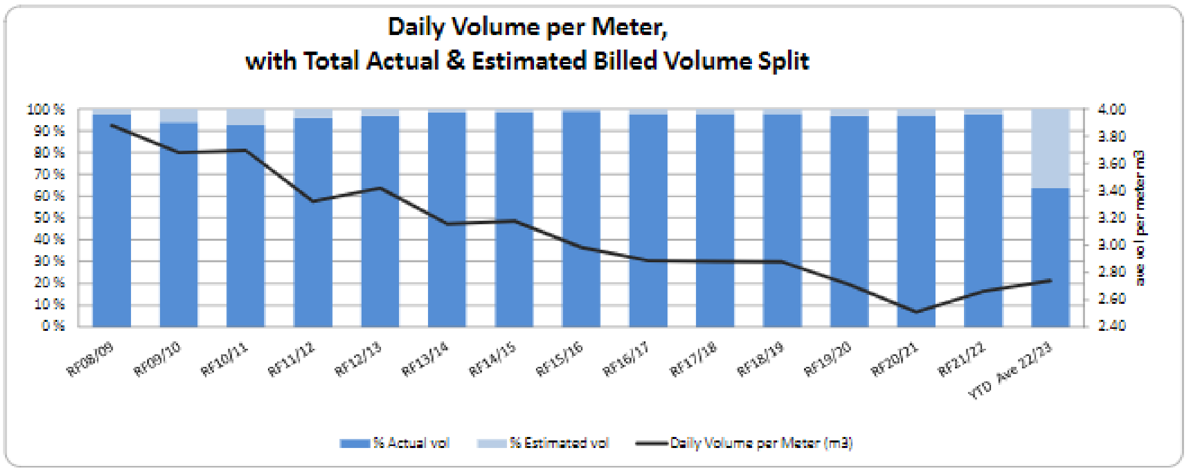
Revenue for the year at £1,385 million, was £26 million lower than anticipated in the Final Determination. The reduction was mainly due to charge increases being lower than assumed in the Final Determination which were based on CPI inflation +2%. The actual increase for 2022/23 was aligned to CPI inflation and in 2021/22 charges increased 1.8% above CPI but wholesale volumes were also impacted by the Covid pandemic in 2021/22.

In 2021/22 revenue was £13m lower than anticipated in the Final Determination. Consequently, revenue, on a cumulative basis for the first two years of the regulatory period, was £39 million lower

[1] LTNC Items - Responsive repair and refurbishment costs, developer contributions and tax.

[2] Updated for outturn inflation and realignment of operating expenditure. After the Final Determination was published, Scottish Water realigned operating expenditure to reflect improvements to its systems of cost capture. This change has the effect of reducing the allowed for operating expenditure by c. £50m per year and increasing the allowed costs for responsive repair and refurbishment expenditure by c. £50m per year.

than the level anticipated in the Final Determination. The associated shortfalls in the K factor relative to the Final Determination were 0.2% and 2.204% respectively. Wholesale volumes in 2022/23 returned to pre-pandemic levels. The graph below shows wholesale volumes per year (the black line) and it can be seen that the average volume per meter (the righthand side axis) in 2023/23 was similar to the levels in 2019/20.



Operating Costs, PFI and Interest charges

Costs before items subject to LTNC for the year were £729 million £55m lower than the Final Determination.

Exposure to increased inflation was managed effectively. Operating costs increased by £27m or 7% to £416m (2022: £389m) due to inflationary impacts associated with payroll, including increased national insurance costs, and chemical costs with the latter increasing by 60% or £12m. Key to keeping the increase below the increase in CPI (10.1%) was our electricity procurement strategy which enabled the forward purchase of our electricity requirements before the start of the 2022/23 financial year. Electricity costs in the year were £56m, accounting for 7.7% of costs before items subject to LTNC Without forward purchasing of our electricity needs, costs for the year could have been £65m higher.

PFI costs increased by £6m or 4%, to £177m (2022: £171m). This was predominantly due to contract indexation, particularly the impact of gas indexation on the Levenmouth contract, offset by savings from the folding of the Aberdeen Environmental Services Group of companies into Scottish Water's wastewater operations.

Interest charges in the year decreased by £6m to £136m (2022: £142m) mainly as a result of increased interest income from funds on deposit. However, as set out in the Prospects section below, increased electricity costs and other inflationary pressures will impact our performance in 2023/24.

Costs before items subject to LTNC, on a cumulative basis for the first two years of the regulatory period, were £69 million lower than anticipated in the Final Determination.

Long-Term Normative Charge Items (LTNC)

Responsive repair and refurbishment expenditure is difficult to predict over a short-term time horizon as there can be significant variability in the annual level of expenditure associated with, for example, significant water main bursts or collapsed sewers. A LTNC has been applied to remove variability with the expectation that the long-term normative charges will balance with actual expenditure incurred over the 2021-27 period. Developer contributions and corporation tax charges will also experience significant annual variability. Therefore, we have also adopted a long-term normative charge approach for these costs. Consequently, Tier 1 cost performance relative to the Final Determination, is focussed on costs before items subject to LTNC.

Expenditure in the year to 31 March 2023 on responsive repairs and refurbishment activities was £192 million compared to the anticipated LTNC charge for the year of £215 million, which was £48 million lower than the level within the Final Determination of £263 million. The year-n-year increase was £40m (2022 £152m) due to increased volumes, inflationary impacts and improved cost capture processes covering replacement and repair activities. Cumulatively, the LTNCs for responsive repairs and refurbishment were £75 million lower than the level assumed in the Final Determination.

For developer contributions and taxation, the normative charges were £30 million per annum for each cost. In the year to 31 March 2023 actual expenditure was £33 million and zero respectively. Consequently, total actual expenditure on LTNC items in the year was £225 million, £50 million lower than the anticipated LTNC.

As we progress through the 2023-27 period rebasing of LTNCs will be required to reflect actual expenditure trends and up-to-date forecasts. These updates will be highlighted within our interim and annual reports and in our M Table commentary.

Surplus to support planned investment

The total available to support planned investment after charging for LTNC items for the year was £381 million. This was £56 million higher than that anticipated in the Final Determination for the year, due to lower costs more than offsetting the lower revenue. Cumulatively, since the start of the regulatory period, the surplus to support planned investment was £64 million higher.

Capital Investment

Our gross planned investment, on a regulatory accounting basis, in the year was £694 million, which was £49 million or c. 6% higher than our plan. When combined with responsive repair and refurbishment costs, total regulated investment was £886 million in the year. The table below compares performance to the investment expectations in the Final Determination.

Investment on a regulatory accounting basis	Actual 2022/23 £m	Final Determination 2022/23 £m	Inc/(dec) 2022/23 £m	Cumulative inc/(dec) 2021-23 £m
Planned investment	694	521	173	(31)[3]
Responsive repair & refurbishment costs	192	263	(71)	(161)[4]
Total	886	784	102	(192)

Prospects for 2023/24

[3] In 2021/22 planned investment (excluding completion) was £505 million, £31 million lower than the Final Determination Level. Completion investment in 2021/22 was £118 million, £173 million lower than the Final Determination level.

[4] In 2021/22 responsive repair & refurbishment costs were £152 million, £90 million lower than the Final Determination Level

We remain committed to delivering our Strategic Plan, increasing investment to replace our ageing assets, achieving our net zero ambitions and taking all possible steps to drive for further efficiency to reduce our expenditure, targeting at least a 1% year-on-year real reduction (CPI-1%) in line with the challenging target set in the Final Determination.

Our budgeted regulated income & expenditure for the year to 31 March 2024 compared to the Final Determination is presented below.

SW Regulated Income & Expenditure Statement	Budget 2023/24 £m	WICS financial model underpinning FD 2023/24 £m	Inc/(dec) 2023/24 £m	Cumulative Inc/(dec)
Total revenue	**1,458**	**1,608**	**(150)**	**(189)**
Regulatory operating costs	(484)	(636)	(25)	(11)
PFI operating costs	(177)			
Interest charges	(142)	(184)	42	97
Costs before items subject to LTNC	**(803)**	**(820)**	**17**	**86**
Total available to support investment before LTNC items	**655**	**788**	**(133)**	**(103)**
Responsive repair & refurbishment costs	(215)	(275)	60	135
Developer contributions	(30)	(35)	5	9
Tax paid	(20)	(5)	(15)	(60)
Total LTNC Items	**(265)**	**(315)**	**50**	**84**
Surplus after charging LTNC items	**390**	**473**	**(83)**	**(19)**

Customer charges for 2023/24 have increased by 5% after extensive discussions with the Scottish Government. The increase is 8.1% below the expected level in the Final Determination for 2023/24. The difference in budgeted revenue to the level anticipated in the Final Determination is wholly attributable to the K factor difference. If the revenue budget for 2023/24 is uplifted by the difference to the K factor assumed in the Final Determination (an uplift of c 10.5%) budgeted revenue would be slightly above the level in the financial modelling underpinning the Final Determination.

