United Utilities Group PLC

Annual Report and Financial Statements for the year ended 31 March 2019

United Utilities
helping life flow smoothly

Cover photo:
The cycle of our water and wastewater services, much of which are designed to use gravity to move the water naturally in the most efficient way

Contents

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Look out for

Read more content within our Annual Report

You can read more in our online Annual Report at **unitedutilities.com/corporate** where we maintain a wide range of information of interest to institutional and private investors including:

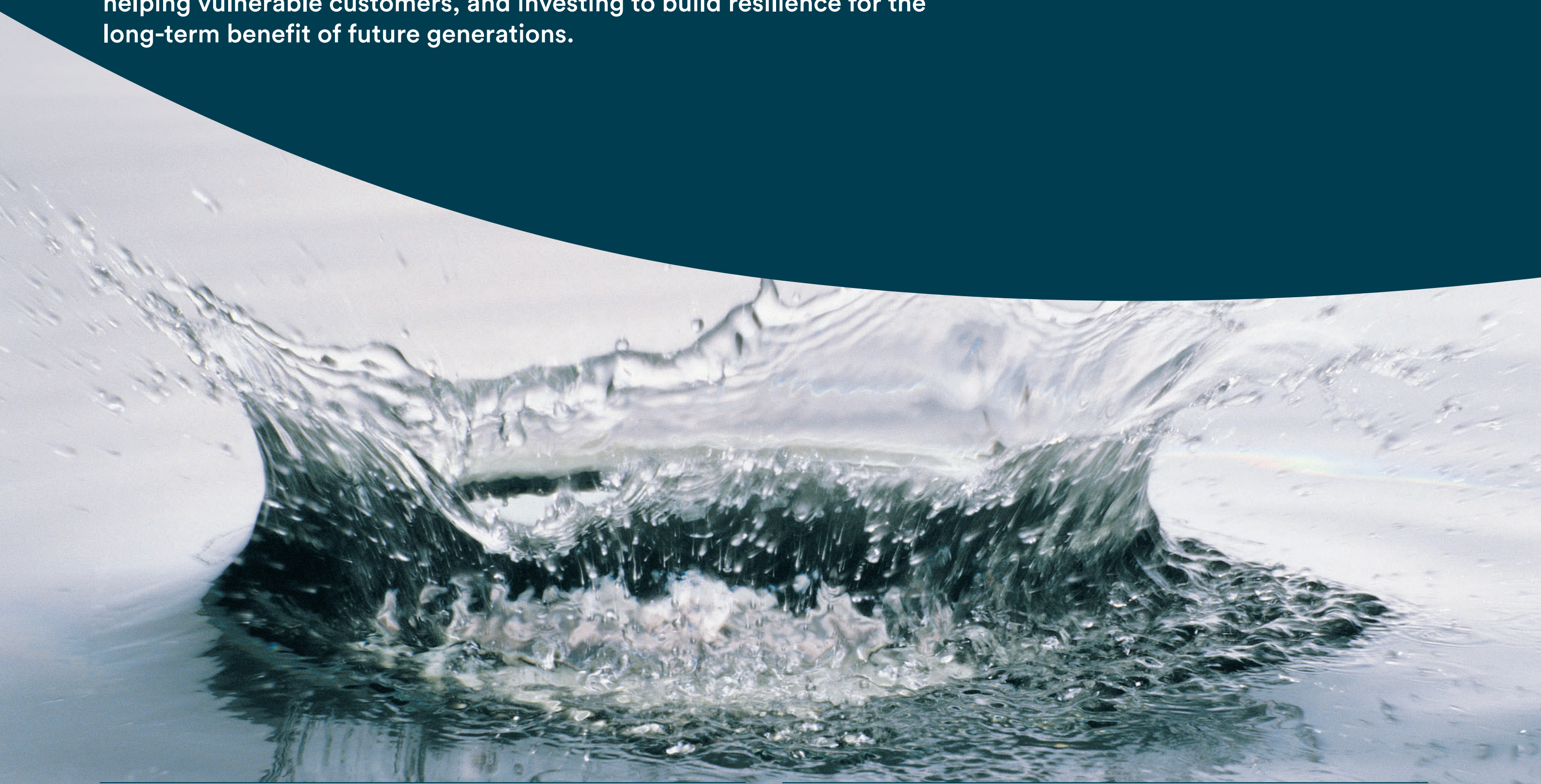
- Latest news and press releases;
- Reports and publications; and
- Corporate responsibility content.

