

EXPLAINING OUR TAX CONTRIBUTION 2022/23

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SEVERN
TRENT

FOREWORD

At Severn Trent, we know that when we are united by our clear social Purpose, we can drive positive change and deliver better outcomes for all our stakeholders – our customers, our colleagues, our investors, the society we live in and the environment we depend on. Our approach to tax is no exception, we are committed to managing our tax affairs in a responsible manner, paying the right amount of tax at the right time in compliance with UK tax rules and acting in accordance with the values set out in our corporate responsibility framework.

As an infrastructure business we continue to make a significant investment in our networks and this year being no exception with £726.8m invested. Paying tax is also one of the important ways that we contribute to society. The contributions we make help fund vital public services and investment in people and public infrastructure. We believe that building trust with our customers, colleagues and other stakeholders on issues such as tax is important. This is why we are committed to paying our fair share of tax and helping our stakeholders understand our tax position and the contributions we make through our transparent reporting.

Over the past year, we are delighted to have retained our Fair Tax Mark for the fourth year running. This much sought-after recognition demonstrates we're a company that's committed to managing our tax affairs responsibly and supporting measures aimed at enhancing tax transparency. This approach has also been recognised by the Chartered Governance Institute in the year, with Severn Trent winning the prestigious 'Annual Report of the Year – FTSE 100' award.

Over the past year, we have continued to pay our fair share of tax and are pleased to have contributed over £132m in taxes to public finances.

We hope you enjoy reading our report.

Helen Miles
Chief Financial Officer



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OUR APPROACH TO TAX IS DRIVEN BY THE INTERESTS OF OUR STAKEHOLDERS



Customers

The effective management of our tax affairs is in the best interests of our customers as it helps to keep our bills as low as possible. This is particularly true for our regulated business where the taxes we pay are included in the calculation of customers' bills.



Colleagues

Our colleagues tell us they want to work for a socially responsible business that pays the right amount of tax at the right time, complies with all relevant tax laws and is open and transparent about its tax affairs.



Shareholders

As a listed business, responsible and efficient management of our tax affairs helps us deliver attractive, sustainable post-tax returns in the form of dividends.



Government Agencies

We maintain an open and transparent relationship with Government Agencies including Ofwat, HMRC and the Valuation Office Agency (VOA) and ensure they are kept up to date with business developments.



Communities

The communities we serve have an interest in how we manage our taxes and want us to act in a socially responsible way.

We make a significant financial contribution to the communities we serve through the business rates we pay direct to local authorities as well as broader taxes.

Our Approach to Tax

- We will manage our tax affairs responsibly, recognising the interests of all our stakeholders;
- We will not undertake aggressive tax planning or any planning that is not aligned with the economic and commercial activities of our business;
 - We will make use of incentives made available by Government to encourage investment; and
- We will maintain an open, transparent and collaborative relationship with HMRC consistent with maintaining our good working relationship.

A copy of our tax strategy is available at <https://www.severntrent.com/content/dam/stw-plc/responsibility/tax-strategy.pdf>. Our tax strategy is reviewed annually and approved by the board. Compliance with our strategy is tested regularly by our internal audit function.

TAX RISK MANAGEMENT FRAMEWORK

“... [Our] success depends on our commitment to exceptional corporate governance standards, which underpin the confident delivery of everything we do. It drives ethical behaviours, informs sound decision making, enables the effective running of our business and, ultimately, builds trust. The Board is fully committed to open and transparent reporting.” (Governance Report FY23 – Chair’s introduction).

Our Tax Strategy outlines our approach to tax risk management. Through good tax governance we manage tax risks by ensuring roles and responsibilities for tax are clearly defined and understood. We have operational procedures and controls in place and ensure day to day management of the risks identified. When addressing tax risk, we consider the impact on our business and our stakeholders.

As part of our overall risk management framework, all tax risks are reviewed annually for both the possibility of occurrence and the potential impact on our objectives. We have a robust tax risk framework through which we identify key risks and implement controls to minimise the occurrence and impact of these risks.