Operating costs are budgeted to increase in 2023/24 due to higher electricity costs (53% of our electricity costs are exposed to market prices in 2023/24 with the other 47% being secured with forward power purchase agreements to 2026/27) and both our operating and PFI costs will increase due to the impacts of inflation. Consequently, we are monitoring energy prices closely as well as inflation forecasts covering our key supply chain requirements. The budget also reflects c. £5m of costs to improve waste water treatment works compliance, reduce the overall cost of managing the Glasgow Sludge Main (through more up front operational work to reduce reactive repair (Tier 1A) expenditure) and increased operational activities associated with SUDS. However, relative to the Final Determination, we anticipate these pressures will be offset by lower net interest charges and further efficiency improvement relative to the Final Determination. So, we are budgeting to outperform costs within the Final Determination, before items subject to LTNC, by £17 million in 2023/24.

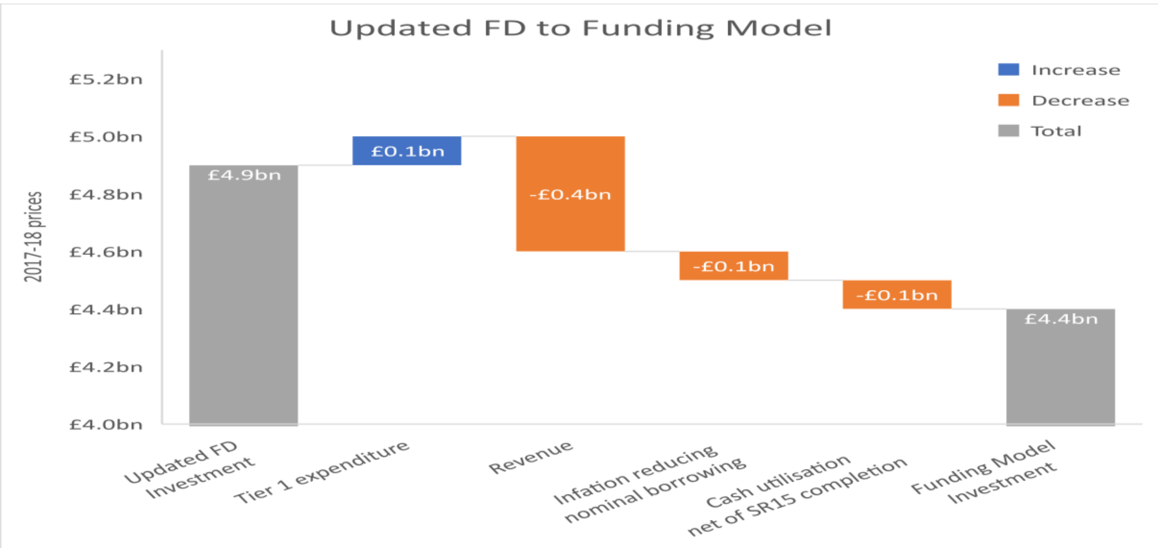
For LTNC items in 2023/24 we have maintained the level for responsive repair and refurbishment at £215 million. This is broadly the middle of our forecast range for responsive repair and refurbishment over the 2021-27 period of £1.15bn to £1.45bn[5], which is slightly lower than the Final Determination assumption of £1.55bn[6]. We have also maintained the level for developer contributions. Tax payments have been reduced to £20m reflecting lower forecast tax payments[7].

Net new borrowing from the Scottish Government in 2023/24 is planned to be £196 million. This includes additional Government borrowing of c £25 million to replace the £31 million external bank debt repaid held by Aberdeen Environmental Services Ltd. The Scottish Government has confirmed that this is appropriate given that, at the time of acquisition, Scottish Water's gross borrowings were reduced to reflect the external bank debt being included within Scottish Water's borrowing cap. As such, Group total borrowing will remain unchanged.

Over the 2021-27 regulatory period, our expectation is that our costs before LTNC items, will be c. £0.1bn lower than the Final Determination. However, in alignment with the Final Determination, to achieve real charge increases of 12.6% over the regulatory period, charges will need to increase significantly above CPI inflation for the last three years of the regulatory period as shown in the table below:

2021/22 Real Increase	2022/23 Real Increase	2023/24 Real Increase	2024/25 Required real increase	2025/26 Required real increase	2026/227 Required real increase
1.8%	0%	(6.1%)	2.3%[8]	6.8%	7.9%

Due to the profile of charge increases, revenue will still be c £0.4 billion lower than the Final Determination. Consequently, our central planning assumption is that we could finance £4.4 billion[9] of investment, £0.5 billion less than the Final Determination level. This is shown in the waterfall diagram below.



[5] In 2017/18 prices this is a range of £0.9bn to £1.2bn
[6] £1.3bn in 2017/18 prices
[7] The budget for 2023/24 was finalised prior to the UK Government Budget in March 2023. If the 100% capital allowances for new plant and equipment are confirmed then forecast tax payments to 2026/27 will drop to nil.
[8] The real increases for 24-27 have been profiled to give the same level of nominal charges each year (c. 8.5%) based on the February 2023 Bank of England inflation forecasts.
[9] In 2017/18 prices

2 Introduction

SW produces statutory consolidated accounts incorporating the results of all subsidiary companies. The consolidated statements also include the income statement, balance sheet and cash flow (and relevant notes) for SW only ('company'). Reconciliations between the statutory accounts and the regulatory tables are detailed in Table M3 and Appendix 1 to this document.

M Table financial information is for SW company only (i.e. excluding all subsidiaries), and is analysed between Core and Non-Core where required. The exceptions to this are tables M18W and M18WW with this explained in Section 5.

The M Tables have been completed using the historical cost information, except for the addition of current cost non-current assets and current cost depreciation charge within tables M4 and M5.

Significant transactions in the year

Highland PFI completed in May 2022 with the assets and activities transferring into Scottish Water from that date.

From the 1 October 2022 the activities of the North-East PFI companies were absorbed into the regulated activities of Scottish Water. AES, Aberdeen Environmental Services (Holdings) Ltd and Aberdeen Holdco Ltd ceased trading from that date. The corresponding contracts for PFI services to Scottish Water also terminated on the same date.

SWHH acquired the four North-East PFI companies for £16.2 million in December 2018 and continued to provide funding to Scottish Water Services (Grampian) since that date.

To acquire the entities, and to establish a "hold harmless" position for SWHH, Scottish Water paid a consideration to SWHH of £19.7m (as detailed below) for £16.9m of net assets in AES. The loss of £3.1m, including the cost of acquisition, has been recognised within PFI costs in Table M1 (line M1.11).

'Hold harmless' payment summary	**£m**
SWHH original investment in December 2018	(16.2)
Acquisition costs incurred by SWHH in December 2018	(2.5)
Total Dividends received in period of ownership	17.8
Intercompany Loans provided to SWSG in period of ownership	(18.8)
Consideration paid to SWHH by Scottish Water	**(19.7)**

The table below provides additional analysis of the values presented on the cash flow statement for the company within the statutory financial statements for the year ended 31 March 2023:

	£m
Intercompany loan to AES to enable settlement of external debt	(30.9)
Consideration paid to SWHH for net assets in AES	(19.7)
Cost of acquisition	(0.2)
Cash absorbed into SW from AES net assets	15.5

Acquisition of assets and liabilities of subsidiary per cash flow	**(35.3)**
Property, plant and equipment absorbed into regulated activities	32.2
Non-cash impact of acquisition of assets and liabilities of subsidiary	**(3.1)**

The effect of these two PFIs being absorbed within SW regulated is summarised in the table below.

