**Company Registration No. 4677985**

# ARTESIAN FINANCE II PLC

**Annual Report and Financial Statements**

Year ended 31 March 2022

# ANNUAL REPORT AND FINANCIAL STATEMENTS 2022

## CONTENTS


| CONTENTS | PAGE |
|---|---|
| Officers and professional advisers | 1 |
| Strategic report | 2-3 |
| Directors’ report | 4-5 |
| Directors' responsibilities statement | 6 |
| Independent auditor’s report | 7-11 |
| Statement of comprehensive income | 12 |
| Statement of financial position | 13 |
| Statement of changes in equity | 14 |
| Statement of cash flows | 15 |
| Notes to the Financial Statements | 16-24 |

# ANNUAL REPORT AND FINANCIAL STATEMENTS 2022

## OFFICERS AND PROFESSIONAL ADVISERS

### DIRECTORS

Colin Benford
Apex Trust Corporate Limited
Apex Corporate Services (UK) Limited

### SECRETARY

Apex Trust Corporate Limited
Bastion House
6th Floor
140 London Wall
London
United Kingdom
EC2Y 5DN

### REGISTERED OFFICE

Bastion House
6$^{th}$ Floor
140 London Wall
London
United Kingdom
EC2Y 5DN

### BANKERS

The Royal Bank of Scotland plc
Corporate Banking
5th Floor
250 Bishopsgate
London
United Kingdom
EC2M 4AA

### AUDITOR

Ernst & Young LLP
25 Churchill Place
Canary wharf
London
United Kingdom
E14 5EY

## STRATEGIC REPORT

The "Directors" present their strategic report for Artesian Finance II plc ("the Company") for the year ended 31 March 2022.

### ACTIVITIES

The Company was incorporated in the United Kingdom and commenced operations on 25 February 2003. It is registered as a public limited company under the Companies Act 2006.

The principal activity of the Company is to hold loans advanced to water companies.

### PRINCIPAL ACTIVITY

The Company is authorised to issue bonds up to £500,000,000 (2021: £500,000,000) ("the Bonds"). The Company has no intention to change the business activities. The Bonds are unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest under the terms of a guarantee issued by Assured Guaranty UK Limited (formerly Assured Guaranty (Europe) Plc).

### BUSINESS REVIEW

The loan portfolio of the Company consists of two fixed rate and three UK Retail Price Index ("RPI") linked loans which were funded through the issuance of the fixed rate bonds. Total return swaps were entered into by the Company to exchange RPI linked cash flows it receives on the loans for the fixed coupon amount payable on the Bonds. The net fair value increase of these assets is £26,533,000 (2021: £13,296,000); offset by a net fair value increase of the liabilities of £26,635,000 (2021: £13,238,000). Total assets are the key performance indicator for the Company. The total assets for 2022 are £852,868,000 (2021: £826,389,000).

### PRINCIPAL RISKS AND UNCERTAINTIES

The principal risks facing the Company are liquidity risk, interest rate risk and credit risk. These risks have been monitored on an ongoing basis during the period and the Company has policies in place to mitigate these risks to enable it to continue as a going concern. Refer to note 1 of the Financial Statements for details.

The directors acknowledge that the global macro-economic indicators and general business environment remained challenging, both in 2021 and during the first half of 2022. Market liquidity constraints, limited availability of credit and difficult trading conditions continue to pose significant challenges to businesses and borrowers to whom the Company has exposure.

The COVID-19 pandemic has prompted many changes that may prove to be permanent shifts in customer behaviour and economic activity, such as changes in spending patterns and more working from home. These changes may have long-lasting impacts on the economic environment, including asset prices. The Company's assets are comprised of fixed rate and RPI linked loans to UK incorporated water companies, which are collateralised to listed fixed rate bonds. The most likely expected financial impact is in respect of the loans advanced by the Company. This impact is not expected to be significant given that a guarantee is provided by Assured Guaranty UK Limited, which unconditionally and irrevocably guarantees all scheduled payments of principal and interest throughout the life of all related bonds issued.

The directors believe that the Company is not directly impacted by the on-going conflict in Ukraine and the associated Russian sanctions. If, as seems likely, the conflict in Ukraine impacts economic growth in Europe, then there could be an indirect effect on the Company, but the directors anticipate the impact would be minimal and certainly no worse than the economic turbulence experienced during the COVID-19 pandemic.

Further, we have considered the existence of total return swaps and our assessment of financial performance of the underlying water companies and their liquidity position, which has mitigated the uncertainties associated with Covid-19 including the different ways in which this could impact the cash flows, solvency and liquidity position of the Company.

Based on this assessment, the Directors have a reasonable expectation that there is no material impact of Covid-19 on the Company's financial instruments valuation or liquidity and the Company has adequate resources to continue in operational existence for the period to 31st August 2023, which is in excess of 12 months from when the financial statements are authorised for issue.

We continue to monitor the potential impact of the above matters on the Company.

Notwithstanding the risks and uncertainties above, the financial statements have been prepared on the going concern basis as discussed in Note 1.

## STRATEGIC REPORT (CONTINUED)

### PRINCIPAL RISKS AND UNCERTAINTIES (CONTINUED)

**Credit risk**

The main risk arising from the Company's financial instruments is credit risk. The Company faces the credit risk that the borrowers might not be able to meet their obligations as they fall due. The Company has purchased a guarantee over the principal and the interest due on the bonds from Assured Guaranty UK Limited, who are currently rated by Standard & Poor's at AA (2021: AA).

The maximum exposure to credit risk arising on the Company's financial assets as at the reporting date and prior year end is the Statement of Financial Position amount. No loans are past due or impaired at the year-end or prior year-end.

