NORTHUMBRIAN WATER LIMITED FINANCIAL STATEMENTS AND ANNUAL PERFORMANCE REPORT

FOR THE YEAR ENDED 31 MARCH 2016

Registered company no: 02366703

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CHAIRMAN'S STATEMENT

CHAIRMAN'S STATEMENT

I am pleased to introduce the combined Financial Statements and Annual Performance Report (APR) of Northumbrian Water Limited (NWL or the Company) for the year ended 31 March 2016.

There are a number of changes in our reporting this year, combining what have previously been two separate documents, the Accounts and the APR, into a single document, transitioning to new international accounting standards and reporting under revised regulatory guidelines set out by the Water Service Regulation Authority (Ofwat).

Alongside this report, we will again be publishing additional information about our performance and governance arrangements in a more customer friendly style on our website.

NWL continues to strive to become the national leader in the provision of sustainable water and wastewater services and our Chief Executive Officer (CEO), Heidi Mottram, confirms in her report that we have made steady progress across most of our key measures of success during 2015-16. NWL is absolutely committed to consistent delivery of outstanding customer service, and operational excellence remains central to this. The Board works closely with the executive to ensure that the Company delivers continuous improvements in the key areas of customer service and in health, safety and environmental performance.

People continue to be one of our strategic themes and a full Health and Safety (H&S) update is the first item we consider on each Board agenda. This is a top priority for the Board, which reviews the H&S updates carefully and invests significant time with the Company's management to ensure that the H&S strategy for 2016 to 2020 will deliver even better performance. The environment is another important strategic theme and the Board reviews environmental performance at each Board meeting. The Strategic Report, below, sets out our very sound environmental performance in more detail.

The Company's excellent customer service and operational performance are supported by the high corporate governance standards maintained by the Board, which has regard to the principles underpinning the UK Corporate Governance Code (UK CGC) as required by the Company's Instrument of Appointment (the Licence). Whilst the Board does not consider that full compliance with all the detailed provisions of the UK CGC is practicable, given that NWL is privately owned, or is necessary for sound governance, the Board has embraced the key elements of the UK CGC's principles. The Corporate Governance report (on page 45) describes and explains some minor aspects of the UK CGC which we have chosen not to fully adopt. The Company also has in place a further governance code, developed after discussions with Ofwat, which balances the legitimate interests of all stakeholders. Compliance with this code is reported on page 53 of this document.

Andrew J Hunter

The Board functions as an integrated whole 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 central to investment and operational decisions. The involvement of our Independent Non-Executive Directors (INEDs) is critically important to NWL's governance and the Company has four, rather than the three required by its Licence. Paul Rew, our Senior INED, confirms in his report that the INEDs are fully involved in all the main aspects of NWL's governance and participate in the Board meetings of our holding company, Northumbrian Water Group Limited (NWGL).

The Board, supported by the Risk & Compliance Committee, has ultimate responsibility for risk management and determines risk appetite. The Risk & Compliance Committee receives regular updates on the top-rated risks and priorities for assurance and conducts 'deep-dives' into key areas of risk. On the Board's behalf the Risk & Compliance Committee has conducted a robust assessment of the principal risks facing the Company. One notable recent event was the UK voting to leave the European Union (EU), and the Board is closely monitoring the resultant uncertainty in the financial markets and assessing potential impacts on the Company. These risks, and how they are managed, are described on page 36 of the Strategic Report.

As Heidi confirms in her report, the Company's preparations for the opening of the non-household retail market in 2017 are well advanced. NWL is working very hard to ensure that it will be an effective and efficient wholesaler of those services once the market opens, whilst continuing to provide first class services to its domestic customers.

I can assure our stakeholders that NWL's responsibilities as a significant supplier of water and wastewater services are recognised fully by the directors and influence all key decisions.

The Board will continue to drive the performance of the Company forward to ensure that all our customers are delighted with our services in 2016-17 and beyond.

Andrew J Hunter
Chairman

CHIEF EXECUTIVE OFFICER'S REPORT

I am pleased to introduce our annual report on our performance for the year ended 31 March 2016. Whilst this has been the first year of a new regulatory cycle, our vision to be the national leader in the provision of sustainable water and wastewater services, our business outcomes and our values remain constant. I am delighted that we have shown steady improvement across the majority of our key measures of success and remain at the forefront of performance in our industry.

Customers are at the heart of our business and this year we have worked with our customers, as well as our employees and supply chain partners, to develop our new 'Living Water, Loving Customers' strategy. This strategy focuses on those areas that our customers have told us are their important priorities. We are also progressing well with the implementation of our new integrated customer care and billing system. I am confident that these initiatives will help us to achieve our aim of delivering an unrivalled customer experience.

In our water business we continue to provide a reliable supply of clean water, continuing our industry leading performance on interruptions to supply and award winning approach to water efficiency. We were delighted to have Sir David Attenborough officially open Abberton reservoir, the culmination of many years of effort and investment to secure water supplies to Essex for decades to come. Sir David was impressed with how a project to deliver economic sustainability had also added value to the environment and biodiversity.

Ensuring the security of our water supply against a backdrop of changing climate and increasing population requires long term planning and we are proud to have been able to work with other water companies to lead the development of the new national water framework.

The quality of the water we produce remains exceptionally high and we have continued to make great strides tackling discolouration of water and in our catchment management approach to reducing pesticides in our water resources.


Heidi Mottram

In our wastewater business reducing sewer flooding remains one of our highest business priorities and I'm pleased that we have seen a further reduction in flooding incidents this year. We are working with a number of partners to promote innovative and sustainable urban drainage solutions to reduce the long term flooding risks. We were pleased to host visits from the Chief Executives of Ofwat and the Environment Agency (EA), as well as senior water officials at the Department for Environment Food & Rural Affairs (DEFRA), to one such scheme where we have worked with the EA to provide a holistic and multi-agency solution, including diverting a small river, which is helping to protect hundreds of properties.

Our wastewater treatment continues to be industry leading and 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. In December 2014, at one plant, we also began to clean and transform the biogas from the AAD process into biomethane for injection to the gas distribution network. Through 2015 this has continued to contribute to the proportion of renewable gas in the national gas grid, supporting the long term sustainability of the nation's gas supply and reducing the carbon footprint of the UK as a whole.

Innovative approaches such as this are leading to step changes in our industry and we have been actively contributing to Ofwat's thinking on Water 2020 and their 'Marketplace For Ideas' to explore other creative approaches to future challenges.

Sadly, many parts of the world still face challenges on the very basics of water supply and sanitation and I was fortunate enough to have the opportunity to travel to Malawi to see first hand the incredible work that WaterAid, the charity we co-founded in 1981, carries out. The charity's whole philosophy is based on creating sustainability in the villages they work with, bringing clean water and good health which enables the children to go to school, get educated and improve their chances of having a great life. Experiences like this really do put things into perspective and emphasise how lucky we are to live in this country and have the resources that are available to us.

Looking forward, the opening of the competitive market in 2017 is coming ever closer, when all non-household customers will be able to choose their retail supplier. Our preparations are well advanced and I am confident that we will be ready for market opening in April 2017 for both our wholesale and retail operations. Whilst, as NWL we will exit the non-household retail market, our parent company, NWGL, intends to compete in this retail market through its separate subsidiary, NWG Business Limited (NWGBL), building on our existing expertise and reputation.

Further ahead, the Government has asked the water industry regulator, Ofwat, to investigate the cost and benefits of extending retail competition to household customers. We agree that customers must be central to the future development of the water industry. We are already deeply committed to engaging with our customers in building our future plans and I am delighted to welcome Jim Dixon as the new independent chair of our Water Forum customer challenge group. Jim has a wealth of experience which he will use to challenge our plans and ensure that we remain focused on the needs of our customers and other stakeholder groups. I look forward to working with him over the coming years as we develop our future plans.

Although we have just completed the first year of the current price control period, we are already planning ahead to the next price review and are pleased that Ofwat has already published many key aspects of its intended regulatory approach through its Water 2020 programme. Whilst more information is required to understand the potential impact of some of these changes, we are keen to continue to engage with Ofwat as its approach develops.

Whilst we are proud of what we have achieved, we are never complacent and will continue to make further service improvements in 2016-17 and beyond. I hope you find our financial statements and Annual Performance Report (APR) helpful and informative.

H Mottram OBE
Chief Executive Officer (CEO)

STRATEGIC REPORT

FOR THE YEAR ENDED 31 MARCH 2016

STRATEGIC REPORT

BUSINESS OVERVIEW

NWL is one of ten regulated Water and Sewerage Companies (WASCs) in England and Wales, operating in the north east of England, trading as Northumbrian Water (NW), and in the south east of England, trading as Essex & Suffolk Water (ESW).

In the north east, the business comprises the supply of both potable and raw water and the collection, treatment and disposal of sewage and sewage sludge, serving 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 only wastewater services in Hartlepool.

In the south, we supply water services to 1.5 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.

NWL operates within a strict regulatory environment. Ofwat regulates prices and levels of customer service, while the Drinking Water Inspectorate (DWI) monitors drinking water quality and the EA covers environmental protection. Customers' interests are represented by the Consumer Council for Water (CCWater).

NWL owns a number of subsidiary companies which carry out financing activities on behalf of the Company (see note 10 of the Statutory Financial Statements) which, together with the Company, form the NWL group.

NWL's immediate parent company is NWGL. CK Hutchison Holdings Limited (CKHH), a company listed on the Hong Kong Stock Exchange, is the ultimate pavrent undertaking and controlling party of NWGL and, therefore, NWL. Further information about the structure and ownership of NWGL is provided on page 32 in the financial performance and structure section of this report.

STRATEGIC REPORT

REGULATORY AND LEGISLATIVE DEVELOPMENTS

CHANGES IN FINANCIAL REPORTING

The financial statements within this report have been produced under Financial Reporting Standard (FRS) 101 for the first time, which adopts International Financial Reporting Standards (IFRS) with some permitted reduced disclosures. This replaces the previously applied UK Generally Accepted Accounting Practice (UK GAAP), in accordance with FRS 100, issued by the Financial Reporting Council (FRC). FRS 100 required all UK companies to transition to either IFRS, with reduced disclosures under FRS 101 for eligible entities, or FRS 102, a new UK GAAP based on similar principles to IFRS. The transition from UK GAAP to IFRS is described in notes 1a and 24 of the Statutory Financial Statements.

CHANGES IN REGULATORY REPORTING

In February 2015, after a period of consultation, Ofwat published revised regulatory reporting requirements and accounting guidelines, effective from 1 April 2015. We report against these requirements in our APR on pages 105 to 209, and also explain the assurance that we have obtained on this information.

Within the APR we report information against the four separate price controls, for wholesale water and wastewater and for household and non-household retail, set in our Final Determination (FD) of prices for 2015 to 2020, which we received from Ofwat in December 2014. As part of this FD we also agreed our business outcome statements, measures of success and outcome delivery incentives for the period.

The business outcomes were developed in consultation with our customers and stakeholders, and express the high level objectives that our actions are intended to deliver. They represent what customers and society value in the long term. We report on our progress against our outcomes within the Business Performance section of this report and in 'Our Performance in 2015-16' in the APR. Further information is available on our websites (**www.nwl.co.uk**, **www.eswater.co.uk** and **www.welivewater.co.uk**).

In addition to the APR requirements, Ofwat has issued a number of documents during the year outlining its expectations of companies in respect of: a monitoring framework for reporting of non-financial performance; transparency of reporting on corporate governance matters; and how companies demonstrate long term financial resilience. In response, we have further strengthened our approach on each of these areas within this report.

WATER 2020

Although we are reporting on only the first year of the current five year price control period, we are already looking ahead to the next price control review for 2020 to 2025 (PR19). In December 2015, Ofwat published a consultation on the 'Regulatory Framework for Wholesale Markets and the 2019 Price Review', to which we responded positively.

Following this, in May 2016, Ofwat published 'Water 2020: our regulatory approach for water and wastewater services in England and Wales'. This confirmed some key changes to the approach to be taken at PR19 including separate price controls for water resources and sewage sludge, moving from Retail Prices Index (RPI) to Consumer Prices Index (CPI) indexation for customer bills and 50% of Regulatory Capital Value (RCV) growth, greater customer engagement and understanding and an increased focus on long term operational resilience.

We will continue to engage with Ofwat as its approach develops.

RETAIL COMPETITION

The Water Act 2014 created a competitive market for retail water and wastewater services for all non-households with a target date for market opening of April 2017. We have proactively engaged with this process through our involvement with the Open Water programme and, more recently, with Market Operator Services Limited (MOSL), of which NWL was one of the three founding members.

Ofwat has published an integrated plan for the opening of the retail water market on its website. The plan sets out the various key activities that need to be undertaken by DEFRA, Ofwat, MOSL and all trading parties, including existing water companies and new entrants, in order to implement the new market. One important strand of the plan is the assurance framework developed to provide confidence that the market and companies will be ready for market opening.

Our preparations for the opening of this market are well advanced in terms of process, systems and organisational development, from both a wholesaler and retailer perspective. The Board provided its first assurance letter to MOSL and Ofwat on the effectiveness of our plans in February 2016. We are confident that we will be able to provide the further assurance letters required in respect of interim preparation, in October 2016, and market readiness, in February 2017.

NWGL intends to compete in the non-household retail market and its separate subsidiary, NWGBL, will seek to enter the market as a retailer.

In November 2015, HM Treasury announced that Ofwat will provide an assessment of the costs and benefits of extending retail competition to household water customers by summer 2016. In response to Ofwat's call for evidence, we commissioned a report to identify lessons to be learned from competition in the energy retail market and jointly commissioned a study into potential impacts on vulnerable customers. We strongly support Ofwat's statement that the review be evidence based and believe that customers' views should be at the heart of the review.

Jim Dixon

WATER FORUMS

The insight and challenge provided by our Water Forum stakeholder groups was fundamental to the development of our business plan for the 2015 to 2020 price control review (PR14). Since then we have carried out a comprehensive review of the role of the Water Forums, taking account of the views of existing Forum members, customers, Ofwat and the Company. Led by our new independent Water Forum Chair, Jim Dixon, we have determined that the Forums will be more clearly focused on outcomes for customers, rather than the regulatory agenda. They will play a key part in our customer and stakeholder engagement strategies.

Jim has had a long career in countryside management, public administration and heritage management. He has held senior roles in the RSPB, Natural England's predecessor organisations and within DEFRA and, for four years, led the 15 UK National Parks. He has appointed other members as theme leads and the first meeting of the new Water Forum took place in July 2016. He has made the following statement in respect of his appointment.

"I am delighted to have been appointed as the Independent Chair of the Northumbrian and Essex & Suffolk Water Forums. The Forums have an important role to play in helping to assure that NWL is supplying as good a service to its customers as possible. Whilst this is a well-run Company, there is always room for improvement. The operating environment, customer's expectations and the regulatory world change constantly. A company like NWL has to adjust, grow and respond to its customers' ever-changing needs.

The Forums are a way in which constructive challenge can be brought to the company's work. By bringing together a range of experts, such as people from business, communities, agencies and the voluntary sector, a range of perspectives can come together to examine the company's performance. Whether it is the company's indicators of sustainable development, or its annual performance report or plans for stakeholder engagement, the Forums can bring a critical eye to bear.

I have been very impressed so far with the professionalism of all of the staff that I have met. My first impressions are of a commitment to serving customers, of working together as one team and being a good partner to other organisations and the community. As the Forums develop, I want to test out these impressions and use data and the expertise of other Forum members to probe and test the assumptions, plans and performance of Northumbrian Water Limited."

Jim Dixon
Chair of the Water Forums

BUSINESS STRATEGY AND OUTCOMES

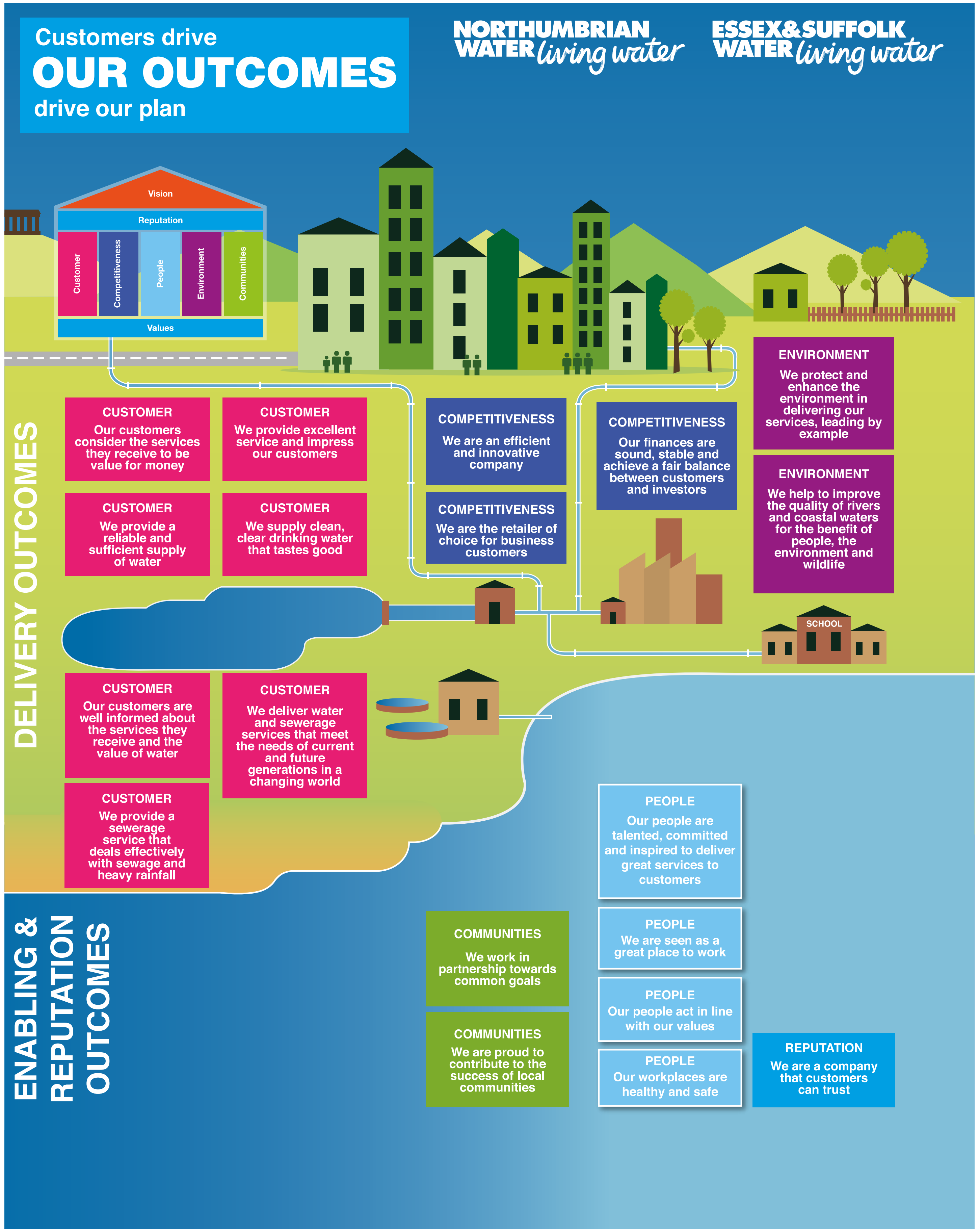
NWL's vision is to 'be the national leader in the provision of sustainable water and wastewater services'. We want to continue to deliver value to customers and other stakeholders by focusing on our core competencies of water and wastewater management.

We have underpinned our drive to be the best with five strategic themes, Competitiveness, Customer, People, Environment and Communities, described below, and achieving the right balance between them is essential to our success and reputation. Our business outcomes are aligned to these themes and encapsulate our long-term goals and what we aim to achieve. We have 12 delivery outcomes, which cover our strategic themes of Customer, Environment and Competitiveness, and a further seven enabling outcomes which cover our strategic themes of Communities, People and our overall reputation.

OUR VALUES

As important as our clear direction and goals is our clear sense of values. We have made a commitment to five core values, described below, and these are the principles which define how we will work to achieve the vision.

- **One team –** we work together consistently, promoting co-operation, to achieve our corporate objectives.
- **Customer focused** – we aim to exceed the expectations of our external and internal customers.
- **Results driven** – we take personal responsibility for achieving excellent business results.
- **Creative** – we continuously strive for innovative and better ways to deliver our business.
- **Ethical** – we are open and honest in meeting our commitments, with a responsible approach to the environment and our communities.



PERFORMANCE

In order to measure delivery of the Company business plan and goals, we use a balanced scorecard of Key Performance Indicators (KPIs) covering the full range of our strategic themes.

We set our targets on a path to deliver our national leader vision, which means that they are often more stretching than our regulatory performance commitments. We are pleased that we have shown steady improvement across the majority of our key measures of success and continue to demonstrate industry leading performance in many areas, for example, water supply interruptions. The table opposite details actual performance against the balanced scorecard KPIs and our future targets.

In order to ensure alignment of the management team, this balanced scorecard represents 90% of the criteria contributing to their annual bonus, with a further 10% available for the achievement of bespoke personal targets. Further information about the executive Directors' remuneration is provided in the Statement of Directors' Pay and Standards of Performance on pages 137 to 146 of the APR.

On the table opposite, targets which are measured on a calendar year basis (denoted by C in the table) reflect the performance period January to December 2015. Targets which are measured on a regulatory year basis (denoted by R in the table) reflect the performance period April 2015 to March 2016.

In order to reflect our customers' priorities, we have made one change to the scorecard measures for 2016-17 which is to replace Just an Hour participation with category 1 and 2 pollution incidents.

The targets opposite are internal measures set at stretching levels so as to drive year on year performance improvements. In addition to the KPIs opposite, we measure our performance against each of our outcomes through a range of Measures of Success (MoS). As part of our PR14 FD, some of these measures include Performance Commitments (PCs) and levels of performance that will attract either a reward or penalty at PR19. Table 3A of the APR reports our performance on all of our MoS and shows that we achieved the vast majority of our PCs in 2015-16.

The following sections provide an update on our progress against our business outcomes, grouped under our strategic themes.

STRATEGIC REPORT

ACTUAL PERFORMANCE AGAINST THE KPI TARGETS AND FUTURE TARGETS

		2015-16			2016-17
SCORECARD MEASURE	PERFORMANCE PERIOD	TARGET	PERFORMANCE	ACHIEVED	TARGET
COMPETITIVENESS					
Group EBIT	C	budget	not achieved	no	budget
Group cash available for distribution	C	budget	achieved	yes	budget
CUSTOMER					
Customer satisfaction					
- SIM qualitative score	R	>=4.65	4.38	no	>=4.7
- SIM quantitative score	R	<=85.0	95.7	no	<=80.0
Water supply interruptions >3 hours (average minutes per property)	R	<=5.00	3.20	yes	<=4.00
Mean zonal compliance	C	>=99.9	99.96	yes	>=99.97
Repeat sewer flooding (properties)	R	<=269	82	yes	<=96
PEOPLE					
Employee engagement score	C	>=81%	74%	no	>=81%
Lost time reportable accidents (no.)	C	<=3	7	no	<=3
ENVIRONMENT					
Leakage (Mld)					
- NW	C	<=141	135	yes	<=127
- ESW	C	<=66	62	yes	<=61.8
Pollution incidents category 1 & 2	C	n/a	n/a	n/a	<=1
STW failing LUT consent (%)	C	0	1	no	0
COMMUNITIES					
BITC CR Index	R	4*	4*	yes	4*
Just an Hour (employee participation)	C	>=50%	53%	yes	removed

CUSTOMER

Our aim is to deliver an unrivalled customer experience in line with our vision and values. We measure this through a range of customer surveys, either carried out for the whole sector on behalf of Ofwat or CCWater, or that we commission directly.

SERVICE INCENTIVE MECHANISM (SIM)

Ofwat's SIM measures our customers' experience 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. The SIM measure has changed this year to place a greater emphasis on the quality of the customer experience, from first point of contact to the resolution of the issue, and is now based on customer satisfaction levels for all inbound customer contact to NWL. We welcome this change because we believe customers' views of performance are more representative of customer experience than quantitative measures, such as the number of unwanted contacts.

Our SIM score for 2015-16 was 83.64, placing us fourth of the ten WASCs. This was disappointing as we were placed second after the initial three quarterly surveys but scored lower in the fourth and final wave of surveys. We are reviewing the feedback received very carefully and will take full account of the learning points as we work towards our goal of providing the best customer experience in the industry.

WE PROVIDE EXCELLENT SERVICE AND IMPRESS OUR CUSTOMERS

CUSTOMER SATISFACTION

To satisfy our customers we need to understand what they value in terms of water and wastewater services, complaint resolution and communications. We establish expectations through extensive engagement with customers and ask around 10,000 customers each week what they think of our service.

A high level of customer satisfaction has been confirmed through our quarterly tracking research, undertaken for us by an independent company. Our current customers' overall satisfaction level of 8.5 is the best we have achieved since the research tracking programme started. We also benchmark our customers' satisfaction outside the water industry through our Net Promoter Score (NPS), which measures customer advocacy, the loyalty that exists between us and our customers. Our NPS has continued to improve year on year, improving from +42 to +49 in 2015, ranking us alongside many high profile household names.

OUR CUSTOMERS CONSIDER THE SERVICES THEY RECEIVE TO BE VALUE FOR MONEY

OUR CUSTOMERS ARE WELL INFORMED ABOUT THE SEVICES THEY RECEIVE AND THE VALUE OF WATER

VALUE FOR MONEY

We use two surveys to help us assess whether our customers think we offer good value for money.

Each year CCWater asks customers for their views about the services they receive from their water and sewerage company and the value for money of those services. The most recent national results, published in 2016, showed that a high proportion of customers in the Northumbrian region continued to be satisfied with their water and sewerage services, though satisfaction reduced in the Eastern region, which includes ESW. We are working hard to improve the satisfaction score.

We also commission independent surveys which showed an improvement in the value for money score from 8.1 in 2014 to 8.2 in 2015. In terms of keeping customers informed, at the end of 2015, 94% of our customers told us that they are supplied with all the information they want to feel informed about our services. This has increased by 3% since it was first included in our tracking research in 2014.

LIVING WATER, LOVING CUSTOMERS

During 2015, we have worked with our customers, employees and supply chain partners to develop our new strategy to deliver an unrivalled customer experience, in line with our vision and values. Our strategy, 'Living Water, Loving Customers', expresses our customer service ethos as a core element of our brand and culture. It addresses those areas that our customers have told us are important priorities, including taking personal ownership for customers' problems, keeping our promises, making things easy for customers and showing each customer that they are special.

We are also investing in our systems and processes to support the service that we provide to our customers. During the year, we have invested in a new Voice of the Customer system, which enables customers to provide real time feedback on our customer service. This feedback is then shared with our people at an individual level providing a great opportunity to understand and improve the customer service they offer.

The implementation of our new integrated customer care and billing system is progressing well. This programme of work, which we have called ONCE (Our New Customer Experience), will replace our existing billing, collection and customer contact systems, enhancing our ability to deliver great customer service. We are on track to use the new system to deliver our wholesale operation to business customers upon the opening of the competitive market in April 2017. We will then deliver household billing in October 2017 and operational contact in April 2018.

SUPPORTPLUS

We understand that there are times when some of our customers can find themselves in a difficult financial situation. To help provide the best possible customer service at all times, we have developed a partnership with the national debt charity StepChange, who complement our vision and work creatively with us to deliver against our customers' priorities.

We worked with StepChange to design our SupportPlus tariffs, which we launched in January 2015. These schemes incentivise customers to get back into the payment habit and StepChange provides support, advice and access to these support packages. In 2015 more than 2,000 of our customers received advice and support to help manage debt from StepChange. We continued to expand and develop our activity in this area with our customer teams receiving specialist training from the charity and being able to directly refer customers to StepChange, giving time for the customer to work with StepChange to achieve an action plan and debt solution.

RELIABLE WATER SUPPLY

We have further improved our industry leading performance on minimising water supply interruptions to only 3 minutes and 20 seconds per property served in 2015-16 for interruptions greater than three hours. We achieved this by providing alternative temporary supplies where appropriate and through significantly improved operational response. This was supported by our lowest ever number of water mains bursts. We attribute this improvement to our early proactive interventions to monitor and improve the condition of our water supply network, alongside favourable weather conditions.

The level of leakage from our network was significantly lower than the PCs agreed in our final determination for both our NW and ESW operating areas. We achieved this by monitoring the condition of our network proactively and responding swiftly to water mains bursts.

During 2015-16, 221 properties were classed as experiencing poor water pressure, only slightly higher than our PC of 216. We address properties that fail the pressure standard either within the year in which they fail or through longer term planning or investment. This usually involves the installation of short lengths of additional pipe, small pumping stations, or reconfiguring our water supply network.

LONGER TERM RESILIENCE

The Security of Supply Index (SoSI) measures our capacity to maintain reliable supplies of water in periods of drought. The SoSI for both our operating regions remained at 100% in 2015-16, supported by Kielder Reservoir in our NW region and the extension to Abberton Reservoir in the ESW region.

We have continued to actively promote water efficiency across our operating regions, successfully delivering our whole-town approach called ‘Every Drop Counts’ in Grays, Essex and Berwick upon Tweed, Northumberland. In both locations the higher level of customer awareness led to greater water savings than carrying out single projects in a number of different locations. Our work on water efficiency has again been recognised with awards for our H2eco Analysis research programme, #watersavingselfie social media campaign and Bourne Leisure Holiday Park retrofit scheme at the 2016 Waterwise Awards.

WE PROVIDE A RELIABLE AND SUFFICIENT SUPPLY OF WATER

WE SUPPLY CLEAN, CLEAR DRINKING WATER THAT TASTES GOOD

STRATEGIC REPORT

WATER QUALITY

Our strategy for drinking water quality remains focused on both public health and customer confidence and our overall drinking water compliance remains extremely high at 99.96%. In total we carried out around 128,000 tests companywide at customer taps and only 29 failed to meet strict quality standards, but importantly with no risk to public health. Our aim is to reduce the number of water quality compliance failures further, through a combination of improved water treatment and targeted maintenance of the network.

Another driver of improving water quality performance is our approach to catchment management. We work actively with farmers and other land managers to prevent or reduce pesticides, such as metaldehyde, entering the rivers supplying our treatment works. We have extended our catchment activities to include proactive abstraction management, identifying peaks in pesticides in rivers and reacting quickly to change when we abstract water for our treatment processes. The number of metaldehyde failures has subsequently been significantly reduced from 94 in 2013 to only one in 2015.

CLEAN CLEAR WATER THAT TASTES GOOD

Since 2005 we have had an ongoing programme of work in place with DWI to reduce discoloured water in our NW region. This has been delivered through a major programme of large diameter trunk main cleansing, which will be completed in November 2016, supported by other innovations such as unidirectional district metering area flushing, pipeline management to condition higher risk large mains and the development of two operational training centres. This programme has reduced discoloured water contacts from 14,000 in 2005 to our best ever performance of 2,923 in 2015. We aim to continue with our strategy to improve performance further for our customers through reducing sources of discolouration, such as manganese, and continuing proactive flushing of our network.

The taste and odour of our tap water is really important to our customers. We have undertaken research with our customers and with internal service teams to examine their experiences of taste and odour issues. This has allowed us to carry out a number of initiatives to improve satisfaction, including improvements in treatment and in communication, contributing to a reduction in contact on taste and odour issues in 2015.

SEWER FLOODING

Internal sewer flooding is undoubtedly one of the worst experiences our customers can have and reducing sewer flooding remains one of our highest business priorities. Following on from our strong internal sewer flooding performance in the previous year, we have seen a further reduction in internal, external and repeat flooding incidents across our network in 2015-16. Whilst this improvement in performance is excellent, it is important to note that this is a volatile measure that can be influenced in any year by the extent of wet weather and intense storms. However, we are confident that our work is gradually making our sewerage system more resilient to the extremes of weather.

We have also continued to improve our operational processes to greatly improve the service we provide to our customers following a sewer flooding incident. This includes accelerating the investigation process and providing property protection measures for customers whilst feasibility studies and design work is carried out.

The number of sewer collapses reduced further in 2015-16 and we expect it to continue to be industry-leading when results are published. To reduce the risk from blockages, we have increased sewer lining to address tree root intrusion, sewer cleansing and sewer inspections. We also use bacillius bacteria in some areas of the network to combat fat, oil and grease issues.

We are always looking for innovative ways to educate, inform and engage with our customers. Our 'Love Your Drain' campaign features a character called Dwaine Pipe who we use to improve awareness about the causes of blockages. Working together with our customers in a positive way to change behaviour has had a real impact on reducing the number of unnecessary sewer blockages caused by material such as baby wipes, fats, oils and grease. In particular, our innovative work with schools and food outlets is helping to change customer behaviour. Our research shows that in the first 36 months of the campaign, total blockages were reduced by over 15%.

WE PROVIDE A SEWERAGE SERVICE THAT DEALS EFFECTIVELY WITH SEWAGE AND HEAVY RAINFALL

STRATEGIC REPORT

SUSTAINABLE URBAN DRAINAGE SOLUTIONS

In addition to addressing immediate flooding issues, we are working in collaboration with other stakeholders, such as local authorities and the EA, to promote partnership schemes that will reduce flood risk, as well as delivering wider benefits to local communities and the environment. During 2015-16 we have continued to deliver a number of highly innovative and sustainable solutions to reduce flood risk. Our proactive activity includes sustainable solutions that divert, delay and store rain water to reduce the risk to properties that have been flooded before, as well as delivering flood risk reduction to other properties which are at risk.

Much of this work has been carried out in partnership with other agencies, for example, the Northumbria Integrated Drainage Partnership (NIDP), a partnership between the Company, all 13 Lead Local Flood Authorities in our region and the EA. An example of work delivered through the NIDP approach is a flood risk reduction scheme at Brunton Park in Newcastle, where the innovative solution included the diversion of the River Ouseburn. Our approach has been recognised and we received an Institute of Water (Northern) Innovation Award and won the Utility Week Water Industry Achievement Award 2015 in the category of 'Sustainable Drainage and Flood Management'.

In 2015-16, we have launched our programme of Community Action Plans which aim to proactively deliver flood risk reduction in the most effective manner whilst developing community involvement and promoting partnership working. Our collaborative work with South Tyneside Council and the Wildfowl & Wetlands Trust (WWT) to launch our Sustainable Drainage for Schools initiative recently won the Sustainable Drainage and Flood Management Initiative of the Year at the Water Industry Achievement Awards in May 2016. It features an education programme and the installation of sustainable drainage features to reduce flood risk.

LEADING ASSET MANAGEMENT

We are committed to delivering leading asset management and we adopt best practice as demonstrated by our accreditation to ISO 55001. We use the concept of 'Asset Health' as an innovative way of monitoring, protecting and incentivising the long term sustainable stewardship of our assets. To monitor Asset Health we use two baskets of measures, one for water and one for wastewater. The MoS in our water Asset Health basket are discoloured water complaints, overall drinking water compliance, properties experiencing poor pressure and water mains bursts. The MoS in our wastewater Asset Health basket are sewage treatment works discharge compliance, pollution incidents, sewer collapses and repeat sewer flooding.

As the Asset Health concept is about the long term stewardship of our assets, performance is not assessed annually, but on a three year average basis at each of three assessment points: at the end of 2017-18, 2018-19 and 2019-20. We aim to meet or exceed our PCs for our Asset Health MoS at these assessment points. More information on our performance against the individual measures can be found earlier in this report and in the commentary to Table 3A of our APR.

WE DELIVER WATER AND SEWERAGE SERVICES THAT MEET THE NEEDS OF CURRENT AND FUTURE GENERATIONS IN A CHANGING WORLD

STRATEGIC REPORT

ENVIRONMENT

The environment is critical to us and our stakeholders and we acknowledge our responsibilities to protect and enhance the natural environment.

Our carbon management plan is helping to reduce our carbon footprint and we aim to adopt good environmental practice in all aspects of our activity. Our integrated quality and environmental management systems are certified under ISO 9001, ISO 14001 and OHSAS 18001.

SEWAGE TREATMENT WORKS DISCHARGE COMPLIANCE

Our sewage treatment works (STW) compliance performance has been excellent for a number of years and in 2015-16 there were no STWs failing their discharge consent against the Upper Tier standard. However, we were disappointed to have one site fail against the 'Look-Up Table' permit conditions, our first failure in eight years, which was a consequence of external action taken by a third party.

We are continuing to improve the way we monitor the discharges coming from our STWs, with increased on-line instrumentation and early warning trigger management so that we can resolve problems before there is an impact on the water environment.

POLLUTION INCIDENTS

We saw an increase in the number of reported pollution incidents in the year, partly as a result of changes in reporting mainly affecting pollution incidents recorded from sewage pumping stations. Our strong monitoring approach led to us self-reporting 82% of incidents in 2015.

To improve our performance, we continue to invest in sewer level monitoring technology and trend analysis to aid prediction of where pollution incidents are likely to occur and to detect and resolve problems at a warning level before they cause an overflow. Over 87% of our Combined Sewer Outfalls are now monitored.

In 2015, we reviewed our award winning Water Rangers initiative that encourages members of the public to make regular observations on a watercourse and alert us to any unusual discharges. The Water Rangers deliver real benefits through early identification of pollution incidents, enabling prompt remedial action. We are now planning to extend this initiative to cover additional areas identified as at risk of pollution as well as increasing the number of Water Rangers patrolling our waterways.

WE HELP TO IMPROVE THE QUALITY OF RIVERS AND COASTAL WATERS FOR THE BENEFIT OF PEOPLE, THE ENVIRONMENT AND WILDLIFE

BATHING WATER QUALITY COMPLIANCE

We are very proud that our bathing waters are some of the cleanest in the country. Last year saw the first classifications for designated bathing beaches under the revised Bathing Water Directive with 33 of our 34 beaches meeting the tighter requirements (Sufficient or better) and 30 classed as either Good or Excellent. We have continued to invest in improvements and investigations to identify what we can do to further improve bathing water.

An investigation at Spittal beach, which was classified as Poor, has predicted the beach is likely to return to Sufficient status after the 2016 bathing season. This bathing water is impacted by diffuse agricultural sources and we are working in partnership with the EA, the Scottish Environment Protection Agency and Northumberland County Council to achieve all possible improvements.

ENERGY EFFICIENCY

Our carbon management plan has the aim of reducing our greenhouse gas (GHG) emissions by 35% by 2020 against a 2008 baseline. We remain ahead of target with emissions down by 27% compared to the baseline. However, energy usage in an individual year can be volatile, depending upon levels of rainfall and pumping requirements, and our emissions in 2015-16 increased in comparison with the prior year from 213.6 kilo tonnes CO2e to 225.2 kilo tonnes CO2e. This performance is explained in more detail on page 54 of the Directors' Report.

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 AAD plants. In December 2014, at one plant, we also began to clean and transform the biogas from the AAD process into biomethane for injection to the gas distribution network. Through 2015 this has continued to contribute to the proportion of renewable gas in the national gas grid, supporting the long term sustainability of the nation's gas supply and reducing the carbon footprint of the UK as a whole.

WE PROTECT AND ENHANCE THE ENVIRONMENT IN DELIVERING OUR SERVICES, LEADING BY EXAMPLE

COMPETITIVENESS

The financial performance of the Company is detailed in the financial performance and structure section later in this report.

INNOVATION

Innovation, the successful exploitation of new ideas, underpins our current performance and is the key to our future success. We work in partnership with universities, research organisations and the wider industry to develop and implement leading edge technical solutions, driving the development of, and making best use of, technologies and business processes to achieve our outcomes.

We have a great track record of applying innovative and creative solutions, which is a reflection of the willingness of our people and partners to continuously strive for better and more efficient ways to deliver our business. Examples include exploring opportunities for use of unmanned aerial vehicle technology for asset inspection, the 'porcupine' low cost device for tracing potential sources of non-flushable materials in the sewer network, and the development of a monitor for air valves on sewer rising mains, to identify problems before they result in pipe bursts.

To meet the challenges of delivering our AMP6 (Asset Management Plan) capital investment programme as efficiently and effectively as possible, we have implemented a new operating model in respect of the way we interact with our supply chain. This is based on four key principles, in line with best practice and the UK Government Construction Strategy 2010. These principles are: we operate as a well-informed professional client; we offer clear visibility of, and commitment to, future workload to suppliers; we engage suppliers as early as practicable in the delivery process to add value and innovation; and we create the right environment for collaboration and co-operation, incentivising innovation and performance. We believe that this will enable us to deliver our business outcomes significantly more efficiently than in AMP5.

We use innovative ways of working to drive performance improvement across the business. One example of this is the way we have worked with students from Northumbria University to bring fresh perspectives and ideas to business challenges.

WE ARE THE RETAILER OF CHOICE FOR BUSINESS CUSTOMERS

Whilst only the largest customers currently have the option to switch retailer, we aim to deliver excellent customer service to all of our business customers. Our larger customers receive an account management service providing a single point of contact for all their needs and we collect regular feedback from these customers to ensure that this service is meeting their requirements. This feedback gives us a positive NPS of 32 for this specific activity.

We have continued our preparations for the opening of the competitive market for non-household retail services in April 2017 and have invested in a new customer system that will underpin the core processes of the market, including the billing of non-household customers. NWGL intends to actively compete in this market and its separate subsidiary, NWGBL, will seek to enter the market as a retailer.

WE ARE AN EFFICIENT AND INNOVATIVE COMPANY

STRATEGIC REPORT

PEOPLE

EMPLOYEE SATISFACTION AND ENGAGEMENT

We put great effort into creating an environment where our people are encouraged to engage and perform to the best of their ability. We engage with our employees through our Employee Relations Framework and through a range of communication channels including annual director roadshows, structured team talk briefings every two months, our weekly H2info ebulletin, and digital tools such as our intranet and Yammer. To recognise the contribution of our people, who bring our vision and values to life every day in the way they do their jobs, we have continued to grow our internal employee Vision and Values Awards, known as the ViVa Awards. In 2015-16, 314 people and teams were nominated by colleagues for demonstrating our company values and our winners were celebrated at an awards ceremony in June 2016.

We continue to take a lead role to develop skills at a national level in response to the Government's Employer Ownership of Skills pilot and review of apprenticeships and we have pioneered the new Trailblazer approach to apprenticeships in the water industry. We are strongly represented in the Energy and Efficiency partnership, an important sector-wide skills initiative, which has focused in 2015 on developing employability with young people. Each year we support around 9,000 young people through schools, colleges and universities by providing opportunities to develop their experience and skills, and we have continued to provide apprenticeships, graduate placements and sponsored higher education programmes.

In January 2015 we began a consultation regarding proposed changes to our defined benefit pension scheme, of which about half our workforce are members. As a result of the feedback received during consultation the Company made significant changes to the final outcome, which was implemented in January 2016. We really value the feedback that we received during the consultation and we continue to take the opportunity to work with our people to improve our employee relations framework.

Our annual employee survey was carried out after the end of this consultation process and the resulting engagement and satisfaction index score was below our target. However, there were still some very positive messages in the survey results with 74% of employees proud to work for the Company and 84% of our people enjoying their job.

In November 2015 we were accredited as a Living Wage Employer. This means that every employee in the Company will earn at least the Living Wage, an hourly rate set independently and calculated according to the basic cost of living for the UK. As part of this commitment, the Living Wage will also be extended to people who work for third party contractors and suppliers over time as contracts are awarded or renewed.

