NORTHUMBRIAN WATER LIMITED ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2019

NORTHUMBRIAN WATER *living water*

ESSEX&SUFFOLK WATER *living water*

Registered company no: 02366703

ANNUAL REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2019

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CHAIRMAN'S STATEMENT

A J Hunter

The Board of Northumbrian Water Limited (NWL or the Company) never loses sight of the fact that, for most of our customers, we are the only available supplier of water.

We realise that this brings with it very significant responsibilities and high expectations on the part of everyone we serve and interact with. As a result, each year the Board challenges itself and the Company's employees to deliver even better performance so that our customers' rising expectations can continue to be met. Our Company's vision however remains the same - to be the national leader in the provision of sustainable water and wastewater services.

This year we have also articulated the Company's purpose, as detailed in our Strategic Report (on pages 12 and 13), which recognises the Company's operational and financial remit alongside its broader role in society. It is one of the duties of the Board to balance the interests of all our stakeholders fairly, whilst meeting our fiduciary duties as directors. As Chairman, I believe the Board strikes the required balance very well, assisted by the strong governance arrangements we have in place, which are set out in detail in our Corporate Governance report.

Turning to our progress over the last year, our performance is underpinned by our five strategic themes: Customer, Environment, Competitiveness, People and Communities. At each meeting the Board has reviewed performance against a balanced scorecard of measures related to these strategic themes in addition to health and safety, financial performance and other key factors. For a more detailed overview of our work and progress on these themes, please refer to our Strategic Report.

Our Chief Executive Officer (CEO), Heidi Mottram, confirms in her Review that we have delivered strong performance against existing commitments, but also laid solid foundations for the coming years in our 2020-25 Business Plan. Heidi draws out the key features, but I would highlight that our new customer contact and billing system has been a success, which will streamline our services as we move further towards a fully-digital customer experience. I am also very proud of our work to support our most vulnerable customers.

Overall operational performance has been very good; our water supplies have remained resilient, notwithstanding very challenging weather conditions, and our significant efforts to reduce leakage have helped deliver our leakage targets. We had no discharge compliance failures at sewage treatment works and we reduced pollution incidents from our assets.

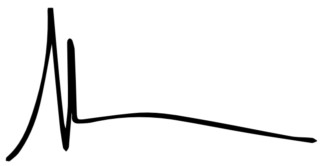
On 31 August 2018 we submitted our Business Plan for 2020-25. As Heidi notes in her Review, this was a hugely collaborative and consultative exercise, conducted in partnership with our customers and other key stakeholders and we were both pleased with the very positive response our Business Plan received, including 91% customer support. The Board recognised the enormous effort from all employees that has enabled the Company to offer significant bill reductions to our customers alongside real improvements in service. It was clear from our detailed and extensive work with customers that they share our firm belief that protecting the environment and ensuring the resilience of our services should remain two of our key priorities. We are confident that our Business Plan will enable us to deliver on those fronts in a cost effective manner, as we have evidenced to Ofwat, and as supported by detailed analysis that confirms the investment we are proposing is in our customers' best interests for the long term. We have now re-submitted our Business Plan and are confident it will deliver excellent service to our customers, notwithstanding the very high bar we have set for ourselves that now needs to be achieved.

Like any other business, NWL also requires substantial investment to remain resilient and reliable and it's reasonable for shareholders and lenders to expect a fair return on the very significant investment they have made in the Company. Whilst I am pleased to confirm that the Company has retained its strong investment grade credit ratings and remains within its financial Key Performance Indicator (KPI) targets, as reported in the balanced scorecard on **pages 19 and 20**, there are real challenges ahead as we await Ofwat's Draft Determination of the 2019 Price Review (PR19) this summer.

As always, the Board will continue to drive the performance of the Company forward to ensure we deliver even better services to our customers, both in 2019–20 and beyond.

I would again like to sincerely thank all our employees for their dedication and commitment this year. Our people are our "front-line" and our performance depends entirely on their engagement and hard work.

I hope you find our Annual Report and Financial Statements interesting and helpful.



A J Hunter
Chairman

CHIEF EXECUTIVE OFFICER'S REVIEW

Our vision is to be the national leader in the provision of sustainable water and wastewater services, and I am delighted that we have made further progress towards this vision during 2018/19, and remain one of the leaders in our industry.

H Mottram

This has been a very important year not just delivering continued strong performance against our current commitments but laying the foundations for the next five years in our 2020-25 Business Plan. My review highlights some of the achievements we are most proud of this year as well as summarising the key features of our future plans.

OUR PERFORMANCE

Customers

It was a very important year in our customer team as we implemented our new customer contact and billing system. This was a significant undertaking and I would like to personally thank the project and business teams for their tremendous efforts. I believe that our new system gives us a great platform to transform our engagement with customers, which we will further enhance when we introduce our new digital platforms later this year. This will be especially important as the sector moves to a new holistic measure of customer experience.

We know from our research that customer expectations of the services we provide are rising all of the time and that we need to continuously improve to match or exceed their expectations. However, it is also important that we are able to support customers who are in more vulnerable circumstances and our 'Water Without the Worry' campaign brings together all of our inclusivity work from social tariffs to our priority services register. I am particularly proud of the commitment we launched in May last year to eradicate water poverty across the areas we service by 2030, in partnership with the charity, National Energy Action.

Water

This has been a very challenging year for our water business with the after effects of the 'Beast from the East' being followed by an extended period of hot, dry weather. However, we have been able to demonstrate the resilience of our services and continued to deliver high quality water to our customers. I was particularly pleased that we were able to deliver our leakage commitments thanks to a number of innovative approaches we've introduced over the past year, from satellite technology in the sky to our four-legged friend, springer spaniel Denzel, sniffing out leaks on the ground.

Our innovations stretch beyond leakage and we are proud of our innovative culture. This was embodied by our second Innovation Festival last year and, working with our partners, we are now starting to see some of these ideas develop into reality. For example, we've worked with Ordnance Survey, local authorities and other utility services to produce an underground map of all utility pipes and cables in Sunderland. This innovation will help our people to work more safely and will save us and other utilities tens of millions of pounds each year. I was delighted to host a visit from the Minister for Implementation to demonstrate the underground mapping project and we are looking forward to working with government and others to expand the work nationally and showcase the powers of data sharing for public good.

Wastewater

In our wastewater business we were delighted to achieve our target of zero discharge compliance failures at our sewage treatment works, building on our very strong record over several years. This has been achieved through our innovative operational management and early warning systems which allow us to understand and manage risks across our works in real time.

A similar focused approach has transformed our performance in reducing pollution incidents from our assets. In recent years, our performance in this area was not as strong as we wanted it to be, so we created a special project team to develop ideas as part of a zero tolerance approach to pollution. Through use of data analytics to target proactive maintenance and rapid response to minimise the impact of events, we have achieved some impressive results.

Staying on the theme of our environment, we have continued our commitment to renewable energy. Not only do we continue to make ‘power from poo’ through using 100% of our sewage sludge to generate energy, a large portion of our power requirements are now met through long-term ‘renewable only’ agreements, specifically from offshore wind farms. This has allowed us to commit to becoming a carbon neutral company within the next decade. We are the only company in the sector to have been awarded four stars by the Environment Agency in its Environmental Performance assessment.

Our People and the Communities we serve

The common theme running through all of these achievements is that they are the result of the hard work that our people put in every single day. Through our Great Place To Work strategy we aspire for all of our people to have a great experience at work, to understand the part they play to achieve our vision and to deliver an unrivalled customer experience. We were delighted that our efforts to achieve this were recognised recently as one of the Sunday Times 25 Best Big Companies to Work For in the UK.

Another commitment we made during the year was joining over 90 signatories to the Waste to Wealth Commitment. By signing this Commitment, we recognise the Intergovernmental Panel on Climate Change challenge that we only have 12 years to change our relationship with the resources we use, if we are to avoid catastrophic climate change and restore the health of our environment. We have taken this forward into the ambitious goals we have set for the future such as eliminating avoidable waste by 2025 and having the lowest levels of leakage in the country in our water-stressed Essex & Suffolk Water (ESW) region. This has also contributed to us being recognised as one of the ‘most ethical companies’ in the world by the Ethisphere Institute, the only water company in the world to be included.

LOOKING FORWARD

We are incredibly proud of the Business Plan we submitted for 2020-25, which was shaped by over 400,000 of our customers. Our Business Plan clearly sets out our ambition to deliver world class service to our customers as well as significant improvements for the environment, and the initiatives we will deliver to achieve this. At the same time, our Business Plan delivers a substantial reduction in bills for all of our customers of 14% to 17% across water and wastewater.

We were delighted that 91% of our customers accepted our Business Plan and, while we were surprised that Ofwat did not accept our original plan and requested that we resubmit it, based on detailed evidence we still believe our Business Plan will deliver unrivalled service at an affordable cost for our customers.

We focused our Business Plan around six themes and fourteen ambitious goals that will have a fundamental impact on the way our customers experience their water and wastewater services in future. Underpinning these goals are a series of stretching Performance Commitments (PCs) that will continue to push the performance and efficiency frontier. The highlights of our Business Plan are shown overleaf.

We are proud of our achievements to date, but we are never complacent and will continue to make further service improvements in 2019/20 and beyond into 2020-25. I hope you find our Annual Report and Financial Statements helpful and informative.

H Mottram CBE
CEO

UNRIVALLED CUSTOMER EXPERIENCE

Our customers' expectations are rising, and what customers want from us is changing too. We will deliver a package of measures to support our aim to deliver an unrivalled customer experience.

Our ambitious goals in this area are to:

- Deliver world class customer service; and
- Give every single customer the opportunity to have a strong voice and engage with us, with at least 2m customers participating by 2025.

AFFORDABLE AND INCLUSIVE SERVICES

Water and sewerage services should be affordable for all of our customers, whatever their circumstances, and they should all have equal access to an unrivalled customer experience.

Our ambitious goal in this area is to:

- Eradicate water poverty in our operating areas by 2030.

RELIABLE AND RESILIENT SERVICES

We will continue to deliver reliable and resilient services by anticipating change, planning ahead, and by making the right long-term decision about how to run our business.

Our ambitious goals in this area are to:

- Have the lowest levels of leakage in the country in our water-stressed ESW operating area;
- Have a per capita consumption (PCC) for water use of 118 litres per person per day by 2040;
- Promote confidence in our drinking water so that nine out of ten of our customers choose tap water over bottled water; and
- Eradicate sewer flooding in the home as a result of our assets and operations.

LEADING IN INNOVATION

Super-charging our innovation culture is essential if we are to continue to deliver unrivalled experiences within the context of rising customer expectations, technological advances and changing political and physical climates.

Our ambitious goal in this area is to:

- Be leading in innovation within the water sector and beyond.

IMPROVING THE ENVIRONMENT

We will create a step change in our environmental activities, building on our role as stewards of the environment to demonstrate leadership, and to protect and improve the environment within our regions.

Our ambitious goals for this area are to:

- Be leading in the sustainable use of natural resources, through achieving zero avoidable waste by 2025 and being carbon neutral by 2027;
- Demonstrate leadership in catchment management to enhance natural capital and deliver net gain for biodiversity;
- Have the best rivers and beaches in the country; and
- Have zero pollutions as a result of our assets and operations.

BUILDING SUCCESSFUL ECONOMIES IN OUR REGIONS

As a responsible business with a strong track record, it is important to us that we demonstrate leadership and make a wider contribution to life within our regions.

Our ambitious goals within this area are to:

- Spend at least 60p in every £1 with suppliers in our regions; and
- Be the most socially responsible water company.

This **Annual Report and Financial Statements** is just one of a suite of documents we have published to provide our stakeholders with easily accessible information on our performance and governance. We have also published:

Annual Performance Report: setting out how we have performed against the commitments we made in our Business Plan for 2015-20 and how we are continually striving to improve the services we deliver to our customers and our business Outcomes. There is also an accessible summary version.

Our Contribution Report: presenting the social, environmental and economic impact we have on the communities we serve.

Data Assurance Summary: explaining how we ensure that the information we report is accurate, clear and transparent and deliver against the commitments in Our Assurance Plan.

All of these documents are available on our websites at **www.nwl.co.uk** and **www.eswater.co.uk**.

BUSINESS OVERVIEW

Our vision is to be the national leader in sustainable water and wastewater services.

We provide water and wastewater services to our customers in the north east of England, trading as Northumbrian Water (NW), and water services only to our customers in the south east of England, trading as Essex & Suffolk Water (ESW).

We employ over 3,000 people

2.7 MILLION

NW supplies water and wastewater services to 2.7 million people in the major population centres of Tyneside, Wearside and Teesside as well as the large rural areas of Northumberland and County Durham. We provide wastewater services only in Hartlepool.

1.6 MILLION IN ESSEX

0.3 MILLION IN SUFFOLK

ESW supplies water services to **1.6 million** people in Essex and **0.3 million** in Suffolk. Our Essex area is part rural and part urban and includes the main population centres of Chelmsford, Southend and the London Boroughs of Barking and Dagenham and Havering and Redbridge. Our Suffolk area is mainly rural with the largest towns being Great Yarmouth and Lowestoft.

We operate and maintain:

- 52 water treatment works;
- 330 water pumping stations;
- 324 water service reservoirs;
- 26,032km of water mains;
- 411 sewage treatment works;
- 957 sewage pumping stations; and
- 30,069km of sewers.

Every day we supply 1.1 billion litres of water

NWL is part of the Northumbrian Water Group (NWG or the Group). The ultimate parent undertaking of NWL is CK Hutchison Holdings Limited (CKHH), a company listed on The Stock Exchange of Hong Kong Limited. Further information about the structure and ownership of NWG is provided on page 50 of this report.

OUR HIGHLIGHTS

ERADICATING WATER POVERTY

Launched commitment to eradicate water poverty across our supply areas

WATER COMPANY OF THE YEAR 2018

Prestigious Utility Week award

BUSINESS PLAN SHAPED BY 400,000 CUSTOMERS

Ambitious Business Plan for 2020-25 accepted by 91% of customers

4* ENVIRONMENTAL PERFORMANCE ASSESSMENT

Environment Agency measure of water and wastewater company performance

100% SEWAGE TREATMENT WORKS COMPLIANCE

All works meeting strict Environment Agency standards

SECOND INNOVATION FESTIVAL

Industry leading approach to Innovation (a third Festival was held in July 2019)

100% OF SEWAGE SLUDGE CONVERTED TO RENEWABLE ENERGY

Benefitting customers and the environment

GREENHOUSE GAS EMISSIONS HALVED OVER LAST 10 YEARS

Long-term Carbon Management Plan delivered ahead of target

ROSPA 'HIGHLY COMMENDED IN WATER INDUSTRY' AWARD

Recognising Health and Safety performance and culture

TOP 25 SUNDAY TIMES BEST BIG COMPANIES TO WORK FOR

High levels of employee engagement and satisfaction

ONE OF WORLD'S MOST ETHICAL COMPANIES

Only water and wastewater company in the world on Ethisphere list

ALIGNING OUR PURPOSE TO OUR VISION AND VALUES

While we have always led with purpose and clearly communicated our vision and values to our people and our stakeholders, we want to explicitly define our true purpose; our reason for doing what we do.

Sustainability is at the core of our purpose. This means seeking to protect and enhance the environment in everything we do; being the best we can in meeting our customers' needs and having a positive impact on the communities where we operate; and making a financial return so we are economically viable long into the future.

OUR PURPOSE

Water is life. Every living cell on earth needs water to survive. The single most essential ingredient for human life to thrive, is clean drinking water. Our work is instrumental in fulfilling our basic human needs and protecting the source of life.

WE ARE CUSTODIANS OF WATER

Delivering reliable and resilient services that are vital to public health.

We are the current caretakers of the water in our regions, and we take this important responsibility very seriously. Day to day our practical purpose is to supply safe clean water, and effectively remove and treat wastewater so that our communities benefit from excellent public health. At a macro level our purpose is so much more; safeguarding the water supply for future generations requires innovative solutions, anticipating and instigating change, planning ahead and making the right long-term decisions about how to run our business. While our ambition is strong, we set effective and sustainable targets, always considering the lasting impact we leave behind.

WE ARE STEWARDS OF THE ENVIRONMENT

Valuing the natural capital and ecosystems we depend on.

We hold ourselves to account on an ambitious set of indicators designed to protect and improve the environment within our regions, going well beyond our regulatory obligations. We know our operations can be resource intensive but that we can also make a significant contribution to reducing plastic pollution, producing renewable energy, reducing carbon emissions, preventing flooding and improving public access to recreation. It's not enough to offset or compensate for loss of natural resources, our operational activities should have a lasting positive impact on protecting and improving the natural environment too.

WE ARE COMMITTED TO DELIVERING WORLD-CLASS CUSTOMER SERVICE

Giving unrivalled customer experiences every time.

We strive to give our customers leading customer service in the water industry and beyond. Our customer service ethos is core to our brand, values and culture; our people have a drive and energy to truly put our customers at the heart of everything they do. We listen to our customers and are empowered to take action to help them. Our customers are supported to participate fully in our business and in designing the services they receive. Every customer voice is important. Our people are passionate about delivering world-class customer service; they know it is expected of them, and they are committed to it because they believe the services we provide are essential to life and wellbeing. We all want our customers to always have complete trust and confidence in what we do. We own a customer's problem, keep our promises and show each customer that they are special by focusing on individual needs. We know that every interaction with every customer matters.

WE ARE THE LIFEBLOOD THAT FLOWS THROUGH OUR COMMUNITIES

Demonstrating our value and making a wider contribution to society.

We are integral to our communities, always listening to our customers so that we understand what matters most to them and what their expectations are of us. We have a unique opportunity to be able to operate a business that delivers public value. Protecting the most vulnerable people in our society drives us to eliminate water poverty and increase the disposable incomes of those who need it most, reducing the worry they face. Working, living and volunteering amongst our customers helps us to understand and foster a positive impact on the wellbeing of the communities we serve.

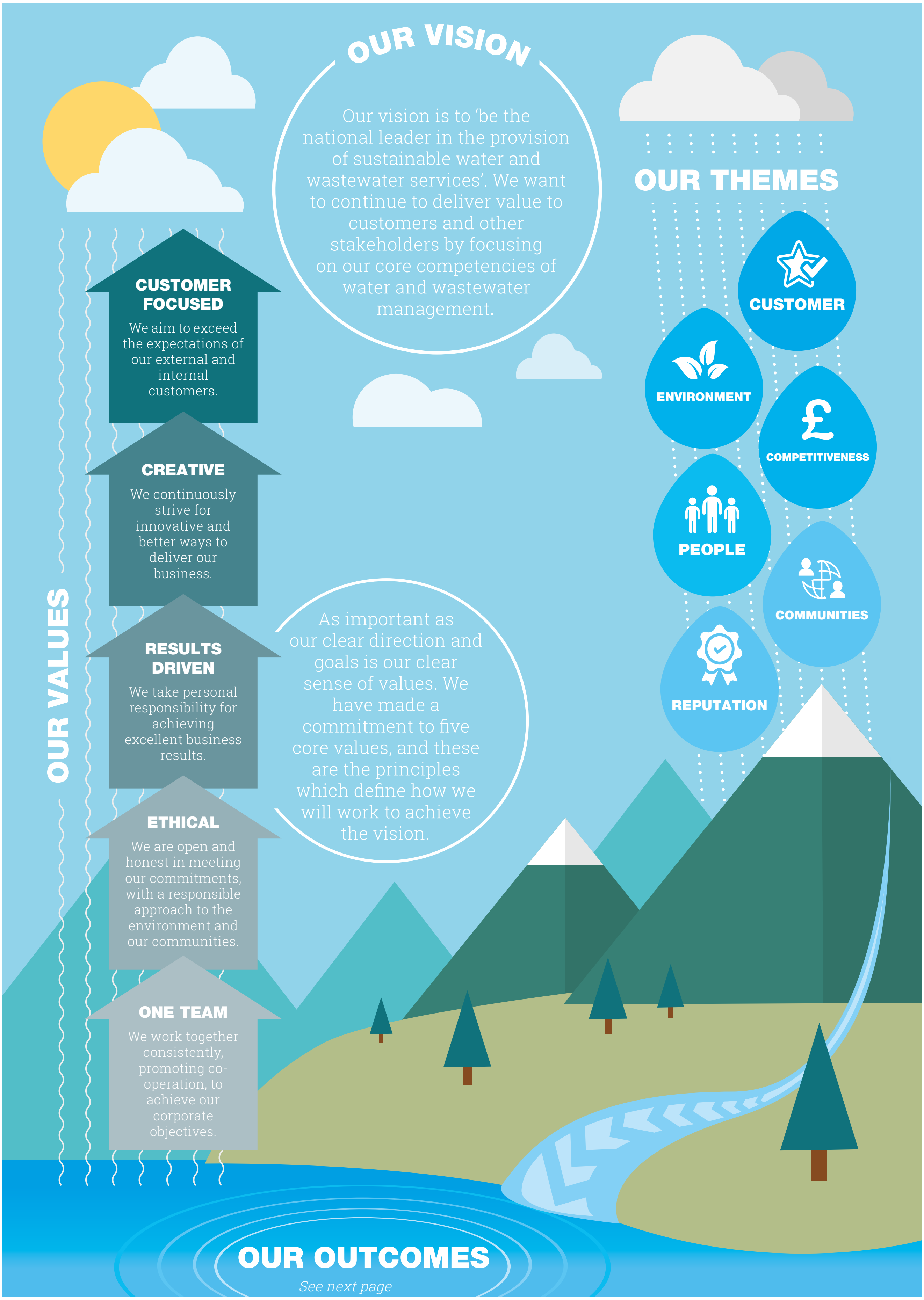
WE ENABLE EXTRAORDINARY LEADERS

Empowering people to know their purpose.

We work hard to give our people and the jobs they do a real sense of meaning. Working with a sense of purpose enables personal fulfilment. We foster a high performing culture and value diverse perspectives and skills. We support our leaders to develop high emotional intelligence, enabling our people to behave in the right and responsible way. Our aspiration is for all our people to have a great experience at work and understand the part their play to achieve our purpose and live our Company values. Our people have clear Outcomes and are held to account, enabling them to take personal responsibility as they contribute to our sustainability in a balanced way, always striving to be leading.

You can read more about how we live our purpose in the case studies that follow in our Annual Performance Report and in **Our Contribution report** for 2019, which looks at our influence and impact in the wider economy, the environment and society.

BUSINESS MODEL



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OUR OUTCOMES

THEME	OUTCOME
CUSTOMER	• We deliver water and sewerage services that meet the needs of current and future generations in a changing world. • We supply clean, clear drinking water that tastes good. • We provide a reliable and sufficient supply of water. • Our customers consider the services they receive to be value for money. • Our customers are well informed about the services they receive and the value of water. • We provide a sewerage service that deals effectively with sewage and heavy rainfall. • We provide excellent service and impress our customers.
ENVIRONMENT	• We help improve the quality of rivers and coastal waters for the benefit of people, the environment and wildlife. • We protect and enhance the environment in delivering our services, leading by example.
COMPETITIVENESS	• We are an efficient and innovative company. • Our finances are sound, stable and achieve a fair balance between customers and investors.
PEOPLE	• Our people are talented, committed and inspired to deliver great services to customers. • Our people act in line with our values. • We are seen as a great place to work. • Our workplaces are healthy and safe.
COMMUNITIES	• We are proud to contribute to the success of local communities. • We work in partnership towards common goals.
REPUTATION	• We are a company that customers trust.

OUR STAKEHOLDERS

We provide essential services to our customers and, as a licenced water and wastewater undertaker, we operate within a strict regulatory environment.

It is very important to us that we understand the needs of our many stakeholders to ensure that we continue to provide a great service and deliver our business Outcomes. We engage proactively with all of our stakeholders in our continuing efforts to provide an unrivalled customer experience.

CUSTOMER VOICE

Over recent years we have progressed from customer consultation to a culture of deep customer participation, with customers co-creating our strategy and approach to customer service, levels of PCs and how investments are made. Customer participation has been fundamental to the development of our Business Plan strategy, helping us to understand what matters most to customers about the services we provide, which areas of the business they would most like to influence and the best ways for us to engage with them.

As a result we published our **Customer Participation report**: 'From customer consultation to a culture of customer participation'. Co-creation has become second nature for us, with customers shaping how investments are made and experiences are delivered. It was therefore a given to build on this when we started thinking about our 2020-25 Business Plan engagement and we have carried out design sprints, co-creation workshops and focus groups across all areas of the price review, having completely open conversations with customers about all areas of service. In all, we engaged with over 400,000 of our customers to help shape our Business Plan with 91% of customers accepting our Business Plan.

Our Water Forums, one each for our NW and ESW customers, bring together a range of experts from various stakeholders to challenge the Company on behalf of our customers. They inform our approach to customer research and engagement on matters such as PCs and social tariffs research as well as challenging us to consider areas where performance and outcomes for customers could be improved.

On a national and regional basis, customers' interests are represented by the Consumer Council for Water (CCWater). We share and review customer literature with them before publication and engage on how we support vulnerable customers, as well as holding quarterly liaison meetings and attending regional public meetings.

GOVERNMENT AND REGULATORY CONTEXT

Ofwat regulates prices and levels of customer service. We engage on key issues such as market reform and future price controls as well as the need to demonstrate strong governance and the importance of maintaining the trust and confidence of our customers. This is achieved through our regular reporting, such as our **Annual Performance Report** (APR), responding to consultations, regular peer to peer contact and participating in the market place for ideas.

The Drinking Water Inspectorate (DWI) monitors drinking water quality and we engage at both an operational and strategic level to review performance and promote good practice, in addition to reviewing specific improvement schemes.

The Environment Agency (EA) covers environmental protection and we liaise on our environmental performance, discharge compliance and sewer flooding. In addition to regular performance reviews, we have worked collaboratively through catchment partnerships and providing strategic input to the 21st Century drainage programme.

OUR PEOPLE AND DELIVERY PARTNERS

We engage with our employees both through our Employee Relations Framework and via a range of communication channels, such as team briefings, director roadshows and regular internal communications. This covers a wide range of subjects from Health and Safety (H&S) and staff benefits to values and behaviours and diversity. Our approach is described in more detail in the Performance Review section, under the People heading on **pages 38 to 44**.

To meet the challenges of delivering our AMP6 (Asset Management Plan) capital investment programme as efficiently and effectively as possible, we implemented a new operating model with our supply chain, based around collaboration and co-operation. This involves joint framework governance groups, integrated programme delivery teams, joint recruitment campaigns and a joint framework for Health and Safety, co-created with our partners.

CIVIL SOCIETY

We work closely with many non-government organisations and charities to deliver our corporate social responsibility commitments and build strong relationships with the communities we serve.

Our activity in this area is explained in detail in **Our Contribution Report**, available on our websites, and is summarised on **pages 45 to 47** under the Communities heading of our Performance Review.

We work with the media to help communicate messages to our customers through news releases, case studies and social media messaging. This covers a wide range of subjects such as the local impacts of capital investment schemes, environmental and community investment and corporate campaigns, such as Every Drop Counts and our Refill campaign.

INVESTORS

We are conscious of our duty to act in the best interests of our shareholders and we seek to achieve a fair balance between them and our customers and other stakeholders, including debt investors.

PERFORMANCE REVIEW

In order to measure delivery of the Company Business Plan and goals, we use a balanced scorecard of KPIs covering the full range of our strategic themes.

The top section of the Performance table on pages 19 to 20 (with a blue header block) shows our performance against the Outcomes, Measures of Success (MoS) and PCs we agreed in the PR14 price review.

We are pleased that we have achieved the majority of our performance targets, against a background of challenging weather conditions over the period. However, we aim to achieve all of our PCs and we are always disappointed when our performance doesn't meet our targets, albeit narrowly in some cases. We show (●) where we have met our performance against our promise in the year, (●) where we have not met our performance but not incurred a penalty and (●) where we have not met our performance and incurred a penalty.

The bottom section (with a green header block) reports our performance against our internal targets under our Competitiveness, People and Communities Outcomes.

In respect of lost time reportable accidents, whilst our performance remains good and improved on last year, we have not achieved the extremely stretching targets we set ourselves. Health and safety remains a top priority for the Board and we describe the work we continue to carry out in this area on pages 43 to 44.

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ACTUAL PERFORMANCE AGAINST THE KPI TARGETS AND FUTURE TARGETS

SCORECARD MEASURE	UNITS	2017/18 PERFORMANCE	PC	2018/19 PERFORMANCE	ACHIEVED	2019/20 PC
Customer						
We provide excellent service and impress our customers						
Ofwat Service Incentive Mechanism (SIM)	score (out of 100)	86.4	>=90	85.9	●	>=90
Independent overall customer satisfaction survey	score (out of 10)	8.7	>=8.2	8.7	●	>=8.2
Domestic customer satisfaction, net promoter score	score	+44	>=32	+43	●	>=32
Independent survey on keeping customers informed	%	94	>=94	93	●	>=94
Our customers consider the services they receive to be value for money						
NWL independent value for money survey	score (out of 10)	8.2	>=7.9	8.2	●	>=7.9
CCWater value for money survey – Water NW	%	78	>=83	75	●	>=83
CCWater value for money survey – Sewerage NW	%	78	>=84	78	●	>=84
CCWater value for money survey – Water ESW	%	71	>=73	71	●	>=73
We supply clean, clear drinking water that tastes good						
Overall drinking water compliance	%	99.938	100	99.949	●	100
Discoloured water complaints	no. of complaints	2,532	<=2,908	2,594	●	<=2,908
Satisfaction with taste and odour of tap water	no. of complaints	978	<=987	1,060	●	<=987
We provide a reliable and sufficient supply of water						
Leakage – NW	Ml/day	137.1	<=137	136.3	●	<=137
Leakage – ESW	Ml/day	66.2	<=66	64.2	●	<=66
Interruptions to water supply for more than 3 hours	average minutes/ property	05:23	<=05:29	09:12	●	<=05:00
Properties experiencing poor water pressure	no. of properties	186	<=216	200	●	<=216
Water mains bursts	no. of burst mains	4,214	<=4,586	3,853	●	<=4,586

table continued…

SCORECARD MEASURE	UNITS	2017/18 PERFORMANCE	PC	2018/19 PERFORMANCE	ACHIEVED	2019/20 PC
We provide a sewerage service that deals effectively with sewage and heavy rainfall						
Properties flooded externally	no. of properties	944	<=1,318	902	●	<=1,318
Properties flooded internally	no. of properties	96	<=186	124	●	<=186
Repeat sewer flooding	no. of properties	38	<=496	60	●	<=496
Properties flooded externally – transferred network (TDS)	no. of properties	2,726	<=2,931	2,967	●	<=2,931
Properties flooded internally (TDS)	no. of properties	199	<=228	246	●	<=228
Sewer collapses	number	46	<=58	49	●	<=58
Sewer collapses (TDS)	number	51	<=84	59	●	<=84
Environment						
We help improve the quality of rivers and coastal waters for the benefit of people, the environment and wildlife						
Pollution incidents (category 3)	number	58	<=115	59	●	<=115
Bathing water quality compliance	no. sufficient	34	>=34	33	●	>=34
Sewage treatment works discharge compliance	no. failing works	2	0	0	●	0
We protect and enhance the environment						
Greenhouse gas emissions	ktCO2e	164	<=161	148	●	<=150

SCORECARD MEASURE	UNITS	2017/18 PERFORMANCE	TARGET	2018/19 PERFORMANCE	ACHIEVED	2019/20 TARGET
Competitiveness						
Gearing: net debt to Regulatory Capital Value (RCV)	%	66.4	<=77.5	67.2	●	<=77.5
Interest cover	times	3.5	>=2.4	3.6	●	>=2.4
People						
Employee engagement – internal survey	%	80	n/a	n/a	n/a	>=79
Employee engagement – external survey	score	n/a	2*	One to Watch	●	n/a
Lost time reportable accidents	number	9	<=3	7	●	<=3
Communities						
Ethisphere	y/n	not awarded	award	awarded	●	award

CUSTOMER

SERVICE INCENTIVE MECHANISM

Ofwat's SIM measures our customers' experiences of dealing with us and provides a good indication of how well we are serving those customers who have had a reason to contact us.

This was an exceptional year as we implemented our new customer care and billing system, which has given us a great platform to improve our customer experience as part of our transformational change programme, described in more detail below. However, introducing a new end-to-end billing system brought lots of change for our customers and our people and took some time to settle down. Though we reached a period of 'stabilisation' fairly quickly, we did have higher contact levels for a time which contributed to a slight reduction in our SIM score from 86.4 to 85.9.

> "Our customers are well informed about the services they receive and the value of water"

We are confident the investment we've made in improving our customer care and billing system will really help us deliver on our ambition to provide world class customer experiences as we move forward into our 'optimisation' phase and all positive changes are properly embedded and understood. We were delighted to win a prestigious industry award for our system implementation at the Utility Week Awards in December 2018.

For the next reporting period, Ofwat is introducing C-MeX (customer measure of experience) to replace SIM. In addition to assessing service received, this will also incorporate a broader view of customers' wider experience and perception of our Company. We welcome this change as it gives us opportunity to understand a more holistic reflection of customers' experiences with their water and wastewater providers.

UNRIVALLED CUSTOMER EXPERIENCE

Our clear ambition is to provide an unrivalled customer experience to each and every customer, whatever their circumstances or needs, and however they choose to contact us. Understanding our customers' preferences and changing needs is key to our success in providing an unrivalled customer experience to each and every one of our customers, whenever they engage with us. Across 2018-19, we have seen from both our own research and also research from the Institute of Customer Service, that customers are more discerning in their choices, that they appreciate and anticipate being able to communicate on their terms, through channels they choose, and at times they choose to engage with businesses.

Our new two-way texting platform enables us to communicate quickly with customers, in ways that they have told us they are happy to hear from us. Two way texting allows us to communicate in real-time with our customers, sharing information updates and receiving feedback quickly. For example, sending text messages to acknowledge reports of leaks and expected repair dates, to confirm water supplies have been fully restored after interruptions to supply and to confirm reported issues are fully resolved.

Understanding our customers and getting a real feel for how we're performing in our service delivery underpins everything we do. We use the Rant and Rave system to capture feedback which is then used to influence decision making right across the business. It enables us to hear directly and quickly from the customers we serve about all the good things we do and any areas where we could improve our service. Since going live in 2015 we have received nearly 300,000 surveys back from customers rating our service provision and providing feedback directly to every customer facing employee. In the past year, we received an average of 6,000 surveys back from customers each month with 82% of them scoring us 5/5 as well as providing valuable feedback to help us to continuously improve our service.

> "We provide excellent service and impress our customers"

We routinely collaborate with our water and wastewater customers to push the boundaries of what we deliver, and we've been huge fans of customer participation for years now. It's an ethos that underpins our Unrivalled Customer Experience strategy, and its benefits in unlocking value, building trust and enacting behaviour change, were shown in our Customer Participation report 'From customer consultation to a culture of customer participation', as well as in Ofwat and Corporate Culture's Tapped In report in 2017.

TRANSFORMATIONAL CHANGE

This ambition is why we've been investing so strongly in our transformational change programme, ONCE (Our New Customer Experience). The premise of our ONCE programme is that a customer should only have to tell us once about something and we'll have the agility, focus and people with the right skills, to create a positive experience from it. Our transformation reached a key milestone with the implementation of our new Customer Care and Billing system in the year, in addition to our new Customer Experience Platform implemented last year. These systems use intuitive technology to identify who is calling, allowing customers to be instantly routed to the right team.

We have also been progressing our 'Think Digital' programme, developing new digital platforms, apps, skills, and innovations that will enable us to improve our online and mobile experiences. This is a huge opportunity for us to improve experiences for those customers who want to do things themselves, without having to speak with someone, or wait for a response. We will launch our new web platform in autumn 2019 which will allow us to accelerate improvements to digital customer experience. Every digital customer journey is being redesigned from scratch with customer experience central to our thinking.