Welcome to our Annual Report and Financial Statements for the year ended 31 March 2019

United Utilities is the UK's largest listed water and wastewater company. Our purpose is to provide great service to customers and communities in the North West, creating long-term value for all of our stakeholders.

We provide essential services that are relied on by millions of people every day, and our embedded innovation culture and pioneering Systems Thinking approach help us create value for a range of stakeholders.

We continually strive to improve our services, delivering more for less, helping vulnerable customers, and investing to build resilience for the long-term benefit of future generations.



Materiality

Our Annual Report and Financial Statements aim to meet the information needs of our investors to help them make informed decisions regarding their participation – for example, whether to buy, sell or hold our shares or bonds, whether to engage with management on issues, and how to vote their shares. We have included information that we believe is material to these decisions, which is presented in a way that we believe is fair, balanced and understandable.

We engage with – and recognise that this report will be read by – a wide variety of other stakeholders including customers, suppliers, employees, analysts, regulators, community bodies, politicians, non-governmental organisations, and devolved authorities. Where we believe that a topic is material to a large number of them, which is assessed in part through a matrix approach to stakeholder materiality as set out on page 45, we either include it in this report or refer the reader to other reports and information (such as our regulatory reports, customer communications, or corporate responsibility web pages).

We believe this approach meets the requirements of company law, the UK Corporate Governance Code, IFRS and the International <IR> Framework, and that we go beyond those requirements where we feel it is particularly helpful to do so and where that can be done without making the report unnecessarily lengthy or difficult to read.

Integrated Report

This Annual Report is an Integrated Report and has been prepared and presented in accordance with the International <IR> Framework published by the International Integrated Reporting Council in December 2013. The board, which is responsible for the integrity of this report, has considered the preparation and presentation of this report and concluded that it has been prepared and presented in accordance with the Framework.

Dr John McAdam
Chairman

Steve Mogford
Chief Executive Officer

United Utilities
helping life flow smoothly

We have submitted our business plan for the 2020–25 regulatory period

We received the highest grades in the sector against the test areas in Ofwat's initial assessment of plans, and were one of only three companies to be awarded a fast-track rating.

We see this achievement as recognition of the quality of our plan and of the transformation we have made as a business, which has been delivered through a consistent customer-focused approach and a drive for continuous improvement.

We were the only company to retain self-assurance status in Ofwat's Company Monitoring Framework assessment. We have now held this top rating for three years in a row, recognising the consistently high level of trust and confidence that stakeholders can place in the quality and transparency of our reporting.

What to look for in this Annual Report

Consistent approach

We maintain a consistent and sustainable approach that provides a strong foundation stakeholders can rely on.

Page 15
Our purpose and strategy

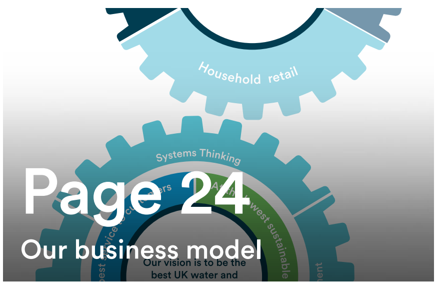
Look out for our strategic themes throughout this report:

- The best service to customers
- At the lowest sustainable cost
- In a responsible manner

Our strategy is broken down into these three themes, which form the framework through which we create value for our stakeholders.

These strategic themes are embedded throughout this report. Our performance measurement, risk assessment and remuneration policy are all aligned to them, often to more than one of the three themes, such is the interconnectivity of what we do.

Page 17
Our competitive advantages



Page 24
Our business model

Continuous improvement

We strive for continuous improvement in our performance and in our reporting.

Page 19
Our business plan submission for 2020–25

Page 39
How we create value for stakeholders

Page 152
Our s172(1) statement

Proud to be leading the industry across a host of measures

Most embedded
innovation culture

Fast-tracked
business plan with highest overall grades

Sector-leading
approach to affordability and vulnerability

...all while maintaining **sector-**

Read more about our business plan on pages 19 to 23

Read more about our operational performance on pages 56 to 61

Sector-leading rating with the Environment Agency

Highest levels of trust and confidence in our reporting

High quality approach to customer engagement

leading resilience all year round

Chairman and Chief Executive Officer's review

Our consistent focus on customers and pioneering Systems Thinking approach have helped us go from strength to strength.