DIVERSITY AND EQUAL OPPORTUNITIES

We have continued throughout the year to ensure that our people are fairly treated and we proactively promote diversity and inclusion to reap the benefits of a diverse workforce. 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.

At the end of the year, the Company had 3,139 employees of which 2,110 were male and 1,029 female. Of the 12 Directors, 10 were male and two were female. The Executive management team has an even split of five male and five female members.

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.

OUR PEOPLE ACT IN LINE WITH OUR VALUES

OUR WORKPLACES ARE HEALTHY AND SAFE

The H&S of our employees and contractors is a responsibility that we take very seriously and whilst we were pleased that lost time accidents stabilised at a low level during 2015, maintaining the improvement in accident performance achieved in 2014, our ambition is to have no accidents. We are certified under OHSAS 18001 Occupational Health and Safety Systems and our first surveillance assessment under a new certification arrangement identified few minor non-conformances.

We have been awarded the Royal Society for the Prevention of Accidents (RoSPA) Gold Medal Award in recognition of achieving the RoSPA Gold Award for five consecutive years. The RoSPA Gold Award recognises organisations which have achieved a high level of performance and demonstrated well developed occupational H&S management systems and culture.

The wellbeing of our workforce is key to maintaining good levels of attendance and to support engagement with the Company. This year we have developed a strong network of Wellbeing Champions and mental health first aiders and we continue to benchmark to ensure we remain at the forefront of best practice. We were pleased that an assessment by the Trade Union Congress recognised our continued progress by awarding us a Gold standard in the Better Health at Work Award.

OUR PEOPLE ARE TALENTED, COMMITTED AND INSPIRED TO DELIVER GREAT SERVICES TO CUSTOMERS

COMMUNITIES

We are dedicated to building strong relationships with the communities we serve and we ensure that corporate responsibility is embedded in the business.

In 2015 we continued to ensure that at least 1% of our pre tax profits were re-invested in our communities through dedicating expertise, employee time, money and facilities.

JUST AN HOUR

Just an Hour is our highly successful employee volunteering programme which takes our community support beyond just cash donations, utilising the wealth of knowledge, skills and expertise of our employees. This is a structured programme of employee involvement in the community designed to impact on education, the environment and the general wellbeing of the community.

Since the launch of Just an Hour in 2002, our employees have committed more than 100,000 hours in support of the communities we serve and more than half of our workforce are actively engaged in the programme, supporting 979 organisations with volunteers in 2015.

PARTNERSHIPS

We are proud of the long history we have of successfully working in partnership with a range of organisations and the help this enables us to give our communities and the local environment. We work with organisations across a broad range of sectors, including business, charitable, historical, cultural, educational and environmental bodies. Our work in our communities is based on our Partnerships Strategy, which gives a clear direction to ensure we are focusing our efforts on the things that our customers have told us are most important to them. This work is detailed in our Annual Partnership report, available on our websites.

Our work in this area has contributed to us being listed in 2015 as one of the world's most ethical companies by Ethisphere. This is the sixth consecutive year we have been listed and we remain the only water and sewerage company in the world to be included on this prestigious list.

WE WORK IN PARTNERSHIP TOWARDS COMMON GOALS

WE ARE PROUD TO CONTRIBUTE TO THE SUCCESS OF LOCAL COMMUNITIES

GRASSROOTS SUPPORT

In addition to our larger flagship partnerships, we also provide effective grassroots support to a large number of organisations in our community, this year supporting over 1,570 community initiatives. Key events that we have supported, including Lumiere in Durham and the Tour of Northumberland, have contributed an additional £9m to the local economy.

Supplying top quality tap water that is great value for money is integral to what we do and we are pleased to provide our very own bottled tap water to charities and not for profit groups for use at outside events. Since starting the scheme in 2005, we are proud to have provided more than one million bottles of water to support community events.

Four Community Foundations hold endowment funds that are used to support a range of community and charitable activities across our areas of supply. These are long term investments with the income from the funds being donated, with the advice of the Community Foundations, by a committee of our people.

Our Branch Out fund helps to deliver projects that benefit the natural environment and our local communities. This is about working in partnership to reconnect habitats for the benefit of people and wildlife. In 2015, through Branch Out we supported a variety of partners with 21 projects providing close to £80,000 in funding. This funding has unlocked almost £900,000 in match funding for our partners.

WE ARE A COMPANY THAT CUSTOMERS CAN TRUST

WATERAID

Northumbrian Water was one of the water companies that set up the international charity WaterAid in 1981 and our fundraising committee volunteers have raised millions of pounds since then. WaterAid transforms lives through providing safe water, sanitation and simple hygiene education and we continue to support the charity as one of our strategic partners. In 2015, our CEO, Heidi Mottram, went to Malawi to see for herself what WaterAid achieves for some of the world's poorest people.

In 2015, Northumbrian Water raised funds which will give over 13,000 people in developing countries access to clean water. We also launched a new five-year partnership with WaterAid aiming to raise £1m to support the delivery of clean water and safe toilets to some of Madagascar's poorest communities. In doing so, we will be helping to bring clean water and sanitation to over 70,000 people.

TRUST

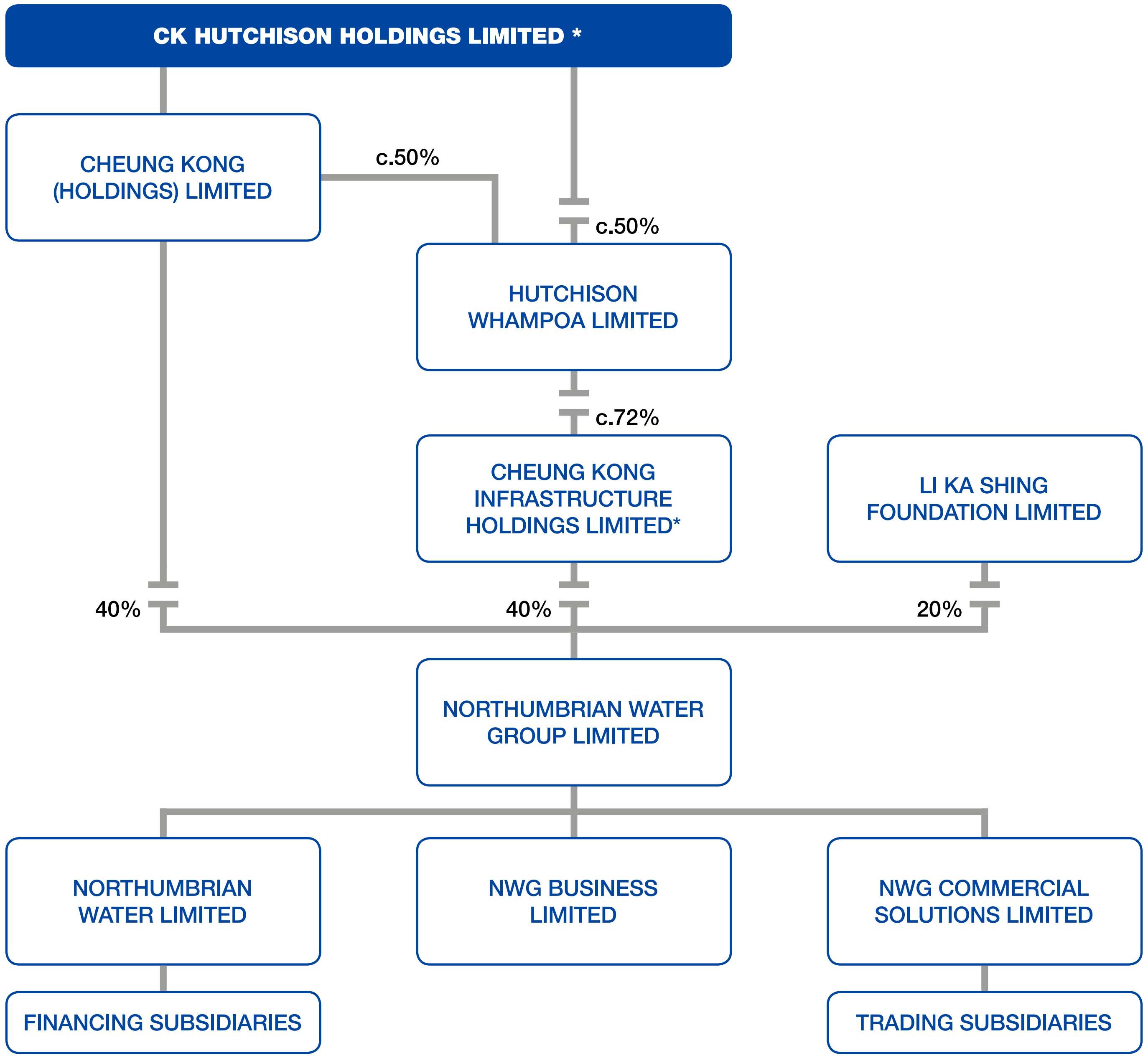
Each year CCWater asks customers for their views about the services they receive from their water and sewerage company and we are proud that for the second year running, that survey has named us as the most trusted water company. We have robust governance and assurance arrangements in place to ensure that when we publish information it is accurate, clear and transparent. In doing so we aim to continue to build trust and confidence with our customers and stakeholders.

FINANCIAL PERFORMANCE AND STRUCTURE

GROUP STRUCTURE

NWL is a wholly owned subsidiary of NWGL. NWGL has two other direct subsidiaries, NWGCSL, which acts as a holding company for other non-regulated trading companies, and NWGBL, which carries out retail activities in Scotland and to which NWL's current non-household customer base will transition at the opening of the market in April 2017.

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 (the Group) up to CKHH. The chart shows the principal intermediate holding companies, which are wholly owned unless otherwise shown.



* Companies listed on the Hong Kong Stock Exchange

STRATEGIC REPORT

FINANCIAL PERFORMANCE

In addition to the Balanced Scorecard, we use a range of financial indicators to monitor performance. All of our financial KPIs below remained better than the target for the year.

		PERFORMANCE		TARGET
KPI	TARGET 2015-16	2015-16	2014-15	2016-17
Gearing: net debt to RCV – NWL group[1]	<72%	70%	68%	<72%
Cash interest cover (times) – NWL group	>3.0	4.8	3.3	>3.0
Cash flow to net debt (%) – NWL group	>13	19	20	>13

[1] See note 10 of the Statutory Financial Statements

The Company's income statement, statement of comprehensive income, balance sheet and statement of changes in equity are set out on pages 60 to 64. The statutory financial statements have been prepared on an historical cost basis in accordance with FRS 101, reflecting IFRS with reduced disclosures. The key accounting policies are summarised in note 1 to the statutory financial statements on pages 65 to 69 and have been applied consistently to current and preceding period information. Further information on the transition to FRS 101 is provided in note 24 of the Statutory Financial Statements.

During 2014, the Company changed its accounting reference date from 31 December to 31 March, therefore prior period values relate to a 15 month period and are not directly comparable to the current year values which reflect 12 months trading. However, after adjusting for exceptional items, the underlying operating profit for the current year is broadly in line with the underlying performance in the previous period.

Revenue was £805.5m for the year ended 31 March 2016 (15 months ended 31 March 2015: £985.3m). Wholesale charges were set in line with the PR14 FD, increased by RPI of 2.6% with effect from April 2015. Table 2I of the APR reports that wholesale revenue was £4.5m higher than the FD and explains the difference.

Operating costs, including capital maintenance costs, for the year ended 31 March 2016 were £432.8m (15 months ended 31 March 2015: £588.6m). This included an exceptional one-off accounting credit of £38.9m related to changes to a defined benefit pension scheme which came into effect in January 2016 after consultation with members. The prior period included an exceptional one-off asset impairment charge of £30.7m in relation to sludge drying plant abandoned as a result of the successful implementation of AAD. Both of these items are explained further in note 3 of the Statutory Financial Statements.

Underlying costs, excluding exceptional items and with prior period costs pro-rated to a 12 month basis, have increased in the year. This reflects general inflationary pressures, including staff costs, higher pension charges, higher power usage in the year and increased depreciation resulting from our capital investment programme. We are also choosing to address some issues with opex solutions which may previously have been addressed through capital investment, notably in respect of SuDs, sewer flooding mitigation and our catchment management approach.

Net interest payable was £106.3m in the year ended 31 March 2016 (15 months ended 31 March 2015: £138.1m). Whilst the charge was naturally lower due to the shorter accounting period, this was further reduced by lower charges on index linked debt due to lower levels of prevailing RPI during the year, partially offset by interest received in the prior year on tax recoverable as a result of prior period capital allowances claims agreed with HM Revenue & Customs (HMRC).

Profit on ordinary activities before taxation for the year ended 31 March 2016 was £266.4m (15 months ended 31 March 2015: £258.6m). Current tax for the year ended 31 March 2016 was a charge of £33.3m (15 months ended 31 March 2015: credit of £17.1m). The prior period included exceptional credit adjustments of £64.5m in respect of prior period capital allowances claims agreed with HMRC. Deferred tax for the year ended 31 March 2016 was a credit of £29.8m (15 months ended 31 March 2015: credit of £4.5m), reflecting a reduction in deferred tax liabilities due to changes in future corporation tax rates enacted during the year. The current tax credit and deferred tax charge are explained in more detail in note 7 of the Statutory Financial Statements. Profit for the year ended 31 March 2016 was £262.9m (15 months ended 31 March 2015: £280.2m).

The Directors do not recommend payment of a final ordinary dividend (31 March 2015: £nil). Total dividends paid in the year ended 31 March 2016 were £211.0m (15 months ended 31 March 2015: £311.5m). As a result of the change in the Company's statutory accounting reference date, the timing of dividend payments was amended in the prior period which resulted in three interim dividends being paid compared to two in the current year. The underlying dividend policy has remained unchanged and is explained in note 8 of the Statutory Financial Statements.

STRATEGIC REPORT

CAPITAL INVESTMENT

Total fixed asset additions in the year ended 31 March 2016 were £223.2m. Around £156m 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 particular, we have continued to invest heavily in our sewer network to reduce the risk of sewer flooding.

We commenced the ONCE programme to transform our billing and customer contact systems for household customers and in readiness for the opening of the non-household retail market. We also started work on two of our most significant AMP6 projects, the upgrade of Horsley water treatment works, which serves Newcastle, and addressing sewage spills at Whitburn, to ensure timely delivery of benefits and outcomes.

CAPITAL STRUCTURE AND LIQUIDITY

The Company's long term debt structure remained largely unchanged with 62% fixed at an average rate of 5.71%, 30% index linked at an average real rate of 1.27% and 8% on a variable rate basis. The blended average nominal rate for the Company for the year ended 31 March 2016 was 4.39% (15 months ended 31 March 2015: 4.82%).

In September 2015, the European Investment Bank (EIB) approved a new £250m loan facility, to support our AMP6 capital plan, with a £150m tranche available immediately and the remaining £100m tranche to be available for drawdown in 2017. The initial £150m was drawn in October 2015 on a variable rate basis and swapped through to index linked at a favourable real rate of -0.22%.

We have a committed five year bank facility in place to maintain general liquidity, with a total value of £350m maturing in 2019. This was undrawn at 31 March 2016. Looking ahead, we are currently developing our strategy for the refinancing of a £300m bond, which matures in October 2017.

Gearing increased slightly as a result of adjustments made to the opening RCV in the PR14 FD but remains within target. Cash interest cover and cash flow to net debt ratios remain comfortably better than target. The Company retains strong investment grade credit rating of BBB+ from Standard & Poors (S&P) and Baa1 from Moody's. Our Fitch rating arrangement was terminated in the year as it was no longer efficient to maintain three corporate ratings.

Whilst the S&P rating outlook remains stable, in January 2016 Moody's changed its outlook to negative from stable, citing potential concerns about the gearing levels of our parent company, NWGL, in spite of also recognising the strength of the regulatory ring-fence. We report on our financial resilience in our viability statement on page 55.

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 our strong investment grade credit rating at BBB+ (Standard & Poors) and Baa1 (Moody's). 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 2016, NWL had £350m (31 March 2015: £258m) of undrawn bank facilities, provided by a group of five key relationship banks, which mature in 2019.

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 2016, 62% (31 March 2015: 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(o) of the Statutory 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 2016, the Company had forward foreign exchange contracts of £5.8m (31 March 2015: £2.7m) 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.

PRINCIPAL RISKS AND UNCERTAINTIES

The Board sets the tone for risk management within the Company and determines the appropriate risk appetite. The Board's approach to monitoring, managing and mitigating risk is set out in the Governance Report.

The Risk & Compliance 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 risks identified by the Board. The principal business risks facing the Company, and our approach to mitigating these risks, are set out in the table below.

DESCRIPTION OF RISK	MITIGATION	CHANGE
Health & safety Whilst our health and safety performance is strong, we can never be complacent and remain conscious of the significant inherent risk in our operational and construction workplaces.	The health and safety of our staff, contractors and members of the public is our highest priority, and our leading indicators are reported quarterly to Management Team and Board along with actions to ensure continuous improvement. Health and safety is embedded in our culture and processes through training, clear procedures and guidelines, risk assessments and regular inspections. All accidents and incidents are investigated and closure of recommendations tracked.	No change (continuous improvement).
Water service failure A problem in our water system causing either a major loss of supply or unfit water to be supplied. This could have many potential causes, including the failure of a strategic water main or treatment works or contamination of a service reservoir.	We have well developed business continuity plans in place for managing incidents, down to a site specific level, which are regularly tested. We operate risk-based prioritisation process for the maintenance and replacement of our assets, which is ISO 55001 certified. Access is restricted to treated water assets through authorisation and physical security measures.	No change.
Sewerage service failure A problem in our sewerage system causing either significant environmental pollution or customer impact. This could have many potential causes, including insufficient network capacity to cope with severe weather events and consequences of sewer collapses or blockages.	We continue to invest heavily in preventing sewer flooding and pollution through a wide range of approaches including proactive monitoring and sewer cleaning, mitigation, prevention through SUDS and public education, and investment to increase network capacity (see pages 22 to 23 for more detail).	No change.

Table continued on next page

DESCRIPTION OF RISK	MITIGATION	CHANGE
Information management failure Loss of key business systems due to a malicious attack or failure of cyber security. Release of sensitive data in breach of the Data Protection Act or Environmental Information Regulations. Loss of billing data integrity during transition to a new billing system for household customers.	Continuous improvement of information security controls though software and hardware access controls, infrastructure resilience and disaster recovery plans. Focus on user awareness through briefings and training, supported by a dedicated internal team. Strong programme management of new billing system under same governance structure as non-household retail competition (described below).	No change to existing risks. Billing system transition has been added.
Regulatory changes Changes to the Licence or regulatory methodology that may adversely impact on the balance of risk and return or reduce investor confidence in the stability and predictability of the regulatory framework.	Externally driven, but we actively engage with Ofwat through responding to formal consultations, regular direct dialogue, contributing to the 'market for ideas' and through other forums such as Water UK.	Change through the development of Water 2020 approach.
Retail competition Difficulties with the opening of the non-household retail market. Potential introduction of household retail competition unsupported by clear benefits.	Our preparations for non-household retail market opening are well advanced and supported by robust governance arrangements with wholesale and retail programme boards reporting into a Management Team sub-group and the Assurance Committee. External assurance has been provided by PA Consulting and Deloitte LLP. We have contributed to Ofwat's call for evidence in respect of their assessment of the costs and benefits of household retail competition.	Reduced risk for non-household competition as preparations have progressed. New risk in respect of potential household competition.
Funding and liquidity risk Inability to access future funding at acceptable rates, credit rating downgrade or loss of liquidity.	The Board has approved treasury policies which set out how we manage treasury risks (see pages 34 to 35). We are committed to maintaining our strong investment grade credit ratings and manage our financial plans accordingly (see viability statement on page 55). Management is monitoring the uncertainty in the financial markets following the UK voting to leave the EU.	Increased risk due to uncertainty in financial markets after EU referendum result.
Financial performance Failure to deliver financial plans due to significant adverse movements on costs, interest or tax or failure to deliver efficiency commitments. Impact of sustained low RPI on RCV and gearing.	We have committed to a range of efficiency actions, for both opex and capex, and progress is reported monthly to Management Team. 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. Our viability statement on page 55 reports on the financial resilience of our plan.	Increased risk due to the low level of prevailing RPI.

NEW RISKS

As part of their assessment of principal risks, the Risk & Compliance Committee decided that the inherent health and safety risk, and potential seriousness of any incidents, should be added to the principal risks, though they agreed that the Company's management processes were strong in this area. The Committee also added the risk of failing to deliver our financial plans, recognising the impact of the sustained period of prevailing low RPI inflation on our business model. The retail competition risk has been extended to incorporate the proposal by government to introduce household competition by 2020, announced in November 2015.

As noted in the table on page 37 the Board is monitoring the uncertainty in the financial markets following the UK voting to leave the EU and assessing potential impacts on the Company.

INCREASING RISKS

The risk of unfavourable regulatory changes at PR19, specifically in relation to moving from RPI to CPI inflation for some items, has increased as Ofwat has developed its Water 2020 approach.

REDUCING RISKS

Our preparations for non-household retail market opening are progressing well within a robust governance and assurance framework.

MParker

By order of the Board
M Parker, Company Secretary,
15 July 2016

GOVERNANCE REPORT

FOR THE YEAR ENDED 31 MARCH 2016

GOVERNANCE REPORT

DIRECTORS

The Directors who served during the year were as follows:

NAME	ROLE
A J Hunter	Non-Executive Chairman
P Rew	Senior Independent Non-Executive Director
H Mottram OBE	Chief Executive Officer
C I Johns	Finance Director
A C Jones	Assets and Assurance Director
M Fay CBE	Independent Non-Executive Director
Dr S Lyster	Independent Non-Executive Director
M A B Nègre	Independent Non-Executive Director
F R Frame	Non-Executive Director
T C E Ip[1]	Non-Executive Director
H L Kam	Non-Executive Director
D N Macrae	Non-Executive Director
L S Chan[2]	Alternate Non-Executive Director
W C W Tong-Barnes	Alternate Non-Executive Director

[1]T C E Ip resigned from the Board on 14 July 2016.
[2]L S Chan was appointed as a Non-Executive Director on 14 July 2016.

Information about Directors' remuneration is contained in note 4 of the Statutory Financial Statements and the Statement on Directors' Pay and Standards of Performance in the APR.

SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR'S REPORT

As Senior Independent Non-executive Director I am pleased to be able to describe the role of NWL's INEDs, on whose behalf I can fully endorse the comments of our Chairman, Andy Hunter, in his statement.

Paul Rew

As mentioned by the Chairman, the INEDs play a key role in NWL's governance, assurance and decision making. I chair the Audit Committee, the Assurance Sub-Group (which I explain below) and the Risk & Compliance Committee; fellow INEDs sit on both of those Committees, the Assurance Sub-Group and the Remuneration Committee. 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. Whilst the Committees are not entirely comprised of INEDs, as suggested by the UK CGC, the Board believes that their composition is appropriate to the Company's circumstances. The three members of the Assurance Sub-Group are all INEDs.

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. In order to sharpen the focus on assurance, the Audit Committee invited the Assurance Sub-Group to closely review (i) NWL's preparations for the opening of the non-household retail market; and (ii) NWL's major transformation project to procure a new billing system and facilitate working with MOSL once the market opens. This has involved three meetings with management and independent assurance providers and has enabled the Board to achieve a high degree of confidence that these projects are being delivered to a high standard.

Most decisions relating to NWL are made by the NWL Board alone and the only decisions referred to the NWGL Board are 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 are present at its Board meetings and participate fully, which encourages a cohesive approach at both Boards.

I would like to emphasise that, in addition to our work on assurance and our participation in formal meetings, the INEDs have had very broad involvement in NWL's overall business. We have all taken part in extensive sessions with management on risk and customer service and have already met with the new Chairman of our Water Forums. We have also met from time to time without management or the other directors being present and attended seminars arranged by Ofwat and other events relating to the water sector.

I remain satisfied that the balance of experience and expertise on the Board of NWL, its Committees and the Assurance Sub-Group ensures that the interests of all the Company's stakeholders, and especially customers, are protected and that the Company's governance is both sound and appropriate.

P Rew
Senior Independent
Non-Executive Director

CORPORATE GOVERNANCE

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, beyond those which would otherwise apply to a private company, 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 bespoke Governance Code (the NWL Code), which the Board put in place in March 2014, following discussions with Ofwat.

The arrangements and functioning of the Board and its Committees have regard to the Licence obligations, the UK CGC and the NWL Code, in the context of a company which is not a listed public limited company. The Board considers that an appropriate balance has been achieved between the interests of shareholders, customers and other stakeholders.

The Board considers that it complies substantially with the relevant provisions of the UK CGC, to the extent that it is compatible with NWL's ownership structure, except as explained on page 53. Compliance with the NWL Code is reported on page 53.

BOARD RESPONSIBILITIES AND PROCESSES

The Board sets, implements and supports the Company's vision, values and strategy and ensures compliance with Group policies and legal and regulatory obligations. Within the Group framework, NWL operates as a standalone company and its strategy is determined solely by the NWL Board. During the year, the only decisions referred to the NWGL Board were certain large contract awards, capital project approvals and substantial funding arrangements and, in each case, the NWGL Board accepted the recommendations of the NWL Board.

The Board receives detailed reports from the Executive Directors in advance of Board meetings, covering each aspect of the Company's activities. The first substantive item on each Board agenda is health and safety; this is the Board's top priority and the Company's health and safety record is excellent (see page 29 for details). There are also regular reports on operational performance, customer service, 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 Strategic Report. The Chairman of the Audit Committee and Assurance Sub- Committee reports fully to the Board on their work.

The Chairman 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. The Board recognises that customers' interests are best served when the Company is flexible and innovative, so the Executive team 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 and management. The Board makes key strategic decisions and approves the annual and medium term business plans. It also approves 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.

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.

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

BOARD BALANCE AND INDEPENDENCE

The composition of the Board is as follows:

A J Hunter (Non-Executive Chairman) joined the Board in October 2011. He was appointed by Cheung Kong Infrastructure Holdings Limited (CKI), which is listed on the Hong Kong Stock Exchange and is a substantial shareholder in the Group. A J Hunter is Deputy Managing Director of CKI and 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. He 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 and a Master's degree in Business Administration. He is a member of the Institute of Chartered Accountants of Scotland and of the Hong Kong Institute of Certified Public Accountants. He is Chairman of NWGL's Remuneration Committee.

P Rew (Senior Independent Non-Executive Director) joined the Board in 2010. He 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. He is a Non-Executive Director of DEFRA and the Care Quality Commission and chairs their Audit Committees, and was formerly a Non-Executive Director of the Met Office. He is Chairman of NWGL's Audit Committee and Risk & Compliance Committee and is also a member of the Remuneration Committee.

H Mottram (CEO) joined the Board in 2010, when she was appointed as CEO of NWL and NWGL. Prior to her current position, Ms Mottram held a number of senior management roles, including Managing Director of Northern Rail Limited, Commercial Director of Arriva Trains, and Operations Director of Midland Mainline as well as various senior positions in Great North Eastern Railway. She is a Non-Executive Director of Eurostar International Limited and a Board Member of the North East Local Enterprise Partnership. She is also a Board Member of Kielder Water and Forest Park Development Trust, as well as a member of the CBI Board, Newcastle University Council and the Institute of Water. Ms Mottram was named Rail Business Manager of the Year in 2009 for being an "inspirational leader", she was awarded an OBE in the New Year honours list in 2010 for services to the rail industry, and is also the Prince of Wales' Ambassador for Business in the north east of England.

C I Johns (Finance Director) joined the Board in 2013. He was previously Finance Director of Northern Gas Networks Limited (NGN) since 2005, which is also part of the Cheung Kong Group. Before joining NGN, C I Johns worked in the financial services sector. He is a Chartered Accountant and has held senior financial management positions in both Yorkshire and London. His 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.

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

M Fay (Independent Non-Executive Director) joined the Board in 2010. She was Managing Director of Tyne Tees Television until December 2003 when she became Chairman of One North East, a position she held until August 2010. She is Deputy Chairman of The Sage Gateshead, a Governor of the University of Sunderland, Patron of Tees Valley Community Foundation and a Deputy Lieutenant for Tyne and Wear. M Fay is a member of NWGL's Remuneration Committee.

Dr S Lyster (Independent Non-Executive Director) joined the Board in 2006. He is a lawyer by training, qualified in both the UK and the USA and 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 the World Land Trust and a Trustee of Conservation International-UK, the Kilverstone Wildlife Conservation Trust and the Rural Community Council of Essex. In July 2014, Dr Lyster was appointed to the Board of Natural England. He is a member of NWGL's Audit Committee and Risk & Compliance Committee.

M A B Nègre (Independent Non-Executive Director) joined the Board in 2006. He 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. He was a founding Director of NWGL when it acquired the Group from Suez SA in 2003. He currently chairs Ecofin Vista Hedge Fund Limited, is a Non-Executive Director of listed Investment Trust EW & PO plc and holds a number of Directorships focused on utilities. He sits on the supervisory board of Messieurs Hottinger & Cie. M A B Nègre is a member of NWGL's Audit Committee and the Risk & Compliance Committee.

L S Chan (Non-Executive Director) joined the Board in 2016. He was appointed by CKH and has been an Executive Director of CKI since January 2011 and Chief Financial Officer of CKI since January 2006. He 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).

F R Frame (Non-Executive Director) joined the Board in November 2011 and was appointed by Li Ka Shing Foundation Limited, a company limited by guarantee and a charity which is a substantial shareholder in the Company. 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, Baxter International Inc and Consolidated Press International Limited. He holds the degrees of Master of Arts and Bachelor of Laws.

T C E Ip (Non-Executive Director) joined the Board in October 2011 and resigned in 2016. He was appointed by CKH, of which he is Deputy Managing Director, a well as being Deputy Chairman of CKI and Deputy Managing Director of CKHH. T C E Ip has been an Executive Director of CKI since its incorporation in May 1996 and its Deputy Chairman since February 2003. T C E Ip is Senior Vice President and Chief Investment Officer of CK Life Sciences Int'l., (Holdings) Inc., a Non-Executive Director of TOM Group Limited, ARA Asset Management Limited, AVIC International Holding (HK) Limited, Real Nutriceutical Group Limited and Shougang Concord International Enterprises Company Limited. T C E Ip is also a Non-Executive Director of a number of companies which manage significant listed real estate investment trusts. He holds a Bachelor of Arts degree in Economics and a Master of Science degree in Business Administration.

H L Kam (Non-Executive Director) joined the Board in October 2011. He was appointed by Cheung Kong (Holdings) Limited (CKH), which is a substantial shareholder in the Company and is now wholly owned by Cheung Kong Hutchison Holdings Limited (CKHH). He is Group Managing Director of CKI and Deputy Managing Director of CKHH. H L Kam has been Group Managing Director of CKI since its incorporation in May 1996. He has also been Deputy Managing Director of CKH since February 1993. He is President and Chief Executive Officer of CK Life Sciences Int'l., (Holdings) Inc., and an Executive Director of Hutchison Whampoa Limited and Power Assets Holdings Limited. Mr Kam is also Chairman of Hui Xian Asset Management Limited, which manages Hui Xian Real Estate Investment Trust, a listed real estate investment trust. He holds a Bachelor of Science degree in Engineering and a Master's degree in Business Administration.

D N Macrae (Non-Executive Director) joined the Board in October 2011. He was appointed by CKI, where he holds the position of Head of International Business. D N Macrae has over 22 years of 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 NWGL's Audit Committee, Risk & Compliance Committee, and Remuneration Committee.

The Chairman and CEO have clearly defined roles and responsibilities. The Chairman leads the Board and creates the conditions for overall Board and individual Director effectiveness, both inside and outside the boardroom. The CEO is responsible for running the Company's business on a day-to-day basis. A J Hunter, D N Macrae, H L Kam, T C E Ip, F R Frame and H Mottram were also Directors of NWGL in the year.

The Non-Executive Directors bring to the Board many years of business experience as well as financial expertise and the ability and willingness to constructively challenge and help develop proposals on strategy.

The General Counsel and Company Secretary, M Parker, assists the Board to ensure that good corporate governance compliance is achieved. He is also Company Secretary of NWGL and is secretary to all Board committees.

ATTENDANCE AT BOARD MEETINGS

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

NAME	ATTENDANCE
A J Hunter	5
P Rew	5
H Mottram OBE	5
C I Johns	5
A C Jones	5
M Fay CBE	5
Dr S Lyster	5
M A B Nègre	5
F R Frame	5
T C E Ip	1*
H L Kam	4
D N Macrae	5

* During the year it has been difficult for T C E Ip to attend Board meetings in the UK. Mr Ip resigned from the Board on 14 July 2016 and L S Chan, who has been an alternate Director since October 2011, has replaced him. Mr Chan attended four of the five meetings during the year.

RISK MANAGEMENT AND INTERNAL CONTROLS

The Board has ultimate responsibility for risk management 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 monitors the management of fundamental risks and approves major decisions affecting the Company's risk profile. The Board is supported in this by the Risk & Compliance Committee, as explained below.

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, being potentially high impact risks which are foreseeable but with a high degree of uncertainty.

The Management Team implements policies on risk management and internal control and ensures that risks are appropriately identified and managed within the business. This approach is set out in a Risk Management Framework, which has been endorsed by the Risk & Compliance Committee. The Management Team 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 Risk & Compliance Committee, 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, future performance, solvency or liquidity. These principal risks, and how they are managed, are described on page 36 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 Audit Committee in monitoring the effectiveness of the internal control framework with primary assurance being provided by the Internal Audit team.

EFFECTIVENESS OF RISK MANAGEMENT AND INTERNAL CONTROL SYSTEMS

The Risk & Compliance Committee, 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 and its 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.

BOARD COMMITTEES

During the year, the NWGL Board had Audit, Risk & Compliance and Remuneration Committees to assist it in the performance of its duties. The Board sets the terms of reference of the Committees and receives regular reports from their chairmen at Board meetings.

AUDIT COMMITTEE

The role of the Audit Committee is to assist both Executive and Non-Executive Directors of Group companies to discharge their individual and collective responsibilities in relation to:

- Ensuring the financial and accounting systems of each Group company are providing accurate and up-to-date information on its current position;
- Ensuring the Group's published financial statements represent a true and fair reflection of this position;
- Ensuring the integrity of the Group's regulatory reporting systems and the accuracy of its regulatory reports; and
- Assessing the integrity of its internal financial controls.

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

The members of the Audit Committee are P Rew (Chairman), Dr S Lyster, M A B Nègre, D N Macrae and L S Chan.

During the year, and up to the date of approval of these financial statements, the Audit Committee assisted both Executive and Non-Executive Directors to discharge their individual and collective responsibilities. Its work included the following:

- Reviewing the draft financial statements and APR, considering reports from the external auditor setting out the audit approach and plan, significant audit risks and conclusions on the Group's internal controls and risk management;
- Reviewing the appropriateness of accounting policies, significant accounting judgements and evidence supporting the going concern basis for the accounts and recommending approval of the Statutory Financial Statements to the Board;
- Reviewing and commenting on the APR, including the underlying assurance, reviewing evidence to support the Condition F6A.2A certificate (statement of sufficiency of financial resources) and recommending its approval to the Board;
- Monitoring the effectiveness of the internal audit function;
- Approving the external auditor's fees for both audit and non-audit services, by reference to the agreed policy;
- Approving the internal audit work programme for the year and reviewing progress against the programme;
- 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
- Reviewing the risk and control framework and reporting, including management of tax compliance matters and approval of financial approval rules.

The Audit Committee Chairman reports formally to the NWGL and NWL Boards following each Audit Committee meeting and its minutes are circulated to both Boards.

Attendance at the four scheduled Audit Committee meetings during the year was as follows:

NAME	ATTENDANCE
P Rew	4
Dr S Lyster	4
M A B Nègre	4
D N Macrae	4
L S Chan	3

Given the increasing need for careful and thorough assurance of a number of NWL's key projects, to ensure compliance, efficiency and excellent customer outcomes, during the year the Audit Committee has formed an Assurance Sub-Group whose three members are all INEDs.

Although the Sub-Group has a broad remit, its work during the year has focused on NWL's preparations for the opening of the non-household retail market and NWL's major transformation project to implement a new billing system to enable NWL to work with MOSL after market opening and, at a later date, manage household customer billing and contact. The Sub-Group has held three meetings with Executive Directors, senior management and independent assurance providers during the year and attendance was as follows:

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

In anticipation of the opening of the non-household retail market in April 2017, the Board proposes to establish a separate NWL Audit Committee, to be supported by an NWL Assurance Sub-Committee. NWGL's Audit Committee will continue to operate and will be supported by an NWGL Assurance Sub-Committee. It is anticipated that these arrangements will be in place before 1 April 2017.

RISK & COMPLIANCE COMMITTEE

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

The members of the Risk & Compliance Committee are P Rew (Chairman), Dr S Lyster, M A B Nègre, D N Macrae and L S Chan.

During the year, and up to the date of approval of these financial statements, the Risk & Compliance Committee assisted the Board to discharge its responsibilities. Its work included the following:

- Completing the implementation of a significantly enhanced risk management framework and corporate risk register, based on a detailed bottom-up assessment of risk across the Company and departmental risk registers developed by risk champions in each department;
- 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 the management of specific areas of risk in relation to health and safety, the vehicle operator's licence and environmental compliance;
- Reviewing cyber security and steps being taken to enhance security;
- 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; and
- Reviewing business continuity arrangements.

The effectiveness of the Risk & Compliance Committee is enhanced by 'deep-dive' sessions at which specific risks are addressed in great detail.

Attendance at the three scheduled Risk & Compliance Committee meetings during the year was as follows:

NAME	ATTENDANCE
P Rew	3
Dr S Lyster	3
M A B Nègre	3
D N Macrae	2
L S Chan	2

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 Audit Committee and the Risk & Compliance Committee.

REMUNERATION COMMITTEE

The Remuneration Committee is a Committee of the Board of NWGL which has delegated authority to determine the remuneration of the Executive and Non-Executive Directors and such other members of the Executive management team as the NWGL Board considers appropriate. Remuneration is determined within a policy designed to ensure that executives are provided with appropriate incentives to encourage enhanced performance and are, in a fair and responsible way, rewarded for their individual contributions to the Group's success.

The members of the Remuneration Committee are A J Hunter (Chairman), H Mottram, P Rew, M Fay and D N Macrae. S Salter, from the management team, provides advice to the Remuneration Committee from time to time. H Mottram does not participate in discussions relating to her own remuneration and her bonus targets are set directly by the Chairman.

The work of the Remuneration Committee is explained in the Statement on Directors' Pay and Standards of Performance in the APR. The Company complies with its obligations under Section 35A of the Water Act 2003 by disclosing in its regulatory accounts a detailed breakdown of remuneration paid to the Executive Directors of NWL, which includes those elements linked to NWL's standards of performance.

All members of the Committee attended the two scheduled meetings during the year.

INEDS AND THE COMPANY'S LICENCE

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 46 and 47 above. They were appointed on the recommendation of the Nomination Committee of Northumbrian Water Group plc, when it was independently listed.

The INEDs attend and participate in decisions at all NWGL Board meetings, at meetings of NWGL's Audit, Risk & Compliance and Remuneration Committees and at meetings of the Assurance Sub- Group of the Audit Committee (whose members are P Rew (Chairman), Dr S Lyster and M A B Nègre). Whilst these were, throughout the year, formally constituted at the NWGL level, the vast majority of their work related to the Company's activities. The INEDs have therefore played a full part in all 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 and of the Sub-Group.

THE UK CORPORATE GOVERNANCE CODE

The Board considers that it complies substantially with the relevant provisions of the UK CGC where they are appropriate for a privately held company, except as explained below.

Code Provisions

A.3.1: The Chairman was appointed by the Group's shareholders.

A.4.2: The Chairman has informal discussions with the Non-Executive Directors as the need arises, though it has not been necessary to hold formal meetings with them without the executives present. The Non-Executive Directors have not appraised the performance during the year of the Chairman, but all Directors will have the opportunity to comment on his performance as part of the current Board evaluation.

B.1.1: The Board has determined that M A B Nègre is independent, notwithstanding that he served on the NWGL Board for more than nine years and has served on the NWL Board since 2006. M A B 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. He continues to contribute a constructive and challenging perspective to Board discussions. The Board is therefore satisfied that M A B Nègre is independent for the purposes of the UK CGC.

The Board has also determined that Dr S Lyster is independent, notwithstanding that he has served on the NWL Board since 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 ESW supply area. The Board is satisfied that Dr Lyster continues to demonstrate a fully independent approach and to offer valuable constructive challenge; the Board is therefore satisfied that he is independent for the purposes of the UK CGC.

B.1.2: The Board comprises a Chairman appointed by the Group's shareholders, four further Non-Executive Directors who are not independent as defined by the UK CGC, four INEDs and three Executive Directors (including the CEO). This balance has served the Company and its stakeholders well to date.

B.2.1, B.2.2 and B.2.4: There is not a permanent Nomination Committee. The Company has confirmed (in its governance document) that 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 Non-Executive Directors will participate. Moreover, the Board has agreed to ensure that the recruitment process for INEDs is such that a diverse range of candidates is encouraged to apply.

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; Independent Directors keep up to date with developments in the sector via updates at Board meetings and external seminars.

B.6: The Company is conducting an internal review of the Board's performance during the year and the findings will be reviewed at the Board meeting in August 2016. The performance of Executive Directors is appraised by the CEO and all Executive Directors participate in NWL's extensive 360° feedback system.

B.7: Annual re-election is not relevant to a privately owned company.

D.1: The Company's policy on remuneration and the detailed remuneration disclosures are set out in the Statement on Directors' Pay and Standards of Performance in the APR.

D.2.1: The membership of the Remuneration Committee is disclosed on page 52, and this is considered to be appropriate given the Company's ownership.

Schedule B: There were five Board meetings during the year, as well as four meetings of the Audit Committee, three meetings of the Risk & Compliance Committee and two meetings of the Remuneration Committee.

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 and, accordingly, commenced performance evaluations in 2015. As disclosed above, an internal review of the performance of the Board during the year is in progress.

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 was updated during the year and now provides clearer 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.

GOVERNANCE REPORT

DIRECTORS' REPORT

DIRECTORS

The Directors who served during the year are listed on page 43 of the Governance Report.

DISCLOSURES PROVIDED IN THE STRATEGIC REPORT

Future developments which may impact on the Company are described in the Regulatory and Legislative Developments section of the Strategic Report.

Our approach to innovation is described in the Performance section of our Strategic Report under the Competitiveness heading and the costs of research and development are disclosed in note 3 of the Statutory Financial Statements.

Our policies in respect of the employment for disabled persons and employee involvement are set out in the Performance section of our Strategic Report under the People heading.

Information on results and dividends is 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, external costs of £4,796 were associated with these activities in respect of the Labour party. In addition, Company representatives also attended the party conferences of the Labour and Conservative parties.

GREENHOUSE GAS EMISSIONS

Our carbon management plan has the aim of reducing our GHG emissions by 35% by 2020 against a 2008 baseline. We remain ahead of target with emissions down by 27% compared to the baseline. The protocol that we use for measuring our emissions is based on the Carbon Accounting Workbook developed and updated annually by the Water Research Council, 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.