We are also exploring other innovative approaches to engaging with our customers and understanding what tools would add value to their interactions with us. One example is our new Alexa Skill, available to download from the skill store, allowing customers to ask about water disruptions in their area and also how much water day to day things use. We are now exploring how we can use this to engage more with our visually impaired customers in relation to their bills.

It's a clear part of our unrivalled customer experience strategy that voice remains a key channel as we know that for some of our customers that will always be their first choice. This means that we always put as much effort into refining and developing our voice channels as we do to our digital programmes.

CUSTOMER SATISFACTION AND VALUE FOR MONEY

Our aim is to deliver an unrivalled customer experience and, in addition to our SIM performance, we track various measures of customer satisfaction with the services we provide and the value for money of those services.

Our own customer satisfaction research is carried out quarterly by an independent company and we were delighted to match our best score of 8.7 in 2018. As an alternative indicator, we use Net Promoter Score to measure customer advocacy, the loyalty that exists between a company and its customers, and are proud to have maintained our strong positive score of +43, which ranks us alongside leading UK businesses.

Our customers tell us that it is important to keep them well informed and 93% of our customers have told us that they were satisfied that they are supplied with all the information they need to feel informed about the services we provide. Over the last few years, as we've prepared to submit our PR19 Business Plan to Ofwat, we've engaged with more than 400,000 customers. We've reached out to them in new and innovative ways about exciting new ideas, as well as talking with them in time-tested ways that we know they recognise and trust.

Our customers have also told us that value for money is very important to them, and this is a key area where they would like to be involved in influencing our future plans. We use two surveys to help us assess whether our customers think we offer good value for money.

> "Our customers consider the services they receive to be value for money"

CCWater carries out research with customers about the value for money of services provided. The results showed levels of satisfaction above the industry average in our NW region for both water and sewerage services, but marginally below average levels in our ESW area where average bills are higher. Whilst results stayed the same for water services in our ESW area and wastewater services in our NW area, we were disappointed that the results for water services in our NW region were lower than last year and that we did not achieve our PC against these measures. We continue to strive to keep bills at affordable levels and we describe our work to support customers in vulnerable circumstance below. We also commission independent surveys for which the value for money score has remained consistent over the last four years at 8.2 out of 10.

SUPPORTING CUSTOMERS IN VULNERABLE CIRCUMSTANCES

We have continued our focus on our support for customers who are in vulnerable circumstances and we recently published our Inclusivity Strategy, which we developed in partnership with our customers. We know that customers' circumstances change as their lives evolve and we know from research for our Inclusivity Strategy, that customers will likely flex in and out of needing a little extra help during their lives. We've engaged with lots of our customers to ensure we have a deep understanding of what this means to them, and we're delighted that our customers have strongly voiced that we do.

Through our strong partnership with the debt charity StepChange we continue to assist our customers to receive holistic debt advice. With the benefit of our data sharing agreement with StepChange we know which of our customers are seeking debt advice so that we can provide them with the breathing space they need to work through their finances.

We launched our customer-funded affordability tariff from 1 April 2018, providing a discount of up to 50% for low income households where their water bills represent more than 3% of net income. With the further support from our customer research we have, from 1 April 2019, extended our affordability tariff to include those on receipt of pension credits. We target promotion of our affordability and priority services to areas where we have the highest levels of customers in difficulty.

In May 2018 we launched our commitment to eradicating water poverty across our supply areas, and an innovative new research and delivery partnership with charity National Energy Action (NEA). We confirmed this commitment as one of the key ambitions in our PR19 Business Plan. The case study overleaf describes this in more detail.

WATER WITHOUT THE WORRY – ERADICATING WATER POVERTY

We committed to a bold new project, working with National Energy Action, the charity that leads in tackling fuel poverty.

At the forefront of this is our commitment to eradicate Water Poverty across all the areas we serve by 2030, challenging all of its causes to make a difference to the lives of our most vulnerable customers.

A household paying more than 3% of their income on water, after housing costs, is defined as being in Water Poverty. It is estimated around 400,000 customers are living in water poverty across our regions. Our aim is that by 2025 we expect to have helped around 300,000 customers and 400,000 by 2030.

With NEA we will be funding the new Water Poverty Unit, to take on the challenge of bringing affordable water and affordable warmth to vulnerable and low income householders. This is a multi-year commitment that will not only help us understand what opportunities there are to help our most vulnerable customers, but also offer opportunities for the wider water, and utilities sector, to take on the challenges set by Ofwat and Ofgem.

As part of delivering this commitment we launched the 'Water without the Worry' initiative, an umbrella campaign bringing together all of our inclusivity work under one banner. This will link together all of our services, from social tariffs and metering to our priority services register, targeting appropriate customers and providing clarity for our people.

Adam Scorer, Chief Executive, NEA, said: "This is a tremendously exciting project. We are delighted to use our 35 years' experience tackling fuel poverty to help better understand and tackle water poverty. People who struggle to afford a warm and dry home will struggle to afford other essential services, such as water. Understanding what works and how it can be applied in energy and water should bring benefits to both sectors and we look forward to working with NWG, and other water stakeholders, to help make it happen."

WATER QUALITY

The water we supply must meet stringent quality standards, set by the DWI, to ensure that it is safe to drink and free of colour and particles, poor tastes and smells. Our overall drinking water compliance remains high at 99.949%, improving on the previous year. To put this in context, this represented only 50 failures from around 81,475 tests, importantly, with no risk to public health.

Whilst we do expect some variation in performance due to samples being taken on a random basis, we are committed to improving water quality even further and have been delivering our plans to achieve this. We have been working throughout our water supply system, from protecting raw water by our catchment management activities through to investing in improvements to our water treatment and distribution processes and systems.

"We supply clean, clear drinking water that tastes good"

We are continually evolving our processes to improve water quality performance over the longer term through our catchment management approach. We work in partnership, within the framework of Defra's catchment based approach, bringing people together to attain the necessary sustainable improvements in the quality of our rivers, reservoirs and groundwater. As part of our PR19 Business Plan we have developed a new partnership scheme 'Improving the Water Environment' to continue this work for the next five years.

CLEAN CLEAR WATER THAT TASTES GOOD

We have been working to reduce the number of discoloured water complaints in our NW area for more than ten years now and have seen a significant improvement over this time. However, our performance has deteriorated slightly from 2,532 contacts in 2017 to 2,594 contacts in 2018 and, when we compare to other companies in the industry, we recognise there is still more to do. We are making improvements at our water treatment works and actively managing our networks to reduce the accumulation of discolouration material. To continue our improvement journey we have identified a new programme of work, with DWI support, for our plans for 2020–25.

The drinking water we supply is of a very high quality but occasionally some of our customers perceive different tastes or odours. This can occur as a result of the use of chlorine to maintain good hygiene in our water supply network, a change in where a customer's water comes from, or how it is treated, or even issues with a customer's own plumbing. We received a slight increase in taste and odour contacts in 2018, though this still represents upper quartile performance in the sector. We have been carrying out research and data science projects to understand where we can improve our customer experience.

RELIABLE WATER SUPPLY

Delivering a reliable supply of water to customers is core to what we do and we have delivered industry leading performance on interruptions to supply over a number of years. We had a challenging year in 2018/19 with more large interruption events occurring than we have seen for some time, increasing the average interruption time per property, although the number of mains bursts reduced in the year. We also invested to increase the pressure for over a thousand customers in the year, leaving less than 200 customers receiving low pressure at the year end.

"We provide a reliable and sufficient supply of water"

We understand the importance of minimising waste from our water networks through leakage. After a difficult year for leakage management in 2017/18, we continued to face extremely challenging conditions for leakage management in 2018/19. We began the year with very high leakage levels in both of our operating areas following the 'Beast from the East' in March 2018. This was followed by a prolonged hot summer causing further mains bursts. However, we maintained a relentless focus on managing leakage and were delighted to achieve our targets in both of our operating regions.

These results have been supported by the introduction of a number of innovative new techniques over the last couple of years (see case study on page 26). Recognising the importance that our customers place on this matter, we have rolled out our leakage portal. This is a new web based service where customers can report non-emergency leaks and view the status of all current reported leaks on a digital map of our operational areas. Customers can opt to receive ongoing updates for any leak, including photos as work progresses to resolve the issue.

STRATEGIC REPORT
GOVERNANCE REPORT
STATUTORY FINANCIAL STATEMENTS

LEAKAGE INNOVATION

We are determined to bring down leakage across our network, and have been utilising a number of innovative new techniques to help us achieve our goal.

This includes harnessing the power of space satellites to help us spot leaks on the ground. Utilising the same technology that helps find water on other planets, we can capture detailed imagery that is sent to our leakage technicians so they can carry out further investigations.

The first phase of activity is primarily focused on large trunk mains that often run through rural areas. These are particularly difficult to identify leaks on due to the terrain and the geography of the region. The sheer speed of the process, the detail it gives, and the distances the images cover will help us further improve our leakage performance.

We have also brought a four-legged friend on board to help us battle leakage! Denzel is a springer spaniel who has been trained to sniff out and locate leaks by recognising the tiniest traces of chlorine used to disinfect our water supplies.

Our customers can also be a great help to us by reporting leaks to us when they see them so we can investigate and fix them as quickly as possible. In 2018 we launched our new online interactive leak map, to make it easier than ever for customers to report leaks to us.

The simple online map allows customers to check if a leak has already been reported to us, and send us details if we don't already know about it. Customers can provide details on the type of leak and even upload their own photos so we can tell how urgent it is. Once a leak has been reported to us we provide updates on the action we are taking, so our customers can track the progress we are making on repairs.

WATER EFFICIENCY

In addition to reducing water lost from our network, we have continued our award-winning whole-town approach to water efficiency, Every Drop Counts, developing this further with a greater focus on changing behaviour. In 2018 we targeted Washington in Tyne & Wear, helping our customers to achieve average savings of 22 litres per property per day, and Barking in our ESW region, where the households we visited saved almost 40 litres per day.

Our exciting new children's play, Super Splash Heroes, has built on our previous primary school work, engaging with over 31,400 pupils in 198 schools on water efficiency over this year. The premise behind Super Splash Heroes is that every single child has the potential to be a Super Splash Hero. The characters are children who transform into heroes by changing their attitudes to using and saving water. The play aims to demonstrate how people can make little changes that will have a big impact on the world around them and to inspire children to make a positive difference through the way they use water.

"We provide a sewerage service that deals effectively with sewage and heavy rainfall"

SEWER FLOODING

Sewer flooding is one of the worst service failures our customers can experience and reducing this remains one of our highest business priorities. The numbers of properties experiencing internal or repeat flooding have reduced significantly over recent years, though we were disappointed to see the numbers increase slightly in 2018/19.

As well as providing capital investment solutions where appropriate and responding quickly and efficiently to issues on our sewer network, our education campaign, 'Love Your Drain' has continued to grow. Spearheaded by the character Dwaine Pipe, we use the campaign to inform household customers about the causes of blockages and what can be disposed of down the toilet and sink, as well as working with businesses about the correct disposal of fats, oils and grease.

SUSTAINABLE URBAN DRAINAGE SOLUTIONS

In addition to addressing immediate flooding issues, we work with other organisations to develop sustainable solutions to build resilience against flood risk. In February 2019, we hosted a successful workshop on Sustainable Urban Water Management, bringing together over 80 partners to think about the barriers and challenges of implementing more sustainable drainage schemes (SuDS) within our regions and actions that could be taken to support the 2019 Year of Green Action. This included representatives from many of our Local Authorities, developers, consultants and environmental NGOs together with NWL and the EA.

"We deliver water and sewerage services that meet the needs of current and future generations in a changing world"

As an example of a SuDS scheme, we are working in partnership with North Tyneside Council and the EA to reduce the risk of flooding to more than 3,500 homes in the Killingworth and Longbenton area of North Tyneside. The scheme uses natural solutions, such as grassed storage areas, as well as traditional infrastructure, to control the amount of surface water entering the sewer network and reducing flood risk. Instead of flooding back to the sewerage system, overflows from the lake will spill into natural grassed areas that run alongside it and drain back to a local watercourse.

Our Rainwise initiative uses data from planning authorities and the EA to identify areas that have flooded or may flood in future. We then work with the communities to explore the best solutions for them. As well as our physical installation schemes, we raise awareness among residents and schools, through our 'SuDS for Schools' educational programme, putting customer participation at the heart of the programme. Rainwise started in 2015 and we've reduced flood risk for over 4,000 properties so far.

INTELLIGENT ASSET MANAGEMENT

We adopt an integrated approach to managing our assets, which means finding the right balance between operational and long-term maintenance and investing in new assets at the right time, in the interests of current and future customers. We have company-wide accreditation to ISO 55001 Asset Management, demonstrating that we follow best practice in the long-term management of our assets.

Our Intelligent Asset Management (iAM) programme is building on this approach and will deliver both improved systems and processes and enhanced data and analytics to improve how we manage our assets. The first two phases of this programme, covering customer contact for operational matters and below ground assets, are being implemented in 2019/20.

ASSET HEALTH

We use the concept of Asset Health to assess the effectiveness of our long-term stewardship of our assets, based on two baskets of measures, for water and wastewater. As asset health is about the long-term stewardship of our assets, we assess our performance on a three-year rolling average basis.

Three out of four of our measures for water exceeded their PC for the three year period 2016/17 to 2018/19. However, our PC for overall drinking water compliance is set at a zero failure rate and, though we have a very high level of compliance, we did have a small number of failures in the year.

On wastewater, all measures exceeded their PC in the year. We had zero sewage treatment works discharge compliance failures in the year, against a PC of zero failures. However on a three year rolling basis we had an average of one failure due to a very low number of failures in the previous two years.

More detail on our asset health performance is available in our **APR**.

RESILIENCE FRAMEWORK

We manage a large and complex asset base where a failure could have significant impacts on our customers and the environment. We know from our research that our customers are increasingly interested in the reliability and resilience of their water and wastewater services.

We have a strong track record as a resilient company. Our water resources are very secure and we have a security of supply index of 100% in all of our water resource zones across the full 40 year planning horizon of our water resources management plan. Our sewer flooding performance for both internal flooding and repeat flooding incidents demonstrates a magnitude of improvement since 2015.

We understand that the uncertainties that exist in today's world, such as climate change, will continue to challenge our business into the future. To demonstrate that we are moving to a position of strength in the future we have developed our own Resilience Framework, an effective way to show the interdependency and complexity of our business systems across corporate, financial and operational aspects. Our Resilience Framework provides a structure for us to achieve resilience in the round by taking an integrated and systematic approach to understanding risk and resilience challenges across all of our business areas. More information on this can be found in our Business Plan at **www.nwgourplan.co.uk**.

ENVIRONMENT

ENVIRONMENTAL PERFORMANCE ASSESSMENT

The EA uses its Environmental Performance Assessment (EPA) to compare performance between water and wastewater companies. It looks at measures on pollution, discharge permit compliance, sewage sludge, delivering environmental improvement schemes and security of water supply. For 2018/19 we were very pleased to be assessed as 4* for our overall performance, classed a Leading status.

POLLUTION INCIDENTS

We manage and maintain a network of almost 30,000km of sewers across the NW region. When we have problems in our sewerage system, such as from blockages and mechanical breakdowns, untreated sewage can sometimes escape into watercourses and the sea causing environmental harm. On occasion, we experience problems with our water supply systems that can also result in environmental impacts.

> "We help to improve the quality of rivers and coastal waters for the benefit of people, the environment and wildlife"

Our transformative pollution management programme, described in the case study on page 32, has helped to reduce the number of incidents significantly in recent years. This focused approach has looked at every incremental improvement that can be made in performance across all our assets. In addition, we have continued our award winning Water Rangers scheme through which a team of dedicated volunteers monitor our waterways and report back incidents so we can respond swiftly.

In 2018, we had our lowest ever number of serious incidents with 2 pollution incidents. These were both Category 2 incidents with one associated with a surface water sewer and the other from a water treatment works. We continue to work hard with the EA, our operational teams and through our Pollution Best Practice Group, to make sure lessons are learnt and serious incidents are reduced further. Our aim remains to have zero serious pollution incidents by 2020.

BATHING WATER QUALITY COMPLIANCE

Our bathing waters in the NW region continue to be amongst the cleanest in the country. Our aim is to contribute to all of the region's bathing waters being 'Sufficient' or better, working in partnership to make this happen as we recognise water quality can be affected by a number of sources, such as run-off from agriculture, urban pollution and from birds or animals.

We had the highest percentage of bathing waters achieving the Excellent standard across England, Wales and Scotland, with 24 out of 34 achieving the highest standard. However, one of our bathing waters, at Cullercoats in North Tyneside, continued its deterioration from 'Good' in 2016 to 'Poor' in 2018.

Since September 2017, we have been working in partnership with the EA and local authority to understand the reasons for the localised decline in bathing water quality at Cullercoats. These extensive investigations have already ruled out a number of potential factors and the EA continue testing outside of the normal bathing water season, with results showing some signs for optimism. The joint investigations will continue until the cause is identified and any remedial works that can be done has been carried out. Already, activities have identified and allowed proactive measures to be taken on a number of third party sites, as well as on parts of our network.

SEWAGE TREATMENT WORKS DISCHARGE COMPLIANCE

The EA sets strict standards for effluent discharged into rivers, estuaries and the sea. These standards are set individually for each of our sewage treatment works, taking into account what is required to protect water quality and ecology. We have a very strong discharge compliance record and achieved our target of zero failures in 2018. This is also consistent with our objective to be a 4* company in the EA's Environmental Performance Assessment.

> "We protect and enhance the environment in delivering our services, leading by example"

We are continuing our planning to meet future new and tighter consent standards and to satisfy our obligations in working towards meeting 'Good' Water Framework Directive status in our rivers. To do this, we will build on our innovative operational management and early warning systems, TriM (trigger management system) and DRIVE (Dynamic Risk Index and Visit Effectiveness), a tool that allows us to understand real-time compliance risk across all of our treatment works. These systems have been adopted both at works with numeric permits and those with descriptive permits. Our operators are also intervening more frequently at our descriptive works in order to prevent permit non-compliance and potential resulting pollution incidents.

We are continually evolving our processes and continuing to work in partnership to attain the necessary sustainable improvements in river water quality, supporting a catchment-based approach to managing the water environment. We are working within four catchment partnerships across the north east, in Northumberland, Tyne, Wear and Tees. A key aim is to ensure our customers' money is spent on well justified schemes that will deliver real improvements to water quality and ecology.

ENERGY EFFICIENCY

Ten years ago we committed to a carbon management plan with the aim of reducing our greenhouse gas (GHG) emissions by 35% by 2020 against a 2008 baseline. We are delighted that we have achieved this goal early with net emissions of 148.2 ktonnes CO2e in 2018/19, compared to 303 ktonnes CO2e in 2008, a reduction of more than half. This has been achieved through a combination of improved energy efficiency and the development of renewable energy along with lower emissions linked to grid electricity. This performance is explained in more detail on **page 94** of the Governance Report.

However, we intend to take this further and have made a new commitment to becoming carbon neutral by 2027. This is achievable in part as a result of our commitment to purchasing renewable energy only through our supply agreement with Ørsted, who generate emission free energy from wind farms around the UK coastline. In addition, we have entered into a ten year corporate Power Purchase Agreement (PPA) with Ørsted, the first of its kind in the UK, to take around a quarter of our renewable energy demand from an offshore wind farm at a long-term fixed price.

We remain focused on energy efficiency and are investigating using real time energy cost data in our management tools such as Aquadapt, which optimises pumping in the supply of water avoiding the use of energy when costs are highest. We are also using data analytics, site energy audits, trigger management and investment in energy efficient assets to drive down our underlying consumption.

In respect of renewable energy, we remain the first and only wastewater company in the UK to use 100% of the sludge remaining after sewage treatment to produce renewable energy at two thermal hydrolysis advanced anaerobic digestion (AAD) plants. We are also continuing to explore other opportunities on solar and industrial scale energy storage.

POLLUTION SOLUTION

Ensuring that we protect and enhance the environment in everything we do is a key part of our vision to be the national leader in the provision of sustainable water and wastewater services.

However, in 2016 we found our pollution performance to be below the level we wanted it to be.

To tackle this we brought together a specialist project team to generate a step change in our pollution performance and it has achieved impressive results. The project team was focused on developing and then implementing ideas to improve pollution performance across our whole wastewater network and assets.

We engaged with our people to form a 'blue-light' pollution response team that allowed a small group of individuals to become experts in how they respond to pollution and minimise the impacts. The teams also introduced weekly incident review and learning meetings and a new escalation protocol, all as part of a zero tolerance approach to pollution. We also began to increasingly use data to promote proactive asset maintenance. For example, we targeted increased maintenance and inspection of sewers near watercourses and CSOs.

The project increased a clear step change in our performance. The Environment Agency's performance report for 2017 showed how we achieved an industry leading 1st place for category 1-3 pollution incidents in 2017 and 3rd place in category 1-2 pollutions. The number of category 1-2 pollutions had been reduced from 9 to 2 and category 3 pollutions reduced from 102 to 58. This performance was maintained for 2018, though with only 1 of the more serious category 1-2 incidents.

COMPETITIVENESS

FINANCIAL PERFORMANCE

The financial performance of the Company is detailed in the Financial Performance and Structure section later in this report.

INNOVATION

Northumbrian Water won the 2018 Transformation and Innovation Award. Showcasing a constant desire for innovation throughout the Company, Northumbrian Water was selected first by the judges for the depth and breadth of the Company's innovative culture.

"We are an efficient and innovative company"

We believe that innovation is the process of turning ideas into business value, and that this is everyone's responsibility. We have engaged with and empowered our people to develop a culture which is open to future change and the potential to improve the lives of our customers and the environment that we live and work in.

We see transformation, innovation and a culture that supports both as the main ways in which we can continue to improve the service that we offer our customers. Driving innovation opens up countless opportunities for us, for example, working with partners to deliver ground-breaking underground mapping, helping us shift from being reactive to issues to predicting and resolving things before they become a problem. Our Innovation Festivals have ensured that innovation is engrained in the way we identify and implement change throughout the business.

We held our second InvestQuest event in 2018, where our employees put forward ideas of how they could generate efficiencies for an investment of up to £250,000. The best ideas were put to our panel of directors in a 'Dragon's Den' style. Peter Gill, Lead Process Technician, and Marc Taylor, Process Technician, were this year's winners with their smart diffusion idea to reduce power consumption at sewage treatment works.

INNOVATION PARTNERSHIPS

We are at our best and most innovative when we combine our people and ideas with those from the outside world. Accordingly, we have built strong relationships with organisations and individuals to support our innovation initiatives. These innovation partnerships have given us early sight of latest thinking and product developments.

We have strengthened our partnership with Durham University, launching an Innovate UK-funded Knowledge Transfer Partnership to develop solutions that will increase flood-resilience in communities, and continue to work with the University, the NE Environment Agency and Durham County Council to support local SMEs and regional growth through the ERDF-funded NE Water Hub.

Our partnership with Newcastle University has grown to include hosting a cohort of 15 third-year undergraduate placements from across science and engineering. We are also proud to be supporting three new doctoral training programmes with Newcastle, Northumbria, Cranfield, Sheffield and Nottingham universities: Water Resilience for Infrastructure and Cities (WRIC), Geospatial Systems and One Planet.

Through our membership of the Cross Utility Innovation Group (with Northern Gas Networks, Northern Powergrid and Yorkshire Water) we share knowledge and look for opportunities for collaboration to tackle shared needs. During 2018 the group held a dissemination event to share the results of our collaborative project on Social cost of Streetworks. In June 2019 we held a joint event to share information and best practice on remote imaging, using satellites and drones.

"Our finances are sound, stable and achieve a fair balance between customers and investors"

NWG INNOVATION FESTIVAL

We held our second NWG Innovation Festival in July 2018, which doubled in size compared to our inaugural Festival in 2017 with almost 2,000 attendees from over 500 organisations. The Festival combined a series of activities including design sprints, tackling major social and environmental issues, and data hackathons, where over 100 data scientists gathered together to solve leakage and flooding problems. We also held a 'Day of Innovation' in September in our ESW area.

Our Festivals have proven to be an effective breeding ground for new ideas, with 34 projects started in the wake of the inaugural event in 2017, including England's first moss tree installed in Newcastle City Centre, seeking to highlight and tackle the problem of urban pollution, usage of data-led heat maps to allow greater targeting of leaks and the creation of the Refill campaign to cut down on single-use plastics by offering fountains in major towns and cities where people can top up water bottles for free. The case study overleaf describes three of the ideas from our 2018 Festival which are being progressed.

The Festival returned in July 2019 for a third year, bigger and better than ever, and we will be staging a three-day Innovate East event in our ESW area in September 2019.

INNOVATION FESTIVAL

As part of our 'Following our Innovation Festival 2018' we carried out 13 design sprints. These are just three of the ideas that have developed further with our partners.

Deeper Underground

Knowing what is underground is vital when we are carrying out works. At our 2018 Innovation Festival we worked with Ordnance Survey (OS) to explore the possibility of creating a shared underground map system that would improve worker safety and reduce the time that the public are inconvenienced by roadworks.

Working with OS and other partners Northern Gas Networks, Northern Powergrid, Openreach, Newcastle City Council, Sunderland City Council and Durham County Council, we are progressing this exciting project that will bring maps of services together for the first time.

Working with our partners we have pooled data to create an underground map of part of the Sunderland area, which covers around 140,000 properties. A digital map is provided of the infrastructure that exists underground, detailing pipework and cables for water, gas, electricity or telecoms. The technology works on a PC, laptop, smartphone or tablet and is accessible for people out on the ground. If the trial is successful we will work alongside OS and our other partners to introduce an underground map covering our entire operating area.

Knowing what is underground before we start digging will really help to protect the safety of our workforce, and reduce the disruption and frustration we cause to our customers through roadworks. If the project works successfully in our operating region we are keen to develop this as a national platform.

Barnacle

The 'Smart Objectives' design sprint looked at ways to use Smart technology to help change and improve customers' lives. The result was 'Barnacle', a smart sensor that can help detect potential issues with a customer's water supply and raise alerts before they are even aware there's a problem.

Gathering data at individual customer level, 'Barnacle' will be placed inside a toilet cistern without the need for installation or any technical or plumbing knowledge. The aim will be to detect discoloured water, identify poor water pressure, identify water leakage through the toilet and highlight risks of freezing pipes. We are also exploring whether Barnacle can detect leaks, either in the supply pipe or deeper within the network.

Along with CGI, we are working with other interested parties to develop this idea into an opportunity to help water customers everywhere. A proof of concept prototype Barnacle has been built, and work is underway to build an automated test rig to perform rigorous performance testing.

Digital Twins

We are working in partnership with Newcastle University on an exciting project to help protect communities from flooding and incidents through the use of pioneering software. Together with four post-graduate students, we are exploring the use of 'digital twin' technology for the benefit of our customers and the environment.

A digital twin, is a virtual model of the real world. It will allow us to run computer-generated simulations of incidents such as burst pipes, heavy rainfall or serious flooding to show what could happen to peoples' homes and local communities over the following 24 hours. This will help us to improve planning, decision-making and response times during real world incidents.

The students are currently helping to develop the 'Twincident' idea, gathering real time data from individual systems across the water and sewer network, and using them in a common framework. Part of this transformation is made possible due to water-modelling software tools developed from fundamental research at Newcastle University over the last six years.

RESEARCH AND TECHNOLOGY

Alongside engaging our people, suppliers and customers in innovative thinking, we continue to: invest in research and technology development, working with partners to deliver projects to help us achieve our current and future PCs. Notable successes this year include:

- Initiating a programme of research into digital twins with Newcastle University (see case study on page 36);
- Building an algal bioreactor to enable one of our employees to embark on a part-time PhD researching the ability of algae to take up nutrients, reducing the energy needed to deal with them in our treatment processes;
- Working with Nuron to deploy the world's first optical fibre-based continuous in-pipe wastewater monitoring system, which will significantly improve the quality of information we collect from our sewer network, enabling us to improve customer service and environmental protection;
- Launching of an Innovate UK-funded Knowledge Transfer Partnership with Durham University to develop a community-based approach to increasing resilience to flooding; and
- Continuing our Royal Society Industry Fellowship with Professor Guangtao Fu of Exeter University on Real-time Decision Analytics for Smart Water Infrastructure.

PEOPLE

GREAT PLACE TO WORK

Our aspiration is for all of our people, current and future, to have a great experience at work and to understand the part they play to achieve our vision, outcomes and to deliver an unrivalled customer experience. We know from our last employee survey that for 81% of our people, work is an important part of their life and that 74% of our people feel proud to work here. We aspire to have an inclusive and diverse culture where our people are supported by their managers, feel confident that their voice is heard and have a workplace where everyone can thrive and feel empowered to be the best they can be.

> "We are seen as a great place to work"

We have continued to develop our employee engagement through our Great Place to Work (GPTW) programme, based on the four themes of My Voice, My Manager, Our Values and Our Shared Story. We engage with our employees through our Employee Relations Framework and through a range of communication channels including director roadshows, structured Team Talk briefings every two months, our weekly H2info e-bulletin, and digital tools such as our intranet and Yammer.

Our annual employee roadshows provide an opportunity for our people to understand our vision and progress towards this. Our CEO, Heidi Mottram, attends all of the roadshow sessions and this year we made it even more personal with groups of 12 having the opportunity to hold an open discussion with Heidi and their director.

> "Our people are talented, committed and inspired to deliver great services to customers"

It's important that people understand the part they play to achieve our vision and outcomes. Our bi-monthly Teamtalk events ensure everyone comes together to discuss performance and key areas of focus. After a session with our CEO, our leaders cascade to their teams with the support of a pack including videos and interactive activities to bring the message to life. In 2018 we held a 'Teamtalk Takeover' where the whole session was focused on our Business Plan submission. This ensured everyone in the business understood how they would contribute to the 14 ambitious goals in the Business Plan.

Our annual employee survey and six-monthly pulse surveys are an opportunity for employees to tell us how they feel about working here. Managers have received results reports for their teams and are involving teams in creating local action plans. We were delighted to be named as one of the Sunday Times 25 Best Big Companies to Work For in the UK in February 2019, coming in at number 19 and being the only water company in the list. Our place in the Top 25 was based entirely on employee feedback through the Best Companies B-Heard survey which took place in October 2018, with 75% of our employees responding across a range of factors, including wellbeing, pay and benefits, personal growth and leadership.

We continue to be accredited as a Living Wage Employer with the Living Wage Foundation, which means that every employee in the Company earns at least the Living Wage, an hourly rate set independently and calculated according to the basic cost of living for the UK.

OUR VALUES AND BEHAVIOURS

Now in its eighth year, our employee awards scheme, known as ViVa (Vision and Values), is our way of saying thank you to our employees for doing a great job or going the extra mile. The best individuals and teams from these nominations are invited to an annual awards ceremony, attended this year by 140 employees.

From over 210 nominations, we ended up with two overall winners in 2018, Billy Pogue, Distribution Technician, and the Wastewater Pollution Reduction Team who each walked away with a £3,000 prize. Billy was recognised for his outstanding dedication to delivering great customer service. He is knowledgeable, polite and has a willingness to solve any issue he's faced with. Billy's consistently great customer service has seen him score 5 out of 5 on our rant and rave system, 88 times in the last year. The Wastewater Pollution Reduction team was our other overall winner after their results driven attitude has seen us move from bottom in the industry to top in the last year. In a real One team effort they have worked really hard to not just deliver great results, they have cleaned up the environment for our communities too.

"Our people act in line with our values"

We developed 'Our Behaviours' with our people across the Company to identify the behaviours we all need to demonstrate to enable us to achieve our medium-term goals and deliver our vision of being national leader. These are embedded into our recruitment and induction process, training, performance management and 360° feedback for all of our people managers.

NWG ACADEMY

Our NWG Academy is a strategy and plan of activities to ensure we have the skills, knowledge and talent we need to continue to give our customers the service they expect and deserve, sustainably. NWG Academy activities are focused to raise our profile as an industry and an employer with the future workforce, develop the talent already in the business to ensure everyone is fit for the future and retain knowledge as people retire.

The majority of our jobs need people to use Science, Technology, Engineering or Maths (STEM) skills to a greater or lesser extent. We also know that, as technology advances, there is an increasing demand for people with these skills in organisations across our operating areas but no real increase in the numbers of young people choosing to study these subjects. We actively take opportunities to support national and local initiatives, and partner with other organisations to work with young people to try to spark their interest in a career using STEM skills.

The WISE Campaign aims to promote women in science, technology and engineering, and has an objective of reaching 200,000, 11-19 year old girls in the next 5 years and encouraging them to find rewarding careers in STEM, where they will be happy and successful. A number of our people who are happy and successful in their STEM careers have volunteered to take the campaign into schools.

When the Apprenticeship Levy was introduced in 2016, we viewed this as an opportunity to use it as funding for the learning and assessment cost of apprenticeships. We've introduced apprenticeships for young people at the start of their career, in areas we've never had apprentices before, such as our Laboratories and Water Regulations team. We've also been able to give people working for us the opportunity to build on their knowledge to support their career and professional development.

Moving forward, we have joined with other utility sector organisations in a Procurement Skills Accord. This collaboration will be a powerful way to address sector-wide skills gaps and shortages. In addition to committing to continue to develop the skills of our people, we will use our procurement practices to encourage investment in training and skills across our supply chain. We have signed up to challenging commitments to encourage our suppliers to become signatories and agree training targets with them and to promote the continuous development of the skills of our workforce and that of our suppliers.

We recognise the importance of effective leadership to empower our people to take ownership and responsibility for delivering an unrivalled experience for our customers. In 2018 we concluded our Extraordinary Leaders Programme (ELP), an 18-month senior leadership development programme launched in June 2017 focused on developing emotional intelligence and organisational trust. We continue to look for ways we can develop and support our managers to be the best they can be and build trusted relationships with their teams. In 2018 we launched our Leadership and Management Development Programme for all new people managers within the Company, designed to provide our managers with a foundation of excellence in their leadership roles.

NATIONAL APPRENTICESHIP WEEK

Apprenticeships form a large part of our learning and development, but it's not all about young people.

In fact, the majority of our people who are using an apprenticeship programme – more than 200 of them – are doing so having already been with us for a number of years, sometimes decades.

However, we used National Apprenticeship Week (NAW) 2019 as an opportunity to help parents understand the benefits of apprenticeships. After all, they are key influencers in the post-16 decision-making process.

We teamed up with the Apprenticeships Ambassador Network North East to kick off NAW 2019 with two events, one of which was aimed at parents and sharing the experience of existing apprentices and their parents.

As part of this, and of our wider National Apprenticeship Week activity, we took a step seen as unique and went out to meet some parents and ask them how their son or daughter's apprenticeship had changed their opinions of this route into employment.

Mandy Cullen, whose son Dale is an apprentice in our Corporate Communications team, said: "I'm thrilled that 20-somethings still have a role that they can go into, earn, learn, and really get a good understanding of the workplace, a full-time job, and it's really, really life changing. It sounds over the top, but it has been, for Dale, really life changing."

Claire Swift, mother of Information Services Degree Apprentice Amber, added: "Everybody always worries about the outcome at the end, no matter who you talk to. But now, I would say, that's always been our worry, of 'are you going to get a job?' but now I can see the benefits that you don't actually need to worry about that."

We also hosted an event to help educate and encourage businesses that do not already take advantage of apprenticeships.

DIVERSITY AND EQUAL OPPORTUNITIES

We recognise the value and importance of diversity and inclusion in our workforce. Our aim is to support all of our people to be the best that they can be in an environment that values and capitalises on everyone's contribution, not only focusing on those elements of diversity that are protected by law.