Pictured: Dr John McAdam, Chairman and Steve Mogford, Chief Executive Officer

Overview

This has been a busy year. Extreme weather caused operational challenges for the sector as a whole, and we submitted our business plan for the next regulatory period. Throughout these competing priorities, we maintained a resilient and high-quality service and grew stronger as a company.

We made further improvements in customer satisfaction and delivered our best performance to date against our outcome delivery incentives, despite our targets being tougher this year. We met our leakage target for the 13th consecutive year, and we maintained high standards of environmental performance and drinking water quality.

Our 2020–25 business plan submission received the highest grades in the sector and a fast-track rating in Ofwat's initial assessment.

These achievements are a testament to the transformation we have delivered over recent years and the hard work of all our team.

Continuing to improve service for customers

Our purpose and strategy are centred around customers. This has been our focus for many years and underpins customer satisfaction improvements year after year.

We achieved our best ever Service Incentive Mechanism (SIM) scores this year, and our performance across the first four years of this regulatory period means we expect to be eligible for a financial reward of around £16 million.

Proving that good service costs less, we have reduced the amount it costs to serve our customers by 27 per cent since the start of this regulatory period, as a result of our improved operational performance, digital strategy, and driving down bad debt.

Our household bad debt has reduced from 3.6 per cent of regulated revenue in 2014/15 to 2.1 per cent in 2018/19, and customer bills have reduced in real terms since 2010.

We have taken the lead in transforming how the sector supports customers, particularly those in vulnerable circumstances. We have the sector's most innovative and ambitious assistance schemes, supporting over 100,000 customers struggling to pay. We held the second North West Affordability Summit this year, launching the North West Hardship Hub, the first of its kind in the country. This platform helps the money advice community in our region locate cross-sector assistance schemes all in one place, making it easier for them to find the best help for their clients.

Read more about how we are **working together to support those in need** on page 57

Our efforts are being recognised externally. We were awarded the Institute of Customer Service 'Service Mark with Distinction'. We were the first water company accredited by the Chartered Institute of Credit Management for our work with customers struggling to pay; and we achieved Shaw Trust Accessibility status as a further recognition of our work supporting customers in vulnerable circumstances.

Rising to challenges and improving our resilience

2018 was a year of unprecedented extremes of weather, with a deep freeze and rapid thaw in the early part of the calendar year swiftly followed by an intense heatwave in the summer. It was the driest summer for our region since modern records began in 1961, meaning our impounding reservoirs were at much lower levels than usual. The soaring temperatures contributed to a huge increase in demand for water.

We undertook a series of actions to minimise any impact on customers and protect water resources. We increased communication to encourage customers to use water wisely. We significantly increased our leak detection efforts to help manage leakage. We used our fleet of Alternative Supply Vehicles (ASVs) to help maintain pressure in the network at peak times. We brought back into service groundwater supplies such as boreholes that had not been used for many years, and we used our West East Link Main to pump water around our region.

Read more about how we are **responding to extreme weather conditions** on page 30

The tireless hard work of our employees, together with the support of customers and regulators over this period, meant we were able to maintain an unrestricted service to customers. Our ability to manage these extreme conditions further demonstrates the benefits of our Systems Thinking approach. Many of the actions we took to protect service to customers would not have been possible without it.

Our actions resulted in one-off additional costs of around £80 million, which has further improved the high level of resilience we have already embedded into our service. For example, our investment in ASVs has been critical to improving our water service, an efficient way of helping to keep customers supplied during planned and unplanned interruptions.

Delivering strong and sustainable financial performance

Our financial performance from a statutory perspective has been very good this year.

Underlying earnings per share is 55.5 pence, an increase of 24 per cent and more than covering the dividend for the year. The main drivers of this increase are our allowed regulatory revenue profile and a decrease in the underlying net finance expense due to lower RPI inflation applied to our index-linked debt, partly offset by increases in infrastructure renewals expenditure and depreciation.

Reported earnings per share is 53.3 pence, which is slightly lower than the underlying figure, mainly due to exceptional costs associated with the dry weather period and fair value movements. Adjusting items are outlined in the reconciliation table on pages 66 and 67. The £80 million additional dry weather costs include £25.6 million operating costs and £10.5 million infrastructure renewals expenditure, with the remainder being capital expenditure.