Our total net operational GHG emissions for the year ended 31 March 2016 increased to 225.2 ktonnes CO_2e (31 March 2015: 213.6 ktonnes CO_2e). This reflected an increase in energy usage of 12% less a 7% reduction in the emissions factor applied for grid electricity, partly reversing an increase seen in the previous year.

The increase in usage was largely driven by weather conditions, with dry weather in our NW region in spring and summer 2015 requiring us to carry out more transfers of water resources and utilise more energy intensive treatment works, whilst high winter rainfall significantly increased sewage pumping activity. In addition, our new process to transform biogas from AAD into biomethane and inject this into the national grid, as described on page 25, contributes to long term sustainability of the UK's gas supply but, perversely, has caused an increase in our emissions reported under current rules as the benefit of the gas export is not included in the calculation. If the gas export had been included, like exported electricity, our emissions would have been 217.4 ktonnes CO_2e.

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. As described above, these measures can be volatile depending upon levels of rainfall and pumping requirements, therefore we focus on longer term trends.

ANNUAL OPERATIONAL GHG INTENSITY RATIO	2015-16	2014-15
Emissions/Ml of water	239	246
Emissions/Ml of sewage treated (flow to full treatment)	319	300
Emissions/Ml of sewage treated (water distribution input)	607	540

DIRECTORS' INDEMNIFICATION

NWGL had Directors' and Officers' insurance in place for the year to 31 March 2016. On 28 November 2005 NWGL entered into a deed of indemnity to grant the Directors of NWGL and its subsidiaries further protection against liability to third parties, 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 April 2016;
- 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 £350m of five year committed bank facilities as back up liquidity (maturing in 2019), and a further £100m of committed financing from the EIB, both of which were undrawn at 31 March 2016; and
- The Company's formal governance and risk management arrangements which are monitored by the Audit Committee, Risk & Compliance Committee and Board.

VIABILITY STATEMENT

The Directors believe that the Company is well placed to manage its business risks successfully and expect that the business can continue to operate effectively over the long term and, specifically, meet its financial obligations over the four years to March 2020. 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 Final Determination 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 £350m five year committed bank facility as back up liquidity (maturing in 2019), and a further £100m of committed financing from the EIB, both of which were undrawn at 31 March 2016;
- The key financial ratios over the planning horizon of the Company's medium term plan to March 2020 as reflected in strong investment grade credit ratings; and
- The principal risks and uncertainties facing the Company and the mitigating controls, as described on pages 36 to 38, which are strongly monitored by the Audit Committee, Risk & Compliance Committee and Board.

The Directors have chosen a period of four years to March 2020 to assess the viability of the Company after considering the significant increase in uncertainty of financial forecasts beyond the end of the current regulatory price control period, given the changes being proposed under Ofwat's Water 2020 programme.

The medium term plan has been stress tested under a number of adverse, but possible, scenarios which would directly impact on the Company's financial model, in the context of the Company's financial objective of retaining a strong investment grade credit rating. The scenarios tested included: a sustained period of lower RPI; increased interest rates for future borrowings; increased current tax charges; failure to deliver totex efficiency targets; potential cost shocks; and a deterioration in the defined benefit pension scheme deficit due to external market factors.

To the extent that any of these scenarios, in isolation or combination, would place retention of the Company's credit rating at risk, the Directors are confident that this could be mitigated by application of the Board's flexible dividend policy alongside targeted management actions. Separate third party assurance agreed upon procedures have been performed on the calculations and stress testing of the plan in order to provide independent assurance to the Directors of the impact of the various scenarios.

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 United Kingdom (UK) Generally Accepted Accounting Practice (UK Accounting Standards and applicable law), including FRS 101 Reduced Disclosure Framework, with certain exceptions required by Ofwat which are detailed in note (a) of the Regulatory Accounting Policies and Disclosures in the APR. 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 proper 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 consider that the 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 report and financial statements has been produced as well as reviewing and commenting on the report.

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.

MParker

By order of the Board
M Parker,
Company Secretary,
15 July 2016

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

Registered in England and Wales
Registered no: 02366703

STATUTORY FINANCIAL STATEMENTS

INCOME STATEMENT

FOR THE YEAR ENDED 31 MARCH 2016

	NOTE	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
		£'m	£'m
CONTINUING OPERATIONS			
Revenue	2	805.5	985.3
Operating costs (including exceptional operating items)	3	(432.8)	(588.6)
Operating profit		**372.7**	**396.7**
Finance costs	6	(106.3)	(138.1)
Profit before taxation		**266.4**	**258.6**
Taxation	7(a)	(3.5)	21.6
Profit for the period attributable to the shareholder of the company		**262.9**	**280.2**

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 MARCH 2016

	NOTE	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
		£'m	£'m
Profit for the period		262.9	280.2
ITEMS THAT WILL NOT BE RECLASSIFIED SUBSEQUENTLY TO PROFIT AND LOSS:			
Actuarial (losses) / gains	21	(49.5)	19.7
Deferred tax related to actuarial (losses) / gains	7(b)	7.6	(3.9)
ITEMS THAT MAY BE RECLASSIFIED SUBSEQUENTLY TO PROFIT AND LOSS:			
Losses on cash flow hedges taken to equity		(15.9)	(4.6)
Tax on items charged to equity that may be reclassified		2.9	0.9
Other comprehensive (loss) / income		(54.9)	12.1
Total comprehensive income for the period attributable to the shareholder of the Company		**208.0**	**292.3**

BALANCE SHEET AT 31 MARCH 2016

(REGISTERED NUMBER 02366703)

	NOTE	31 MARCH 2016	31 MARCH 2015
		£'m	£'m
NON-CURRENT ASSETS			
Property, plant and equipment	9	4,169.6	4,075.4
Financial investments	10	160.9	160.9
		4,330.5	**4,236.3**
CURRENT ASSETS			
Inventories	11	2.4	2.3
Trade and other receivables	12	185.7	251.2
		188.1	**253.5**
Total assets		**4,518.6**	**4,489.8**
CURRENT LIABILITIES			
Trade and other payables	13	(158.0)	(174.1)
Borrowings	14	(96.8)	(207.5)
Obligations under finance leases	15(a)	(8.5)	(5.8)
Provisions	16	(0.2)	(0.2)
		(263.5)	**(387.6)**

STATUTORY FINANCIAL STATEMENTS

	NOTE	31 MARCH 2016	31 MARCH 2015
		£'m	£'m
NON-CURRENT LIABILITIES			
Borrowings	14	(2,447.8)	(2,289.3)
Obligations under finance leases	15(a)	(101.2)	(101.9)
Provisions	16	(1.4)	(1.6)
Deferred tax liabilities	7(d)	(404.7)	(445.0)
Pension liability	21	(89.9)	(86.7)
Hedging instruments	18	(31.3)	(14.0)
Grants and deferred income	17	(511.8)	(493.7)
		(3,588.1)	**(3,432.2)**
Total liabilities		**(3,851.6)**	**(3,819.8)**
Net assets		**667.0**	**670.0**
CAPITAL AND RESERVES			
Share capital	19	122.7	122.7
Cash flow hedge reserve		(24.2)	(11.2)
Profit and loss account		568.5	558.5
Equity attributable to the shareholder of the Company		**667.0**	**670.0**

Heidi Mottram

Approved by the Board of Directors on 15 July 2016
and signed on their behalf by: H Mottram

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 MARCH 2016

	NOTE	SHARE CAPITAL	CASH FLOW HEDGE RESERVE	RETAINED EARNINGS	TOTAL EQUITY
		£'m	£'m	£'m	£'m
At 1 January 2014		**122.7**	**(7.5)**	**574.0**	**689.2**
Profit for the period		-	-	280.2	280.2
Other comprehensive income		-	(3.7)	15.8	12.1
Total comprehensive income and expense for the period		-	(3.7)	296.0	292.3
Dividends	8	-	-	(311.5)	(311.5)
At 31 March 2015		**122.7**	**(11.2)**	**558.5**	**670.0**
Profit for the year		-	-	262.9	262.9
Other comprehensive income		-	(13.0)	(41.9)	(54.9)
Total comprehensive income and expense for the year		-	(13.0)	221.0	208.0
Dividends	8	-	-	(211.0)	(211.0)
At 31 March 2016		**122.7**	**(24.2)**	**568.5**	**667.0**

NOTES TO THE STATUTORY FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2016

1. ACCOUNTING POLICIES

NWL is incorporated in the United Kingdom under the Companies Act. 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 56. The nature of the Company's operations and its principal activities are set out in the Strategic Report on pages 9 to 39.

These financial statements are presented in 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, because it is included in the group accounts of NWGL (see note 23).

(A) BASIS OF ACCOUNTING

In accordance with FRS 100 issued by the FRC, the UK GAAP applied by the Company in its previous financial statements is no longer applicable. The Company meets the definition of a qualifying entity under FRS 101 and has therefore adopted FRS 101 as its accounting framework for the year ended 31 March 2016 and, in doing so, has applied the requirements of IFRS 1 First Time Adoption of International Financial Reporting Standards.

These financial statements have been prepared in accordance with FRS 101, incorporating the Amendments to FRS 101 issued by the FRC in July 2015 and the amendments to Company law made by The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015 prior to their mandatory effective date of accounting periods beginning on or after 1 January 2016.

In accordance with IFRS 1 (appendix D16), at the date of transition, the Company has measured its assets and liabilities at the carrying amounts included in NWGL's consolidated financial statements. Prior period values have been restated on a consistent basis.

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 2016, the Company had net current liabilities of £75.4m (31 March 2015: £134.1m). 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 £350m (31 March 2015: £258m) and the £100m committed EIB funding. 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 United Kingdom. All water and sewerage charges billed to customers are recognised pro-rata over the period to which they relate. For consumption by measured customers which has not yet been billed, an accrual is estimated.

(C) CASH FLOW STATEMENT

As permitted by FRS 101, the Company has elected not to present a cash flow statement.

(D) 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	4-200 years (see below)
Fixtures, fittings, tools and equipment	4-10 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

(E) FINANCIAL INVESTMENTS

Financial investments are stated at their purchase cost, less provision for diminution in value (note 10).

(F) 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. Capital grants and contributions relating to property, plant and equipment are treated as deferred income and amortised to the income statement over the expected useful economic lives of the related assets.

Deferred income relating to assets adopted from developers, recognised in accordance with IFRIC 18, is amortised to the income statement over the expected useful economic lives of the related assets.

(G) 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.

(H) INVENTORIES

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

(I) PENSION COSTS

The Company is the principal employer of the Northumbrian Water Pension Scheme (NWPS or the Scheme), which has both a defined benefit section and a defined contribution section.

The cost of providing benefits under the defined benefit 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.

(J) 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.

(K) 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.

(L) RESEARCH AND DEVELOPMENT

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

(M) DERIVATIVE FINANCIAL INSTRUMENTS

The Company utilises interest and inflation rate swaps, gilt locks 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. Interest rate swap agreements are used to manage interest rate exposures. 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 IAS 39. In summary, these criteria relate to initial designation and documentation of the hedge relationship, prospective testing of the relationship to demonstrate the expectation that the hedge will be highly effective throughout its life and subsequent retrospective testing of the hedge to verify effectiveness.

Under IFRS 13, 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 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 is 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 equity 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 equity 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 equity 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 equity is kept in equity until the forecast transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the income statement.

(N) 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 current and non-current liabilities less cash and cash equivalents, short term cash deposits, financial investments and loans receivable.

(O) BAD DEBTS

(i) Bad debt write offs

Debt is only written off after all available economic options for collecting the debt have been exhausted and the debt has been deemed to be uncollectable. This may be because the debt is considered to be impossible, impractical, inefficient or uneconomic to collect.

Situations where this may arise and where debt may be written off are as follows:

- Where the customer has absconded without paying and strategies to trace their whereabouts and collect outstanding monies have been fully exhausted;
- Where the customer has died without leaving an estate or has left an insufficient estate on which to levy execution;
- Where the customer does not have any assets or has insufficient assets on which to levy execution;
- Where the value of the debt makes it uneconomic to pursue;
- Where county court proceedings and attempts to recover the debt by debt collection agencies have proved unsuccessful; and
- Where the customer has been declared bankrupt, is in liquidation or is subject to insolvency proceedings or a debt relief order and no dividend has been or is likely to be received.

For debt to be written off there must be a legitimate charge against the debtor. If it is considered that part or all of the debt is incorrect or unsubstantiated, then such elements are dealt with through the issue of a credit note.

(ii) Bad debt provisioning

The Company's bad and doubtful debts provision policy has remained unchanged during the year and has been consistently applied in the current and prior periods.

The bad debt provision is charged to operating costs to reflect the company's assessment of the risk of non recoverability of debtors. It is calculated by applying expected recovery rates to debts outstanding at the end of the accounting period. These recovery rates take into account the age of the debt, payment history and type of debt.

Higher provisioning percentages are applied to categories of debt which are considered to be of greater risk, including those with a poor payment history as well as to those of greater age. Bad debt provisioning rates are reviewed annually to reflect the latest collection performance data from the company's billing system. All debt greater than 48 months old is fully provided for. Actual amounts recovered may differ from the estimated levels of recovery which could impact on operating results.

The provision has increased from £77.3m at 31 March 2015 to £83.7m at 31 March 2016. This reflects the additional provision made in the year as outstanding debt has aged. This has added to the existing provision for older debt which remains fully provided for as the debt is only written off in the specific circumstance outlined above.

(P) 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.

The Company capitalises borrowing costs for all eligible assets when construction commenced on or after 1 April 2009 and continues to expense borrowing costs relating to construction projects that commenced prior to that date.

(Q) 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. The Directors consider that the significant judgements applied at the balance sheet date, which may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are:

- 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 21;
- The estimation of income for measured water and sewerage services supplied but not billed at the end of the financial period. Consumption by measured customers is billed periodically in arrears with large commercial customers being billed monthly and smaller commercial customers and domestic customers being billed 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;
- The bad debt provision, which is calculated by applying a range of percentages to debt of different ages, as described on note 1(o) above. 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. The value of the bad debt provision is sensitive to the specific percentages applied;
- 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(d) above.

STATUTORY FINANCIAL STATEMENTS

2. SEGMENTAL INFORMATION

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

3. OPERATING COSTS

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'m	**£'m**
Materials and consumables	21.0	24.9
Manpower costs (note 5)	129.9	152.6
Pension curtailment	(38.9)	-
Own work capitalised	(36.3)	(43.0)
Depreciation of property, plant and equipment	126.0	150.6
Impairment of tangible fixed assets	-	32.6
Profit on disposal of property, plant and equipment	(0.4)	(1.0)
Amortisation of capital grants	(5.4)	(5.7)
Costs of research and development	0.8	1.0
Operating lease payments	1.2	1.7
Bad debt charge	18.8	19.2
Other operating costs	216.1	255.7
	432.8	**588.6**

STATUTORY FINANCIAL STATEMENTS

The Company carried out an extensive consultation with employees on changes to a defined benefit pension scheme which resulted in changes being made to future benefits. Pension accounting rules, under IAS 19 Employee Benefits, require the impact of these scheme changes to be reported as a past service cost in the income statement. This has resulted in an exceptional accounting credit of £38.9m being recognised in the year ended 31 March 2016.

In the prior period, the impairment of tangible fixed assets includes an exceptional charge of £30.7m in relation to sludge drying plant at Bran Sands. This plant was constructed in the 1990s as a regional centre for the treatment and disposal of the sludge generated from NWL's wastewater treatment process. In response to a combination of high operating costs and the emergence of new technologies, the sludge strategy was subsequently reviewed leading to the construction of two AAD plants at Bran Sands and Howdon. The sludge drying plant was initially retained as alternative capacity, however, during the period, management decided that the two AAD plants were operating to the expected standard of performance and reliability and that the sludge drying plant would be abandoned.

Auditor's remuneration in respect of the statutory audit amounted to £129k (15 months ended 31 March 2015: £131k), including fees for a subsidiary, Northumbrian Water Finance plc (NWF), of £6k (15 months ended 31 March 2015: £6k). Fees of £58k (years ended 31 March 2015 and 31 March 2014: £104k) were incurred in respect of the APR, including the audit of the Regulatory Accounting Statements in accordance with the opinion on pages 145 to 147, 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 £75k (15 months ended 31 March 2015: £60k) were incurred for non-audit services comprising assurance work in respect of a project to implement a new customer billing system and other assurance to third parties.

4. DIRECTORS' EMOLUMENTS

(A) DIRECTORS' REMUNERATION

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

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'000	£'000
Emoluments (including benefits in kind)	**1,836**	**2,218**

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 2016 was a member of a defined benefit pension scheme where the Company makes contributions towards the cost (31 March 2015: 1).

Two of the Directors at 31 March 2016 were members of a defined contribution scheme where the Company makes contributions towards the cost (31 March 2015: 2).

The Directors' remuneration policy and a detailed report showing total remuneration for each Director, for the 12 months to 31 March 2016, are provided in the Statement on Directors' Pay and Standards of Performance on pages 137 to 143.

(B) HIGHEST PAID DIRECTOR

The amounts for remuneration shown in note 4(a) include the following in respect of the highest paid Director:

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'000	£'000
Emoluments (including benefits in kind)	**706**	**836**

In the year ended 31 March 2016, the highest paid Director was a member of the defined contribution scheme and the payments made to that scheme of £35k (fifteen months ended 31 March 2015: £35k) are included within the emoluments figure above.

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5. EMPLOYEE INFORMATION

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

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'m	£'m
GROSS COSTS CHARGED TO THE INCOME STATEMENT:		
Wages and salaries	76.0	90.8
Social security costs	7.2	8.3
Other pensions costs	16.2	17.6
	99.4	**116.7**
COSTS RECHARGED TO OTHER GROUP COMPANIES:		
Wages and salaries	3.0	3.0
	3.0	**3.0**
NET COSTS CHARGED TO THE PROFIT AND LOSS ACCOUNT:		
Wages and salaries	73.0	87.8
Social security costs	7.2	8.3
Other pensions costs	16.2	17.6
	96.4	**113.7**
COSTS CHARGED TO CAPITAL SCHEMES		
Wages and salaries	25.8	30.9
Social security costs	2.4	2.8
Other pensions costs	5.3	5.2
	33.5	**38.9**
Total net employee costs	**129.9**	**152.6**

The table above excludes the exceptional pension credit in the year ended 31 March 2016 (see note 3). The average monthly number of employees on the payroll during the financial year was 3,125 (fifteen months ended 31 March 2015: 3,053).

6. NET FINANCE COSTS

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'m	£'m
FINANCE COSTS PAYABLE:		
Bank overdrafts and loans	17.3	21.6
Receivable in respect of derivatives	(0.9)	-
Amounts due to group companies	89.1	111.5
Amortisation of discount, fees, loan issue costs and other financing items	1.3	1.2
Accretion on index linked bonds	7.5	19.5
Interest cost on pension plan obligations	2.1	4.9
Obligations under finance leases	3.9	5.7
	120.3	**164.4**
Less amounts capitalised on qualifying assets	(5.4)	(9.4)
	114.9	**155.0**
Fair value losses on derivative financial instruments	1.4	-
Total finance costs payable	**116.3**	**155.0**
FINANCE INCOME RECEIVABLE:		
Bank deposits	(0.3)	(4.7)
Amounts due from group companies	(9.7)	(12.2)
Total finance costs receivable	**(10.0)**	**(16.9)**
Net finance costs payable	**106.3**	**138.1**

STATUTORY FINANCIAL STATEMENTS

7. TAXATION

(A) TAX ON PROFIT ON ORDINARY ACTIVITIES:

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'m	£'m
CURRENT TAX:		
UK current income tax charge 20% (15 months ended 31 March 2015: 21.39%)	8.2	7.6
Adjustments in respect of prior periods	(1.7)	(68.3)
Payable in respect of group relief for the current year	25.6	45.0
Adjustments in respect of prior period group relief	1.2	(1.4)
Total current tax	**33.3**	**(17.1)**
DEFERRED TAX:		
Origination and reversal of timing differences in the period at 18% (15 months ended 31 March 2015: 20%)	16.5	1.1
Impact of reduction in rate of UK corporation tax	(46.6)	-
Adjustments in respect of prior periods	0.3	(5.6)
Total deferred tax	**(29.8)**	**(4.5)**
Tax charge / (credit) in the income statement	**3.5**	**(21.6)**

The rate of corporation tax was reduced from 21% to 20% with effect from 1 April 2015. Further reductions to 19% (with effect from 1 April 2017) and to 18% (with effect from 1 April 2020) have been enacted by the Finance (No. 2) Act 2015. Accordingly, deferred tax has been provided in line with the rates at which temporary differences are expected to reverse.

Tax losses have been provisionally claimed as group relief from other group companies, for which payment is being made at the full rate of tax. In addition, tax losses have been provisionally claimed as consortium relief from a related company for which payment is being made at less than the full rate of tax.

(B) TAX RELATING TO ITEMS CHARGED OUTSIDE THE INCOME STATEMENT:

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'m	£'m
DEFERRED TAX:		
Actuarial gains and losses on pension scheme	(8.9)	3.9
Impact of reduction in rate of UK corporation tax	1.3	-
Financial instruments	(2.9)	(0.9)
Tax (credit) / charge in the statement of comprehensive income	**(10.5)**	**3.0**

STATUTORY FINANCIAL STATEMENTS

(C) RECONCILIATION OF THE TAX CHARGE / (CREDIT):

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'m	£'m
Profit on ordinary activities before tax	**266.4**	**258.6**
Profit on ordinary activities multiplied by standard rate of corporation tax of 20% (15 months ended 31 March 2015: 21.39%)	53.3	55.3
EFFECTS OF:		
Expenses not deductible for tax purposes	0.1	0.2
Non-taxable income and other tax reliefs	(1.6)	(1.9)
Depreciation in respect of non-qualifying items	1.0	1.2
Permanent differences on transition to IFRS	0.6	-
Consortium relief payable at less than the standard rate	(1.9)	(1.3)
Impact on deferred tax of change in tax rate	(46.6)	-
Deferred tax movement not at average rate for the period	(1.8)	0.2
Adjustments in respect of prior periods	0.4	(75.3)
Transfer pricing adjustments	(0.8)	(0.8)
Balancing payment payable	0.8	0.8
Total current tax charge / (credit) (note 7(a))	**3.5**	**(21.6)**

STATUTORY FINANCIAL STATEMENTS

(D) DEFERRED TAX

	ACCELERATED TAX DEPRECIATION	DEFERRED INCOME	RETIREMENT BENEFIT OBLIGATIONS	FAIR VALUE HEDGING INSTRUMENTS	BUSINESS COMBINATIONS	OTHER	TOTAL
	£'m	£'m	£'m	£'m	£'m	£'m	£'m
At January 2014	509.8	(54.5)	(17.7)	(1.9)	7.1	3.7	446.5
Charge/(credit) in the income statement	3.0	(4.4)	(4.4)	-	(0.2)	1.5	(4.5)
Charge/(credit) in other comprehensive income	-	-	3.9	(0.9)	-	-	3.0
At 31 March 2015	**512.8**	**(58.9)**	**(18.2)**	**(2.8)**	**6.9**	**5.2**	**445.0**
Charge/(credit) in the income statement	(39.5)	4.9	5.5	(0.3)	(0.8)	0.4	(29.8)
Charge/(credit) in other comprehensive income	-	-	(7.6)	(2.9)	-	-	(10.5)
At 31 March 2016	**473.3**	**(54.0)**	**(20.3)**	**(6.0)**	**6.1**	**5.6**	**404.7**

(E) FACTORS THAT MAY AFFECT FUTURE TAX CHARGES:

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

In addition to the changes to the main rate of corporation tax referred to in note 7(a), the UK Government has proposed that the rate of tax applicable from April 2020 should be reduced by a further 1% to 17%. The proposal was included in the Finance Bill 2016 published on 24 March 2016 but, as this change had not been enacted or substantively enacted by the balance sheet date, it has not been used as a basis to calculate the Company's tax position. If the rate had applied at the balance sheet date, the company's deferred tax liabilities would have been £22.5m lower, at £382.2m.

8. DIVIDENDS

	12 MONTHS ENDED 31 MARCH 2016	15 MONTHS ENDED 31 MARCH 2015
	£'m	£'m
EQUITY: **DIVIDENDS PAID:**		
Interim paid for the year ended 31 March 2016 of nil (period ended 31 March 2015: 84.18p) per share on an aggregated basis	-	103.2
Interim paid for the year ended 31 March 2016 of 85.61p (period ended 31 March 2015: 84.18p) per share on an aggregated basis	105.0	103.3
Interim paid for the year ended 31 March 2016 of 86.42p (period ended 31 March 2015: 85.61p) per share on an aggregated basis	106.0	105.0
Total dividends paid in the period	**211.0**	**311.5**

No final dividend was proposed for the year ended 31 March 2016 (period ended 31 March 2015: nil).

The Directors have a policy which aims to grow dividends on a slow but regular basis and which takes into account the principle of incentive based price cap regulation, including operating and investment performance. Following a change in the Company's statutory accounting reference date, the timing of dividend payments was amended, with the payment budgeted for April 2015 advanced by one month and paid in March 2015. As a consequence, a third interim dividend was paid in the previous period. This did not change the underlying dividend policy, or change the total dividend paid to the shareholder in the calendar year to 31 December 2015.

Accordingly, the level of dividend has been 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 stable strong investment grade credit ratings.

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9. PROPERTY, PLANT AND EQUIPMENT

	FREEHOLD LAND AND BUILDINGS	INFRASTRUCTURE ASSETS	OPERATIONAL STRUCTURES, PLANT AND MACHINERY	FIXTURES, FITTINGS, TOOLS AND EQUIPMENT	ASSETS IN THE COURSE OF CONSTRUCTION	TOTAL
	£'m	£'m	£'m	£'m	£'m	£'m
COST:						
At 1 April 2015	146.2	2,525.4	2,694.1	243.5	83.8	5,693.0
Additions	-	6.4	2.9	0.9	213.0	223.2
Schemes commissioned	1.1	82.9	80.4	14.1	(178.5)	-
Disposals	(1.4)	(5.5)	(2.8)	(0.2)	-	(9.9)
At 31 March 2016	**145.9**	**2,609.2**	**2,774.6**	**258.3**	**118.3**	**5,906.3**
DEPRECIATION:						
At 1 April 2015	51.5	305.6	1,084.6	175.9	-	1,617.6
Charge for the year	2.9	28.1	80.9	14.1	-	126.0
Disposals	(0.8)	(3.6)	(2.3)	(0.2)	-	(6.9)
At 31 March 2016	**53.6**	**330.1**	**1,163.2**	**189.8**	**-**	**1,736.7**
NET BOOK VALUE:						
At 31 March 2016	**92.3**	**2,279.1**	**1,611.4**	**68.5**	**118.3**	**4,169.6**
At 31 March 2015	**94.7**	**2,219.8**	**1,609.5**	**67.6**	**83.8**	**4,075.4**
LEASED ASSETS INCLUDED ABOVE:						
Net book value:						
At 31 March 2016	**-**	**44.8**	**18.0**	**-**	**-**	**62.8**
At 31 March 2015	**-**	**45.3**	**18.6**	**-**	**-**	**63.9**

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 £30.0m (31 March 2015: £24.6m). The capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation was 5.62% (15 months ended 31 March 2015: 5.62%).

10. FINANCIAL INVESTMENTS

	LOANS TO GROUP COMPANIES
	£'m
At 1 April 2015 and 31 March 2016	**160.9**

(A) LOANS TO GROUP COMPANIES

In May 2004, the Company made a loan of £159.0m to Northumbrian Services Limited (NSL), maturing in January 2034. Following a restructuring of the NWGL group, this loan was reassigned to NWGL on 29 March 2016 at a variable interest rate linked to LIBOR.

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 2016 the balance was £1.9m (31 March 2015: £1.9m).

(B) SUBSIDIARIES

The Company's interests in subsidiaries at 31 March 2016 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	Finance
Reiver Holdings Limited	England and Wales	Ordinary shares of £1	100	Holding company

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.

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11. INVENTORIES

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
Raw materials and consumables	**2.4**	**2.3**

12. TRADE AND OTHER RECEIVABLES

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
Trade receivables	177.2	170.5
Doubtful debt provision	(83.7)	(77.3)
Income tax receivable	10.7	73.3
Amounts owed by other group companies	4.8	6.1
Other receivables	4.7	7.0
Prepayments and accrued income	72.0	71.6
	185.7	**251.2**

13. TRADE AND OTHER PAYABLES

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
Trade payables	8.7	8.5
Amounts owed to other group companies	13.7	24.1
Amounts owed to related parties	3.8	9.5
Taxation and social security	3.5	2.5
Other payables	24.9	29.2
Accruals and deferred income	103.4	100.3
	158.0	**174.1**

14. LOANS AND BORROWINGS

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
CURRENT:		
Bank overdrafts	2.5	0.7
Current instalments due on external borrowings	-	124.3
Current instalments due on internal borrowings	94.3	82.5
	96.8	**207.5**
NON-CURRENT:		
Non-current instalments due on external borrowings	558.7	406.8
Non-current instalments due on internal borrowings	1,889.1	1,882.5
	2,447.8	**2,289.3**

STATUTORY FINANCIAL STATEMENTS

(A) EXTERNAL BORROWINGS:

Loans wholly repayable within five years amount to £190.8m (31 March 2015: £125.3m).

Loans not wholly repayable within five years amount to £367.9m (31 March 2015: £407.1m) and bear interest rates in the range 1.47% to 5.35%.

The fair value loss on the Company's outstanding interest rate swaps in the year to 31 March 2016 was £7.8m (15 months to 31 March 2015: £9.3m) in relation to interest rate swaps with a notional principal of £360m (15 months to 31 March 2015: £70.0m).

(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 (15 months ended 31 March 2015: £0.3m). Amortisation of loan issue receipts during the year amounted to £0.3m (15 months ended 31 March 2015: £0.4m).

NWF issued £300m Guaranteed Eurobonds in December 2001, maturing October 2017, with an annual coupon of 6.0%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £301.0m. Amortisation of loan receipts during the year amounted to £0.1m (15 months ended 31 March 2015: £0.1m).

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 (15 months ended 31 March 2015: £0.3m).

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 £150.0m. Indexation accretion during the year amounted to £2.1m (15 months ended 31 March 2015: £5.2m).

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 £0.8m (15 months ended 31 March 2015: £2.0m).

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 £2.7m (15 months ended 31 March 2015: £6.7m).

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 £338.8m. Finance costs allocated during the year amounted to £0.7m (15 months ended 31 March 2015: £0.9m).

15. OBLIGATIONS UNDER HIRE PURCHASE CONTRACTS AND FINANCE LEASES

(A) OBLIGATIONS UNDER HIRE PURCHASE CONTRACTS AND FINANCE LEASES ARE AS FOLLOWS:

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
AMOUNTS DUE:		
Within one year	8.5	5.8
In the second to fifth years inclusive	66.3	68.7
After five years	78.7	82.7
	153.5	**157.2**
LESS:		
Finance charge allocated to future periods	(43.8)	(49.5)
	109.7	**107.7**
DISCLOSED AS DUE:		
Current liability	8.5	5.8
Non current liability	101.2	101.9
	109.7	**107.7**

STATUTORY FINANCIAL STATEMENTS

(B) LEASE COMMITMENTS:

The Company has entered into non-cancellable operating leases in respect of land and buildings, plant, machinery and motor vehicles. The future minimum rentals payable under non-cancellable operating leases are as follows:

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
Not later than one year	0.7	0.7
After one year but not more than five years	2.7	2.8
After five years	35.0	34.9
	38.4	**38.4**

16. PROVISIONS

	£'M
PENSION PROVISION FOR FORMER EMPLOYEES:	
At 1 April 2015	1.8
Utilised during the period	(0.2)
At 31 March 2016	**1.6**
ANALYSED AS:	
Current	0.2
Non-current	1.4
	1.6

The provision 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 seven years.

17. GRANTS AND DEFERRED INCOME

	CAPITAL GRANTS AND CONTRIBUTIONS	PROCEEDS FROM KIELDER SECURITISATION	TOTAL
	£'m	£'m	£'m
At 1 April 2015	358.8	134.9	493.7
Additions	32.6	-	32.6
Disposal	(1.7)	-	(1.7)
Amortised during the period	(5.8)	(7.0)	(12.8)
At 31 March 2016	**383.9**	**127.9**	**511.8**

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 income is amortised to the income statement of the Company over the life of the assignment.

18. FINANCIAL INSTRUMENTS

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
Financial liabilities that are designated and effective as hedging instruments carried at fair value:		
Interest rate swaps	16.3	9.0
Power forward contracts	13.6	5.0
Financial liabilities carried at fair value through profit and loss:		
Interest rate swaps	0.5	-
Fuel hedge	0.9	-
	31.3	**14.0**

STATUTORY FINANCIAL STATEMENTS

At 31 March 2016, 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 2016, the Company held the following interest rate swap, designated as a hedge of future interest cash flows, used to 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%

At 31 March 2016 and 31 March 2015, the Company held the following forward power contracts, designated as hedges of expected future purchases:

NOTIONAL AMOUNT	START DATE	TERMINATION DATE	PRICE PER MWH £
166,896 MWH	1 April 2018	30 September 2018	50.7
165,984 MWH	1 October 2018	31 March 2019	56.2
166,896 MWH	1 April 2019	30 September 2019	52.2
166,896 MWH	1 October 2019	31 March 2020	56.8

At 31 March 2016 (31 March 2015:nil), 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 2016	31 March 2017	0.3025
3,000,000 litres	1 April 2017	31 March 2018	0.3250
3,000,000 litres	1 April 2018	31 March 2019	0.3435
3,000,000 litres	1 April 2019	31 March 2020	0.3562

19. SHARE CAPITAL

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
AUTHORISED:		
122,650,000 Ordinary Shares of £1 each (31 March 2015: 122,650,000)	**122.7**	**122.7**
Allotted, called-up and fully paid:		
122,650,000 Ordinary Shares of £1 each (31 March 2015: 122,650,000)	**122.7**	**122.7**

NWL is a company limited by shares.

20. FINANCIAL COMMITMENTS

(A) CAPITAL COMMITMENTS:

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
(a) Contractual commitments for the acquisition of property, plant and equipment	**144.2**	**89.5**

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 2016 the Company held forward foreign exchange contracts of £5.8m (31 March 2015: £2.7m) for the purpose of hedging the foreign currency risk of committed future purchases.

21. PENSIONS

NWL participates in the Group defined benefit pension scheme, NWPS, providing benefits to 1,446 active members at 31 March 2016 (31 March 2015: 1,604). 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 2013. At that date, the value of assets amounted to £785.9m and the liabilities were £946.2m, resulting in a deficit of £160.3m and a funding level of 83.1%.

The finalisation of this valuation was deferred until November 2015, because the Company commenced a consultation with members on proposed changes to the Scheme in January 2015. The consultation concluded in September 2015 and agreed a number of changes to the original proposal.

The main changes to the scheme, which took effect from 1 January 2016, were to base benefits on a career average revalued earnings (CARE) basis, changing from a final salary basis, with accrued benefits at the date of implementation to be revalued in line with CPI and future CARE accrual to be revalued at RPI, both capped at 2.5%.

Recognition of the benefit changes in the actuarial valuation would have resulted in a revised deficit of £106m at 31 December 2013. The Trustee took account of both the Scheme changes and significant adverse post-valuation market movements between the valuation date and 31 March 2015 in setting its contribution strategy. The future service contribution rate jointly payable by members and the employers from 1 January 2016 is 29.4% of pensionable salaries. Members' contributions are 7.3% on average with the employers paying 22.1%, including 1.5% in respect of insurance premiums and expenses. In addition, the employers committed to making deficit reduction payments of £11m per annum, commencing 1 April 2015, increasing annually by RPI.

Employer contributions of £23.2m were paid in the year to 31 March 2016, of which £11m related to deficit reduction, with a further £3.7m paid on behalf of employees under a salary sacrifice arrangement. For the year to 31 March 2017, employer contributions, including deficit reduction, are projected to be £23.1m. In addition, the employers expect to pay £3.8m on behalf of employees under the salary sacrifice arrangement.

The Scheme also has a defined contribution section which had 1,530 active members at 31 March 2016 (31 March 2015: 1,356). 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 £4.4m (15 months ended 31 March 2015: £4.5m).

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 2016. Investments have been valued, for this purpose, at fair value.

FRS 101 ACTUARIAL ASSUMPTIONS:	31 MARCH 2016	31 MARCH 2015
Discount rate	3.6%	3.3%
Pay increases[1]	3.0%	3.0%
Price inflation (RPI)	2.9%	2.9%
Price inflation (CPI)	1.9%	1.9%
Pension increases linked to RPI	2.9%	2.9%
Pension increases linked to CPI	1.9%	1.9%
Mortality assumptions[2]		
- Life expectancy for a member aged 65 - female (years)	24.9	24.7
- Life expectancy for a member aged 65 - male (years)	23.2	22.4

[1] including promotional salary scale

[2] March 2016 scheme specific bespoke 'Vitacurves' ; March 2015 115% of PCMA00/PCFA00 (year of birth with medium cohort improvements).

THE FAIR VALUE OF THE ASSETS IN THE NWPS AND THE PRESENT VALUE OF THE LIABILITIES IN THE SCHEME ARE SHOWN BELOW:

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
Equities	350.5	372.8
Debt securities	278.4	281.7
Property related funds	105.4	96.0
Cash	31.7	39.0
Other	104.2	94.7
Total fair value of assets	870.2	884.2
Present value of liabilities	(960.1)	(970.9)
Deficit	**(89.9)**	**(86.7)**

THE AMOUNTS RECOGNISED IN THE INCOME STATEMENT AND IN THE STATEMENT OF COMPREHENSIVE INCOME ARE ANALYSED AS FOLLOWS:

RECOGNISED IN THE INCOME STATEMENT:	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
Current service cost	14.9	16.6
Administration cost	1.7	1.7
Past service cost	0.8	0.2
Exceptional pension credit	(38.9)	-
Recognised in operating costs in arriving at operating profit	**(21.5)**	**18.5**
Net interest cost on plan obligations	(2.1)	(4.9)
Recognised in finance costs	**(2.1)**	**(4.9**
RECOGNISED IN THE STATEMENT OF COMPREHENSIVE INCOME:		
Changes in demographic assumptions	(7.5)	29.1
Changes in financial assumptions	49.7	(104.5)
Return on assets (excluding amounts included in finance costs)	(25.5)	94.3
Other actuarial (losses) / gains	(66.2)	0.8
Net actuarial (losses) / gains	**(49.5)**	**19.7**

The exceptional pension credit is explained in note 3 on page 71.

	31 MARCH 2016	31 MARCH 2015
	£'m	£'m
CHANGES IN THE PRESENT VALUE OF THE DEFINED PENSION OBLIGATION ARE ANALYSED AS FOLLOWS:		
At start of period	970.9	872.2
Current service cost	14.9	16.6
Administration cost	1.7	1.7
Past service cost	0.8	0.2
Exceptional pension credit	(38.9)	-
Interest cost	31.0	49.1
Contributions by plan participants	0.2	0.2
Benefits paid	(44.5)	(43.7)
REMEASUREMENT:		
Changes in demographic assumptions	7.5	(29.1)
Changes in financial assumptions	(49.7)	104.5
Other actuarial gains and losses	66.2	(0.8)
At end of period	**960.1**	**970.9**
CHANGES IN THE FAIR VALUE OF PLAN ASSETS ARE ANALYSED AS FOLLOWS:		
At start of period	884.2	785.5
Interest income on scheme assets	28.9	44.2
Contributions by employer	26.9	3.7
Contributions by plan participants	0.2	0.2
Benefits paid	(44.5)	(43.7)
Return on assets (excluding amounts included in finance costs)	(25.5)	94.3
At end of period	**870.2**	**884.2**

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 they have 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.

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 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 their investment strategy in light of the revised term and nature of the Scheme's liabilities.

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.

Change in assumptions compared with actuarial assumption for the NWPS:

IMPACT OF CHANGES IN ACTUARIAL ASSUMPTIONS FOR THE NWPS	
	£'m
ACTUARIAL VALUE OF LIABILITIES ON 31 MARCH 2016:	
0.5% decrease in discount rate	1,043.9
1 year increase in life expectancy	988.9
-0.5% change in salary increases	960.1
-0.5% change in inflation	881.3

MATURITY PROFILE OF THE DEFINED BENEFIT OBLIGATION FOR THE YEAR ENDED 31 MARCH 2016:

	NUMBER OF MEMBERS	LIABILITY SPLIT (%)	DURATION (YEARS)
Active members	1,446	38	24.3
Deferred members	1,200	14	21.3
Pensioners	3,149	48	12.3

22. 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 IAS 24 'Related Party Disclosures' from disclosing transactions with other members of the Group headed by NWGL.

Transactions with related parties outside of the NWGL group comprised purchases of £4.7m (15 months ended 31 March 2015: £2.4m), sales of £nil (15 months ended 31 March 2015: £0.1m) and consortium tax relief of £9.5m (15 months ended 31 March 2015: £7.1m). There were no amounts due from or to these companies at 31 March 2016 (15 months ended 31 March 2015: £nil) in respect of sales or purchases. £3.8m (15 months ended 31 March 2015: £9.5m) is owed in respect of tax losses surrendered to Hutchison 3G UK Limited (note 13).

The companies with which NWL had transactions during the year, included in the above balances, were as follows:

- Cheung Kong Infrastructure Holdings Limited;
- Northern Gas Networks Limited;
- Hutchison 3G UK Limited;
- Hutchison Whampoa (Europe) Limited; and
- UK Power Networks (Operations) Limited.

23. 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 Hong Kong Stock Exchange. 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**.

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.

STATUTORY FINANCIAL STATEMENTS

24. TRANSITION TO IFRS

This is the first year the Company has presented its financial statements under FRS 101. The following disclosures are required in the year of transition. The previous financial statements were for the fifteen months ended 31 March 2015, therefore the date of transition to FRS 101 was 1 January 2014.

(A) RECONCILIATION OF EQUITY:

	CASH FLOW HEDGE RESERVE	PROFIT AND LOSS ACCOUNT	SHARE CAPITAL	TOTAL EQUITY
	£'m	£'m	£'m	£'m
AS AT 1 JANUARY 2014				
Equity reported under previous UK GAAP	-	789.0	122.7	911.7
Property, plant and equipment (IAS 16)	-	61.2	-	61.2
Capitalisation of interest (IAS 23)	-	14.1	-	14.1
Financial instruments (IAS 39)	(9.4)	-	-	(9.4)
Borrowings	-	(2.3)	-	(2.3)
Deferred tax	1.9	(125.5)	-	(123.6)
Deferred tax discount	-	(162.5)	-	(162.5)
Equity reported under FRS 101	**(7.5)**	**574.0**	**122.7**	**689.2**
AS AT 31 MARCH 2015				
Equity reported under previous UK GAAP	-	678.8	122.7	801.5
Property, plant and equipment (IAS 16)	-	76.8	-	76.8
Capitalisation of interest (IAS 23)	-	22.5	-	22.5
Financial instruments (IAS 39)	(14.0)	-	-	(14.0)
Borrowings	-	(1.4)	-	(1.4)
Deferred tax	2.8	(77.1)	-	(74.3)
Deferred tax discount	-	(141.1)	-	(141.1)
Equity reported under FRS 101	**(11.2)**	**558.5**	**122.7**	**670.0**

(B) RECONCILIATION OF TOTAL COMPREHENSIVE INCOME FOR THE 15 MONTHS ENDED 31 MARCH 2015:

	£'m
Total comprehensive income for the 15 months under previous UK GAAP	201.3
Property, plant and equipment (IAS 16)	15.6
Capitalisation of interest (IAS 23)	8.4
Financial instruments (IAS 39)	(4.6)
Borrowings	0.9
Deferred tax	49.3
Deferred tax discount	21.4
Total comprehensive income for the 15 month period under FRS 101	**292.3**

(C) NOTES ON RECONCILIATION OF EQUITY AS AT 1 JANUARY 2014:

As stated in note 1(a), upon transition to IFRS, the Company has measured its assets and liabilities at the carrying amounts included in NWGL's consolidated financial statements, which were reported under IFRS. This is in accordance with appendix D16 of IFRS 1 First-time Adoption of IFRS.