GENDER DIVERSITY AT 31 MARCH 2019

	Female	Male
Board	2	10
Executive Leadership Team	5	5
Full company	1,033	2,128

In common with many engineering and operating businesses, and in line with what is typically seen in the water industry, our business is currently predominantly male. We are committed to improving our gender balance and are taking positive steps to ensure that our roles are attractive to women as well as men. This has included reviewing the language, imagery and job titles we use when we recruit and highlighting our female role models in operational roles. In 2018 we shared our aspiration to achieve gender-balanced shortlists for senior roles and all apprentice and graduate recruitment, and gender-balanced interview panels for senior roles, and other roles where possible, to minimise the impact of unconscious bias.

We continue to focus on creating an inclusive culture and attracting people from diverse backgrounds to come and work for us. Our aim is to support all of our people to be the best they can be in an environment where they can thrive at work and we are proud that 83% of respondents in our last employee survey agreed that they feel comfortable being themselves at work.

Our Equal Opportunity Policy seeks to ensure that all our current employees and potential employees are treated with respect. We welcome job applications from all parts of the community and it is our intention that all job applicants and employees are treated equally, regardless of their age, ability, marital or partnership status, race, religion or belief, gender or sexual orientation.

We welcome employment applications from people with disabilities and, where existing employees develop disabilities, they are supported to remain in employment, wherever practicable, by providing appropriate adjustments to their roles and/or effective redeployments. Occupational health physicians assist this process with professional medical advice.

GENDER PAY GAP REPORT

We are committed to the principle of equality of opportunity and equal treatment for all of our employees. We published our gender pay gap figures in our Gender Pay Report March 2019, which is available on our websites. The tables below summarise the results from this report, the causes of our pay gap and the steps we are taking to reduce the pay gap.

The gender pay gap is the difference between the average hourly pay for men and women working for an organisation. It is not the same as equal pay which is about a man and woman receiving equal pay for the same or similar job or work of equal value. We are confident we comply with our legal obligations in relation to Equal Pay.

The mean gender pay gap is the percentage difference in the average hourly pay for women compared to men. The median pay gap is the difference between the hourly pay rate for the median woman compared to the median man.

GENDER PAY DATA

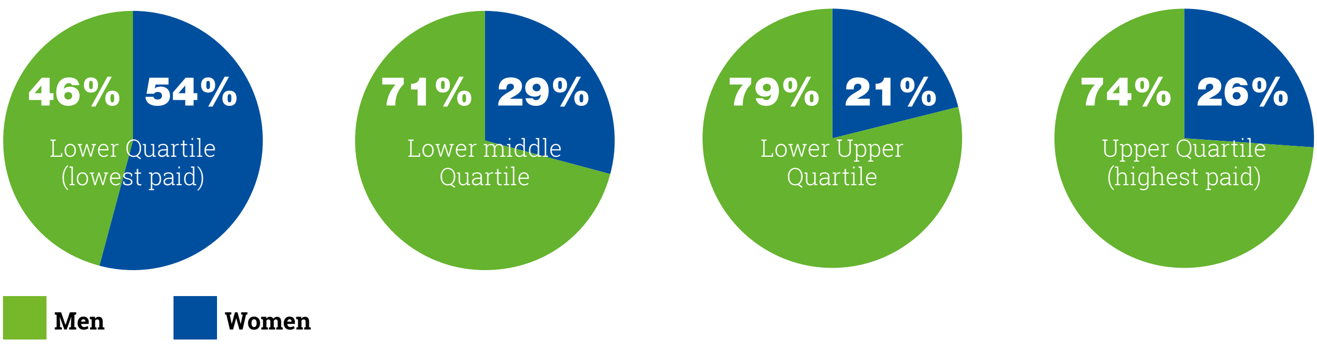
	Mean		
	2017	2018	OFFICE FOR NATIONAL STATISTICS
Pay Gap	11.5%	12%	17.1%
Bonus Gap	13.93%	36.2%	N/A

	Median		
	2017	2018	OFFICE FOR NATIONAL STATISTICS
Pay Gap	17.2%	17.6%	17.9%
Bonus Gap	0%	0%	N/A

PROPORTION OF MEN AND WOMEN PAID A BONUS

Proportion of women	20%
Proportion of men	20%

PROPORTION OF MEN AND WOMEN BY PAY QUARTILES



Figures are based on 774 employees in each quartile.

Our mean and median pay gaps have increased slightly from 2017, however overall since 2010 there is a downward trend in our gender pay gap with our mean pay gap reducing by 7% over this time. We are confident that we will continue to make progress in this area with the activities set out in our action plan.

We have identified a number of key influencers on our gender pay gap.

- More men than women work for the Company - the water industry has historically attracted more men than women and with a low employee turnover, we have a legacy of males with long service. While this means we have people with a great deal of skills and knowledge, it reduces the opportunity for new recruits, including women, to move into more senior roles.
- Fewer females than males studying STEM subjects - currently 22% of the UK STEM workforce is female and changing this will take time. However, we are taking a lead in STEM education in our local communities and our social media strategy and continuing our focus on encouraging girls into the water industry and making sure our job roles at all levels are attractive to women as well as men.
- We have more women than men in our lower pay quartile - this includes our contact centre operation where we employ more females.
- We have more men than women in our senior and middle management population - we continue to work hard to attract and develop more females to these senior roles and have increased the number of females in our senior management roles by 13% over the past ten years.

HOW ARE WE ADDRESSING OUR GENDER PAY GAP?

Over the past year we have continued to develop and embed our actions to improve gender balance at all levels of our business and reduce our gender pay gap. We have set clear areas of focus to further improve across recruitment, attracting girls into STEM careers, leadership development, highlighting role models and fostering collaborative relationships.

Our Action Plan for 2019/20:

- roll-out a female talent development programme with a cohort of our high-potential females;
- expand the activity and reach of the WISE North East Hub with new steering group members and encourage greater networking to support aspiring females across the region;
- launch an NWG women's network;
- conduct a diversity and inclusion audit to understand the experiences of both our men and women and identify areas of focus and actions;
- ensure all people managers have had training in unconscious bias to educate and raise awareness of the impact of bias on decision-making;
- extend the requirement for gender-balanced shortlists in our recruitment process; and
- maximise the opportunity of our 2019 NWG Innovation Festival to challenge gender stereotypes.

In April 2019 we started the process to sign up to the Social Mobility Pledge. Becoming a Social Mobility Pledge accredited demonstrates our commitment to accessing and progressing talent from all backgrounds, and highlights our work towards improving social mobility.

The three main areas we are committed to are:

- more partnerships with school and colleges, providing careers advice or coaching;
- structured work experience and/or apprenticeship opportunities to people from disadvantaged backgrounds or circumstances; and
- adopting open employee recruitment practices which promote a level playing field for people from disadvantaged backgrounds or circumstances.

HEALTH AND SAFETY

It is our aspiration and ethical responsibility to make sure that everyone goes home safe every day, which extends to our employees, supply chain partners and customers. We were very disappointed to see an increase in lost time reportable accidents in 2018/19. However we remain confident that the significantly increased awareness and focus on safety within the business through our Everyone Home Safe Every Day initiative, will lead to sustainable long-term improvements.

> "Our workplaces are healthy and safe"

Engaging our people is central to achieving this. Our engagement activity through the Everyone Home Safe Every Day campaign is about bringing people together, using technology and conversation hand in hand so our people go home safely to their family every day. With lots of our employees having worked for the organisation for years, we've explored new ways to communicate and engage with our workforce. Taking a different approach to the way we engage with our people about safety has made people sit back and take more notice about the things they do every day.

In the past year, nearly 2,000 employees have attended an Everyone Home Safe Every Day half day workshop; over 6,000 '60-Second Checks' were completed and over 650 Safety Conversations were held. During these checks 235 jobs were stopped as employees deemed it was not safe to continue, which is another positive measure. By using innovation and technology we've helped people understand the vital role they all play to stay safe at work. Our employee roadshows included a virtual reality safety session, allowing employees to experience different virtual scenarios to help them look for hazards they'd see in their working day.

We are certified under OHSAS 18001 Occupational Health and Safety Systems and during the year we started a review of our safety systems and procedures with an emphasis on rationalising and simplifying processes. In 2018 we were delighted to be recognised by the Royal Society for the Prevention of Accidents (RoSPA) for outstanding performance in health and safety, receiving the 'highly commended in the water industry' award. The award recognised our robust and high quality safety management system together with consistently excellent health and safety performance, acknowledging how we have progressed with our safety culture.

WELLBEING

We are committed to providing an environment where people can maintain good physical and mental health and make informed lifestyle choices. Our 'Live Well, Work Well, Be Well' health and wellbeing programme continues to evolve and is driven by our top reasons for absence and feedback we receive from employees. As part of our annual wellbeing calendar we hold wellbeing challenges for individuals or teams focusing on physical (weight loss and physical activity) and mental (energy and resilience) challenges, as well as quarterly wellbeing weeks and monthly awareness campaigns.

Our network of Wellbeing Champions support our people by ensuring their teams are aware of our internal wellbeing support such as our Employee Assistance Programme for mental health and our Physiotherapy service for physical health. We have continued our focus on mental health and over the last year have trained over 30 Mental Health First Aiders across the business to support people who may be struggling with their mental health. We have also started a new programme for all people managers to receive mental health awareness training to equip them to have conversations with their people and spot signs and symptoms, and personal resilience workshops are available to all employees.

At the end of 2018 we were re-awarded Continuing Excellence in the North East Better Health at Work Award, a partnership project between the local authorities, NHS and Trades Union Congress, for our ongoing commitment to support the wellbeing of our employees.

COMMUNITIES

Our customers tell us that supporting our local communities is an important part of water company life and something they want us to do.

As a responsible business with a strong track record, it is important to us that we demonstrate leadership and make a wider contribution to life within our regions and the economic wellbeing of the customers and communities we serve.

"We are proud to contribute to the success of local communities"

We use our skills, assets and experience to support communities in areas that our customers have told us are most important to them. Our activities have a 'ripple effect', going far beyond our direct investment through trade with local suppliers to benefit our regional economies. We have a far reaching and extensive community programme that includes employee volunteering, supporting important local events, engaging and helping to educate young people around important issues and long standing partnerships that meet local community needs.

EMPLOYEE VOLUNTEERING

We are proud that our people give their time and resources to the causes that are important to our communities. 'Just an Hour' is our highly successful employee volunteering programme. We know our communities can benefit from the wealth of knowledge, skills and expertise our employees have to give and each of our employees is given the opportunity to take a minimum of 15 working hours a year to support community initiatives. In 2018, almost half of our people volunteered their time, giving support to more than 600 organisations.

POWERED BY WATER

Our Powered by Water sporting partnerships were designed to benefit thousands of young people across our NW and ESW supply areas, teaching them the importance of staying well hydrated and avoiding sugary drinks. Powered by Water is an interactive educational workshop delivered with our partners Newcastle Eagles Community Foundation, MFC Foundation in Teeside, Foundation of Light in Sunderland, Essex Cricket Foundation and Mowden Park Rugby Club in Darlington. In 2018 over 27,500 young people participated in a Powered by Water workshop, and thousands more will have the opportunity to take part in 2019.

WATER RANGERS

We started our award winning Water Rangers scheme in 2014. Volunteers monitor public access routes next to watercourses across the north east that are prone to pollution. In 2018 we expanded the Water Rangers scheme and 1,836 patrols were completed by 78 volunteers.

BRANCH OUT

Our Branch Out fund helps to deliver projects that benefit the natural environment and their local communities. A healthy natural environment is essential for us today and to make sure we can continue to supply top quality drinking water and safely remove wastewater in the future. We supported 17 Branch Out projects in 2018 providing £60,000 in funding, and enabling our partners to bring in additional funds in excess of £1.8m to put towards Branch Out projects in our local communities.

PARTNERSHIPS

Partnership working within our regions is an essential aspect of our approach. By working in partnership with others to deliver common objectives, we can deliver efficiencies and multiple benefits, and support others to achieve their goals too. Our Partnerships Strategy gives us clear direction to make sure we are focusing our efforts on the things our customers have told us are important to them.

"We work in partnership towards common goals"

We work with partners across sectors at a range of levels, from making sure we provide effective grassroots support to a large number of organisations in our community, to a small number of larger strategic flagship partners co-delivering with us in line with our vision and values.

We look beyond our annual finance and performance reporting and also report on our influence and impact in the wider economy, the environment and society in **Our Contribution** report, which is available on our websites.

COMMUNITY PARTNERSHIPS

Our contribution in 2018/19 will be detailed in Our Contribution report, but some of the highlights are shown below.

- 19,485 customers receiving support to make their bills more affordable;
- £962,837 financial contribution to environmental, community and charitable non-governmental organisations;
- 955 organisations supported;
- 48% of our people volunteered to support community projects giving us 13,992 hours;
- 13,000 young people supported through our employability activity;
- 962 'Refill Stations';
- 12,000 people given access to clean water and sanitation through our fundraising for WaterAid;
- over 850,000 visitors to our historical and ecological sites; and
- 1,836 patrols by 78 water ranger volunteers to help protect our rivers.

STRATEGIC REPORT
GOVERNANCE REPORT
STATUTORY FINANCIAL STATEMENTS

GREAT EXHIBITION OF THE NORTH

When the River Tyne's water was launched into the sky by giant fountains as part of the Great Exhibition of the North launch event, onlookers could rest assured that they were seeing great quality H2O in action.

Once one of the dirtiest and most polluted rivers in the UK, the water quality in the Tyne has vastly improved over recent decades, having even become a leading habitat for salmon.

Water sampling conducted by our team to support the event has shown that the industrial pollution of yesteryear remains firmly in the past. More than 20 sets of samples were taken over the weeks leading up to the Festival by our Scientific Services team, in preparation of the Great Exhibition of the North launch event, to make sure the water is as high quality as the 80 days of events that followed.

We were a Supporting Partner of the Exhibition, not only providing the water sampling service to the event, but also involved with and present at a number of the Festival's events. The Great Exhibition of the North was all about celebrating what is fantastic about the North of England, and we are happy to say that the water in the iconic River Tyne is something worth shouting about.

Our region's industrial history has, in the past, blighted rivers such as the Tyne and Tees, but work conducted by ourselves and partners such as the Environment Agency, has resulted in an amazing transformation over the past 30 years or so.

Also on show as part of the Great Exhibition was our industry-leading approach to making 'Power From Poo' which was built into the summer's activities – as part of a special LEGO® showcase! LEGO® artist Steve Mayes, who runs North Tyneside firm Brick This, created an interactive model representing our innovative Advanced Anaerobic Digestion (AAD) work, which uses sludge from wastewater treatment to create energy. We're the only water company in the UK to use 100% of its wastewater sludge in this way at facilities in Howdon, in North Tyneside, and at Bran Sands, on Teesside.

Great Exhibition of the North programme of events (by Richard Kenworthy)

REPUTATION

TRUST

We have been named as one of the 'most ethical companies' in the world by the Ethisphere institute, the eighth time that we've received this global recognition. Ethisphere promotes best practices for ethics and compliance globally, recognising companies for transparency and standards of integrity. We're the only water company in the world to be included in this year's World's Most Ethical Company list and one of only two UK based companies on the list.

"We are a company that customers can trust"

Each year CCWater asks customers for their views about the services they receive from their water and sewerage company. We were pleased that our score for trust increased in our ESW operating region but disappointed that our score dipped in our NW operating region, however our NW score was still above industry average.

Our assurance framework builds upon our integrated management system. We have company-wide accreditation to: ISO 9001 Quality Management; ISO 14001 Environmental Management; OHSAS 18001 Occupational Health & Safety Management; and ISO 55001 Asset Management. In addition our sampling and laboratory analysis are accredited to ISO 17025 and we are working towards achieving company-wide accreditation to ISO 22301 Business Continuity Management.

We work in partnership with customers all year round so that they can trust we have their best interests at heart in everything we do. Throughout 2018 we carried out customer research as part of our PR19 Business Plan and were delighted that 91% of customers involved accepted our Plan. We believe we received such excellent levels of customer support for our Plan, because it was shaped by the views of more than 400,000 customers, as well as by other stakeholders.

In June 2018, Heidi Mottram, our CEO, was awarded a CBE for services to the water industry and business community in the Queen's Birthday Honours list. Upon receiving the award, Heidi said "Though I'm really proud to receive this award, it's really great recognition for the outstanding service we provide together every day. I'll be accepting it on behalf of all of the fantastic team who make NWL such a brilliant place to work."

RESPONSIBLE PROCUREMENT

Responsible procurement plays a vital role in ensuring we can achieve our vision. We are committed to ethically procuring goods, works and services in a way that generates maximum value, not only to our organisation but also to society and the economy while enhancing the environment.

As part of this, we developed the AIME programme which is our way of making a difference, driving continuous improvement and sharing best practice to instil responsible procurement in everything we do. AIME stands for Awareness, Identification, Measurement and Enhancement, setting a consistent approach and objectives for all procurement activities. This has led to a series of creative approaches being adopted.

All procurement staff have undertaken training delivered by the Ethical Trading Initiative, and have all passed the Chartered Institute of Procurement & Supply (CIPS) Ethical test. We developed a Responsible Procurement Toolkit, to help non-procurement staff with purchasing authority to understand key considerations when making procurement decisions, and clauses were used in frameworks and contracts to ensure social value commitments were made by suppliers.

Our approach was recognised at the CIPS Supply Chain Management Awards 2018, which are recognised as a global benchmark for procurement excellence. We were named as overall winners, as well as awarded Best Contribution to Corporate Responsibility. In addition, for the seventh time in eight years, we topped British Water's annual list for supplier satisfaction.

Our commitment to responsible procurement will also support our goal to spend 60p out of every £1 with suppliers in our operating areas.

WASTE TO WEALTH COMMITMENT

We are proud to be taking a lead in changing the way resources are used.

To show our commitment we joined over 90 signatories, including Sky, The Co-operative Bank and Marks & Spencer, to the Waste to Wealth Commitment, which is set to improve the way resources are used and eliminate avoidable waste by 2030.

The event, organised by Business in the Community, was attended by HRH The Prince of Wales, who not only delivered a keynote address, but also got to see our LEGO® 'Power from Poo' model exhibited by Sludge Process Optimisation Controller Tony Rutherford.

By signing this Commitment, we recognise the Intergovernmental Panel on Climate Change challenge that we only have 12 years to change our relationship with the resources we use, if we are to avoid catastrophic climate change and restore the health of our environment. We are committing to set targets; work collectively; redesign how resources are used; collaborate across industry; and reconvene and report on progress annually.

In our PR19 Business Plan we have set a target of eliminating avoidable waste by 2025 and being carbon neutral by 2027, as well as having the lowest levels of leakage in the country in our water-stressed ESW region and reducing per capita consumption of water use to 118 litres per person per day by 2040.

We have been converting 100% of our wastewater sludge to energy for a number of years, the only UK water company to do so. We inject 88GWh of energy into the grid annually at our Howdon site on Tyneside and are developing a second gas-to-grid plant at Bran Sands on Teesside.

"Northumbrian Water has demonstrated leadership and commitment to tackle systemic challenges by signing up to the Waste to Wealth Commitment."

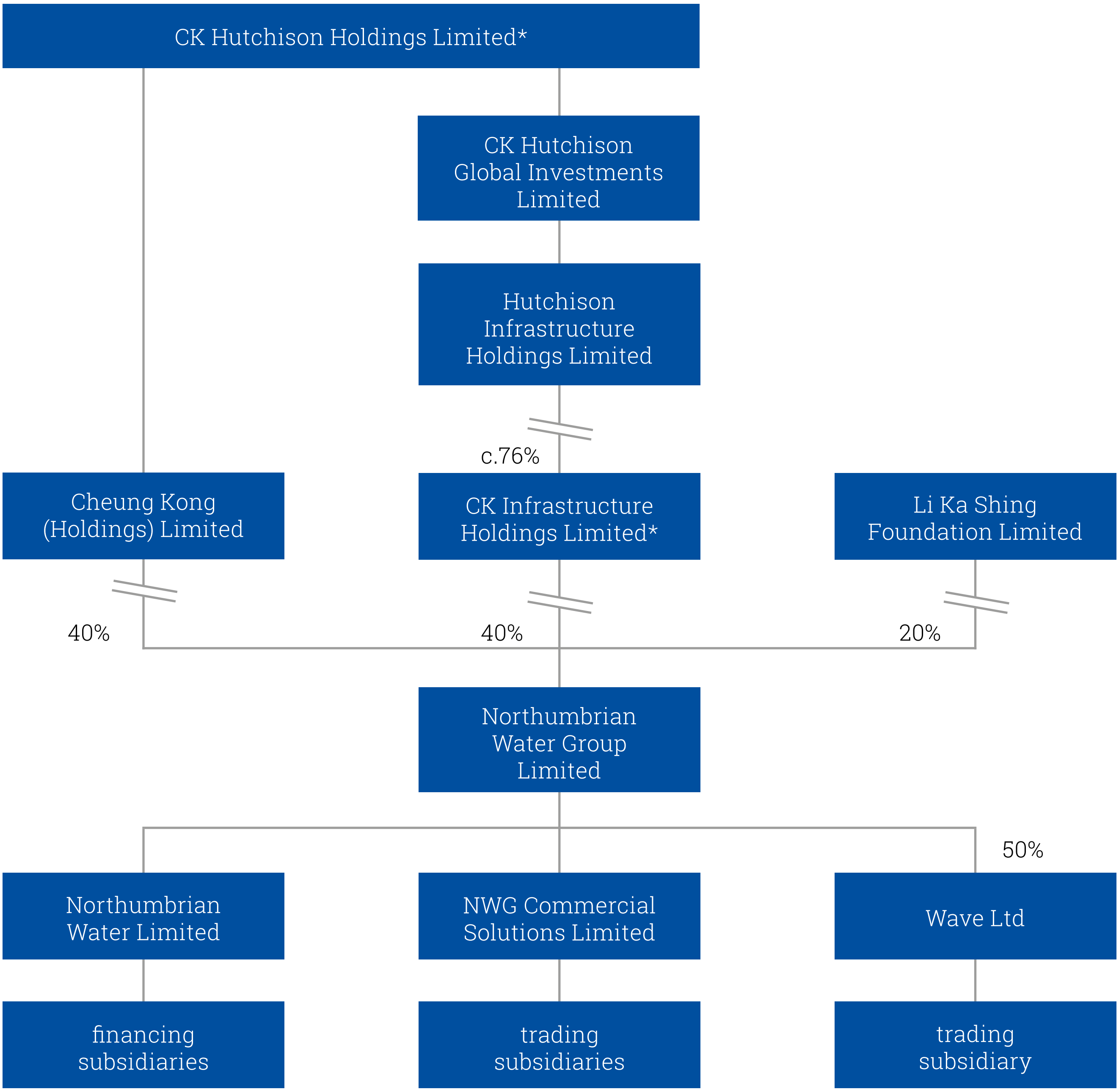
Gudrun Cartwright, environment director at Business in the Community.

FINANCIAL PERFORMANCE AND STRUCTURE

GROUP STRUCTURE

NWL is a wholly owned subsidiary of Northumbrian Water Group Limited (NWGL). NWGL has one other direct subsidiary, NWG Commercial Solutions Limited, which acts as a holding company for other non-regulated trading companies. NWGL also owns 50% of a joint venture company, Wave Ltd. which, through its trading subsidiary, carries out non-household (NHH) retail activities in England and Scotland.

In the Directors' opinion, CKHH is the ultimate parent undertaking and controlling party of NWGL and, therefore, NWL. The chart below shows the structure of the Northumbrian Water Group up to CKHH, as at 31 March 2019. The chart shows the principal intermediate holding companies, which are wholly owned unless otherwise shown (the percentage values represent economic interests).



* Companies listed on The Stock Exchange of Hong Kong Limited.

FINANCIAL PERFORMANCE

The financial KPIs we report in our balanced scorecard on page 20 reflect the financial covenants underpinning our committed bank facilities, which are reported to each Board meeting. These KPIs remained better than the target for the year.

The Company's income statement, statement of comprehensive income, balance sheet and statement of changes in equity are set out on pages 99 to 102. The Financial Statements have been prepared on an historical cost basis in accordance with Financial Reporting Standard (FRS) 101, reflecting International Financial Reporting Standards (IFRS) with reduced disclosures. The key accounting policies are summarised in note 1 to the Financial Statements on pages 103 to 109. Significant new accounting standards, IFRS 15 Revenue from Contracts with Customers and IFRS 9 Financial Instruments, were adopted in the year.

Revenue was £869.1m for the year ended 31 March 2019 (31 March 2018: £834.6m). This reflects an increase in wholesale charges, set in line with the revenue allowance from the Final Determination (FD) of price controls for 2015-20, which increased by a 'K factor' of 0.1% plus RPI of 3.9%, and the impact of implementing IFRS15, the new revenue accounting standard, which resulted in an additional £7.2m being recognised in revenue in 2018/19.

Operating costs, including capital maintenance costs, for the year ended 31 March 2019 were £530.3m (31 March 2018: £495.7m). The increase of £34.6m reflects a one-off cost related to the equalisation of guaranteed minimum pensions (see note 23), increased water supply costs due to an extended period of dry weather conditions, upward cost pressures on chemical prices and non-commodity energy costs and other inflationary pressures. In addition, the amortisation of capital contributions was treated as a negative operating cost in the prior year but reported as revenue, under IFRS, in the current year.

Net interest payable was £130.9m in the year ended 31 March 2019 (31 March 2018: £133.7m). The reduction of £2.8m relates to lower accretion on index-linked bonds, lower interest cost of pensions and increased capitalisation of interest, partially offset by adverse movements on the valuation of derivatives. Profit on ordinary activities before taxation for the year ended 31 March 2019 was £207.9m (31 March 2018: £205.2m).

The current tax charge for the year ended 31 March 2019 was £33.6m (31 March 2018: £32.7m). The increase in the charge mainly reflects higher profit before tax. The deferred tax charge for the year ended 31 March 2019 was £5.5m (31 March 2018: £6.7m). Further details of the net tax charge are provided in note 8 to the Financial Statements. Profit for the year ended 31 March 2019 was £168.8m (31 March 2018: £165.8m).

Total dividends paid in the year ended 31 March 2019 were £130.0m (31 March 2018: £125.4m). The Directors recommended payment of a final ordinary dividend of £65.0m (31 March 2018: £65.0m), which was approved and paid after the balance sheet date. The dividend policy is explained in note 9 to the Financial Statements

CAPITAL INVESTMENT

Total fixed asset additions in the year ended 31 March 2019 were £279.5m (31 March 2018: £260.7m); £255.4m net of capital contributions (31 March 2018: £230.7m). Around £190m of this investment related to the maintenance of our asset base to ensure the continued provision of sustainable water and wastewater services in the areas we serve. In addition we have continued to enhance our asset base, in particular to reduce the risk of sewer flooding, to improve water and wastewater treatment compliance and to support new development activity in our areas of operation.

Significant investments in the year included the completion of our ONCE programme to transform our billing and customer contact systems for household customers and progress on the upgrade of Horsley water treatment works, which serves Newcastle. We have also continued with the implementation stage of our iAM programme, which aims to transform our management of our asset base in support of many of our business outcomes.

CAPITAL STRUCTURE AND LIQUIDITY

The Company's long-term debt structure remained largely unchanged with 63% fixed at an average rate of 4.44%, 35% index-linked at an average real rate of 1.71% and 2% on a variable rate basis, after allowing for hedging instruments. The blended average nominal rate for the Company for the year ended 31 March 2019 was 4.19% (31 March 2018: 4.64%).

In December 2018 we renewed our committed five year bank facility, which is for the purpose of maintaining general liquidity. The value was increased to £450m, from £350m, and will mature in 2023, with an option to extend for a further two years. The facility had £440m undrawn at 31 March 2019.

On 2 July 2019, following a reverse enquiry from a a large UK Pension Fund, NWL, through the Company's financing subsidiary Northumbrian Water Finance plc (NWF), agreed and priced its first UK CPI private placement issuance on a forward settlement basis for a tenor of 20 years, maturing 29 October 2039. The final note purchase agreement was agreed on 2 July 2019 and the notes priced with a CPI real yield of 0.242%.

The gearing KPI, which is measured per the financial covenant for the committed facility and excludes loans receivable, increased slightly from 66.4% to 67.2%, remaining well within target. Interest cover improved slightly from 3.5 to 3.6, also remaining comfortably better than target.

The Company retains strong investment grade credit ratings of BBB+ (negative outlook) from Standard & Poor's (S&P) and Baa1 (negative outlook) from Moody's. The Moody's outlook reflects its view on the gearing level of our parent company, NWGL, whilst recognising the strength of the regulatory ring-fence. The S&P outlook was changed from stable to negative reflecting uncertainty from the regulatory price setting process. We report on our financial resilience in our viability statement on pages 95 to 96.

TREASURY POLICIES

The Board is responsible for the financing strategy of the Company which is determined within treasury policies set by NWGL. The treasury policies set out how the risks associated with treasury activities are managed, which are summarised below. On occasion, derivatives are used as part of this process, but the treasury policy prohibits their use for speculation.

Funding risk

The level of capital expenditure which NWL is obliged to incur is such that we cannot be wholly cash financed by internally generated sources. As a result, we must rely upon raising additional finance on a regular basis, to be principally used to fund the long-term assets required by the regulated business. In order to raise this finance efficiently, the Board's aim is to retain prudent investment grade credit ratings. A reduction in the credit rating would likely restrict future sources of funding, increase the associated cost of new borrowing and prompt discussions with the EIB about the existing facilities in place.

Liquidity risk

The Company's policy is to have available standby committed bank borrowing facilities with a value of no less than £50m and with a bank agreement availability period of no less than three months. At 31 March 2019, NWL had £440m (31 March 2018: £350m) of undrawn bank facilities, provided by a group of five key relationship banks, which mature in 2023, with an option to extend for a further two years.

Interest rate risk

The Company finances its operations through a mixture of retained profits and borrowings. It borrows at both fixed and variable rates of interest and, on occasion, uses derivatives to generate the desired interest profile and to manage its exposure to interest rate fluctuations. The Company's policy is to keep a minimum 50% of its borrowings at fixed rates of interest. At 31 March 2019, 63% (31 March 2018: 64%) of the borrowings of the Company were at fixed rates of interest. Index-linked borrowings are treated as variable rate debt.

Credit risk

The Company invests surplus cash with banks on a short-term basis. The treasury policy specifies which counterparties the Company can invest with and sets a limit for the maximum exposure to each counterparty. These limits take account of published credit ratings. There is no material customer credit risk as no individual customer accounts for a significant proportion of income or debt. Note 1(p) of the Financial Statements sets out the Company's bad debt policy.

Foreign currency risk

The Company's policy is that any foreign currency exposure in excess of £100,000 sterling equivalent of a transactional nature, or £3m sterling equivalent of a translation nature, should be covered as soon as they are identified. At 31 March 2019, the Company had forward foreign exchange contracts of £4.3m (31 March 2018: £7m) for the purpose of hedging the foreign currency risk of committed future purchases.

Market price risk

The Company's exposure to market price risk principally comprises interest rate exposure. The Company's policy is to accept a degree of interest rate risk. On the basis of the Company's analysis, it is estimated that a 1% rise in interest rates would not have a significant effect.

RISK REPORT

RISK MANAGEMENT FRAMEWORK

The Board sets the tone for risk management within the Company, supported by the Risk & Compliance Sub-committee, and determines the appropriate risk appetite. The Board's view of acceptable risk is based on a balanced view of all of the risks in the operating environment and it aims to ensure an appropriate balance between risk aversion and opportunities. The Board's approach to monitoring, managing and mitigating risk, and the work undertaken by the Risk & Compliance Sub-committee during the year, is set out in the Governance Report.

The ELT implements policies on risk management and internal control, ensuring that risks are appropriately controlled, managed and reported and that remedial action is taken as appropriate. The Company's approach to risk management is set out in our Risk Management Framework, which has been endorsed by the Risk & Compliance Sub-committee, and is managed through a corporate risk model.

The Risk Management Framework sets out our process for identifying, analysing and evaluating risk across the business. Risk champions within each area of the business co-ordinate the identification and assessment of risks for their area of responsibility and record these in a departmental risk register. Risk champions meet on a quarterly basis to share learning and ensure consistency of approach.

Each risk is assessed against defined likelihood and consequence criteria on both an unmanaged and managed basis, producing a risk score. The management controls and responsibilities are documented and the effectiveness of the control assessed. An assurance map details the external and internal assurance provided over the controls. We also set a target risk and, where this is below the current managed risk score, set out an action plan to achieve the desired risk reduction.

Those risks in the departmental risk registers with a managed risk score above a defined threshold are classed as 'significant risks' and are reported in the Corporate Risk Register. This is reviewed monthly by the ELT and at each meeting of the Risk & Compliance Sub-committee.

We define strategic risks as those which are foreseeable, but not with sufficient clarity to be assessed within the corporate risk model. These are captured in a Strategic Risk Register and a sub-group of the Board reviews these strategic risks annually, most recently in November 2018.

PRINCIPAL RISKS AND UNCERTAINTIES

The Risk & Compliance Sub-committee, on behalf of the Board, carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity, taking account of both the highest rated risks on our Corporate Risk Register and the Strategic Risk Register identified by the Sub-committee.

The principal business risks facing the Company, and our approach to mitigating these risks, are set out in the table below. The risks are not set out in order of priority. The table also shows how these risks relate to our business Outcomes and any changes in the level of risk compared to last year. These principal risks have also been considered in our assessment of financial resilience, as set out in our viability statement on pages 95 to 96.

OPERATIONAL RISKS

DESCRIPTION OF RISK	MITIGATION	CHANGE FROM PRIOR YEAR
Health & safety The nature of our operational and construction workplaces means that there is a significant inherent risk to the health and safety of our staff and supply chain of which we are acutely conscious. *Our workplaces are healthy and safe*	The health and safety of our staff, contractors and members of the public is our highest priority. We are proud of our record of maintaining a healthy and safe workplace, but not complacent, and we are working hard to improve this further. Health and safety matters are given a high priority at all meetings of our ELT and Board. Long-term planning and targets are set to drive continuous improvement. This is underpinned by our focus on improving behavioural safety and creating a great safety culture. Our health and safety management system defines clear arrangements and responsibilities for implementation and management throughout the Company, and this is externally audited as part of our OHSAS 18001 certification.	No change (focus on continuous improvement).
Customer trust and confidence Our customers are at the heart of everything we do and failure to deliver a consistently unrivalled customer experience or negative media coverage resulting in a poor public perception of our reputation could damage our customers' trust and confidence in our business. *We provide excellent service and impress our customers* *Our customers consider the services they receive to be value for money* *We are a company that customers can trust*	Our unrivalled customer experience strategy was co-created with our customers so that we could understand what was really important to them. We continue to involve customers through active participation and over 400,000 of our customers helped to shape our Business Plan for 2020-25. We have invested in significant improvements in our customer facing systems and we are now working on improving the digital experience we offer to our customers. We continue to improve our support for customers in vulnerable circumstances, through our Inclusivity Strategy, StepChange partnership and new affordability tariffs. We plan to take this further through our commitment to eradicate water poverty across our supply areas.	No change (focus on continuous improvement against a background of increasing customer expectations).
Water service failure A problem in our water system could cause either a major loss of supply or for unfit water to be supplied. This could have many potential causes, including the failure of a strategic water main or treatment works, loss of power supply or contamination of a service reservoir. *We provide a reliable and sufficient supply of water* *We supply clean, clear drinking water that tastes good*	We operate a risk-based prioritisation process for the maintenance and replacement of our assets. We are ISO 55001 (Asset Management) certified on a company-wide basis, demonstrating that we follow best practice in the long-term management of our assets. We monitor the effectiveness of our asset management through a number of asset health measures. We have well developed business continuity plans in place for managing incidents, down to a site specific level. These are regularly tested. We restrict access to our treated water network through authorisation and physical security measures.	No change.