**Liquidity risk**

Liquidity risk is the risk that the Company is unable to meet its obligations as they fall due.

Funding has been obtained through the issue of bonds.

Liquidity risk is mitigated by both matching the timing of receipts and payments on the loans and derivative with the obligations on the bonds and having in place a guarantee to ensure that its obligations on the bonds can be met.

**Interest rate risk**

Interest rate risk is managed by matching the interest terms of the bonds issued with the loans held. Total return swaps were entered into by the Company to exchange index-linked cash flows it receives on its loan assets for the fixed coupon amount payable on the bonds. The swap counterparties continue to have high credit ratings; therefore no significant interest rate risk issues are noted.

**Director's Duties**

Section 172(1) of the Companies Act 2006 (Section 172) is one of the statutory duties that directors have and requires them to promote the success of the Company for the benefit of shareholders as a whole while taking into account the interests of other stakeholders and, in so doing, have regard to the matters set out in Section 172(1)(a) to (f). These include the long term consequences of decisions, colleague interests, the need to foster the Company's business relationships with suppliers, customers and others; the impact on community and the environment and the Company's reputation.

Directors are supported in the discharge of their duties by the Company Secretary. All directors receive guidance on their statutory duties, including Section 172(1), and were briefed on the reporting requirements introduced by the Companies (Miscellaneous Reporting) Regulations 2018 in advance of the effective date.

Approved by the Board of Directors and signed on behalf of the Board

Colin Benford
Director
Date: 2 August 2022

# DIRECTORS' REPORT

The Directors present their annual report and the audited financial statements of the Company for the year ended 31 March 2022.

## RESULTS AND DIVIDENDS

The results for the year and the state of the Company's affairs as at 31 March 2022 are set out in the accompanying financial statements. The Directors do not recommend the payment of a dividend (2021: Nil).

## DIRECTORS

The Directors who served throughout the year are as follows:

Colin Benford
Apex Trust Corporate Limited
Apex Corporate Services (UK) Limited

None of the Directors has any beneficial interest in the Company (2021: Nil).

## EMPLOYEES

The Company had no employees in the current year or prior year.

## DIRECTORS' INDEMNITIES

Apex Trust Corporate Limited provided third party indemnity provisions for the benefit of Colin Benford during the year. These indemnity provisions remain in force at the date of this report.

## CORPORATE GOVERNANCE

The Board of Directors has overall responsibility for the Company's internal controls systems and risk control which are managed in accordance with the terms of the Bonds issued, as described in the Offering Circular for the Bonds. These are monitored through regular meetings of the Board.

## FUTURE DEVELOPMENTS

The Directors do not anticipate any changes to the present level of activity or the nature of the Company's business in the near future.

## AUDITOR

Ernst & Young LLP has expressed their willingness to continue in office as auditor and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting.

## GOING CONCERN

The Company's business activities, performance and position, as well as principal risks and uncertainties are set out on page 2. In addition, note 1 to the financial statements includes the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments; and its exposures to credit risk and liquidity risk.

The Company has met its level of expected results for the financial period, and determined that its assets are performing as at the Statement of Financial Position date and therefore does not expect a shortfall in cash receipts from the borrowers. As at the Statement of Financial Position date, the Company has net assets of £1,195,000 (2021: £1,274,000). Currently the long-term assets are funded by long-term fixed rate bonds.

Total return swaps were entered into by the Company to exchange index-linked cash flows it receives on its loan assets for the fixed coupon amount payable on the Bonds. The swap counterparties continue to have high credit ratings; therefore no significant credit issues are noted. In order to protect the Company and the bond holders in the event of a shortfall of funds available to pay amounts on the Bonds, the Company has purchased a guarantee over the principal and the interest due on the bonds from Assured Guaranty UK Limited, who are currently rated by Standard & Poor's at AA (2021: AA).

## DIRECTORS' REPORT (CONTINUED)

### GOING CONCERN (CONTINUED)

After making enquiries, and considering the uncertainties set out on page 2, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the period to 31st August 2023, which is in excess of 12 months from when the financial statements are authorised for issue. For these reasons, they continue to adopt the going concern basis in preparing the Annual Report and Financial Statements.

### DISCLOSURE OF INFORMATION TO THE AUDITOR

Each of the persons who is a Director at the date of approval of this report confirms that:

(1) so far as the Director is aware, there is no relevant audit information of which the Company's auditor is unaware; and

(2) the Director has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of S418 of the Companies Act 2006.

Approved by the Board of Directors and signed on behalf of the Board

Colin Benford
Director
Date: 2 August 2022

## DIRECTORS' RESPONSIBILITIES STATEMENT

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

Company law requires the Directors to prepare a Strategic Report, Directors' Report and financial statements for each financial year. Under that law, the Directors have elected to prepare the financial statements in accordance with FRS 102, The Financial Reporting Standard applicable in the UK and Republic of Ireland; and must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs at the end of the year and the profit or loss of the Company for that year. In preparing these financial statements, the Directors are required to:

- Select suitable accounting policies in accordance with section 10 of FRS 102 and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with specific requirements in FRS 102 is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the company financial position and financial performance;

in respect of the company financial statements, state whether FRS 102 has been followed, subject to any material departures disclosed and explained in the financial statements; and prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that they have complied with the above requirements in preparing the financial statements.