What are our key tax risks and how are they managed?

Key Tax Risk	How our key risks are managed
Tax legislation	One key tax risk is the introduction of unanticipated tax practice or legislative changes. We actively engage with relevant tax authorities to mitigate these risks and work with the water industry, through Water UK, to assess and communicate the impact of any such changes on our business.
Financial reporting	We implement strong tax compliance procedures and controls which ensure the presentation of our tax position in our financial reports is accurate, complete and transparent. Our annual report and accounts are also subject to an independent third party audit to give added assurance to the reader on the robustness of the disclosures.
Tax compliance	Our wider risk management framework and governance process gives us confidence that the tax returns we file are correct and complete and can be traced through the accounting system to the underlying source data, giving assurance to our commitment to pay the right amount of tax at the right time.

Helen Miles (our CFO) is ultimately responsible for tax governance within Severn Trent as our Senior Accounting Officer and certifies on an annual basis that we have taken reasonable steps to ensure we have appropriate tax accounting arrangements in place to ensure our tax liabilities are calculated accurately.

Helen is supported by an experienced team of tax and finance professionals with water industry expertise. The team works hand in hand with the business to mitigate tax risk and engages with external tax advisers on more complex areas of tax or where there is tax uncertainty.

TAX TRANSPARENCY

We support measures aimed at enhancing tax transparency and are committed to providing regular information on our tax affairs in a clear and straightforward way for our stakeholders. This provides them with confidence that we are paying our fair share of tax.

To this end, we provide transparent disclosure of our tax affairs, the amounts and types of taxes we pay and where we pay tax.

This year, we retained the Fair Tax Mark. It recognises that we're a company that does the right thing – paying the right amount of tax, in the right place, at the right time. Most importantly, this accreditation shows our customers that we are a responsible business taking a great deal of pride in being open and transparent in how we do things.



Fair Tax



WHAT TAXES DO WE PAY?



* Due to changes in government policy allowing accelerated tax relief for investment (explained on the next page).

CORPORATION TAX

We pay corporation tax on our profits, almost all of which are generated in the UK, so they're subject to UK corporation tax at the current rate of 19%.

Corporation Tax changes announced by the UK Government and the impact on Severn Trent's corporation tax profile.

In March 2021, the UK Government announced the introduction of a new capital allowance 'super deduction' tax relief, available from 1 April 2021 to 31 March 2023. It is our approach to make use of available incentives, such as the super deduction, offered by the Government to encourage investment where they align with our business objectives and help us invest in our operations and people (as outlined in our Tax Strategy).

As an infrastructure business, we invested £726.8m in our networks during the year and part of this investment will qualify for the super deduction. The changes announced to the capital allowance regime have reduced our current tax payable in the year to nil. The benefit we receive from this change is that the expenditure we have incurred is deducted from our taxable profits earlier than it otherwise would have been. We account for this timing difference through deferred tax.

Also announced in the UK 2021 Spring Budget was an increase in the main rate of corporation tax from 19% to 25% from 1 April 2023. We expect the impact of the increase in the corporation tax rate to result in higher corporation tax payments in future years which is also reflected in our deferred tax charge.

The chart overleaf shows why the tax we paid in the year was lower than the charge in our accounts.



One example of a project expected to qualify for the super deduction is the roll out of a large scale trial of smart water meters in our region to help customers save water and save money on their water bills as part of our Green Recovery programme.