STRATEGIC REPORT
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DESCRIPTION OF RISK	MITIGATION	CHANGE FROM PRIOR YEAR
Wastewater service failure A problem in our wastewater system could cause either significant environmental pollution or flooding of customer properties. This could have many potential causes, including insufficient network capacity to cope with severe weather events, misconnected properties and the consequences of sewer blockages or collapses. *We provide a sewerage service that deals effectively with sewage and heavy rainfall*	We operate a risk-based prioritisation process for the maintenance and replacement of our assets. We are ISO 55001 (Asset Management) certified on a company-wide basis, demonstrating that we follow best practice in the long-term management of our assets. We monitor the effectiveness of our asset management through a number of asset health measures. We continue to invest heavily in preventing pollution and sewer flooding and have a pollution management programme with multiple workstreams to tackle the root causes. We engage with our customers and local communities through initiatives such as 'Love Your Drain' and Water Rangers and working with partners to deliver SuDS. We are also investing significantly in proactive maintenance and cleaning of the network, real time monitoring and analysis, flooding mitigation and investment to increase network capacity.	No change.
Cyber security Key business systems could be lost as a result of a malicious attack or failure of cyber security. Sensitive data could be released in breach of the Data Protection Act, General Data Protection Regulation (GDPR) or Environmental Information Regulations (EIR). New obligations brought into force under the Networks & Information Systems (NIS) Directive. *We are a company that customers can trust*	Our Information Security policy sets out our commitment to the continuous improvement of information security controls and culture throughout the business. This is delivered through software and hardware access controls, additional levels of security for web-facing systems and clear policies and procedures and user awareness, supported by briefings and training. We have implemented a resilient infrastructure which includes full back-up and recovery, and also fail-over to other hardware in the event of a local failure. Data is protected through access controls, laptop encryption and awareness briefings. A ten point data protection action plan has been developed to further mitigate the risks. This activity is supported by a dedicated team covering security, data protection and EIR.	Increased potential penalties under GDPR and NIS Directive.

DESCRIPTION OF RISK	MITIGATION	CHANGE FROM PRIOR YEAR
Effect of climate change In the short term, climate change may cause more volatile weather conditions which could impact on customer service through disrupting water supply or causing sewer flooding. Over the longer term, climate change could impact on water resources resilience and the integrity of our assets. This may be exacerbated by growing population and ongoing urbanisation. *We provide a reliable and sufficient supply of water* *We provide a sewerage service that deals effectively with sewage and heavy rainfall* *We deliver water and sewerage services that meet the needs of current and future generations in a changing world*	Our approach to mitigating short-term risks of service failures on our water and wastewater businesses are set out in the risks above. We consider the longer-term impacts of climate change in our long-term planning, such as our Water Resource Management Plan, and identify long-term solutions to future potential resilience issues well in advance. Our Resilience Framework provides a structure for us to achieve resilience in the round by taking an integrated and systematic approach to understanding risk and resilience challenges across all of our business areas and how they interact.	No change – increasing risk over the long term.

FINANCIAL RISKS

DESCRIPTION OF RISK	MITIGATION	CHANGE FROM PRIOR YEAR
Regulatory and political changes Changes to the Licence or regulatory methodology could impact adversely on the balance of risk and return or reduce investor confidence in the stability and predictability of the regulatory framework. A change in government could introduce significant changes in policy, including nationalisation, impacting upon the Company. *Our finances are sound, stable and achieve a fair balance between customers and investors*	Externally driven, but we have actively engaged with Ofwat throughout the current price review process by responding to formal consultations, regular direct dialogue, contributing to the 'market for ideas' and through other forums such as Water UK. We continue to engage with all political stakeholders, both directly and through Water UK, to ensure that any debate is well-informed. This risk is also mitigated by our excellent performance, behaviours and values.	Increased political uncertainty.

Funding and liquidity risk A key funding risk would be an inability to access future funding at acceptable rates due to market uncertainty. Future borrowing costs could increase as a result of a credit rating downgrade or the loss of EIB as a source of low cost funding, due to Brexit. Liquidity risk could arise due to breaching financial covenants on committed facilities. *Our finances are sound, stable and achieve a fair balance between customers and investors*	The Board has approved treasury policies which set out how we manage treasury risks (see page 52). Our five year plans identify future borrowing requirements and we plan our financing strategy accordingly over this time horizon. This is supported by £450m of standby committed borrowing facilities, of which £440m was undrawn at 31 March 2019, and we maintain substantial headroom in the financial covenants for these facilities. We are committed to maintaining our investment grade credit ratings and manage our financial plans accordingly. Our viability statement on pages 95 and 96 reports on the financial resilience of our plan over a six year time horizon.	Risk remains heightened due to uncertainty in financial markets as a result of the UK's process to exit the EU.

DESCRIPTION OF RISK	MITIGATION	CHANGE FROM PRIOR YEAR
Pensions Risk of increased pension deficit at the next actuarial valuation of our defined benefit pension scheme (at 31 December 2019) as a result of market conditions, increasing balance sheet liabilities and some measures of gearing. Risk of increased employer contributions, for either ongoing service obligations or to repair the pension deficit. *Our finances are sound, stable and achieve a fair balance between customers and investors*	We have an agreed schedule of contributions from our most recent actuarial valuation of our defined benefit pension scheme, as at 31 December 2016. Our employer covenant remains strong, reflecting the long-term nature of our business and 25 year rolling term of our Licence.	New principal risk. This is an area of increased focus across the sector.
Financial performance A failure to deliver our financial plans could impact on expected shareholder returns. This could result from significant adverse movements on costs, interest or tax or a failure to deliver efficiency commitments. A sustained period of low RPI could depress RCV, increasing gearing. An adverse outcome of the PR19 price review, compared to current plans, could result in lower than expected revenues. *Our finances are sound, stable and achieve a fair balance between customers and investors*	We are implementing a range of efficiency actions for both operating and capital expenditure and progress is reported monthly to ELT. We have fixed commodity prices for electricity and fuel to March 2020 and maintain more than 50% of our borrowings on fixed rates, providing certainty. We resubmitted our PR19 Business Plan in the light of Ofwat's Initial Assessment, including additional evidence supporting our expenditure plans. Our viability statement on pages 95 and 96 reports on the financial resilience of our plan over a six year time horizon.	No change (continued uncertainty through regulatory price setting process).

BREXIT RISK

The Risk & Compliance Sub-committee has considered risks to the business which could result from the UK leaving the European Union (EU) with no deal, but does not consider this to be a principal risk, other than in relation to future EIB funding as explained above. We have engaged with government, our supply chain and other stakeholders to review potential impacts of a no deal Brexit. Whilst NWL operates entirely within the UK, we are conscious that some of our supply chain does rely on transportation from Europe. We have made appropriate preparations to mitigate against these risks and ensure continuity of service.

NEW RISKS

As part of their assessment of principal risks, the Risk & Compliance Sub-committee decided that the risks associated with the Company's defined benefit pension scheme should be identified as a principal risk, separate from the existing financial performance risk.

By order of the Board

H Mottram, CEO
12 July 2019

GOVERNANCE REPORT

CHAIRMAN'S INTRODUCTION

We provide essential public services to millions of customers and we are generally the only supplier available. We also have key environmental responsibilities and we are a significant employer and buyer of goods and services.


A J Hunter

The NWL Board fully recognises and understands its responsibilities and has listened carefully to the views of our many stakeholders throughout the preparation of our PR19 Business Plan. The Board is therefore fully committed to ensuring that NWL continues to provide excellent customer service, and that it is ethical and fair in its relationship with all stakeholders.

Corporate governance requirements continue to evolve and Ofwat has recently prescribed four new objectives (the 2019 Objectives) which it expects us to meet. These are set out on pages 68 to 73, below, where we have also explained how we meet them.

Ofwat has recently consulted on incorporating the 2019 Objectives into each company's Instrument of Appointment (Licence). Along with most others in the sector, NWL has consented to the change following discussions with Ofwat, noting Ofwat's acknowledgement that companies will have scope to demonstrate compliance in different ways. That flexibility is consistent both with the "comply or explain" principle enshrined in the UK Corporate Governance Code (UK CGC) and the view of the Financial Reporting Council (FRC) that there is no "one-size-fits-all" version of corporate governance.

Although we expect the 2019 Objectives to become the primary governance framework against which NWL will report, NWL still has in place a further governance code (the NWL Code), developed in discussion with Ofwat in response to its original Board leadership, transparency and governance principles (the 2014 Ofwat Principles). NWL also, currently, has a Licence obligation to have particular regard to the UK CGC.

As a private company with a single ultimate controlling shareholder, we believe it is consistent with good corporate governance for there to be significant shareholder representation on the Board, including the Chairmanship. This is also supported by the Wates Corporate Governance Principles for Large Private Companies (the Wates Review), which the FRC has developed for large, private companies such as NWL. The Non-executive Directors (NEDs) (excluding me as Chairman) are not a majority on the Board and are no greater than the number of Independent NEDs (INEDs), who play a very significant role in the functioning of the Company. The INEDs are instrumental in all aspects of the Board's work, and take a leading role on the various Board Committees where a great deal of important work to support the Board's decisions has been done during the year. The Board relies on the Committees, which are effectively led by the INEDs (within agreed parameters), to handle a very significant volume of important work and present options and proposals to the Board.

Our four INEDs (more than the three required by our Licence) are highly experienced, capable and independently-minded people who bring a diverse range of backgrounds and talents to the Board, as well as a determination to champion customers' interests, environmental matters, and maintain good governance. Working with the other NEDs, they are very effective in scrutinising the performance of management in meeting agreed goals and objectives and monitoring the reporting of performance. We believe our current arrangements, with strong INED input, ensure that there is sufficient independent membership and judgement on the Board, further supporting the Board and its Committees in making high quality decisions that address diverse customer and stakeholder needs.

As I explained in last year's report, the Board continues to function as an integrated whole. All Directors have the same legal responsibilities and each Director understands his or her individual responsibility to act in the best interests of the Company, as well as the importance of the service provided to our customers and our environmental responsibilities. All Directors play a full part in Board meetings and shape the Company's strategy, as well as ensuring that customers' interests are fully considered in any investment and operational decisions. The composition of the Board ensures a sound balance of experience, knowledge and independence and that decision making is not dominated by any single group.

Paul Rew, our Senior INED, again confirms in his report (on **pages 62 and 63**) that the INEDs are fully involved in all the main aspects of NWL's governance and, throughout the year, were invited to, and participated in, all the Board meetings of our holding company, NWGL (except in relation to NHH retail business).

In practice, the Company complies with the 2019 Ofwat Objectives and the 2014 Ofwat Principles. We clearly highlight the very few exceptions in compliance with the principles and more detailed provisions of the UK CGC 2016 in line with the UK CGC's "comply or explain" principle. The effective arrangements which the Board and its Committees have in place to ensure such compliance are explained in some detail below in the Corporate Governance Report (on **pages 64 to 81**).

The Board and Audit Committee (AC) are fully aware of, and have discussed, the revisions made in 2018 to the UK CGC and to other corporate governance provisions and disclosure requirements and I am happy to confirm that many of the proposals are entirely consistent with the Company's existing purpose, culture and approach.

Ofwat has recently conducted a significant consultation on "Putting the sector back in balance", which we addressed in our PR19 Business Plan. Ofwat made some observations on our approach in its Initial Assessment of Business Plans, in response to which the NWL Remuneration Committee elected to partly modify the composition of NWL's short and long-term executive pay incentive targets.

Finally, I am pleased to confirm that our recent Board evaluation exercise delivered very positive feedback on how the Board operates. We again engaged Professor Giovanna Michelon (a specialist in corporate governance and social responsibility) to facilitate the exercise and her report concludes that the Board and its Committees are working well, with particular reference to its healthy and challenging discussions, the balanced mix of expertise and knowledge and the high quality work carried out by the Committees. These findings are entirely consistent with my own view of how well the Board works, on behalf of all the Company's stakeholders.

A J Hunter
Chairman

SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR'S REPORT

As Senior Independent Non-Executive Director (SINED) I am pleased to be able to describe the role of NWL's INEDs, and the key role played by the INEDs in the Board Committees and Sub-committees.

Paul Rew

I can fully endorse the Chairman's explanation of the key role which the INEDs continue to play in NWL's governance, assurance and decision making. I chair the AC, the Assurance Sub-committee, the Risk & Compliance Sub-committee (R&CSC) and the PR19 Board Sub-group, which I explain below. Fellow INEDs sit on all these bodies, as well as on the Remuneration and Nomination Committees. INEDs form the largest group on the PR19 Board Sub-group and are the majority on all the other Committees and Sub-committees.

We are therefore fully involved in all the main aspects of NWL's governance and the Board is satisfied that this enables it to ensure that sound governance is maintained.

Last year I explained the role of the PR19 Board Sub-group, which this year has provided very considerable integrated support to the Board as a whole in driving forward and assuring preparation of NWL's PR19 Business Plan. All INEDs sit on the PR19 Board Sub-group, as do NWL's three Executive Directors and two shareholder-representative NEDs. The PR19 Board Sub-group has been fully involved in all aspects of the development of the Business Plan and all members have carefully reviewed and challenged both the overall strategy and the detailed submissions, as well as the re-submissions following Ofwat's Initial Assessment of Business Plans. On the ground, INEDs have been involved in customer focus groups, meetings of the Water Forums and other stakeholder groups. I would particularly like to thank my fellow INEDs for the very significant commitment of time and expertise they have all made to the PR19 project.

I describe the recent work of the PR19 Board Sub-group, which has met nine times during 2018/19, in a little more detail at **page 74** below. I can assure our customers that their interests continued to be at the heart of its discussions. To this end, my fellow INED, Margaret Fay, with her deep roots in the north east and passion for customer service, has co-ordinated the efforts of the whole Board to champion customers' interests throughout the PR19 process and ensured that customers' views were reflected fully and accurately in the Business Plan.

The INEDs recognise the increasing need for careful and thorough assurance of many of the key projects being undertaken by NWL, to ensure compliance, efficiency and excellent outcomes for customers. An Assurance Sub-committee closely reviewed NWL's major transformation project to implement a new customer care and billing system which successfully went live during the year. We have also carefully overseen the implementation of NWL's assurance framework and the appointment and work of a number of external assurers who have scrutinised aspects of the Company's Business Plan and non-financial performance, as well as the work of our financial auditors. Throughout the preparation of the Business Plan, the INEDs have had a particular focus on company resilience in its many forms and that important work will be carried forward through the R&CSC.

Most decisions relating to NWL are made by the NWL Board alone and the only decisions referred to the NWGL Board were certain large contract awards, capital project approvals, substantial funding arrangements and the re-appointment of certain Directors. During the last year, the NWGL Board has endorsed all the recommendations of the NWL Board. Although the INEDs are not members of the NWGL Board, we have been present at its Board meetings this year, which has continued to encourage a cohesive approach at both Boards and given us full transparency. Naturally, we have not received papers relating to the NHH retail market or been present when that has been under discussion.

I would like to emphasise that, in addition to our extensive work on assurance and our participation in formal meetings, the INEDs have had very broad and continuous involvement in NWL's overall business. We have again all taken part in extensive sessions with management on business risk and customer service. We have also met from time to time without management or the other Directors being present (with and without the Company's auditors) and attended seminars arranged by Ofwat and other events relating to the water sector. Beyond the formal work of the Board and its various committees, INEDs continue to ensure they have more informal insight into the development of the Company's business through other avenues such as NWL's Innovation Festival, customer focus groups, convening and chairing meetings on environmental issues and habitat initiatives, Water Forums, chairing internal sprints on safety matters, and through discussions with Directors and staff at informal events.

In conclusion, I and the other INEDs believe that the Board and Committees have sufficient independent membership. Our INEDs, through their leading role in the Committees, exert significant influence in setting the direction which the Board takes in all key areas of strategy and business planning, monitoring, governance and reporting.

Paul Rew

P Rew
Senior Independent Non-Executive Director

CORPORATE GOVERNANCE

BOARD MEMBERSHIP

The composition of the Board is as follows:


A J Hunter

A J Hunter (Non-Executive Chairman) joined the Board in October 2011. Mr Hunter is Deputy Managing Director of CK Infrastructure Holdings Limited (CKI), which is listed on The Hong Kong Stock Exchange and is a substantial shareholder in the Group. Mr Hunter is an Executive Director of Power Assets Holdings Limited, a listed company. He has been an Executive Director of CKI since December 2006 and Deputy Managing Director since May 2010. Mr Hunter acted as the Chief Operating Officer of CKI from December 2006 to May 2010. Prior to his appointment to the board of Power Assets Holdings Limited in 1999, Mr Hunter was Finance Director of the Hutchison Property Group. He holds a Master of Arts degree, a Master's degree in Business Administration and is a member of the Institute of Chartered Accountants of Scotland and of the Hong Kong Institute of Certified Public Accountants. Mr Hunter chairs the Remuneration Committee and Nomination Committee.

Key strengths: Leadership, strategic overview, finance and infrastructure.


C I Johns

C I Johns (Finance Director) joined the Board in 2013, having served as Finance Director of Northern Gas Networks Limited (NGN), which is also part of the Cheung Kong Group, since 2005. Before joining NGN, Mr Johns, who is a Chartered Accountant, held senior financial management positions in the financial services sector, in both Yorkshire and London. Mr Johns' previous positions include being Head of Finance and Accounting within the UK lending operations of Provident Financial plc, and a senior management role in the Financial Reporting and Control Group of Morgan Stanley.

Key strengths: Finance and infrastructure.governance.


H Mottram

H Mottram (CEO) joined the Board in 2010, when she was appointed as CEO of NWL and NWGL. Ms Mottram is a Non-Executive Director of Eurostar International Limited, Vice-Chair of the North East Local Enterprise Partnership, a member of the CBI Board and Vice-Chair of Newcastle University Council. Ms Mottram was named North East Business Executive of the Year in 2017 recognising her significant contribution to business in the north east of England. She was awarded an OBE in 2010 for services to the rail industry and a CBE in 2018 for services to the water industry and business community.

Key strengths: Leadership, corporate overview, infrastructure and customer service.


P Rew

P Rew (Senior Independent Non-Executive Director) joined the Board in 2010. Mr Rew is a Chartered Accountant and was a partner in PricewaterhouseCoopers LLP (PwC) from 1987 until 2010, where he was lead partner for a diverse range of FTSE 100 clients and for PwC's UK energy, utilities and mining sector practice. Mr Rew is a Non-Executive Director of the Care Quality Commission and chairs their Audit Committee. He was formerly a Non-Executive Director of the Met Office and, until July 2018, of Defra. He chairs the PR19 Board Sub-group, Audit Committee, Assurance Sub-committee and Risk & Compliance Sub-committee, and is also a member of the Remuneration Committee and Nomination Committee.

Key strengths: Finance, risk and corporate governance.

A C Jones

A C Jones (Assets and Assurance Director) joined the NWL Board in 2004. An economist by background, Mr Jones holds an MBA with distinction from Warwick and has extensive experience in dealing with government and regulatory bodies. Mr Jones is a Chartered Environmentalist and worked as a government economist and economic consultant before joining the water industry. He has held non-executive positions at a number of water industry organisations and is currently Chair of Landlord Tenant Access Portal Limited and Deputy Chair of a locally based enterprise development business.

Key strengths: Economic regulation and corporate planning.

M Fay

M Fay (Independent Non-Executive Director) joined the Board in 2010. Ms Fay was Managing Director of Tyne Tees Television until December 2003 when she became Chair of One North East, a position she held until August 2010, and was Deputy Chair of The Sage Gateshead until March 2018. Ms Fay is Deputy Chair of Governors of the University of Sunderland, Chair of South Tyneside Council's Economic Regeneration Board and became Chair of the Customs House South Shields in September 2018. She was awarded a CBE in 2010 for services to regional development and is a Deputy Lieutenant for Tyne and Wear. Ms Fay is a member of the PR19 Board Sub-group, Remuneration Committee and Nomination Committee.

Key strengths: Corporate overview and customer service.

Dr S Lyster

Dr S Lyster (Independent Non-Executive Director) joined the Board in 2006. A lawyer by training, Dr Lyster qualified in both the UK and the USA and is the author of the leading legal textbook on international wildlife law. Dr Lyster was Chief Executive of LEAD International from 2005 to 2011. Before joining LEAD, he was Director General of The Wildlife Trusts and previously worked for World Wildlife Fund for nine years, where he was responsible for its global policy work on international conventions. He is Chairman of Conservation International-UK, a Trustee of Kilverstone Wildlife Conservation Trust and the Rural Community Council of Essex, and a Council member of World Land Trust. In July 2014, Dr Lyster was appointed to the Board of Natural England and he is a Deputy Lieutenant for the County of Essex. Dr Lyster is a member of the PR19 Board Sub-group, Audit Committee, Remuneration Committee, Nomination Committee, and the Assurance Sub-committee and Risk & Compliance Sub-committee.

Key strengths: Conservation, the environment and law.

M A B Nègre

M A B Nègre (Independent Non-Executive Director) joined the Board in 2006. Mr Nègre was, between April 2000 and April 2001, the CEO of the former Northumbrian Water Group plc and the chief corporate representative of its parent company, Suez, in the UK. Mr Nègre was a founding Director of NWGL when it acquired the Group from Suez SA in 2003 and listed it on the London Stock Exchange (LSE). He currently chairs Ecofin Vista Hedge Fund and Ecofin Global Renewable and Infrastructure Fund and is a Non-Executive Director of LSE-listed Investment Trust EGL plc. Mr Nègre sits on the supervisory board of Messieurs Hottinger & Cie. He is a member of the PR19 Board Sub-group, Audit Committee, Assurance Sub-committee and Risk & Compliance Sub-committee.

Key strengths: Strategy, utilities and infrastructure.

F R Frame

F R Frame (Non-Executive Director) joined the Board in November 2011, having been appointed by Li Ka Shing Foundation Limited, a company limited by guarantee and a charity, which is a substantial shareholder in the Group. A lawyer by profession, Mr Frame served as Deputy Chairman of The Hongkong and Shanghai Banking Corporation; as Chairman of South China Morning Post Limited and The Wallem Group Limited; and as a Director of The Weir Group plc, Swire Pacific Limited, The British Bank of the Middle East, Edinburgh Dragon Trust plc and Baxter International Inc. He holds the degrees of Master of Arts and Bachelor of Laws.

Key strengths: Corporate overview and law.

H L Kam (Non-Executive Director) joined the Board in October 2011, having been appointed by Cheung Kong (Holdings) Limited (CKH), a wholly-owned subsidiary of CK Hutchison Holdings Limited of which he is the Deputy Managing Director. Mr Kam is also Group Managing Director of CKI, a position he has held since its incorporation in May 1996. He is the Deputy Managing Director of CK Asset Holdings Ltd., President and Chief Executive Officer of CK Life Sciences Int'l. (Holdings) Inc., as well as Chairman of Hui Xian Asset Management Limited, which manages Hui Xian Real Estate Investment Trust, a listed real estate investment trust. Mr Kam holds a Bachelor of Science degree in Engineering and a Master's degree in Business Administration.

Key strengths: Leadership, strategic overview, finance and infrastructure.

L S Chan (Non-Executive Director) joined the Board in 2016, having been appointed by CKH, and has been an Executive Director of CKI since January 2011 and Chief Financial Officer of CKI since January 2006. Mr Chan joined Hutchison Whampoa Limited, which is a substantial shareholder of CKI, in January 1992 and has been with the Cheung Kong Group since May 1994. Mr Chan is a fellow of the Hong Kong Institute of Certified Public Accountants, a fellow of the Association of Chartered Certified Accountants and also a member of the Institute of Certified Management Accountants (Australia). He is a member of the PR19 Board Sub-group and Audit Committee.

Key strengths: Finance, infrastructure and corporate overview.

D N Macrae (Non-Executive Director) joined the Board in October 2011, and represents CK Infrastructure Holdings Limited, where he holds the position of Head of International Business. Mr Macrae has over 22 years' experience in the infrastructure investment field and holds a Bachelor's and a Master's degree in Philosophy, Politics & Economics. He is a member of the PR19 Board Sub-group, Remuneration Committee and Nomination Committee.

Key strengths: Finance, infrastructure and corporate overview.

STRATEGIC REPORT
GOVERNANCE REPORT
STATUTORY FINANCIAL STATEMENTS

ATTENDANCE AT BOARD MEETINGS

There were five scheduled meetings during the year and one short additional meeting. The Board considered this sufficient to enable it to discharge its duties effectively, and will meet out of the agreed cycle for any other matters, for time-critical matters or significant matters that arise as necessary.

Attendance at the five scheduled meetings during the year was as follows:

NAME	ATTENDANCE
A J Hunter	5
P Rew	5
H Mottram	5
C I Johns	5
A C Jones	5
M Fay	5
Dr S Lyster	5
M A B Nègre	5
F R Frame	3
H L Kam	4
D N Macrae	4
L S Chan	5

The one short, additional Board meeting was attended by all Directors except C I Johns and H L Kam.

COMPLIANCE WITH CORPORATE GOVERNANCE OBLIGATIONS

The Boards of the Company and its holding company, NWGL, are committed to high standards of corporate governance. The Company's Licence contains provisions to ensure that the Company's governance is sound and that its Directors, acting as such, act independently of parent companies. The Licence requires the Company to have particular regard to the UK CGC. Good governance is further underpinned by the 2014 Ofwat Principles, the 2019 Ofwat Objectives and the bespoke governance code, the NWL Code, which the Board put in place in March 2014, following discussion with Ofwat in response to the Ofwat Principles. The NWL Code has been reviewed each year to ensure it is still appropriate and the Board will consider a further review during 2019 in light of the 2019 Ofwat Objectives.

The arrangements and functioning of the Board, its Committees and Sub-committees adhere to the Licence obligations and follow the NWL Code, the 2014 Ofwat Principles, 2019 Ofwat Objectives and the UK CGC 2016, subject to the exceptions explained below. The Board believes that, as a private company with a single ultimate shareholder, it is consistent with good corporate governance for there to be significant shareholder representation on the Board, including the Chairmanship. This is also supported by the recently-published Wates Review. The Board considers that the balance which has been achieved ensures good governance and takes account of the interests of shareholders, customers and other stakeholders. There are four INEDs (more than the three required by the Licence), four NEDs (excluding the Chairman) and three Executive Directors. Although not technically independent, one of the NEDs, F R Frame, is not and never has been an employee of the shareholders and brings an additional strong and experienced voice to the Board, and the Board is satisfied with the mitigation put in place to ensure that good governance is achieved. These arrangements, with strong INED input which is expanded upon in the section below on meeting the 2019 Ofwat Objectives, ensure that there is sufficient independent challenge and judgement on the Board.

The Chairman comments (in his introduction to the Governance Report on pages 60 and 61) on the balance of the Board, which functions as an integrated whole, and the quality and contribution of the INEDs. As the Chairman mentions in his introduction, the INEDs work with the other NEDs to scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. The NEDs carefully review regular, detailed reports which compare all aspects of the Company's performance with agreed targets and hold management to account. The goals and targets (against which the NEDs monitor performance) relate to undertakings and responsibilities to all stakeholders, rather than being purely financial. The INEDs bring an independent approach to this scrutiny and the breadth of their experience and their strong understanding of the operations of the business supports their effective involvement in Board decisions.

The Chairman ensures that the Board works in a collegiate way, in the best interests of the Company and its stakeholders, and that each Director has an equal voice. All members of the Board are content that the balance of the Board is appropriate, in the context of a private company in the water sector with a single ultimate controlling shareholder, and that it has supported and delivered good governance. The Directors have all been able to allocate sufficient time to the Company to discharge their responsibilities effectively.

The Licence requires the Company to obtain undertakings from its ultimate controllers to underpin the Licence and to require the Company's Board to include 'not less than three independent Non-Executive Directors, who shall be persons of standing with relevant experience' and who have collective knowledge of, and connections with, the Company's areas of supply and customers. Throughout the year, the Company had four INEDs, P Rew, Dr S Lyster and M Fay (who were the three INEDs for the purposes of the Licence) and M A B Nègre. Their biographical details are set out on **pages 64 and 65** above. They were appointed on the recommendation of the Nomination Committee of Northumbrian Water Group plc, when it was independently listed. The Board has rigorously reviewed the re-appointment of the INEDs and determined that they are independent for the purposes of the UK CGC, notwithstanding that they have served on the Board for more than six years. Further detail is given on **page 80**.

As the Chairman says in his introduction (on **page 60**), the INEDs, within agreed parameters, effectively lead the work of the Committees, which hold very full meetings with considerable workloads, to prepare the ground for the Board. The INEDs also attend NWGL Board meetings (except in relation to the non-household retail market) and have therefore played a full part in relevant strategic decisions both at the NWL and NWGL Boards. All Directors' views have been given full consideration and due weight in all proceedings of the Board and Committees, Sub-committees and PR19 Board Sub-group.

There is a clear division of responsibilities between the Chairman and CEO. This has been set out in writing and agreed by the Board, in line with the UK CGC.

The Board considers that it complies substantially with the relevant provisions of the UK CGC 2016, except as explained on **pages 79 to 81**. Compliance with the NWL Code is reported on **page 81**.

BOARD LEADERSHIP, TRANSPARENCY AND GOVERNANCE – THE 2019 OFWAT OBJECTIVES

We explain below how we meet the objectives on board leadership, transparency and governance as published by Ofwat in January 2019.

(i) The Board of the Appointee establishes the company's purpose, strategy and values, and is satisfied that these and its culture reflect the needs of all those it serves.

NWL Purpose Statement

The Board has developed the Purpose Statement set out below:

ALIGNING OUR PURPOSE TO OUR VISION AND VALUES

While we have always led with purpose and clearly communicated our vision and values to our people and our stakeholders, we want to explicitly define our true purpose; our reason for doing what we do.

Sustainability is at the core of our purpose, ensuring that we make a financial return so that we are economically viable and support successful economies in our regions; ensuring that we protect our environment for current and future generations, and striving to achieve the ambitious goals that are most important to our customers.

OUR PURPOSE

Water is life. Every living cell on earth needs water to survive. The single most essential ingredient for human life to thrive, is clean drinking water. Our work is instrumental in fulfilling our basic human needs and protecting the source of life.

WE ARE CUSTODIANS OF WATER

Delivering reliable and resilient services that are vital to public health.

We are the current caretakers of the water in our regions, and we take this important responsibility very seriously. Day to day our literal purpose is to supply safe clean water, and effectively remove and treat wastewater so that our communities benefit from excellent public health. At a macro level our purpose is so much more; safeguarding the water supply for future generations requires innovative solutions, anticipating and instigating change, planning ahead and making the right long-term decisions about how to run our business. While our ambition is strong, we set effective and sustainable targets, always considering the lasting impact we leave behind.

WE ARE STEWARDS OF THE ENVIRONMENT

Valuing the natural capital and ecosystems we depend on.

We hold ourselves to account on an ambitious set of indicators designed to protect and improve the environment within our regions, going well beyond our regulatory obligations. We know our operations can be resource hungry but that we can also make a significant contribution to reducing plastic pollution, producing renewable energy, reducing carbon emissions, preventing flooding and improving public access to recreation. It's not enough to offset or compensate for loss of natural resources, our operational activities should have a lasting positive impact on protecting and improving the natural environment too.

WE ARE COMMITTED TO DELIVERING WORLD-CLASS CUSTOMER SERVICE

Giving unrivalled customer experiences every time.

We strive to give our customers leading customer service in the water industry and beyond. Our customer service ethos is core to our brand, values and culture; our people have a drive and energy to truly put our customers at the heart of everything they do. We listen to our customers and are empowered to take action to help them. Our customers are supported to participate fully in our business and in designing the services they receive. Every customer voice is important. Our people are passionate about delivering world-class customer service; they know it is expected of them, and they are committed to it because they believe the services we provide are essential to life and wellbeing. We all want our customers to always have complete trust and confidence in what we do. We own a customer's problem, keep our promises and show each customer that they are special by focusing on individual needs. We know that every interaction with every customer matters.

WE ARE THE LIFEBLOOD THAT FLOWS THROUGH OUR COMMUNITIES

Demonstrating our value and making a wider contribution to society.

We are integral to our communities, always listening to our customers so that we understand what matters most to them and what their expectations are of us. We have a unique opportunity to be able to operate a business that delivers public value. Protecting the most vulnerable people in our society drives us to eliminate water poverty and increase the disposable incomes of those who need it most, reducing the worry they face. Working, living and volunteering amongst our customers helps us to understand and foster a positive impact on the wellbeing of the communities we serve.

WE ENABLE EXTRAORDINARY LEADERS

Empowering people to know their purpose.

We work hard to give our people and the jobs they do a real sense of meaning. Working with a sense of purpose enables personal fulfilment. We foster a high performing culture and value diverse perspectives and skills. We support our leaders to develop high emotional intelligence, enabling our people to behave in the right and responsible way. Our aspiration is for all our people to have a great experience at work and understand the part their play to achieve our purpose and live our company values. Our people have clear Outcomes and are held to account, enabling them to take personal responsibility as they contribute to our sustainability in a balanced way, always striving to be leading.

You can read more about how we live our purpose in the case studies that follow in our **Annual Performance Report** and in **Our Contribution report** for 2019, which looks at our influence and impact in the wider economy, the environment and society.

The Board has ensured, through the process of developing the Business Plan, that the Company's strategy, values and culture are consistent with the purpose as described above. The Company has in place various very strong and effective processes to ensure that behaviour throughout the business is aligned with the Company's purpose. There is a clear line of sight from the Board, through the Executive Leadership Team (ELT), to the reporting lines throughout the Company. The ELT members, including the CEO, are highly visible and have a strong focus on values and culture. This has been embedded through the extensive "Our Way" and other management development programmes with an emphasis on behaviours and taking personal responsibility. The Board would not hesitate to take corrective action if it found misalignment.

Ofwat continues to class the Company's Assurance Plan as "exceeds expectations".

A Board Statement as detailed in Ofwat's provision iv to the "purpose, values and culture" objective is included in NWL's Annual Performance Report for the year ended 31 March 2019.

(ii) The Appointee has an effective Board with full responsibility for all aspects of the Appointee's business for the long term.

The Board sets, implements and supports the Company's vision, values, standards and strategy and ensures compliance with policies and legal and regulatory obligations.

The Board has ultimate responsibility for risk management and determines appropriate risk appetite. The Board's view of acceptable risk is based on a balanced assessment of all of the risks in the operating environment and aims to ensure an appropriate balance between risk aversion and opportunities. The Board monitors the management of risks and approves major decisions affecting the Company's risk profile. The Board is supported in this by the R&CSC, from which it receives regular and detailed reports.

The Board requires management to identify and assess the impact of risks to the business using a corporate risk model. In addition, during the year, a sub-group of the Board carried out a review of strategic risks, which are potentially high-impact risks which are foreseeable but with a high degree of uncertainty.

The Board receives detailed reports from the Executive Directors in advance of Board meetings, covering each aspect of the Company's activities.

The Chairman leads the Board and ensures that all items on the Board agendas are discussed openly and that all Directors have an opportunity to express their views. He encourages constructive challenge, so that ideas and proposals are tested and explored fully. This enables the Board to provide entrepreneurial leadership, as required by the UK CGC, within the framework of the controls described in this document. The Board recognises that customers' interests are best served when the Company is flexible and innovative, so the ELT is always encouraged to think laterally and consider a range of solutions for each issue.

The Company has adopted terms of reference which set out the matters reserved to the Board for approval and matters which are, or can be, delegated to the Committees, Sub-committees and management. These are published on the Company's website. The Board makes key strategic decisions, approves the annual budget and notes the medium-term business plans. It also approves key regulatory submissions and very significant investments or expenditure which is not in the normal course of business. Investments which form part of projects within approved business plans are authorised by committees below Board level. Although this formal framework is very effective, the ELT takes great care to ensure that matters which relate to the quality of the Company's services to customers, leakage, water quality and environmental performance are discussed fully by the Board.