Approved by the Board of Directors
and signed on behalf of the Board

Colin Benford
Director
Date: 2 August 2022

**Opinion**

We have audited the financial statements of Artesian Finance II Plc for the year ended 31 March 2022 which comprise the Statement of comprehensive income, the Statement of financial position, the Statement of changes in equity, Statement of cash flows and the related notes 1 to 14 including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the financial statements:

- give a true and fair view of the company's affairs as at 31 March 2022 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

**Basis for opinion**

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

**Conclusions relating to going concern**

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. Our evaluation of the directors' assessment of the company's ability to continue to adopt the going concern basis of accounting included confirmation of our understanding of the nature of the company, with the bonds being collateralised by underlying loans to water companies, and a guarantee in place to unconditionally and irrevocably guarantee all scheduled payments of principal and interest due throughout the life of the bonds. We also reviewed the director's going concern disclosures, including analysis of the impact of COVID-19, and assessed the financial performance of the underlying water companies. Based on the procedures performed, we concur with the directors' assessment that the use of the going concern basis is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for the period to 31st August 2023, which is in excess of 12 months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the company's ability to continue as a going concern.

**Overview of our audit approach**

| | |
|---|---|
| Key audit matters | • The calculation of the fair value of loans, bonds and derivatives is subject to the risk of management override as it includes a high degree of subjectivity in the fair value model and depends on assumptions used by management. |
| Materiality | • Overall materiality of £4.13m which represents 0.5% of Total assets. |

**An overview of the scope of our audit**

**Tailoring the scope**

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for the company. This enables us to form an opinion on the financial statements. We take into account size, risk profile, the organisation of the company and effectiveness of controls, including controls and changes in the business environment when assessing the level of work to be performed. All audit work was performed directly by the audit engagement team.

**Changes from the prior year**

There were no changes to the scope of our audit compared to the prior year.

**Key audit matters**

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

<table>
<tr><th>Risk</th><th>Our response to the risk</th><th>Key observations communicated to those charged with governance</th></tr>
<tr><td colspan="3">The calculation of the fair value of loans, bonds and derivatives is subject to the risk of management override as it includes a high degree of subjectivity in the fair value model and depends on assumptions used by management.</td></tr>
<tr><td rowspan="2">We consider inappropriate valuation of financial instruments held at fair value and related revenue recognition as a significant risk. Based on our assessment of the level of management judgement involved in selection of valuation techniques/models and relevant inputs, the following instruments were classified as part of the significant risk:<br>• Loans advanced to water companies (£852m as at 31 March 2022 and £824m as at 31 March 2021, as per Note 1 on page 17, and Note 7 on page 19)<br>• Bonds issued (£460m as at 31 March 2022 and £504m as at 31 March 2021, as per Note 1 on page 17, and Note 9 on page 20)<br>• Total return swap derivative financial instruments (net value of £390m as at 31 March 2022 and £319m as at 31 March 2021, as per Note 1 on page 17, and Note 11 on page 21)<br>Our assessment of the significant risk did not change compared to the previous year as there were no significant changes in the company's activities.</td><td>We performed a walkthrough to confirm our understanding of the company's process and adequacy of controls in the area of relating to financial instruments. We applied a fully substantive approach to our audit due to limited number of transactions performed by the company in the year ended 31 March 2022.<br>We involved our valuation and modelling specialists to:<br>• Independently re-value the loans advanced to water companies using prices of comparable positions and other data points.<br>• Assess the appropriateness of the valuation techniques and significant assumptions used to determine the fair value of bonds issued.<br>• Independently re-value the total return swap derivatives using independent data and taking into account an underlying reference curve in calibrating the bond price (Z-spread).<br>• Perform corroborative calculations to understand the impact on value of certain key assumptions adopted by management.</td><td rowspan="2">Based on the procedures performed, we concluded that the fair value of financial instruments and the recognition of related income is fairly stated, in all material respects as at 31 March 2022 and for the year then ended, in accordance with FRS 102.</td></tr>
<tr><td>We have performed a review of financial statements disclosures relating to financial instruments to ensure these disclosures are appropriate and in accordance with FRS 102.</td></tr>
</table>

**Our application of materiality**

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

**Materiality**

*The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.*

We determined materiality for the company to be £4.13 million (2021: £4.13 million), which is 0.5% (2021: 0.5%) of Total assets. We believe that total assets represent the key focus for the users of the financial statements, being the Bond holders who will focus more on the underlying assets that form the main source for repaying the interest and principal of the bonds issued. We therefore considered total assets to be the most appropriate basis for determination of our materiality.

During the course of our audit, we reassessed initial materiality and did not apply significant changes to the materiality calculation.

**Performance materiality**

*The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.*

On the basis of our risk assessments, together with our assessment of the company's overall control environment, our judgement was that performance materiality was 50% (2021: 50%) of our planning materiality, namely £2.1m (2021: £2.1m). We have set performance materiality at this percentage based on various considerations including the risks factors identified and the adoption of a fully substantive audit approach.

**Reporting threshold**

*An amount below which identified misstatements are considered as being clearly trivial.*

We agreed with the those charged with governance that we would report to them all uncorrected audit differences in excess of £207k (2021: £207k), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

**Other information**

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

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

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

We have nothing to report in this regard.

**Opinions on other matters prescribed by the Companies Act 2006**

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

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

**Matters on which we are required to report by exception**

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

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

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

**Responsibilities of directors**

As explained more fully in the directors' responsibilities statement set out on page 6, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

**Auditor's responsibilities for the audit of the financial statements**

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

**Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud**

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

However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the company and management.

Our approach was as follows:

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the company and determined that the most significant are:
    - UK Companies Act 2006
    - Tax legislation (governed by HM Revenue and Customs)
    - UK GAAP including FRS 102
- We understood how Artesian Finance II Plc is complying with those frameworks by inquiring with management and directors as to any known instances of non-compliance or suspected non-compliance with laws and regulations. We reviewed correspondence between the Company and regulators, and minutes of Board Committee meetings.
- We assessed the susceptibility of the company's financial statements to material misstatement, including how fraud might occur by testing all material adjustments which affect the financial statements to assess their appropriateness. These procedures were designed to provide reasonable assurance that the financial statements were free from fraud and error.