WHY OUR TAX PAID WAS LOWER THAN THE CHARGE IN OUR INCOME STATEMENT



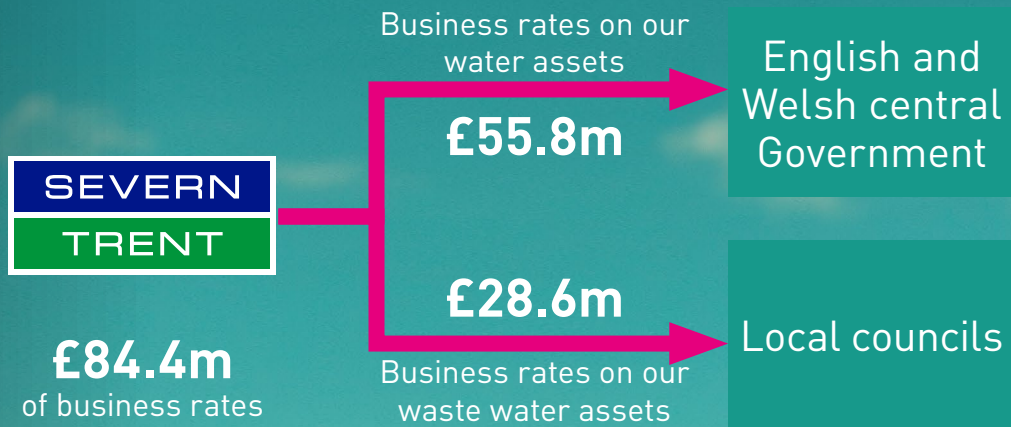
- 1 The corporation tax charge for this year in our financial statement was £35.7m.
- 2 The tax charge on our profits includes amounts that are payable to HMRC now (current tax) and amounts that may become payable in the future where tax relief is received earlier than items are charged to our income statement (deferred tax).
- 3 We estimate our tax charge when we prepare our accounts and may make adjustments to arrive at the amount of tax we owe in our corporation tax returns.
- 4 No cash tax liability is estimated for 2022/23.
- 5 Our net tax payments of £4.0 million related to previous years (2021/22: £1.2m).

BUSINESS RATES

Just like any other company, we pay business rates on all non-domestic property and infrastructure unless subject to a relief.

Business rates on our water assets, such as our pipelines and service reservoirs, are paid directly to central government. The Valuation Office Agency (VOA) carries out periodic revaluations to reflect changes in the assets assessed. We work with the VOA ahead of each revaluation to ensure that the amount paid for these assets is fairly assessed.

We pay business rates on our waste water assets, such as sewage treatment works, directly to the local council where the assets are located, which means the tax goes directly to the communities we serve. We regularly review the individual valuations for each of our sites to ensure that the correct business rates are being paid for these sites.



NATIONAL INSURANCE CONTRIBUTIONS

We manage two types of National Insurance Contributions (NICs):

- **Employer NICs** are a cost to us of employing our colleagues and are based on their salaries.
- **Employee NICs** are costs incurred by our colleagues that we collect and pay to the UK Government on our colleagues' behalf.

How does the UK Government use our National Insurance Contributions?*



In 2022/23 we employed on average **7,651** colleagues and paid **£35.3m** in Employer NICs, while also collecting **£23.6m** in Employee NICs.

*source: <https://www.gov.uk/national-insurance/what-national-insurance-is-for>

ENVIRONMENTAL TAXES

The process of providing clean water and cleaning waste water consumes a lot of energy. The consumption of energy is an area that the Government chooses to tax to encourage environmentally positive behaviours.

The energy we use in our business is either generated from our waste and renewables businesses or purchased from renewable sources. Across the Severn Trent group, we currently generate renewable energy equivalent to 53% of our total electricity use and purchase the remainder from third parties, incurring £6.6m of Climate Change Levy this year.

Reducing our energy use and self-generating renewable, green energy tackles the main sources of our emissions and brings financial benefits for both ourselves and our customers. We have signed up to the triple pledge of:

- **Net zero** carbon emissions by 2030.
- **100%** renewable energy use by 2030.
- **100%** electric vehicles by 2030 (where suitable models are available).

We are tackling this through innovative means such as energy generation from sewage, food waste and energy crops in addition to sources such as solar, wind and hydroelectricity. We are determined to play a leading role in addressing the impact of climate change and mitigating our own impact, the impact of our supply chain and adapting to the challenges that climate change may bring in the future.

We are on track with our Triple Carbon Pledge, and now only use fully renewable-backed electricity from our energy suppliers. Our electric vehicle fleet continues to increase in size. Our Severn Trent Green Power business recycles over 500,000 tonnes of green and mixed food waste each year. The green energy produced from food waste helps to meet our net zero targets and keep our energy costs down.