Read more about **our financial performance for 2018/19** on pages 62 to 67

The board has proposed a final dividend of 27.52 pence per ordinary share, taking the total dividend for 2018/19 to 41.28 pence. This is an increase of 3.9 per cent, in line with our policy for this regulatory period of targeting an annual growth rate of at least RPI inflation through to 2020.

We have had a pension surplus on an IAS 19 basis for many years and this is well controlled through our asset-liability matching approach. The IAS 19 surplus increased to £484 million at 31 March 2019.

The funding position is assessed using a different basis to value liabilities. While maintaining a pension surplus on an IAS 19 basis, we have had a deficit on a funding basis, and have been making deficit recovery contributions of around £40 million per year. It was confirmed in the most recent triennial valuation, signed off as at 31 March 2018, that these contributions would address the funding deficit by December 2021. However, in April 2019, we prepaid the remaining agreed deficit recovery contributions at a discount, meaning we are now in a pension surplus position on an IAS 19 basis and have eliminated the deficit on a funding basis, achieving self-sufficiency.

This is a responsible approach, mitigating risk for all of our stakeholders at a time when regulators, including Ofwat and The Pensions Regulator, are highlighting the importance of this area and in some cases, intervening to protect pension scheme members and customers.

As part of our business plan submission for the next regulatory period, we have set out a range of considerations that will determine the future level of dividends paid. One of these is the impact of pension deficits. With our historic well managed approach to pensions and strong level of funding, we do not expect future funding of our pension scheme to act as a constraint in the 2020–25 period.

We have a consistent policy of targeting gearing of 55–65 per cent, measured as net debt to regulatory capital value. This has been supportive of United Utilities Water Limited's A3 credit rating with Moody's, which affirmed a stable outlook on our credit rating following Ofwat's initial assessment of business plans, despite retaining a negative outlook on the sector in general.

This, alongside our pension position, gives us an extremely robust capital base and provides a high degree of resilience and financial flexibility as we look to the future.

Performing well against our regulatory contract

From an economic perspective, there are four key drivers of value – total expenditure (totex), SIM performance, outcome delivery incentives (ODIs), and financing. We are delivering good results against all of these areas, demonstrating strong all-round performance in the current regulatory period.

As previously mentioned, we anticipate being eligible for a SIM reward of around £16 million thanks to our improved performance for customers.

On financing, the low cost of debt we have locked-in places us in a strong position to outperform the industry allowed cost of debt in the current regulatory period, and into the next period.

On totex, we remain confident in outperforming our totex allowance by £100 million against the scope of our 2015–20 final determination.

Sitting outside the scope of the final determination is an additional £350 million we have committed to invest from our total outperformance, including £250 million in resilience that we had committed to previously and £100 million to give us a flying start for the next regulatory period, and the £80 million additional totex related to the dry weather event.

KEY FACTS

£350 million
additional investment of outperformance

£19 million
ODI reward for 2018/19 against tougher targets

£16 million
expected SIM reward for the 2015–20 period

Fast-track
business plan for 2020–25

Top rating
for the high quality and transparency of our reporting

Chairman and Chief Executive Officer's review

Although our ODI reward-penalty range was skewed to the downside, we expect to earn a net reward of around £30 million for the 2015–20 period. This year's performance was our best so far, with a net reward of £19.2 million bringing our cumulative position for the first four years of the period to a net reward of £21.4 million.

This performance, across the range of our ODIs, demonstrates the benefit of the accelerated investment we made early in the period. It is particularly pleasing given we were delivering against increasingly challenging targets and dealing with extremes of weather. Our expected out-turn position equates to performance towards the top end of our estimates, providing a solid foundation for the next regulatory period.

Achieving a fast-track rating for our business plan

Our business plan submission for the 2020–25 period received the highest grades for the sector against the test areas set out in Ofwat's initial assessment, and was commended as industry leading in many areas.

This achievement demonstrates the transformation we have achieved in recent years, both in terms of operational performance and efficiency, as well as the high quality of our plan and our ambition for further improvement in the next regulatory period.

Read more about **our business plan submission for 2020–25** on pages 19 to 23

As previously mentioned, we have committed an additional £100 million investment towards a flying start to the 2020–25 period. The main priorities for this investment include three of our toughest performance targets: leakage, supply interruptions and sewer flooding.

Supporting employees' health and wellbeing

We are committed to protecting the health and wellbeing of our employees, and have made significant efforts in this area over recent years.