	£m	£m
Increase in SW operating costs included in E tables:		
Sewerage (E7)	0.8	
Treatment (E7)	3.3	
Sludge (E10)	2.3	
		6.4
Local authority rates (not included in E tables)		0.7
Total increase in SW operating costs		**7.1**
Reduction in PFI costs (E3a.24 and E3a.26)		**(22.4)**

The reduction in PFI costs are reconciled in Table E3a.24 and E3a.26 in columns 10,20,40,50,60 and 70.

3 Tables M1 to M31

The commentary provided in this section for individual tables explains significant year-on-year movements or provides additional guidance on how the information was obtained and/or calculated. There are no comments on the tables which are self-explanatory.

<u>Table M1 – Tier 1 Income and Cost Statement</u>
Table M1 represents the Tier 1 income and cost statement, consistent with the financial reporting to the Scottish Water Board and as reported in the financial commentary of Scottish Water's Performance and Prospects Report for 2022/23.

Tier 1 revenue excluding infrastructure charges income and disposal proceeds (line M1.4) increased £80m or 6.2% to £1,365m (2021-22: 1,285m). This mainly reflects the charge increase in the year of 4.2%. The remaining increase has been driven by new connections to services and increased wholesale consumption, which has now returned to pre-pandemic levels.

Disposal proceeds (line 1.6) decreased £3.1m to £0.7m (2021-22: £3.8m).

Net new borrowing (line M1.8) reduced £110m to £125m (2021-22: £235m). The net new borrowing in the year reflects the borrowing per the Final Determination with a reduction of £50m in the year. The reduction in the year was due to additional borrowing of an equal sum in the prior year, effectively balancing total new loans from 2021-2023 with the borrowing limit outlined in the Final Determination for the same period.

Tier 1 operating costs before interest and tax (line M1.14) increased £82m or 11% to £819m. Each of the key lines and variances are explained in further detail below:

- Operating expenditure (line M1.10) increased £27m or 7% to £416m (2021-22: £389m) due to inflationary impacts associated with employee costs, including increased national insurance costs, and chemical costs with the latter increasing by 60% or £12m.
- PPP costs (Line M1.11) increased by £6m or 4%, to £177m (2022: £171m). This was predominantly due to contract indexation, particularly the impact of gas indexation on the Levenmouth contract, partially offset by savings from the folding of the Highland and North-East PFI activities into Scottish Water's waste water operations as shown in the significant transaction section above. A reconciliation of year-on-year movements is shown below:

	£m
2021-22 PPP costs (Line M1.11)	171
Contract indexation	21
Gas indexation impact at Levenmouth	7
Reduction in PFI costs from folding in of Highland and North-East PFI activities	(22)
2022-23 PPP costs (Line M1.11)	177

- Responsive repair and refurbishment (Line M1.12) increased by £41m or 27% to £192m (2021-22: £152m) due to increased volumes which were influenced by increased disruptions to the network including the freeze/thaw period experienced in December 2022, inflationary pressure on market prices and improved cost capture between replacement and repair activities.
- Developer contributions (Line M1.13) increased by £8m or 32% to £33m (2021-22: £25m) due to a catch up of activities from prior years.
- Net interest charges (line M1.15) reduced £6m or 4% to £136m (2021-22: £142m) resulting from increased interest income from funds on deposit and a small reduction in weighted average interest cost of 0.1% to 3.1%.
- Tax paid in the year reduced by £15m to nil. The decrease reflects an increase in capital allowances claimed, mainly due to the availability of super deductions which were introduced by the UK government in response to the impact of the Covid-19 pandemic.

Memo lines 1.22 to 1.24 provide a like-for-like comparison of Operating costs with line M1.23 showing the amount of expenditure, which prior to 2021-22, will have been recognised as operating expenditure.

A reconciliation to the statutory income statement is presented in Table M3.

Table M3 – Tier 1 Income and Cost Statement – Reconciliation to Statutory Accounts
Table M3 reconciles the regulatory Tier 1 income and costs (Table M1) to the statutory income statement presentation shown in Table M4 Stat and SW's statutory income statement. The adjustments in Table M3 reflect:

- the inclusion of depreciation charges (line 3.11 to 3.13);
- the removal of balance sheet and cash flow items generally associated with capital investment in lines 3.4, 3.5, and 3.10;
- the capitalisation of refurbishment expenditure and the expensing of planned repair costs (line 3.9);
- IFRS adjustments relating to Cloud service costs, pension costs (IAS 19), PFI costs (IFRIC 12) and the tax charge, including deferred tax.

An additional column has been added in Table M3 to recognise the reallocation of the loss from the absorption of the North-East PFI activities into the waste water operations of Scottish Water. Detailed analysis has been provided in the significant transactions section above.

Table M4 and M4b – Regulatory Accounts Income and Expenditure

Table M4 is a regulatory accounting P&L that reflects regulatory accounting information with current cost depreciation based on Modern Equivalent Asset Values (MEAV) (rather than based on historic cost), with responsive and planned repair costs (line 4.4) aligned to presentation within the statutory income statement but excludes the majority of IFRS adjustments.

The majority of lines are populated from information presented in Table M1 and M3. All current cost adjustments have been calculated on a MEAV basis as agreed with WICS.

Lines M4.1, M4.3 and M4.11 have been explained earlier in the commentary under Table M1. The remaining lines are explained in turn below:

Operating expenditure (line M4.2) is M1.10 reduced by £0.2m to reflect the accounting for Research & Development tax benefits in the year. This adjustment follows the accounting treatment.

Responsive and planned repairs (line M4.4) increased £60m to £230m (2021-22: £170m). The increase is predominately driven by the increase as detailed in the responsive repair and refurbishment explanation (Line 1.12) for Table M1. Line M3.9 on Table M3 reconciles the responsive repair and refurbishment expenditure in M1.

Current cost depreciation (Line M4.5) has been calculated using MEAV. The MEAV adjustment in 2022-23 increases depreciation charges of £301m shown in lines M3.11 to M3.13 by £372m to £673m. The increase in the year of £87m reflects the increase in the MEAV which is mostly driven by inflation in the year.

Profit or loss on disposal (line M4.9) represents the disposal proceeds shown in Table M1 (line M1.6) less the cost of disposal.

Taxation shown in lines M4.13 and M4.14 shows the split of the tax charge shown on Table M3 excluding adjustments to tax relating to IFRS pension adjustments (line M3.19) between current and deferred tax.

Other gains and losses (Line 4b.4) shows the movement in the MEAV adjustment to Tangible Assets presented in Table M5. The value reported in 2021-22 represents the initial adjustment to Tangible Assets. This has been presented within other comprehensive income to be consistent with revaluation gains and losses under IFRS accounting to create a current cost reserve in Table M5. However, this adjustment should not be confused with revaluation.

Appendix 1.1 shows a reconciliation of the M4 regulatory income and expenditure account to the Table M4 Stat IFRS income and expenditure account.

Table M5 – Regulatory Accounts Balance Sheet

Table M5 is a regulatory accounting Balance Sheet that reflects regulatory accounting information using MEAV rather than historic cost with responsive and planned repair costs aligned to statutory accounting presentation but excludes the majority of IFRS adjustments

Tangible Assets (Line 5.1) and Current cost reserve (Line 5.23), represent MEAV adjusted values as explained in the M4 commentary above.

Working Capital and other creditors (line M5.2 and M5.14) are linked to Table M11. Commentary for M11 below highlights any significant movements when compared to prior year.

Cash balances (M5.3 and M5.4) decreased £125m to £390m (2021-22: £515m). The reduction in cash reflects the lower borrowing, the growth of the investment programme in the year and the £35m acquisition costs relating to the absorption of North-East PFI activities into Scottish Water.

Income and expenditure (Line 5.22) has increased £79m to £1,754m (2021-22: £1,675) reflecting the profit retained in line M4.19 of negative £293m and adding back the MEAV adjustment to depreciation of £372m outlined in the M4 and M4b commentary above.

The current cost reserve (line 5.23) has increased £9,469m reflecting the other gains and losses reported in line M4b.4. less the MEAV adjustment to depreciation outlined above.

Appendix 1.2 reconciles the regulatory accounts balance sheet to the Table M5 Stat IFRS balance sheet and SW's statutory accounts balance sheet.

Table M6 – Regulatory Income and Expenditure and Cash Flow

Table M6 is a regulatory cash flow that aligns to the regulatory current cost P&L (Table M4) and the regulatory current cost Balance Sheet (Table M5). It includes a reconciliation to the 'Net cash flow from operating activities' (line 6.8) from the operating profit in M4.8.