The Company has also adopted financial approval rules which set out the authorisation processes and financial limits to be applied to financial transactions within the Company. The terms of reference and financial approval rules are reviewed regularly by the Board. The Standing or Executive Committees can take decisions not delegated to specific committees between Board meetings. All Directors receive notice of Standing Committee meetings and may participate if they wish. Decisions taken by the Standing or Executive Committees are reported at the next Board meeting. The Company's Board meets at least five times each year.

The Company has put in place Directors' and Officers' insurance cover for the benefit of all Directors of the Company. In addition, NWGL entered into a Deed of Indemnity on 21 March 2017 to provide Directors of NWGL and its subsidiaries further protection against potential liability.

During the year, the Board received regular detailed updates from the Executive Directors on each aspect of the Company's work. There are also regular reports on each Board agenda on customer service, operational performance, health and safety, management of key business risks, the investment programme and regulatory matters. There is a strong focus on the Company's success in delivering its key outcomes, as explained in the Strategic Report. The Chairman of the AC, R&CSC and Assurance Sub-committee reports fully to the Board on their work. In addition, the following significant matters were considered by the Board, as a matter of sound governance:

- the Annual Report and Financial Statements;
- the annual business plan;
- data security;
- decisions on tariffs;
- approval of several significant capital projects;
- review of performance commitment targets and related investment priorities; and
- preparations for PR19 including approval of the PR19 Business Plan.

Several members of the Board attended the Company's Innovation Festival, held in July 2018, and participated in various design sprints. More details of the Festival are given in the case study on pages 35 and 36. As reported last year, members of the Board were also involved in PR19 customer research sessions, and the Chair and Vice-Chair of the Water Forums (NWL's customer challenge groups) have attended Board meetings.

The Board also reviewed the results of the 2019 Best Companies survey, and was pleased to note NWL's ranking as one of the best 25 big companies to work for. The Board also meets and discusses issues with the Company's employees whenever possible.

The effectiveness of NWL's Board has been independently evaluated in each of the last two years (by Professor Giovanna Michelon (a specialist in corporate governance and social responsibility), and very good results achieved. Further details are given below. NWL's Board is absolutely focused on the sustainable, long-term success of NWL. Although proper regard is given to the interests of shareholders, in accordance with company law, NWL's Board has full responsibility for all aspects of the Company's business, including the freedom to set, and accountability for, all aspects of NWL's strategy. This is evidenced by the fact that the PR19 Business Plan was developed and approved entirely by the NWL Board. Any conflicts of interest are declared and Directors do not speak or vote on matters where a potential conflict arose.

Except for certain large contract approvals, funding arrangements and extensions of Directors' contracts, no matters are referred to the NWGL Board. Moreover, all NWL's Board committees report solely to NWL's Board.

(iii) The Board of the Appointee's leadership and approach to transparency and governance engenders trust in the Appointee and ensures accountability for their actions.

NWL publishes the information referred to in this objective in a form and level of detail that is accessible and clear for customers and stakeholders. An explanation of group structure is provided at page 50 of this document and an explanation of dividend policies and dividends paid at page 116. As stated in the dividend policy, when determining dividends the Directors have regard to the Company's operational performance, the level of service provided to its customers and employees' interests, specifically in relation to pension obligations. A fuller description of how the dividend policy is applied is included on pages 131 and 132 of our APR.

An explanation of principal risks, and our approach to mitigating these risks, is provided on pages 53 to 58 and details of attendance at meetings at page 67.

A full explanation of the Company's executive pay policy is provided in the Remuneration Committee Report on pages 82 to 93, including how the criteria for the short-term incentive plan have significant linkage to benefits for our customers and the wider environment. The Remuneration Committee Report also explains changes which will take effect from 2020 to further increase the proportion of performance-related executive pay aligned to delivering benefits for our customers, in both the short-term and long-term incentive plans.

All decisions have been reached by consensus and no votes held.

(iv) The Board of the Appointee and its committees are competent, well run, and have sufficient independent membership, ensuring they can make high quality decisions that address diverse customer and stakeholder needs.

The Board is satisfied that this objective is met and this conclusion is substantiated by the following:

1. The 2018 and 2019 independent Board Reviews did not raise any major concerns and overall the assessments confirmed a sound and effective Board.

In 2018 and 2019, Professor Giovanna Michelon (a specialist in corporate governance and social responsibility) conducted independent evaluation processes to assess the Board's effectiveness in collectively working for the long-term success of the Company and fulfilling its three key roles of setting the strategic direction of the Company, monitoring management performance and providing support and advice. Professor Michelon had no connection with NWL prior to conducting the 2018 evaluation. Paul Rew is an advisory board member of the business school at which Professor Michelon was employed until May 2019 but was not involved in her appointment.

Professor Michelon's 2019 report concluded that the Board is working in a solid way, possibly thanks to the long-term relationships it is founded upon, a high level of trust and the deep knowledge and expertise of the INEDs, healthy and challenging discussions and the high quality work carried out by its Committees. More specifically:

(1) All participating Directors were clearly satisfied with the mix of skills and experience of both executive and non-executive (and independent) Directors, with the secretarial support and quality of documentation and Board minutes;

(2) The Chairman's leadership style was described as "empowering" and able to create an atmosphere where all people feel comfortable to comment and are very appreciative of other people's opinions during the meetings;

(3) The risk management process led by the Board and its committees was felt to be very detailed and thorough; and

(4) Board members fully understood the Company's strategic positioning, and the key issues in the competitive/institutional environments and the culture of the Board aligned with the values of the organisation.

The report prepared by Professor Michelon in 2018, and summarised in last year's Governance Report, suggested that the Board could refine its approach to prioritising the business at meetings. In response to this, the Company's Board pack has been substantially restructured, so that key items and papers are in a single document, with routine papers and supporting materials in another. This has improved efficiency at Board meetings and enabled attention to be focused on the most important matters and the improvement was noted in Professor Michelon's 2019 report.

No significant areas for improvement were identified in the 2019 report. However, it was noted that there may be scope to increase the overall profile of the Board with employees and other business partners.

2. The number and quality of the INEDs on the Board and Committees is clearly "sufficient" for high quality decision-making addressing diverse customer and stakeholder needs.

NWL has four INEDs, rather than three as required by the Licence. Although they are not the largest single group, they have a strong, influential and effective voice. Professor Michelon has confirmed that, on the basis of her interviews with Directors, the INEDs express judgement independently of the shareholders and management. She reports that they all have extensive experience, are not afraid to speak their minds and act as critical friends, and combine an appropriate level of scepticism with independent reasoning and ethical professionalism. She adds that their relatively long tenure gives them real knowledge and understanding of the dynamics of the political and regulatory context in which the Company operates, and ensures that the INEDs fully appreciate, and are equipped to meet, the expectations of stakeholders, customers and employees in particular. It should be highlighted, however, that in the day-to-day work of the Board there is no differentiation between Executive Directors, NEDs and the INEDs. All the Directors have the same legal responsibilities, which they work constructively and seamlessly together to discharge.

It is vital to note that the INEDs play a leading part in the Board committees and sub-committees. Importantly, the AC is chaired by the SINED and three of the four members are INEDs. The R&CSC is, similarly, chaired by the SINED and all three members are INEDs. Professor Michelon described the AC and R&CSC as the "engine rooms" of the Board, with an overall focus on ensuring that NWL has the resilience and long-term financial and operational stability to provide customers with a reliable service and meet the expectations of other stakeholders. More specifically, the AC and R&CSC deliver much of the preparatory work on the Annual Report and Financial Statements and Annual Performance Report, review the work of the internal audit function, review risk management and advise the Board on risk appetite and monitoring compliance with covenants and management of debt. At the AC, there is a particular focus on matters which directly impact customers, such as Guaranteed Standards of Service (GSS) compliance, whilst the R&CSC has held recent "deep dives" on leakage, water resources and cyber security. The AC and R&CSC report fully and frame proposals on all these matters for the Board to consider. Therefore, in addition to their direct input to the Board, the influence of the INEDs and their contribution to the running of the Company, through the AC and R&CSC, is very significant and highly valued.

In September 2018 NWL submitted its PR19 Business Plan to Ofwat, underpinned by a very substantial programme of work. A critically important part of this was to understand the expectations of all NWL's stakeholders and to identify the best and most efficient ways of meeting them over the life of the Business Plan. These stakeholders included customers, employees, shareholders, regulators, suppliers and environmentalists, and civil society generally. The four INEDs were the largest single group on the PR19 Board Sub-group, which drove the production of NWL's Business Plan and provided integrated support to the Board and management in assuring the Plan. The INEDs played a full and active role in the work of the Sub-group and, as part of this, regularly attended meetings of NWL's Water Forums and customer participation workshops, to ensure they had a first-hand understanding of customers' needs and priorities ahead of the price review. This Sub-group was also chaired by the SINED, and again the INEDs, through their active participation in this Sub-group, led many of the key decisions and ambitious positions reflected in the Plan.

The Remuneration Committee also includes a majority of INEDs, who are therefore fully engaged in all discussions and decisions on executive incentivisation and reward, with a view to meeting goals relating to customers and other stakeholders.

The INEDs make full use of their individual professional expertise and personal interests to make an important contribution to addressing the needs of stakeholders other than customers. For example, Simon Lyster is a board member of Natural England with a strong interest in the environment and long term resilience. This role is directly relevant to NWL's position as a custodian of the environment and Dr Lyster brings an expertise in environmental protection as well as an understanding of stakeholder perspectives in this area. Similarly, Paul Rew was a Non-executive Director of Defra until 2018, enabling him to bring extensive knowledge of environmental matters and stakeholders to his role at NWL. Martin Nègre brings first class knowledge of the global utilities sector, whilst Margaret Fay champions customers and has excellent contacts across NWL's north eastern operating area.

In conclusion, the Board believes that the Board, Committees and Sub-committees have sufficient independent membership to meet the objective. We have evidenced above that our INEDs, through their leading role in the Committees, exert significant influence in setting the direction which the Board takes in all key areas of monitoring, governance and reporting, whilst working collegiately with the other Directors. Professor Michelon has, importantly, endorsed this view, as well as advising us that, in her opinion, the absolute number and relative proportion on the Board of INEDs does not itself matter, when governance is sound and decision making appropriate.

AUTHORISATION OF DIRECTORS' CONFLICTS OF INTEREST

Directors have a statutory duty, under s175 of the Companies Act 2006, to avoid a situation in which they have, or could have, a conflict of interest with the Company's interests. However, there is no breach of this duty if the Board has authorised the matter in question. The Articles permit Directors (other than the Director having the interest in question) to authorise any situation giving rise to a known or potential conflict. A register of the interests which have been authorised is maintained by the Company Secretary and is available at every Board meeting

WORK OF THE COMMITTEES

Details of the work of the PR19 Board Sub-group, AC, R&CSC and Nomination Committee is set out below. During the year, in addition to her review of the effectiveness of the Board, Professor Michelon also conducted a review of the effectiveness of the AC, the R&CSC and the Assurance Sub-committee. The evaluation was conducted by means of a questionnaire and a number of one-to-one interviews, following which Professor Michelon produced a written report. The main findings were as follows:

- Directors were satisfied that the AC and Sub-committees are working appropriately and are well chaired;

- Oversight of external audit, risk management and internal controls and assurance is considered to be excellent;
- The composition of the AC and Sub-committees is believed to be appropriate; and
- The quality of feedback to the Board is thought to be high.

Professor Michelon also reported that there may be scope for more training and technical updates and to ensure that the number and timing of meetings is kept under review. She also noted a suggestion that the Internal Audit function may be able to make use of further insights or alternative methodologies via more use of co-sourcing. Finally, she suggested that Internal Audit reports could usefully highlight the risks associated with the areas covered by audits in the event that any errors were identified.

PR19 BOARD SUB-GROUP

As reported in last year's Governance Report, given the critical importance of our Business Plan proposals, the Board formed a dedicated PR19 Board Sub-group to provide integrated support to both the Board and management in producing and assuring NWL's Business Plan.

All INEDs sit on the PR19 Board Sub-group, as do NWL's three Executive Directors and two NEDs. The Sub-group met five times during 2017/18 and nine times during 2018/19.

The Sub-group discussed detailed reports from the Company's PR19 team, covering each aspect of the preparation of the Business Plan for PR19. This included:

- customer engagement and participation;
- affordability and inclusivity;
- our goals and ambitions;
- the drive for upper quartile efficiency;
- the Water Industry National Environment Programme;
- the enhancement programme and resilience;
- establishing MoS, PCs and Outcome Delivery Incentives (ODIs);
- the progress of the Business Plan against programme milestones; and
- assurance of the Business Plan.

The PR19 Board Sub-group worked closely with the Company's full Board, ELT and relevant senior managers below that level, as well as external assurance providers. In addition, INEDs regularly attended meetings of NWL's Water Forums and customer participation workshops, to ensure they had a first-hand understanding of customers' needs, priorities and concerns ahead of the price review. Following management's confirmation to the Board that the proposed PR19 Business Plan was deliverable, coupled with a supportive recommendation from the PR19 Board Sub-group, the Board approved the submission of the PR19 Business Plan on 18 July 2018.

On 31 January 2019, Ofwat published its PR19 Initial Assessment of Business Plans, categorising NWL as "slow track" and requiring it to revise some elements of its Business Plan. The PR19 Board Sub-group met on 12 February 2019 to discuss how this would be approached, as well as identifying several aspects of the assessment which the Company wished Ofwat to reconsider. These matters were all set out in the revised Business Plan which the full Board approved on 29 March 2019 and which was resubmitted on 1 April 2019.

AUDIT COMMITTEE REPORT

Introduction by the Chairman of the Committee, Paul Rew

The role of the AC is to assist both Executive and NEDs of NWL and its subsidiaries (the NWL Group) to discharge their individual and collective responsibilities in relation to:

- ensuring the financial and accounting systems of each NWL Group company are providing accurate and up-to-date information on its current position;
- ensuring the published Financial Statement of the NWL Group companies represent a true and fair reflection of this position;
- ensuring the integrity of the Company's regulatory reporting systems and the accuracy of its regulatory reports; and
- assessing the integrity of internal financial controls.

The Committee also maintains oversight of internal and external auditors. I have worked with the members of the Committee and with management to produce an action plan for the Committee, setting out the business to be addressed at each meeting. This plan is dynamic and is updated throughout the year. The members of the Committee are updated regularly on developments in financial reporting requirements and on any changes in NWL's regulatory environment.

Members of the Audit Committee

The members of the AC are P Rew (Chairman), Dr S Lyster, M A B Nègre and L S Chan.

The CEO, Finance Director, Assets and Assurance Director, Internal Audit Manager and the external auditor normally attend the Committee's meetings by invitation and Martin Parker is Secretary to the Committee. Other senior managers and advisers are invited to attend as appropriate.

The work of the Audit Committee

During the year, and up to the date of approval of these Financial Statements, the AC assisted both Executive and NEDs to discharge their individual and collective responsibilities. Its work included the following:

External Audit

- reviewing the draft Financial Statements and Annual Performance Report, considering reports from the external auditor setting out the audit approach and plan, significant audit risks and conclusions on the NWL Group's internal controls and risk management;
- considering the key areas of judgement in the Financial Statements, reviewing reports from management, and ensuring these are consistent with those set out in note 1(r) to the Financial Statements on page 108;
- reviewing the appropriateness of accounting policies and evidence supporting the going concern basis for the Financial Statements and recommending approval of the Financial Statements to the Board;
- reviewing and monitoring the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements; and
- approving the external auditor's fees for both audit and non-audit services, by reference to the agreed policy (see further details below).

The Committee monitors the independence of the audit through different reviews and actions including:

- confirmation that the auditor is, in its professional judgement, independent of the NWL Group;
- obtaining from it an account of all relationships which may affect the firm's independence and the objectivity;
- rotation of the lead audit partner every five years. NWL's current lead audit partner first signed the Annual Report in 2016;
- maintaining a policy regarding the engagement of the auditor to conduct non-audit work and monitoring the level of audit fees compared to non-audit fees (see further details below);
- considering audit tender requirements, being tenders every 10 years and mandatory rotation after 20 years. Deloitte was first appointed in respect of the 2012 Annual Report;
- considering new accounting standards and reviewing their applicability to the Company;
- reviewing the approaches taken to bad debt and taxation provisioning as well as unbilled revenue recognition; and
- reviewing reporting from management or the external auditor on the accounting judgments associated with property, plant and equipment, and assumptions taken regarding valuing financial instruments and the defined benefit pension scheme liability.

In addition, the Committee considers the effectiveness of the external audit through their interaction through the year. This included consideration of the level of experience, industry knowledge and expertise of the audit team, and their delivery of appropriate challenge in a knowledgeable and constructive manner. A survey of key stakeholders was completed which also supported this review.

Non-Audit Fees

The Company has adopted a formal policy on the provision of audit services, which was updated with effect from 1 April 2017, to reflect the Financial Reporting Council's Revised Ethical Standards 2016.

The policy provides for general pre-approval of a range of services which are generally regarded as audit related, where the fees are equal to or less than £50,000. It also sets out a broad range of prohibited activities.

Services which are not prohibited, but which have not been pre-approved and in respect of which the fee is equal to or less than £50,000 can be approved by the AC Chairman, who reports such approval to the AC. If the fee for such services will exceed £50,000 the approval of the AC is required.

The policy imposes a cap on non-audit fees equal to 70% of average audit fees for the previous three years.

Where Deloitte LLP is engaged to provide non-audit services, this results from its extensive knowledge of NWL's business and the sector generally, as well as demonstrating the required expertise and capability to provide good value for money.

Non-audit related work undertaken by Deloitte LLP in 2018-19 amounted to fees of £158,000, which represents 36% of total fees paid to Deloitte LLP. The fees paid are set out in note 4 to the Financial Statements on page 110. The non-audit work in 2018-19 comprised assurance work in respect of PR19 submissions, consultancy work by Deloitte's subsidiary Market Gravity and advice on Bran Sands gas-to-grid, as well as some smaller items of consultancy work.

The AC also holds in camera sessions with the audit partner.

Having considered the effectiveness and independence assessments above, the AC agreed to recommend to the Board that Deloitte LLP continues as external auditor.

Internal Audit

The NWL Group operates a blended model for its internal audit function. Under this model, the internal audit team conducts the majority of the work, including core financial controls and regulatory reporting reviews. Reviews of specialist technical areas are outsourced to firms with appropriate experience and qualifications when felt necessary.

The Committee reviews and approves the internal audit plan for the year. Its review is designed to ensure that focus is given to the areas of highest risk for the NWL Group and that the audit work focuses on key controls.

Internal audit reports reviewed by the Committee during 2018/19 included:

- April 2018

  Customer Accounts and Billing

  Procurement – Building Maintenance

  Fuel Cards

  Review of contractor tender process
- August 2018

  Regulatory data assurance reports APR and PR19

  Procurement – Purchasing cards
- January 2019

  Process Review – Interruptions

  CKI/CKHH audit report – IS general controls and pollution incident reporting

  Travel and Entertainment cards
- April 2019

  Process Review – Sewer Flooding

  Financial Accounting

  Wholesale Services

  Process Review – Service Reservoir and Water Tower Inspection Programme

In addition, at each of its scheduled meetings the Committee received reports detailing progress with implementing recommendations previously raised by internal audit and is satisfied that management has taken appropriate steps to implement the recommendations raised.

The Chair of the Committee, independent of management, maintains regular and direct contact with both the internal and external auditor, allowing open dialogue and feedback.

The Committee has considered the effectiveness of internal audit. There was also an external assessment completed by the Chartered Institute of Internal Auditors during the year which overall noted that the function "clearly meets the expectations of its stakeholders". The Committee is satisfied that the current model described above remains appropriate for the Group.

Work with other assurance providers

Support with data assurance work for the principal regulatory reporting (including the APR, Water Resource Management Plan and PR19 in the year) provided by Deloitte LLP for financial tables and PricewaterhouseCoopers (PwC) or our Internal Audit team for non-financial tables.

Our overall approach to assurance of regulatory data has been approved by the Committee and is described below:

- business as usual assurance for our ongoing data capture and measurement processes;
- each piece of data must be provided by the nominated data provider and reviewed before being audited. This is controlled by a workflow system which was introduced this year; and
- additional independent technical assurance was procured (from PwC as our External Technical Auditor) to examine areas that were identified as being higher risk as defined by our regulatory data risk management framework as approved by the Committee. Our approach is described in our draft and final assurance plans with the results being described in our Data Assurance Summary annually.

Reports from Deloitte LLP, PwC and Internal Audit are received and reviewed by the Committee.

Other compliance matters

- reviewing and commenting on the Annual Performance Report, including the underlying assurance, reviewing evidence to support the Condition F6A.2A certificate (statement of sufficiency of financial resources) and long-term Viability Statement and recommending their approval to the Board;
- approving arrangements for monitoring compliance with the Company's procedures designed to prevent bribery, having regard to the Bribery Act 2010 and the updated code of conduct 'Our Way at NWG', including receiving reports on any whistleblowing allegations; and
- management of tax compliance matters and other tax issues, including Base Erosion and Profit Shifting (BEPS) and replacing NWL's Advance Thin Capitalisation Agreement with HMRC.

The AC Chairman reports formally to the NWL Board following each AC meeting, and its minutes are circulated to both NWL and NWGL Boards.

Attendance at the five AC meetings during the year was as follows:

NAME	ATTENDANCE
P Rew	5
Dr S Lyster	5
M A B Nègre	5
L S Chan	1

Given the need for careful and thorough assurance of a number of NWL's key projects, to ensure compliance, efficiency and excellent customer outcomes, the AC has an Assurance Sub-committee whose three members are all INEDs. Although the Sub-committee has a broad remit, its work during the year focused on:

- NWL's major transformation project to implement a new billing system to manage household customer billing and contact;
- the assurance plan for March 2019 reporting; and
- assurance of 2019/20 charges.

The Sub-committee met once with Executive Directors, senior management and independent assurance providers during the year and all the members were present.

P Rew
Chairman of the Audit Committee

RISK & COMPLIANCE SUB-COMMITTEE REPORT

Introduction by the Chairman of the Sub-committee, Paul Rew

The role of the Sub-committee is to assist both Executive and NEDs to discharge their individual and collective responsibilities in relation to assessing the scope and effectiveness of the NWL Group's risk management systems and the integrity of its internal financial controls.

Members of the Risk & Compliance Sub-committee

The members of the R&CSC are P Rew (Chairman), Dr S Lyster and M A B Nègre.

The work of the Risk & Compliance Sub-committee

The ELT implements policies on risk management and internal control and ensures that risks are appropriately identified and managed within the business, to ensure that the Company's resources and capacity to deliver services as required by customers remain resilient. This approach is set out in a Risk Management Framework, which has been endorsed by the R&CSC. The ELT reviews the approach to risk management in detail every year and reviews the significant risks every month. Any significant issues are reported by the CEO to the Board. Senior management implements policies on risk management and internal control.

The R&CSC, on behalf of the Board, has performed a robust assessment of the principal risks facing the Company, including those that would threaten its business model, resilience, future performance, solvency or liquidity. These principal risks, and how they are managed, are described on pages 53 to 58 in the Strategic Report.

The internal control framework supports the risk management process, ensuring that risks are appropriately managed, that controls are effective and that appropriate remedial action is taken where identified. Risks are mapped against the providers of assurance, whether this be management, internal or external assurance. The Board is supported by the AC in monitoring the effectiveness of the internal control framework with primary assurance being provided by the internal audit team.

The R&CSC, on behalf of the Board, has carried out an annual review of the effectiveness of the Company's risk management and internal control systems. This review confirmed that the Company has strong systems of internal control and robust processes in place to enable it to identify, evaluate and manage the risks it faces and to ensure that its obligations are met. These systems and processes are embedded in the organisation and are reviewed regularly by the Board, its Committees and Sub-committees. The annual review confirmed that the risk management and internal control systems have operated effectively through the year and that there have been no significant failings or weaknesses.

During the year, and up to the date of approval of these Financial Statements, the work of the R&CSC included the following:

- reviewing reports at each meeting on the top-rated managed risks and priorities for assurance (being those risks with the biggest reduction between the business (gross) and managed (net) risk scores), representing key control areas for the Company;
- reviewing high impact, low likelihood risks which have a rare to unlikely likelihood of occurrence but a potentially catastrophic level of impact;
- reviewing the management of specific areas of risk in relation to the introduction of the new customer care and billing system and other matters including Health and Safety (H&S) and business continuity arrangements;
- advising the Board on risk appetite and exposure and reviewing risk assessment processes as well as keeping the effectiveness of the risk and internal control management systems under review;
- monitoring compliance with covenants and treasury risks;
- reviewing management of customer debt;
- "deep dives" on leakage and cyber security; and
- reviewing the risk and control framework and reporting;

Attendance at the three scheduled R&CSC meetings during the year was as follows:

NAME	ATTENDANCE
P Rew	3
Dr S Lyster	3
M A B Nègre	3

The Sub-committee holds a special meeting with other members of the Board each year to conduct a separate strategic risk review exercise.

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The Board is able to monitor the impact of environmental, social and governance matters on the Company's business, to assess the impact of significant risks on the business and to evaluate methods of managing these risks through reports it receives from the AC and the R&CSC.

P Rew

Chairman of the Risk & Compliance Sub-committee

NOMINATION COMMITTEE

The Nomination Committee has wide-ranging terms of reference which are available on the Company's website. The members during the year were A J Hunter (Chairman), P Rew, M Fay, Dr S Lyster and D N Macrae. The Committee met once formally during the year, principally to discuss the provisions of the UK Corporate Governance Code 2018 and set out a programme of work for the year. There were further ad hoc discussions as required through the year.

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE 2016

The Board considers that it complies substantially with the relevant provisions of the UK CGC where they are appropriate for a privately-owned company, except as explained below. The Board also concurs with the FRC, including in relation to the UK CGC, that there is no "one-size-fits-all" version of corporate governance. In addition, the Board also explains below how NWL has complied with certain provisions, where we believe this will be helpful.

Code Provisions

A.3.1: The Chairman was appointed by the Group's shareholders which is considered to be appropriate, given that NWL is a private company with a single ultimate controlling shareholder. This is also supported by the Wates Review, which has been specifically developed by the FRC for large, private companies such as NWL. As per the 2014 Ofwat Principles, there is a SINED, P Rew, who is available to liaise with Ofwat in respect of any regulatory matter.

A.4.2: The Chairman has informal discussions with the NEDs (both individually and collectively) as the need arises, though it has not been felt necessary to hold formal meetings with them without the executives present. The NEDs have not formally appraised the performance during the year of the Chairman, but such an appraisal will be conducted in following up the Board performance review.

B.1.1: The Board has determined that the following Directors are independent for the purposes of the UK CGC, notwithstanding that they have served on the Board for more than nine years:

- M A B Nègre (appointed in 2006). Mr Nègre has no prior connections with the Group's shareholders. He is a very experienced director, and brings to the Board an excellent understanding of the business coupled with sound commercial judgment. The Board is satisfied that he continues to demonstrate a fully independent approach and to contribute a constructive and challenging perspective to Board discussions.
- Dr S Lyster (appointed in 2006). Dr Lyster has no prior connections with the Group or its shareholders. He is a very experienced director, with particular expertise in wildlife, conservation and environmental matters, which are central to the Company's work. He lives in the Company's Essex and Suffolk supply area. The Board is satisfied that Dr Lyster continues to demonstrate a fully independent approach and to offer valuable constructive challenge.
- M Fay (appointed in 2010). Mrs Fay has no prior connection with the Group or its subsidiaries. She is a very experienced Director, with very strong connections to customers in the Company's north-eastern service area, where she has lived throughout her life. The Board is satisfied that she continues to demonstrate a fully independent approach and to constructively challenge and bring fresh and innovative perspectives to Board discussions.
- P Rew (appointed in 2010). Mr Rew has no prior connections with the Group or its shareholders. He brings expertise in finance, risk, corporate governance and compliance and has very significant experience as an audit committee chairman in substantial and complex organisations. The Board is satisfied that Mr Rew continues to demonstrate a fully independent approach and to offer constructive challenge.

All four INEDs were appointed under the auspices of NWL's Nomination Committee while NWGL (then Northumbrian Water Group plc) was a separately-listed company with no relationship with the current shareholders.

As part of her recent review of the effectiveness of the Board and its Committees and Sub-committees (as detailed on **page 72**), Professor Michelon paid particular attention to the independence of the INEDs. She addressed this issue with the other members of the Board and, in interviewing the INEDs, specifically assessed their independence. This enabled her to conclude that "all four INEDs still demonstrate the required level of independence to continue to perform their roles effectively". She stated that "they are very experienced and mature people, who have the strength of character and ethical core to enable them to speak out at Board meetings and put their views across clearly. They also display a very helpful and healthy degree of scepticism and independent mindedness and I am confident that they can be relied on to protect the interests of the Company and all its stakeholders." In her view, the INEDs have a sophisticated understanding of the work of NWL, the needs and aspirations of its customers and the complex and challenging political and regulatory arena in which it operates. As such, the value of this understanding should not be underestimated.

B.1.2: The Board comprises a Chairman and four further NEDs appointed by the Group's shareholders, four INEDs and three Executive Directors (including the CEO). As explained in the Chairman's Statement, SINED's Report and Corporate Governance obligations section on **pages 67 to 68**, the Board considers that this is an appropriate balance in the context of a private company with a single ultimate controlling shareholder.

B.2.1, B.2.2 and B.2.4: The Nomination Committee met on 22 January 2019. The Company has confirmed (in its governance document) that any new INEDs and Executive Directors will be appointed on an objective basis and by means of a formal, rigorous and transparent procedure, in which all NEDs will participate. Moreover, the Board has agreed to ensure that the recruitment process for INEDs is such that a diverse range of suitably qualified candidates is encouraged to apply.

The CEO has kept the Board informed of the extensive work being done within the Company in relation to diversity.

B.4: INEDs receive induction on joining the Board and continually update their knowledge of, and familiarity with, the Company. The Chairman does not formally review with each Director their training and development needs. For Executive Directors this is managed by the CEO and INEDs keep up to date with developments in the sector via briefings and updates at Board meetings and external seminars and meetings.

B.6: The Company has conducted an externally-facilitated review of the Board's performance and that of the Committees and Sub-committees and the findings will be reviewed at the Board meeting in July 2019. The feedback from the review was again positive and no material concerns were raised. The performance of Executive Directors is appraised by the CEO and all Executive Directors participate in NWL's extensive 360° feedback system.

The Board rigorously reviews the contributions of any Directors whose appointments are extended beyond a term of six years.

B.7: Annual re-election by shareholders is not considered to be appropriate in the case of a privately-owned company.

C.3.1: The AC comprises three INEDs and one NED. This is considered to be appropriate in the context of a private company with a single ultimate controlling shareholder. The Committee ensures that high standards of governance and good practice are maintained.

D.1: The Company's policy on remuneration and the detailed remuneration disclosures are set out in the Remuneration Committee Report on **pages 82 to 93**.

D.2.1: The Remuneration Committee is chaired by A J Hunter, the shareholder-appointed Chairman of the Board. Although this is not compliant with the 2019 Ofwat Objectives, it is considered to be appropriate in the context of a private company with a single ultimate controlling shareholder. In this ownership model the shareholders are not exposed to the risk of the Committee agreeing to unduly generous remuneration packages for executive directors. The other members of the Committee are P Rew, M Fay and Dr S Lyster (all INEDs) and D N Macrae (NED), meaning that there is a majority of INEDs in accordance with the 2014 Ofwat Principles.

E.1: The Chairman was appointed by CK Infrastructure Holdings Limited, which is a significant, indirect shareholder in NWL. He is therefore well placed to convey to the Board the shareholders' views when required. The NEDs regularly meet representatives of the ultimate controlling shareholder and therefore have every opportunity to understand their views.

E.2: As a private company with a single ultimate controlling shareholder, the Company does not consider it necessary to hold annual general meetings.

Recent revisions to the UK CGC and other corporate governance provisions

As the Chairman mentions in his introduction to this Report (on **pages 60 and 61**), the Board is fully aware of the recent changes to the UK CGC and other corporate governance provisions and disclosure requirements. The proposals are generally consistent with the Company's existing processes, purpose, culture and approach and the Company therefore expects to confirm a high level of compliance when it reports against the new provisions in 2020.

NORTHUMBRIAN WATER LIMITED BOARD GOVERNANCE CODE

In March 2014, following discussions with Ofwat, the Board put in place a bespoke Governance Code (the NWL Code), which is available on the NWL website. The Company follows the NWL Code.

CODE OF CONDUCT

The Group has a code of conduct, 'Our Way at NWG', covering its relationships with customers, employees, suppliers, local communities, shareholders, other investors and regulators. This document provides clear guidance to employees in relation to personal conduct, conflicts of interest and a number of other matters. As part of the annual staff appraisal system, all employees are required to confirm that they have seen the code of conduct.

REMUNERATION COMMITTEE REPORT

The following report has been produced in accordance with section 35A of the Water Industry Act 1991. It also has regard to the requirements of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 in respect of directors' remuneration reporting for quoted companies, albeit in the context of a company which is not a listed public limited company.

ANNUAL STATEMENT

The work of the Remuneration Committee comprises the adoption of principles and standards in relation to executive remuneration and benefits, as well as agreeing individual remuneration packages. All decisions regarding Directors' remuneration are taken by the Remuneration Committee, other than where stated.

Members of the Remuneration Committee

The members of the Remuneration Committee during the year were A J Hunter (Chairman), P Rew, M Fay, Dr S Lyster and D N Macrae. H Mottram attends Committee meetings but does not participate in discussions relating to her own remuneration. There is a majority of INEDs in accordance with the Ofwat Principles.

Please see the explanation in respect of the chairmanship of the Remuneration Committee provided on **page 80**, in commenting on compliance with Provision D.2.1 of the UK CGC.

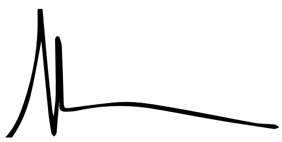
The work of the Remuneration Committee

The Remuneration Committee met once during the year in January 2019. All members attended the meeting. No substantial changes were made to the directors' remuneration policy, or individual Directors' remuneration, during the year. Set out below is a brief summary of the work of the Committee:

- reviewing Executive pay and Non-Executive Directors' fees, taking account of market data, and agreed annual pay awards to take effect from 1 January 2019;
- considering an assurance report from the Internal Audit Manager on performance against targets reflected in incentive recommendations for the 2018 Short Term Incentive Plan (STIP) and Long Term Incentive Plan (LTIP);
- agreeing STIP payments for the 2018 calendar year;
- agreeing the level at which the LTIP award in respect of the 2018 calendar year would vest;
- setting performance targets for the STIP for Executive Directors and senior managers for the 2019 calendar year; and
- setting performance targets for the LTIP scheme for the award in respect of the 2019 calendar year.

The Committee also considered a report on forthcoming changes to corporate governance guidance in respect of executive remuneration.

Subsequent to 31 March 2019, the Committee met in May 2019 to discuss and agree changes to the structures of the STIP and LTIP, to take effect from 2020. The changes are described in more detail on **page 93,** but serve the purpose of further increasing the proportion of performance-related executive pay which is aligned to delivering benefits for our customers.



A J Hunter
Chairman of the Remuneration Committee

DIRECTORS' REMUNERATION POLICY

The policy of the Remuneration Committee is to pay no more than necessary to attract and retain good quality directors, and to ensure that policy is aligned with market practice. For Executive Directors the reward policy is designed to achieve a balance between attraction, reward for performance and retention, and salaries are based on relevant market benchmarks, which are reviewed typically every three years. For Non-Executive Directors, fees paid reflect market practice for similar sized companies, and may be enhanced for roles leading Board Committees.