We engage with employees to help them with lifestyle choices. For example, we help them to quit smoking and offer incentives for those who stay smoke-free for six months. We have reduced employee inactivity rates through initiatives such as standing desks and walking meetings, as well as offering discounted gym memberships and an onsite gym at our head office. We offer nutritional programmes and have health kiosks where employees can measure their weight and blood pressure.

As well as physical health, we focus on mental health. We offer free confidential support services for employees, and have trained mental health champions and first aiders across the business. We joined other businesses in the year in an initiative aimed at ending the stigma of talking about mental health in the workplace.

Our progress in this area has been recognised externally. We were named one of Britain's Healthiest Workplaces 2018 and the third most improved organisation; we were reaccredited with the Workplace Wellbeing Charter in 2018; and we received two employee wellbeing accolades at the Reward and Employee Benefits Association (REBA) awards for physical wellbeing and mental wellbeing.

Read more about how we are **creating a healthy workplace** on page 33

Maintaining high standards of corporate governance

We consistently operate in a manner that aims to deliver the highest levels of corporate governance. Our board continues to provide sound and prudent governance, consistent with the principles of the UK Corporate Governance Code.

We continued to demonstrate good drinking water quality compliance, as assessed by the Drinking Water Inspectorate. We have delivered a range of improvements in our water transformation programme, which has driven a significant reduction in the risk of water quality events. We once again retained Industry


Pictured: Manchester skyline

Leading Company status in the Environment Agency's annual assessment, and we achieved a World Class rating in the Dow Jones Sustainability Index for the eleventh consecutive year.

Ofwat's Company Monitoring Framework Assessment provides an assessment of the trust and confidence stakeholders can have in the accuracy, completeness and transparency of company reporting. Integrity is one of our core values and we were delighted to be awarded the top self-assurance rating again this year, the only company to have held this for three consecutive years.

Outlook

The acceleration of investment we made in the current regulatory period, along with our additional investment, Systems Thinking approach and financial risk management, are delivering sustainable improvements in performance and resilience. Our customer satisfaction is among the top of the water and wastewater companies in the sector.

The benefit of accelerated investment to deliver earlier improvements to service is clear to see. Given our total anticipated outperformance for the 2015–20 regulatory period, we are reinvesting £350 million of our outperformance to deliver enhanced resilience and improved performance earlier in the next regulatory period.

We are proud of the transformation we have delivered and the performance of our team during the year. We are excited about the opportunity the 2020–25 period represents as we deliver our purpose to provide great service to customers and communities in the North West, creating long-term value for all of our stakeholders.

We would like to express our gratitude to our employees for their hard work and dedication, and to customers and other stakeholders for their continued support.

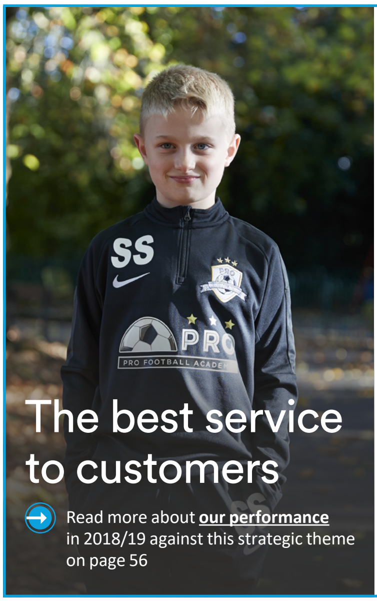
Dr John McAdam
Chairman

Steve Mogford
Chief Executive Officer

The strategic report on pages 10 to 77 was approved at a meeting of the board on 22 May 2019 and signed off on its behalf by Steve Mogford, Chief Executive Officer.

2018/19 highlights
Operational highlights

We have delivered another strong performance against a more challenging backdrop



The best service to customers

Read more about **our performance** in 2018/19 against this strategic theme on page 56

Year-on-year improvements in customer satisfaction and lower bills

- Our pioneering Systems Thinking approach has delivered sustained year-on-year improvements in service for customers
- We achieved our best ever Service Incentive Mechanism (SIM) scores, ranking us among the best water and wastewater companies, and we anticipate being eligible for a SIM reward of around £16 million for the 2015–20 regulatory period
- We have delivered these improvements at lower cost, with a 27 per cent reduction in cost to serve, and customer bills have reduced in real terms since 2010