A new line has been added to represent the cash outflows relating to the absorption of the North East PFI activities into Scottish Water. Line M6.7 represents the non-cash loss on acquisition shown on Table M3. Further detail has been provided in the significant transactions section above.

Interest paid (line 6.10) of £141m includes intercompany interest paid to Business Stream of £1.4m and £1.1m to 3rd party LPs in relation to the settlement of wholesale billing and reconciliation process. The interest paid has been offset by interest income of £4m reflecting increased interest income from funds on deposit due to higher interest rates.

The total capital expenditure has been separated into component parts across lines 6.14 to 6.17. The tables below provide the detail and the reconciliation of the total capital investment to lines 6.14 to 6.17:

		M Table / line ref		2021/22 £m	2022/23 £m
Opening short term capital creditor		M11.10	(21/22)	105.3	105.3
Add:	Capital investment (net of contributions)			786.3	908.8
Add:	Group asset purchase - SW Grampian			-	1.5
Less:	Responsive and planned repairs			(169.7)	(230.5)
	Closing short term capital creditor	M11.10	(22/23)	(105.3)	(131.7)
=>					
	Capital expenditure			**616.6**	**653.4**
Analysed:					
	Capital enhancement and growth expenditure	M6.14		330.9	283.1
	Asset replacement expenditure	M6.15		217.5	281.6
	Asset refurbishment expenditure (Tier 1a excluding responsive and planned repairs)	M6.16		49.8	71.1
	Developer Contributions	M6.17		18.4	17.6
	Capital expenditure (total)			**616.6**	**653.4**

Capital investment (net of contributions) is analysed further in the table below.

		2021/22 £m	2022/23 £m
	Responsive repair and refurbishment (line M1.12)	151.9	192.4
	Tier 2 investment (Per M8 commetary below)	622.9	693.8
	Developer contributions (Line M1.13)	24.6	32.7
Less:	PFI investment	(2.5)	-
	Contributions	(10.2)	(3.4)
	Insurance recovery	(0.4)	(6.7)
	Capital investment (net of contributions)	**786.3**	**908.8**

Table M6R – Regulatory Accounts – Ratio information

This table provides all the information for, and calculation of, the basic ratios in one place. The ratios calculated in Table M6R are the clean calculation using the actual financial information, with all figures referenced from the relevant M Tables.

Table M7 – Analysis of Turnover and Operating Income

Table M7 analyses regulatory income between water and wastewater.

Turnover from services supplied to household customers increased by £51m or 5.4% to £990m (2021-22: £939m) (line M7.1) reflecting the increase in household charges of 4.2% for both water and wastewater services, effective from 1 April 2022, and the net increase in properties connected to the network. The additional lines (lines M7.17 – M7.20) provide detail on the movements in household revenue. The change in line M7.19 reflects the expansion of the Water Charge Reduction Scheme in 2021-22 which increased from a 25% reduction to 35% along with changes in the volumes of exemptions.

Turnover from wholesale services provided to Licensed Providers increased by £26m or 8% to £359m (2021-22: £333m) (line M7.3) reflecting tariff increase of 4.2% (shown in M7.21) for both water and wastewater services, an increase in consumption as outlined in Table M1 commentary above, and a net year on year reduction in the income uncertainty provision of £5m (2021-22 IUP top-up of £7m and 2022-23 IUP top- up of £2m). The additional lines (lines M7.21 – M7.26) provide a further analysis of the year-on-year movements in wholesale revenue.

Turnover from other sales increased £3m or 21% to £15m (2021-22: £12m) reflecting additional windfarm rental income in the year (line M7.7).

Cash receipts in respect of infrastructure charges income were broadly in line with prior year at £20m (Line M7.10) and disposal proceeds were down £3m to £1m as explained in M1 commentary above (line M7.11).

Table M8 – Movements in Cash Balance

Table M8 compares the financial flows delivered in the year to those in the Final Determination updated for inflation (and the closing position in 2020-21) and reconciles movements from the closing Final Determination cash position to the closing actual cash position of Scottish Water at 31 March 2023.

The Final Determination model has been updated to reflect:

- the 2020-21 closing position for household, wholesale and other revenue;

- the 2020-21 closing position for cash (less SR15 completion);
- CPI inflation of 3.98% and 10.06% for 2021-22 and 2022-23 respectively; and
- price increase of 2.7% and 6.2% based on a preceding October CPI of 0.7% and 4.2% for 2021-22 and 2022-23.

The updated Final Determination model has then been compared to actual reported Tier 1 performance (as per Table M1), planned investment (Tier 2) performance (as set out in the Overview Commentary in section 1 above) and net new borrowing (as per Table M29) in 2022-23. Closing cash per the updated Final Determination model, closing cash and Tier 2 expenditure have been reported excluding completion to allow for a like-for-like comparison to the Final Determination:

- Closing cash per the Final Determination is reported as £109m, being £429m reported 2020-21 closing cash position, less £291m of SR15 completion costs, less £29m of cash utilisation as per the Final Determination model.
- Scottish Water closing cash is reported as £279m, being £390m closing cash reported on Table M5, lines M5.3 and M5.4, less remaining SR15 completion costs of £111m.
- Tier 2 investment in the year was £694m including completion costs of £61m compared. So, excluding completion Tier 2 investment was £633m compared to modelled FD Tier 2 investment of £520m for 2022-23.

Our updated Final Determination model and working file is included as part of our annual return submission and is summarised in the table in the overview section.

Working capital movements reflect the difference between the Tier 1 statement, Tier 2 investment, and the total cash movement in the year. It should be noted that the working capital movement in table M8 is not equivalent to the working capital movement in M11. This is because M8 compares the Tier 1 and Tier 2 movements on an accruals basis against the Final Determination which is on a purely cash basis. M11 however, compares the movement in balance sheet balances from 2021-22 to 2022-23. The basis of the calculation used is consistent with the basis outlined as part of the WICS queries in 2021-22 (Query M-13).

Timing Impacts (cols G to J) arise where cash inflows/outflows are expected to be utilised/recovered during a future year of the regulatory period relative to the updated Final Determination model. Timing differences for LTNC items are shown as the expected LTNC level less the actual performance in the year as summarised in the table below and reflect the values presented in the overview in section 1:

LTNC item	LTNC	Actual	Timing
Responsive repair and refurbishment	215	192.4	22.6
Developer contributions	30	32.7	-2.7
Tax paid	30	0	30

The borrowing timing adjustment is calculated as the difference between the borrowing received in the year compared to the borrowing levels outlined in the Final Determination financial model. The reduced borrowing in the year of £50m is explained in the M1 commentary above.

The Tier 2 investment timing adjustment is calculated as total Tier 2 investment of £694m less SR15 completion costs in the year of £61m, giving £633m of SR21 Tier 2 investment. When compared to Tier 2 investment per the updated Final Determination of £521m the timing impact equates to £112m.

<u>Table M11 – Regulatory Accounts Working capital (Core)</u>
Table M11 sets out the movements in working capital. All of the balances presented in Table M11 are on a regulatory accounting basis except for lines 11.18 and 11.19. Appendix 1.2 shows the

reallocation of working capital reported in M11.15 and M11.16 (shown as Line 5.2 and 5.14 on appendix 1.2) to the reported statutory IFRS company balance sheet.

Table M18W and M18WW commentary – see Section 4.2 below

Table M21 – Taxation analysis

Table M21 provides a taxation analysis,

The 2021/22 data has been updated to reflect the actual 2021/22 tax computation submitted to HMRC. We

Two additional lines have been added into M21 to show the impact of super deductions as explained in Table M1 commentary.

Tables M27a and M28a – Consolidated IFRS Income Statement and Historic Cost Balance Sheet

The consolidation tables – M27a and M28a – include the results of Scottish Water and all its subsidiaries. Business Stream's results are included in the Licensed column and all other subsidiaries have been added to the non-core non-licensed column. IFRS adjustments are included within M27a and M28a to arrive at the presentation within the Performance and Prospects report. The core column is linked to tables M4 and M5.

The core column in M27a is populated with the values from Table M4 with current cost items being removed in the core IFRS adjustment column (Lines M27.5 and M27b.4) The consolidated column allows for a direct comparison to the published total comprehensive income for the year.