- Based on this understanding, we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved inquiring of key management as well as reviewing correspondence with the relevant authorities.

A further description of our responsibilities for the audit of the financial statements is located on the

Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

**Other matters we are required to address**

- We were appointed by the company on 29 September 2017 to audit the financial statements for the year ending 31 March 2017 and subsequent financial periods.

  The period of total uninterrupted engagement including previous renewals and reappointments is 6 years, covering the years ending 31 March 2017 to 31 March 2022.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the company and we remain independent of the company in conducting the audit.
- The audit opinion is consistent with the additional report to those charged with governance.

**Use of our report**

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

Jean-Philippe Faillat (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London
Date: 05 August 2022

## STATEMENT OF COMPREHENSIVE INCOME
**For the year ended 31 March 2022**

| | Note | 2022 £'000 | 2021 £'000 |
|---|---|---|---|
| Interest income | 3 | 20,806 | 20,806 |
| Interest expense | | (20,757) | (20,757) |
| Net interest income | | 49 | 49 |
| Operating expenses | 4 | (76) | (89) |
| Other operating income | | 59 | 59 |
| Change in fair value of loans | 11 | 27,904 | 13,644 |
| Change in fair value of bonds | 11 | 43,597 | 12,682 |
| Change in fair value of swaps | 11 | (71,603) | (26,268) |
| **(LOSS)/PROFIT FOR THE YEAR BEFORE TAXATION** | | (70) | 77 |
| Tax charge | 6 | (9) | (9) |
| **TOTAL COMPREHENSIVE (LOSS)/INCOME FOR THE YEAR** | | (79) | 68 |

The accompanying notes from pages 16 to 24 are an integral part of these financial statements.

The results above arose wholly from continuing operations in the current and prior year.

## STATEMENT OF FINANCIAL POSITION
## As at 31 March 2022

| | Note | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Loans to customers | 7 | 831,724 | 805,254 |
| **CURRENT ASSETS** | | | |
| Loans to customers | 7 | 20,578 | 19,144 |
| Cash and cash equivalents | | 566 | 620 |
| Derivatives at fair value | 11 | - | 1,371 |
| | | 21,144 | 21,135 |
| **TOTAL ASSETS** | | 852,868 | 826,389 |
| **CURRENT LIABILITIES** | | | |
| Other payables | 8 | 41 | 118 |
| Tax liabilities | 6 | 9 | 9 |
| Bonds issued | 9 | 20,354 | 20,470 |
| Derivatives at fair value | 11 | 174 | - |
| | | 20,578 | 20,597 |
| **NON-CURRENT LIABILITIES** | | | |
| Bonds issued | 9 | 440,572 | 484,053 |
| Derivatives at fair value | 11 | 390,523 | 320,465 |
| | | 831,095 | 804,518 |
| **TOTAL LIABILITIES** | | 851,673 | 825,115 |
| **NET ASSETS** | | 1,195 | 1,274 |
| **EQUITY** | | | |
| Share capital | 10 | 13 | 13 |
| Retained earnings | | 1,182 | 1,261 |
| **TOTAL EQUITY** | | 1,195 | 1,274 |

The accompanying notes from pages 16 to 24 are an integral part of these financial statements.

These financial statements of Artesian Finance II plc, registration number 4677985, were approved and authorised for issue by the Board of Directors on 2 August 2022.

Signed on behalf of the Board of Directors

Colin Benford
Director
Date: 2 August 2022

## STATEMENT OF CHANGES IN EQUITY

### For the year ended 31 March 2022

| | Share capital £'000 | Retained earnings £'000 | Total £'000 |
|---|---|---|---|
| **Balance at 01 April 2020** | 13 | 1,193 | 1,206 |
| Total comprehensive income for the financial year | - | 68 | 68 |
| **Balance at 31 March 2021** | 13 | 1,261 | 1,274 |
| Total comprehensive loss for the financial year | - | (79) | (79) |
| **Balance at 31 March 2022** | 13 | 1,182 | 1,195 |

The accompanying notes from pages 16 to 24 are an integral part of these financial statements.

## STATEMENT OF CASH FLOWS
## For the year ended 31 March 2022

| | Note | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|---|
| **Operating (loss)/profit before taxation** | | (70) | 77 |
| Adjustments for: | | | |
| Changes in fair value of swaps | 11 | 71,603 | 26,268 |
| Changes in fair value of loans | 11 | (27,904) | (13,644) |
| Changes in fair value of bonds | 11 | (43,597) | (12,682) |
| Changes in other payables | | (77) | 64 |
| **Net cash flows from operating activities before tax** | | (45) | 83 |
| Tax paid | | (9) | (9) |
| **Net cash flows from operating activities after tax** | | (54) | 74 |
| **Net (decrease)/increase in cash and cash equivalents** | | (54) | 74 |
| Cash and cash equivalents at the beginning of the year | | 620 | 546 |
| **Cash and cash equivalents at the end of the year** | | 566 | 620 |
| **Supplemental information** | | | |
| Interest received | | 20,806 | 20,806 |
| Interest paid | | (20,757) | (20,757) |

The accompanying notes from pages 16 to 24 are an integral part of these financial statements.