Property, plant and equipment (IAS 16)

Adjustments in respect of IAS 16 (£61.2m) have been made to property, plant and equipment (note 9) and grants and deferred income (note 17) to reflect the carrying amount included in NWGL's consolidated financial statements. This principally relates to differences in accounting for maintenance activity on infrastructure assets.

Under previous UK GAAP, as permitted by FRS 15.97, the depreciation charge for infrastructure assets being maintained in a steady state under a certified asset management plan was calculated as the average long term maintenance expenditure, net of contributions. Under IAS 16 this treatment may not be applied. Components of the infrastructure network have been identified and useful economic lives and residual values determined so that each part can be depreciated individually.

As a result, property, plant and equipment has increased by £89.4m and capital grants and deferred income by £28.2m.

Capitalisation of interest (IAS 23)

The net book value of property, plant and equipment has been increased by £14.1m in respect of borrowing costs which have been capitalised as part of the cost of construction of assets, less subsequent depreciation.

Transfers of assets from customers (IFRIC 18)

The carrying value of both property, plant and equipment and deferred capital grants and deferred income has been increased by £57.5m in respect of assets transferred from customers for non-cash consideration, under IFRIC 18. This typically represents network assets and wastewater pumping stations adopted by the Company from developers. This has no net impact on either equity reserves or total comprehensive income.

Financial Instruments (IAS 39)

Under FRS 101, the Company is required to apply IAS 39 Financial Instruments: Recognition and Measurement (note 18). The impact of recognising the fair value of an interest rate swap upon transition, was a liability of £9.4m.

Borrowings

A fair value adjustment of £2.3m was made in the consolidated financial statements of NWGL reflecting a historic transaction which changed the counter party to a finance lease. This has been recognised in the accounts of the Company on transition to IFRS.

Deferred tax

Deferred tax has been provided in respect of the changes to carrying values detailed above. Discounting of deferred tax, which was included in the previous UK GAAP numbers but is not permitted under IAS 12, has been removed.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF NORTHUMBRIAN WATER LIMITED

We have audited the financial statements of Northumbrian Water Limited for the year ended 31 March 2016 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 24. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) including FRS 101 Reduced Disclosure Framework.

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.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR

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. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OPINION ON FINANCIAL STATEMENTS

In our opinion the financial statements:

- Give a true and fair view of the state of the Company's affairs as at 31 March 2016 and of its profit for the year then ended;
- Have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- Have been prepared in accordance with the requirements of the Companies Act 2006.

OPINION ON OTHER MATTER 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 Governance Report (including 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 Governance Report (including 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 and the Governance Report (including the Directors' Report).

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

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

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

Anthony Matthews

Anthony Matthews (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Newcastle Upon Tyne, United Kingdom,
15 July 2016

ANNUAL PERFORMANCE REPORT

INTRODUCTION

The APR sets out the performance in 2015-16 of NWL's regulated business, as defined under our Licence, in both financial terms and against our business outcome performance commitments. The purpose of this report is provide a transparent and reliable account of our performance and to confirm our compliance with the terms of our Licence.

Further information about our performance and governance is available on our websites in a more customer-friendly presentation, at **www.nwl.co.uk**, **www.eswater.co.uk** and **www.welivewater.co.uk**.

The APR has been structured in the following sections and complies with the requirements of Ofwat's Regulatory Accounting Guidelines (RAGs).

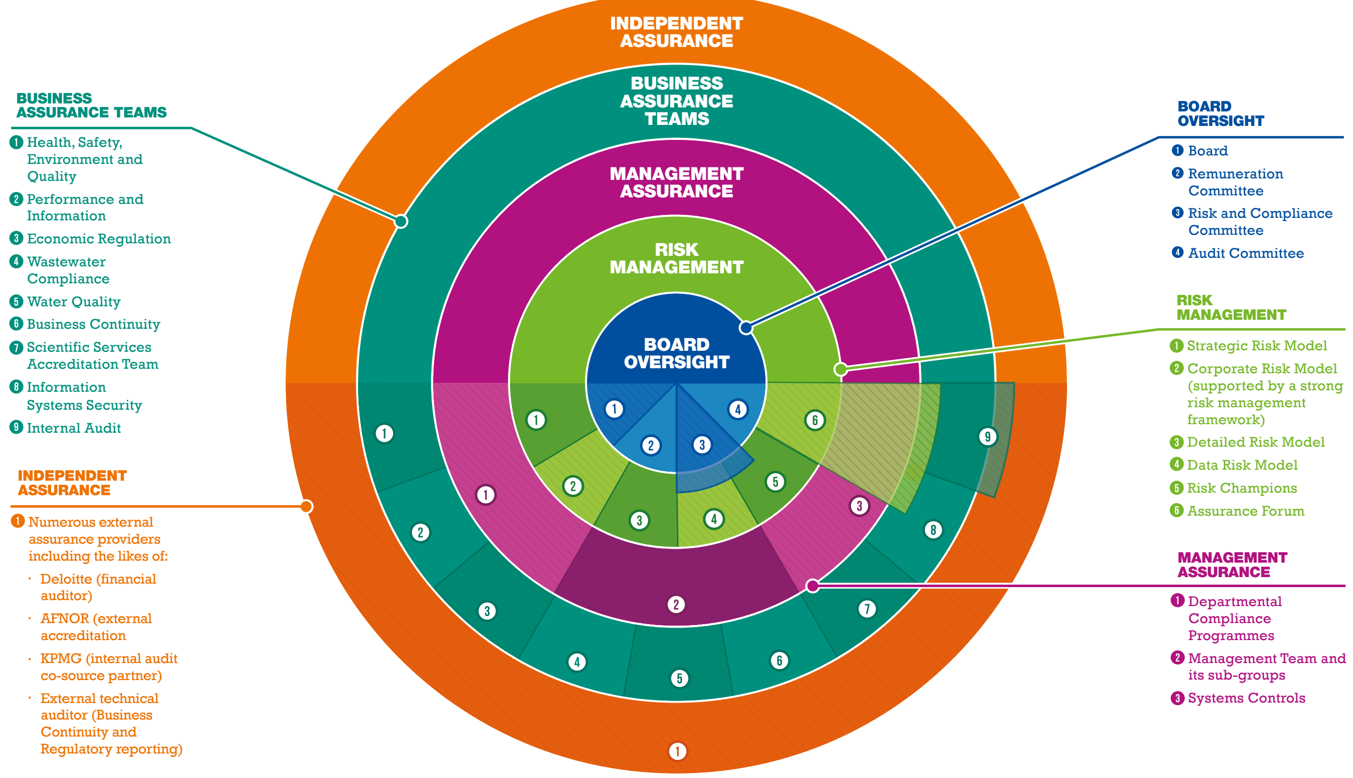
ANNUAL PERFORMANCE REPORT

GOVERNANCE AND ASSURANCE

It is important that we have robust governance and assurance arrangements in place to ensure that the information in this report is accurate, clear and transparent. In doing so, we will continue to provide stakeholders with trust and confidence.

We have well established governance and assurance arrangements, in the form of an assurance framework, which we use to ensure that our information is of appropriate quality. This consists of a number of tiers of assurance, as shown in the diagram below.

ASSURANCE FRAMEWORK



ANNUAL PERFORMANCE REPORT

- **Board Oversight** - The Board has ownership of the arrangements for governance and assurance of regulatory submissions and reporting. This is monitored and controlled through the Board's Audit Committee and Risk & Compliance Committee with regular reporting by the Committees to the Board.
- **Risk Management** - We use a data risk assessment, and a risks, strengths and weaknesses review as part of our regulatory reporting processes, to determine levels of risk and target assurance activity. This is a robust and mature process and is embedded within the Company's risk management processes. The Board sets the tone for risk management, determines the appropriate risk appetite, monitors the management of fundamental risk and approves major decisions affecting the Company's risk profile.
- **Management Assurance** - The Management Team implements the Board's strategies and closely monitors performance. This includes ensuring that sufficient and suitable resources (human and financial) are applied to scrutinise performance and identify and manage risk. The Management Team ensure there is appropriate assignment of responsibilities, corporate structures and reporting lines and accountabilities, supported by annual positive assurances on systems and controls.
- **Business Assurance** - We have many teams who are separate from the operational activities which monitor, capture and manage the data we report. Specifically this includes our Internal Audit Team. Accountable directly to the Audit Committee, this team provides strong, independent assurance. As such their remit sits across this tier and the following one.
- **Independent Assurance** - Our business assurance teams are supplemented with external specialist providers where we require technical and/or external assurance.

DATA ASSURANCE SUMMARY

We have obtained specific independent assurance for each section of our APR.

REGULATORY ACCOUNTING STATEMENTS

The Regulatory Accounting Statements comprise the regulatory accounting policies and disclosures, regulatory financial reporting statements (tables 1A to 1E), price review and other segmental reporting (tables 2A to 2I), Appointed business taxation, the statement on Directors' pay and standards of performance and transactions with associated companies. These can be found on pages 112 to 147.

This section has been audited by Deloitte LLP and the independent auditor's report to Ofwat and Directors of NWL can be found on pages 150 to 153. This confirms that the Regulatory Accounting Statements fairly present the state of the Company's affairs at 31 March 2016 and the profit and cash flow for the year in accordance with Ofwat's RAGs and our Licence obligations.

PERFORMANCE SUMMARY

The arrangements for assurance of our performance against our outcomes, MoS and PCs on pages 154 to 191 have been developed in line with Ofwat's Company Monitoring Framework, published in June 2015, as set out in our Assurance Plan. We published our Assurance Plan in March 2016, after consulting with stakeholders, and it is available on our website at **https://www.nwl.co.uk/your-home/Assurance.aspx**. How we report progress against our PCs for 2015-2020 is a key focus of this plan and the Assurance Plan provides full details of how a risk assessment has been used to target the most appropriate assurance activities for each MoS.

We have applied the approach set out in our Assurance Plan to provide assurance on all of the results reported in Table 3A Outcome Performance Table. This comprises a mix of appropriate independent external assurance and internal assurance from our Internal Audit team.

Our independent technical auditor, Atkins, has submitted an Assurance Statement Report which states:

- At a component level the various teams compiling the documents and information had an understanding of and were meeting their obligations;
- The Company has sufficient processes and internal systems of control to fully meet its obligations;
- The Company has sufficient processes and internal systems in place to identify, manage and review its risks; and
- The Company's explanations of how it will manage and/or mitigate material or potentially material risks are soundly based.

Our Internal Audit Manager confirmed to the Audit Committee that the assurance work was carried out in accordance with the Assurance Plan and that any material items identified have been corrected. Recommendations have been made where processes could be improved as part of our commitment to continuous improvement.

The performance against MoS and associated narrative explanation have been considered by the Company's Audit Committee on behalf of the Board.

ADDITIONAL REGULATORY INFORMATION

Independent assurance of the additional regulatory information in tables 4A to 4I, on pages 192 to 209, has been provided by Deloitte LLP under a separate engagement to their audit opinions on the Statutory Financial Statements and Regulatory Accounting Statements.

Deloitte has carried out agreed upon procedures which broadly comprise confirming that the information contained in the tables has been calculated in a consistent manner with the RAGs, agreeing information back to supporting documentation and verifying the accuracy of calculations. In addition, for tables 4D to 4F Deloitte has confirmed that the information has been prepared in accordance with the Company's accounting separation methodology, which is published on our websites.

ANNUAL PERFORMANCE REPORT

DIRECTORS' RESPONSIBILITIES AND DECLARATIONS

FOR THE YEAR ENDED 31 MARCH 2016

DIRECTORS' RESPONSIBILITIES STATEMENT

The Directors are responsible under Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewerage undertaker under the Water Industry Act 1991 for:

- Ensuring that proper accounting records are maintained by the Appointee to enable compliance with the requirements of Condition F and having regard also to the terms of guidelines notified by the Water Services Regulation Authority ('the Authority') to the Appointee from time to time;
- Preparing on a consistent basis for each financial year regulatory accounts in accordance with Condition F, having regard also to the terms of guidelines notified by the Authority from time to time, which so far as is reasonably practicable have the same content as the annual financial statements of the Appointee prepared under the Companies Act 2006 and which are prepared in accordance with the formats, accounting policies and principles which apply to those financial statements; and
- Preparing such other financial and related information as is required by Condition F having regard also to the terms of guidelines issued by the Authority from time to time.

RISK AND COMPLIANCE STATEMENT

The Board confirms that:

- It considers the Company has a full understanding of, and is meeting, its obligations and has taken steps to understand and meet customer expectations;
- It has satisfied itself that the Company has sufficient processes and internal systems of control to fully meet its obligations; and
- The Company has appropriate systems and processes in place to allow it to identify, manage and review its risks.

DISCLOSURE OF INFORMATION TO AUDITORS

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.

CONDITION K (RING FENCING)

The Directors confirm that, as at 31 March 2016, the Company was in compliance with paragraph 3.1 of Condition K of the Instrument of Appointment in that the Appointee had available to it sufficient rights and assets to enable a special administrator to manage the affairs, business and property of the Appointee, should a special administration order be made.

CONDITION F6A.2A CERTIFICATE (FINANCIAL AND MANAGEMENT RESOURCES TO CARRY OUT THE REGULATED ACTIVITIES)

The Directors certify that, in their opinion:

- The Appointee will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months the Regulated Activities (including the investment programme necessary to fulfil the Appointee's obligations under the Appointment);
- The Appointee will, for at least the next 12 months, have available to it management resources and systems of planning and internal control which are sufficient to enable it to carry out those functions as required by subparagraph 6A.1 of Condition F of the Instrument of Appointment; and
- All contracts entered into with any Associated Company include all necessary provisions and requirements concerning the standard of service to be supplied to the Appointee, to ensure that it is able to meet all its obligations as a water and sewerage undertaker.

In providing this certificate, 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 April 2016;
- 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 £350m of five year committed bank facilities as back up liquidity (maturing in 2019), and a further £100m of committed financing from the EIB, both of which were undrawn at 31 March 2016; and
- The Company's formal governance and risk management arrangements which are monitored by the Audit Committee, Risk & Compliance Committee and Board.

CONDITION F6A.6 (CREDIT RATING)

The Directors also confirm that throughout 2015-16 the Appointee has ensured that it, and an Associated Company as issuer of debt on its behalf, has maintained at all times an issuer credit rating which is a strong investment grade rating.

VIABILITY STATEMENT

The Directors believe that the Appointed Business is well placed to manage its business risks successfully and expect that the business can continue to operate effectively over the long term and, specifically, meet its financial obligations over the next four years. Further information in respect of this statement is provided in the Governance Report on page 55.

MParker

By order of the Board
M Parker
Company Secretary
15 July 2016

REGULATORY ACCOUNTING POLICIES AND DISCLOSURES

FOR THE YEAR ENDED 31 MARCH 2016

(A) REGULATORY ACCOUNTS - BASIS OF ACCOUNTING

The Regulatory Accounting Statements, on pages 112 to 147 of the APR, have been prepared in accordance with the RAGs issued by Ofwat. They have been prepared on a consistent basis to the Statutory Financial Statements, applying the accounting policies set out on pages 65 to 69, with the following exceptions:

- Income relating to energy generation, which is recorded as revenue in the statutory accounts, has been recorded as negative operating expenditure;
- Rental income, which is recorded as revenue in the statutory accounts, has been recorded as other income below operating profit;
- Profit on disposal of fixed assets, which is recorded as operating costs in the statutory accounts, has been recorded as other operating income; and
- Borrowing costs that are directly attributable to the acquisition or construction of an asset, which are capitalised in the statutory accounts, are charged to the income statement.

The information reported in the Regulatory Accounting Statements relates to NWL's Appointed business only, except where stated. The Appointed business comprises Regulated Activities, defined in Condition A of the Licence to be 'functions of' and the 'duties imposed on' a water and sewerage undertaker by the Water Industry Act 1991. Such duties are consequently those necessary for the Company to fulfil its duty as a water and sewerage undertaker.

The accounts have been prepared on a going concern basis which assumes that the Company will have adequate funding to meet its liabilities as they fall due in the foreseeable future.

(B) REVENUE RECOGNITION

The revenue recognition policy is the same in the regulatory and statutory accounts, other than the exceptions related to income from energy generation and rental income, as explained above.

RAG3 states that companies should not de-recognise turnover for amounts billed which they deem to be uncollectable, meaning that IAS 18.9 should be disapplied in this respect. NWL complies with this requirement.

Revenue from water and sewerage charges billed to customers is recognised pro-rata over the period to which it related. For consumption by measured customers which has not yet been billed, revenue is estimated and accrued using a defined methodology based upon historical usage and the relevant tariff per customer. Invoices raised or payments received where the service has not been provided are not recognised in revenue in the year but are treated as receipts in advance.

Additional charges added to a customer's account as a result of debt recovery activity, such as court costs or solicitors fees, are recognised as negative operating costs when payment is received in both the statutory and regulatory accounts. They are not recognised in revenue.

Charges for water and sewerage services remain due in full whilst a property contains furnishings and fittings or when a property is unfurnished and water is being used for any purpose including refurbishment. If the Company has turned off the supply of water at the mains to a property at a customer's request then water supply charges are not payable.

If the supply of water is turned off and the property is unfurnished the property is considered unoccupied and charges are not payable. If, however, the supply of water is turned off and the property remains furnished it is considered ready for occupation and in this case sewerage charges in respect of the drainage of surface water and contribution to highway drainage continue to be payable.

If a property is recorded as empty in the billing system an empty property process is followed. The purpose of this process is to verify whether the property is occupied or not and, if occupied, to identify the chargeable person and raise a bill. No bills are raised in the name of 'the occupier'.

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The empty property process comprises a number of steps including an initial letter asking the occupier to either contact the Company or return a completed registration form, a check of the property record against Land Registry information and visits to the property by Company representatives. If these steps confirm that a property appears to be empty then the supply may be turned off.

New properties are charged from the date a meter is installed, if consumption is being recorded on the meter. If the property is unoccupied but water is being registered the developer will be charged. Once the developer is no longer responsible for a property, if no new occupier has been identified the property will be treated as unoccupied and the empty property process followed, as outlined above.

A retrospective review has confirmed that there were no significant differences between the measured income accrual at 31 March 2015 of £59.0m and the amounts subsequently billed to customers of £58.7m.

(C) BAD DEBT POLICY

The policy for bad and doubtful debts is applied consistently between the statutory and regulatory accounts in accordance with the policy stated in note 1(o) of the Statutory Financial Statements.

(D) CAPITALISATION POLICY

The policy for the capitalisation of costs as items of property, plant and equipment is applied consistently between the statutory and regulatory accounts in accordance with the policy stated in note 1(d) of the Financial Statements and
in accordance with IAS 16 property, plant and equipment.

The application of this policy is summarised below. Further detail is provided in the accounting separation methodology statement published on our websites.

The cost of construction or purchase of new or replacement infrastructure and non-infrastructure assets is capitalised. Cost includes any costs directly attributable to bringing the asset into condition for use in the business, including directly attributable overhead costs but excluding general overhead costs. The costs of infrastructure and non-infrastructure assets are depreciated over their useful economic lives.

On the infrastructure network, capital replacement of assets includes any renewal of a full pipe length of main or sewer and replacement of ancillaries such as stop taps, valves, meter chambers and manhole covers.

Subsequent maintenance expenditure is treated as an operating cost unless it provides an enhancement of economic benefits in excess of the expected standard of performance such as an extension in the estimated useful life or an increase in capacity, in which case it is capitalised. Examples of maintenance costs charged as operating costs include pipe and tank cleaning, inspections, surveys and zonal studies.

Further detail is provided in the accounting separation methodology statement published on our websites.

(E) ACCOUNTING SEPARATION POLICY

Cost allocations have been prepared in accordance with RAG 2.05 and RAG 4.05 for the definitions for the regulatory accounting tables. All costs are recorded in the accounting records by cost centre. Cost centres are defined either as a direct department, comprising operational and customer functions, or a support department. Direct departments are mostly directly allocated to service activities based on the nature of the function, although some costs require apportionment on an appropriate basis. Support departments are apportioned across the price controls either based upon a specific analysis of the costs or by apportionment by an appropriate cost driver. Once allocated to the appropriate price control the costs are then allocated to service activities pro-rata to full time equivalent staff numbers of the direct departments.

Fixed assets directly involved in the activities within each business unit are recorded against that business unit using direct allocation per the location or asset type. Where an asset is utilised in more than one business unit, the asset is allocated to the business unit of principal use and costs are recharged to other different business units on the same basis used to allocate operating expenditure.

Further detail is provided in the accounting separation methodology statement published on our websites.

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SECTION 1: REGULATORY FINANCIAL REPORTING

1A INCOME STATEMENT
FINANCIAL PERFORMANCE FOR THE 12 MONTHS ENDED 31 MARCH 2016

		ADJUSTMENTS			
	STATUTORY	DIFFERENCES BETWEEN STATUTORY AND RAG DEFINITIONS	NON-APPOINTED	TOTAL ADJUSTMENTS	TOTAL APPOINTED ACTIVITIES
	£'m	£'m	£'m	£'m	£'m
Revenue	805.5	(7.2)	(26.1)	(33.3)	772.2
Operating costs	(432.8)	5.8	16.5	22.3	(410.5)
Other operating income	-	0.4	-	0.4	0.4
Operating profit	**372.7**	**(1.0)**	**(9.6)**	**(10.6)**	**362.1**
Other income	-	2.2	(2.0)	0.2	0.2
Interest income	10.0	-	(9.7)	(9.7)	0.3
Interest expense	(112.8)	(5.4)	-	(5.4)	(118.2)
Other interest expense	(2.1)	-	-	-	(2.1)
Profit before tax and fair value movements	**267.8**	**(4.2)**	**(21.3)**	**(25.5)**	**242.3**
Fair value gains/(losses) on financial instruments	(1.4)	-	-	-	(1.4)
Profit before tax	**266.4**	**(4.2)**	**(21.3)**	**(25.5)**	**240.9**
UK Corporation tax	(33.3)	-	2.9	2.9	(30.4)
Deferred tax	29.8	0.3	(0.1)	0.2	30.0
Profit for the year	**262.9**	**(3.9)**	**(18.5)**	**(22.4)**	**240.5**

Differences between statutory and RAG definitions are explained in note (a) of the Regulatory Accounting Policies and Disclosures.

The change to profit reflects borrowing costs, which are capitalised in the Statutory Financial Statements but charged to the income statement in the Regulatory Accounting Statements, and the associated depreciation and deferred tax. Other changes are presentational in nature:

- Income relating to energy generation has been reclassified from revenue in the statutory accounts to negative operating costs;
- Rental income has been reclassified from revenue in the statutory accounts to other income; and
- Profit on disposal of fixed assets has been reclassified from operating costs in the statutory accounts to other operating income.

1B STATEMENT OF COMPREHENSIVE INCOME
FINANCIAL PERFORMANCE FOR THE 12 MONTHS ENDED 31 MARCH 2016

		ADJUSTMENTS			
	STATUTORY	DIFFERENCES BETWEEN STATUTORY AND RAG DEFINITIONS	NON-APPOINTED	TOTAL ADJUSTMENTS	TOTAL APPOINTED ACTIVITIES
	£'m	£'m	£'m	£'m	£'m
Profit for the year	262.9	(3.9)	(18.5)	(22.4)	240.5
Actuarial losses on post employment plans	(41.9)	-	0.5	0.5	(41.4)
Other comprehensive income	(13.0)	-	-	-	(13.0)
Total Comprehensive income for the year	**208.0**	**(3.9)**	**(18.0)**	**(21.9)**	**186.1**

1C STATEMENT OF FINANCIAL POSITION
FINANCIAL PERFORMANCE FOR THE 12 MONTHS ENDED 31 MARCH 2016
(REGISTERED NUMBER 02366703)

		ADJUSTMENTS			
	STATUTORY	DIFFERENCES BETWEEN STATUTORY AND RAG DEFINITIONS	NON-APPOINTED	TOTAL ADJUSTMENTS	TOTAL APPOINTED ACTIVITIES
	£'m	£'m	£'m	£'m	£'m
NON-CURRENT ASSETS					
Fixed assets	4,169.6	(26.9)	(97.4)	(124.3)	4,045.3
Intangible assets	-	-	-	-	-
Investments - loans to group companies	160.9	-	(160.9)	(160.9)	-
Investments - other	-	-	-	-	-
Total non-current assets	**4,330.5**	**(26.9)**	**(258.3)**	**(285.2)**	**4,045.3**
CURRENT ASSETS					
Inventories	2.4	-	(0.4)	(0.4)	2.0
Trade & other receivables	185.7	41.2	(3.3)	37.9	223.6
Cash & cash equivalents	-	36.5	(36.5)	-	-
Total current assets	**188.1**	**77.7**	**(40.2)**	**37.5**	**225.6**
CURRENT LIABILITIES					
Trade & other payables	(125.7)	(39.6)	43.0	3.4	(122.3)
Capex creditor	(32.3)	-	0.8	0.8	(31.5)
Borrowings	(105.3)	(36.5)	-	(36.5)	(141.8)
Current tax liabilities	-	(1.5)	1.5	-	-
Provisions	(0.2)	-	-	-	(0.2)
Total current liabilities	**(263.5)**	**(77.6)**	**45.3**	**(32.3)**	**(295.8)**
Net current assets / (liabilities)	**(75.4)**	**0.1**	**5.1**	**5.2**	**(70.2)**

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		ADJUSTMENTS			
	STATUTORY	DIFFERENCES BETWEEN STATUTORY AND RAG DEFINITIONS	NON-APPOINTED	TOTAL ADJUSTMENTS	TOTAL APPOINTED ACTIVITIES
	£'m	£'m	£'m	£'m	£'m
NON-CURRENT LIABILITIES					
Trade & other payables	-	-	-	-	-
Borrowings	(2,549.0)	-	-	-	(2,549.0)
Financial instruments	(31.3)	-	-	-	(31.3)
Retirement benefit obligations	(89.9)	-	1.9	1.9	(88.0)
Provisions	(1.4)	-	-	-	(1.4)
Deferred income - grants and contributions	(511.8)	-	135.0	135.0	(376.8)
Deferred tax	(404.7)	4.9	1.5	6.4	(398.3)
Total non-current liabilities	**(3,588.1)**	**4.9**	**138.4**	**143.3**	**(3,444.8)**
Net assets	**667.0**	**(21.9)**	**(114.8)**	**(136.7)**	**530.3**
EQUITY					
Called up share capital	122.7	-	(30.6)	(30.6)	92.1
Retained earnings & other reserves	544.3	(21.9)	(84.2)	(106.1)	438.2
Total Equity	**667.0**	**(21.9)**	**(114.8)**	**(136.7)**	**530.3**

Heidi Mottram

Approved by the Board of Directors on 15 July 2016 and signed on their behalf by:
H Mottram

Differences between statutory and RAG definitions are explained in note (a) of the Regulatory Accounting Policies and Disclosures.

Differences in relation to fixed assets and retained earnings reflect borrowing costs, which are capitalised in the Statutory Financial Statements but charged to the income statement in the Regulatory Accounting Statements, and the associated depreciation and deferred tax. Other changes reflect trading balances between the appointed and non-appointed businesses, which were settled immediately after the balance sheet date.

1D STATEMENT OF CASH FLOWS FOR THE APPOINTED BUSINESS
FINANCIAL PERFORMANCE FOR THE 12 MONTHS ENDED 31 MARCH 2016

	TOTAL APPOINTED ACTIVITIES
	£'m
Operating profit	362.1
Other income	0.2
Depreciation	123.3
Amortisation of grants and contributions	(5.7)
Changes in working capital	(41.6)
Pension contributions	(26.4)
Movement in provisions	(8.3)
Profit on sale of fixed assets	(0.4)
Cash generated from operations	**403.2**
Net interest paid	(103.6)
Tax received	16.1
Net cash generated from operating activities	**315.7**
INVESTING ACTIVITIES	
Capital expenditure	(206.3)
Grants & contributions	23.7
Disposal of fixed assets	1.6
Other	-
Net cash used in investing activities	**(181.0)**
Net cash generated before financing activities	**134.7**

Table continued on next page

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	TOTAL APPOINTED ACTIVITIES
	£'m
CASHFLOWS FROM FINANCING ACTIVITIES	
Equity dividends paid	(200.0)
Net loans received	33.8
Cash inflow from equity financing	-
Net cash generated from financing activities	**(166.2)**
Decrease in net cash	**(31.5)**

1E NET DEBT ANALYSIS AS AT 31 MARCH 2016 APPOINTED BUSINESS ONLY

	INTEREST RATE RISK PROFILE			
	FIXED RATE	FLOATING RATE	INDEX LINKED	TOTAL
	£'m	£'m	£'m	£'m
Borrowings (excluding preference shares)	1,659.7	226.9	804.2	2,690.8
Preference share capital				-
Total borrowings				**2,690.8**
Cash				-
Short term deposits				-
Net Debt				**2,690.8**
Gearing %				69.5%
Adjusted gearing				**69.5%**
Full year equivalent nominal interest cost	94.8	5.6	17.7	118.1
Full year equivalent cash interest payment	94.8	5.6	10.2	110.6
INDICATIVE INTEREST RATES				
Indicative weighted average nominal interest rate	5.71%	2.46%	2.20%	4.39%
Indicative weighted average cash interest rate	5.71%	2.46%	1.27%	4.11%

SECTION 2: PRICE REVIEW AND OTHER SEGMENTAL REPORTING

2A SEGMENTAL INCOME STATEMENT FOR THE 12 MONTHS ENDED 31 MARCH 2016

	RETAIL		WHOLESALE		
	HOUSEHOLD	NON-HOUSEHOLD	WATER	WASTEWATER	TOTAL
	£'m	£'m	£'m	£'m	£'m
Revenue - price control	57.1	9.2	406.8	289.6	762.7
Revenue - non price control	0.5	0.3	6.3	2.4	9.5
Operating costs	(44.1)	(6.9)	(231.6)	(127.9)	(410.5)
Other operating income	0.1	-	0.5	(0.2)	0.4
Operating profit before recharges	**13.6**	**2.6**	**182.0**	**163.9**	**362.1**
Recharges from other segments	(1.3)	(0.2)	-	(5.2)	(6.7)
Recharges to other segments	0.1	-	6.6	-	6.7
Operating profit	**12.4**	**2.4**	**188.6**	**158.7**	**362.1**

Surface water drainage rebates	**0.4**

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2B TOTEX ANALYSIS: WHOLESALE WATER AND WASTEWATER FOR THE 12 MONTHS ENDED 31 MARCH 2016

	WATER	WASTEWATER	TOTAL
	£'m	£'m	£'m
OPERATING EXPENDITURE			
Power	20.3	14.5	34.8
Income treated as negative expenditure	(0.2)	(4.0)	(4.2)
Service charges/ discharge consents	22.0	2.5	24.5
Bulk supply/ Bulk discharge	2.7	-	2.7
Other operating expenditure	82.8	56.5	139.3
Local authority rates	23.1	6.4	29.5
Total operating expenditure excluding third party services	**150.7**	**75.9**	**226.6**
Third party services	13.8	3.7	17.5
Total operating expenditure	**164.5**	**79.6**	**244.1**
CAPITAL EXPENDITURE			
Maintaining the long term capability of the assets - infra	24.6	18.1	42.7
Maintaining the long term capability of the assets - non- infra	61.8	34.8	96.6
Other capital expenditure - infra	16.5	25.0	41.5
Other capital expenditure - non-infra	3.8	10.6	14.4
Total gross capital expenditure excluding third party services	**106.7**	**88.5**	**195.2**
Third party services	-	-	-
Total gross capital expenditure	**106.7**	**88.5**	**195.2**
Grants and contributions (price control)	**(11.7)**	**(4.8)**	**(16.5)**
Totex	**259.5**	**163.3**	**422.8**

Table continued on next page

	WATER	WASTEWATER	TOTAL
	£'m	£'m	£'m
CASH EXPENDITURE			
Pension deficit recovery payments	5.6	2.8	8.4
Other cash items	17.1	8.7	25.8
TOTAL			
Totex including cash items	**282.2**	**174.8**	**457.0**

Pension deficit recovery payments represents the wholesale proportion of the £11m deficit reduction payments made to the NWPS pension scheme during the year (see note 21 of the statutory financial statements), which is not reflected in the accounting pension charge.

Other cash items reflects the difference between the accounting pension charge included within other operating expenditure, and the wholesale proportion of employer's cash contributions to the NWPS (excluding deficit reduction payments). This is a large positive value in the year because the accounting charge included an exceptional, non-cash credit reflecting changes made to future benefit, as described in note 3 of the Statutory Financial Statements.

2C OPERATING COST ANALYSIS: RETAIL FOR THE 12 MONTHS ENDED 31 MARCH 2016

	HOUSEHOLD	NON-HOUSEHOLD	TOTAL
	£'m	£'m	£'m
OPERATING EXPENDITURE			
Customer services	12.7	1.7	14.4
Debt management	4.7	0.3	5.0
Doubtful debts	20.6	3.9	24.5
Meter reading	2.2	0.4	2.6
Services to developers	-	0.2	0.2
Other operating expenditure	1.0	0.4	1.4
Total operating expenditure excluding third party services	**41.2**	**6.9**	**48.1**
Third party services operating expenditure	0.1	-	0.1
Total operating expenditure	**41.3**	**6.9**	**48.2**
Depreciation	2.8	-	2.8
Total operating costs	**44.1**	**6.9**	**51.0**
Debt written off	**7.9**	**4.4**	**12.3**

RETAIL COST RECONCILIATION TO FD

Household retail costs include an atypical non-cash accounting pension credit of £7.6m (see note 3 of the Statutory Financial Statements). Removing this credit from the total operating expenditure reported above would give an underlying household retail cost of £48.9m. This is £2.4m lower than the PR14 FD allowance of £51.3m.

In accordance with changes in RAG 2.05 guidance, some costs which were classified as retail costs at PR14 have now been allocated to wholesale water services. This specifically relates to activity on customer side leaks and demand-side water efficiency where the main driver is to manage leakage as part of our wholesale outcome 'we provide a reliable and sufficient supply of water'. The total costs reclassified are £4.1m, as reported on table 4F.

Compared on a like for like basis, underlying household retail costs would therefore be £1.7m higher than PR14 FD, reflecting inflationary pressures on costs which were not included in the allowance.

Non-household retail costs include atypical items in respect of a non-cash accounting pension credit of £0.8m (see note 3 of Statutory Financial Statements) and £2.6m bad debt write off due to the closure of a large industrial customer. Removing these items from the total operating expenditure reported above would give an underlying non-household retail cost of £5.1m. This is £0.2m higher than the PR14 FD allowance of £4.9m, reflecting inflationary pressures on costs which were not included in the allowance.

2D HISTORIC COST ANALYSIS OF FIXED ASSETS: WHOLESALE AND RETAIL

	WHOLESALE		RETAIL		
	WATER	WASTEWATER	HOUSEHOLD	NON-HOUSEHOLD	TOTAL
	£'m	£'m	£'m	£'m	£'m
COST					
At 1 April 2015	2,942.9	2,580.3	31.4	-	5,554.6
Disposals	(4.9)	(3.2)	(1.5)	-	(9.6)
Additions	106.8	93.3	7.6	5.2	212.9
At 31 March 2016	**3,044.8**	**2,670.4**	**37.5**	**5.2**	**5,757.9**
DEPRECIATION					
At 1 April 2015	(924.1)	(656.0)	(15.9)	-	(1,596.0)
Disposals	4.6	1.2	1.0	-	6.8
Charge for the year	(70.3)	(50.3)	(2.8)	-	(123.4)
At 31 March 2016	**(989.8)**	**(705.1)**	**(17.7)**	**-**	**(1,712.6)**
Net book amount at 31 March 2016	**2,055.0**	**1,965.3**	**19.8**	**5.2**	**4,045.3**
Net book amount at 1 April 2015	**2,018.8**	**1,924.3**	**15.5**	**-**	**3,958.6**

2E ANALYSIS OF CAPITAL CONTRIBUTIONS AND LAND SALES: WHOLESALE FOR THE 12 MONTHS ENDED 31 MARCH 2016

	FULLY RECOGNISED IN INCOME STATEMENT	CAPITALISED AND AMORTISED AGAINST DEPRECIATION	FULLY NETTED OFF CAPEX	TOTAL
	£'m	£'m	£'m	£'m
GRANTS AND CONTRIBUTIONS - WATER				
Connection charges (s45)	-	5.8	-	5.8
Infrastructure charge receipts (s146)	-	4.5	-	4.5
Requisitioned mains (s43, s55 & s56)	-	1.4	-	1.4
Diversions (s185)	-	1.4	-	1.4
Other Contributions	-	0.2	-	0.2
Total	**-**	**13.3**	**-**	**13.3**
GRANTS AND CONTRIBUTIONS - WASTEWATER				
Infrastructure charge receipts (s146)	-	3.0	-	3.0
Requisitioned sewers (s100)	-	1.8	-	1.8
Diversions (s185)	-	7.3	-	7.3
Other Contributions	-	1.0	-	1.0
Total	**-**	**13.1**	**-**	**13.1**

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	WATER	WASTE WATER	TOTAL
	£'m	£'m	£'m
BALANCE SHEET			
Brought forward	228.3	127.3	355.6
Capitalised in year	13.4	10.3	23.7
Adopted assets	0.3	4.5	4.8
Disposals	-	(1.7)	(1.7)
Amortisation (in income statement)	(3.8)	(1.8)	(5.6)
Carried forward	**238.2**	**138.6**	**376.8**
Land Sales	**1.7**	**-**	**1.7**

The upper section of the table reflects grants and contributions received in the year on a cash basis, being £13.3m water and £13.1m wastewater. The lower section of the table reflects grants and contributions capitalised during the year on capital schemes which have been commissioned, being £13.4m water and £10.3m wastewater.

Grants and contributions falling within the wholesale price control, and therefore also reported on table 2B, comprise connection charges, infrastructure charge receipts and requisitioned mains and sewers.

2F HOUSEHOLD REVENUES BY CUSTOMER TYPE

	WHOLESALE CHARGES REVENUE	RETAIL REVENUE	TOTAL REVENUE	NUMBER OF CUSTOMERS	AVERAGE HOUSEHOLD RETAIL REVENUE PER CUSTOMER
	£'m	£'m	£'m	000s	£
Unmeasured water only customer	78.6	7.6	86.2	309.7	24.6
Unmeasured wastewater only customer	7.0	0.3	7.3	33.8	10.4
Unmeasured water and wastewater customer	264.1	23.3	287.4	720.5	32.3
Measured water only customer	76.6	12.0	88.6	424.1	28.2
Measured wastewater only customer	5.0	0.4	5.4	31.5	13.4
Measured water and wastewater customer	94.5	13.5	108.0	341.1	39.5
Total	**525.8**	**57.1**	**582.9**	**1,860.7**	**30.7**

2G NON-HOUSEHOLD WATER REVENUES BY CUSTOMER TYPE

	WHOLESALE CHARGES REVENUE	RETAIL REVENUE	TOTAL REVENUE	NUMBER OF CUSTOMERS	AVERAGE NON-HOUSEHOLD RETAIL REVENUE PER CUSTOMER
	£'m	£'m	£'m	nr	£
NON-DEFAULT TARIFFS					
Total non-default tariffs	**1.1**	**-**	**1.1**	**6**	**-**
DEFAULT TARIFFS					
Cust type 01, Unmeasured, Unmeas Water N, Unmeasured	1.7	0.2	1.9	6,456	33.2
Cust type 02, Unmeasured, Unmeas Water S, Unmeasured	0.7	0.1	0.8	1,749	36.2
Cust type 03, Measured, Meas Water N std, Measured	29.2	2.9	32.1	49,987	57.8
Cust type 04, Measured, Meas Water N f20, Measured	3.7	0.2	3.9	115	1,550.1
Cust type 05, Measured, Meas Water N fx, Measured	4.3	0.2	4.5	45	3,841.7
Cust type 06, Measured, Meas Water N f+, Measured	11.4	0.1	11.5	25	5,522.0
Cust type 07, Measured, Meas Water S std, Measured	24.1	1.7	25.8	34,128	50.1
Cust type 08, Measured, Meas Water S f20, Measured	2.7	0.1	2.8	68	1,076.0
Cust type 09, Measured, Meas Water S fx, Measured	3.5	0.1	3.6	29	3,967.7
Cust type 10, Measured, Meas Water S f+, Measured	2.9	-	2.9	8	5,661.7
Cust type 15, Measured, Ind Water, Measured	6.8	0.1	6.9	13	7,040.8
Total default tariffs	**91.0**	**5.7**	**96.7**	**92,623**	**61.5**
Total	**92.1**	**5.7**	**97.8**	**92,629**	**61.5**

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2H NON-HOUSEHOLD WASTEWATER REVENUE BY CUSTOMER TYPE

	WHOLESALE CHARGES REVENUE	RETAIL REVENUE	TOTAL REVENUE	NUMBER OF CUSTOMERS	AVERAGE NON-HOUSEHOLD RETAIL REVENUE PER CUSTOMER
	£'m	£'m	£'m	nr	£
NON-DEFAULT TARIFFS					
Total non-default tariffs	**-**	**-**	**-**	**-**	**-**
DEFAULT TARIFFS					
Cust type 11, Unmeasured, Unmeas Sew, Unmeasured	4.2	0.4	4.6	10,688	34.8
Cust type 12, Measured, Meas Sew - std, Measured	58.2	2.8	61.0	44,046	62.5
Cust type 13, Measured, Meas Sew - LU, Measured	4.0	0.1	4.1	26	3,681.1
Cust type 14, Measured, Trade Effluent - std, Measured	6.8	0.2	7.0	381	509.7
Cust type 16, Measured, Trade Effluent - Special Agreement, measured	5.3	-	5.3	6	8,578.6
Total default tariffs	**78.5**	**3.5**	**82.0**	**55,147**	**62.8**
Total	**78.5**	**3.5**	**82.0**	**55,147**	**62.8**

2I REVENUE ANALYSIS FOR THE 12 MONTHS ENDED 31 MARCH 2016

	HOUSEHOLD	NON-HOUSEHOLD	TOTAL
	£'m	£'m	£'m
WHOLESALE CHARGE - WATER			
Unmeasured	197.0	2.4	199.4
Measured	117.7	82.9	200.6
Third party revenue	-	6.8	6.8
Total	**314.7**	**92.1**	**406.8**
WHOLESALE CHARGE - WASTEWATER			
Unmeasured	152.7	4.2	156.9
Measured	58.4	74.3	132.7
Third party revenue	-	-	-
Total	**211.1**	**78.5**	**289.6**
Wholesale Total	**525.8**	**170.6**	**696.4**
RETAIL REVENUE			
Unmeasured	31.2	0.7	31.9
Measured	25.9	8.4	34.3
Retail third party revenue	-	0.1	0.1
Retail total	**57.1**	**9.2**	**66.3**
THIRD PARTY REVENUE - NON-PRICE CONTROL			
Bulk Supplies			2.3
Other third party revenue			5.9
Other appointed revenue			1.3
Total appointed revenue			**772.2**

Table continued on next page

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	WATER	WASTEWATER	TOTAL
	£'m	£'m	£'m
Wholesale revenue governed by price control	406.8	289.6	696.4
Grants & contributions	11.7	4.8	16.5
Total revenue governed by wholesale price control	**418.5**	**294.4**	**712.9**
Amount assumed in wholesale determination	**413.6**	**294.8**	**708.4**
DIFFERENCE	**4.9**	**(0.4)**	**4.5**

WHOLESALE REVENUE CONTROL RECONCILIATION TO FD

Wholesale water revenue was £4.9m (1.2%) higher than the revenue allowance from the PR14 price control. This comprised £3.1m from standard published water charges and £1.8m from grants and contributions. The higher water charges primarily related to higher than expected water usage by households in ESW and by non-households in the NW region. Higher new development activity generated more infrastructure charges and new connection charges than expected.