The core column in M28a is populated with the values from Table M5 with current cost items being removed in the core IFRS adjustment column (lines M28a.1 and M28a.23).

The significant movements in tables M27a and M28a are explained in the sections below:

Table M27a – Consolidated IFRS Income Statement

The core IFRS adjustments, excluding the current cost adjustments explained above, are:

- M27.2 - The operating expense adjustment reflects the accounting treatment of Cloud software service costs as presented in Table M3.7.
- M27.3 - This expense adjustment reflects the adjustments associated with PFI finance lease costs under IFRIC 12 to separate the costs into a liability repayment and an interest cost as shown in line M27.9. and also includes the reallocation shown in Table M3 in the AES acquisition column as explained in Table M3 commentary above and the significant transactions section.
- M27b.2 - Is the net actuarial gain at March 2023 calculated from changes in actuarial assumptions and expected return on assets set at the beginning of the year. The actuarial assumptions and valuation of the defined benefit pension scheme calculation are provided by independent qualified actuaries.
- M27b.3 - This represents the actuarial service cost and interest expense of the defined benefit pension scheme, net of actual cost of contributions paid to the pension funds as per IAS19.

The intercompany items being visibly eliminated (in col 5) on this table are the intercompany wholesale income in SW and the intercompany cost of sales in Business Stream. The intercompany interest between SW and Business Stream already eliminates across line 27.11.

Non-core / non-licensed includes the remaining non regulatory business within SW, the results for the two holdings companies (Scottish Water Business Stream Holdings (SWBSH) & Scottish Water Horizons Holdings (SWHH), SWH, and the North-East PFI companies. From the 1st October 2022 the activities of the North-East PFI were absorbed into the regulated activities of Scottish Water as explained in the significant transaction section above.

Table M28a – Consolidated Historic Cost Balance Sheet

The core IFRS adjustments, excluding the current cost adjustments explained above, are:

- M28a.2 - This entry primarily relates to the timing of pension fund contribution payments reflected in M28.17.
- M28a.17 - This represents the net pension liability required under IAS19 at the end of the period. This is independently calculated and is audited as part of our year end audit to ensure compliance with the standard. Actuarial assumption changes result in the pension liability being presented as an asset for 2022/23. Additional information can be obtained from note 22 to the Financials in our Performance & Prospects report for 2022-23.
- M28a.18 - This entry is reducing the unfunded pension benefit provision already included in post-employment asset / liabilities, line M28.17.
- M28a.24 – This value represents the remaining liability under IFRIC 12 for all PFI contracts.

The Non-core / non licensed column includes the remaining non regulatory business within SW and the balance sheets of SWBSH, SWHH, SWH, and the North-East PFI companies. From the 1st October 2022 the activities of the North-East PFI were absorbed into the regulated activities of Scottish Water as explained in the significant transaction section above.

Table M29 – Interest

Table M29 reconciles the movement in net interest expense presented on Table M4 (line M4.11).

Line M29.11 adjusts the calculation in line M29.7 for timing differences. This is required as a reconciling item as line M29.7 assumes all new borrowing and borrowing repaid takes place at the start of the year. Table M30 provides more detail on the drawdown and repayment dates.

Interest income increased £4m (line M 29.9) reflecting increasing interest rates throughout the year from cash on deposit.

Prepaid wholesale charges interest (line M29.10) increased £2m to £3m. The prior year was lower as it reflected the reintroduction of wholesale charge repayments following the temporary relaxation of prepayments from Licensed Providers to provide market security during the covid-19 pandemic period.

Tables M30 & M31 – Inventory of loans

Tables M30 and M31 provide a full listing of SW's loans.

Table M30 details the principal value of the loans due for repayment in full by their maturity dates. The listing includes details of the £123m of loans repaid during 2022/23.

Table M31 details the loans which have periodic repayment of the principal throughout the term of the loan.

Table M4 Stat – IFRS Statutory Accounts Income & Expenditure

Table M4a provides the results of Scottish Water Core on the IFRS Accounting basis. The non-cash pension adjustments, as calculated under IAS 19, have all been included in Table M4b Stat.

The reconciliation of the results shown in Table M4 (regulatory accounts income & expenditure) to the results in Tables M4 Stat is provided in Appendix 1.1. The reconciling items are purely the IFRS entries in respect of PFI costs and cloud software expenditure, and the removal of fixed asset current cost adjustments. The net impact on the profit before tax is summarised below.

(Increase)/decrease in costs			£m	*Note ref.*
	Loss before tax per table M4 (line M4.12)		**(266.1)**	
IAS38	Cloud software expenditure	(17.0)		*1.*
IFRIC 12	PFI costs - depreciation & lease liability	10.0		*2.*
	Current cost depreciation	371.5		
Scottish Water - net decrease in costs			**364.5**	
	Profit before tax on table M4 stat (line M4Stat.12)		**98.4**	

1. *IAS 38 'Intangible assets'*

In April 2021 the IFRS Interpretations Committee (IFRIC) published an agenda decision in relation to the application of IAS 38 Intangible Assets to configuration or customisation costs in a cloud computing arrangement. The agenda decision provides new guidance specific to cloud computing arrangements and provides a framework for the accounting treatment of 'implementation costs.

Scottish Water previously accounted for all implementation costs as Property, plant and equipment and these were subject to depreciation on a straight-line basis over the useful lives of the assets. The new guidance states that implementation costs should be recognised as an intangible asset if costs incurred meet the definition of an intangible asset under IAS 38. If it is not possible to identify an asset, then the costs should be expensed in the year in which they occur if the costs incurred are for a service that is distinguishable from the core software service and over the life of the contract with the supplier if the service is not distinguishable from the core software service.

Cloud software costs identified and expensed during the year amounted to £17m and are included within line M4Stat.2.

2. *IAS 17 'Leases' & IFRIC 12 'Service concession arrangements'*

Under IFRIC 12, the PFI service concession arrangements were reclassified as finance leases resulting in the PFI assets being brought on to Scottish Water's balance sheet. The annual PFI costs incurred are broken down into three categories: operating costs, finance costs and a reduction of the finance lease obligation. In addition, there is a depreciation charge calculated in respect of the leased assets held on the balance sheet.

In Table M4 stat, line M4Stat.3 'PPP costs' consists of the operating costs totalling £139m in 2022-23. The total depreciation charges of £17m are in line 4.5, the finance costs of £13m are in line 4.11 and Scottish Water internal costs are included in line 4.3.

The table below provides the reconciliation from Table M4 to Table M4 stat.

	M Table / line ref	2022/23 £m
Total PPP costs in Table M4	M4.3	**177.4**
IFRS adjustments:		
Less: Depreciation charges - PPP leased assets		(12.9)
Less: Finance lease obligation - to balance sheet		(22.6)
Less: North-East PFI acquisition costs		(3.1)
Total PPP costs in Table M4 Stat	M4.3 stat	**138.8**

The North-East PFI acquisition costs are detailed in the significant transaction section.

Table M4b Stat – Regulatory Accounts – Statement of comprehensive income

This table has been completed on a consistent basis with prior years and includes all of the IAS 19 'Employee benefits' adjustments in respect of the post-employment benefits. These IFRS adjustments are all non-cash.

The profit for the year (line M4bStat.1) is the Core retained profit from Table M4 Stat (line M4Stat.19).

The actuarial gains/losses on post-employment plans (line M4bStat.2), net of related deferred taxation, are as reported in the statutory results for Scottish Water. The gross pension liability decreased £623m to a gross asset position of £580m. To comply with IFRIC 14 and IAS 19 the pension asset is restricted to reflect the amount the employer is entitled to as an unconditional refund of the surplus or reduction in future contributions to the pension fund. This restriction amounted to £555m giving a surplus of £25m. The decrease in scheme liabilities of £736m (£181m after the restriction above), primarily due to a change in financial assumptions, was offset by lower-than-expected returns on scheme assets of £80m. Together, these represent the gross actuarial gain of £101m which, net of deferred tax, forms the £75m credit in M4b stat.

The post-employment plans (non-cash), net of tax (line M4bStat.3) consists of the total service cost and the net financing expense as calculated under IAS 19 which replace the 'normal management' operating costs as charged in tables M1 and M4 (line M4.2). The net adjustment of £30.7m is analysed as follows:

	SW £m
Pension service cost adjustments	(37.1)
Interest on pension scheme net liabilities	(1.8)
Deferred tax on IAS 19 adjustments	8.2
	(30.7)

There were no other gains or losses (line M4bStat.4).