| **ANALYSIS OF CHANGE IN NET DEBT** | Bonds Issued<br>£'000 | Derivative Instruments<br>£'000 | Net Debts<br>£'000 |
|---|---|---|---|
| Opening balance as at 01 April 2021 | 504,523 | 319,094 | 823,617 |
| Cash Movement | - | - | - |
| Non Cash Movement | (43,597) | 71,603 | 28,006 |
| **Closing balance as at 31 March 2022** | 460,926 | 390,697 | 851,623 |

| **ANALYSIS OF CHANGE IN NET DEBT** | Bonds Issued<br>£'000 | Derivative Instruments<br>£'000 | Net Debts<br>£'000 |
|---|---|---|---|
| Opening balance as at 01 April 2020 | 517,205 | 292,826 | 810,031 |
| Cash Movement | - | - | - |
| Non Cash Movement | (12,682) | 26,268 | 13,586 |
| **Closing balance as at 31 March 2021** | 504,523 | 319,094 | 823,617 |

# NOTES TO THE FINANCIAL STATEMENTS
## For the year ended 31 March 2022

### 1. ACCOUNTING POLICIES

**General information**

Artesian Finance II plc ("the Company") is a public company limited by shares incorporated and registered in England in the United Kingdom under the Companies Act 2006. The address of the registered office is given on page 1. The nature of the Company's operations and its principal activities are set out in the Strategic Report.

**Basis of accounting**

The financial statements have been prepared in accordance with Financial Reporting Standard (FRS) applicable in the UK and Republic of Ireland issued by the Financial Reporting Council. The Company has presented its financial statements under Financial Reporting Standard 102 (FRS 102) issued by the Financial Reporting Council. The financial statements have been prepared on a going concern basis as explained below.

**Going Concern**

The directors acknowledge that the global macro-economic indicators and general business environment remained challenging both in 2021 and during the first half of 2022. Market liquidity constraints, limited availability of credit and difficult trading conditions continue to pose significant challenges to businesses and borrowers to whom the Company has exposure.

The COVID-19 pandemic has prompted many changes that may prove to be permanent shifts in customer behaviour and economic activity, such as changes in spending patterns and more working from home. These changes may have long-lasting impacts on the economic environment, including asset prices. The Company's assets are comprised of fixed rate and RPI linked loans to UK incorporated water companies, which are collateralised to listed fixed rate bonds. The most likely expected financial impact is in respect of the loans advanced by the Company. This impact is not expected to be significant given that a guarantee is provided by Assured Guaranty UK Limited, which unconditionally and irrevocably guarantees all scheduled payments of principal and interest throughout the life of all related bonds issued.

The directors believe that the Company is not directly impacted by the on-going conflict in Ukraine and the associated Russian sanctions. If, as seems likely, the conflict in Ukraine impacts economic growth in Europe, then there could be an indirect effect on the Company, but the directors anticipate the impact would be minimal and certainly no worse than the economic turbulence experienced during the COVID-19 pandemic.

Further, we have considered the existence of total return swaps and our assessment of financial performance of the underlying water companies and their liquidity position, which has mitigated the uncertainties associated with Covid-l9 including the different ways in which this could impact the cash flows, solvency and liquidity position of the Company.

Based on this assessment, the Directors have a reasonable expectation that there is no material impact of Covid-19 on the Company's financial instruments valuation or liquidity and the Company has adequate resources to continue in operational existence for the period to 31st August 2023, which is in excess of 12 months from when the financial statements are authorised for issue and have prepared the financial statements on a going concern basis.

**Critical accounting judgements**

The preparation of financial statements in conformity with FRS 102 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expense, in particular the estimation of future cash flows on the Loans to customers and Loan notes issued in order to determine the fair value of these instruments.

**Financial instruments**

Financial assets and financial liabilities are recognised in the Company's Statement of Financial Position when the Company becomes a party to the contractual provisions of the instrument. The Company's financial instruments comprise Loans to customers, Bond liabilities, derivative financial instruments, cash and creditors, which arise directly from its operations and are part of its principal activity.

# NOTES TO THE FINANCIAL STATEMENTS
## For the year ended 31 March 2022

### 1. ACCOUNTING POLICIES (CONTINUED)

**Financial instruments (continued)**

Under FRS 102, in accounting for its financial instruments a reporting entity is required to apply either;

a) the full provisions of Section 11 "Basic Financial Instruments" and Section 12 "Other Financial Instruments" of FRS 102;
b) the recognition and measurement provisions of International Accounting Standards 39 "Financial Instruments: Recognition and Measurement" ("IAS 39") and only the disclosure requirements of Sections 11 and 12 of FRS 102; or
c) the recognition and measurement provisions of International Financial Reporting Standards ("IFRS") 9 "Financial Instruments" ("IFRS 9") and the disclosure requirements of Sections 11 and 12 of FRS 102.

The Company has elected to apply the recognition and measurement provisions of IAS 39 and the disclosure requirements of Sections 11 and 12 of FRS 102.

**Loans to customers**

Loans to customers were designated and are accounted for in these financial statements as financial assets 'at fair value through profit or loss' (FVTPL) with any gain or loss on re-measurement being recognised in the statement of comprehensive income. Loans to customers were designated at FVTPL to significantly reduce a measurement or recognition inconsistency that would otherwise arise. Interest earned on the Loans to customers is included in the interest income line item in the statement of comprehensive income. Fair value is determined in the manner described in Note 11.

**Bonds issued**

The Bonds were designated and are accounted for at FVTPL with any gain or loss on re-measurement being recognised in the statement of comprehensive income. The Bonds were designated at FVTPL to significantly reduce a measurement or recognition inconsistency that would otherwise arise. Interest incurred on the Bonds is included in the interest expense line item in the statement of comprehensive income.

**Fair valuation**

The carrying amounts of all the Company's financial instruments equate to their fair values. For the fixed rate bonds issued, observed market prices (indicative bid and ask observations) have been used to determine fair values. For other financial instruments where no market values are available, fair values have been calculated by discounting cash flows at prevailing interest rates. In the calculation of discount factors for the fixed rate and RPI linked loans and total return swaps, a spread consistent with that implied on the fixed rate bonds issued has been applied.