The numbers of reported properties were broadly in line with forecast and the number of void properties increased slightly. These movements did not generate material differences from the allowed revenue.

Wholesale wastewater revenue was £0.4m (0.1%) lower than the allowed revenue. Whilst capital contributions from new development activity were £1.7m higher than forecast and the higher water usage was reflected in wastewater revenue, these were more than offset by the impact of the closure of a large non-household customer.

It is planned that the wholesale revenue allowances to be recovered in 2017-18 will be adjusted to take account of the over recovery on water and under recovery on wastewater occurring in 2015-16. This assumes that the relevant Licence modifications are made.

APPOINTED BUSINESS TAXATION FOR THE 12 MONTHS ENDED 31 MARCH 2016

	TOTAL APPOINTED ACTIVITIES
	£'m
Profit on ordinary activities before tax	**240.9**
Profit on ordinary activities multiplied by standard rate of corporation tax of 20%	**48.2**
EFFECTS OF:	
Expenses not deductible for tax purposes	0.1
Non-taxable income and other tax reliefs	(0.1)
Depreciation in respect of non-qualifying items	0.9
Permanent differences on transition to FRS101	0.5
Consortium relief payable at less than the standard rate	(1.9)
Impact of tax rate change on deferred tax	(45.9)
Deferred tax movement not at average rate for year	(1.8)
Adjustments in respect of prior years	0.4
Transfer pricing adjustments	(0.8)
Balancing payment payable	0.8
Total tax charge	**0.4**

CURRENT TAX RECONCILIATION TO FD

The difference between tax allowed in the FD of £79.7m and the current tax charge for the Appointed business of £30.4m (per table 1A on page 114) is principally due to amounts subject to tax on the transition to FRS 101. The FD included anticipated charges in relation to changes in accounting for infrastructure maintenance expenditure under FRS 101, which may not now be incurred, subject to agreement with HMRC.

ANNUAL PERFORMANCE REPORT

DISCLOSURE OF TRANSACTIONS WITH ASSOCIATES

SERVICES SUPPLIED BY THE APPOINTEE TO ASSOCIATED COMPANIES:

ASSOCIATE	SERVICE	TURNOVER	TERMS OF SUPPLY	VALUE
		£'m		£'m
AquaGib	Sale of materials	12.7	Negotiated	0.2
Vehicle Lease and Service Limited (VLS)	Rental of garage and service charges	14.2	Negotiated	0.1

SERVICES SUPPLIED TO THE APPOINTEE BY ASSOCIATED COMPANIES:

ASSOCIATE	SERVICE	TURNOVER	TERMS OF SUPPLY	VALUE
		£'m		£'m
CKI	Software licensing agreements	2,437.8	Negotiated	4.6
Northern Gas Networks Limited (NGN)	Gas main diversions	415.8	No market	0.1
NWGL	Holding company charges	6.2	No market	0.9
Three Rivers Insurance Company Limited (TRICL)	Public liability insurance (deductible infill policy)	0.5	No market	0.5
VLS	Vehicle maintenance and capital finance charge	14.2	Competitive letting	7.7

Turnover data for AquaGib, NGN, NWGL and TRICL relates to the year to 31 March 2016. Turnover data for VLS and CKI relates to the year to 31 December 2015.

INFORMATION IN RELATION TO ALLOCATIONS AND APPORTIONMENTS

The appointed and non-appointed businesses operate separate accounting records including sales and purchase ledgers. Revenue, operating costs, assets and liabilities are taken directly from these records.

Revenue is separately recorded between wholesale water and wastewater and household and non-household retail services and no apportionment has been necessary. Operating costs have been allocated between wholesale water and wastewater and household and non-household retail services in accordance with the guidance set out in RAG 4.05.

Overhead costs incurred in the appointed business which relate to the non-appointed business have been allocated using an activity based approach to comply with RAG 5.06.

Interest has been allocated between the appointed and non-appointed businesses on the basis of actual cash balances held by these businesses during the year at market rates. Capital costs and the related depreciation charges are specifically identifiable to the appropriate business and service.

AMOUNTS BORROWED BY THE APPOINTEE FROM ASSOCIATED COMPANIES

The Company has loans amounting to £1,983.4m due to NWF, a subsidiary company. Details of these loans and the associated guarantees are provided in note 14 of the Statutory Financial Statements.

The Company acquires vehicles from VLS, an associated company, on a finance lease basis. During the year, new finance leases of £1.6m were entered into and capital repayments of £3.3m were made. The year end finance lease creditor was £9.0m. All leases are at a fixed interest rate of 6%.

GUARANTEES OR OTHER FORMS OF SECURITY

There were no guarantees or other forms of security provided by the appointee to any associate during the year, other than those relating to amounts borrowed from NWF, outlined above.

DIVIDENDS PAID AND PROPOSED

During the year, the appointed business paid and proposed dividends to its immediate parent companies as follows:

	£'m
DIVIDENDS PAID:	
Interim paid for the period ended 31 March 2016	99.7
Interim paid for the period ended 31 March 2016	100.3
Total dividends paid in the period	**200.0**

No final dividend was proposed for the period ended 31 March 2016 (31 March 2015: nil).

The Directors have a policy which aims to grow dividends on a slow but regular basis and which takes into account the principle of incentive based price cap regulation, including operating and investment performance.

Accordingly, the level of dividend has been 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 stable strong investment grade credit ratings.

OMISSION OF RIGHT

There were no omissions by the appointee to exercise any rights which would cause the net assets to decrease.

WAIVERS

There were no waivers by the appointee of any consideration, remuneration or other payment owed to it by any associated company.

The information in this note has been produced to comply with the requirements of RAG 5.06 Transfer Pricing in the Water Industry and the disclosures required by paragraph 6 of Condition F of the Company's operating licence.

The Directors confirm that, to the best of their knowledge, all transactions with associated companies have been disclosed.

STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE

(A) COMPLIANCE WITH LEGISLATION

The following statement on Directors' remuneration is disclosed in accordance with section 35A of the Water Act 2003. 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. The information in section (d) below has been audited.

(B) STATEMENT BY THE CHAIRMAN OF THE REMUNERATION COMMITTEE

The members of the Remuneration Committee (the Committee) are A J Hunter (Chairman), H Mottram, P Rew, M Fay and D N Macrae. S Salter, from the management team, provides advice to the Committee from time to time. H Mottram does not participate in discussions relating to her own remuneration and her bonus targets are set directly by the Chairman.

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 Committee, other than where stated.

During the year, the Committee:

- Conducted a market review of Directors' base salaries, primarily to reflect changes in responsibilities since the retirement of G Neave (Operations Director) in December 2014;
- Agreed bonuses for the 2015 calendar year;
- Set performance targets for Executive Directors and senior managers for the 2016 calendar year;
- Agreed the level at which the Long Term Incentive Plan (LTIP) award in respect of the 2015 calendar year would vest; and
- Revised the structure of the LTIP scheme for the award in respect of the 2016 calendar year.

A J Hunter
Chairman of the Remuneration Committee

(C) 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.

EXECUTIVE DIRECTORS

The remuneration of the Executive Directors comprises:

- Basic salary;
- Benefits in kind;
- A performance related annual bonus;
- Annual LTIP awards; and
- Pension benefits.

In addition to reviewing each constituent element, the Committee reviews the remuneration packages as a whole to ensure that they remain appropriate in terms of structure and quantum.

BASIC SALARY

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.

BENEFITS IN KIND

Benefits provided to the Executive Directors comprise car and fuel allowances and healthcare. There is no variable performance related element.

BONUS

The annual bonus is related to performance in the year, and is assessed on a calendar year basis. The performance targets are firmly linked to NWL's strategic themes (customer, competitiveness, people, environment and communities). 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.

Bonuses are paid in cash with no deferral. A clawback applies in the event that results on which the bonus is paid are subsequently found to be inaccurate or there has been relevant misconduct on the part of the employee. The bonus is structured with three elements, determined by the 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 maximum bonus payable, as a percentage of basic salary, is 70% for the CEO and 50% for the other Executive Directors.

LTIP

Executive Directors participate in a cash based LTIP. The purpose of the LTIP is to remain competitive in the executive market and encourage retention of key people.

The Committee revised the structure of the LTIP during the year. Vesting continues to be based on performance in the first calendar year after award. However, the payment date has been changed such that for the LTIP awarded in 2016, payment is deferred until the completion of four years from the start of the performance period, rather than deferred for three years as applied for previous awards.

In addition, the structure has been simplified so that the LTIP awarded in 2016 is payable on financial performance only, 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.

Previous awards were structured in three elements with 70% related to financial performance, 15% related to customer service performance and 15% related to asset performance.

The maximum LTIP payable, as a percentage of basic salary, is 50% for the CEO and 30% for the other Executive Directors.

PENSION

The Company operates the NWPS which has defined benefit and defined contribution sections. The defined benefit section closed to new entrants on 31 December 2007.

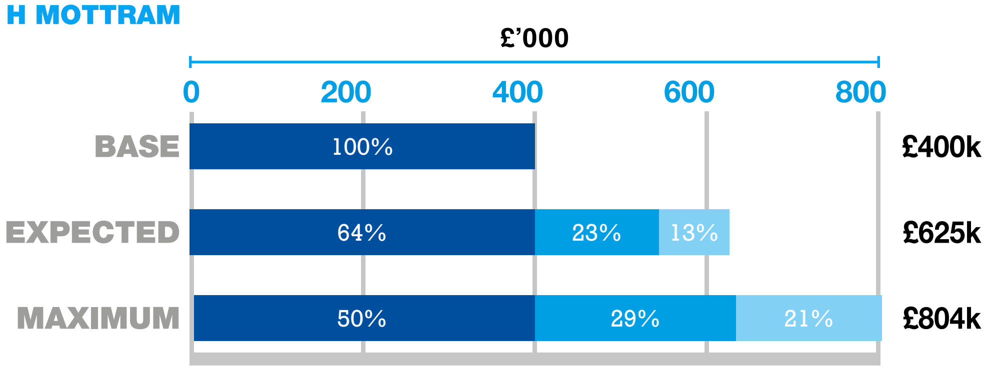
A C Jones participates in a defined benefit section, making an employee contribution of 8% of basic salary (under a salary sacrifice arrangement) and receiving an employer contribution equivalent to 18.9% of salary, up to 31 December 2015, and 22.1% with effect from 1 January 2016. Benefits are calculated on a CARE basis with future accrual at 1/45th of salary per annum.

H Mottram and C I Johns participate in the defined contribution section of the NWPS. They each make an employee contribution of 8% of their respective basic salaries and receive an employer contribution of 15% of salary, up to the annual pension contribution taxation limits.

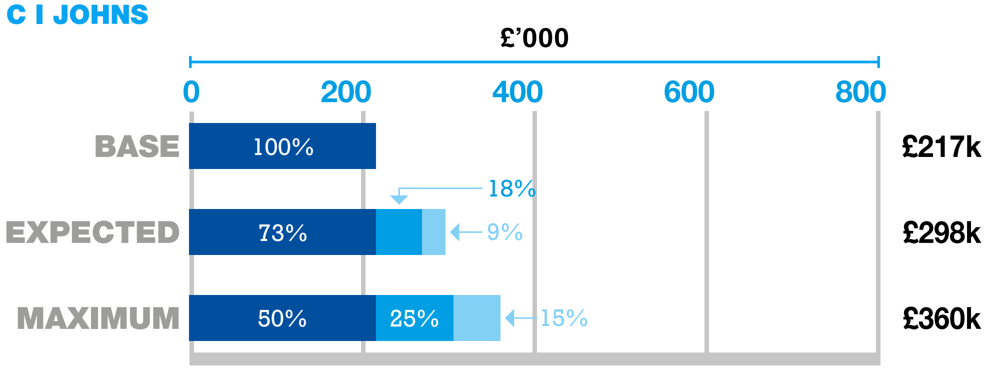
More details of the NWPS are provided in note 21 of the Statutory Financial Statements. There is no variable performance related element.

ILLUSTRATION OF REMUNERATION POLICY

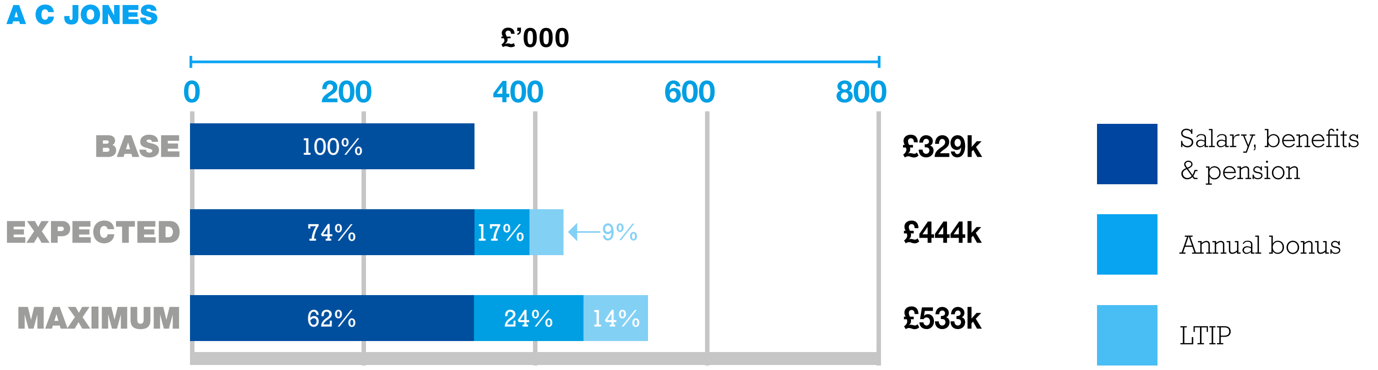
H MOTTRAM



C I JOHNS



A C JONES



For the purposes of the graph, annual bonus has been assumed to achieve 60% of the maximum potential value and LTIP has been assumed to achieve 50% of the maximum value, though awards are dependent upon actual performance. Information on actual awards for bonus and LTIP in respect of 2015 is provided on pages 141 to 142.

NON-EXECUTIVE DIRECTORS

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 bonus, 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.

(D) DIRECTORS' REMUNERATION IN 2015-16

The table below shows the total remuneration paid by the Company to Directors during the 12 month periods to 31 March 2015 and 2016. 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		BENEFITS IN KIND		BONUS		LTIP		PENSION		TOTAL REMUNERATION	
	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
H Mottram	324	319	9	10	210	206	102	99	61	60	706	694
C I Johns	162	159	9	9	41	48	32	31	43	42	287	289
A C Jones	252	212	14	14	58	60	41	40	281	56	646	382
G Neave	-	189	-	11	-	68	-	45	-	22	-	335
M Fay	43	42	-	-	-	-	-	-	-	-	43	42
F R Frame	13	12	-	-	-	-	-	-	-	-	13	12
Dr S Lyster	43	42	-	-	-	-	-	-	-	-	43	42
M A B Nègre	43	42	-	-	-	-	-	-	-	-	43	42
P Rew	55	54	-	-	-	-	-	-	-	-	55	54
	935	**1,071**	**32**	**44**	**309**	**382**	**175**	**215**	**385**	**180**	**1,836**	**1,892**

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.

G Neave resigned from the Board on 31 December 2014.

A C Jones is a member of the defined benefit section of the NWPS, therefore the pension value shown in the table above has been calculated in accordance with the 2013 Regulations. This represents the estimated increase in the capital value of his pension resulting from the decision by the Committee to increase his salary to reflect his extended responsibilities, as described on the next page.

BASIC SALARY

In 2012 the Committee agreed to restructure the remuneration of the Executive Directors by reducing the value of bonus and LTIP awards and offsetting this with an adjustment to basic pay (with advice from Hay Group, independent external reward consultants). This became effective from January 2013. For 2016, senior executives were awarded an annual increase in their basic salaries of 1.5%, which was less than the level awarded to most employees.

During 2015, the Committee conducted a market review of Directors' base salaries, primarily to reflect changes in responsibilities since the retirement of G Neave in December 2014. For A C Jones, this included taking responsibility for the asset management process, from strategy and planning to asset delivery, including delivery of capital efficiency targets.

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.

BONUS

The annual bonus for the calendar year 2015 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 detailed on page 17 of the Strategic Report and summarised below.

SCORECARD MEASURE	% OF TOTAL AWARDED	% OF TOTAL BONUS POTENTIAL
Competitiveness	12.5	50
Customer	12	16
People	-	8
Environment	4	8
Communities	8	8
Total	**36.5**	**90**

In respect of the 10% of bonus related to personal targets, the individual targets were as follows:

- H Mottram had targets including delivering expected financial performance, retention of existing credit ratings, delivery of outstanding customer service, a wider set of KPIs relating to a Balanced Scorecard of targets and leadership and delivery of the Company's Business Plan;
- C I Johns had targets including delivering expected financial performance, retention of existing credit ratings, maintaining the sustainability of the NWPS and implementing a financial business partnering model to support the business to achieve efficiency objectives; and
- A C Jones had targets including delivering changes to the asset planning and delivery process to deliver target efficiencies, enhancing regulatory relationships with DWI, Ofwat and EA and improving customer and community experience with capital investment projects.

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 bonus 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 bonus award.

The total annual bonus awards for 2015 were as follows:

	BONUS AWARDED (OUT OF 100%)	MAXIMUM BONUS (% OF BASIC SALARY)	BONUS AWARDED (% OF BASIC SALARY)
H Mottram	90.5%	70%	63.3%
C I Johns	46.5%	50%	23.3%
A C Jones	46.5%	50%	23.3%

LTIP

A cash LTIP was awarded by the Committee in 2015, structured in accordance with the policy in place prior to the change made by the Committee during 2015, as follows:

- Up to 70% payable on financial performance targets;
- Up to 15% payable on SIM performance targets; and
- Up to 15% payable on asset performance targets.

The scheme related to the period January 2015 to December 2017. Performance targets were assessed in the first year of the scheme with payment deferred until early 2018, after the end of the three year scheme period.

The Committee assessed the performance against the scheme criteria in April 2016. In respect of financial performance, 35% out of the maximum of 70% available vested.

In respect of SIM performance, NWL's combined score was assessed as being third position, compared against the other water and sewerage companies in England and Wales. This resulted in 11.25% out of the maximum of 15% available against this metric vesting.

All asset classes were assessed at stable serviceability, therefore the full 15% available against this metric vested.

The Committee therefore approved that the 2015 LTIP should vest at 61.25%. This is not dependent upon any future performance conditions being met.

ANNUAL PERFORMANCE REPORT

PENSION

Pension arrangements operated in accordance with the policy outlined on page 139.

For A C Jones, the value reported in the table on page 140 reflects the increase in the capital value of his accrued benefits in the year, calculated in accordance with Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2013. This takes account of the salary review conducted by the Committee during 2015 which reflected the increase his responsibilities in relation to the asset management process and capital efficiency targets.

BONUS

The Balanced Scorecard targets for 2016-17 are detailed on page 17 of the Strategic Report.

PERSONAL TARGETS FOR 2016 HAVE BEEN SET AS FOLLOWS:

- H Mottram has targets including delivering expected financial performance, retention of existing credit ratings, delivery of outstanding customer service, ensuring business readiness for the opening of the non household retail market, a wider set of KPIs relating to a Balanced Scorecard of targets and leadership and delivery of the Company's Business Plan.
- C I Johns has targets including delivering expected financial performance, retention of existing credit ratings, implementing new financial reporting standards across all Group companies and successfully implementing a Group restructuring.
- A C Jones has targets including the development of a collaborative working culture with our asset delivery partners in support of capital efficiency targets, overseeing the development and implementation of a behavioural safety programme, engagement with Ofwat's Water 2020 programme and commencement of preparations for the PR19 price review.

(E) IMPLEMENTATION OF REMUNERATION POLICY IN 2016-17

There have been no changes made by the Committee to the remuneration policy to be implemented in 2016-17, other than the change to the LTIP scheme described below. A change has been made to the component parts of the Balanced Scorecard, replacing employee participation in Just an Hour with category 1 and 2 pollution events, as defined by the EA.

LTIP

A new cash based LTIP was awarded by the Committee in 2016 for the period January 2016 to December 2018 structured in accordance with the revised policy outlined on page 138, as follows:

- Up to 50% payable on delivery of distributions to Group shareholder in line with the Board plan; and
- Up to 50% payable on Group profit after tax performance.

The maximum LTIP payable, as a percentage of basic salary, is 50% for H Mottram and 30% for C I Johns and A C Jones.

ANNUAL PERFORMANCE REPORT

INDEPENDENT AUDITOR'S REPORT TO THE WATER SERVICES REGULATION AUTHORITY ('WSRA') AND DIRECTORS OF NORTHUMBRIAN WATER LIMITED

OPINION ON ANNUAL PERFORMANCE REPORT

In our opinion, Northumbrian Water Limited's (the Company) Regulatory Accounting Statements within the Annual Performance Report:

- Fairly present in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA (RAG1.06, RAG2.05, RAG3.08, RAG4.05 and RAG5.06) and the accounting policies set out on pages 112 to 113 (including the accounting separation methodology), the state of the Company's affairs at 31 March 2016 and its profit and its cash flow for the year then ended; and
- Have been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines and the accounting policies (including the accounting separation methodology).

BASIS OF PREPARATION

Financial information other than that prepared on the basis of FRS 101 does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in statutory financial statements prepared in accordance with the Companies Act 2006. The Annual Performance Report is separate from the statutory financial statements of the Company and has not been prepared under the basis of International Financial Reporting Standards as adopted by the European Union ('IFRSs').

In forming our opinion on the Regulatory Accounting Statements within the Annual Performance Report, which is not modified, we draw attention to the fact that the Annual Performance Report has been prepared in accordance with Condition F, the Regulatory Accounting Guidelines, the accounting policies (including the accounting seperation methodology) set out in the statement of accounting policies and under the historical cost convention.

The Regulatory Accounting Statements on pages 112 to 147 have been drawn up in accordance with Regulatory Accounting Guidelines with a number of departures from IFRSs. A summary of the effect of these departures from Generally Accepted Accounting Practice in the Company's statutory financial statements is included in the tables within section 1.

ANNUAL PERFORMANCE REPORT

WHAT WE HAVE AUDITED

The sections within the Company's Annual Performance Report that we have audited ('the Regulatory Accounting Statements') comprise:

- The regulatory financial reporting tables comprising the income statement (table 1A), the statement of comprehensive income (table 1B), the statement of financial position (table 1C), the statement of cash flows (table 1D) and the net debt analysis (table 1E) and the related notes; and
- The regulatory price review and other segmental reporting tables comprising the segmental income statement (table 2A), the totex analysis for wholesale water and wastewater (table 2B), the operating cost analysis for retail (table 2C), the historical cost analysis of fixed assets for wholesale and retail (table 2D), the analysis of capital contributions and land sales for wholesale (table 2E), the household water revenues by customer type (table 2F), the non-household water revenues by customer type (table 2G), the non-household wastewater revenues by customer type (table 2H) and the revenue analysis by customer type (table 2I) and the related notes.

The financial reporting framework that has been applied in their preparation comprises the basis of preparation and accounting policies set out in the notes to the Annual Performance Report.

In applying the financial reporting framework, the Directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

We have not audited the Outcome performance table (Table 3A) and the additional regulatory information in tables 4A to 4I.

This report is made, on terms that have been agreed, solely to the Company and the WSRA in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewage undertaker under the Water Industry Act 1991 ('Condition F'). Our audit work has been undertaken so that we might state to the Company and the WSRA those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under Condition F to procure such a report and (b) to facilitate the carrying out by the WSRA of its regulatory functions, 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 WRSA, for our audit work, for this report or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF THE WSRA, THE DIRECTORS AND AUDITORS

As explained more fully in the Statement of Directors' Responsibilities set out on page 110, the Directors are responsible for the preparation of the Annual Performance Report and for their fair presentation in accordance with the basis of preparation and accounting policies. Our responsibility is to audit and express an opinion on the Regulatory Accounting Statements within the Annual Performance Report in accordance with International Standards on Auditing (UK and Ireland) ('ISAs (UK & Ireland)'), except as stated in the section on 'What an audit of the Annual Performance report involves' below, and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities' issued by the Institute of Chartered Accountants in England and Wales. Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

WHAT AN AUDIT OF THE ANNUAL PERFORMANCE REPORT INVOLVES

An audit involves obtaining evidence about the amounts and disclosures in the Regulatory Accounting Statements sufficient to give reasonable assurance that the Regulatory Accounting Statements within the Annual Performance Report are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the Annual Performance Report. In addition, we read all the financial and non-financial information in the Financial Statements and Annual Performance Report to identify material inconsistencies with the audited sections of the Annual Performance Report and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

We have not assessed whether the accounting policies are appropriate to the circumstances of the Company where these are laid down by Condition F. Where Condition F does not give specific guidance on the accounting policies to be followed, our audit includes an assessment of whether the accounting policies adopted in respect of the transactions and balances required to be included in the Annual Performance Report are consistent with those used in the preparation of the statutory financial statements of the company. Furthermore, as the nature, form and content of Annual Performance Report is determined by the WSRA, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under ISAs (UK & Ireland).

The Company has presented the allocation of operating costs and assets in accordance with the accounting separation policy set out on page 143 and its Accounting Separation Methodology Statement published on the Company's website on 15 July 2016. We are not required to assess whether the methods of cost allocation set out in the Methodology Statement are appropriate to the circumstances of the Company or whether they meet the requirements of the WSRA, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK & Ireland).

OPINION ON OTHER MATTERS PRESCRIBED BY CONDITION F

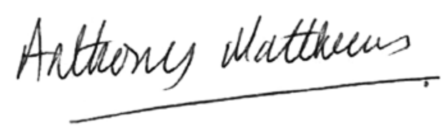
Under the terms of our contract we have assumed responsibility to provide those additional opinions required by Condition F in relation to the accounting records. In our opinion:

- Proper accounting records have been kept by the appointee as required by paragraph 3 of Condition F; and
- The Regulatory Accounting Statements are in agreement with the accounting records and returns retained for the purpose of preparing the Annual Performance Report.

OTHER MATTERS

The nature, form and content of the Annual Performance Report is determined by the WSRA. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the WRSA's purposes. Accordingly we make no such assessment.

Our opinion on the Regulatory Accounting Statements within the Annual Performance Report is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2016 on which we reported on 15 July 2015, which are prepared for a different purpose. Our audit report in relation to the statutory financial statements of the Company (our 'Statutory audit') was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our Statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a statutory audit report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our Statutory audit report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.



Anthony Matthews (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Newcastle Upon Tyne, United Kingdom
15 July 2016

OUR PERFORMANCE 2015-16

INTRODUCTION

This is the first year of our customer focused business plan for 2015-2020 and we are changing the way that we report our performance to reflect our new approach based on Outcomes, measures of success and performance commitments.

ANNUAL PERFORMANCE REPORT

Outcomes express the high-level objectives that our actions intend to deliver. They represent what customers and society value in the long-term. In consultation with our customers and stakeholders, we have developed and agreed 12 delivery Outcomes which cover our strategic themes of customer, environment and competitiveness. We have also developed an additional seven enabling Outcomes which cover our strategic themes of communities, people and reputation.

Everything we do is covered by an Outcome and to deliver Outcomes we have clear metrics that show how we are performing – our **measures of success** (MoS).

Each Outcome can have several measures of success and we must, as a minimum, deliver a stable level of service to our customers – these are our **performance commitments** (PC).

For delivering better performance we could earn a financial reward. However, poor performance means that we could incur a financial penalty. These are called **outcome delivery incentives** or ODI.

Our two baskets of **Asset Health measures** (one for wastewater services and one for water services) are an innovative way of monitoring, protecting and incentivising the long-term sustainable stewardship of our assets. They are linked to our customers' valuations of service improvements that they want us to deliver between 2015 and 2020.

This performance summary will set out in an open, transparent and clear way the work that we are doing to deliver our Outcomes and provide the water and wastewater services that our customers want. It provides the extended commentary for Table 3A.

Measurement of performance and calculation of any penalties or rewards is calculated using the methodology stated in our PR14 Final Determination, and is subject to robust assurance. Some of the ODI have earned a reward in the year to 31 March 2016, although this will not be reflected in the RCV until 1 April 2020 in the next price control period.

For MoS within our Asset Health baskets, the methodology states that these are measured on a three-year average. Within this performance summary, we have also included actual annual performance.

Within Table 3A, performance against PCs for the Asset Health measures have not been assessed although actual three-year average performance is shown. This is because the first assessment point, for penalty and/or reward, will not take place until the end of 2017-18.

This commentary highlights our performance, by Outcome, reporting against each of our measures of success. It also covers our enabling and reputational Outcomes which are not part of Table 3A.

We have engaged with our Water Forums to discuss our performance and further information about our performance is available in a more customer-friendly presentation on our websites at **www.nwl.co.uk**, **www.eswater.co.uk** and **www.welivewater.co.uk.**

ANNUAL PERFORMANCE REPORT

SECTION 3: PERFORMANCE SUMMARY

3A OUTCOME PERFORMANCE TABLE

UNIQUE ID	PERFORMANCE COMMITMENT	UNITS	2014-15 PERFORMANCE LEVEL - ACTUAL	2015-16 PERFORMANCE LEVEL - ACTUAL	2015-16 COMMITTED PERFORMANCE LEVEL MET?	NOTIONAL REWARD OR PENALTY ACCRUED AT 31 MARCH 2016	NOTIONAL REWARD OR PENALTY ACCRUED AT 31 MARCH 2016	TOTAL AMP6 REWARD OR PENALTY 31 MARCH 2020 FORECAST	TOTAL AMP6 REWARD OR PENALTY 31 MARCH 2020 FORECAST
							£'m		£'m
W-A1	Asset Health measures - water	n/a	n/a	n/a	-	-	-	-	-
W-B1	Satisfaction with taste and odour of tap water	nr	1,405	1,225	Yes	Reward deadband	-	-	-
W-B2	Overall drinking water compliance (AH)	%	99.930	99,937	-	-	-	-	-
W-B3	Discoloured water complaints (AH)	nr	4,292	3,762	-	-	-	Reward	0.2
W-C1	Interruptions to water supply for more than 3 hours (average time per property per year)	seconds	236	200	Yes	Reward	3.8	Reward	9.8
W-C2	Properties experiencing poor water pressure (AH)	nr	254	238	-	-	-	-	-
W-C3	Water mains bursts (AH)	nr	3,964	3,916	-	-	-	-	-
W-C4	Leakage Northumbrian area	Ml/d	136.77	134.66	Yes	Reward deadband	-	-	-
W-C5	Leakage Essex and Suffolk area	Ml/d	60.86	62.42	Yes	Reward deadband	-	-	-
W-D1	NWL independent overall customer satisfaction score	score	8.3	8.5	Yes	-	-	-	-
W-D2	SIM	score	83.72	83.64	No	-	-	-	-
W-D3	Domestic customer satisfaction, net promoter score	nr	42	49	Yes	-	-	-	-
W-E1	NWL independent survey on keeping customers informed	%	91	94	-	-	-	-	-
W-F1	Greenhouse gas emissions	$KtCO_2e$	213.6	225.2	No	-	-	-	-
W-F2	Annual environmental performance report	n/a	n/a	n/a	Yes	-	-	-	-
S-A1	Asset Health measures - wastewater	n/a	n/a	n/a	-	-	-	-	-
S-B1	Properties flooded externally	nr	1,170	1,061	Yes	Reward	0.2	Reward	0.2
S-B2	Properties flooded internally	nr	228	143	Yes	Reward	0.5	Reward	2.0
S-B3	Repeat sewer flooding (AH)	nr	555	184	-	-	-	Reward	3.8
S-B4	Sewer collapses (AH)	nr	49	48	-	-	-	-	-
S-B5	Transferred drains and sewers - internal sewer flooding	nr	188	219	Yes	Reward deadband	-	-	-
S-B6	Transferred drains and sewers - external sewer flooding	nr	2,479	2,506	Yes	Reward deadband	-	-	-
S-B7	Transferred drains and sewers - sewer collapses	nr	74	58	Yes	-	-	-	-
S-C1	Sewage treatment works discharge compliance (AH)	nr	1	1	-	-	-	-	-

Table continued overleaf

ANNUAL PERFORMANCE REPORT

CONTINUED 3A OUTCOME PERFORMANCE TABLE

UNIQUE ID	PERFORMANCE COMMITMENT	UNITS	2014-15 PERFORMANCE LEVEL - ACTUAL	2015-16 PERFORMANCE LEVEL - ACTUAL	2015-16 COMMITTED PERFORMANCE LEVEL MET?	NOTIONAL REWARD OR PENALTY ACCRUED AT 31 MARCH 2016	NOTIONAL REWARD OR PENALTY ACCRUED AT 31 MARCH 2016	TOTAL AMP6 REWARD OR PENALTY 31 MARCH 2020 FORECAST	TOTAL AMP6 REWARD OR PENALTY 31 MARCH 2020 FORECAST
							£'m		£'m
S-C2	Pollution incidents (category 3) (AH)	nr	136	124	-	-	-	-	-
S-C3	Bathing water compliance	nr	33	33	Yes	-	-	-	-
S-C4	Whitburn combined sewer overflow scheme	yes/no	n/a	n/a	-	-	-	-	-
S-D1	NWL independent overall customer satisfaction score	score	8.3	8.5	Yes	-	-	-	-
S-D2	SIM	score	83.72	83.64	No	-	-	-	-
S-D3	Domestic customer satisfaction, net promoter score	nr	42	49	Yes	-	-	-	-
S-E1	NWL independent survey on keeping customers informed	%	91	94	-	-	-	-	-
S-F1	Greenhouse gas emissions	$KtCO_2e$	213.6	225.2	No	-	-	-	-
S-F2	Annual environmental performance report	n/a	n/a	n/a	Yes	-	-	-	-
R-B1	NWL independent overall customer satisfaction score	score	8.3	8.5	Yes	-	-	-	-
R-B2	SIM	score	83.72	83.64	No	-	-	-	-
R-B3	Domestic customer satisfaction, net promoter score	nr	42	49	Yes	-	-	-	-
R-C1	NWL independent value for money survey	score	8.1	8.2	Yes	-	-	-	-
R-C2	Satisfied with value for money of water services - Northumbrian region (CCWater research)	%	78	77	No	-	-	-	-
R-C3	Satisfied with value for money of sewerage services - Northumbrian region (CCWater research)	%	81	79	No	-	-	-	-
R-C4	Satisfied with value for money of water services - Essex & Suffolk region (CCWater research)	%	73	70	No	-	-	-	-
R-D1	NWL independent survey on keeping customers informed	%	91	94	-	-	-	-	-
R-E1	Greenhouse gas emissions	$KtCO_2e$	213.6	225.2	No	-	-	-	-
R-E2	Annual environmental performance report	n/a	n/a	n/a	Yes	-	-	-	-
R-F1	Delivering a consolidated Customer Information and Billing system	yes/no	n/a	n/a	-	-	-	-	-

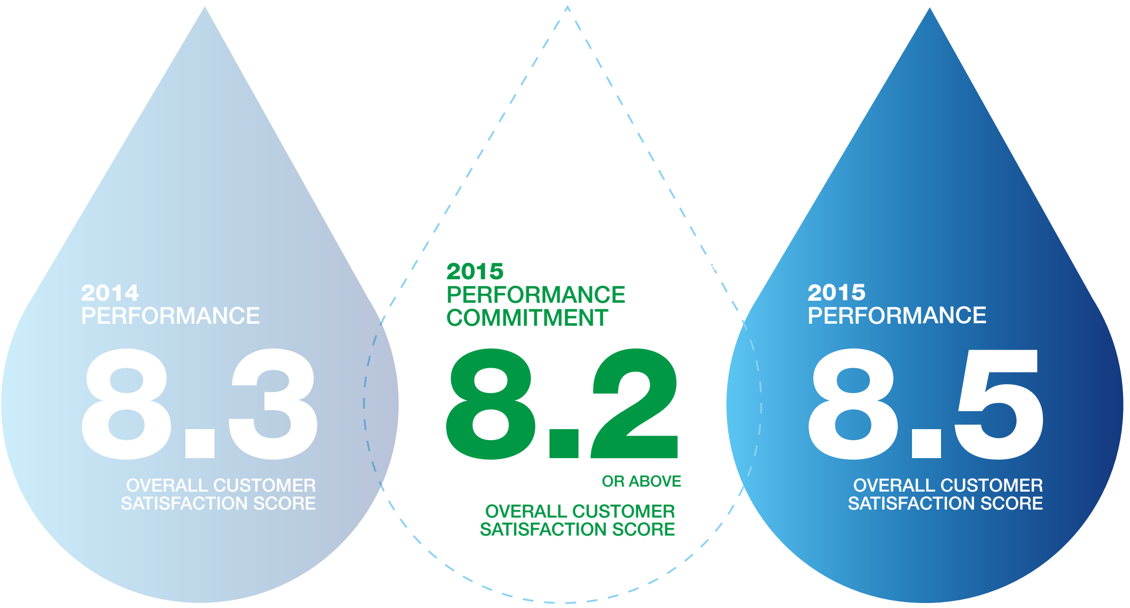
2015-16 PERFORMANCE - OUR DELIVERY OUTCOMES

- We provide excellent service and impress our customers
- 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

OUR MEASURES OF SUCCESS AND PERFORMANCE COMMITMENTS

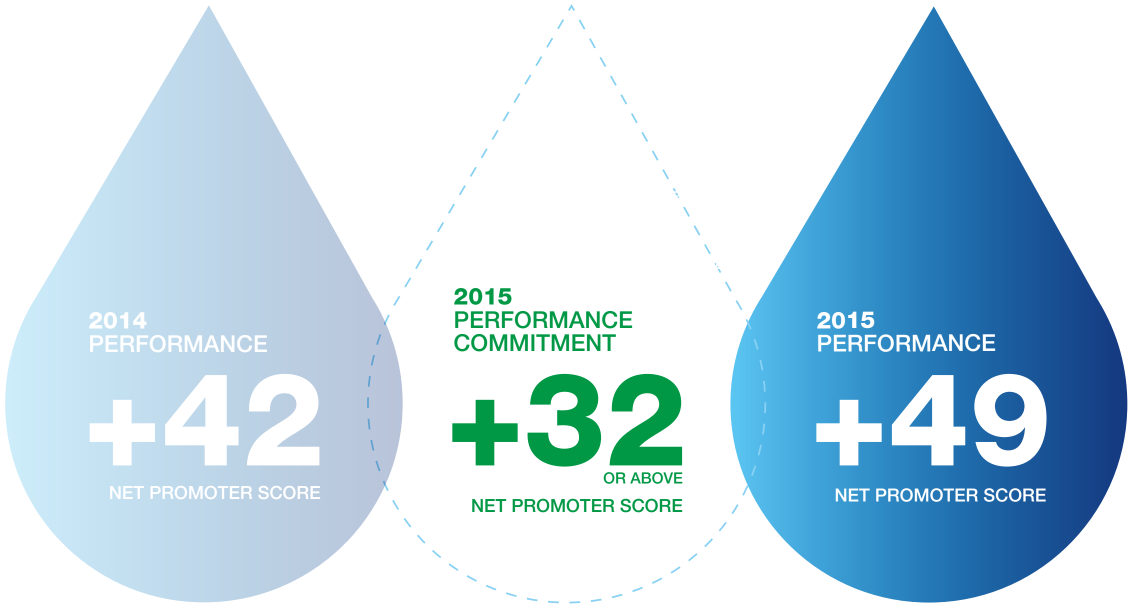
These three Outcomes are very closely connected, so we have grouped them together for the purpose of this report. They cover seven MoS: independent overall customer satisfaction survey; Ofwat service incentive mechanism; domestic customer satisfaction (net promoter score); independent value for money survey; and three CCWater value for money surveys covering water and wastewater services.

INDEPENDENT OVERALL CUSTOMER SATISFACTION SURVEY (W-D1, S-D1 & R-D1)



A high level of customer satisfaction has been confirmed through our quarterly tracking research, undertaken for us by an independent company. Our customers' overall satisfaction has improved at the end of 2015 compared to 2014. This satisfaction level of 8.5 is our best experienced since the research tracking programmes started, and better than our PC of 8.2.

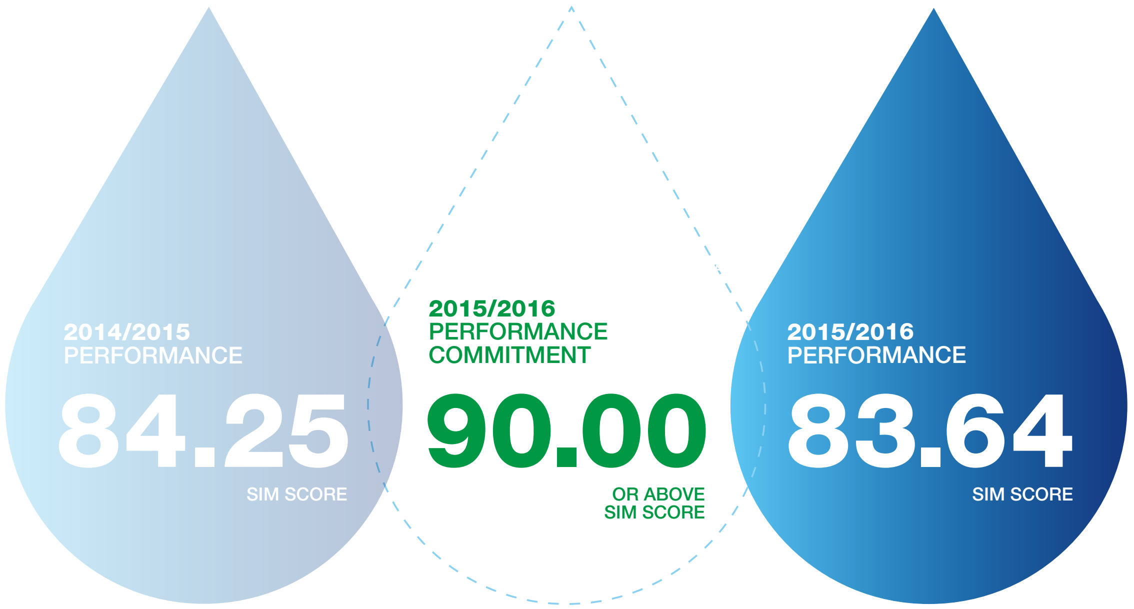
DOMESTIC CUSTOMER SATISFACTION, NET PROMOTER SCORE (NPS) (W-D3 & S-D3)



There is no single measure that will provide us with the full picture of our customers' satisfaction, so to benchmark ourselves outside the water industry, we have been measuring our NPS. This measures customer advocacy (the loyalty that exists between us and our customers).