Executive Directors

The remuneration of the Executive Directors comprises:

- basic salary;
- benefits in kind;
- a performance related STIP;
- annual LTIP awards; and
- pension benefits.

In addition to reviewing each constituent element, the Remuneration Committee reviews the remuneration packages as a whole to ensure that they remain appropriate in terms of structure and quantum. In 2012 the Remuneration Committee restructured the remuneration of the Executive Directors, with advice from Hay Group, independent external reward consultants. This resulted in a reduction in the value of performance related STIP and LTIP awards, offset by an adjustment to basic pay. The Remuneration Committee is satisfied that this balance between fixed and performance related remuneration remains appropriate.

A significant proportion of remuneration is linked to Company performance through the short-term and long-term incentive plans, with 50% of the CEO's maximum remuneration being linked to performance and around 40% for the other Executive Directors, as illustrated on page 86.

The remuneration policy is designed to incentivise performance across all the full range of the Company's strategic themes and not to over-emphasise short-term financial gains. The following table describes the policy in more detail, explaining the purpose of each component, how the policy operates and, for the variable elements of remuneration, the maximum amount payable and how performance is assessed.

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PURPOSE	OPERATION	PERFORMANCE ASSESSMENT	MAXIMUM PAYABLE
Basic salary			
Basic salaries are set at a level to attract and retain Directors with the leadership capabilities to deliver the Company's vision of being the national leader in the provision of sustainable water and wastewater services and to reflect the external market.	Basic salary is reviewed annually based on individual contributions, periodic benchmarking to the external market and with regard to the expected pay award for other groups of employees.	The basic salaries payable to Directors of NWL are not directly linked to specific standards of performance in connection with the carrying out of functions of a 'relevant undertaker'. There is no variable performance related element.	Fixed annual amount determined annually by the Remuneration Committee.
Benefits in kind			
Other employment benefits provided in accordance with the Company's policy on provision of benefits to all staff.	Benefits provided to the Executive Directors comprise car and fuel allowances, healthcare and professional subscriptions.	There is no variable performance related element.	Fixed annual amount set in accordance with the Company's policies on provision of benefits to all staff.
STIP			
The purpose of the STIP is to focus on delivering key business performance targets in the year. The performance targets are firmly linked to NWL's strategic themes (customer, environment, competitiveness, people and communities) as reported in the balanced scorecard. Stretching targets are set which are aligned to the Company's vision of being the national leader in the provision of sustainable water and wastewater services.	The STIP is assessed on a calendar year basis. Awards are paid in cash with no deferral, other than for specific reasons, such as a performance metric not being finalised at the point of award. A clawback applies in the event that results on which the STIP is paid are subsequently found to be inaccurate or there has been relevant misconduct on the part of the employee.	The STIP is structured with three elements, determined by the Remuneration Committee: • up to 50% payable on financial targets; • up to 40% payable on balanced scorecard targets; and • up to 10% payable on performance against personal targets. The Chairman retains the right to award an additional discretionary bonus to the CEO, taking account of overall performance.	The maximum STIP payable, as a percentage of basic salary, is 70% for the CEO and 50% for the other Executive Directors.

table continued...

PURPOSE	OPERATION	PERFORMANCE ASSESSMENT	MAXIMUM PAYABLE
LTIP			
Our LTIP is structured differently from others in the sector and is designed to operate as a modest retention mechanism only.	The LTIP is a cash based award, with deferred payment. Vesting of the LTIP is based on performance in the first calendar year after award. Payment is deferred until the completion of four years from the start of the performance period.	The LTIP is structured with 50% related to delivery of expected distributions to Group shareholders in line with the Board approved plan and 50% related to achievement of the Group profit after tax target. For each element, there will be no vesting if less than 97.5% of the target value is achieved, increasing on a sliding scale to 50% vesting if 100% of the target is achieved and 100% vesting if 105% of the target is achieved.	The maximum LTIP payable, as a percentage of basic salary, is 50% for the CEO and 30% for the other Executive Directors.
Pension			
Pension benefits are provided at a level to reflect market expectations.	The Company operates the Northumbrian Water Pension Scheme (NWPS or the Scheme) which has defined benefit and defined contribution sections. The defined benefit section closed to new entrants on 31 December 2007. More details of the NWPS are provided in note 23 of the Financial Statements.	There is no variable performance related element.	H Mottram left the NWPS in 2016 and receives additional salary payments in lieu of pension contributions. C I Johns participates in the defined contribution section of the NWPS, making an employee contribution of 8% of basic salary (under a salary sacrifice arrangement) and receiving an employer contribution of 15% of salary, up to the annual pension contribution taxation limit, and additional salary payments in lieu of pension contributions. A C Jones participates in a defined benefit section, making an employee contribution of 8% of pensionable salary (under a salary sacrifice arrangement) and receiving an employer contribution equivalent to 25.5% of pensionable salary. Benefits are calculated on a career average revalued earnings basis with future accrual at 1/45th of salary per annum.

ILLUSTRATION OF REMUNERATION POLICY

The graphs below show for each Executive Director, for the proportion of their remuneration borne by the Company:

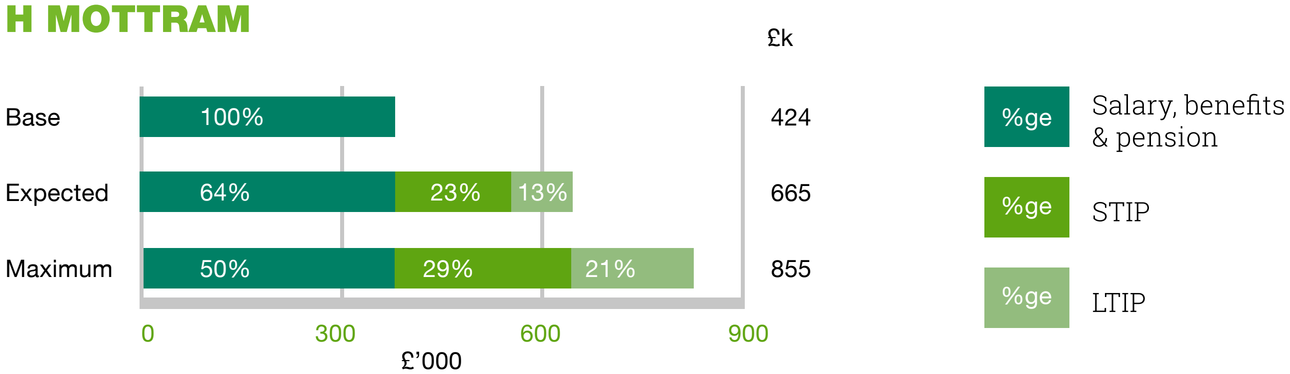
- the base level of remuneration, which is not dependent upon performance and comprises basic salary, benefits in kind and pension;
- the expected level of remuneration, reflecting a typical level of performance against targets for the STIP and LTIP; and
- the maximum level of remuneration, if all STIP and LTIP performance targets were fully achieved.

For H Mottram, 50% of maximum remuneration is linked to Company performance through the STIP and LTIP. For C I Johns and A C Jones, the equivalent proportions are 40%.

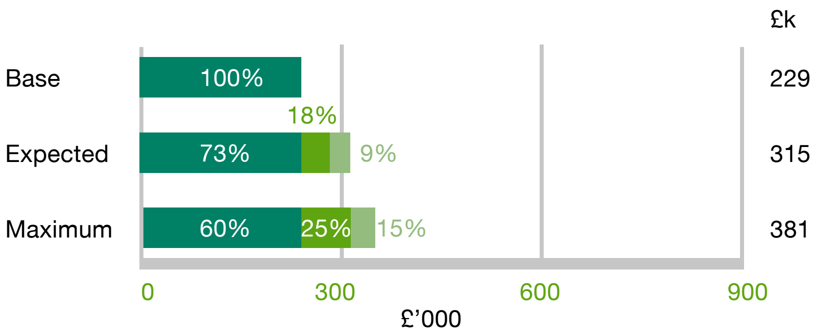
For the purposes of the graph, the expected level of performance for the STIP has been assumed to achieve 60% of the maximum potential value and the LTIP has been assumed to achieve 50% of the maximum value, though awards are dependent upon actual performance.

Information on actual awards for the STIP and LTIP in respect of 2018 is provided on **page 90**.

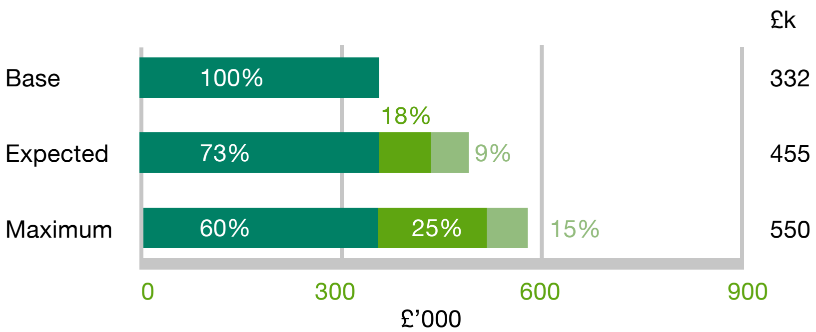
H MOTTRAM



C I JOHNS



A C JONES



NON-EXECUTIVE DIRECTORS

FEES	OTHER COMPONENTS OF REMUNERATION	REMUNERATION ELSEWHERE IN THE GROUP
The Company's policy is that the Independent Non-Executive Directors receive fees for their duties. The level of fees is set by reference to the market. An additional fee is paid to the Chair of the Audit Committee to reflect the additional responsibilities and time commitment involved.	The Non-Executive Directors do not receive benefits in kind and do not participate in the STIP, LTIP or pension schemes operated by the Company.	The INEDs do not receive any other remuneration from the Company, the Group or its shareholders. In respect of the Non-Executive Directors appointed by the Group's shareholders, F R Frame receives the same base fee for performing his duties as a Director of both the Company and NWGL. This fee is shared with NWL paying a 30% proportion and NWGL paying the remaining 70%. The other Non-Executive Directors receive no remuneration from the Company.

SERVICE CONTRACTS

The service contracts of Executive Directors have a notice period of 12 months from either side.

The contracts do not contain any specific provisions related to payment for loss of office. Any such payments would be at the discretion of the Remuneration Committee and would take account of the contractual notice period and any STIP payments considered to have been earned. LTIP awards will typically lapse, although the Remuneration Committee may approve payment of outstanding LTIP awards if a Director is considered to be a 'good leaver', for example upon retirement.

INEDs and F R Frame are engaged on a contract for services with a notice period of 6 months from either side. No payment is made for loss of office other than accrued fees.

The other Non-Executive Directors do not have service contracts with the Company, and receive no payment from the Company.

APPROACH TO REMUNERATION ON RECRUITMENT

Newly appointed Directors are remunerated in accordance with the policy set out in this report.

CONSIDERATION OF SHAREHOLDER VIEWS

The Remuneration Committee comprises two shareholder-appointed Directors and three INEDs. In the context of a private company with a single ultimate controlling shareholder, this ensures that the views of the shareholder are taken into account when setting executive remuneration, whilst also maintaining a strong independent presence on the Committee.

CONSIDERATION OF EMPLOYMENT CONDITIONS ELSEWHERE IN THE COMPANY

The Remuneration Committee reviews Directors' pay on an annual basis, taking account of market trend information and pay awards for the wider workforce in the Company. Whilst Directors' remuneration is not specifically consulted on with employees, in general, annual pay awards for Directors reflect the target pay awards for the workforce, which are subject to consultation under the Company's Employee Relations Framework. The incentive pay arrangements for executives are not mirrored elsewhere, but are considered to be relatively modest in comparison with market comparisons.

Directors' remuneration packages are benchmarked against market data on a periodic basis, typically every three years, with support from external advisers. The salary benchmarking is reviewed annually for senior managers and every three years for the wider workforce.

DIRECTORS' REMUNERATION IN 2018/19 (AUDITED)

The table below shows the total remuneration paid by the Company to Directors during the year, along with comparative information for the previous year. The table has been produced in accordance with the requirements of Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013.

	SALARIES AND FEES £'000		BENEFITS IN KIND £'000		STIP £'000		LTIP £'000		PENSION £'000		TOTAL REMUNERATION £'000	
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
H Mottram*	366	358	9	10	192	217	44	43	40	39	651	667
C I Johns*	189	183	10	10	47	76	14	14	25	25	285	308
A C Jones	276	270	19	22	67	109	20	20	26	30	408	451
M Fay	47	46		-		-		-		-	47	46
F R Frame*	14	14		-		-		-		-	14	14
Dr S Lyster	47	46		-		-		-		-	47	46
M A B Nègre	47	46		-		-		-		-	47	46
P Rew	62	61		-		-		-		-	62	61
	1,048	**1,024**	**38**	**42**	**306**	**402**	**78**	**77**	**91**	**94**	**1,561**	**1,639**

*The table shows only the proportion of remuneration borne by the Company. For two of the Directors, H Mottram and C I Johns, NWL pays 70% of their remuneration and NWGL pays the remaining 30%. For F R Frame, NWL pays 30% of his remuneration and NWGL pays the remaining 70%. For the other Directors reported in the table, NWL pays 100% of their remuneration.

H Mottram and C I Johns receive salary payments in lieu of employer pension contributions. These payments are reported under the pension heading in the table.

BASIC SALARY

Basic salary is set by reference to market data and trends.

For the calendar year 2018, senior executives were awarded an annual increase in their basic salaries of 2.4%, which compared to a 2.9% general increase to most employees.

For the calendar year 2019, senior executives were awarded an annual increase in their basic salaries of 2.5%. This was the same as the level awarded to other senior managers but less than that awarded to other employees of 2.8%.

BENEFITS

Taxable benefits provided to the Executive Directors comprise car and fuel allowance, healthcare and professional subscriptions. The values are not significant in the context of overall remuneration.

STIP

The STIP for the 2018 calendar year was structured by the Committee in accordance with the policy outlined above, as follows:

- up to 50% payable on balanced scorecard financial targets;
- up to 40% payable on balanced scorecard non-financial targets; and
- up to 10% payable on performance against personal targets.

The balanced scorecard measures and targets, and performance against the targets in the year, are shown in the table below. These targets are internal measures set at stretching levels so as to drive year on year performance improvements on a path to deliver our 'national leader' vision. This means that they are often more stretching than the regulatory PCs reported in the Performance Review section on pages 18 and 19.

SCORECARD MEASURE	TARGET	PERFORMANCE	ACHIEVED	% OF TOTAL AWARDED	% OF TOTAL STIP POTENTIAL
Customer					
Customer satisfaction					
- SIM qualitative score	>=4.65	4.48	no	-	3
- SIM quantitative score	<=85	75.25	yes	1	1
Water supply interruptions >3 hours (average minutes per property)	<=3:50	5:23	no	-	4
Mean zonal compliance	>=99.97	99.95	no	-	4
Repeat sewer flooding (properties)	<=71	38	yes	4	4
Environment					
Leakage (Mld)					
- NW	<=133	137	no	-	2
- ESW	<=60	66	no	-	2
Pollution incidents category 1 & 2	<=1	1	yes	4	4
Sewage treatment works failing consent	0	0	yes	4	4
Competitiveness					
Group Earnings Before Interest and Taxes (EBIT)	budget	not achieved	no	-	25
Group cash available for distribution	budget	achieved	yes	25	25
People					
Employee engagement score	2*	One to watch	no	-	4
Lost time reportable accidents (no.)	<=3	7	no	-	4
Communities					
Ethisphere	award	awarded	yes	4	4
Total STIP related to balanced scorecard				**42**	**90**

The personal targets related to the delivery of strategic objectives relevant to each Director's role.

A number of these targets related to NWL's performance as a relevant undertaker. In assessing overall performance, the Committee takes into account the Company's position in Ofwat reports.

For the CEO, in addition to the STIP calculation explained above, a further discretionary award was made by the Committee to reflect the Board's continued satisfaction with the CEO's performance. This remained within the limit of the overall potential maximum STIP award.

The total STIP awards for 2018 were as follows:

	STIP awarded (out of 100%)	MAXIMUM STIP (% OF BASIC SALARY)	STIP AWARDED (% OF BASIC SALARY)
H Mottram	78.2%	70%	54.8%
C I Johns	50.0%	50%	25.0%
A C Jones	50.0%	50%	25.0%

LTIP

A cash LTIP was awarded by the Committee in 2018, structured in accordance with the policy outlined above, as follows:

- up to 50% payable on achievement of the Group profit after tax target; and
- up to 50% payable on delivery of expected distributions to Group shareholders.

The scheme related to the period January 2018 to December 2021. Performance targets were assessed in the first year of the scheme with payment deferred until early 2022, after the end of the four year scheme period.

The Committee assessed the performance against the scheme criteria in January 2019. In respect of Group profit performance zero vested and for Group distributions 25% of the 50% available vested.

The Committee therefore approved that the 2018 LTIP should vest at 25%. This is not dependent upon any future performance conditions being met.

The total LTIP awards for 2018 were as follows:

	LTIP awarded (out of 100%)	MAXIMUM LTIP (% OF BASIC SALARY)	LTIP AWARDED (% OF BASIC SALARY)
H Mottram	25%	50%	12.5%
C I Johns	25%	30%	7.5%
A C Jones	25%	30%	7.5%

PENSION

Pension arrangements operated in accordance with the policy outlined on page 85.

A C Jones is a member of the defined benefit section of the NWPS, therefore the pension value shown in the table on page 88 has been calculated in accordance with the 2013 Regulations and represents the estimated increase in the capital value of his pension in the year.

PERCENTAGE CHANGE IN CEO REMUNERATION

The table below shows the change in remuneration for 2018/19 compared to 2017/18 for the CEO and for other employees. In order to make a meaningful comparison, other employees includes only those who have been employed for the full two year period and excludes senior management whose remuneration is set by the Remuneration Committee. STIP has been compared to the annual bonus paid to the senior management cohort.

	CHANGE IN CEO REMUNERATION	CHANGE IN OTHER EMPLOYEES' REMUNERATION
Salaries and fees	2.2%	4.2%
Benefits in kind	(8.7%)	3.8%
STIP / annual bonus	(11.3%)	23.0%

CEO PAY RATIO

The Companies (Miscellaneous Reporting) Regulations 2018 introduced new legislation is respect of reporting ratio of CEO pay compared to other employees. The table below shows this information produced in accordance with the legislation.

YEAR	METHOD	25TH PERCENTILE RATIO	MEDIAN PAY RATIO	75TH PERCENTILE RATIO
2019	Option A	22:1	17:1	14:1

The Company has chosen Option A (as set out in the said Regulations) for calculating the pay ratio on the basis that it represents the most complete data set. The employees representing each of the percentiles were based on the full year remuneration of staff employed throughout the year. The pension cost for those employees in the defined benefit section of the pension scheme have been calculated based on the estimated employer contributions as applying the method set out in section 229 of the Finance Act 2004 for all members would not be practical. Under Option A, the value of the full-year renumeration of each relevant employee is listed in order from lowest to highest and the values at the 25th, 50th and 75th percentile points identified.

£000	25TH PERCENTILE EMPLOYEE	MEDIAN PAY EMPLOYEE	75TH PERCENTILE EMPLOYEE
Salary component of pay and benefits	25	33	42
Total pay and benefits	29	38	48

CEO REMUNERATION OVER TIME

Since the current remuneration policy was put in place in 2012, the basic salary of the CEO has increased by the same, or less than, the average pay award for the majority of employees each year, which has been targeted to ensure we keep pace with the general cost of living. Over the same period, the maximum potential bonus available under the STIP and LTIP has remained a constant proportion of salary and the actual bonuses awarded have increased year on year by less than 2%.

RELATIVE IMPORTANCE OF SPEND ON PAY

The table below shows total staff costs and dividends paid for the current and prior years, and the year on year change.

	2019	2018	CHANGE
Staff costs (note 6)	144.7	137.2	5.5%
Dividends (note 9)	130.0	125.4	3.7%

STIP

The balanced scorecard targets for 2019/20 are shown in the table below. These are internal measures set at stretching levels so as to drive year on year performance improvements on a path to deliver our 'national leader' vision. This means that they are often more stretching than the regulatory PCs reported in the Performance Review section on pages 18 to 19.

SCORECARD MEASURE	TARGET	%OF TOTAL STIP POTENTIAL
Customer		
Customer satisfaction[1]		
- SIM qualitative score	>=4.65	3
- SIM quantitative score	<=75	1
Water supply interruptions >3 hours (average minutes per property) [1]	<=3.45	4
Mean zonal compliance	>=99.97	4
Repeat sewer flooding (properties)	<=60	4
Environment		
Leakage (Mld)[1]		
- NW	<=134	2
- ESW	<=66	2
Pollution incidents category 1 & 2	<=1	4
Discharge permit compliance (EPA)	>=99%	4
Competitiveness		
Group EBIT	budget	25
Group cash available for distribution	budget	25
People		
Employee engagement score	80	4
Lost time reportable accidents (no.) [1]	<=3	4
Communities		
BITC Platinum Plus/Ethisphere/CCW 'Most Trusted Water Company'	Award	4
Personal targets		10

[1] Where stretching targets are set which are designed to achieve industry leading performance, the Remuneration Committee has agreed that if the target score is not achieved but actual performance is at an industry leading level and has shown an improvement on prior year performance, the target will be deemed to have been achieved.

Personal targets have been set which relate to the delivery of strategic objectives relevant to each Director's role.

CHANGES TO FUTURE REMUNERATION POLICY

At its meeting in May 2019, the Remuneration Committee agreed to revise the structures of the STIP and LTIP, taking effect from 2020, to increase the proportion of performance-related executive pay which is aligned to delivering benefits for our customers.

For the STIP the 10% proportion related to personal targets will be removed and the proportion linked to non-financial balanced scorecard measures will increase to 50%. The Remuneration Committee will review the structure annually and may choose to revise the individual measures within the STIP to reflect appropriate performance objectives but the 50% weighting for customer-focused measures will not be reduced.

For the LTIP, the 50% related to Group profit after tax will be replaced by 50% related to Return on Regulated Equity (RoRE). This is a measure which takes account of performance on customer service, outcome delivery incentives and totex, which drive benefits for customers.

DIRECTORS' REPORT

DIRECTORS

The Directors who served during the year, and to the date of signing, are listed on pages 64 to 66 of the Governance Report.

DISCLOSURES PROVIDED IN THE STRATEGIC REPORT

Future developments which may impact on the Company are described in the CEO's Report and in the Strategic Report.

Our approach to innovation is described in the Performance Review section of our Strategic Report under the Competitiveness heading and the costs of research and development are disclosed in note 4 of the Financial Statements.

Our policies in respect of the employment of disabled persons and employee involvement are set out in the Performance Review section of our Strategic Report under Diversity and Equal opportunities on page 41.

Information on results and dividends and capital structure and equity are contained in the Financial Performance and Structure section of the Strategic Report. Our policies in relation to the use of financial instruments and treasury operations are set out in the same section under the 'Treasury policies' heading.

POLITICAL DONATIONS

NWL does not support any political party and we do not, directly or through any subsidiary, make what are commonly regarded as donations to any political party or other political organisation. However, the wide definition of donations in the Political Parties, Elections and Referendums Act 2000 covers activities which form part of the necessary relationship between the Company and political parties and political organisations. These activities include attending party conferences, as these provide the best opportunity to meet a range of stakeholders, both national and local, to explain our activities, as well as local meetings with MPs, MEPs and their agents. During the year, no external costs were associated with these activities, however, Company representatives attended the party conferences of the Labour and Conservative parties.

GREENHOUSE GAS EMISSIONS

We set out our carbon management plan in 2009 with the aim of reducing our GHG emissions by 35% by 2020 against a 2008 baseline. We have now achieved this target, with total net operational GHG emissions for the year ended 31 March 2019 reducing to 148.2 ktonnes CO2e (31 March 2018: 163.5 ktonnes CO2e), less than half the figure of 303 ktonnes CO2e in 2008 reported on a consistent basis.

The protocol that we use for measuring our emissions is based on the Carbon Accounting Workbook developed and updated annually by the consultants Ricardo, on behalf of the water industry, and published by UK Water Industry Research. This is founded on international and Defra protocols but includes additions that are specific to the water industry.

A change in the international protocols on emissions reporting in 2015 allows companies use an emissions factor that is specific to the source of the energy they use. This is to provide a greater incentive to buy cleaner power. From April 2018, all our electricity has been purchased from Ørsted and originates from offshore wind farms with zero associated emissions. Applying the new protocols would mean that our emissions in the year fall to 44 ktonnes CO2e, a reduction of over 85% since 2008.

In addition to absolute emissions we also monitor the emissions intensity of our operations using three measures, one relating to the water service and two for wastewater. Two of these measures have shown a significant decrease compared to the prior year with the other showing only a marginal increase. These measures can be volatile depending upon levels of rainfall and pumping requirements.

ANNUAL OPERATIONAL GHG INTENSITY RATIO	2018/19	2017/18
Emissions/Ml of water	163	193
Emissions/Ml of sewage treated (flow to full treatment)	208	205
Emissions/Ml of sewage treated (water distribution input)	361	390

Figures in kgCO_2e/Ml

In February 2019, NWL agreed the UK's first offshore wind Corporate Power Purchase Agreement with Ørsted. The ground-breaking deal sees NWL take a third of its electricity directly from the Race Bank offshore wind farm. The move supports NWL's industry-leading commitment to be Carbon Neutral by 2027, building upon its existing solar, hydro, and biogas operations.

DIRECTORS' INDEMNIFICATION

The Company has maintained Directors' and Officers' ('D&O') insurance cover throughout the year to 31 March 2019, provided under group-wide D&O insurance placed by CKHH, the Company's ultimate parent company and controlling shareholder.

On 21 March 2017 NWGL entered into a deed of indemnity to grant the Directors of NWGL and its subsidiaries further protection against liability to third parties, subject to the conditions set out in the Companies Act 2006, and this remains in place.

DIRECTORS' STATEMENT

As required under s418 of the Companies Act 2006, so far as each current Director is aware, there is no relevant audit information of which the Company's auditor is unaware and each Director has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

AUDITOR

Pursuant to s487 of the Companies Act 2006, Deloitte LLP is deemed to be re-appointed as the Company's auditor for the ensuing year.

FINANCIAL STATEMENTS PREPARATION AND GOING CONCERN

The Directors confirm that, in their opinion, the Company has sufficient financial resources and facilities available to enable it to carry out its activities for at least the next 12 months. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Financial Statements. In arriving at their decision, the Directors have taken into account:

- the financial strength of the Company at the balance sheet date and financial performance, which is in line with expectations and reviewed at each Board meeting, most recently in July 2019;
- the key financial ratios over the next 12 month planning horizon, as reflected in strong investment grade credit ratings;
- the fact that the Company has in place £450m of five year committed bank facilities as back up liquidity (maturing in 2023), of which £440m was undrawn at 31 March 2019; and
- the Company's formal governance and risk management arrangements which are monitored by the Audit Committee, Risk & Compliance Sub-committee and Board.

VIABILITY STATEMENT

The Directors believe that the Company is well placed to manage its business risks and expect that the business can continue to operate effectively and meet its financial obligations over the six years to March 2025, and over the long term beyond this time horizon. In arriving at their opinion, the Directors have taken into account:

- the Licence which is in place on a rolling 25 year basis;
- the certainty on wholesale and household retail price controls to March 2020 provided by the 2014 FD by Ofwat, following its acceptance by the Board;
- the financial strength of the Company at the balance sheet date and the fact that the Company has a £450m five year committed bank facility as back up liquidity (maturing in 2023), of which £440m was undrawn at 31 March 2019;
- the Company's draft business plan for the next price control period from 2020-25;
- the key financial ratios over the planning horizon of the Company's medium-term plan (MTP) to March 2025 as reflected in investment grade credit ratings;
- the Board's flexible dividend policy; and
- the principal risks and uncertainties facing the Company and the mitigating controls, as described on pages 54 to 58, which are monitored by the Audit Committee, Risk & Compliance Sub-committee and Board.

The Directors have chosen a period of six years to March 2025 to assess the viability of the Company to align with the business planning process for the regulatory price review period to March 2025. Whilst the Directors do not believe that it is possible to test financial resilience beyond March 2025 to the same level of robust detail, given uncertainty of revenue and returns past this point, they have performed a higher level assessment of viability beyond six years and are confident that the business will continue to operate effectively and remain financially resilient in the long term.

The MTP has been stress tested under a number of plausible and severe adverse scenarios. The scenarios were selected by the Board after considering the principal risk and uncertainties facing the Company, as set out on **pages 54 to 58** of the Strategic Report, and the key economic and financial variables which could impact on the MTP. The combined impact of multiple scenarios has also been tested.

The stress tests were assessed in the context of NWL's overarching financial objective of maintaining prudent investment grade credit ratings from S&P and Moody's. Whilst the viability statement relates specifically to NWL, both rating agencies take account of NWGL metrics in their methodologies, therefore, the impact on both NWL and NWGL financial plans have been considered.

The scenarios tested were:

- lower RPI and CPIH inflation, leading to reduced allowed revenue and RCV and therefore gearing;
- increased future borrowing rates for new and refinanced debt, increasing interest charges and reducing interest cover metrics;
- prolonged closure of the credit markets in response to uncertainty caused by Brexit, resulting in an inability to raise finance;
- increased current tax payments resulting from increased tax rates in the event of a change in government, causing increased net debt and gearing;
- increased defined benefit pension scheme deficit and revised schedule of contributions, resulting in increased contribution payments and higher gearing under rating agency methodologies;
- adverse outcome of PR19 compared to MTP assumptions, through a lower cost and revenue allowance or tougher ODI mechansims, increasing gearing through either higher net debt or lower RCV;
- impact of a credit rating downgrade, causing increased borrowing costs and potentially triggering repayment of existing debt and refinancing;
- higher operating and capital investment costs, as a result of not achieving the levels of outperformance targeted in the MTP, causing increased net debt and gearing;
- impact of a major incident crystallising one of the principal risks identified on **pages 54 to 58**, causing a significant cash outflow and increased net debt and gearing; and
- reduced ODI rewards or increased ODI penalties as a result of performance not achieving targeted levels of outperformance, reducing future revenues.

A number of combined scenarios were also tested. These were determined by considering which scenarios were most likely to occur in combination. The combined scenarios tested were:

- adverse economic conditions, comprising reduced indexation, increased borrowing costs and closure of credit markets;
- external impacts, comprising increased tax and pension payments, adverse PR19 outcome and credit rating downgrade; and
- shortfall in operational performance, comprising higher totex, major operational incident and reduced ODI rewards.

To the extent that any of these scenarios, in isolation or combination, would place retention of the Company's investment grade credit rating at risk, the Directors are confident that this could be mitigated by a combination of efficient delivery of our outcomes and performance commitments in the remainder of the current price control period and in the period 2020-25, targeting RORE outperformance in the next price control period by delivering exceptional levels of service and performance for our customers, and by application of the Board's flexible dividend policy.

The Board engaged Deloitte LLP to provide third party assurance, in the form of agreed upon procedures performed on the calculations and stress testing of the plan, to provide independent assurance on the impact of the stress testing scenarios on the MTP.

FAIR, BALANCED AND UNDERSTANDABLE

The Directors consider that the Annual Report and Financial Statements, taken as a whole, is fair, balanced and understandable and provides the information necessary for stakeholders to assess the Company's performance, business model and strategy. In reaching this conclusion, the Board has taken advice from the Audit Committee which has considered the process by which the Annual Report and Financial Statements has been produced as well as reviewing and commenting on the Report.

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 Financial Statements for each financial year. Under that law the Directors have elected to prepare the Financial Statements in accordance with UK Generally Accepted Accounting Practice (UK Accounting Standards and applicable law), including FRS 101 Reduced Disclosure Framework. Under company law the Directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing these Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have 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 which 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 to 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 are responsible for the maintenance and integrity of the corporate and financial information on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board

M Parker,
Company Secretary,
12 July 2019

Registered office
Northumbria House, Abbey Road, Pity Me, Durham, DH1 5FJ

Registered in England and Wales
Registered no: 02366703

FINANCIAL STATEMENTS

INCOME STATEMENT

FOR THE YEAR ENDED 31 MARCH 2019

	NOTE	2019 £'m	2018 £'m
Continuing operations			
Revenue	3	869.1	834.6
Operating costs	4	(530.3)	(495.7)
Operating profit		**338.8**	**338.9**
Finance costs	7	(130.9)	(133.7)
Profit before taxation		**207.9**	**205.2**
Taxation	8(a)	(39.1)	(39.4)
Profit for the year attributable to the shareholder of the Company		**168.8**	**165.8**

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 MARCH 2019

	NOTE	2019 £'m	2018 £'m
Profit for the year		168.8	165.8
Items that will not be reclassified subsequently to profit and loss:			
Actuarial (losses) / gains	23	(20.6)	55.0
Deferred tax related to actuarial losses / (gains)	8(b)	3.5	(10.1)
Items that may be reclassified subsequently to profit and loss:			
Profit on cash flow hedges taken to equity		2.1	11.7
Deferred tax on items charged to equity that may be reclassified	8(b)	(0.4)	(2.3)
Other comprehensive (loss) / income		**(15.4)**	**54.3**
Total comprehensive income for the year attributable to the shareholder of the Company		**153.4**	**220.1**

BALANCE SHEET

AT 31 MARCH 2019 (REGISTERED NUMBER 02366703)

	NOTE	2019 £'m	Restated 2018[1] £'m
Non-current assets			
Intangible assets	10	74.7	67.2
Property, plant and equipment	11	4,452.3	4,318.7
Financial investments	12	160.9	160.9
		4,687.9	**4,546.8**
Current assets			
Inventories	13	3.6	3.0
Trade and other receivables	14	182.9	160.6
Short-term cash deposits		5.0	92.0
Cash and cash equivalents		-	2.2
		191.5	**257.8**
Total assets		**4,879.4**	**4,804.6**
Current liabilities			
Trade and other payables	15	(177.7)	(169.1)
Borrowings	16	(47.2)	(35.7)
Obligations under finance leases	17(a)	(4.0)	(3.0)
Provisions	18	(0.2)	(0.2)
		(229.1)	**(208.0)**
Non-current liabilities			
Borrowings	16	(2,767.4)	(2,774.4)
Obligations under finance leases	17(a)	(56.9)	(56.5)
Provisions	18	(0.9)	(1.1)
Deferred tax liabilities	8(d)	(409.0)	(394.6)
Pension liability	23	(108.5)	(94.3)
Hedging instruments	20	(42.2)	(32.8)
Other payables		-	(0.6)
Grants and deferred income	19	(490.3)	(549.4)
		(3,875.2)	**(3,903.7)**
Total liabilities		**(4,104.3)**	**(4,111.7)**
Net assets		**775.1**	**692.9**
Capital and Reserves			
Share capital	21	122.7	122.7
Cash flow hedge reserve		(9.9)	(11.6)
Profit and loss account		662.3	581.8
Equity attributable to the shareholder of the Company		**775.1**	**692.9**

[1] The prior year balances have been restated to reflect a reclassification of assets related to computer software as intangible assets, in accordance with IAS 38 Intangible Assets (see note 10).