**Derivative Instruments**

The Company does not enter into speculative derivative contracts. Derivative financial instruments are recorded at FVTPL, with any gain or loss on re-measurement being recognised in the statement of comprehensive income. The derivative instruments are classified as held for trading.

**Revenue recognition**

Financial assets and financial liabilities are recorded at fair value. Changes in fair value are recognised in profit or loss separately from interest income and expense.

**Segmental analysis**

The Directors have determined that the Company has only one reportable operating segment as all the investment income arises in the United Kingdom.

**Taxation**

The Company has elected to be taxed under the 'permanent' tax regime, for securitisation companies (contained in Statutory Instrument 2006/3296), under which the Company is taxed broadly by reference to its cash profit retained by the issuer during the period and not by reference to its accounting profit.

## NOTES TO THE FINANCIAL STATEMENTS
## For the year ended 31 March 2022

### 1. ACCOUNTING POLICIES (CONTINUED)

**Derecognition**

The Company derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Company is recognised as a separate asset or liability. The Company derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

**Key sources of estimation uncertainty**

The estimates and associated assumptions including credit risk are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements on carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates used in the financial statements.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both the current and future periods.

**Netting / Offsetting Assessment**

Netting / Offsetting assessment has been performed according to FRS 102. A financial asset and a financial liability shall be offset and the net amount presented in the statement of financial position when and only when, an entity:

- currently has a legally enforceable right to set off the recognised amounts; and
- intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

The Company does not meet any of the criteria mentioned above and therefore, the financial statements have not been presented on a net basis.

### 2. DIRECTORS AND EMPLOYEES

None of the Directors received any emoluments for their services to the Company during the year (2021: £nil).

None of the Directors have any interests in the Company as at year end (2021: £nil).

None of the Directors had any material interest in any contract of significance in relation to the business of the Company (2021: none).

The Company does not have any employees (2021: none).

### 3. INTEREST INCOME

| | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|
| Interest income on loans | 19,509 | 19,100 |
| Interest income on swaps | 1,297 | 1,706 |
| | 20,806 | 20,806 |

### 4. OPERATING EXPENSES

| | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|
| Administrative expenses incurred | 76 | 89 |

## NOTES TO THE FINANCIAL STATEMENTS
**For the year ended 31 March 2022**

### 5. REMUNERATION OF AUDITOR

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| **Amounts paid or payable to auditor:** | | |
| Audit of the Company's accounts: | | |
| Charge for the year* | 34 | 38 |

* Audit fees disclosed are exclusive of VAT.

### 6. TAXATION

a) Tax on profits/(losses)

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Current taxation: | | |
| Charge for the year | 9 | 9 |
| Tax charge for the year | 9 | 9 |

b) Reconciliation of the total tax charge

The actual tax charge differs from the expected tax charge computed by applying the standard rate of UK corporation tax of 19% (2021: 19%) as follows:

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| (Loss)/profit before tax | (70) | 77 |
| Expected tax (credit)/charge | (13) | 15 |
| Effects of: | | |
| Adjustment under s14(4) SI 2006/3296 | 13 | (15) |
| Adjustment under s14(1)(a)(ii) SI 2006/3296 | 9 | 9 |
| Total tax charge for the year | 9 | 9 |

The Company is taxed in accordance with Statutory Instrument No. 3296 'The Taxation of Securitisation Companies Regulations 2006' which requires that tax is charged on the cash profit retained by the issuer. No other amounts are taxable. There is no deferred tax recognised or unrecognised.

The UK Corporation tax rate applicable to the company from 1 April 2020 is 19%.

It was announced in the UK Government's Budget on 3 March 2021 that the main UK corporation tax rate will increase to 25% from 1 April 2023. This change was substantively enacted on 24 May 2021.

### 7. LOANS TO CUSTOMERS

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Loans to customers – fixed rate | 76,679 | 83,949 |
| Loans to customers – RPI indexed | 775,623 | 740,449 |
| | 852,302 | 824,398 |
| Loans falling due within one year | 20,578 | 19,144 |
| Loans falling due after more than one year | 831,724 | 805,254 |
| | 852,302 | 824,398 |

## NOTES TO THE FINANCIAL STATEMENTS
## For the year ended 31 March 2022

The loan portfolio at year end has nominal values amounting to £321,500,000 (2021: £321,500,000) and comprises of five loans to four water companies. Out of these five loans, three of them have RPI index-linked principal and interest rate characteristics while the remaining two have fixed rates of interest (see Note 11). The loans are due to mature on 30 September 2033, but the borrowers have the right to make voluntary prepayments if they give no less than 45 days' written notice in accordance with the loan agreement.

### 8. OTHER PAYABLES

| | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|
| Other payables | 41 | 118 |

### 9. BONDS ISSUED

| | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|
| Fixed rate bonds | (460,926) | (504,523) |
| Amounts falling due within one year | (20,354) | (20,470) |
| Amounts falling due after more than one year | (440,572) | (484,053) |
| | (460,926) | (504,523) |

The Company has issued fixed rate bonds which are listed on the London Stock Exchange with a nominal value of £345,950,000 under the Company's £500,000,000 bond issuance programme. The Bonds bear interest of 6% with a legal maturity date of 30 September 2033. The Bonds can be redeemed early under certain conditions described in the Offering Circular.

In order to protect the Company and the bond holders in the event of a shortfall of funds available to pay amounts on the Bonds, the Company has entered into a guarantee agreement for which borrowers make the payments of premium to an insurer. The guarantee is provided by Assured Guaranty UK Limited, who are rated by S&P at AA (2021: AA), which unconditionally and irrevocably guarantees all scheduled payments of principal and interest throughout the life of all related bonds issued.