Our annual NPS continues to improve year on year. Our NPS in 2015 improved from +42 in 2014 to +49. This is significantly above our PC of +32 and ranks us alongside household names such as Apple and Amazon who operate in highly competitive retail markets where their performance is linked to customer loyalty. This high score indicates that our customers continue to trust our company.

OFWAT SERVICE INCENTIVE MECHANISM (SIM) (W-D2, S-D2 & R-B2)



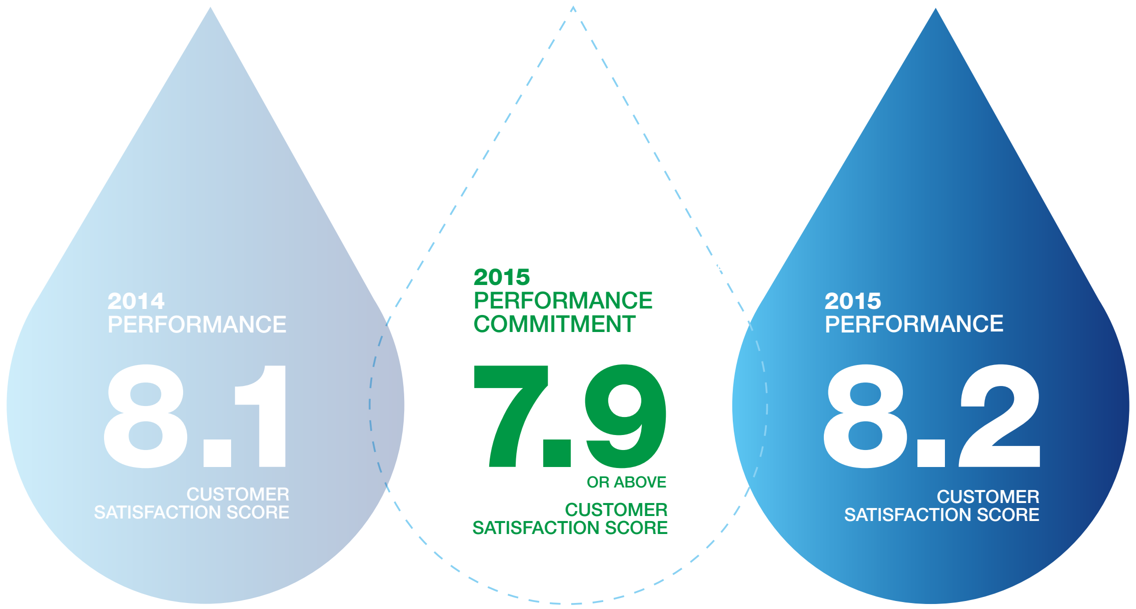
Ofwat's SIM measures our customers' experience of dealing with us and provides a good indication of how well we are serving our customers, who have had a reason to contact us. Our SIM score for 2015-16 was 83.64.

The SIM measure has recently changed and is now based on customer satisfaction levels for all inbound customer contact to NWG. The new measure puts a greater emphasis on the quality of the customer experience, from first point of contact to the resolution of the issue. We welcome this change because we believe customers' views of performance are more important than quantitative measures, such as volume of unwanted contacts.

Our aim is to be the leading Company and we are disappointed not to have achieved a better SIM score. This was predominately due to a poor score on the fourth and final wave of surveys. Some areas for further improvement have been identified including speed of resolution, ownership of issues and keeping customers informed.

Our new strategy for delivering unrivalled customer experience, ' Living Water, Loving Customers', which is discussed later in this section, will help us to deliver these improvements.

INDEPENDENT VALUE FOR MONEY SURVEY (R-C1)

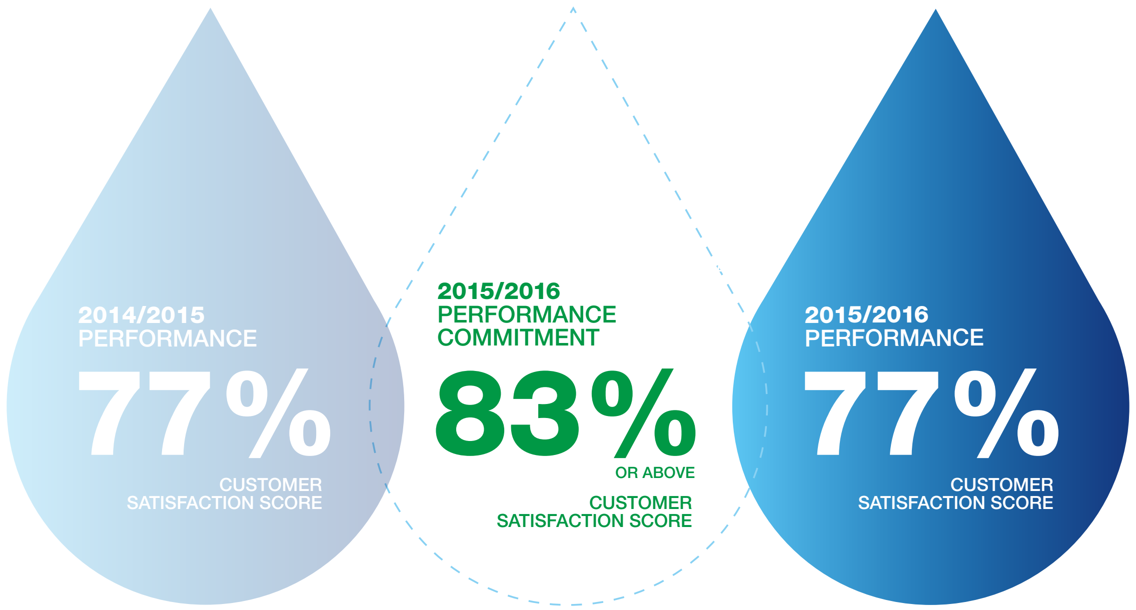


Our value for money survey score improved from 8.1 in 2014 to 8.2 in 2015, which is above our PC of 7.9.

CCWATER VALUE FOR MONEY SURVEY (R-C2, R-C3 & R-C4)

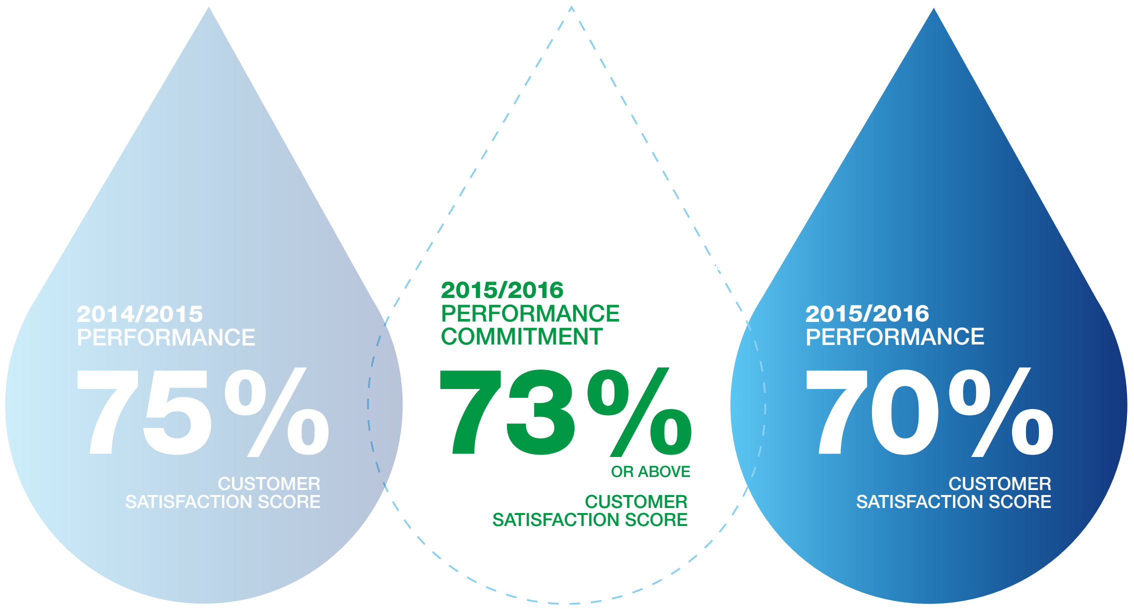
Each year CCWater asks customers for their views about the services they receive from their water and sewerage company and value for money of those services. CCWater consider each of our value for money scores to be stable, based on performance over the last five years. However, we are below our PC for each service and we have described, in the highlights section, a number of steps we are taking to improve our customers' experience.

SATISFIED WITH VALUE FOR MONEY OF WATER SERVICES - NW



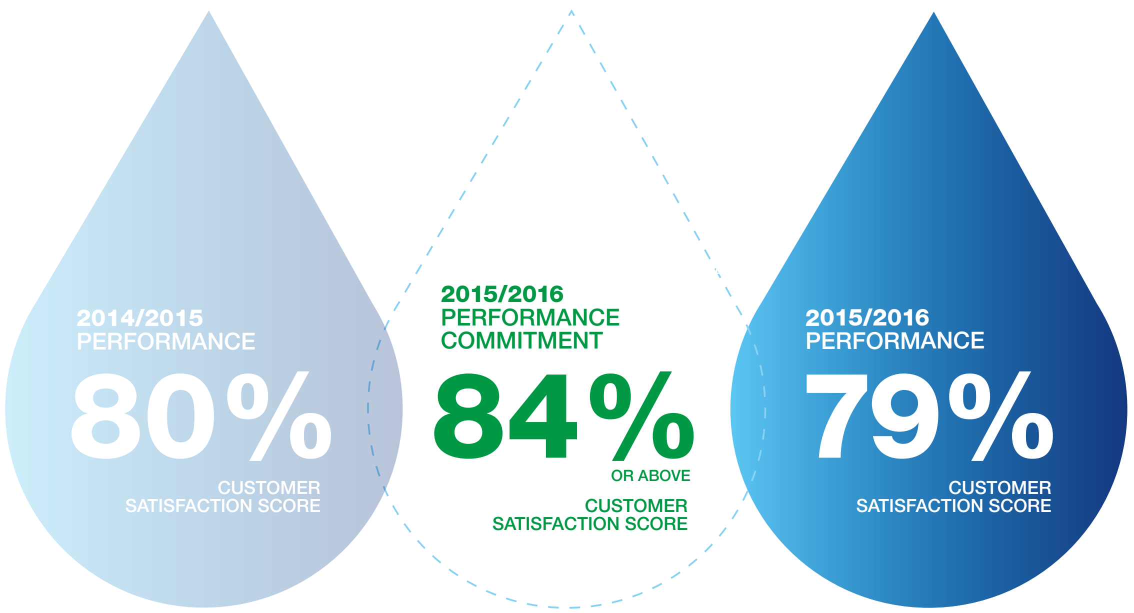
Our PC was set at 83%, which was our best ever performance achieved in 2011. The latest CCWater research results relating to value for money of water services in our Northumbrian Water area remain constant for the last two years at 77%. This is above the industry average of 76%.

SATISFIED WITH VALUE FOR MONEY OF WATER SERVICES-ESW



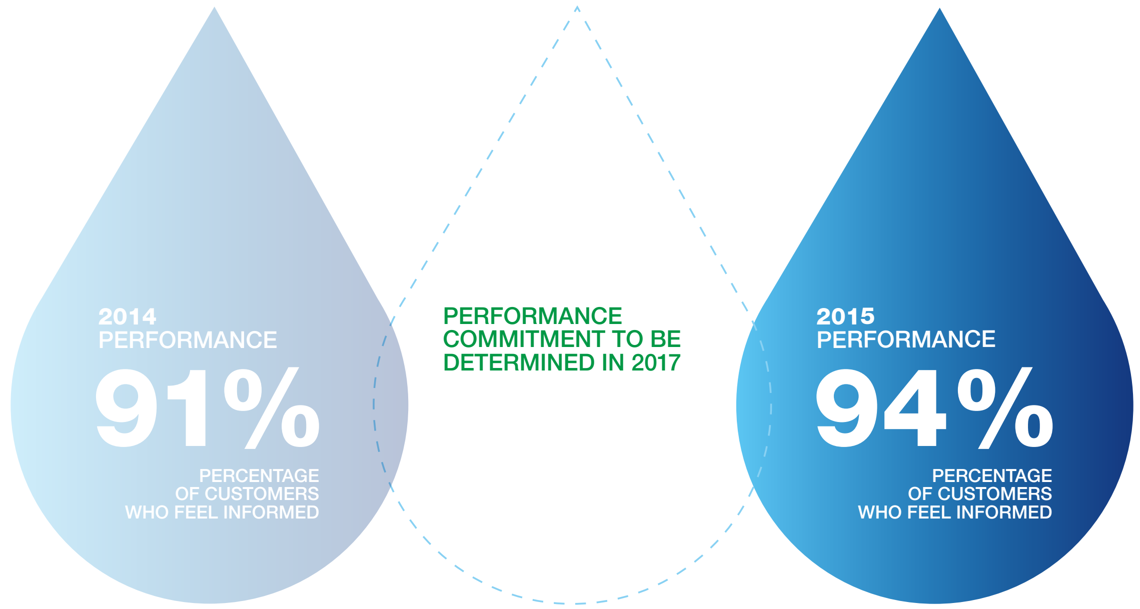
The latest CCWater research results relating to value for money of water services in Essex & Suffolk Water reduced to 70% in 2015-16 from 75% in 2014-15. This is below our PC target of 73%.

SATISFIED WITH VALUE FOR MONEY OF SEWERAGE SERVICES-NW



Our PC was set at 84%, which was our best ever performance achieved in 2011. Customers in the Northumbrian Water region continue to be satisfied with the value for money of their sewerage services (79%). This is above the industry average of 78%.

INDEPENDENT SURVEY ON KEEPING CUSTOMERS INFORMED (W-E1, S-E1 & R-D1)



At the end of 2015, 94% of our customers told us that they are supplied with all the information they want to feel informed about our services. This has increased by 3% since it was first included in our tracking research in 2014. It is important for us to improve our customers' experience of the services we provide. In the next section we highlight work we are carrying out to improve our service with the aim of being the leading water and wastewater company.

HIGHLIGHTS

LIVING WATER, LOVING CUSTOMERS

During 2015, we have worked with our customers, employees and supply chain partners to develop 'Our Unrivalled Customer Experience Strategy' – Living Water, Loving Customers.

Living Water, Loving Customers expresses our customer service ethos as a core element of our brand and culture. It communicates how we will deliver an unrivalled customer experience in line with our vision and values.

Our strategy is driven by our clear ambition to succeed beyond being industry leader, and the forever rising expectations of our customers. In a world where companies are judged more than ever before on their approach to service, we must provide exceptional experiences for customers, consistently.

The strategy addresses each of the areas that our customers have told us are important priorities. These include:

- Showing each customer that they are special – make service extra personal;
- Taking personal ownership for customers' problems;
- Keeping our promises; and
- Making it easy.

Our strategy to deliver unrivalled customer experience coupled with Our Way, the service mindset cultural change programme we have been working on over the last four years, positions us well to realise our aspiration to deliver unrivalled customer service and to be the national leader in the provision of sustainable water and wastewater services.

The services we provide are essential to life and wellbeing, and our customers should always have complete trust and confidence in what we do. We want our service to be recognised as unrivalled, delivering superb value for money and experiences that get talked about for all the right reasons.

EASE OF CONTACT

To help us to improve service we have invested in new workforce management tools and field equipment enabling our people to deliver improved customer service more efficiently. This means that our people have all appropriate customer information accessible to them when working throughout our operating regions.

We are working hard to improve satisfaction when customers need to contact us. To do this we are continuing with our investment in customer service systems and the provision of customer choice in how they wish to contact us. In the last year we have made it easier for customers to pay and access their accounts through our web services. We let customers know when the latest statement is available so that they can keep up to date with their bill and water usage.

We understand that our customers have individual requirements and expectations and want a choice in how they contact us. In the last year we have introduced a web-chat option and we typically see over 800 customers per week choosing to use this service.

Effective communication is critical to customer satisfaction and we are proactive and innovative in how we do this. We use text and voice messaging to keep customers informed of events in their area or to confirm recent transactions. Some 10,000 to 20,000 messages are sent each week.

Our customers tell us that keeping them informed is important to them and by doing so we improve the service we provide and improve customer satisfaction.

OUR NEW CUSTOMER EXPERIENCE PROGRAMME

The implementation of our new integrated customer care and billing system is progressing well. This piece of work which we have called ONCE (Our New Customer Experience) programme will replace our ageing billing, collection and customer contact systems enhancing our ability to deliver great customer service.

The introduction of a new multi million pound customer management system will further enhance our service experienced by customers making it more personal, quicker and integrated. We expect this to have a positive effect on our SIM score.

The first major milestone for our ONCE programme is in line with market opening for business customers in April 2017. At this time, we will commence our wholesale operation using the new system. We are on track to meet this deadline.

Following this, our next major milestone is to improve the customer experience for our Household customers. This will occur in two steps; billing will go live in October 2017 and operational contact will go live in April 2018.

VOICE OF THE CUSTOMER

We have invested in a new Voice of the Customer system which enables customers to provide real time feedback on our customer service. This feedback is then shared with our people at an individual level providing a great opportunity to understand and improve the customer service they offer. The feedback is provided to our customer facing office and field staff providing them with visibility on areas of great service as well as opportunities for improvement. While this is a recent initiative we have already seen a step change in customer satisfaction ratings and expect that this will improve further as the system is opened up to more teams and people.

Collecting real time feedback on our service from customers presents us with the opportunity to further improve our service by being able to address any customers' outstanding concerns or issues immediately. This will drive further improvements in our SIM score as we 'close the loop' in a timely manner.

GUARANTEED SERVICE STANDARDS (GSS) PAYMENTS

We seek to provide excellent service. When things occasionally go wrong, the Water Supply and Sewerage Services (Customer Service Standards) Regulations 2008 require companies to provide compensation payments to customers in certain circumstances.

We do whatever we can to minimise service failures and aim to pay promptly should we fail to meet guaranteed standards. In 2015-16 GSS payments for poor service reduced significantly for the third year in a row. The number of payments of this nature reduced by 34% from 2014-15 numbers with the reduction being largely attributable to a reduction in sewer flooding incident payments. This reflects the investment we have made as a business to improve our performance in this area of service.

CUSTOMER RESEARCH AND ENGAGEMENT

To satisfy our customers we need to understand what they want in terms of water and wastewater services, complaint resolution and communications. We establish expectations through extensive engagement with customers. In this way we build up a picture of where service improvements are necessary and the actions that can be taken to increase customer satisfaction in all of our dealings with customers.

We plan our approach to customer engagement, ensuring the information we gather, both qualitative and quantitative, provides a coherent body of evidence across all of our outcomes, informing both operational and planning requirements.

Our approach to customer research and engagement is evolving, with more emphasis on having real two-way conversations with our customers. For example, we have recently undertaken phase one of our engagement called ''Defining the Conversation'' where we asked our customers to tell us which aspects of our service are important to them and which aspects they want to talk to us about.

A key aspect of our engagement approach is to inform customers about our services to enable more meaningful conversations with them about future strategy and service levels. We also expect that informing customers about the breadth of our services in this way will improve their perception of value for money.

We open up our customer research approach and outcomes to our Water Forums (Customer Challenge Groups) so that we benefit from both challenge and advice from a range of stakeholders. We also discuss research with CCWater and take its comments into account in designing research and interpreting outcomes.

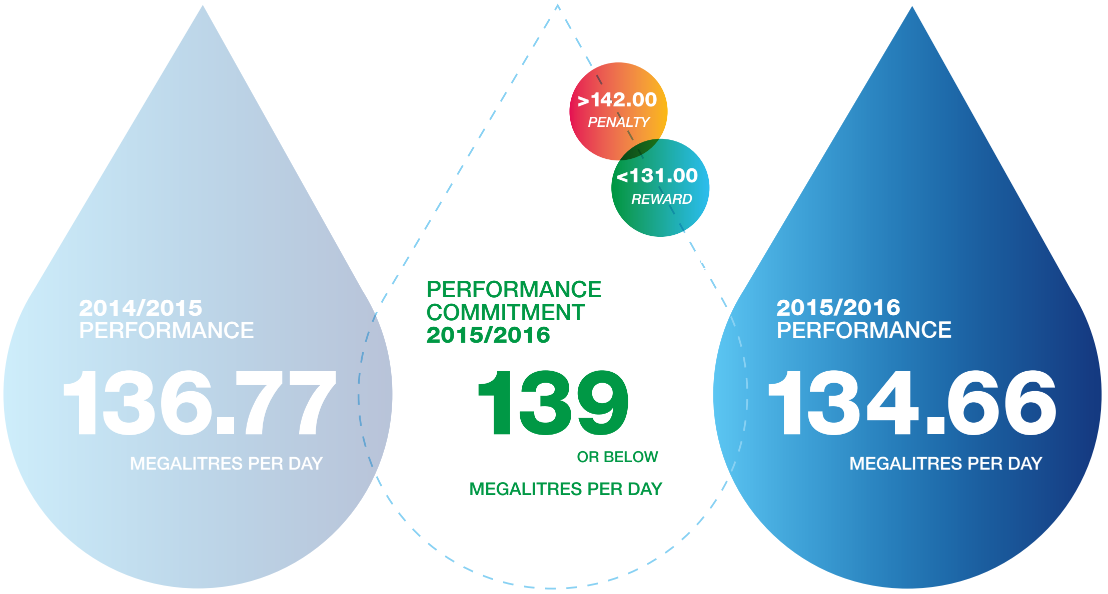
As well as the quarterly customer satisfaction research used for our MoS, we have also introduced a daily survey and ask around 10,000 customers each week what they think of our service.

We provide a reliable and sufficient supply of water

OUR MEASURES OF SUCCESS AND PERFORMANCE COMMITMENTS

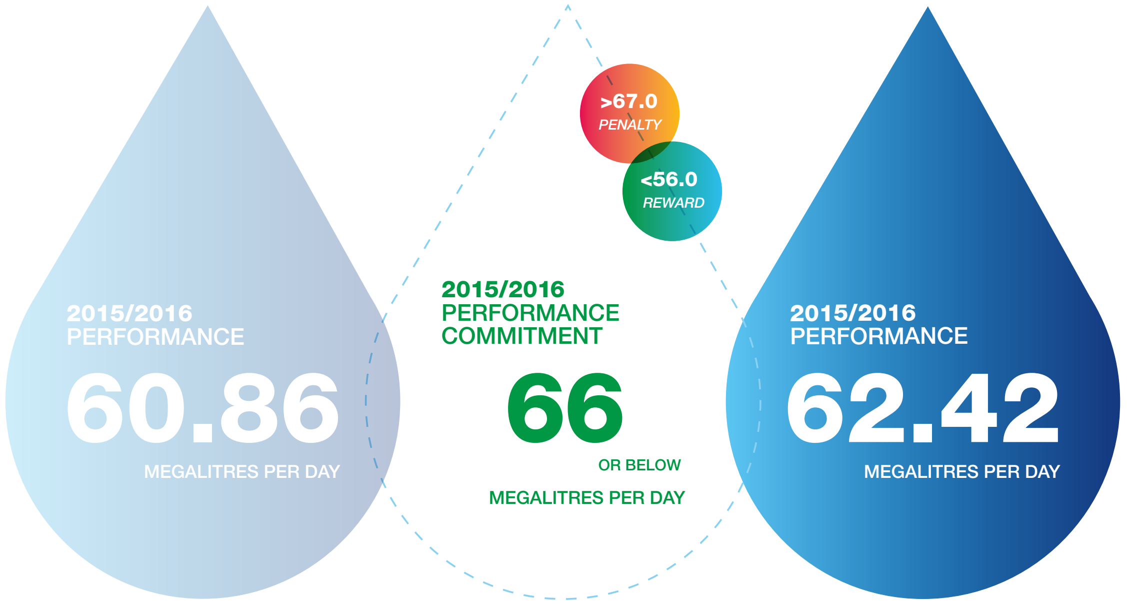
This Outcome has four MoS: leakage and the number of bursts occurring on our water network relating to a sufficient supply and water supply interruptions and properties affected by poor water pressure relating to a reliable supply.

LEAKAGE NW (W-C4)



In 2015-16 our performance in NW was 134.66 Ml/d, which is significantly better than our PC of 139 Ml/d.

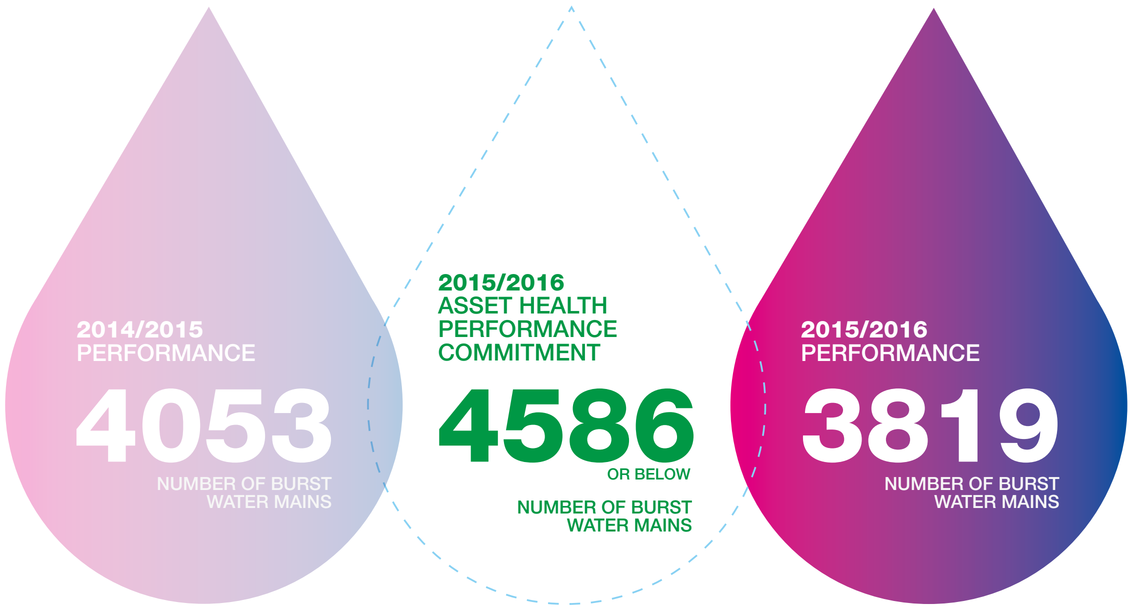
LEAKAGE ESW (W-C5)



Our performance in ESW was 62.42 Ml/d, again this is significantly better than our PC of 66.0 Ml/d.

We achieved this excellent performance in both our regions by instigating early proactive interventions to monitor and improve the condition of our network, and by having a prompt and efficient operational response to water mains bursts.

WATER MAINS BURSTS (W-C3)



The figures above show our annual performance in 2014-15 and 2015-16 for water mains bursts. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017-18, 2018-19 and 2019-20. Consistent with this approach, Table 3A shows our three-year average performance of 3916 for the period 2013-14 to 2015-16, reflecting performance levels in 2013-14 and 2014-15, before the PC was applied.

In 2015-16 we experienced our lowest ever number of water mains bursts, 3819. We attribute this improvement to our early proactive interventions to monitor and improve the condition of our water supply network, alongside favourable weather conditions throughout the year.

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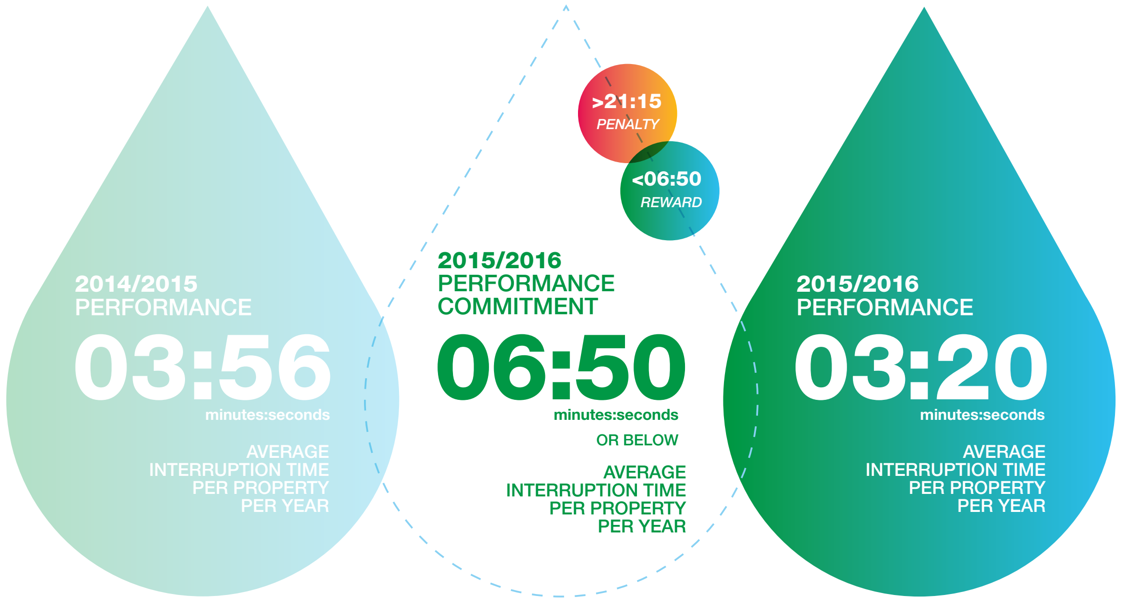
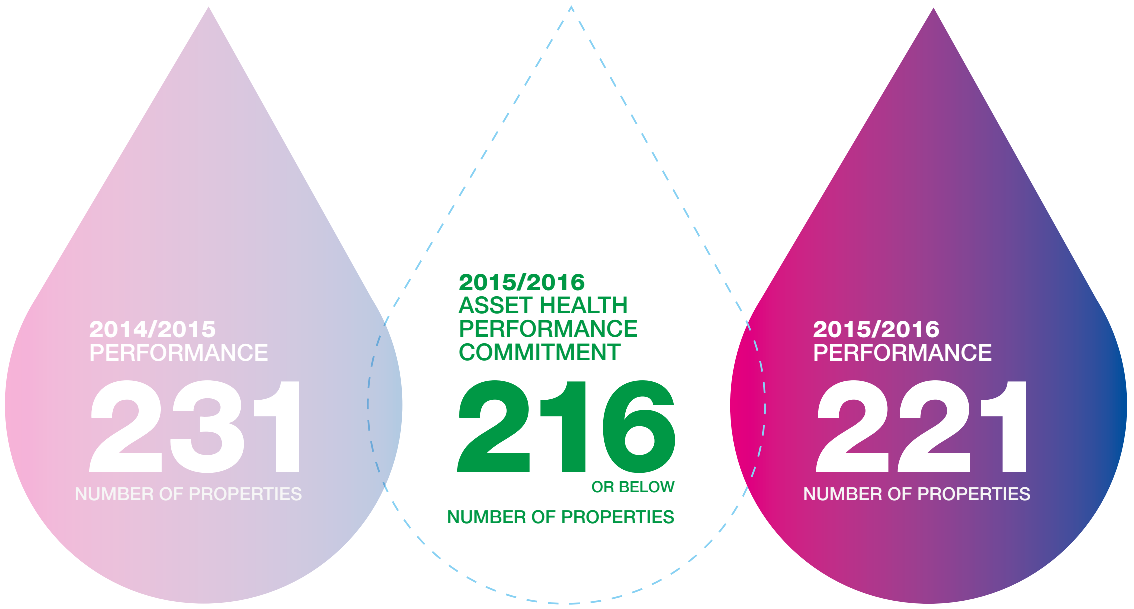
WATER SUPPLY INTERRUPTIONS (W-C1)



Our performance continues to improve in relation to water supply interruptions (greater than 3 hours in length) to 3 minutes and 20 seconds per property served in 2015-16. This is even better than our 2014-15 industry-leading performance of 3 minutes and 56 seconds per property served and much better than our PC of 6 minutes and 50 seconds.

We achieved this leading level of performance by providing alternative temporary supplies where appropriate and through significantly improved operational responses and practices.

PROPERTIES EXPERIENCING POOR WATER PRESSURE (W-C2)



The figures above show our annual performance in 2014-15 and 2015-16 for properties experiencing poor water pressure. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017-18, 2018-19 and 2019-20. Consistent with this approach, Table 3A shows our three-year average performance of 238 for the period 2013-14 to 2015-16, reflecting performance levels in 2013-14 and 2014-15 before the PC was applied. We need to ensure that the improving trend is sustained in 2016-17 and beyond in order to achieve our PC.

During 2015-16, 221 properties were classed as experiencing poor water pressure. This is very slightly higher than our PC of 216.

We address properties that fail the pressure standard either within the year that they fail or through longer term planning or investment. This usually involves the installation of short lengths of additional pipe work or small pumping stations, or reconfigurations of our water supply network.

HIGHLIGHTS

SECURITY OF SUPPLY

The Security of Supply Index (SoSI) is a measure of how resilient we are against periods of drought in ensuring that we are able to meet our customers' demands for a reliable and sufficient supply of water.

The SoSi for both our operating regions in 2015/16 was 100%, the highest achievable level.

In ESW this is attributable to the completion of the extension to Abberton Reservoir, which has secured supplies for the region for 25 years.

In NW it is attributable to the fact that the majority of customers in our NW region are supported by Kielder Reservoir, which has significant surplus capacity and water resources are therefore sufficient.

At the Northern most point of our NW region, we have a small separate water resource zone – Berwick and Fowberry, which is served only by local groundwater sources. We are undertaking an investigation relating to the sustainability of these groundwater sources and taking steps to manage the balance of supply and demand.

These include:

- A National Environment Programme (NEP) sustainability assessment;
- A groundwater nitrate study;
- A borehole rehabilitation programme; and
- A targeted water efficiency programme.

The outputs of the studies will be used to inform our plans for 2020-25.

WATER EFFICIENCY

We have continued with our vigorous promotion of water efficiency in both the ESW and NW areas, achieving water savings equivalent to 0.68 Ml/d in 2015-16. We delivered our successful whole-town approach called "Every Drop Counts" in Grays, Essex and Berwick upon Tweed, Northumberland. In both locations the higher level of customer awareness led to greater water savings than would be achieved by carrying out single projects in a number of different locations.

Our work on water efficiency has again been recognised with awards for our H2eco Analysis research programme, #watersavingselfie social media campaign and Bourne Leisure Holiday Park retrofit scheme at the 2016 Waterwise Awards. Our Every Drop Counts initiative was also awarded as 'winner' at the 2016 SWIG Awards. A further four of our projects were highly commended at the same awards.

METERING

We have continued to offer water meters companywide, free of charge, to those requesting them. All new properties must be metered.

When the occupier of a property changes, we take the opportunity to selectively install a water meter. The number of selective meters installed has started to increase as the housing market has begun to recover, towards the levels expected when forecasts were made in 2014.

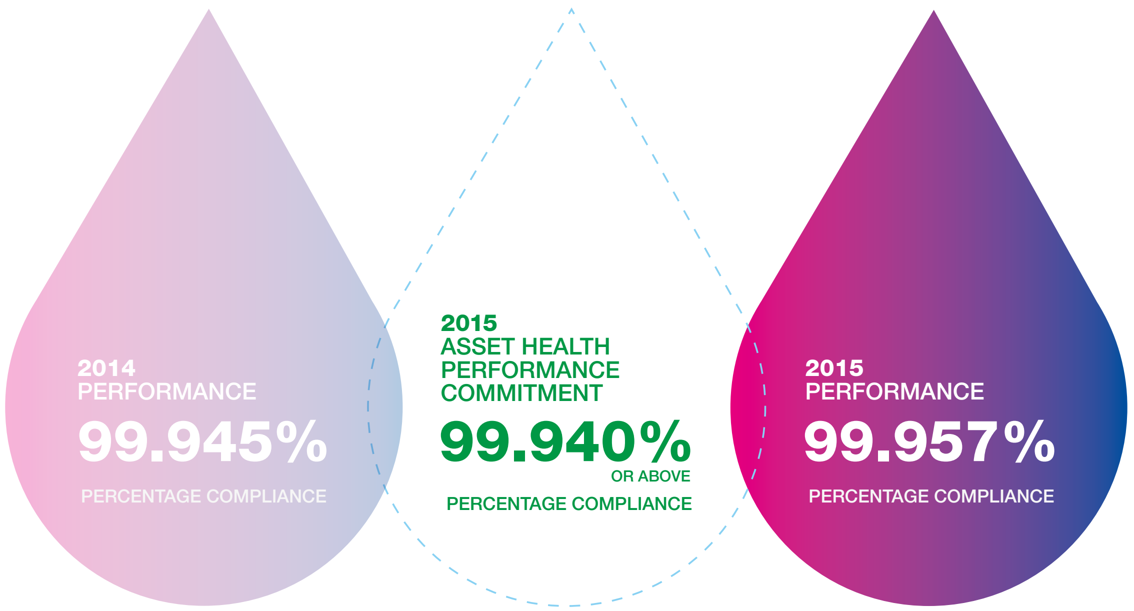
Overall, water meter coverage continues to increase with 59.8% of connected properties metered in Essex, 67.9% in Suffolk and 36.1% in NW. Combined this means that 46.2% of our total connected properties are now metered.

We supply clean, clear drinking water that tastes good

OUR MEASURES OF SUCCESS AND PERFORMANCE COMMITMENTS

This Outcome has three MoS.

OVERALL DRINKING WATER QUALITY COMPLIANCE (W-B2)



The figures above show our annual performance in 2014 and 2015 for Overall Drinking Water Quality Compliance. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017, 2018 and 2019. Consistent with this approach, Table 3A shows our three-year average performance of 99.937% for the period 2013-15, reflecting performance levels in 2013 and 2014 before the PC was applied. We need to ensure that the improving trend in 2014 and 2015 is sustained in 2016 and beyond in order to achieve our PC.

Our strategy for drinking water quality remains focused on both public health and customer confidence.

In 2015 our overall drinking water compliance was 99.957%, exceeding our Asset Health PC of 99.94%

The number of samples passing drinking water quality standards remained very high in 2015 with 99.965% of samples passing for ESW and 99.953% for NW. This represents an improvement in the ESW region whilst maintaining a solid level of compliance in the NW area.

In total we carried out around 128,000 tests companywide at customer taps in 2015 and only 29 failed strict quality standards. This compares to 69 failures seen in 2014. The improvement seen is as a result of reduced taste and odour failures and iron failures. In ESW our abstraction management scheme was a great success and the number of pesticides detected reduced from 12 in 2014 to two in 2015.

Although the overall number of failures has reduced significantly, this only results in a small improvement in the average compliance for all zones. It is important to note that the levels of pesticide, iron and lead recorded are extremely small and do not pose a risk to public health.

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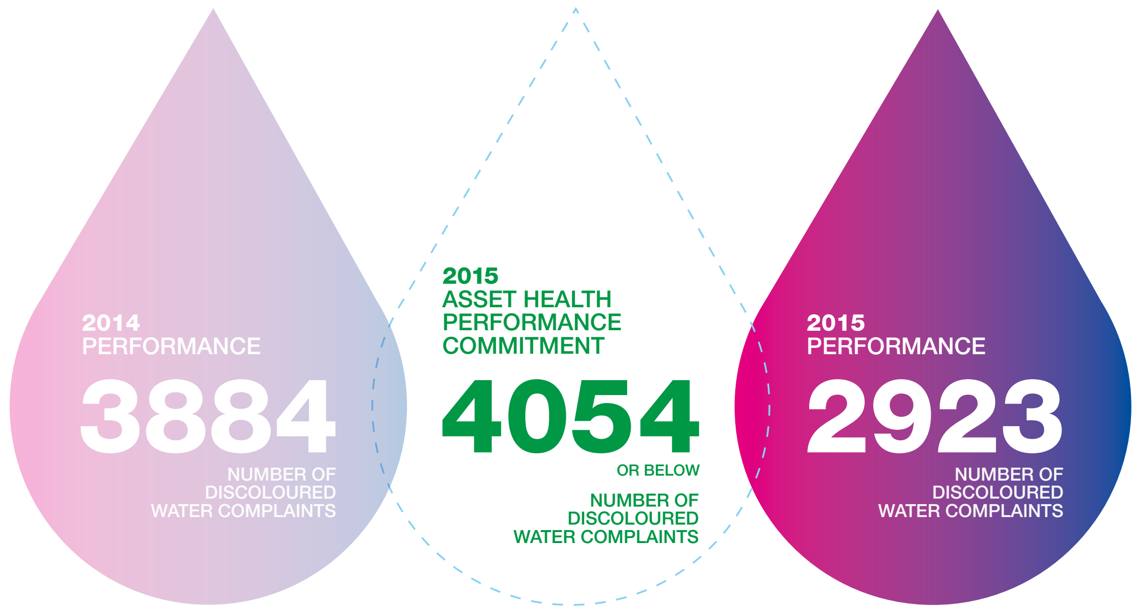
DRINKING WATER QUALITY COMPLIANCE	2014 FAILURES	2014 COMPLIANCE	2015 FAILURES	2015 COMPLIANCE
NW	33	99.947%	17	99.953%
ESW	36	99.942%	12	99.965%

In future we aim to reduce the number of water quality compliance failures further, achieving this through a combination of improved water treatment and targeted maintenance of the network.

Our strategy for drinking water quality remains focused on both public health and consumer confidence. We are committed to the supply of water which is clean, clear and tastes good whilst continuing our delivery of improvement schemes.