Table M5 stat – Regulatory Accounts Balance Sheet

Tangible assets balance (line 5.1) equals the Property, plant & equipment and Intangible asset balance per the IFRS accounts.

PFI assets form part of the Property, plant & equipment balance, and totalled £198m and consists of the SW owned assets and the assets treated as leased under the IFRS basis. The related finance lease liability is shown in line 5.22. The following tables provide additional analysis and reconciliation to the presentation in the statutory accounts.

Balance sheet (see Appendix 1.2)			
Property, plant & equipment			
Leased assets			175.2
Owned assets	*(reclassification)*		22.8
		M5, line 5.1	**198.0**
Other loans & borrowings			
Finance lease liability	< 1 year		(22.3)
	> 1 year		(153.7)
	total	**M5, line 5.22**	**(176.0)**

Other creditors due after one year (line M5Stat.14) consists of payments received in advance of £67m and deferred income of £8m.

Post-employment asset / (liability) (line M5Stat.17) shows the retirement benefit asset under IAS 19, net of the related deferred tax balance, as described in the M4 Stat commentary above and detailed below.

Balance sheet		
Retirement benefit obligations (Post employment liabilities)		24.6
Deferred taxation on retirement benefit obligations		(6.1)
Retirement benefit obligations - net	**M5, line 5.17**	**18.5**

The other provisions total of £24m (line M5Stat.18), reflect a decrease of £1m compared to 2021-22, and represents the wholesale income uncertainty provision. This provision relates to uncertainty around the wholesale/non-domestic income relating to expected credits being applied to estimated bills as part of the CMA process.

Retained earnings (line M5Stat.23) consists of the total of the reserve brought forward from 31 March 2022 and the retained profit for 2022/23 (Table M4 stat, line M4bStat.5), as detailed below.

		£m
Retained earnings reconciliation as per table M5 stat		
Retained earnings as at 31 March 2022	**M5 stat, line 5.23**	1,567.0
Total comprehensive income for the year	**M4 stat, line4b.5**	116.2
Retained earnings carried forward at 31 March 2023	**M5 stat, line 5.23**	**1,683.2**

4 Tables M18W & M18WW

Introduction

The M18 tables are produced for Scottish Water regulated and non-regulated activity (including non-regulated activities within Scottish Water Horizons, prepared on a historic cost basis and excluding IFRS adjustments.

To aid comparison, the table below reconciles Scottish Water's Tier 1 operating costs, as per Table M1, to cost data included in the M18 tables of the Regulatory Accounts.

	Table ref	£m	Diff	Total	M18W/WW Tables M18W	M18WW
Tier 1 operating costs	M1.10	416.2				
Add: Repair and refurbishment expenditure previously expensed as operating expenditure in SR15	M1.23	58.1				
Less: directly capitalised tier 1a spend previosuly expensed as operating expenditure in SR15	M18W.44, M18WW.45	(0.4)				
SW regulated operating costs		**473.9**				
SW Non-reg operating costs		2.6				
SW Horizons operating costs		11.1				
Operating costs		**487.6**	**(6.6)**	**481.0**	272.2	208.8
PFI costs including AES acquisition costs	M1.11	177.5				
Less: AES acquisition costs	M3.8	(3.1)				
PFI Costs		**174.4**	**6.7**	181.1	0.0	181.1
Total operating expenditure	M18W.43, M18WW.44	**662.0**	**0.1**	**662.1**	**272.2**	**389.9**
Explained by charges to SWBS and others for support			**(0.1)**			

The line differences in the table above are explained as follows:

- £6.7m difference between the SW Board report and the M18 Tables re. PFI costs represents costs incurred in providing SW support to PFI activities;
- The expenditure totals differ slightly due to charges to SWBS for support being excluded in the preparation of the M18 tables.

Cost analysis in Tables M18 W and M18 WW was prepared using reports from SW's Activity Based Management (ABM) process. The ABM methodology used in 2022/23 did not differ from the methodology in 2021/22 and was audited as part of the Binnies audit in May 2023. A detailed explanation of the methodology has been provided in Appendix 2 to this commentary.

Commentary

For 2022/23, the operating expenditure sections of the M18 tables have been populated using SW's ABM model on a basis consistent with 2021/22. Rows M18.43 (W) and M18.44 (WW) show total regulated operating costs including responsive repairs and refurbishment costs of £57.7m.

Additional Tier 1a costs previously reported as operating expenditure is shown in rows M18.44 (W) and M18.45 (WW). The table below shows a reconciliation to values included within the M1 table.

Tier 1a Reconcillaition	2022/23 £m
Tier 1a spend reported within Total operating expenditure	57.7
Water M18.44 Repair and refurbishment previously expensed as operating expenditure in SR15 (Tier 1a)	0.2
Wastewater M18.45 Repair and refurbishment previously expensed as operating expenditure in SR15 (Tier 1a)	0.2
M1 table line 1.23 - Repair and refurbishment expenditure previously expensed as operating expenditure in SR15	**58.1**
Water M18.45 Remaining responsive repair and refurbishment expenditure (Tier 1a)	66.9
Wastewater M18.46 Remaining responsive repair and refurbishment expenditure (Tier 1a)	67.4
M1 table line 1.12 - Responsive repair and refurbishment	**192.4**

Total operating costs increased by £41.2m (6.6%) to £662.1m.

Total Operating Costs	2022/23 £m	2021/22 £m	Variance £m
Operating expenditure - Water M18w.43	272.153	256.159	(15.994)
Operating expenditure - Waste M18ww.44	389.956	364.715	(25.241)
	662.109	**620.874**	**(41.235)**

Analysis by activity:

	2022/23 £m	2021/22 £m	Variance £m
Wholesale	592.252	542.358	(49.894)
Retail	56.146	64.133	+7.987
Non Regulated	13.712	14.383	+0.671
	662.109	**620.874**	**(41.235)**

Wholesale activity costs increased by £49.9m (9.2%) from 2021/22 to £592.3m reflecting the following key movements:

Transfer of former PFI sites to Scottish Water control

During 2022/23 6 wastewater treatment works, all previously owned and operated under Private Finance Initiative (PFI) schemes, transferred into SW control. A list of the sites, associated PFI scheme and transfer date are noted below:

Works	PFI Scheme	Transfer Date
Allanfearn	Highland	29 May 2022
Fort William	Highland	29 May 2022
Fraserburgh	North-East	1 October 2022
Nigg	North-East	1 October 2022
Persley	North-East	1 October 2022
Peterhead	North-East	1 October 2022

Year on year cost comparisons include the following impacts relating to the return of the Highland and North-East PFI schemes as detailed in Significant Transactions section above:

	£m
Total increase in SW operating costs	**7.1**
Reduction in PFI costs	**-22.4**

Key year on year operating cost variances at line level include*:*

- An increase in direct employment costs of £6.8m (including £1.8m relating to former PFI sites), primarily driven by pay inflation of £4.0m (6%) and additional overtime to maintain supplies during more extreme periods of dry summer and freezing winter weather of £0.8m;
- An increase in direct power costs of £3.7m (including £1.0m relating to former PFI sites), primarily due to higher unit prices;
- An increase in hired and contracted services of £8.6m (including £1.6m relating to former PFI sites), due to contractor price increases of £3.4m, incident related costs of £1.5m, additional sludge costs of £1.2m relating mainly to compliance issues, and additional tank cleaning costs of £1.0m;
- An increase in PFI costs of £4.1m, primarily due to indexation of contract service fees partially offset by a transfer of NE & Highland schemes into SW's direct cost base;
- Materials and consumables costs increased by £11.8m (including £1.0m relating to former PFI sites), due primarily to higher chemical costs linked to exceptional market driven unit price increases and, to a lesser extent, higher usage to maintain water quality with an increase in distribution input and to ensure wastewater compliance;
- Other direct costs increased by £7.8m (including £1.0m relating to former PFI sites) due to tanker hire costs to maintain water supplies during periods of water shortage and higher insurance claims, fuel costs and property repair costs;
- General and support costs increased by £2.1m, primarily due to pay inflation and general inflation increases on core support costs including digital contracts;
- Costs associated with scientific services increased by £2.5m, reflecting pay and general inflation;
- Local authority rates costs increased by £1.3m (including £0.7m relating to former PFI sites) in line with the change in tax rate for 2022-23.