PRODUCTION TAXES

Production taxes include taxes on our transport activities and insurance policies.

We operate around the clock to ensure that our customers receive the high standard of service they expect from us. Transport is an essential part of delivering this service.

We have a fleet comprising a wide range of vehicles from large water and sludge tankers to the small vans we use for the routine sampling of customer taps.

We incur production taxes, such as fuel duty (£3.1m) and road fund licences (£0.7m), on our transportation activities.

As a business we are always looking for ways to reduce our production taxes. We have already switched some of our fleet to electric vehicles and have pledged to switch our entire fleet to electric vehicles by 2030 where suitable models are available. This year, we continued to add brand-new 100% electric vehicles ('EVs') to our Severn Trent Services fleet. Based at one of our water treatment works that has the ability to produce 30MW renewable energy using solar energy, the Nissan ENV200s will be used by our technicians to deliver operations and maintenance on our water and waste water assets across our MOD contract.

As well as reducing overall mileage we are increasing the fuel efficiency of our transport. We carry out vehicle tracking and driver training in order to encourage our staff to drive in a safer and more efficient way.

Like any other business, our business faces many risks. We choose to protect ourselves by transferring some of these risks to insurance companies. Last year, we paid £1m of Insurance Premium Tax on insurance policies.

COUNTRY BY COUNTRY DATA

We seek to declare profits in the country where the economic substance arises and therefore substantially all of our profits are generated in the UK and are subject to UK corporation tax.

Details of our global activities are provided below:

Country of operation	Tax jurisdiction	Total revenue £m	Profit/loss before tax £m	Income Tax accrued £m	Number of employees	Employee costs* £m	Footnote
UK	UK	2,197.4	915.7	0.2	7,651	382.3	1
Guernsey	Guernsey	1.1	1.1	0	0	0	2
Hong Kong	UK	0	300.0	0	0	0	3
Consolidation adjustments	-	(33.4)	(1048.9)	0	0	0	4
Group	-	2,165.1	167.9	0.2	7,651	382.3	-

* Employee costs includes all costs of paying wages, salaries, social security, pension and share based payments

1. Severn Trent is one of the UK's largest water companies. We operate through regulated and non-regulated businesses. Our regulated businesses provide water and sewage services to more than 4.8 million households and businesses in the Midlands and Wales. Our non-regulated businesses design, build and operate water assets, as well as providing renewable energy generation, property development, developer services and property searches.
2. Lyra Insurance Guernsey Limited is a wholly owned subsidiary company incorporated in Guernsey. It was established to provide insurance services to the Group. The company is subject to the UK Controlled Foreign Company (CFC) rules and therefore the Group incurs tax at the UK Corporation Tax rate on its profits.
3. Athena Holdings Limited is a wholly owned subsidiary company incorporated in Hong Kong. The principal activity of the company is to act as an investment holding company. The profit arose from intra-group dividends that were passed through to Severn Trent Plc. There was no tax impact of these transactions either in the UK or Hong Kong.
4. All of the Severn Trent group revenue is generated in the UK. Corporation tax is levied on an individual entity's taxable profits, but is reported in the Severn Trent Plc group accounts on a consolidated basis. Accordingly, the UK revenue and profit before tax amounts have been aggregated and the consolidation adjustments row operates to strip out intercompany transactions and other adjustments in line with IFRS accounting standards.

KEY TERMS

Business rates	Taxes charged on our properties and infrastructure.
Corporation tax	The tax we pay on the profits we earn.
Employer National Insurance Contributions (NICs)	Taxes charged on employing our colleagues.
Environmental taxes	Taxes designed to promote environmentally positive behavior and includes taxes on the energy we use, such as Climate change Levy.
Production taxes	Taxes charged on our transportation activities, such as fuel duty and vehicle excise duty, and insurance policies, such as Insurance Premium Tax.
Taxes incurred	Includes all taxes that represent a cost to us of running our business.

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