The DWI regulates drinking water quality and reports on water companies' performance can be found at the following link: **http://dwi.defra.gov.uk/about/annual-report/index.htm**

DISCOLOURED WATER COMPLAINTS (W-B3)



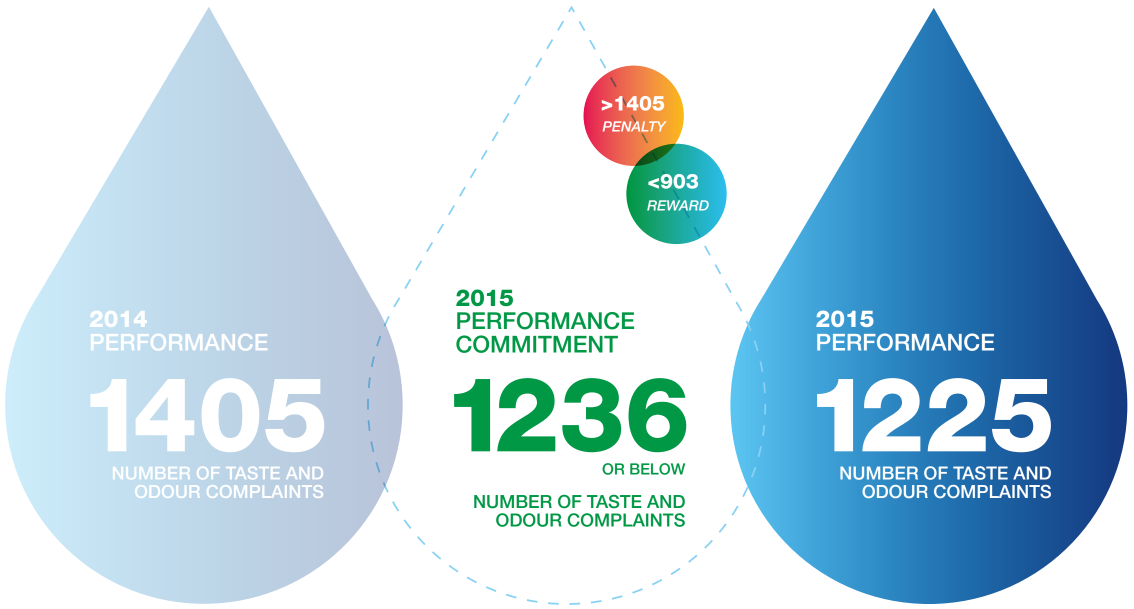
The figures above show our annual performance in 2014 and 2015 for discoloured water complaints. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017, 2018 and 2019. Consistent with this approach, Table 3A shows our three-year average performance of 3,762 for the period 2013-15, reflecting performance levels in 2013 and 2014 before the PC was applied.

Our work to reduce discoloured water contacts has reduced complaints from 3,884 in 2014 to 2,923 in 2015, our best ever performance. We aim to continue with our strategy to improve performance further for our customers.

The improvement strategy includes reducing sources of discolouration and managing the network more effectively. In short we will deliver work at treatment works to further reduce the levels of manganese, which is a source of discolouration as it accumulates in the network. We are also improving water quality at a number of sites for lead compliance reasons, altering the pH to produce stable water. This will reduce the transfer of iron from unlined pipes into the water supply, further reducing discolouration.

Through our discolouration strategy we will continue to manage our trunk mains system, routinely conditioning pipelines so that discolouration risk is minimised. We continue to flush distribution systems to manage any accumulated material while learning about return and regeneration frequencies. We have built centres to train our teams to operate the network without causing disruption. The training at the centres will also positively influence leakage and bursts.

SATISFACTION WITH TASTE AND ODOUR OF TAP WATER (W-B1)



The taste and odour of our tap water is central to our customers' experience of the service we provide and is considered important by our customers. We have undertaken a number of initiatives to improve satisfaction, including improvements in treatment and in communication. In 2014 we received 1405 complaints and in 2015 this improved to 1225 complaints.

We have undertaken research with our customers and with internal service teams to examine their experiences of taste and odour issues. This research is not limited to those who have contacted us about taste and odour but is also engaging with a wider sample of customers to help us better understand the service we provide and how it can be improved.

We are now using this research to improve our service by identifying improvements we can make to increase satisfaction with the taste and odour of our drinking water. For example, we will look to improve how we explain potential reasons for taste and odour issues to our customers, increase the support we provide online and through improved technician visits. We hope that these initiatives, amongst others, will reduce the number of contacts we receive from customers who are not satisfied with the taste and odour of their tap water, allowing us to do even better than our performance commitment in this area of service.

HIGHLIGHTS

PESTICIDES IN WATER

Some of the pesticides that could potentially reach our raw water abstraction points cannot be treated to levels that would pass quality standards. To solve this we work with farmers and other land managers to reduce or stop pesticides entering the rivers supplying our treatment works. This is called 'catchment management' and includes delivering direct advice to farmers and working in partnership with Defra's Catchment Sensitive Farming initiative. This approach also delivers associated benefits for wildlife and fish.

We had formal agreements (undertakings) with the DWI regarding 11 water treatment works relating to the pesticides metaldehyde or clopyralid. These commitments have now been carried forward into revised agreements with DWI for another five years. A number of our catchments have also been designated Safeguarded Zones by the Environment Agency (EA) and we will be carrying out prioritised activities in these areas to try and minimise risk to source waters. This will include bio-bed studies at individual farmyards, where we actively encourage and help farmers to install bio-beds and monitor the impact of them. This overall package of work towards pesticide management is recognised by the EA as part of its National Environment Programme (NEP).

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Our catchment management approach is expected to deliver long term sustainable benefits. However in the short term, metaldehyde (slug pellets) continue to represent a big risk to drinking water quality, particularly in the Essex region. To help mitigate this impact, we have extended our catchment activities to include proactive abstraction management to help protect water resources.

We employ a fast turnaround method for detection of metaldehyde in raw waters which allows us to avoid significant peaks in the pesticide by managing when we take water from the rivers. A decision matrix has been developed alongside this work to determine when to take water into storage and so minimise the risk of accumulation within our reservoirs. The number of metaldehyde failures has subsequently been reduced from 94 in 2013 to 10 in 2014 to 1 in 2015.

MICROBIOLOGICAL PERFORMANCE AT TREATMENT WORKS AND SERVICE RESERVOIRS

The microbiological performance at our treatment works and service reservoirs is very strong, and in 2015 our performance improved with only 8 failures recorded from around 50,000 samples taken during the year. This is our best annual performance and represents continual improvement in this area. It is our aim to eliminate failures completely and we continue to deliver our robust action plans to work toward this ambitious target.

TREATMENT WORKS

The number of treatment works with microbiological failures in the final (treated) water improved in 2015 with only two recorded. Inspection and maintenance regimes on our treated water tanks, process units and sample points continues to be sustained at an enhanced level to manage the risk of failure.

We have carried out extensive filter media investigations to determine whether our rapid gravity filters are performing optimally, and we are using computational fluid dynamic modelling to help understand the hydraulics in our chlorine contact tanks. In addition, we have identified a number of sites which require enhancements to comply with our own internal effective disinfection policy, and have agreed schemes with DWI to install Ultra Violet disinfection at a number of sites by 2020, as well as pH (acidity) correction and chlorine contact tank modifications to help further improve our microbiological performance.

SERVICE RESERVOIRS

Service reservoir microbiological performance significantly improved in 2015 with every site achieving the required 95% annual compliance to satisfy drinking water standards. Only six failures were recorded across more than 300 tanks within the North East, Essex and Suffolk. This equals our best ever performance and the achievement underlines the effectiveness of the enhanced inspection and cleaning regime implemented in 2009, with all service reservoirs now inspected on either a one, three or five year frequency.

MEETING THE REVISED STANDARDS FOR LEAD IN DRINKING WATER

In anticipation of changes to the lead standard, we carried out lead communication pipe replacements in 11 hot spot District Meter Areas (DMA) during the period 2010-15 where the risk of lead exposure was deemed to be high. This work was captured within an undertaking agreed with DWI and the Inspectorate has formally received evidence of scheme completion.

We continue to see lead as a critical part of our water quality programme and we intend to improve the stability of water leaving our treatment works during the period 2015-2020 to ensure lead control measures, such as adding phosphate, are fully effective. In addition, we have identified a further three DMA which have shown a high risk of failure to meet the lead standard and, therefore, we will have commenced communication pipe replacement schemes in all three.

We have recruited a lead liaison officer to help facilitate communication with external agencies and customers on lead matters and help promote awareness and identify opportunities for lead replacement schemes in our operational areas. The purpose of this new role is to focus on vulnerable groups with respect to lead, and so ensure we are fully focused on public health. Our integrated package of work for lead has been captured by DWI under a Regulation 28 commitment.

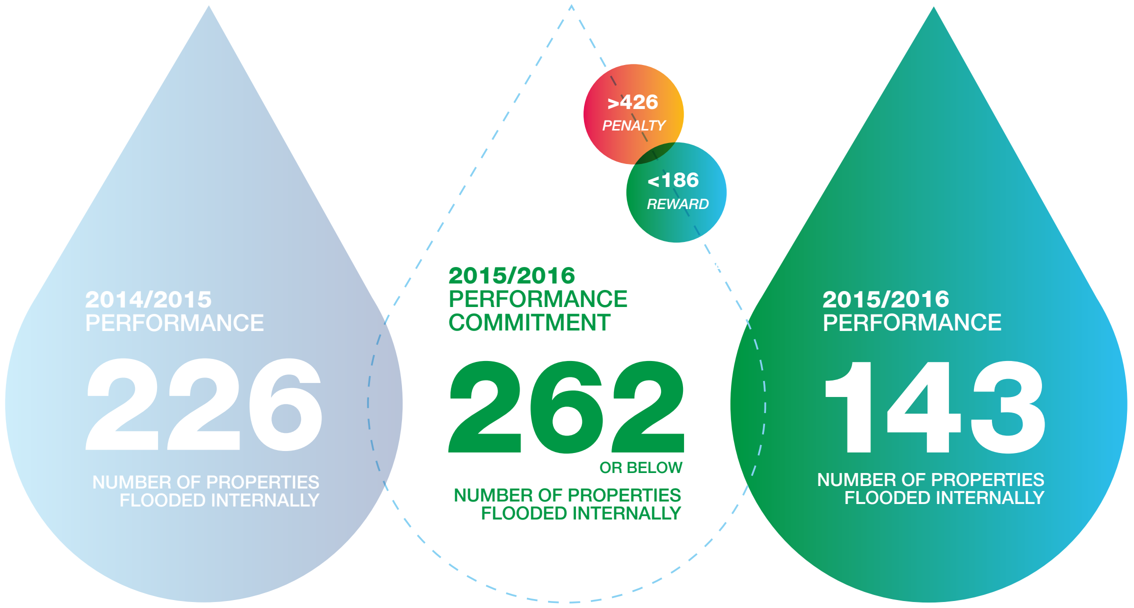
We provide a sewerage service that deals effectively with sewage and heavy rainfall

OUR MEASURES OF SUCCESS AND PERFORMANCE COMMITMENTS

Our sewerage system is an essential network of 30,000km of sewer pipes and pumps that lie unseen beneath virtually every street and road. The ownership of 13,500km of these pipes was transferred to us in October 2011 and those pipes are referred to as transferred drains and sewers (TDS). The remaining 16,500km are known as our public network.

This Outcome has seven measures of success, covering the public and TDS sewerage network, and relating to sewer flooding performance as well as network condition.

PROPERTIES FLOODING INTERNALLY (PUBLIC NETWORK) (S-B2)



We have reduced the number of properties in our area flooded internally from sewers (public network) for all causes, but excluding severe weather, from 226 properties in 2014-15 to 143 in 2015-16. This out-performed our PC of 262.

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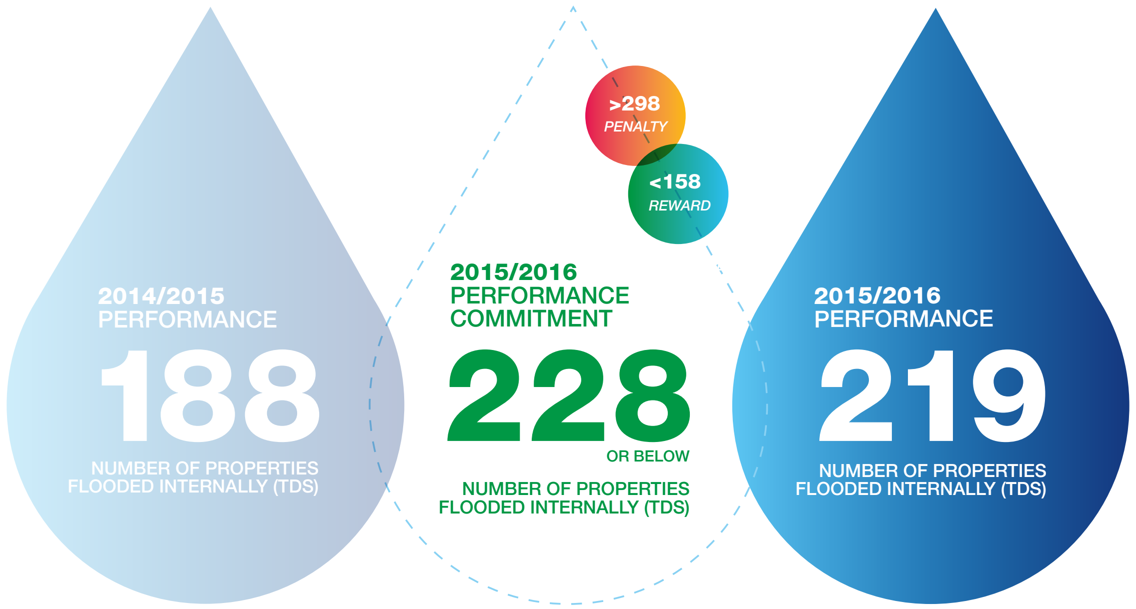
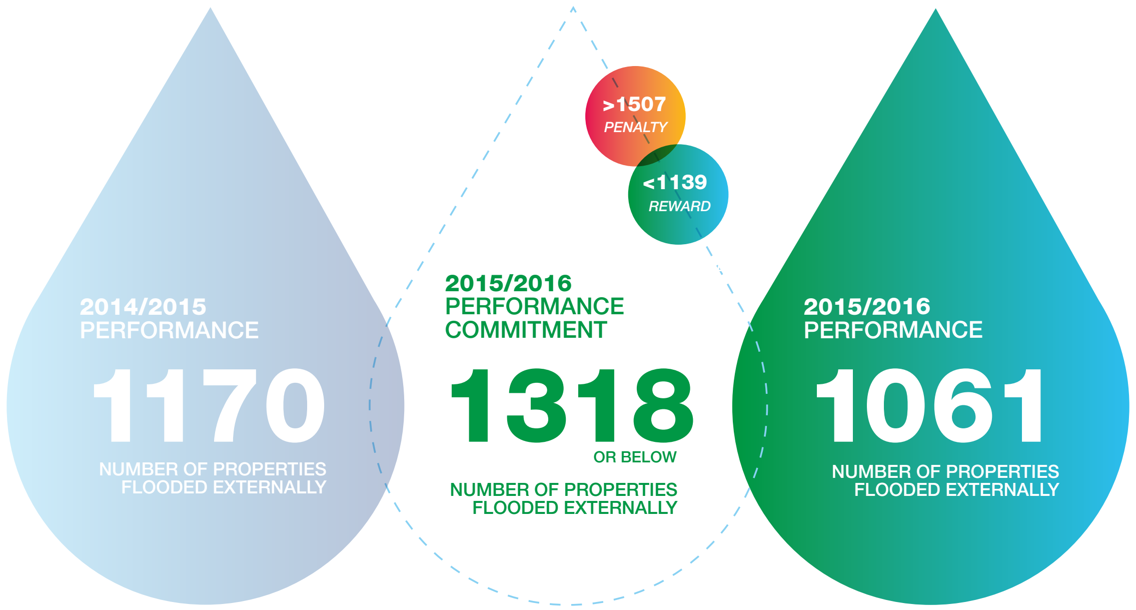
PROPERTIES FLOODING INTERNALLY (TDS NETWORK) (S-B5)



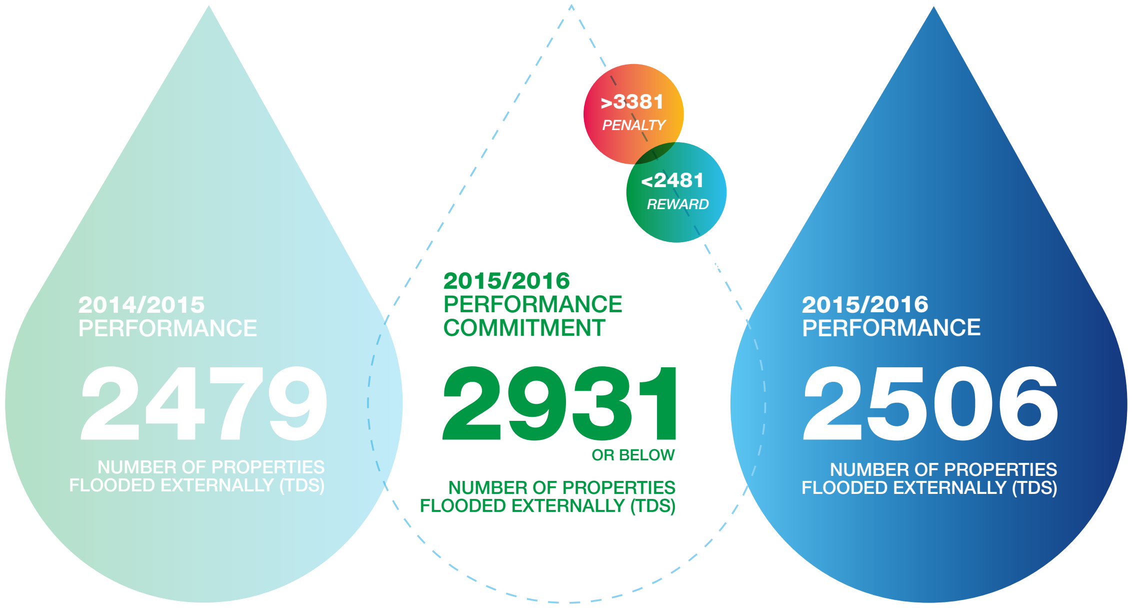
In 2015-16 there was a slight increase in the number of properties flooding internally from our TDS network to 219, but within our PC of 228 properties.

PROPERTIES FLOODING EXTERNALLY (PUBLIC NETWORK) (S-B1)



We met our PC in 2015-16, improving on the previous year's performance.

PROPERTIES FLOODING EXTERNALLY (TDS NETWORK) (S-B6)



We met our PC in 2015-16, improving on the previous year's performance.

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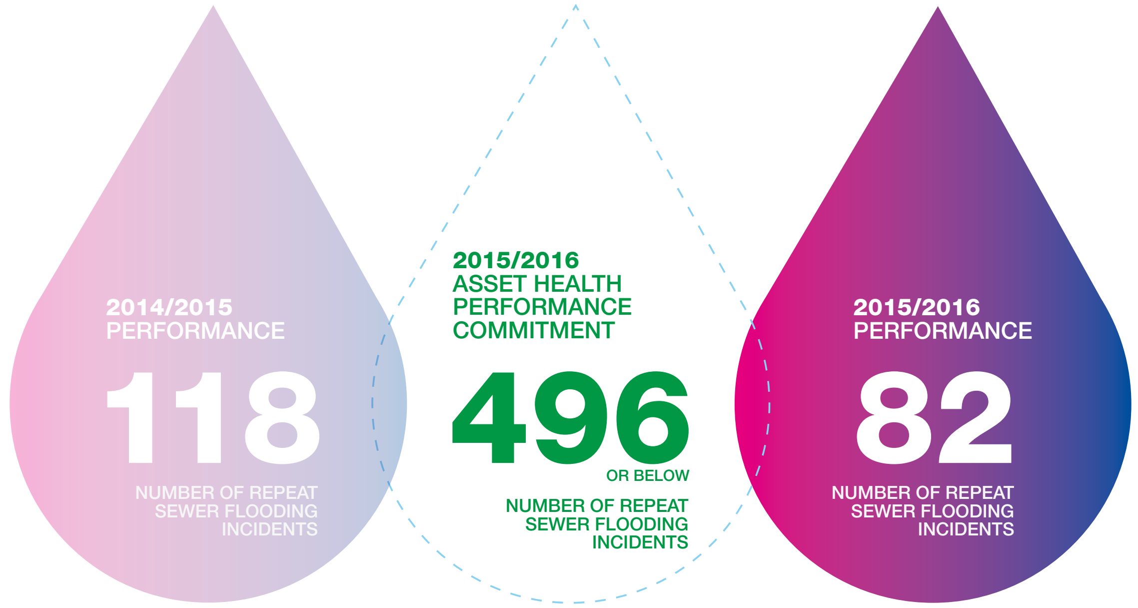
PROPERTIES SUBJECT TO REPEAT FLOODING (WHICH INCLUDES SEVERE WEATHER) (S-B3)

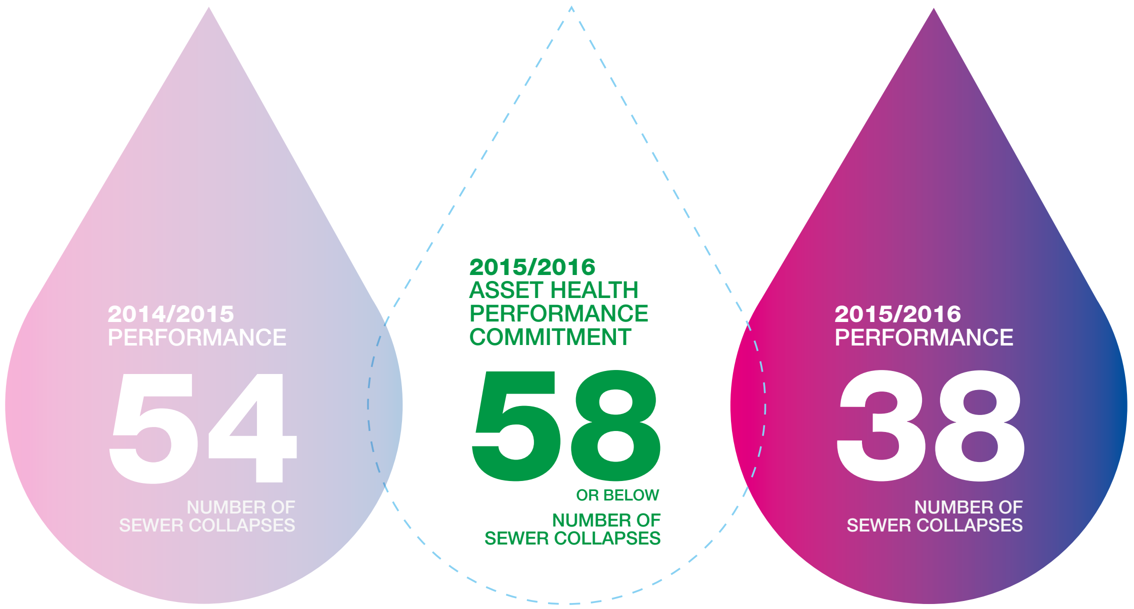


The figures above show our annual performance in 2014-15 and 2015-16 for repeat sewer flooding. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017-18, 2018-19 and 2019-20. Consistent with this approach, Table 3A shows our three-year average performance of 184 for the period 2013-14 to 2015-16, reflecting performance levels in 2013-14 and 2014-15 before the PC was applied.

We have made improvements in repeat sewer flooding, which includes flooding in severe weather, reducing the number to 118 instances in 2014-15 to 82 in 2015-16.

Whilst this improvement in performance is excellent, it is important to note that this is a volatile measure that can be influenced in any year by the extent of wet weather and intense storms. However, our work is gradually making our sewerage system more resilient to the extremes of weather.

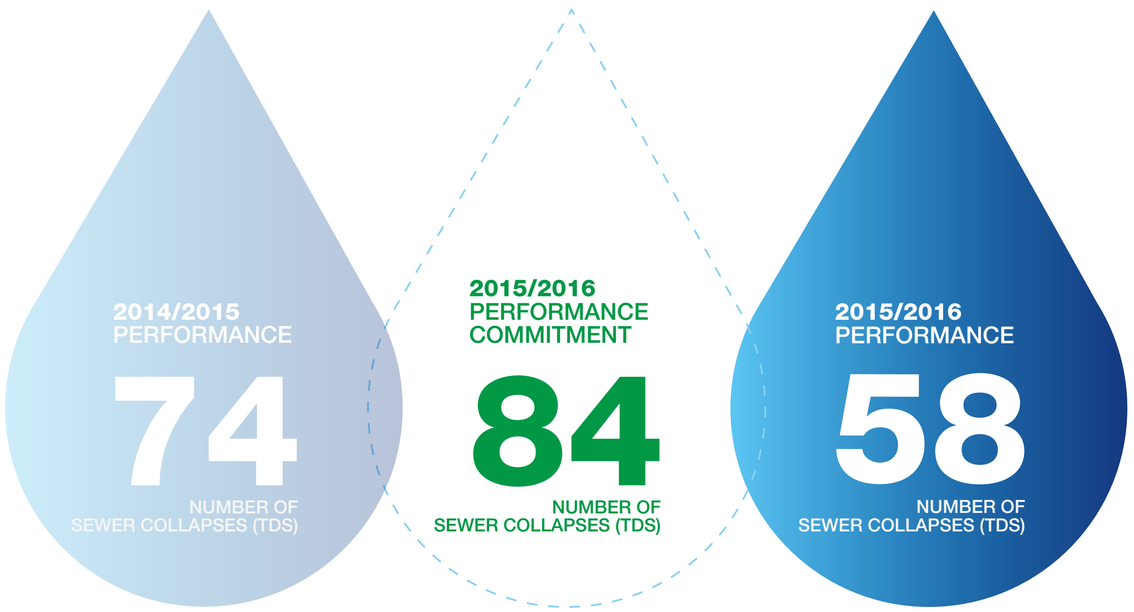
SEWER COLLAPSES (PUBLIC NETWORK) (S-B4)



The figures above show our annual performance in 2014-15 and 2015-16 for sewer collapses on the public sewer network. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017-18, 2018-19 and 2019-20. Consistent with this approach, Table 3A shows our three-year average performance of 48 for the period 2013-14 to 2015-16, reflecting performance levels in 2013-14 and 2014-15 before the PC was applied.

Our sewer collapse performance improved further in 2015-16 and we expect it to continue to be industry-leading when results are published in the summer.

SEWER COLLAPSES (TDS NETWORK) (S-B7)



In 2015-16 we further improved our sewer collapse performance on our TDS network.

HIGHLIGHTS

MANAGING OUR ASSETS

For the majority of our customers the sewerage service that we provide is invisible and not something that they need to think about on a daily basis. Good customer service is providing this invisible service whilst responding quickly and efficiently if issues arise.

Sewer flooding is a significant problem. It can happen when rainfall is so heavy that there is more water than the sewers are designed to transport and they become 'overloaded'. It may also occur when sewers become blocked or broken. In either case sewage escapes from our network and may find its way into our customers' gardens, homes and business premises. Although there are technical differences in the cause of the failure, the unpleasant consequence to our customers is the same.

Undoubtedly the worst service failure that our customers can experience is sewer flooding. It is unpleasant and distressing for customers. When sewage escapes from our network it can also have a detrimental effect on the environment.

We are wholly responsible for maintaining the performance of our sewer network in order to provide an effective sewerage service to our current and future customers. We also have a responsibility to work with other organisations to play our part in resolving wider drainage issues, including surface water flooding which can often lead to sewer flooding. This is particularly important as heavy rainfall is the predominant cause of surface water flooding.

INNOVATIVE, SUSTAINABLE SOLUTIONS IN LIAISON WITH OUR PARTNERS

Whilst the majority of our improvement works have been conventional up-sizing of the network and/or the provision of additional storage, during 2015-16 we have continued to deliver a number of more innovative and sustainable solutions to reduce flood risk. Much of this work has been carried out in partnership with other agencies. For example, our Sustainable Drainage (SuDs) for Schools initiative where we have worked with the Wildfowl and Wetlands Trust to introduce sustainable flood risk reduction solutions at a number of local schools.

Our industry-leading approach to partnership working which led to the formation of the Northumbria Integrated Drainage Partnership (NIDP) continues. This partnership between our company, all 13 Lead Local Flood Authorities (LLFAs) in our region and the EA has developed an agreed proactive approach and implemented a regional risk based prioritisation methodology to identify integrated drainage issues.

An example of work delivered through the NIDP approach is a flood risk reduction scheme at Brunton Park in Newcastle, where the innovative solution included the diversion of the River Ouseburn. Our approach has been recognised and we received an Institute of Water (Northern) Innovation Award and won the Utility Week Water Industry Achievement Award 2015 in the category of 'Sustainable Drainage and Flood Management'.

COMMUNITY ACTION PLANS

In 2015-16, we have launched our programme of Community Action Plans (CAPs). Our aim is to proactively deliver flood risk reduction in the most effective manner whilst developing community involvement and promoting partnership working.

We target local communities (Drainage Areas) to deliver innovative and sustainable flood risk reduction. Our work includes interventions at customers' properties to carry out surface water audits and deliver very localised solutions. For example disconnection of surface water drainage and diversion of it to water courses or water butts. We also consider innovative methods such as landscaping as a flood risk reduction solution.

Wherever possible, we look to deliver sustainable solutions, such as those we have already done with through our SuDs for Schools initiative. Our proactive activity includes sustainable solutions that divert, delay and store rain water to reduce the risk of flooding to properties that have experience flooding as well as delivering flood risk reduction to properties that have not experienced flooding.

OPERATIONAL RESPONSE

We have continued to improve our operational processes. This has enabled us to greatly improve the service we provide to our customers following a sewer flooding incident; including accelerating the subsequent investigation process and providing property level protection measures for customers whilst feasibility studies and design work is carried out.

To reduce the risk from blockages, we have increased sewer lining (to address tree root intrusion), sewer cleansing and sewer inspections. We also use bacillius bacteria (fat eating bugs) in some areas of the network where we have known fat, oil and grease issues.

LOVE YOUR DRAIN

Our 'Love Your Drain' campaign, spearheaded by the campaign character, Dwaine Pipe, continues to grow and to inform customers about the causes of blockages and what can be disposed of down the toilet and sink. Working together with our customers has had a real impact on reducing the number of unnecessary sewer blockages caused by material such as baby wipes, fats, oils and grease. In particular, our innovative work with schools and food outlets is helping to change customer behaviour.

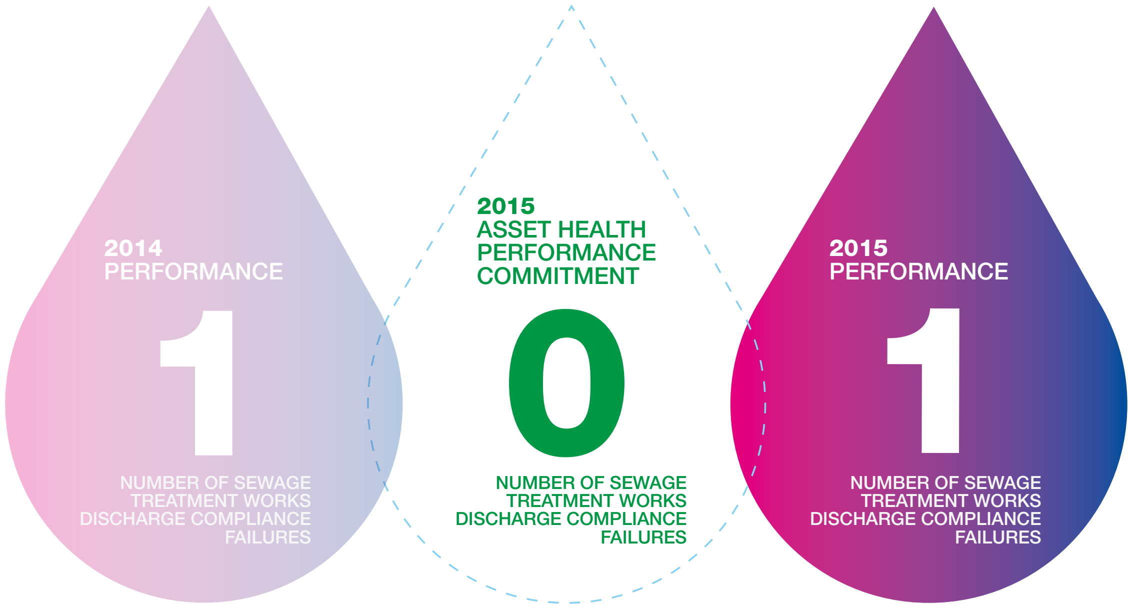
ANNUAL PERFORMANCE REPORT

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

OUR MEASURES OF SUCCESS AND PERFORMANCE COMMITMENTS

This Outcome has three measures of success: sewage treatment works discharge compliance; pollution incidents (category 3); and bathing water quality compliance.

SEWAGE TREATMENT WORKS DISCHARGE COMPLIANCE (S-C1)



The figures above show our annual performance in 2014 and 2015 for sewage treatment works discharge compliance. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017, 2018 and 2019. Consistent with this approach, Table 3a shows our three-year average performance of 1 for the period 2013-15.

Our Sewage Treatment Works (STW) compliance performance has been excellent for a number of years.

Each of our significant STWs has a numerical discharge consent standard designed by the EA to protect the environment. In 2015-16 there were no STWs failing their discharge consent against the Upper Tier standard.

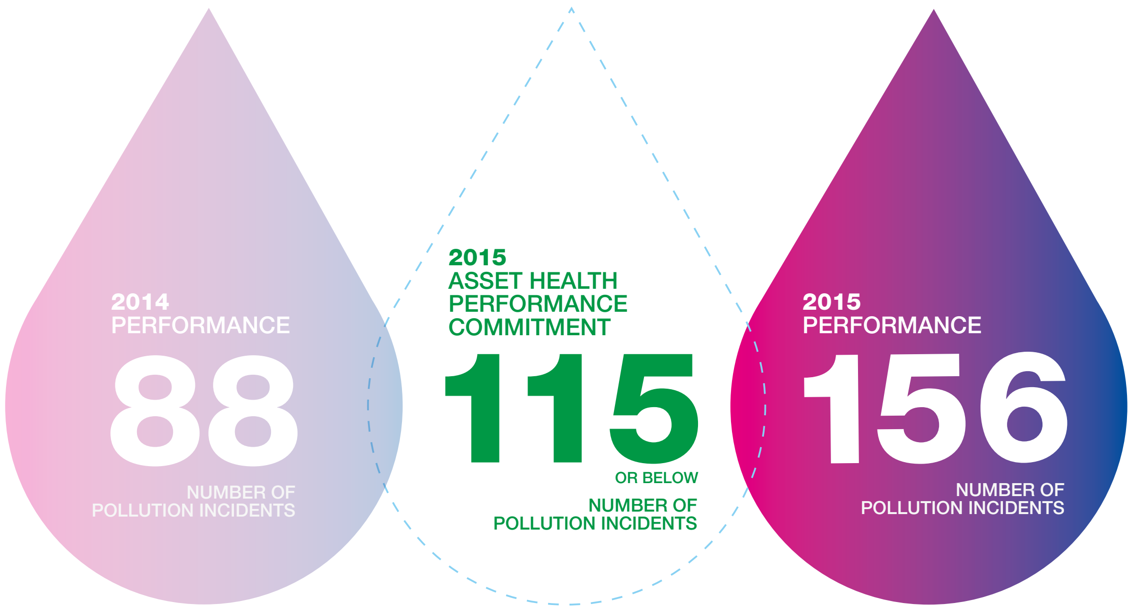
We had one site fail against the 'Look-Up Table' permit conditions in 2015. This was particularly disappointing for us as the sample failures were as a result of third party action. This was the first fail following a run of 100 per cent compliance for seven consecutive years. This now places us a close second to the industry-leading performance position.

In 2015 the EA's report on our STW performance identified only one failed works for NW. This refers to sample exceedances at a site against the look-up table for Biological Oxygen Demand in the permit. These exceedances were linked directly to third party action resulting in the by-pass of a critical treatment process unit. All the other STWs successfully complied with the terms of their permits for the year.

We are continuing to improve the way we monitor the discharges coming from our STWs, with increased on-line instrumentation and early warning trigger management so that we can resolve problems before there is an impact on the water environment.

Investment plans during 2015-2020, as agreed with the EA in the latest phases of the NEP, will reduce the amount of phosphorus being discharged at some of our STWs and will allow us to continue our contribution to improving river water quality in the north east.

POLLUTION INCIDENTS (CATEGORY 3) (S-C2)



The figures above show our annual performance in 2014 and 2015 for category 3 pollution incidents. As this is an Asset Health measure, compliance with our PC will be assessed based on three-year average performance at the end of 2017, 2018 and 2019. Consistent with this approach, Table 3A shows our three-year average performance of 124 for the period 2013-15.

Pollution incidents (including those from transferred drainage services and water-related assets) increased from 88 in 2014 to 156 in 2015. This was a result of changes in reporting mainly affecting pollution incidents recorded from sewage pumping stations.

We had our best ever self-reporting performance in 2015 of 82% compared to our previous best of 71% in 2012 and 55% in 2014.

Of the 156 category 3 incidents, 4 of these were water incidents, all in NW. The number of more serious category 1 and 2 pollution incidents increased to five in 2015 from three in 2014.

To improve our performance, we continue to invest in sewer level monitoring technology and trend analysis to aid prediction of where pollution incidents are likely to occur and to detect and resolve problems at a warning level before they cause an overflow. Over 87% of our Combined Sewer Outfalls (CSOs) are now monitored.

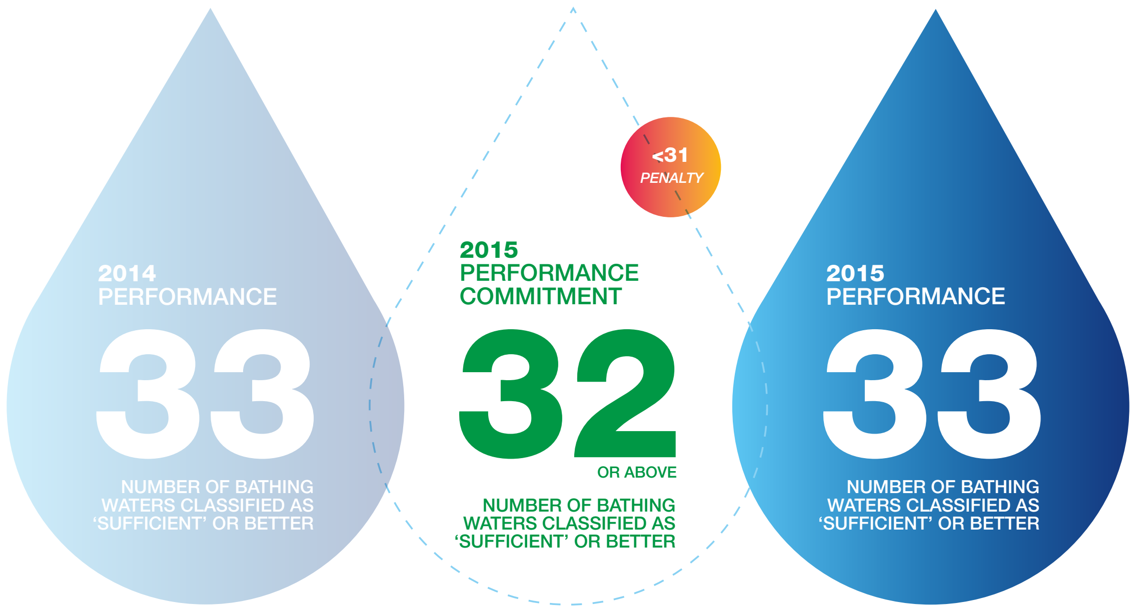
For 332 cases in 2015, operators were alerted and attended site to clear a problem before there was any overflow. By 2020, we aim to have all of our CSOs monitored and to have completed the development of a business intelligence system that will improve our capability for early notifications of potential problems.

Our work in 2015 also included a significant programme of replacement of deteriorating assets.

In 2015, we reviewed our very successful Water Rangers initiative that encourages members of the public to make regular observations on a watercourse and alert us to any unusual discharge into it. The Water Rangers have delivered real benefits via early identification of pollution incidents, enabling prompt remedial action and helping NWG meet its commitment to protecting and improving the environment.

With over 1,600 patrols being recorded since the scheme began in December 2014, we are now planning to extend this initiative to cover additional areas identified as at risk of pollution and also increase the number of Water Rangers we have patrolling our vulnerable waterways.

BATHING WATER QUALITY COMPLIANCE (S-C3)



Our bathing waters are some of the cleanest in the country. Last year we had the first classifications for designated bathing beaches under the revised Bathing Water Directive with 33 of our 34 beaches meeting the tighter requirements (Sufficient or better). 30 bathing waters were classed as either Good (11) or Excellent (19) with 3 being Sufficient.

We have continued to work to ensure that all of our bathing water assets are consistent with the requirements of the Bathing Water Directive by investing in improvements and undertaking investigations towards all bathing beaches being Sufficient or better in our region.

Spittal bathing water at Berwick-upon-Tweed, classified as 'Poor' under the Bathing Water Directive, was believed to be subject to de-designation in 2015 either through usage or disproportionate cost. Following a decision in summer 2015 by Defra not to de-designate, we conducted an investigation. Whilst this bathing water is impacted by agricultural diffuse sources from the River Tweed catchment, the investigation concluded that Spittal is highly likely to return to Sufficient status after the 2016 bathing season.

We will continue to work in partnership with the EA, Scottish Environment Protection Agency (SEPA) and Northumberland County Council to improve bathing water quality at Spittal beach.

We have worked in partnership with the EA and Redcar & Cleveland Borough Council towards improving bathing water quality at Saltburn. We delivered an improvement scheme in the Saltburn catchment meeting our commitments under the National Environment Programme that was completed in autumn 2015. The bathing water has improved from Poor in 2011 to Good in 2015.

Improvement work was also brought forward at Seaham where we made improvements for the Seaham Beach and Seaham Hall bathing waters which were completed in summer 2015.

We are also carrying out investigations to identify what we can do to further improve water quality at nine bathing waters towards more Good and Excellent beaches.

HIGHLIGHTS

UPDATE ON CHANGES TO THE 2015-2020 NATIONAL ENVIRONMENT PROGRAMME (NEP) PHASES 4 AND 5

RIVER QUALITY SCHEMES

A scheme was included in the 2010-15 NEP investment programme to improve the discharge to the watercourse from Sedgeletch STW. Further improvements at this works was also highlighted as being required during 2015-20 to reduce the discharge of phosphorous. It was therefore agreed with the EA that the schemes are combined, carrying out feasibility in 2014-15 to allow construction in 2015-20. The study confirmed that the standard required to make any improvement to the downstream river water quality was lower than technically feasible to achieve. It was therefore agreed that the standard included in the AMP6 NEP would be an annual average of 1 mg/l rather than 2 mg/l of phosphorous. This would ensure improvement to the river as far as practicable based on a technically achievable permit standard.

The NEP also included three other schemes for the removal of phosphorous at Barkershaugh, Chester-le-Street, and Chilton & Windlestone STWs. The EA requested that these schemes be completed early if possible. We completed the work for Barkershaugh and Chester-le-Street in 2014 and Chilton & Windlestone was finished in May 2015.

A number of phosphorus removal schemes are included in the 2015-20 (AMP6) NEP with both no deterioration drivers (delivery March 2018) and pathway to Good improvements schemes (delivery March 2020). Ramshaw STW was included as a no deterioration scheme, and was then also flagged with a tighter consent as part of pathway to Good. In order to avoid abortive investment and to implement the best catchment solution, the EA has agreed in principle that delivery of a solution at Ramshaw can be postponed until the later date of 2020, in order to transfer the flows from Ramshaw to Cockfield for a combined treatment solution. This will need to be detailed and agreed through the formal change protocol process.

The 2015-2021 (AMP6/early AMP7) phase 5 NEP also includes four additional phosphorus removal schemes for delivery early in AMP7.

EVENT DURATION MONITORING

An assessment in 2015 of all our intermittent discharges against the EA's Risk Based Approach to the Monitoring of Storm Discharges resulted in additional requirements for the installation of Event Duration Monitoring (EDM) being included in NEP Phase 5.