Retail activity costs decreased by £8.0m (12.5%) to £56.1m primarily driven by a decrease in bad debt charges of £8.3m.

Non-Regulated costs have decreased by £0.7m (4.7%) (in line with corresponding non-regulated income) reflecting a reduction in the number of developer projects undertaken by Scottish Water Horizons.

5 Appendices

Appendix 1.1

Scottish Water - Year ended 31 March 2023

Reconciliation of Regulatory Accounts Income Statement (Table M4) to IFRS Regulatory Income Statement (Table M4 stat) & Statement of Comprehensive Income (Table M4b)

Line	Description (TABLE M4)	Core	IFRS adjustments CCA Dep'n	IAS 19 Holiday pay	IAS38 Cloud	IFRIC 12 PFI	Category reallocation	Core (Table M4 stat)	Line	Description
		£m	£m	£m	£m	£m	£m	£m		
4.1	Turnover	1,364.904						1,364.904	4.1	Turnover
4.2	Operating expenditure	(416.038)			(16.958)			(432.996)	4.2	Operating expenditure
4.3	PPP costs	(177.443)				35.561	3.077	(138.805)	4.3	PPP costs (excluding PPP interest costs)
4.4	Responsive and planned repairs	(230.479)						(230.479)	4.4	Responsive and planned repairs
4.5	Current Cost Depreciation	(673.173)	371.530			(13.234)		(314.877)	4.5	Depreciation charge
								-		
4.6	Amortisation of deferred income	1.504						1.504	4.6	Amortisation of deferred income
4.7	Operating income	-						-	4.7	Operating income
4.9	Profit or loss on disposal of fixed assets	0.419				0.321	(3.077)	(2.337)	4.9	Profit or loss on disposal of fixed assets
4.10	Other income	-						-		
4.11	Net interest receivable less payable	(135.747)				(12.702)		(148.449)	4.11	Net interest receivable less payable
								-		
								-		
4.12	Profit on ordinary activities before taxation	(266.054)	371.530	-	(16.958)	9.946	-	98.464	4.12	Profit before taxation
4.13	Taxation - current	4.582						4.582	4.13	Taxation - current
4.14	Taxation - deferred	(31.356)						(31.356)	4.14	Taxation - deferred
4.19	Retained profit for year	(292.828)	371.530	-	(16.958)	9.946	-	**71.690**	4.19	Profit retained

Line	Description (Table M4b stat)	Core	IFRS adjustments - IAS 19 Pension adjs and CCA adjustments: Actuarial losses	CCA reversal	Service costs adj	Interest	Tax	Core (Table M4b stat)	Line	Description
			£m	£m	£m	£m	£m	£m		
4b.1	Profit for the year	**(292.828)**						**71.690**	19.1	Profit for the year
4b.2	Actuarial gains/losses on post employment plans	-	75.205	-	-	-	-	75.205	19.2	Actuarial gains/losses on post employment plans
4b.3	Post emp. plans non cash IAS19 adjs, net of tax	-	-	-	(37.094)	(1.775)	8.189	(30.680)	19.3	Post emp. plans non cash IAS19 adjs, net of tax
4b.4	Other gains and losses	9840.170	-	(9,840.170)	-	-	-	-	19.4	Other gains and losses
4b.5	Total comprehensive income for the year	**9,547.342**	75.205	(9,840.170)	(37.094)	(1.775)	8.189	**116.215**	19.5	Total comprehensive income for the year

Appendix 1.2

Scottish Water - Year ended 31 March 2023

Reconciliation of Regulatory Accounts Balance Sheet (Table M5) to IFRS Regulatory Balance Sheet (Table M5 stat) to Company Statutory Balance Sheet

TABLE M5			IFRS adjustments:					TABLE M5 Stat				Reallocations		Statutory Accounts (IFRS)	
			IAS19	CCA	IFRIC12	IAS38	Reallocate								
			Pension /	Fixed assets /	PFI assets/	Cloud									
Line	Description	Core	holiday pay	reserves	finance lease	Software	reserves		Line	Description	Non core	Various		Company	Description
		£m (3dp)						£m (1dp)						£m (1dp)	
	Fixed Assets									*Fixed Assets*					*Fixed Assets*
5.1	Tangible Assets	83,272.125		(76,271.8)	175.2	(61.0)		7,114.5	5.1	Tangible Assets		(9.2)	(i)	7,105.3	Property, plant and equipment
												9.2	(i)	9.2	Intangible assets
								-				37.6	(iv)	37.6	Investments
												24.6	(vii)	24.6	Retirement benefit asset
	Total fixed assets	83,272.125						7,114.5							
												4.1	(iv)	4.1	Inventories
	Other Operating Assets and liabilities											113.8	(iv)	113.8	Trade and other receivables
5.2	Working capital	(260.604)	(36.0)					(296.6)	5.2	Working capital	7.9	305.1	(iv)	16.4	Current tax asset
5.3	Cash at bank and in hand	155.459						155.5	5.3	Cash		(155.5)	(ii)	-	
5.4	Short term deposits	234.800						234.8	5.4	Short term deposits		155.5	(ii)	390.3	Cash and cash equivalents
5.5	Overdrafts	-						-	5.5	Overdrafts				-	
5.6	*Net operating assets*	83,401.780						7,208.2	5.6	*Net operating assets*				7,701.3	*Total Assets*
	Non-operating assets and liabilities														
5.7	Borrowings (excl. govt. loans)	-						-	5.7	Borrowings (excl. govt. loans)		(406.5)	(iv)	(406.5)	Trade and other payables
5.8	Investment - loan to group company	-						-	5.8	Investment - loan to group company		(22.3)	(v)	(22.3)	Other loans and borrowings
5.9	Investment - Other	37.639						37.6	5.9	Investment - Other		(37.6)	(iv)	-	
5.10	Corporation tax payable	16.478						16.5	5.10	Corporation tax payable		(16.5)	(iv)	-	
5.11	Dividends payable	-						-	5.11	Dividends payable					
5.12	Total non-operating assets and liabilities	54.117						54.1	5.12	Total non-operating assets and liabilities					
												(13.9)	(vi)	(13.9)	Provisions for liabilities
	Creditors - amounts falling due after more than one year													(442.7)	*Current Liabilities*
5.13	Borrowings (excl. govt. loans)	-						-	5.13	Borrowings (excl. govt. loans)				-	
5.14	*Other Creditors*	(74.400)						(74.4)	5.14	*Other Creditors*				(74.4)	Trade and other payables
5.15	Total Creditors falling due after more than one year	(74.400)						(74.4)	5.15	Total Creditors falling due after more than one year					
												(153.7)	(v)	(153.7)	Other loans and borrowings
	Provision for liabilities & charges														
5.16	Deferred tax provision	(681.178)						(681.2)	5.16	Deferred tax provision	(1.2)	(6.1)	(vii)	(688.5)	Deferred tax liabilities
5.17	Post employment asset / (liabilities)	-	18.5					18.5	5.17	Post employment asset / (liabilities)		(18.5)	(vii)	-	Retirement benefit obligations
5.18	Other provisions	(32.890)	9.0					(23.9)	5.18	Other provisions		13.9	(vi)	(10.0)	Provisions for liabilities
5.19	Total provisions	(714.068)						(686.6)	5.19	Total provisions					
5.20	*Net assets employed*	82,667.429	(8.5)	(76,271.8)	175.2	(61.0)	-	6,501.3	5.20	*Net assets employed*	6.7	(176.0)		6,332.0	*Net assets*
	Capital and reserves									*Capital & reserves*					*Capital & reserves*
5.21	Government Loans	4,508.736						4,508.7	5.21	Government Loans				4,508.7	Government loans
5.22	Income and expenditure account	1,753.465	(8.5)		175.2	(61.0)	(1,683.2)	176.0	5.22	PPP debt / lease		(176.0)	(v)	(0.0)	
5.23	Current cost reserve	76,271.798		(76,271.8)			1,683.2	1,683.2	5.23	Income and expenditure account	6.7			1,689.9	Retained earnings
5.24	Other reserves	133.430						133.4	5.24	Other reserves				133.4	Other reserves
5.25	*Total capital & reserves*	82,667.429	(8.5)	(76,271.8)	175.2	(61.0)	-	6,501.3	5.25	*Total capital & reserves*	6.7	(176.0)		6,332.0	*Equity*