Approved by the Board of Directors on 12 July 2019 and signed on their behalf by: H Mottram

STRATEGIC REPORT | GOVERNANCE REPORT | STATUTORY FINANCIAL STATEMENTS

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 MARCH 2019

	NOTE	SHARE CAPITAL £'m	CASH FLOW HEDGE RESERVE £'m	RETAINED EARNINGS £'m	TOTAL EQUITY £'m
At 1 April 2017		**122.7**	**(21.0)**	**496.5**	**598.2**
Profit for the year		-	-	165.8	165.8
Other comprehensive income and expense		-	9.4	44.9	54.3
Total comprehensive income and expense for the year		**-**	**9.4**	**210.7**	**220.1**
Dividends	9	-	-	(125.4)	(125.4)
At 31 March 2018		**122.7**	**(11.6)**	**581.8**	**692.9**
Adjustment on initial adoption of IFRS 15		-	-	58.8	58.8
At 1 April 2018		**122.7**	**(11.6)**	**640.6**	**751.7**
Profit for the year		-	-	168.8	168.8
Other comprehensive income and expense		-	1.7	(17.1)	(15.4)
Total comprehensive income and expense for the year		**-**	**1.7**	**151.7**	**153.4**
Dividends	9	-	-	(130.0)	(130.0)
At 31 March 2019		**122.7**	**(9.9)**	**662.3**	**775.1**

Other comprehensive income and expense taken to the cash flow hedge reserve arises from the cumulative amount of gains or losses on hedging instruments, and associated deferred tax, taken directly to equity under the hedge accounting provisions of IAS 39.

Other comprehensive income and expense taken to retained earnings arises from actuarial revaluations, and associated deferred tax, on the Company's defined benefit pension scheme taken directly to equity.

At 1 April 2018 there is an adjustment to retained earnings on adoption of IFRS 15. The Company has elected to apply the standard retrospectively with the cumulative effect of initial application as an opening adjustment to the balance of retained earnings and no prior year re-statement.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2019

1. ACCOUNTING POLICIES

NWL is incorporated in the UK under the Companies Act 2006. The Company is a private company limited by shares and is registered in England and Wales. The address of the Company's registered office is shown on **page 97**. The nature of the Company's operations and its principal activities are set out in the Strategic Report on **page 10**.

These Financial Statements are presented in pounds sterling and all values are rounded to the nearest one hundred thousand pounds (£0.1m) except where otherwise indicated.

These Financial Statements are separate financial statements. The Company is exempt from the preparation and delivery of consolidated financial statements under the terms of Section 400 of the Companies Act 2006, because it is included in the Group Financial Statements of NWGL (see note 25).

(A) BASIS OF ACCOUNTING

These Financial Statements have been prepared in accordance with FRS 101, incorporating the Amendments to FRS 101 issued by the Financial Reporting Council (FRC) in July 2015 and the amendments to Company law made by The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015.

The Company adopted the following new accounting standards in the period:

- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers.

The amended accounting policies are explained below in notes 1(b) Revenue, 1(g) Grants and contributions and 1(n) Derivative financial instruments. The approach adopted to transition to the new standards, and the impact on the Financial Statements, is described in note 1(s).

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available under that standard in relation to financial instruments, presentation of a cash flow statement, standards not yet effective and related party transactions.

The Company has made a prior year adjustment in respect of intangible assets, as disclosed in note 10, but has taken advantage of the disclosure exemption available in FRS 101 to not report a third balance sheet at the start of the preceding period.

The Financial Statements have been prepared under the historical cost convention, with the exception of financial instruments held at fair value through profit and loss.

The Financial Statements have been prepared on a going concern basis, having considered the principal risks and uncertainties, which assumes that the Company will have adequate funding to meet its liabilities as they fall due in the foreseeable future. As at 31 March 2019, the Company had net current liabilities of £37.6m (2018: net current assets of £49.8m). The Directors have reviewed cash flow requirements and are confident that they will be able to meet these from funds available, including the undrawn committed bank facilities of £440m (2018: £350m). Accordingly, the Directors believe it is appropriate to prepare the financial statements on a going concern basis.

(B) REVENUE

Revenue, which excludes Value Added Tax, represents the income receivable in the ordinary course of business for services provided within the UK. The Company adopted IFRS 15 Revenue from Contracts with Customers with effect from 1 April 2018. Under IFRS 15 revenue is recognised as performance obligations to the customer are satisfied.

The Company's principal source of revenue is from water and wastewater charges to customers, which are recognised over the period which the services are provided. For volumetric charges to measured customers, revenue is recognised as the service is supplied. For measured charges which have not yet been billed, an accrual is made based on an estimate of consumption. Wholesale charges for non-household customers are estimated on the basis of market information provided by MOSL. This policy represents no change to the timing of recognition for water and wastewater services upon the adoption of IFRS 15.

1. ACCOUNTING POLICIES (continued)

A secondary source of revenue is contributions to capital investment, particularly from developers.

For contributions related to the connection of new properties to the Company's networks, comprising infrastructure charges, new connection charges, requisitioned mains and sewers and adopted assets, the Company considers that these activities form a combined performance obligation that is not distinct from the ongoing provision of water and wastewater services through the new connection. On this basis, these contributions continue to be recognised as deferred income and amortised to the income statement over the expected useful life of the connection, per note 1(g).

For other contributions to capital investment, most significantly mains and sewer diversions, the Company considers that the performance obligation is satisfied upon completion of the investment, which will typically be the point at which the associated asset is brought into use. On this basis, these contributions are recognised in full in the income statement upon satisfaction of the performance obligation. Contributions received before the performance obligation is satisfied are recorded as receipts in advance.

(C) CASH FLOW STATEMENT

As permitted by FRS 101, the Company has taken advantage of the disclosure exemption available under that standard in relation to presentation of a cash flow statement.

(D) INTANGIBLE ASSETS

Intangible assets, primarily comprising computer software, are recognised at cost less accumulated amortisation and any provision for impairment. Computer software is amortised evenly to its estimated economic life over a period of 2 to 25 years. Software is not amortised until commissioned.

(E) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, including assets in the course of construction, comprise infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls) and other assets (including properties, vehicles and above ground plant and equipment).

Purchased property, plant and equipment are included at cost less accumulated depreciation and any provision for impairment. Cost comprises the aggregate amount incurred and the fair value of any other consideration given to acquire the asset and includes costs directly attributable to making the asset capable of operating as intended.

Where assets are constructed by a developer and adopted by NWL at no cost to the Company, the assets are recognised in the balance sheet at their fair value on the date of the transfer and an equivalent value is recognised in deferred income, in accordance with IFRIC 18 Transfers of Assets from Customers. The fair value is based on the average cost to the Company of constructing an equivalent asset.

Freehold land is not depreciated. Other assets are depreciated evenly over their estimated economic lives, which are principally as follows:

Freehold buildings	30-60 years
Operational structures, plant and machinery	4-92 years
Infrastructure assets (see below)	4-200 years
Fixtures, fittings, tools and equipment	4-25 years

The carrying values of property, plant and equipment are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable and are written down immediately to their recoverable amount. Useful lives and residual values are reviewed annually and, where adjustments are required, these are made prospectively.

Assets in the course of construction are not depreciated until commissioned.

Infrastructure assets

Infrastructure assets comprise a network of systems being mains and sewers, reservoirs, dams and sea outfalls.

Expenditure on infrastructure assets which enhances the asset base is treated as fixed asset additions while maintenance expenditure which does not enhance the asset base is charged as an operating cost.

Infrastructure assets are depreciated evenly to their estimated residual values over their estimated economic lives, which are principally as follows:

Dams and impounding reservoirs	150 years
Water mains	100 years
Sea outfalls	60 years
Sewers	200 years
Dedicated pipelines	4-20 years

1. ACCOUNTING POLICIES (continued)

(F) FINANCIAL INVESTMENTS

Financial investments are stated at their purchase cost, less provision for diminution in value (note 12).

(G) GRANTS AND CONTRIBUTIONS

Grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. Revenue grants are credited to the income statement in the period to which they relate.

Grants and contributions related to the connection of new properties to the Company's networks, comprising infrastructure charges, new connection charges, requisitioned mains and sewers and adopted assets, are recognised as deferred income and amortised to the income statement over the expected useful life of the connection, as explained in note 1(b).

Other grants and contributions to capital investment, most significantly mains and sewer diversions, are recognised in full in the income statement upon satisfaction of the performance obligation to the customer, which is the point at which the associated asset is brought into use. Up to this point, any contributions received are reported as receipts in advance.

(H) HIRE PURCHASE AND LEASING

Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership to the Company, the assets are treated as if they had been purchased at their fair value or, if lower, at the present value of the minimum lease payments. Rentals or leasing payments are treated as comprising a capital element and finance charges, the capital element reducing the outstanding liability and the finance charges being charged to the income statement over the period of the leasing contract at a constant rate on the reducing outstanding liability.

Rentals under operating leases (where the lessor retains a significant proportion of the risks and rewards of ownership) are expensed in the income statement on a straight line basis over the lease term.

(I) INVENTORIES

Inventories are stated at cost less any provision necessary to recognise damage and obsolescence.

(J) PENSION COSTS

The Company is the principal employer of the NWPS, which has both a defined benefit section and a defined contribution section.

The cost of providing benefits under the defined benefit section of the Scheme is determined using the projected unit credit method, which attributes entitlement to benefits to the current period (to determine current service cost) and to the current and prior periods (to determine the present value of defined benefit obligation) and is based on actuarial advice. Past service costs are recognised in the income statement on a straight line basis over the vesting period or immediately if the benefits have vested. When a settlement (eliminating all obligations for benefits already accrued) or a curtailment (reducing future obligations as a result of a material reduction in the scheme membership or a reduction in future entitlement) occurs, the obligation and related plan assets are re-measured using current actuarial assumptions and the resultant gain or loss recognised in the income statement during the period in which the settlement or curtailment occurs. Net interest is calculated by applying the discount rate to the net defined asset or liability.

The service cost is disclosed in manpower costs and the net interest expense is disclosed within finance costs.

Actuarial gains and losses on experience adjustments and changes in actuarial assumptions are recognised in full in the period in which they occur in the statement of comprehensive income.

The costs of the defined contribution section are charged to the income statement in the period they arise.

1. ACCOUNTING POLICIES (continued)

(K) TAXATION

Current tax

Current tax liabilities are measured at the amount expected to be paid to the taxation authorities. The tax rates and tax laws used to compute the amounts are those that are enacted or substantively enacted by the balance sheet date.

Deferred tax

Deferred tax is provided using the liability method on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences except:

- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences and unused tax losses to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and unused tax losses can be utilised except:

- where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted, or substantively enacted, at the balance sheet date.

Deferred tax is recognised in the income statement, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity.

(L) FOREIGN CURRENCY

All transactions denominated in foreign currencies are translated into sterling at the actual rates of exchange ruling at the date of transaction. Foreign currency balances are translated into sterling at the rates of exchange ruling at the balance sheet date. Exchange gains or losses are recognised in the profit and loss account in the period incurred.

(M) RESEARCH AND DEVELOPMENT

Research and development expenditure is charged to the income statement in the period in which it is incurred.

(N) DERIVATIVE FINANCIAL INSTRUMENTS

The Company utilises interest and inflation rate swaps, gilt locks, power forward contracts and forward exchange contracts as derivative financial instruments.

A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the Company in line with the Group's risk management policies. Derivative financial instruments are stated at their fair value.

Hedge accounting is employed in respect of those derivative financial instruments fulfilling the requirements for hedge accounting as prescribed under IFRS 9. The Company has not applied hedge accounting criteria under IFRS 9 on a retrospective basis. Existing derivative financial instruments, if eligible for hedge accounting, continue to apply rhe hedging criteria under the provisions of IAS 39. Any new instruments will apply IFRS 9.

Derivative financial instruments are measured at fair value, which is considered to be the price that would be received to sell an asset or paid to

1. ACCOUNTING POLICIES (continued)

transfer a liability in an orderly transaction reflecting the credit risk of the counterparties in the principal (or most advantageous) market under market conditions as at the balance sheet date.

The fair value of forward exchange contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair value of interest rate swaps and inflation swaps are determined by reference to market values for similar instruments.

Hedging transactions undertaken by the Company are classified as either fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability, or cash flow hedges where they hedge exposure to variability in currency cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecast transaction.

In relation to fair value hedges which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in the income statement.

In relation to cash flow hedges to hedge firm currency commitments which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in the cash flow hedge reserve and the ineffective portion is recognised in the income statement.

When the hedged firm commitment results in the recognition of a non-financial asset or a non-financial liability then, at the time the asset or liability is recognised, the associated gains or losses that had previously been recognised in the cash flow hedge reserve are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability. For all other cash flow hedges, the gains or losses that are recognised in the cash flow hedge reserve are transferred to the income statement in the same periods in which the hedged firm commitment affects the income statement.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the income statement.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in the cash flow hedge reserve is kept in the cash flow hedge reserve until the forecast transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in the cash flow hedge reserve is transferred to the income statement.

(O) INTEREST BEARING LOANS AND BORROWINGS

All loans and borrowings are initially stated at the amount of the net proceeds, being fair value of the consideration received net of issue costs associated with the borrowing. Finance costs (including issue costs) are taken to the income statement over the term of the debt at a constant rate on the balance sheet carrying amount. The carrying amount is increased by the finance charges amortised and reduced by payments made in respect of the accounting period. The carrying amount of index linked borrowings increases annually in line with the relevant RPI, with the accretion being charged to the income statement as finance costs payable. Other borrowing costs are recognised as an expense when incurred.

Realised gains and losses that occur from the early termination of loans and borrowings are taken to the income statement in that period.

Net debt is the sum of all loans and borrowings less cash and cash equivalents, short-term cash deposits, financial investments and loans receivable.

(P) BAD DEBT PROVISIONING

The bad debt provision is calculated by applying a range of percentages to debt of different ages. These percentages also vary between different categories of debt. Higher percentages are applied to those categories of debt which are considered to be of greater risk and also to debt of greater age.

(Q) BORROWING COSTS

Borrowing costs are generally expensed as incurred. Borrowing costs that are directly attributable to the acquisition or construction of an asset that necessarily takes a substantial time to prepare for its intended use are capitalised while the asset is being constructed as part of the cost of that asset.

Capitalisation ceases when the asset is substantially ready for its intended use or sale. If active development is interrupted for an extended period, capitalisation is suspended. When construction occurs piecemeal, and use of each part ceases upon substantial completion of that part, a weighted average cost of borrowings is used.

1. ACCOUNTING POLICIES (continued)

(R) SIGNIFICANT ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the process of applying the accounting policies, the Company is required to make certain judgements, estimates and assumptions that it believes are reasonable based on the information available. Actual results may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

The significant accounting judgements were:

- the estimation of income for measured water and sewerage services supplied but not billed at the end of the financial period. Consumption by measured domestic customers is billed in arrears on quarterly or six-monthly cycles. Revenue is estimated and accrued using a defined methodology based upon historical usage and the relevant tariff per customer. Consumption by non-household properties is billed to the relevant retailer under the terms of the Wholesale Contract and may be either in advance or in arrears. Revenue billed in arrears is estimated by reference to wholesale market settlement reports, adjusted for any additional information obtained after a settlement report has been run;
- the estimation of uncertain tax provisions, which are assessed on advice from independent tax advisers and the status of ongoing discussions with the relevant tax authorities; and
- the asset lives assigned to property, plant and equipment, details of which can be found in note 1(e) above.

The significant accounting estimates were:

- those assumptions used in arriving at the defined benefit pension scheme assets and liabilities under IAS 19. These key assumptions and their possible impact are disclosed in note 23; and
- the bad debt provision, which is determined by estimating expected credit losses based on the Company's historical experience of irrecoverable debts.

(S) TRANSITION TO NEW ACCOUNTING STANDARDS IN THE PERIOD

IFRS 15 Revenue from Contracts with Customers

The Company adopted IFRS 15 with effect from 1 April 2018 and has applied the standard retrospectively with the cumulative effect recognised at the date of initial application. Prior years have not been restated.

The adoption of the standard has had no effect on the timing or amount of revenue recognised in relation to the provision of water and wastewater services to household customers and non-household retailers.

Contributions related to the connection of new properties to the Company's networks, comprising infrastructure charges, new connection charges, requisitioned mains and sewers and adopted assets, continue to be recognised as deferred income and amortised to the income statement over the expected useful life of the connection. However, the amortisation is now reported as revenue rather than as a credit within operating costs.

Other contributions to capital investment, most significantly mains and sewer diversions, are now recognised in full as revenue in the income statement upon satisfaction of the performance obligation. Contributions of this type recognised previously as deferred income in the balance sheet have been reclassified to retained earnings in the opening balance sheet, along with the associated deferred tax.

The transition impact on the opening balance sheet was a reduction in deferred income of £70.8m, an increase in deferred tax liability of £12.0m and a net increase in retained earnings of £58.8m.

In the year to 31 March 2019, £2.4m has been recognised as revenue which would previously have been treated as deferred capital income and amortised over a period of between 4 and 200 years. Sums totalling £9.8m are included within receipts in advance relating to contributions received where the performance obligation has not yet been satisfied. Revenue for the year to 31 March 2019 includes £4.8m which would previously have been classified within operating costs as amortisation of capital grants.

1. ACCOUNTING POLICIES (continued)

IFRS 9 – Financial Instruments

The Company adopted IFRS 9 with effect from 1 April 2018 and has applied the standard retrospectively with the cumulative effect recognised at the date of initial application. Prior years have not been restated.

Adoption of the standard has had no material impact on the Financial Statements in the year.

(T) ACCOUNTING STANDARDS NOT YET ADOPTED

At the balance sheet date, the new accounting standard IFRS 16 Leases was in issue but not yet effective. IFRS 16 will be effective for periods beginning on or after 1 January 2019 and will be applied retrospectively with the cumulative effect of initially applying the standard at the date of initial application. Prior years will not be restated.

This standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. The primary impact will be to reclassify most leases currently classified as operating leases as finance leases, resulting in the recognition of a finance lease obligation and an associated non-current asset.

The Company intends to adopt the practical expedient available under the standard, and not apply the standard to existing contracts not previously identified as containing a lease. However, IFRS 16 will be applied to operating leases disclosed in note 17(b) and new contracts entered into after the date of initial application.

It is anticipated that this will result in the recognition of a finance lease obligation of approximately £3.8m and a corresponding non-current asset of £3.7m, adjusted for prepayments and accruals, with no associated deferred tax impact.

Work is ongoing to ensure that all contractual arrangements falling within scope of the standard are correctly identified. The Company does not anticipate that the adoption of IFRS 16 will have a material impact on the reported profit in the period of initial application.

2. PRIOR YEAR ADJUSTMENT

The Company has reclassified assets related to computer software as intangible assets, in accordance with IAS 38 Intangible Assets. These assets have previously been incorrectly reported within property, plant and equipment. However, upon completion of the significant investment in a new customer contact and billing system, management reviewed the value of computer software and restated these as intangible assets. This change has been applied retrospectively.

In the balance sheet as at 31 March 2018, computer software assets, including assets in the course of construction, with a net book value of £67.2m have been reclassified from property, plant and equipment to intangible assets.

In the balance sheet as at 31 March 2019, computer software assets, including assets in the course of construction, with a net book value of £74.7m have been reclassified from property, plant and equipment to intangible assets.

The movement in intangible assets in the year is disclosed in note 10.

Comparative information has been re-stated in the balance sheet. There was no impact on profits or losses, so no other primary statement was impacted.

3. REVENUE AND SEGMENTAL INFORMATION

The Directors consider that the Company has a single class of business, the provision of water and wastewater services. All revenue is generated from within the United Kingdom.

Appointed business revenue is generated from the regulated activities of the Company, defined in its licence of appointment, necessary to fulfil its duties as a water and sewerage undertaker under the Water Industry Act of 1991.

Non-appointed revenue is generated from the non-regulated activities of the Company.

			2019			2018
	Household £'m	Non Household £'m	Total £'m	Household £'m	Non Household £'m	Total £'m
Wholesale Water	339.4	97.2	436.6	328.3	94.3	422.6
Wholesale Wastewater	237.5	79.2	316.7	226.7	78.1	304.8
Retail	59.6	-	59.6	58.8	-	58.8
	636.5	176.4	812.9	613.8	172.4	786.2
Other appointed business			31.2			20.7
Total appointed business			**844.1**			**806.9**
Non appointed business			25.0			27.7
Total revenue			**869.1**			**834.6**

4. OPERATING COSTS

	2019 £'m	2018 £'m
Materials and consumables	19.9	18.4
Manpower costs (note 6)	144.7	137.2
Own work capitalised	(41.0)	(38.1)
Costs of research and development	0.9	0.7
Operating lease payments	2.4	2.5
Bad debt charge	12.4	9.7
Inventories recognised as an expense	3.4	2.6
Other operating costs	252.5	238.1
Depreciation of property, plant and equipment	129.7	128.2
Amortisation of intangible assets	8.2	7.0
Amortisation of capital grants	-	(6.3)
Profit on disposal of property, plant and equipment	(2.8)	(4.3)
Total operating costs	**530.3**	**495.7**

Auditor's remuneration in respect of the statutory audit of the Financial Statements amounted to £219k (2018: £146k), including fees for a subsidiary, NWF, of £6k (2018: £7k) and fees related to the implementation of new accounting standards and a new customer billing system. Fees of £61k (2018: £68k) were incurred in respect of the APR, including the audit of the Regulatory Accounting Statements, and agreed upon procedures in respect of additional regulatory information, the statement of sufficiency of financial resources and facilities and financial resilience stress testing.

Fees of £158k (2018: £128k) were incurred for non-audit services comprising assurance work in respect of PR19 submissions, other assurance to third parties and consultancy support.

Amortisation of capital grants has been reported within revenue with effect from 1 April 2018 in accordance with IFRS15 Revenue from Contracts with Customers.

5. DIRECTORS' EMOLUMENTS

(a) Directors' remuneration

The remuneration of the Directors of the Company was as follows:

	2019 £'000	2018 £'000
Emoluments (including benefits in kind)	1,565	1,639

For those Directors holding office with both NWL and NWGL, or contributing significantly to the day to day operations of NWGL, costs are apportioned between the companies to reflect the level of activity carried out for each company. This note reflects only the proportion of costs charged to NWL.

One of the Directors at 31 March 2019 was a member of a defined benefit section of the Scheme where the Company makes contributions towards the cost (2018: 1).

One of the Directors at 31 March 2019 was a member of a defined contribution section of the Scheme where the Company makes contributions towards the cost (2018: 1).

The Directors' remuneration policy and a detailed report showing total remuneration for each Director, for the year to 31 March 2019, are set out in the Remuneration Committee Report on pages 82 to 93 of the Governance Report.

(b) Highest paid Director

The amounts for remuneration shown in note 5(a) include the following in respect of the highest paid Director:

	2019 £'000	2018 £'000
Emoluments (including benefits in kind)	651	667

The highest paid Director left the defined contribution section of the NWPS at the beginning of the year ended 31 March 2017, therefore no payments were made to the Scheme in either the current or prior year.

6. EMPLOYEE INFORMATION

The total employment costs of all employees (including Directors) were as follows:

	2019 £'m	2018 £'m
Gross costs charged to the profit and loss account:		
Wages and salaries	81.9	78.1
Social security costs	8.9	8.4
Other pensions costs	18.7	17.7
	109.5	**104.2**
Costs recharged to other Group companies:		
Wages and salaries	2.3	2.2
	2.3	**2.2**
Net costs charged to the profit and loss account:		
Wages and salaries	79.6	75.9
Social security costs	8.9	8.4
Other pensions costs	18.7	17.7
	107.2	**102.0**
Costs charged to capital schemes:		
Wages and salaries	28.4	26.4
Social security costs	3.1	2.9
Other pensions costs	6.0	5.9
	37.5	**35.2**
Total employee costs	**144.7**	**137.2**

The average monthly number of employees during the year was made up as follows:

	2019	2018
Water and waste water services	1,561	1,472
Customer services and meter reading	569	565
Other regulated activities	927	915
Non regulated activities	89	100
	3,146	**3,052**

7. NET FINANCE COSTS

	2019 £'m	2018 £'m
Finance costs payable:		
Bank overdrafts and loans	13.0	15.0
Receivable in respect of derivatives	(4.9)	(2.0)
Payable to subsidiary Group company	85.2	83.4
Payable to other Group company	-	0.1
Amortisation of discount, fees, loan issue costs and other financing items	2.3	1.8
Accretion on index linked bonds	30.2	33.5
Interest cost on pension plan obligations	2.2	3.6
Obligations under finance leases	3.1	2.7
	131.1	**138.1**
Less amounts capitalised on qualifying assets	(8.5)	(6.5)
	122.6	**131.6**
Fair value losses on derivative financial instruments	11.5	4.9
Total finance costs payable	**134.1**	**136.5**
Finance income receivable:		
Bank deposits	(0.3)	(0.5)
Receivable from Group companies	(2.9)	(2.3)
Total finance costs receivable	**(3.2)**	**(2.8)**
Net finance costs payable	**130.9**	**133.7**

8. TAXATION

(a) Tax on profit on ordinary activities

	2019 £'m	2018 £'m
Current tax:		
UK current income tax charge at 19% (2018: 19%)	18.4	17.1
Adjustments in respect of prior periods	(4.1)	9.2
Payable in respect of group relief for the year	16.5	16.0
Adjustments in respect of prior period group relief	2.8	(9.6)
Total current tax	**33.6**	**32.7**
Deferred tax:		
Origination and reversal of temporary differences in the year at 17% (2018: 17%)	4.5	4.9
Adjustments in respect of prior periods	1.0	1.8
Total deferred tax	**5.5**	**6.7**
Tax charge in the income statement	**39.1**	**39.4**

The rate of UK corporation tax for the current year was 19%. The Finance Act 2016 provides that this will be reduced to 17% with effect from 1 April 2020. Deferred tax has been provided wholly at 17% as amounts that are expected to reverse at the higher rate are insignificant.

Tax losses have been provisionally claimed as group relief from other group companies in the current year, for which payment is being made at the full rate of tax.

Net prior year adjustments mainly reflect the benefit of R&D claims submitted during the year.

(b) Tax relating to items charged outside the income statement

	2019 £'m	2018 £'m
Deferred tax:		
Actuarial (losses) / gains on pension scheme	(3.5)	9.4
Adjustment for items expected to reverse at 19%	-	0.7
Financial instruments	0.4	2.0
Adjustment for items expected to reverse at 19%	-	0.3
Tax (credit) / charge in the statement of comprehensive income	**(3.1)**	**12.4**

8. TAXATION (continued)

(c) Reconciliation of the tax charge

	2019 £'m	2018 £'m
Profit on ordinary activities before tax	**207.9**	**205.2**
Profit on ordinary activities multiplied by standard rate of corporation tax of 19% (2018: 19%)	39.5	39.0
Effects of:		
Expenses not deductible for tax purposes	1.1	0.4
Non-taxable gains and amortisation of capital sums	(1.9)	(1.9)
Depreciation in respect of non-qualifying items	1.2	1.1
Adjustment to prior year consortium relief paid for at less than the full rate	-	2.2
Deferred tax movement not at current tax rate for the year	(0.5)	(0.5)
Adjustments in respect of prior periods	(0.3)	(0.9)
Transfer pricing adjustments	(0.8)	(0.8)
Balancing payment payable	0.8	0.8
Total tax charge	**39.1**	**39.4**

The effective rate of tax for the year was 18.8% (2018: 19.2%). The decrease of 0.4% is explained by the absence of any consortium relief adjustments (-1.1%), offset by expenses not deductible for tax purposes (0.3%), prior period adjustments (0.3%) and non-qualifying depreciation (0.1%).

(d) Deferred tax

	ACCELERATED TAX DEPRECIATION £'m	DEFERRED INCOME £'m	RETIREMENT BENEFIT OBLIGATIONS £'m	FAIR VALUE HEDGING INSTRUMENTS £'m	BUSINESS COMBINATIONS £'m	OTHER £'m	TOTAL £'m
At 1 April 2017	**454.8**	**(54.7)**	**(29.3)**	**(7.1)**	**5.6**	**6.2**	**375.5**
Charge/(credit) in the income statement	7.4	(2.6)	1.9	(0.7)	(0.2)	0.9	6.7
Charge in other comprehensive income	-	-	10.1	2.3	-	-	12.4
At 31 March 2018	**462.2**	**(57.3)**	**(17.3)**	**(5.5)**	**5.4**	**7.1**	**394.6**
Adoption of IFRS 15	-	12.0	-	-	-	-	12.0
Charge/(credit) in the income statement	7.1	(2.8)	2.2	(2.1)	(0.1)	1.2	5.5
(Credit)/charge in other comprehensive income	-	-	(3.5)	0.4	-	-	(3.1)
At 31 March 2019	**469.3**	**(48.1)**	**(18.6)**	**(7.2)**	**5.3**	**8.3**	**409.0**

8. TAXATION (continued)

(e) Factors that may affect future tax charges

The future change in the tax rate is referred to in note 8(a) above.

The Company expects to continue to incur high levels of capital expenditure during the remainder of the 2015-20 regulatory review period and in 2020-25 which, under current tax legislation, should result in claims for tax reliefs in excess of depreciation.

9. DIVIDENDS

	2019 £'m	2018 £'m
Equity:		
Dividends paid:		
Special dividend paid for the year ended 31 March 2019 of nil (year ended 31 March 2018: 15.41p) per share on an aggregated basis	-	18.9
Final dividend paid for the year ended 31 March 2018 of 53.00p (year ended 31 March 2017: nil) per share on an aggregated basis	65.0	-
Interim dividend paid for the year ended 31 March 2019 of 53.00p (year ended 31 March 2018: 86.83p) per share on an aggregated basis	65.0	106.5
Total dividends paid in the year	**130.0**	**125.4**
Dividends proposed:		
Final dividend proposed for the year ended 31 March 2019 of 53.00p (year ended 31 March 2018: 53.00p) per share on an aggregated basis	65.0	65.0
Total dividends proposed	**65.0**	**65.0**

In previous years the Company has typically paid two interim dividends in each financial year, in October and March. In 2018, the Directors decided that the second interim dividend payment would be replaced with a final dividend to be paid in April, after the Directors have reviewed the financial position of the Company at the balance sheet date.

A final dividend of £65m for the year ended 31 March 2019 (2018: £65m) was approved by the Board and paid after the balance sheet date.

The Board has a policy which takes into account the principle of incentive based price cap regulation, including operating, investment and financing performance. When declaring dividends, the Directors consider the Company's five-year plan and give due consideration to business performance, the prospects of the Company and the principal risks facing the business.

Specifically, the Board determines the level of dividend declared by reference to:

- the Company's ability to finance its functions;
- the Company's cumulative financial performance and past outperformance; and
- maintaining the Company's investment grade credit ratings.

The Directors also have regard to:

- the Company's operational performance and the level of service provided to its customers; and
- employees' interests and, specifically, compliance with the pension deficit repair plan agreed with the Pension Trustee in respect of the NWPS, as submitted to the Pensions Regulator.

10. INTANGIBLE ASSETS

	SOFTWARE £'m	ASSETS IN DEVELOPMENT £'m	TOTAL £'m
Cost:			
At 1 April 2018	69.5	41.9	111.4
Additions	-	15.7	15.7
Transfers	27.9	(27.9)	-
At 31 March 2019	**97.4**	**29.7**	**127.1**
Amortisation:			
At 1 April 2018	44.2	-	44.2
Charge for the year	8.2	-	8.2
At 31 March 2019	**52.4**	**-**	**52.4**
Carrying value:			
At 31 March 2019	45.0	29.7	74.7
At 31 March 2018	25.3	41.9	67.2

Cumulative borrowing costs capitalised in the cost of intangible assets amount to £4.0m (2018: £2.1m). The capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation was 4.30% (2018: 4.58%).

11. PROPERTY, PLANT AND EQUIPMENT

	FREEHOLD LAND AND BUILDINGS £'m	INFRASTRUCTURE ASSETS £'m	OPERATIONAL STRUCTURES, PLANT AND MACHINERY £'m	FIXTURES, FITTINGS, TOOLS AND EQUIPMENT £'m	ASSETS IN THE COURSE OF CONSTRUCTION £'m	TOTAL £'m
Cost:						
At 1 April 2018 (restated)	154.4	2,781.2	2,941.6	219.1	172.0	6,268.3
Additions	-	12.3	0.3	-	251.2	263.8
Schemes commissioned	3.6	85.8	106.2	4.3	(199.9)	-
Disposals	-	(1.6)	(3.6)	-	-	(5.2)
At 31 March 2019	**158.0**	**2,877.7**	**3,044.5**	**223.4**	**223.3**	**6,526.9**
Depreciation:						
At 1 April 2018 (restated)	59.8	381.7	1,329.5	178.6	-	1,949.6
Charge for the year	3.5	27.7	89.6	8.9	-	129.7
Disposals	-	(1.6)	(3.1)	-	-	(4.7)
At 31 March 2019	**63.3**	**407.8**	**1,416.0**	**187.5**	**-**	**2,074.6**
Carrying value:						
At 31 March 2019	94.7	2,469.9	1,628.5	35.9	223.3	4,452.3
At 31 March 2018 (restated)	94.6	2,399.5	1,612.1	40.5	172.0	4,318.7
Leased assets included above:						
Carrying value:						
At 31 March 2019	-	43.8	11.3	-	-	55.1
At 31 March 2018	-	44.3	10.7	-	-	55.0

Operational structures, plant and machinery include an element of land dedicated to those assets. It is not possible to separately identify the value of all land assets.

Cumulative borrowing costs capitalised in the cost of property, plant and equipment amount to £46.1m (2018: £39.5m). The capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation was 4.30% (2018: 4.58%).

12. FINANCIAL INVESTMENTS

	LOANS TO GROUP COMPANIES £'m
At 1 April 2018 and 31 March 2019	160.9

(a) Loans to Group Companies

In May 2004, the Company made a loan of £159.0m to Northumbrian Services Limited, maturing in January 2034. Following a restructuring of the NWGL group, this loan was reassigned to NWGL in March 2016 at a variable interest rate of LIBOR plus 1% calculated on twice yearly payment dates.

In May 2004, the Company made a loan of £1.5m to Bakethin Holdings Limited, maturing in January 2034. The interest on the loan is capitalised and at 31 March 2019 the balance was £1.9m (2018: £1.9m).

(b) Subsidiaries

The Company's interests in subsidiaries at 31 March 2019 were as follows:

NAME OF UNDERTAKING	COUNTRY OF INCORPORATION OR REGISTRATION AND OPERATION	DESCRIPTION OF SHARES HELD	PROPORTION OF NOMINAL VALUE OF ISSUED SHARES HELD BY COMPANY (%)	BUSINESS ACTIVITY
Northumbrian Water Finance plc	England and Wales	Ordinary shares of £1	100	Holding of finance instruments
Reiver Finance Limited	England and Wales	Ordinary shares of £1	100	Special purpose financing vehicle
Reiver Holdings Limited	England and Wales	Ordinary shares of £1	100	Holding company

The registered office of all subsidiaries listed above is Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ.

Holdings are direct other than Reiver Finance Limited which is indirect.

The Company also has two quasi-subsidiary special purpose entities, Bakethin Holdings Limited, which is wholly owned by Bakethin Charitable Trust, and Bakethin Finance plc, which is a wholly owned subsidiary of Bakethin Holdings Limited. The principal activity of Bakethin Finance plc is as a special purpose financing vehicle.

The registered office of the two quasi-subsidiaries is c/o Wilmington Trust SP Services (London) Limited, Third Floor, 1 King's Arms Yard, London, United Kingdom, EC2R 7AF.

13. INVENTORIES

	2019 £'m	2018 £'m
Raw materials and consumables	3.6	3.0

14. TRADE AND OTHER RECEIVABLES

	2019 £'m	2018 £'m
Trade receivables	170.2	152.2
Doubtful debt provision	(85.6)	(80.0)
Amounts owed by other group companies	2.9	2.6
Other receivables	5.7	7.4
Prepayments and accrued income	89.7	78.4
	182.9	**160.6**

Amounts owed by other group companies includes interest of £0.2m in respect of the financial investment of £159.0m in note 12(a). This loan has a variable interest rate of LIBOR plus 1% calculated on twice yearly payment dates and matures in January 2034. The remaining amounts due from group undertakings are due on demand with no fixed repayment date and bear no interest.