### 10. SHARE CAPITAL

| | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|
| **Authorised** | | |
| 50,000 (2021: 50,000) ordinary shares of £1 each | 50 | 50 |
| **Called up, allotted and partly paid** | | |
| 50,000 (2021: 50,000) ordinary shares partly paid up at 25p each | 13 | 13 |

49,999 shares of the Company are held by Apex Trust Nominees No. 1 Limited as trustee on behalf of a Charitable Trust and 1 share by Apex Corporate Trustees (UK) Limited as trustee on behalf of a Charitable Trust. These shares were issued in 2003 for a cash consideration of 25p each.

# NOTES TO THE FINANCIAL STATEMENTS
## For the year ended 31 March 2022

### 11. FINANCIAL INSTRUMENTS

The Company's financial instruments principally comprise Loans advanced to water companies, Bonds issued, total return swap contracts, cash and other items arising directly from the Company's operations. It is, and has been throughout the year, the Company's policy that no trading in financial instruments shall be undertaken.

**Capital risk management**
The Company manages its capital to enable it to continue as a going concern.

The capital structure of the Company primarily comprises issued bonds. Other sources of funding consist of equity attributable to equity holders of the parent, comprising issued share capital and retained earnings.
The Company is not subject to any externally imposed capital requirements.

**Credit risk**
The main risk arising from the Company's financial instruments is credit risk. The Company faces the credit risk that customers might not be able to meet their obligations as they fall due. While the Loans are secured by a fixed and floating charge over customers' assets and their immediate holding companies, the Company considered the customers' ability to service the Loans to be the principal factor in assessing the credit risk and the decision to lend. With respect to the five loans to UK water board companies, the Directors conclude that there are no past due receivable balances at year-end (2021: £nil). South East Water Limited and Bristol Water plc are rated BAA2 (2021: BAA1) and Southern Water Services Limited is rated BAA3 (2021: BAA1) by Moody's as disclosed in their latest financial statements, Bournemouth Water Limited does not provide a rating. however, the Company performed an assessment based on the latest financial statements and concluded the credit quality is similar to the other water companies.

In order to protect the Company and the bond holders in the event of a shortfall of funds available to pay amounts on the Bonds, the Company has entered into a guarantee agreement for which borrowers make payments of premium to an insurer. The guarantee is provided by Assured Guaranty UK Limited, who are rated by S&P at AA (2021:AA), which unconditionally and irrevocably guarantees all scheduled payments of principal and interest throughout the life of all related bonds issued.

In addition, the Company faces credit risk on the swap counterparties' obligations under the agreement. The swap counterparties JP Morgan is rated A+ (2021: A+) and Belfius Bank SA (formerly known as Dexia Bank SA) is rated A (2021: A-) by S&P, and the Directors and management will continue to monitor this exposure.

The fixed and floating charge over the customers' assets, and their immediate holding companies, make up the primary collateral for the Loans.

The maximum exposure to credit risk arising on the Company's financial assets at the reporting date is the Statement of Financial Position amount of Loans to customers of £852,302,000 (2021: £824,398,000).

The maximum exposure on total return swaps, at the reporting date, is the Statement of Financial Position amount of Derivative Assets of £Nil (2021: £1,371,000). This year's amount of swaps consists of £ Nil (2021: £1,371,000) of derivatives assets and £390,697,000 (2021: £320,465,000) of derivatives liabilities.

The changes in fair value of the designated Loans and Bonds attributable to changes in credit risk have been calculated as a difference between their fair value determined as described in Note 1 and present value of future expected cash flows discounted using 6 month GBP Libor zero coupon curve.

**Financial assets at fair value through profit or loss**

| | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|
| Cumulative change in fair value of the loans attributable to changes in credit risk | (26,691) | (34,310) |
| Change during the year in fair value of the loans attributable to changes in credit risk | 7,619 | 52,019 |

## NOTES TO THE FINANCIAL STATEMENTS
## For the year ended 31 March 2022

### 11. FINANCIAL INSTRUMENTS (CONTINUED)

**Financial liabilities at fair value through profit or loss**

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Cumulative change in fair value of the fixed rate bonds attributable to changes in credit risk | 8,550 | 18,778 |
| Change during the year in fair value of the fixed rate bonds attributable to changes in credit risk | (10,228) | (30,038) |

**Liquidity risk**

Funding for purchase of the loan portfolio was obtained through issuance of fixed rate bonds to the market. The Company has entered into total return swaps to hedge the difference between amounts received on the loans to customers and amounts payable on the Bonds. In order to ensure that the Company has sufficient cash at maturity to redeem the Bonds, the swaps pay any difference between the principal repayment from the borrower and the total amount due to the bondholders.

The Company has in place a guarantee to ensure that sufficient liquidity is maintained to meet the obligations on the Bonds. As such if the Company faces a shortfall in cash resources to pay interest or principal on the notes, the bondholders would receive the required amount from the guarantor.