We have a total of 1,586 intermittent discharges that are mainly CSOs in the sewerage network but also include CSOs and storm discharges at sewage works, and storm discharges at sewage pumping stations.

Sewer level monitoring fulfils the requirements of EDM and a programme to complete the installation at CSOs, together with monitoring technology for the other types of intermittent discharges, is being developed for delivery between 2017 and 2020.

WHITBURN SPILLS REDUCTION

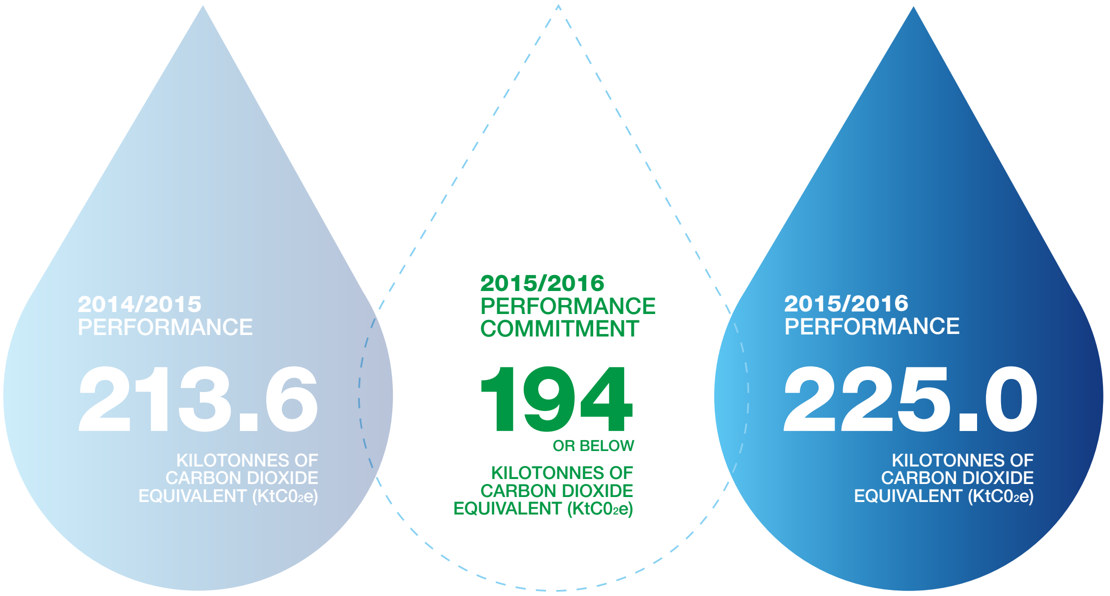
Work commenced on the feasibility phase of the project in November 2015 with our framework suppliers. The solutions identified during the feasibility stage are now being defined and are an optimised combination of existing assets, separation and attenuation of surface water from the sewer network and provision of additional network capacity. This approach will deliver benefits in addition to reducing spill frequency at Whitburn Steel Pumping Station and St Peter's CSO. We have engaged with the EA and Defra who support our proposals and have recently met with the European Commission to discuss them, with positive feedback received. We are also working with the City of Sunderland and South Tyneside Council to ensure that the benefits of the project are maximised.

The work to fully define the solutions is progressing well and is scheduled to be completed in May 2016. This will be followed by the award of a design and construct contract in August 2016. Construction work is scheduled to begin in September 2016 with completion by November 2017, to meet our NEP obligation.

ANNUAL PERFORMANCE REPORT

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

GREENHOUSE GAS EMISSIONS (W-F1 & S-F1)

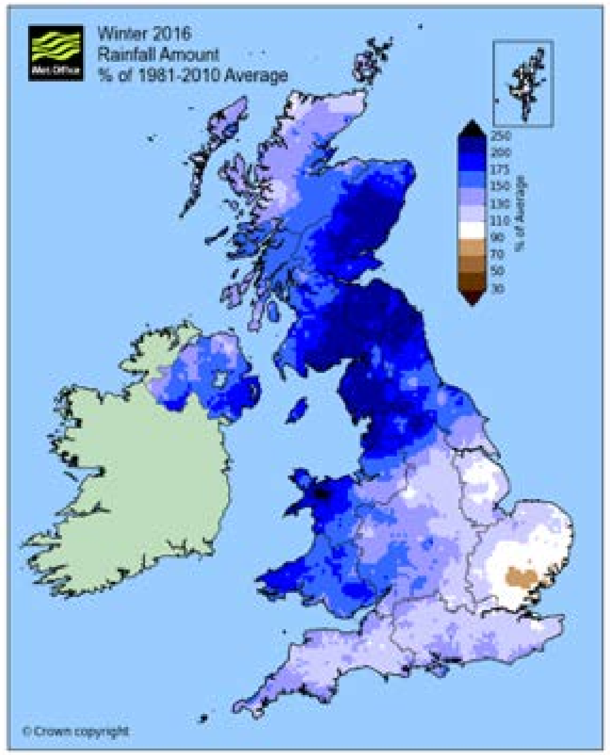


The protocol that we use for measuring our emissions is based on the Carbon Accounting Workbook developed and updated annually by the Water Research Council, on behalf of the water industry, and published by UK Water Industry Research. This is founded on international and DEFRA protocols but includes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

Our total net operational GHG emissions for the year ended 31 March 2016 increased to 225.2 ktonnes CO_2e (31 March 2015: 213.6 ktonnes CO_2e). This reflected an increase in energy usage of 12% less a 7% reduction in the emissions factor applied for grid electricity, partly reversing an increase seen in the previous year.

The increase in usage was largely driven by weather conditions, with dry weather in our NW region in spring and summer 2015 requiring us to carry out more transfers of water resources and utilise more energy intensive treatment works, whilst high winter rainfall significantly increased sewage pumping activity. In addition, our new process to transform biogas from AAD into biomethane and inject this into the national grid contributes to long term sustainability of the UK's gas supply but, perversely, has caused an increase in our emissions reported under current rules as the benefit of the gas export is not included in the calculation. If the gas export had been included, like exported electricity, our emissions would have been 217.4 ktonnes CO_2e.

Our carbon management plan has the aim of reducing our GHG emissions by 35% by 2020 against a 2008 baseline. We remain ahead of target with emissions down by 27% compared to the baseline.



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. As described above, these measures can be volatile depending upon levels of rainfall and pumping requirements, therefore we focus on longer term trends.

ANNUAL OPERATIONAL GHG INTENSITY RATIO	2015-16	2014-15
Emissions/Ml of water	239	246
Emissions/Ml of sewage treated (flow to full treatment)	319	300
Emissions/Ml of sewage treated (water distribution input)	607	540

Figures in kgCO_2e/Ml

ANNUAL ENVIRONMENTAL PERFORMANCE AND ACTIVITY (W-F2 & S-F2)

In March 2016 the independent NWGL Corporate Responsibility Action Groups (CRAG) north and south endorsed the environmental activity of NWGL for 2015 drawing particular attention to the following:

- The official opening of Abberton Reservoir by Sir David Attenborough;
- 100% of sewage sludge being used to generate renewable energy;
- One year of further cleaning the biogas and injecting biomethane into the natural grid;
- Employee engagement with nature through Nature Watch; and
- The volunteer army of Water Rangers who monitor water courses.

The CRAGs encouraged NWL to continue its efforts for 2016.

The next report on our environmental, social and economic performance will come from the Water Forums in 2017.

We deliver water and sewerage services that meet the needs of current and future generations in a changing world (W-A1 & S-A1)

We use the concept of "Asset Health" as an innovative way of monitoring, protecting and incentivising the long-term sustainable stewardship of our assets.

To monitor Asset Health we use two groups of MoS – "baskets", one for water and one for wastewater.

The MoS in our water Asset Health basket are discoloured water complaints, overall drinking water compliance, properties experiencing poor pressure and water mains bursts.

The MoS in our wastewater Asset Health basket are sewage treatment works discharge compliance, pollution incidents, sewer collapses and repeat sewer flooding.

As the Asset Health concept is about the long term stewardship of our assets, performance is not assessed annually, but on a three-year rolling average basis at each of three assessment points: at the end of 2017-18, 2018-19 and 2019-20. We will not assess whether our performance commitments are being met until the first assessment point at the end of 2017-18.

We aim to meet or exceed our PCs for our Asset Health measures at these assessment points. More detail on our year on year performance against these measures can be found earlier in this commentary against each individual measure.

We also have companywide accreditation to ISO55001 for asset management, which demonstrates that we follow best practice in the long term management of our assets.

ANNUAL PERFORMANCE REPORT

OUR ENABLING AND REPUTATION OUTCOMES

We are an efficient and innovative company

INNOVATION

Innovation – the successful exploitation of new ideas – underpins our current performance and is the key to our future success.

It is essential for us to innovate in order to improve service and environmental performance, maintain our large asset base and respond to changes in the regulatory and competitive environment, all at a cost that our customers can afford.

During the last year we have focused efforts on a number of programmes and tools to support our people, creating a culture of innovation. We work in partnership with universities, research organisations and the wider industry to develop and implement leading-edge technical solutions, driving the development of, and making best use of, technologies and business processes to achieve our outcomes.

We have a great track record of applying innovative and creative solutions, which is a reflection of the willingness of our people and partners to continuously strive for better and more efficient ways to deliver our business.

Examples include:

- Deployment of our customer portal, to support engagement and deliver great customer communication for some of our major capital schemes;
- Exploring opportunities for use of Unmanned Aerial Vehicle (UAV, or "drone") technology for asset inspection, reducing cost and health and safety risks;
- Porcupine, a low cost device for tracing potential sources of non-flushable materials in the sewer network;
- Development of a monitor for air valves on sewer rising mains, to identify problems before they result in pipe bursts;
- Working with design students at Northumbria University to bring fresh perspectives and generate new ideas to address our business challenges; and
- Greater use of renewable energy.

To meet the challenges of delivering our AMP6 (Asset Management Plan) capital investment programme as efficiently and effectively as possible, we have implemented a new operating model in respect of the way we interact with our supply chain. This is based on four key principles, in line with best practice and the UK Government Construction Strategy 2010. These principles are: we operate as a well-informed professional client; we offer clear visibility of, and commitment to, future workload to suppliers; we engage suppliers as early as practicable in the delivery process to add value and innovation; and we create the right environment for collaboration and co-operation, incentivising innovation and performance.

Other supporting principles include the separation of planned and reactive work, integration of the design and construction process, delivery arrangements suited to the complexity and nature of the work, and wide adoption of a target cost approach to support joint incentivisation. We believe that this will enable us to deliver our business outcomes significantly more efficiency than in AMP5.

We were re-assessed against the EFQM excellence model in 2015 by a team of independent assessors appointed by the British Quality Foundation. The outcome of the assessment was an EFQM score of 614, achieving the "excellence 600" level. This is a higher standard than the five star level of excellence we achieved in 2012, which is awarded for achieving a score over 500.

WE TOP THE BRITISH WATER SURVEY

For the sixth time in the last seven years NWG has come first in the British Water Survey.

British Water is the trade association for the UK water industry supply chain, representing the industry collectively, to government, regulators, other institutions, customers and the media.

Each year, British Water conducts a survey of water company performance that gathers views from the UK water industry supply chain (contractors, consultants, suppliers) on how the major 12 UK Water and Sewage companies perform and compare with each other. Nine areas of performance are covered including contract procurement, contractual approach, impact on the supply chain, professional qualities and communication.

The survey is completed by NWG suppliers, who range from framework capital contractors and consultants to chemicals suppliers, distribution materials suppliers, IS service providers, and maintenance, waste and operational contractors. Many of our suppliers also work for other water companies and assess their performance as well.

Coming first demonstrates the hard work we've put into building strong working relationships with our suppliers in order to deliver a great service to our customers. This is a great result and we're really proud to have been voted number one again.

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

CREDIT RATING

We have retained our credit rating of BBB+ and Baa1.

We are the retailer of choice for business customers

READINESS FOR RETAIL

NWG continues to develop its retail business in readiness for the opening of the competitive market for retail water and sewerage services in April 2017. Recently the business has reached a key milestone in starting user testing the new customer billing system that will underpin the core processes of the market. The retail business is also finalising its suite of value added services and customer facing communications channels that will support the customer retention and acquisition strategies.

ACCOUNT MANAGEMENT

Existing large industrial customers receive an account management service providing a single point of contact for all their needs. We collect regular feedback from these customers to ensure that this service is meeting requirements. As part of this feedback, net promoter score is measured which currently stands at positive 31.

We are proud to contribute to the success of local communities

JUST AN HOUR

Just an hour is our highly successful employee volunteering programme.

We recognised both the need to take our community support beyond a pure donation of cash and also the wealth of knowledge, skills and expertise of our employees. In response we have developed a structured programme of employee involvement in the community designed to have a positive impact on the wellbeing of our local communities, the health of our environment and the prosperity of our local economies.

Our Just an Hour programme enables each of our employees to spend a minimum of 15 working hours a year on volunteering activities allowing them to support the causes they care about whilst developing their skills.

Since the launch of Just an Hour in 2002, our employees have committed more than 100,000 hours in support of our communities. More than half of our workforce are actively engaged in the programme, with 53% of our people volunteering their time in 2015, giving 16,276 hours to support 979 organisations.

KEY PARTNERS

We work with organisations across a broad range of sectors – including business, charitable, historical, cultural, educational and environmental bodies. We recognise the variety of benefits this mix of partnerships can bring.

- **Educational partners** - In 2015 we engaged with more than 9,000 young people in programmes to support their learning, development and readiness for work;
- **Organisations based on our sites** - We are proud to host a number of partners on our sites; enabling these special places to be enjoyed by the community. In 2015 we welcomed more than 500,000 visitors to these sites;
- **Memberships** - We work with a number of business and trade bodies across our region and nationally, to support engagement with our customers and on significant areas of policy that impact on the wellbeing of the areas we serve; and
- **Cultural, environmental and historic memberships** - We hold memberships with a number or arts, historic and cultural organisations. Our memberships support the important work of these organisations, particularly their work to enhance the quality of life in our local areas.

GRASSROOTS SUPPORT

In addition to our flagship partnerships and key partners, we also have supported grassroots community, charitable and environmental activity. Four Community Foundations hold endowment funds that are used to support a range of community and charitable activities across our areas of supply.

These are long term investments, with the income from the funds being donated, with the advice of the Community Foundations, by a committee of our people.

We value the expertise of our partners at the Community Foundations in expertly managing these funds, having first class knowledge of local needs and helping us direct our grants in the most effective way.

In 2015 through our funds at the Community Foundation we donated £26,416 to help 27 different organisations.

BOTTLED TAP WATER

Supplying top quality tap water that is great value for money is integral to what we do. We are pleased to provide our very own bottled tap water to charities and not for profit groups for use at outside events.

Since starting the scheme in 2005, we are proud to have more than one million bottles of water to support community events. As each bottle contains 500ml this means we have given away a massive 500,000 litres or 6,250 baths over 10 years.

During 2015 our bottled tap water scheme has continued to be popular. We donated 85,000 bottles of tap water to 178 organisations.

BRANCH OUT

Our Branch Out fund helps to deliver projects that benefits the natural environment and their local communities. A healthy natural environment is essential for us today and to ensure we can continue to supply top quality drinking water and safely remove wastewater in the future.

Branch Out is about working in partnership to reconnect habitats for the benefit of people and wildlife. In 2015 the fund has continued to enable number of projects with the aim of helping this region build resilience and adapt to the changing climate whilst bringing benefits to water, wildlife and communities.

In 2015, through Branch Out we supported a variety of partners with 21 projects providing close to £80,000 in funding. This funding has unlocked a further £891,482 in match funding for our partners.

We work in partnership towards common goals

We are proud to contribute to the success of our local communities. In 2015 we continued and extended our extensive activities in this area.

Our work in our communities is based on our Partnerships Strategy, which gives a clear direction to ensure we are focusing our efforts on the things that our customers have told us are most important to them.

Our Partnership Strategy puts working with partners to deliver common goals at the heart of our community activity. Our contribution in 2015 is detailed in our Annual Partnership report, which is available on our websites at:

Northumbrian Water

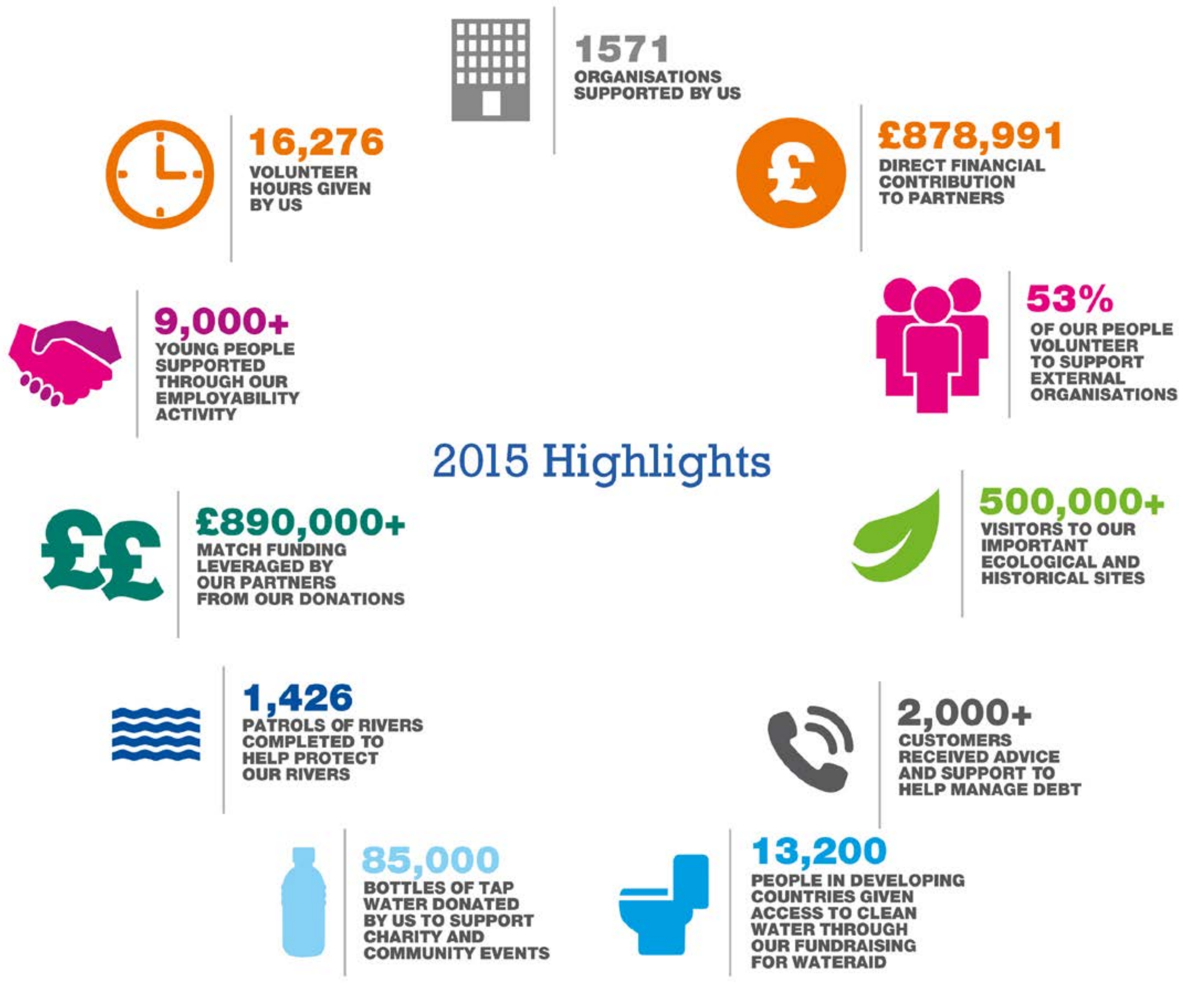
https://www.nwl.co.uk/your-home/community/participation-in-our-communities.aspx

Essex and Suffolk Water

https://www.eswater.co.uk/your-home/participation-in-our-communities.aspx

We are proud of the long history we have of successfully working in partnership with a range of organisations and the help this enables us to give our communities and the local environment, and 2015 was no exception. We continued to ensure that at least 1% of our pre tax profits is re-invested in our communities through dedicating expertise, employee time, money and facilities.

PARTNERSHIP HIGHLIGHTS



Our work in this area has contributed to us being listed in 2015 as one of the world's most ethical companies by Ethisphere. This is the 6th consecutive year we have been listed and we remain the only water and sewerage company in the world to be included on this prestigious list.

We work with partners across sectors at a range of levels; from ensuring we provide first class 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.

Some key examples of our Partnership activity at each of these levels during 2015 is provided on the next page.

FLAGSHIP PARTNERSHIPS:

STEPCHANGE

The national debt charity, StepChange, is one of our flagship partnerships who complement our vision, our purpose and creatively work with us to deliver against our customers' priorities.

We understand that sometimes life's ups and downs mean that some customers may find themselves in a difficult financial situation. To help provide the best possible customer service at all times, we have teamed up with the national debt charity StepChange.

In 2015 more than 2,000 of our customers received advice and support to help manage debt from StepChange. Over the last year we continued our core activity with StepChange:

- Customer teams receiving specialist training from the charity;
- Directly referring customers to StepChange and giving time for the customer to work with StepChange to achieve an action plan and debt solution; and
- Joint communications to customers.

We continued to expand and develop our activity. We worked with StepChange to design our social tariff, which are which we launched in January 2015. The new payment packages are part of our SupportPLUS measures, which we have in place to provide customers with a range of extra help. StepChange provide support, advice and access to these new support packages.

WATER RANGERS

Water Rangers is another of our flagship partnerships. Our Water Rangers scheme is an innovative approach to a very real problem. Having a dedicated team of volunteers who are our eyes on the ground we are able to quickly respond to issues of pollution which benefits the community and the environment by preventing potential pollution incidents. The scheme is a new way for NWL to work in partnership with their communities.

In the Autumn of 2014 we established eight regional teams across the north east of England consisting of volunteers from the general public who patrol, on a weekly basis, 32 public access routes along water courses such as rivers, streams, lakes, beaches and burns. The selected routes cover highly vulnerable areas within the sewage network and the volunteer's role is to observe and report back on the state of the water courses and NWL assets particularly focusing on any potential pollution incidents.

The total number of patrols recorded for the period from December 2014 to December 2015 now stands at 1,426, with 105 issues reported via our customer service Centre of Excellence of which 6 have led to self-reports to the Environment Agency.

Due to the reports received from Water Rangers we are able to act promptly to deal with and prevent potentially serious pollution incidents.

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

All our employees complete a survey each year, which alternates between an external benchmark – the Sunday Times Best Companies survey – and the NWG Employee Survey. In February 2016 employees completed the NWG survey. An independent, specialist organisation runs the survey to ensure confidentiality and to enable us to benchmark response levels and the engagement and satisfaction index results with other organisations. In 2016, 71% of our employees completed the survey giving us good insight into how people feel about working at NWG.

Our Employee survey gives us a good indication of the commitment of our people. 78% of the respondents feel valued by their manager, 84% enjoy their job and 81% believe their colleagues go out of their way to support them. Their talent and inspiration is demonstrated by the recognition of numerous, diverse range external Awards achieved and from the peer nominations for our Viva Awards.

Our people act in line with our values

We have two schemes encouraging individuals to nominate their colleagues when they demonstrate our values. Almost 950 'Viva Thank You' cards were sent in 2015, each one acknowledging appreciation for something someone has done to demonstrate they act in line with our values. Viva (Vision and Values) nominations are submitted by anyone in the business each month to recognise exceptional demonstration of the values, in 2015/16 we have had over 300 nominations. The most extraordinary individuals and teams are invited to an annual Award Ceremony. Our Employee Survey also tells us that 81% of people feel that their colleagues go out of their way to support them; 88% believe they are encouraged to report health & safety issues.

We are seen as a great place to work

Our survey tells us that 84% of our people enjoy their job, 77% of them would recommend working here to others, 74% are proud to work here and 71% believe NWG is a great place to work even though a significant proportion of them were experiencing change which directly impacted them personally.

ANNUAL PERFORMANCE REPORT

Our workplaces are healthy and safe

The health and safety (H&S) of our employees and contractors is an ethical responsibility that we take seriously.

During 2015 we stabilised and maintained the improvement in accident performance achieved in 2014. In the latter part of 2015 the accident incidence rate for lost time accidents, our headline lagging indicator, dropped to below 400 per 100,000 years worked for the first time. This places us within the top quartile of water companies.

We are certified under BS OHSAS 18001 Occupational Health and Safety Systems. We changed certification body in 2015 and our first surveillance assessment under the new arrangement identified few minor non-conformances.

Our 2015 H&S plan of work included the achievement of 43 projects and work streams. One of these was a new approach to safeguarding staff who have to work alone. This project has been shortlisted as a finalist in the Water Industry Achievement Awards 2016 and the Utility Week Star Awards 2016. Other notable projects involved the hazards of radon gas and hand-arm vibration.

We are a company that customers trust

Each year CCWater asks customers for their views about the services they receive from their water and sewerage company and we are proud that for the second year running, that survey has named us as the most trusted water company.

It is important that we have robust governance and assurance arrangements in place to ensure that when we publish information on our performance it is accurate, clear and transparent. In doing so we aim to continue to build trust and confidence with our stakeholders.

Our assurance plan is published in full on our website each year, is based on a well established framework for risk management, and has been developed in line with Ofwat's 'company monitoring framework' (published in June 2015) which describes how it intends to oversee the information water companies provide to customers over the period 2015-20.

This is complemented by companywide accreditation to the following standards which have been in place for a number of years:

- ISO 9001 - a quality management system;
- ISO 14001 - an environmental management system; and
- OHSAS 18001 - an occupational health & safety management system.

In addition our sampling and laboratory analysis are accredited to the demanding ISO 17025 standard and, from 2015, we also have companywide accreditation to ISO 55001 for Asset Management.

ANNUAL PERFORMANCE REPORT

SECTION 4: ADDITIONAL REGULATORY INFORMATION

4A NON-FINANCIAL INFORMATION
FOR THE 12 MONTHS ENDED 31 MARCH 2016

	TOTAL COMPANY 2016		NORTHUMBRIAN WATER 2016		ESSEX & SUFFOLK WATER 2016	
	UNMEASURED	MEASURED	UNMEASURED	MEASURED	UNMEASURED	MEASURED
RETAIL - HOUSEHOLD **NUMBER OF HOUSEHOLDS BILLED ('000)**						
Water only connections	309.7	424.1	6.3	5.4	303.4	418.7
Wastewater only connections	33.8	31.5	33.8	31.5	-	-
Water and wastewater connections	720.5	341.1	720.5	341.1	-	-
Total	**1,064.0**	**796.7**	**760.6**	**378.0**	**303.4**	**418.7**
Number of void households	**80.8**	**47.9**	**46.4**	**17.6**	**34.4**	**30.3**
Per capita consumption (excluding supply pipe leakage) l/h/d			**148.3**	**127.9**	**158.0**	**137.3**

	2016		2016	
	WATER	WASTEWATER	WATER	WASTEWATER
WHOLESALE VOLUME (ML/D)				
Bulk supply export	0.6	-	2.8	-
Bulk supply import	-	-	80.1	-
Distribution input	666.8	-	429.2	-

4B TOTEX ANALYSIS

	CURRENT YEAR	
	WATER	WASTEWATER
	£'m	£'m
ACTUAL TOTEX		
Menu totex	262.8	168.3
ITEMS EXCLUDED FROM THE MENU		
Pension deficit recovery payments	5.6	2.8
Third party costs	13.8	3.7
Other adjustments	-	-
Total costs excluded from the menu	**19.4**	**6.5**
Actual totex	**282.2**	**174.8**
Actual totex base year prices	**266.1**	**164.9**
Allowed totex base year prices	**267.0**	**209.9**

WHOLESALE TOTEX RECONCILIATION TO FD

Our aim is to deliver the business outcomes of our wholesale activities as efficiently as possible, whilst maintaining the health of our assets and supporting excellent customer service. We are confident that we will outperform the wholesale totex allowed in our PR14 Final Determination over the five year price control period, based upon our implementation of a new operating model for efficient delivery of our capital investment programme and our ongoing focus on our opex efficiency programme.

Wholesale water totex was marginally lower than the allowed totex, by £0.9m. This reflected the benefit of efficient delivery of the capital programme, offset by higher than planned opex in the year as a result of dry weather in our NW region requiring us to carry out more transfers of water resources and utilise more energy intensive treatment works.

Wholesale wastewater was £45m lower than the allowed totex, again reflecting the capex delivery but also the benefit of renewable energy generation, including biomethane injection.

ANNUAL PERFORMANCE REPORT

4C FORECAST IMPACT OF PERFORMANCE ON RCV

	2016
	£'m
RCV determined at FD	3,869.7
RCV element of Totex over/(under)spend	(22.7)
Allowance (Rewards/penalties - ODI)	4.5
Projected 'shadow' RCV	**3,851.5**

ANNUAL PERFORMANCE REPORT

4D TOTEX ANALYSIS: WHOLESALE WATER
FOR THE 12 MONTHS ENDED 31 MARCH 2016

	WATER RESOURCES		RAW WATER DISTRIBUTION				
	ABSTRACTION LICENCES	RAW WATER ABSTRACTION	RAW WATER TRANSPORT	RAW WATER STORAGE	WATER TREATMENT	TREATED WATER DISTRIBUTION	TOTAL
	£'m	£'m	£'m	£'m	£'m	£'m	£'m
OPERATING EXPENDITURE							
Power	-	5.7	1.9	-	2.0	10.7	20.3
Income treated as negative expenditure	-	-	-	-	(0.2)	-	(0.2)
Service charges/ discharge consents	21.8	0.1	-	-	0.1	-	22.0
Bulk supply/ Bulk discharge	-	2.7	-	-	-	-	2.7
Other operating expenditure	-	11.8	0.7	0.1	25.6	44.6	82.8
Local authority rates	-	3.2	2.2	-	3.0	14.7	23.1
Total operating expenditure excluding third party services	**21.8**	**23.5**	**4.8**	**0.1**	**30.5**	**70.0**	**150.7**
Third party services	8.4	-	3.2	-	0.4	1.8	13.8
Total operating expenditure	**30.2**	**23.5**	**8.0**	**0.1**	**30.9**	**71.8**	**164.5**
CAPITAL EXPENDITURE							
Maintaining the long term capability of the assets - infra	-	0.9	0.2	-	-	23.5	24.6
Maintaining the long term capability of the assets - non-infra	-	9.4	0.1	-	37.9	14.4	61.8
Other capital expenditure - infra	-	0.9	-	-	-	15.6	16.5
Other capital expenditure - non-infra	-	1.0	-	-	1.9	0.9	3.8
Total gross capital expenditure excluding third party services	**-**	**12.2**	**0.3**	**-**	**39.8**	**54.4**	**106.7**
Third party services	-	-	-	-	-	-	-
Total gross capital expenditure	**-**	**12.2**	**0.3**	**-**	**39.8**	**54.4**	**106.7**
Grants and contributions (price control)	-	-	-	-	-	(11.7)	(11.7)
Totex	**30.2**	**35.7**	**8.3**	**0.1**	**70.7**	**114.5**	**259.5**

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CONTINUED 4D TOTEX ANALYSIS: WHOLESALE WATER FOR THE 12 MONTHS ENDED 31 MARCH 2016

	WATER RESOURCES		RAW WATER DISTRIBUTION				
	ABSTRACTION LICENCES	RAW WATER ABSTRACTION	RAW WATER TRANSPORT	RAW WATER STORAGE	WATER TREATMENT	TREATED WATER DISTRIBUTION	TOTAL
CASH EXPENDITURE							
Pension deficit recovery payments	-	0.7	-	-	1.6	3.3	5.6
Other cash items	-	2.1	0.1	-	4.8	10.1	17.1
Totex including cash items	**30.2**	**38.5**	**8.4**	**0.1**	**77.1**	**127.9**	**282.2**

	LICENCED VOLUME AVAILABLE	VOLUME ABSTRACTED	VOLUME TRANSPORTED	AVERAGE VOLUME STORED	DISTRIBUTION INPUT FROM WATER TREATMENT	DISTRIBUTION INPUT TREATED WATER
UNIT COST INFORMATION (OPERATING EXPENDITURE)						
Volume (Ml)	**751,277**	**438,076**	**285,194**	**53,099**	**400,040**	**400,040**
Unit cost (£/Ml)	**40.3**	**53.7**	**27.8**	**1.8**	**77.2**	**179.6**

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4E TOTEX ANALYSIS: WHOLESALE WASTEWATER FOR THE 12 MONTHS ENDED 31 MARCH 2016

	SEWAGE COLLECTION			SEWAGE TREATMENT		SLUDGE			
	FOUL	SURFACE WATER DRAINAGE	HIGHWAY DRAINAGE	SEWAGE TREATMENT AND DISPOSAL	IMPORTED SLUDGE LIQUOR TREATMENT	SLUDGE TRANSPORT	SLUDGE TREATMENT	SLUDGE DISPOSAL	TOTAL
	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
OPERATING EXPENDITURE									
Power	5.3	-	-	8.7	1.1	-	(0.6)	-	14.5
Income treated as negative expenditure	-	-	-	-	-	-	(4.0)	-	(4.0)
Service charges/ discharge consents	1.1	-	-	1.4	-	-	-	-	2.5
Bulk supply/ Bulk discharge	-	-	-	-	-	-	-	-	-
Other operating expenditure	1.7	13.8	7.6	17.0	0.7	5.8	8.8	1.1	56.5
Local authority rates	0.2	-	-	5.2	-	-	1.0	-	6.4
Total operating expenditure excluding third party services	**8.3**	**13.8**	**7.6**	**32.3**	**1.8**	**5.8**	**5.2**	**1.1**	**75.9**
Third party services	0.3	0.3	-	3.1	-	-	-	-	3.7
Total operating expenditure	**8.6**	**14.1**	**7.6**	**35.4**	**1.8**	**5.8**	**5.2**	**1.1**	**79.6**
CAPITAL EXPENDITURE									
Maintaining the long term capability of the assets - infra	5.1	8.5	4.5	-	-	-	-	-	18.1
Maintaining the long term capability of the assets - non-infra	2.1	3.4	1.9	22.7	1.0	0.3	3.3	0.1	34.8
Other capital expenditure - infra	7.0	11.7	6.3	-	-	-	-	-	25.0
Other capital expenditure - non-infra	0.7	1.1	0.6	7.8	0.4	-	-	-	10.6
Total gross capital expenditure excluding third party services	**14.9**	**24.7**	**13.3**	**30.5**	**1.4**	**0.3**	**3.3**	**0.1**	**88.5**
Third party services	-	-	-	-	-	-	-	-	-
Total gross capital expenditure	**14.9**	**24.7**	**13.3**	**30.5**	**1.4**	**0.3**	**3.3**	**0.1**	**88.5**
Grants and contributions (price control)	(1.4)	(2.2)	(1.2)	-	-		-	-	(4.8)
Totex	**22.1**	**36.6**	**19.7**	**65.9**	**3.2**	**6.1**	**8.5**	**1.2**	**163.3**

Table continued overleaf

CONTINUED 4E TOTEX ANALYSIS: WHOLESALE WASTEWATER FOR THE 12 MONTHS ENDED 31 MARCH 2016

	SEWAGE COLLECTION			SEWAGE TREATMENT		SLUDGE			
	FOUL	SURFACE WATER DRAINAGE	HIGHWAY DRAINAGE	SEWAGE TREATMENT AND DISPOSAL	IMPORTED SLUDGE LIQUOR TREATMENT	SLUDGE TRANSPORT	SLUDGE TREATMENT	SLUDGE DISPOSAL	TOTAL
	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
CASH EXPENDITURE									
Pension deficit recovery payments	1.0	0.2	-	1.3	-	-	0.3	-	2.8
Other cash items	3.2	0.5	-	4.1	-	0.1	0.8	-	8.7
Totex including cash items	**26.3**	**37.3**	**19.7**	**71.3**	**3.2**	**6.2**	**9.6**	**1.2**	**174.8**

	VOLUME COLLECTED FOUL	VOLUME COLLECTED SURFACE WATER DRAINAGE	VOLUME COLLECTED HIGHWAY DRAINAGE	BIOCHEMICAL OXYGEN DEMAND (BOD) SEWAGE	BIOCHEMICAL OXYGEN DEMAND (BOD) IMPORTED SLUDGE LIQUOR	SLUDGE VOLUME TRANSPORTED	SLUDGE TREATMENT DRIED SOLID MASS TREATED	SLUDGE DISPOSAL DRIED SOLID MASS DISPOSED
	Ml	Ml	Ml	Tonnes	Tonnes	M^3	ttds	ttds
UNIT COST INFORMATION (OPERATING EXPENDITURE)								
Volume	177,094	79,583	42,852	68,381	3,867	776,610	68,175	27,304
£/unit	**48.2**	**177.8**	**177.8**	**517.3**	**460.6**	**7.5**	**76.5**	**40.7**

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4F OPERATING COST ANALYSIS: HOUSEHOLD RETAIL FOR THE YEAR ENDED 31 MARCH 2016

	HOUSEHOLD UNMEASURED				HOUSEHOLD MEASURED				
	WATER ONLY	WASTEWATER ONLY	WATER AND WASTEWATER	TOTAL	WATER ONLY	WASTEWATER ONLY	WATER AND WASTEWATER	TOTAL	TOTAL
	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
OPERATING EXPENDITURE									
Customer services	1.3	0.2	3.0	4.5	4.4	0.3	3.5	8.2	12.7
Debt management	0.4	0.1	1.0	1.5	1.7	0.2	1.3	3.2	4.7
Doubtful debts	3.4	-	12.3	15.7	2.7	-	2.2	4.9	20.6
Meter reading	-	-	-	-	1.2	0.1	0.9	2.2	2.2
Other operating expenditure	0.1	-	0.3	0.4	0.3	-	0.3	0.6	1.0
Total operating expenditure excluding third party services	**5.2**	**0.3**	**16.6**	**22.1**	**10.3**	**0.6**	**8.2**	**19.1**	**41.2**
Depreciation	0.5	0.1	1.0	1.6	0.7	-	0.5	1.2	2.8
Total operating costs excluding third party services	**5.7**	**0.4**	**17.6**	**23.7**	**11.0**	**0.6**	**8.7**	**20.3**	**44.0**

OTHER OPERATING EXPENDITURE INCLUDES THE NET RETAIL EXPENDITURE FOR THE FOLLOWING RETAIL ACTIVITIES WHICH ARE PART FUNDED BY WHOLESALE:

	TOTAL
	£'m
Demand-side water efficiency - gross expenditure	1.6
Demand-side water efficiency - expenditure funded by wholesale	(1.6)
Demand-side water efficiency - net retail expenditure	**-**
Customer-side leak repairs - gross expenditure	2.5
Customer-side leak repairs - expenditure funded by wholesale	(2.5)
Customer-side leak repairs - net retail expenditure	**-**

4G WHOLESALE CURRENT COST FINANCIAL PERFORMANCE FOR THE 12 MONTHS ENDED 31 MARCH 2016

	WATER	WASTEWATER	TOTAL
	£'m	£'m	£'m
Revenue	413.1	292.0	705.1
Operating expenditure	(164.5)	(79.6)	(244.1)
Capital maintenance charges	(122.4)	(92.7)	(215.1)
Other operating income	0.5	(0.2)	0.3
Current cost operating profit	**126.7**	**119.5**	**246.2**
Other income	0.1	0.1	0.2
Interest income	0.2	0.1	0.3
Interest expense	(59.7)	(58.5)	(118.2)
Interest expense related to the unwinding of discounted liabilities	(1.4)	(0.7)	(2.1)
Profit before tax and fair value movements	**65.9**	**60.5**	**126.4**
Fair value losses on financial instruments	(0.7)	(0.7)	(1.4)
Profit before tax	**65.2**	**59.8**	**125.0**

4H FINANCIAL METRICS FOR THE 12 MONTHS ENDED 31 MARCH 2016

	UNITS	METRIC
Net debt	£m	2,690.8
Regulated equity	£m	1,178.9
Regulated gearing	%	69.5%
Post tax return on regulated equity	%	18.0%
RORE (return on regulated equity)	%	6.6%
Dividend yield	%	17.0%

Table continued overleaf

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	UNITS	METRIC
Retail profit margin - Household	%	2.7%
Retail profit margin - Non household	%	1.3%
Credit rating	n/a	BBB+/Baa1
Return on RCV	%	8.7%
Dividend cover	n/a	1.2
Funds from operations (FFO)	£m	357.3
Interest cover (cash)	n/a	4.3
Adjusted interest cover (cash)	n/a	2.7
FFO/Debt	n/a	0.1
Effective tax rate	%	12.6%
Free cash flow (RCF)	£m	157.3
RCF/capex	n/a	0.8
Revenue (actual)	£m	762.7
EBITDA (actual)	£m	481.2
Proportion of borrowings which are fixed rate	%	61.7%
Proportion of borrowings which are floating rate	%	8.4%
Proportion of borrowings which are index linked	%	29.9%
Proportion of borrowings due within 1 year or less	%	6.5%
Proportion of borrowings due in more than 1 year but no more than 2 years	%	14.9%
Proportion of borrowings due in more than 2 years but no more than 5 years	%	4.2%
Proportion of borrowings due in more than 5 years but no more than 20 years	%	40.5%
Proportion of borrowings due in more than 20 years	%	33.9%

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4I FINANCIAL DERIVATIVES
FOR THE 12 MONTHS ENDED 31 MARCH 2016

	NOMINAL VALUE BY MATURITY (NET)			TOTAL VALUE			INTEREST RATE (WEIGHTED AVERAGE)	
DERIVATIVE TYPE:	1 TO 2 YEARS	2 TO 5 YEARS	OVER 5 YEARS	NOMINAL VALUE (NET)	MARK TO MARKET	TOTAL ACCRETION	PAYABLE	RECEIVABLE
	£'m	£'m	£'m	£'m	£'m	£'m	%	%
INTEREST RATE SWAP (STERLING)								
Floating to/from fixed rate	10.0	40.0	160.0	210.0	(16.3)	-	3.05%	0.98%
Fixed to/from index-linked	-	-	150.0	150.0	(0.5)	0.6	RPI-0.42%	0.00%
Total	**10.0**	**40.0**	**310.0**	**360.0**	**(16.8)**	**0.6**		
FORWARD CURRENCY CONTRACTS								
Forward currency contracts USD	3.2	2.6	-	5.8	0.1	-	0.00%	0.00%
Total	**3.2**	**2.6**	**-**	**5.8**	**0.1**	**-**		
Total	**13.2**	**42.6**	**310.0**	**365.8**	**(16.7)**	**0.6**		

The total mark to market value of financial derivatives in the table above, a net liability of £16.7m, is different to the value of financial instruments reported in table 1C, the statement of financial position, of a liability of £31.3m. The difference relates to the value of forward power and fuel contracts (£14.5m liability), which are reported in the statement of financial position but not in the table above, and the mark to market value of forward currency contracts (£0.1m asset), which is not recognised in the statement of financial position on the basis that it is not material in value.

Northumbrian Water Limited
Northumbria House
Abbey Road
Pity Me
Durham
DH1 5FG

www.nwl.co.uk | www.eswater.co.uk | www.welivewater.co.uk