15. TRADE AND OTHER PAYABLES

	2019 £'m	2018 £'m
Trade payables	26.1	15.9
Amounts owed to other group companies	11.4	12.2
Taxation and social security	3.5	3.8
Income tax payable	7.1	11.6
Other payables	34.2	30.1
Accruals and deferred income	95.4	95.5
	177.7	**169.1**

Amounts due to group undertakings are due on demand with no fixed repayment date and bear no interest.

16. LOANS AND BORROWINGS

	2019 £'m	2018 £'m
Current:		
Bank overdrafts	0.5	-
Current instalments due on external borrowings	46.7	35.7
	47.2	**35.7**
Non-current:		
Non-current instalments due on external borrowings	530.4	557.7
Non-current instalments due on internal borrowings	2,237.0	2,216.7
	2,767.4	**2,774.4**

(a) External borrowings

Loans wholly repayable within five years amount to £38.6m (2018: £77.4m).

Loans not wholly repayable within five years amount to £538.5m (2018: £516.0m) and bear interest rates in the range 1.47% to 5.35%.

The fair value loss on the Company's outstanding interest rate and RPI swaps in the year to 31 March 2019 was £12.6m (2018: gain of £2.6m) in relation to interest rate swaps with a notional principal of £350.0m (2018: £350.0m).

(b) Internal borrowings

NWF issued £200m and £150m Guaranteed Eurobonds in February 1998 and September 2001 respectively, maturing February 2023, with an annual coupon of 6.875%. The issues were guaranteed by the Company who received the issue proceeds by way of inter-company loans of £194.2m and £163.2m respectively. Finance costs allocated during the year amounted to £0.2m (2018: £0.2m). Amortisation of loan issue receipts during the year amounted to £0.3m (2018: £0.3m).

NWF issued £250m and £100m Guaranteed Eurobonds in December 2002 and December 2004, maturing April 2033 with an annual coupon of 5.625%. Both issues were guaranteed by the Company who received the issue proceeds by way of inter-company loans of £246.6m and £100.8m respectively. Finance costs allocated during the year amounted to £0.2m (2018: £0.2m).

NWF issued £150m Guaranteed Index Linked Eurobonds in September 2005, maturing July 2036, with a real coupon of 2.033%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £149.1m. Indexation accretion during the year amounted to £7.0m (2018: £7.5m). Finance costs allocated during the year amounted to £0.2m (2018: £0.2m)

NWF issued £60m Guaranteed Index Linked Eurobonds in January 2006, maturing January 2041, with a real coupon of 1.6274%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £60.0m. Indexation accretion during the year amounted to £2.7m (2018: £3.0m).

NWF issued two £100m Guaranteed Index Linked Eurobonds in June 2006 with real coupons of 1.7118% and 1.7484% and with maturities of 2049 and 2053 respectively. Both issues were guaranteed by the Company who received the issue proceeds by way of two inter-company loans of £100.0m. Indexation accretion during the year amounted to £9.1m (2018: £9.8m).

NWF issued £360m Guaranteed Eurobonds in January 2012, maturing January 2042, with an annual coupon of 5.125%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £339.3m. Finance costs allocated during the year amounted to £0.7m (2018: £0.7m).

NWF issued £300m Guaranteed Eurobonds in October 2016, maturing October 2026, with an annual coupon of 1.625%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £297.6m. Finance costs allocated during the year amounted to £0.2m (2018: £0.2m).

NWF issued £300m Guaranteed Eurobonds in October 2017, maturing October 2027, with an annual coupon of 2.375%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £298.2m. Finance costs allocated during the year amounted to £0.3m (2018: £0.2).

17. OBLIGATIONS UNDER HIRE PURCHASE CONTRACTS AND FINANCE LEASES

(a) Obligations under hire purchase contracts and finance leases

The Company uses finance leases and hire purchase contracts to acquire plant and machinery and motor vehicles. There are no contingent rents, escalation clauses or material renewal or purchase options. The leases impose no restrictions in respect of dividends or raising additional debt. The obligations are as follows:

	2019 £'m	2018 £'m
Future minimum lease payments due:		
Within one year	6.0	5.5
In the second to fifth years inclusive	18.9	17.7
After five years	70.9	74.0
	95.8	**97.2**
Less:		
Finance charge allocated to future periods	(34.9)	(37.7)
Present value of minimum lease payments	**60.9**	**59.5**
Present value of minimum lease payments:		
Within one year	4.0	3.0
In the second to fifth years inclusive	10.6	9.2
After five years	46.3	47.3
	60.9	**59.5**
Disclosed as due:		
Current liability	4.0	3.0
Non current liability	56.9	56.5
	60.9	**59.5**

(b) Lease commitments

During the year in preparation for the implementation of IFRS 16 (see note 1t), the Company has reviewed the nature of the commitments previously disclosed as operating leases. This review concluded that some items were previously classified as operating leases incorrectly.

The Company has entered into non-cancellable operating leases in respect of land and buildings, plant, machinery and motor vehicles.

Land and building rent reviews are triggered by the lessor and typically take place every 3 to 5 years, at which point there may be an increase in rental payments. There are no purchase options or escalation clauses in respect of these leases and the terms of renewal are governed by Landlord and Tenant legislation. There are no restrictions imposed by these lease arrangements.

There are no contingent rents, escalation clauses or material renewal or purchase options in the terms of the plant, machinery and motor vehicle leases. The leases impose no restrictions in respect of dividends or raising additional debt.

The future minimum rentals payable under non-cancellable operating leases are as follows:

	2019 £'m	2018 £'m
Not later than one year	0.5	1.5
After one year but not more than five years	1.0	4.9
After five years	11.1	39.8
	12.6	**46.2**

18. PROVISIONS

	£'m
Pension provision for former employees:	
At 1 April 2018	1.3
Utilised during the year	(0.2)
At 31 March 2019	**1.1**
Analysed as:	
Current	0.2
Non-current	0.9
	1.1

The provision mainly represents outstanding pension liabilities for pensions that have been awarded on a discretionary basis, mainly to former employees of water companies which have since merged with the Company. These pension liabilities have been calculated by an independent actuary, using the same actuarial assumptions as applied to the defined benefit pension scheme, and are expected to be paid over the remaining lives, which is approximately four years.

In the ordinary course of business, the Company is sometimes subject to claims and potential litigation, whether from regulatory bodies, individuals or particular groups, related to one off matters. The Directors consider that, where it is possible to be estimated, a reasonable and appropriate position has been taken in reflecting such items in these Financial Statements in note 15 and the note above.

It is not currently possible to estimate the financial effect and likely timing of any associated outflow of some matters, given that some are in early stages of discussion, the limited likelihood of the claims against the Company being successful, or the potential range of possible outcomes, and accordingly no provision has been made in the Financial Statements. No reasonably possible financial outcome that would be significant to the Financial Statements has been identified in relation to these remaining matters at the date of the issue of these Financial Statements.

19. GRANTS AND DEFERRED INCOME

	CAPITAL GRANTS AND CONTRIBUTIONS £'m	PROCEEDS FROM KIELDER SECURITISATION £'m	TOTAL £'m
At 1 April 2018	**435.7**	**113.7**	**549.4**
Reclassification on adoption of IFRS 15	(70.8)	-	(70.8)
Additions	24.0	-	24.0
Amortised during the year	(5.3)	(7.0)	(12.3)
At 31 March 2019	**383.6**	**106.7**	**490.3**

Upon the adoption of IFRS 15 Revenue from Contracts with Customers, the treatment of certain capital contributions, most significantly mains and sewer diversions, has changed. These contributions were previously recognised as deferred income and amortised to the income statement over the expected useful life of the associated assets. Under IFRS 15, these contributions are now recognised in full in the income statement at the point at which the associated asset is brought into use. Upon transition, the unamortised amount of historical contributions of this nature, totalling £70.8m, has been reclassified to retained earnings. Please see note 1(s) for more information on the adoption of IFRS 15.

The Kielder securitisation involved the assignment of the right to the future income stream associated with the Kielder operating contract until 2034 to Reiver Finance Limited, a subsidiary company, in return for consideration of £212.1m. This capital sum is amortised to the income statement of the Company over the life of the assignment.

20. FINANCIAL INSTRUMENTS

	2019 £'m	2018 £'m
Financial (assets) / liabilities that are designated and effective as hedging instruments carried at fair value:		
Interest rate swaps	10.9	10.0
Power forward contracts	1.3	3.9
Foreign exchange contracts	(0.3)	0.2
Financial (assets) / liabilities carried at fair value through profit and loss:		
Interest rate swaps	30.4	18.8
Power forward contracts	(0.1)	(0.1)
	42.2	**32.8**

At 31 March 2019, the Company held the following interest rate swaps, designated as hedges of future interest cash flows, used to convert variable rate interest payments to a fixed rate basis:

NOTIONAL AMOUNT	START DATE	TERMINATION DATE	FIXED RATE
£100.0m	15 September 2008	15 March 2022	4.79%
£150.0m	15 October 2015	15 October 2025	2.36%

At 31 March 2019, the Company held the following interest rate swaps, designated as hedges of future interest cash flows, used to convert fixed rate interest payments to an index linked rate basis:

NOTIONAL AMOUNT	START DATE	TERMINATION DATE	INDEX LINKED RATE
£150.0m	15 October 2015	15 October 2025	(0.42%)
£100.0m	22 June 2017	22 June 2027	(1.10%)

At 31 March 2019, the Company held the following forward power contracts, designated as hedges of expected future purchases:

NOTIONAL AMOUNT	START DATE	TERMINATION DATE	PRICE PER MWH £
116,827 MWH	1 April 2019	30 September 2019	52.2
116,827 MWH	1 October 2019	31 March 2020	56.8

At 31 March 2019, the Company held the following fuel hedge, designated as a hedge of expected future purchases:

NOTIONAL AMOUNT	START DATE	TERMINATION DATE	PRICE PER LITRE £
3,000,000 litres	1 April 2019	31 March 2020	0.3562

20. FINANCIAL INSTRUMENTS (continued)

At 31 March 2019, the Company held the following forward exchange contracts, designated as hedges of expected future purchases for which the Company has firm commitments. The forward currency contracts are being used to hedge the foreign currency risk of the firm commitments. The terms of these contracts are as follows:

CURRENCY BOUGHT	MATURITY	EXCHANGE RATE	TRANSACTION VALUE £'m
USD 1,245,000	4 April 2019	1.4550	0.9
USD 1,112,000	31 May 2019	1.2645	0.9
USD 1,245,000	13 March 2020	1.4600	0.8
USD 1,240,404	30 April 2019	1.4069	0.9
USD 1,240,404	30 April 2020	1.4293	0.8
			4.3

At 31 March 2018, the Company held the following forward exchange contracts, designated as hedges of expected future purchases for which the Company has firm commitments. The forward currency contracts are being used to hedge the foreign currency risk of the firm commitments. The terms of these contracts are as follows:

CURRENCY BOUGHT	MATURITY	EXCHANGE RATE	TRANSACTION VALUE £'m
USD 1,245,000	4 April 2018	1.4492	0.9
USD 1,112,000	31 May 2018	1.2500	0.9
USD 1,245,000	4 April 2019	1.4550	0.9
USD 1,112,000	31 May 2019	1.2645	0.9
USD 1,245,000	13 March 2020	1.4600	0.8
USD 1,240,404	30 April 2018	1.3852	0.9
USD 1,240,404	30 April 2019	1.4069	0.9
USD 1,240,404	30 April 2020	1.4293	0.8
			7.0

21. SHARE CAPITAL

	2019 £'m	2018 £'m
Authorised:		
122,650,000 Ordinary Shares of £1 each (31 March 2018: 122,650,000)	122.7	122.7
Allotted, called-up and fully paid:		
122,650,000 Ordinary Shares of £1 each (31 March 2018: 122,650,000)	122.7	122.7

NWL is a company limited by shares.

22. FINANCIAL COMMITMENTS

(a) Capital commitments

	2019 £'m	2018 £'m
Contractual commitments for the acquisition of property, plant and equipment and intangible assets	145.3	130.2

In addition to these commitments, the Company has longer term expenditure plans, including investment to deliver business outcomes, maintain the health of the asset base and provide for new demand and growth in the regulated part of the business.

(b) Foreign currency commitments

At 31 March 2019 the Company held forward foreign exchange contracts of £4.3m (2018: £7.0m) for the purpose of hedging the foreign currency risk of committed future purchases.

(c) Power purchase agreement

In 2018/19 the Company signed a power purchase agreement with Ørsted, to purchase renewable energy from an offshore wind farm which will meet around 25% of the Company's energy demand. The agreement is for a 10 year term at a fixed commodity price, increasing annually by CPI.

The Company has concluded that the 'own use exception' applies, meaning that the PPA contract is not within the scope of IFRS 9 and therefore no further discussions are necessary.

23. PENSIONS

NWL participates in the Group defined benefit pension scheme, NWPS, providing benefits to 1,200 active members at 31 March 2019 (2018: 1,244). The assets of the NWPS are held separately from those of the Group in independently administered funds.

The most recent actuarial valuation of the NWPS was at 31 December 2016. At that date, the value of assets amounted to £954.6m and the liabilities were £1,245.2m, resulting in a deficit of £290.6m and a funding level of 76.7%. The next actuarial valuation will take place at 31 December 2019.

Under the revised schedule of contributions the future service contribution rate, jointly payable by members and the employers, remained at 29.4% of pensionable salaries until 31 December 2017. With effect from 1 January 2018, the employers' contribution was set at £12.3m per annum, increasing annually by RPI. Employee contribution rates remained at between 6% and 8% of pensionable salary, dependent upon which section of the Scheme the employee is a member of. The Company operates a salary sacrifice scheme under which members can elect for the Company to pay employee contributions on their behalf in place of salary. The Company will continue to pay the employer NI savings resulting from the salary sacrifice arrangement as additional employer contributions to the Scheme.

In addition, the employers continue to make deficit reduction payments of £11m per annum, with effect from 1 April 2015, increasing annually by RPI. Deficit reduction payments will increase by £2.6m per annum with effect from 1 April 2021. The deficit reduction payments have been set with the objective of removing the deficit by 31 March 2031, which has been the Company's long-term aim.

Employers' contributions (including associated company contributions) of £27.5m were paid in the year to 31 March 2019, of which £11.8m related to deficit reduction. For the year to 31 March 2020 employers contributions are projected to be £29.6m, including £12.2m in respect of deficit reduction.

Since the last actuarial valuation report, a pension increase exchange exercise has been implemented, which reduced the accounting deficit by an estimated £3.8m in the year to 31 March 2020. Following a High Court case in October 2018, in respect of the equalisation of benefits between males and females in relation to Guaranteed Minimum Pension (GMP) accrued between 1990 and 1997, an additional £4.2m has been added to the scheme liabilities to allow for the expected impact of GMP equalisation on the NWPS.

The Scheme also has a defined contribution section which had 1,957 active members at 31 March 2019 (2018: 1,945). Members can choose to contribute either 3%, 4% or 5% of salary, with employers contributing at either 6%, 7% or 8% depending on the member contribution rate. The contributions paid to the defined contribution section by the Company in the year totalled £6m (2018: £5.3m).

The additional disclosures regarding the defined benefit scheme as required under FRS 101 and the relevant impact on the Financial Statements are set out below. A qualified actuary, using revised assumptions that are consistent with the requirements of FRS 101 has updated the actuarial valuation described above as at 31 March 2019. Investments have been valued, for this purpose, at fair value.

23. PENSIONS (continued)

FRS 101 ACTUARIAL ASSUMPTIONS:	2019	2018
Discount rate	2.40%	2.65%
Pay increases[1]	3.15%	3.00%
Price inflation (RPI)	3.15%	3.00%
Price inflation (CPI)	2.05%	1.90%
Pension increases linked to RPI	3.15%	3.00%
Pension increases linked to CPI	2.05%	1.90%
Mortality assumptions[2]		
- Life expectancy for a member aged 65 - female (years)	23.8	24.2
- Life expectancy for a member aged 65 - male (years)	22.0	22.5

1. including promotional salary scale
2. scheme specific bespoke 'Vitacurves' which reflect the characteristics of the Scheme membership

The fair value of the assets in the NWPS and the present value of the liabilities in the Scheme are shown below:

	2019 £'m	2018 £'m
Equities	293.1	274.1
Corporate bonds	47.0	57.1
Government bonds	466.5	354.9
Property related funds	56.6	95.3
Cash	15.4	111.3
Other	152.2	96.6
Total fair value of assets	**1,030.8**	**989.3**
Present value of liabilities	**(1,139.3)**	**(1,083.6)**
Deficit	**(108.5)**	**(94.3)**

The amounts recognised in the income statement and in the statement of comprehensive income are analysed as follows:

RECOGNISED IN THE INCOME STATEMENT:	2019 £'m	2018 £'m
Current service cost	15.6	16.0
Administration cost	1.9	2.2
Past service cost	1.2	0.1
Recognised in operating costs in arriving at operating profit	**18.7**	**18.3**

23. PENSIONS (continued)

RECOGNISED IN THE INCOME STATEMENT:	2019 £'m	2018 £'m
Net interest cost on plan obligations	2.2	3.6
Recognised in finance costs	**2.2**	**3.6**

RECOGNISED IN THE STATEMENT OF COMPREHENSIVE INCOME:	2019 £'m	2018 £'m
Changes in demographic assumptions	21.5	(6.5)
Changes in financial assumptions	(81.4)	49.0
Return on assets (excluding amounts included in finance costs)	40.0	19.3
Other actuarial losses	(0.9)	(6.9)
Net actuarial (losses) / gains	**(20.8)**	**54.9**
Contributions made by associated company	0.2	0.1
Net actuarial (losses) / gains	**(20.6)**	**55.0**

Changes in the present value of the defined pension obligations are analysed as follows:

	2019 £'m	2018 £'m
At start of period	**1,083.6**	**1,132.5**
Current service cost	15.6	16.0
Administration cost	1.9	2.2
Past service cost	1.2	0.1
Interest cost	28.1	28.1
Contributions by plan participants	0.1	0.1
Benefits paid	(52.0)	(59.8)
Remeasurement:		
Changes in demographic assumptions	(21.5)	6.5
Changes in financial assumptions	81.4	(49.0)
Other actuarial gains and losses	0.9	6.9
At end of period	**1,139.3**	**1,083.6**

23. PENSIONS (continued)

Changes in the fair value of plan assets are analysed as follows:

	2019 £'m	2018 £'m
At start of period	**989.3**	**979.4**
Interest income on scheme assets	25.9	24.5
Contributions by employers (including associated company)	27.5	25.8
Contributions by plan participants	0.1	0.1
Benefits paid	(52.0)	(59.8)
Return on assets (excluding amounts included in finance costs)	40.0	19.3
At end of period	**1,030.8**	**989.3**

Nature of benefits, regulatory framework and other entity's responsibilities for governance of the Scheme

The Scheme is a registered defined benefit scheme subject to the UK regulatory framework for pensions, including the scheme specific funding requirements. The Scheme is operated under trust and as such, the Trustee of the Scheme is responsible for operating the Scheme and it has a statutory responsibility to act in accordance with the Scheme's Trust Deed and Rules, in the best interest of the beneficiaries of the Scheme, and UK legislation (including Trust law). The Trustee has the power to set the contributions that are paid to the Scheme.

Risks to which the Scheme exposes the Company

The nature of the Scheme exposes the Company to the risk of paying unanticipated additional contributions to the Scheme in times of adverse experience. The most financially significant risks are likely to be:

- members living for longer than expected;
- higher than expected actual inflation and salary increase experience;
- lower than expected investment returns; and
- the risk that movements in the value of the Scheme's liabilities are not met by corresponding movements in the value of the Scheme's assets.

23. PENSIONS (continued)

Asset-liability matching strategies used by the Scheme or the Company

The Scheme does not currently use any asset-liability matching strategies. The Trustee's current investment strategy, having consulted with the Company, is to invest the majority of the Scheme's assets in a mix of equities and corporate and government bonds, in order to strike a balance between:

- maximising the returns on the Scheme's assets; and
- minimising the risks associated with lower than expected returns on the Scheme's assets.

The Trustee is required to regularly review its investment strategy in light of the revised term and nature of the Scheme's liabilities. During the year, the Trustee chose to de-risk part of its equity allocation.

Sensitivity to key assumptions

The costs of a pension arrangement require estimates regarding future experience. The financial assumptions used for FRS 101 reporting are the responsibility of the Directors of the Company. These assumptions reflect market conditions at the balance sheet date. Changes in market conditions which result in changes in the net discount rate (essentially the difference between the discount rate and the assumed rates of increases of salaries, deferred pension revaluation or pensions in payment), can have a significant effect on the value of the liabilities reported.

There has been no change in the methodology used to assess the impact of changes in assumptions. Approximate adjustments were made to the defined benefit obligations reflecting the mean term of the liability.

Impact of changes in assumptions compared with actuarial assumption for the NWPS:

Actuarial value of liabilities on 31 March 2019:

	£'m
0.25% reduction in discount rate	1,193.6
0.25% increase in inflation	1,188.0
1 year increase in life expectancy	1,178.0

Maturity profile of the defined benefit obligation for the year ended 31 March 2019:

	NUMBER OF MEMBERS	LIABILITY SPLIT (%)	DURATION (YEARS)
Active members	1,200	37	25
Deferred members	1,095	14	23
Pensioners	3,193	49	13

24. RELATED PARTY DISCLOSURES

The Company is a wholly owned subsidiary of NWGL, whose publicly available consolidated Financial Statements include the Company. Accordingly, the Company is exempt under the terms of FRS101 from disclosing transactions with other members of the Group headed by NWGL.

Transactions with related parties outside of the NWGL group comprised purchases of £11.4m (2018: £12.1m), sales of £158.1m (2018: £110.0m), and a net repayment for prior year consortium tax relief of nil (2018: £8.9m). As at 31 March 2019 £26.8m (2018: £10.7m) is owed from these companies in respect of sales or rebates, and £0.2m (2018: £0.1m) is owed to these companies in respect of purchases.

The Company acquires vehicles from Vehicle Lease and Service Limited, an associated company, on a finance lease basis. During the year, new finance leases of £4.8m (2018: £4.8m) were entered into and capital repayments of £3.4m (2018: £3.6m) were made. The year end finance lease creditor was £12m (2018: £10.7m).

The companies with which NWL had transactions during the year, included in the above balances, were as follows:

- Anglian Water Business (National) Limited;
- CKI;
- Eastern Power Networks;
- Hutchison 3G UK Limited;
- Hutchison Whampoa (Europe) Limited;
- Northern Gas Networks (NGN);
- NWG Business (NWGB);
- Seabank Power Limited;
- UK Power Networks (Operations) Limited; and
- Vehicle Lease and Service Limited.

25. ULTIMATE PARENT UNDERTAKING AND CONTROLLING PARTY

In the Directors' opinion, the Company's ultimate parent undertaking and controlling party is CKHH, a company listed on The Stock Exchange of Hong Kong Limited. This is the parent undertaking of the largest group of undertakings for which group financial statements are drawn up and of which the reporting company is a member. Copies of CKHH's group Financial Statements, which include the Company, are available from **http://www.ckh.com.hk/en/ir/annual.php**. CKHH's registered office is PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands and is incorporated in the Cayman Islands with limited liability.

The parent undertaking of the smallest group of undertakings for which group Financial Statements are drawn up, and of which the reporting company is a member, is NWGL, which is incorporated in England and Wales. Copies of NWGL's group Financial Statements will be available in due course from Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF NORTHUMBRIAN WATER LIMITED

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

OPINION

In our opinion the Financial Statements of Northumbrian Water Limited (the 'Company'):

- give a true and fair view of the state of the Company's affairs as at 31 March 2019 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including Financial Reporting Standard 101 "Reduced Disclosure Framework"; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the Financial Statements which comprise:

- the income statement;
- the statement of comprehensive income;
- the balance sheet;
- the statement of changes in equity; and
- the related notes 1 to 25.

The financial reporting framework that has been applied in the preparation is applicable law and United Kingdom Accounting Standards including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

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 Financial Reporting Council's (the 'FRC's') Ethical Standard, 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.

STRATEGIC REPORT
GOVERNANCE REPORT
STATUTORY FINANCIAL STATEMENTS

SUMMARY OF OUR AUDIT APPROACH

KEY AUDIT MATTERS	The key audit matters that we identified in the current year were: • Classification of capex, opex and capitalised overheads • Provision for bad and doubtful debts • Revenue recognition (valuation of unbilled revenue accrual) Within this report, any new key audit matters are identified with and any key audit matters which are the same as the prior year identified with .
MATERIALITY	The materiality that we used in the current year was £10.3m which was determined on the basis of 5% of profit before tax, adjusted to take account of derivative valuation movements charged to the income statement in the year and capped based on group materiality.
SCOPING	Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.
SIGNIFICANT CHANGES IN OUR APPROACH	Changes in our approach were limited to removing revenue recognition (adjustments to industry data from MOSL) as a key audit matter and significant risk. This is due to the quantum and limited risk in this area given it is now an established data feed and adjustment, no longer being the first year of the retail market.

CONCLUSIONS RELATING TO GOING CONCERN, PRINCIPAL RISKS AND VIABILITY STATEMENT

GOING CONCERN	We have reviewed the Directors' statement in note 1 to the Financial Statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the Company's ability to continue to do so over a period of at least twelve months from the date of approval of the Financial Statements. We considered as part of our risk assessment the nature of the Company, its business model and related risks including where relevant the impact of Brexit, the requirements of the applicable financial reporting framework and the system of internal control. We evaluated the Directors' assessment of the Company's ability to continue as a going concern, including challenging the underlying data and key assumptions used to make the assessment, and evaluated the Directors' plans for future actions in relation to their going concern assessment.	**We confirm that we have nothing material to report, add or draw attention to in respect of these matters.**
PRINCIPAL RISKS AND VIABILITY STATEMENT	Based solely on reading the Directors' statements and considering whether they were consistent with the knowledge we obtained in the course of the audit, including the knowledge obtained in the evaluation of the Directors' assessment of the Company's ability to continue as a going concern, we are required to state whether we have anything material to add or draw attention to in relation to: • the disclosures within the Strategic Report that describe the principal risks and explain how they are being managed or mitigated; • the Directors' confirmation on page 53 that they have carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity; or • the Directors' explanation on pages 95 to 96 as to how they have assessed the prospects of the Company, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.	**We confirm that we have nothing material to report, add or draw attention to in respect of these matters.**

KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgement, 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 forming our opinion thereon, and we do not provide a separate opinion on these matters.

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CLASSIFICATION OF CAPEX, OPEX AND CAPITALISED OVERHEADS	
Key audit matter description	The water industry is capital intensive and pipeline assets require regular maintenance and upgrades. There is an inherent risk in the industry that costs included in property, plant and equipment are not capital in nature and/or are not in line with the capitalisation criteria of IAS 16. Capital expenditure for the year ended 31 March 2019 was £279.5m (2018: £260.7m), together with significant spend on maintenance costs. The classification of expenditure on capital assets also includes the allocation of certain overhead costs to property, plant and equipment reflecting the use of the Company's own teams and resources to complete capital work which requires the application of judgement. The capitalised labour costs were £41m for the year ended 31 March 2019 (2018: £38m). Further details are included within the Strategic Report on page 51 and also notes 1, 10 and 11 to the Financial Statements. During the audit it was identified that intangible assets had been incorrectly classified as tangible assets, which is not in line with the requirements of IAS 38, resulting in a misstatement in the current and prior years. The misstatement has been corrected by management in the current period and a prior period adjustment has been recognised, which resulted in a reclassification between property, plant and equipment to intangible assets of £67.1m as at 31 March 2018. Refer to note 2 for further details.
How the scope of our audit responded to the key audit matter	• We evaluated the design and implementation of management's key controls over the processing of accounting entries associated with capital and operating expenditure; • We reviewed the appropriateness of the Company's capitalisation policies and its approach to determining which costs should be capitalised and which expensed; • We compared the actual capitalised expenditure incurred in the period with regulatory targets and made enquiries of management to understand any under/over spend; • We performed substantive testing on both capitalised and expensed amounts to assess whether these are classified in accordance with the Company's policies and IAS 16; • We continued to challenge management's assumptions by comparing amounts capitalised for each department in the current and prior years and we have understood the reasons behind levels of capitalisation; • We tested a sample of capitalised overheads by agreeing to timesheets and project plans to assess whether capitalisation was appropriate; and • We evaluated the nature of the misstatement and whether correction of this through a prior year adjustment is appropriate.
Key observations	We concluded that the intangibles and property, plant and equipment values are appropriate following the correction of the above mentioned misstatement in the prior years.

table continued...

PROVISION FOR BAD AND DOUBTFUL DEBTS

Key audit matter description	As stated in the critical accounting judgements and key sources of estimation uncertainty in note 1r on page 108 of the Annual Report, the value of the bad debt provision is calculated by applying a range of percentages to debt of different ages with higher percentages applied to different categories of debt depending on an assessment of the level of risk of default. There is a significant customer base, and regulations do not allow NWL to interrupt water supply to domestic customers. The valuation of the bad debt provision is sensitive to the specific percentages applied which are judgemental. Given the implementation of the new IFRS 9 reporting standard in the year, there is also the requirement to assess expected credit losses and enhance disclosures in this area within the Financial Statements. At 31 March 2019 the gross debtors balance was £170.2m (2018: £152.2m) and the bad debt provision was £85.6m (2018: £80.0m). Further details are included within note 1(p) and 14 to the Financial Statements.
How the scope of our audit responded to the key audit matter	• We evaluated the design and implementation of management's key controls over the calculation of the bad debt provision; • We compared the assumptions made by management in calculating the provision to evidence provided from historical collection data; • We assessed the reasonableness of any judgements made in respect of likely future events through discussion of any known events with management and assessment of associated provision; • We reviewed the disclosure regarding the bad debt provision in relation to IFRS 9; • We audited a sample of credit notes raised to determine whether any were as a result of an event known but not appropriately provided for; • We performed sensitivity analysis on the provision to assess the impact of changes in the cash collection rate; and • We reviewed the receivables ageing report to help assess whether overdue debtors are appropriately provided for.
Key observations	The results of our procedures were satisfactory. We have concluded that management's judgements are appropriate and that the provision for bad and doubtful debts was appropriately stated.

table continued...

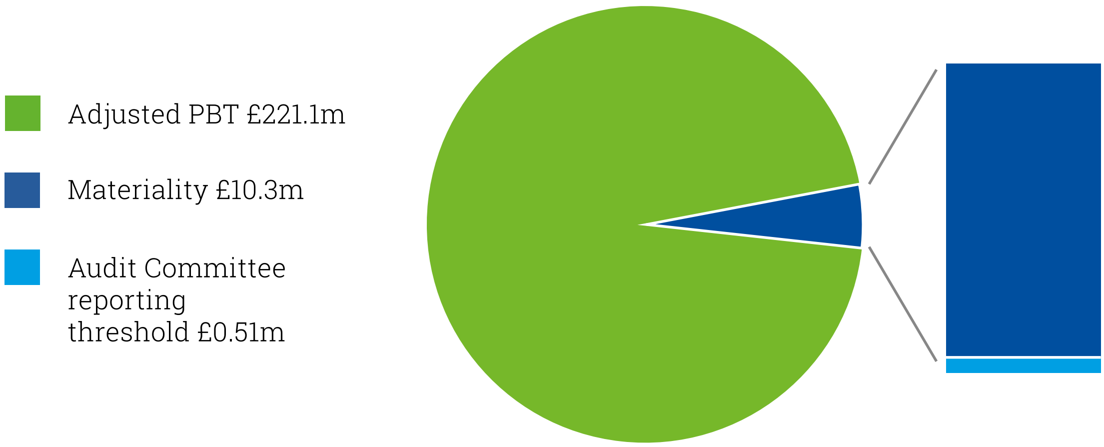
REVENUE RECOGNITION (VALUATION OF UNBILLED REVENUE ACCRUAL)	
Key audit matter description	The nature and scale of NWL's business is such that it is not possible to read all water meters at year end. An estimate is therefore made of the unbilled revenue at the year end. At 31 March 2019 this measured income accrual was £77.6m (2018: £65.7m). Management estimates the amount of water and sewerage services that have been supplied to customers and not billed at year end, based on historic water consumption and default consumption rates. The revenue attributable to this unbilled revenue at year end is accrued. The accrual is both material and judgemental and is therefore considered to be a key audit matter. Further details are included within notes 1(b), 3 and 14 to the Financial Statements.
How the scope of our audit responded to the key audit matter	• We evaluated the design and implementation of management's key controls over the unbilled revenue accrual; • We audited the operating effectiveness of controls over the revenue process to assess the integrity of reported turnover; • We performed substantive testing of the accrued revenue calculation and made an assessment of the appropriateness of accounting estimates made by management; • We reviewed the accrued revenue balance for indications of recoverability risk by tracing a sample to subsequent bill and cash payment; and • We considered historic accuracy by performing retrospective testing on the March 2018 balance.
Key observations	The results of our procedures were satisfactory. We concluded that the valuation of unbilled revenue accrual is appropriate and concurred with management on judgements adopted.

OUR APPLICATION OF MATERIALITY

We define materiality as the magnitude of misstatement in the Financial Statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

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

MATERIALITY	£10.3m (2018: £10.5m)
BASIS FOR DETERMINING MATERIALITY	5% of adjusted pre-tax profit. This was adjusted to take account of derivative valuation movements charged to the income statement in the year. This has been excluded due to the level of volatility of such derivative valuation movements, in order to provide a consistent basis year on year.
RATIONALE FOR THE BENCHMARK APPLIED	Pre-tax profit was selected as the appropriate measure on which to calculate materiality as it is considered an area of focus for the users of the accounts. Materiality equates to 4.7% of adjusted profit before tax, due to the cap that was applied of £10.3m, on the basis that the Company represents 100% of Group profit before tax.



We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £514,800 (2018: £210,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the Financial Statements. The movement from prior year reporting threshold is due to the fact we have seen limited errors in previous years and we are now using the maximum threshold allowed under Deloitte methodologies of 5%, whereas previous years used 2%.

AN OVERVIEW OF THE SCOPE OF OUR AUDIT

NWL operates as a regulated water and wastewater business operating in the UK. Reflecting the nature of this audit and the UK base and business model of the Company no significant scoping decisions were required.

In establishing the overall approach to our audit, we assessed the risk of material misstatement, taking into account the nature, likelihood and potential magnitude of any misstatement. Following this assessment and our calculation of materiality, we applied professional judgement to determine the extent of testing required over each balance in the Financial Statements. Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

OTHER INFORMATION

The Directors are responsible for the other information. The other information comprises the information included in the Annual Report, other than the Financial Statements and our Auditor's Report thereon.

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

In connection with our audit of the Financial Statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Financial Statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the Financial Statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

In this context, matters that we are specifically required to report to you as uncorrected material misstatements of the other information include where we conclude that:

- Fair, balanced and understandable – the statement given by the Directors that they consider the Annual Report and Financial Statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- Audit Committee reporting – the section describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

We have nothing to report in respect of these matters.

RESPONSIBILITIES OF DIRECTORS

As explained more fully in the Directors' Responsibilities Statement, 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.

Details of the extent to which the audit was considered capable of detecting irregularities, including fraud are set out below.

A further description of our responsibilities for the audit of the Financial Statements is located on the FRC's website at: **www.frc.org.uk/auditorsresponsibilities**. This description forms part of our Auditor's Report.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

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 the Directors' Report have been prepared in accordance with applicable legal requirements.

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 any material misstatements in the Strategic Report or the Directors' Report.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

Adequacy of explanations received and accounting records

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

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Company Financial Statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of Directors' remuneration have not been made.

We have nothing to report in respect of this matter.

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.

Anthony Matthews FCA (Senior statutory auditor)

for and on behalf of Deloitte LLP
Statutory Auditor
Newcastle Upon Tyne
United Kingdom
12 July 2019

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