The table below reflects the undiscounted contractual cash flows of financial liabilities at the Statement of Financial Position date.

| As at 31 March 2022 | Carrying amount £'000 | Contractual cash flows £'000 | <1 month £'000 | 1-3 months £'000 | 3 months-1year £'000 | 1-5 years £'000 | 5 years and over £'000 |
|---|---|---|---|---|---|---|---|
| Non-derivative financial Liabilities | | | | | | | |
| Bonds issued | (460,926) | (584,656) | - | - | (20,757) | (83,028) | (480,871) |
| Other creditors | (41) | (41) | (41) | - | - | - | - |
| Current tax liabilities | (9) | (9) | (9) | - | - | - | - |
| | (460,976) | (584,706) | (50) | - | (20,757) | (83,028) | (480,871) |
| Derivative financial liabilities | | | | | | | |
| Total return swaps (net) | (390,697) | (521,744) | - | - | (181) | (10,639) | (510,924) |
| Total | (851,673) | (1,106,450) | (50) | - | (20,938) | (93,667) | (991,795) |

| As at 31 March 2021 | Carrying amount £'000 | Contractual cash flows £'000 | <1 month £'000 | 1-3 months £'000 | 3 months-1year £'000 | 1-5 years £'000 | 5 years and over £'000 |
|---|---|---|---|---|---|---|---|
| Non-derivative financial Liabilities | | | | | | | |
| Bonds issued | (504,523) | (605,413) | - | - | (20,757) | (83,028) | (501,628) |
| Other creditors | (118) | (118) | (67) | (10) | (41) | - | - |
| Current tax liabilities | (9) | (9) | - | - | (9) | - | - |
| | (504,650) | (605,540) | (67) | (10) | (20,807) | (83,028) | (501,628) |
| Derivative financial liabilities | | | | | | | |
| Total return swaps (net) | (319,094) | (401,307) | - | - | 1,390 | (163) | (402,534) |
| Total | (823,744) | (1,006,847) | (67) | (10) | (19,417) | (83,191) | (904,162) |

## 11. FINANCIAL INSTRUMENTS (CONTINUED)

**Liquidity risk (continued)**

The table below reflects the discounted contractual cash flows of financial derivatives at the Statement of Financial Position date.

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Total return swaps | (390,697) | (319,094) |
| Amounts falling due within one year | (174) | 1,371 |
| Amounts falling due after more than one year | (390,523) | (320,465) |

**Interest rate risk**

The Company finances its operations through the issue of bonds at a fixed rate of 6.00% per annum (p.a.). The loan to Bristol Water plc carries a fixed rate of interest of 6.01% p.a. The loans to Southern Water Services Limited, Bournemouth Water Limited and South East Water Limited carry a fixed rate of interest of 4.076% p.a., 3.083% p.a. and 2.801% p.a. respectively, adjusted for the UK RPI indexation on a semi-annual basis. However, the Company has entered into total return swaps in which the Company exchanges the indexation-linked interest it receives on the loans for the fixed coupon amount payable on the Bonds; hence no significant net interest rate risk exists. As such, no sensitivity analysis has been presented. The loans and bonds mature on 30 September 2033.

**Foreign exchange risk**

All transactions and financial instruments are denominated in sterling and consequently no currency exposure arises.

**Fair values of financial assets and financial liabilities**

The carrying amounts of all the Company's financial instruments equate to their fair values. Fair values have been determined using the methods described in Note 1.

| | Opening fair value £'000 | Cash Movement £'000 | Movement in fair value £'000 | Closing fair value £'000 |
|---|---|---|---|---|
| Cash and cash equivalents | 620 | (54) | - | 566 |
| Loans to customers – fixed rate | 83,949 | - | (7,270) | 76,679 |
| Loans to customers – RPI indexed | 740,449 | - | 35,174 | 775,623 |
| Fixed rate bonds | (504,523) | - | 43,597 | (460,926) |
| Total return swaps | (319,094) | - | (71,603) | (390,697) |
| | 1,401 | (54) | (102) | 1,245 |

The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

a) quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);

b) inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices) (Level 2); and

c) inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3).

There have been no transfers between Level 1 and 2 during the year.

## NOTES TO THE FINANCIAL STATEMENTS
## For the year ended 31 March 2022

### 11. FINANCIAL INSTRUMENTS (CONTINUED)

**Fair values of financial assets and financial liabilities (continued)**

**As at 31 March 2022**

| | Total £'000 | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 |
|---|---|---|---|---|
| Financial assets | | | | |
| Loans to customers – fixed rate | 76,679 | - | 76,679 | - |
| Loans to customers – RPI indexed | 775,623 | - | 775,623 | - |
| | 852,302 | - | 852,302 | - |
| Financial liabilities | | | | |
| Fixed rate bonds | 460,926 | - | 460,926 | - |
| Total return swaps | 390,697 | - | 390,697 | - |
| | 851,623 | - | 851,623 | - |

**As at 31 March 2021**

| | Total £'000 | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 |
|---|---|---|---|---|
| Financial assets | | | | |
| Loans to customers – fixed rate | 83,949 | - | 83,949 | - |
| Loans to customers – RPI indexed | 740,449 | - | 740,449 | - |
| Total return swaps | 1,371 | - | 1,371 | - |
| | 825,769 | - | 825,769 | - |
| Financial liabilities | | | | |
| Fixed rate bonds | 504,523 | - | 504,523 | - |
| Total return swaps | 320,465 | - | 320,465 | - |
| | 824,988 | - | 824,988 | - |

### 12. RELATED PARTY TRANSACTIONS

Apex Trust Corporate Limited is the corporate service provider for the Company. During the year, fees incurred for these services were £10,496 (2021: £22,593) and an amount of £nil (2021: £nil) was payable at year end. The Company enters into transactions with the service provider, they include the payment of taxes including UK corporation tax and Value Added Tax.

### 13. ULTIMATE PARENT AND CONTROLLING PARTY

The management determined that the Company has no ultimate controlling party. As described in Note 10, the shares of the Company are held by Apex Trust Nominees No. 1 Limited and Apex Corporate Trustees (UK) Limited as trustees under the terms of a trust declared ultimately for charitable purposes.

### 14. SUBSEQUENT EVENTS

There have been no subsequent events post the Statement of Financial Position date.