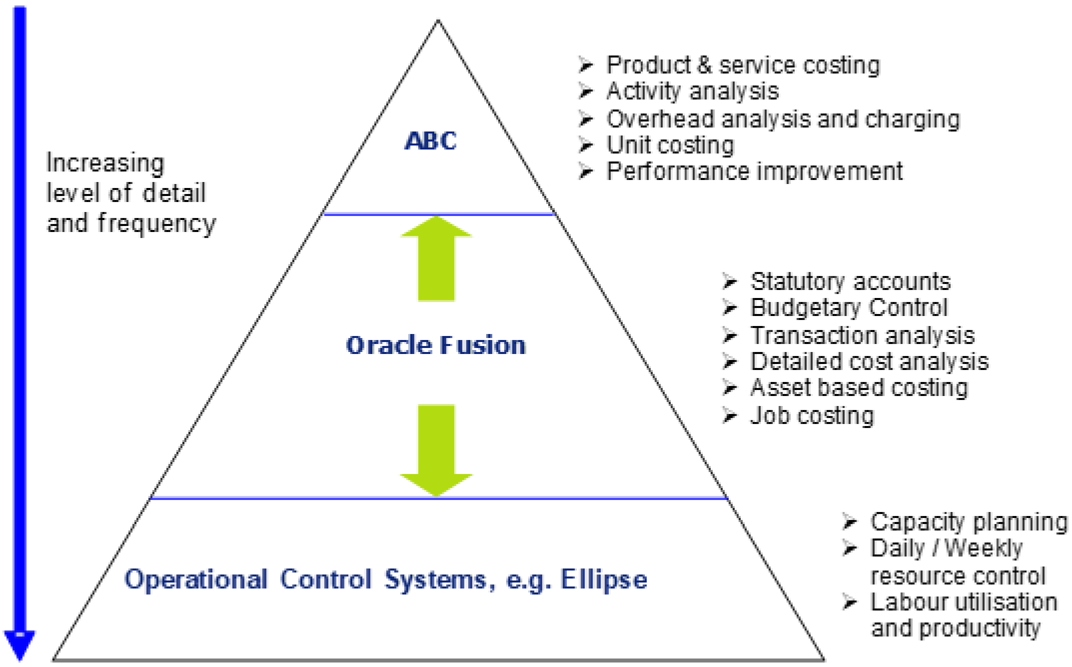
Appendix 2

Methodology for Scottish Water's Activity Based Management (ABM) process

ABM provides analysis of the costs of key activities and processes and seeks to link these to the factors that cause or drive our level of cost. This allows us to develop an understanding of the full cost of providing services, either internally within Scottish Water, or to our external customers.

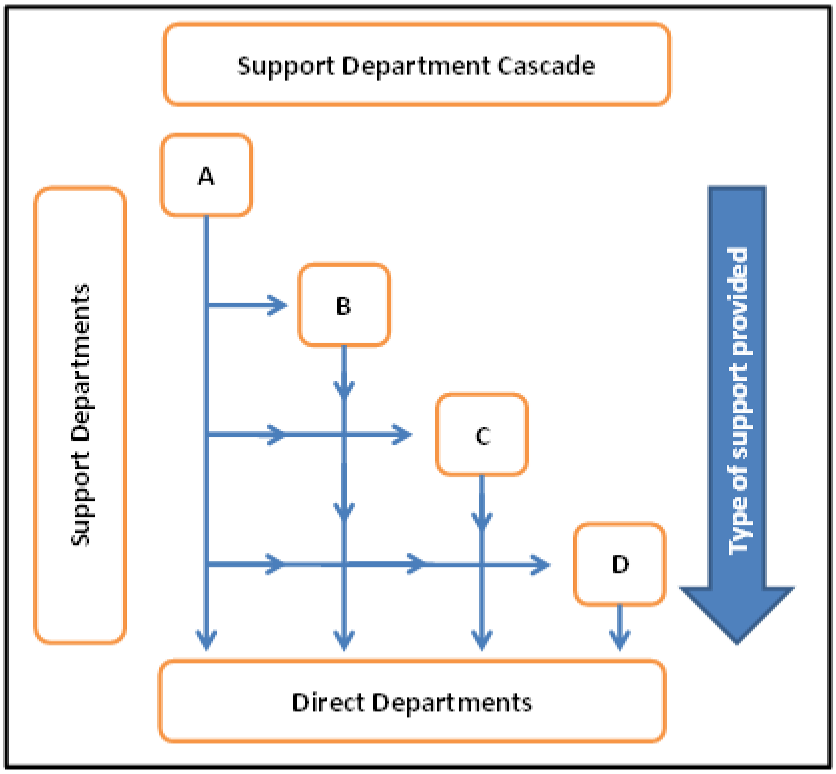
Scottish Water has built an ABM toolkit founded upon consistent principles which apply across some key core systems and processes.

Activity Based Management data (financial and non-financial) is captured in various corporate sources. The key systems which provide ABM analysis for the M18 Tables are:



System	ABM Process Overview
Ellipse Works & Asset Management System	Ellipse is used to hold Scottish Water's Asset Inventory and to manage operational activity by individual job (work order), activity and asset. Time spent working on work orders is captured in Ellipse via timesheets, integrated mobile devices or laptops. Material issued to jobs from stock is also captured by work order. Time and materials are then costed and interfaced to the Oracle Fusion Financial System on a daily basis. See overview diagram below.

Oracle Fusion Financial & Procurement System	Oracle Fusion is Scottish Water's primary financial and procurement system. The key modules utilised by Scottish Water are Procurement, Accounts Payable, Projects, Timesheets, Billing, Accounts Receivable, General Ledger & Fixed Assets. Accounting separation within the Scottish Water group of companies has been enabled within Oracle Fusion. Business Units are the highest level entity in Oracle Fusion and are used to securely separate data whilst providing access to data and processes. Business units have been used to separate all subsidiary companies from Scottish Water. Cross-business unit transactions can only be made via inter-company invoicing. This ensures there is sufficient governance surrounding any inter-company transactions. Within Scottish Water capture of activity based information within Oracle Fusion has been enabled through the set up of our coding structure, systems and processes. Cost codes have been set up within Oracle Fusion to capture and sub-analyse costs by: • Individual work order; • Individual asset; • Each project; • Each support department; and • Expense subjective (account). All costs are held in Oracle Fusion and allocated either directly through Oracle Fusion Procurement or operational costing through the Ellipse-Oracle Fusion interface. Oracle Fusion, therefore, provides comprehensive costing analysis, on a monthly basis, of the costs directly attributable (including some key support activity recharges) to each team, asset, zone, project, service and job.
Excel (ABC) Activity Allocation Model	The ABC calculations are carried out in a model using excel spreadsheets to give transparency of cost allocations and optimise processing time. The overall cost allocation method is broadly unchanged from the earlier Hyperion Profitability & Cost Management (HPCM) model and uses the same cost inputs, cost drivers and processing logic. The process allocates support department costs against support activities in a 'cascade' in order of the nature of support provided, those departments providing the most support to other support departments first, and then cascades costs in one direction only, as shown in the diagram below.

	 The ABC allocation model is structured around Scottish Water's key (c.250) activities and is run annually to cover all profit and loss expenditure. Oracle Fusion feeds total expenditure directly into the modelling process. Where activity splits have already been captured, e.g. Ellipse effort by activity / asset, these are also fed directly into the model process. Costs are analysed by activity and for each activity a non financial driver is captured. The non financial driver is the measurable factor which is judged to drive activity cost, or the level of resource consumption. In the model these drivers are used to allocate activity costs to services. The non financial driver data is collected from a variety of sources. Output from the ABM model is an estimate of the full cost of services, by activity, which feed into the E & M Table classifications.
Non-financial Driver Data Sources	Examples of systems and drivers are: • LIMS – Lab tests processed and samples taken; • Oracle CRM – Customer calls and written contacts; • Gemini – Waste movements; • Ellipse – Number of jobs, man hours, stores issues, etc; and • Oracle Fusion – Number of invoices, purchase orders, customer bills, man hours.

Ellipse / Oracle Fusion Integration