Transforming how the sector supports vulnerable customers

- We have the sector's most innovative and ambitious assistance schemes supporting over 100,000 customers struggling to pay
- We launched the North West Hardship Hub, a one-stop-shop platform to help the money advice community easily locate the best cross-sector assistance schemes for vulnerable people

At the lowest sustainable cost

Read more about **our performance** in 2018/19 against this strategic theme on page 58

Best performance on outcome delivery incentives against a tougher backdrop

- We have achieved our best performance yet on our outcome delivery incentives (ODIs) against a backdrop of increasingly challenging targets and periods of extreme weather
- We earned a net ODI reward of £19.2 million for the year, and we now expect a cumulative ODI reward for the 2015–20 period of around £30 million, at the top end of our previously indicated range

Made strides in operational efficiency

- Our business plan for 2020–25 was assessed as among the most efficient in Ofwat's Initial Assessment of Plans versus its own view of efficient costs, helping us attain a fast-track rating
- We are on track to deliver £100 million in total expenditure (totex) outperformance against the scope of our 2015–20 final determination, and secure a run rate that supports our business plan submission for base totex as we transition into the next regulatory period

In a responsible manner

Read more about **our performance** in 2018/19 against this strategic theme on page 60

Sector-leading approach delivers all-round resilience

- We have met our leakage target for 13 consecutive years
- We are investing £250 million of our outperformance in the current regulatory period to improve resilience further, and have committed to invest an additional £100 million to get a fast start for the next regulatory period
- We have a stable pension surplus on an IAS 19 basis, and in April 2019 we eliminated our funding deficit and achieved self-sufficiency by prepaying the remaining agreed contributions
- Our robust capital structure and relatively low gearing provide long-term financial resilience and future financial flexibility

Consistently trusted reporting

- We have been awarded the top self-assurance status for three years in a row in Ofwat's Company Monitoring Framework assessment, demonstrating that stakeholders can place the highest levels of trust and confidence in the accuracy and completeness of our reporting

2018/19 highlights
Financial highlights

Tight cost control helped us deliver a strong result and we maintain sector-leading financial resilience

Revenue

2018/19	**£1,819m**
2017/18	£1,736m
2016/17	£1,704m
2015/16	£1,730m
2014/15	£1,720m

Revenue of £1,819 million increased by £83 million, largely reflecting the allowed regulatory revenue profile in our final determination for this financial year

Underlying operating profit*

2018/19	**£684.8m**
2017/18	£645.1m
2016/17	£622.9m
2015/16	£604.1m
2014/15	£664.3m

Underlying operating profit of £685 million increased by £40 million, mainly due to the revenue increase partly offset by increases in infrastructure renewals expenditure and depreciation for the year

Reported operating profit*

2018/19	**£634.9m**
2017/18	£636.4m
2016/17	£605.5m
2015/16	£567.9m
2014/15	£653.3m

Reported operating profit of £635 million decreased by £1 million, mainly as a result of the increase in underlying operating profit offset by exceptional one-off costs associated with the extreme dry weather in the summer of 2018

Total dividend per share

2018/19	**41.28p**
2017/18	39.73p
2016/17	38.87p
2015/16	38.45p
2014/15	37.70p

Total dividend per ordinary share of 41.28 pence increased by 3.9 per cent in line with our policy of targeting an annual growth rate of at least RPI inflation through to 2020

Read more about **our financial performance** on pages 62 to 65

* A guide to alternative performance measures and a reconciliation between underlying operating profit and reported operating profit is shown on pages 66 and 67.

Strategic report

The strategic report details our performance over the past year and how it has been achieved in line with our business model and strategy.

Our reservoir at Ennerdale Water - photograph taken by our water services network colleague Ian Greenwood

What we do

Our wholesale water team maintains reservoirs and water treatment works across the region and thousands of kilometres of water pipes in order to collect, treat, store and deliver billions of litres of reliable, clean drinking water to millions of customers 24 hours a day.

Our wholesale wastewater team maintains hundreds of treatment works and thousands of kilometres of wastewater pipes in order to collect wastewater from homes, businesses and surface water run-off, transport and treat it, and return treated water to protect our natural environment.

Our household retail team deals with new connections, metering and billing for millions of customers as well as helping vulnerable customers with our Priority Services and other assistance schemes.

CLEANING AND RETURNING WASTEWATER

569
wastewater treatment works

7,000
kilometres of rivers

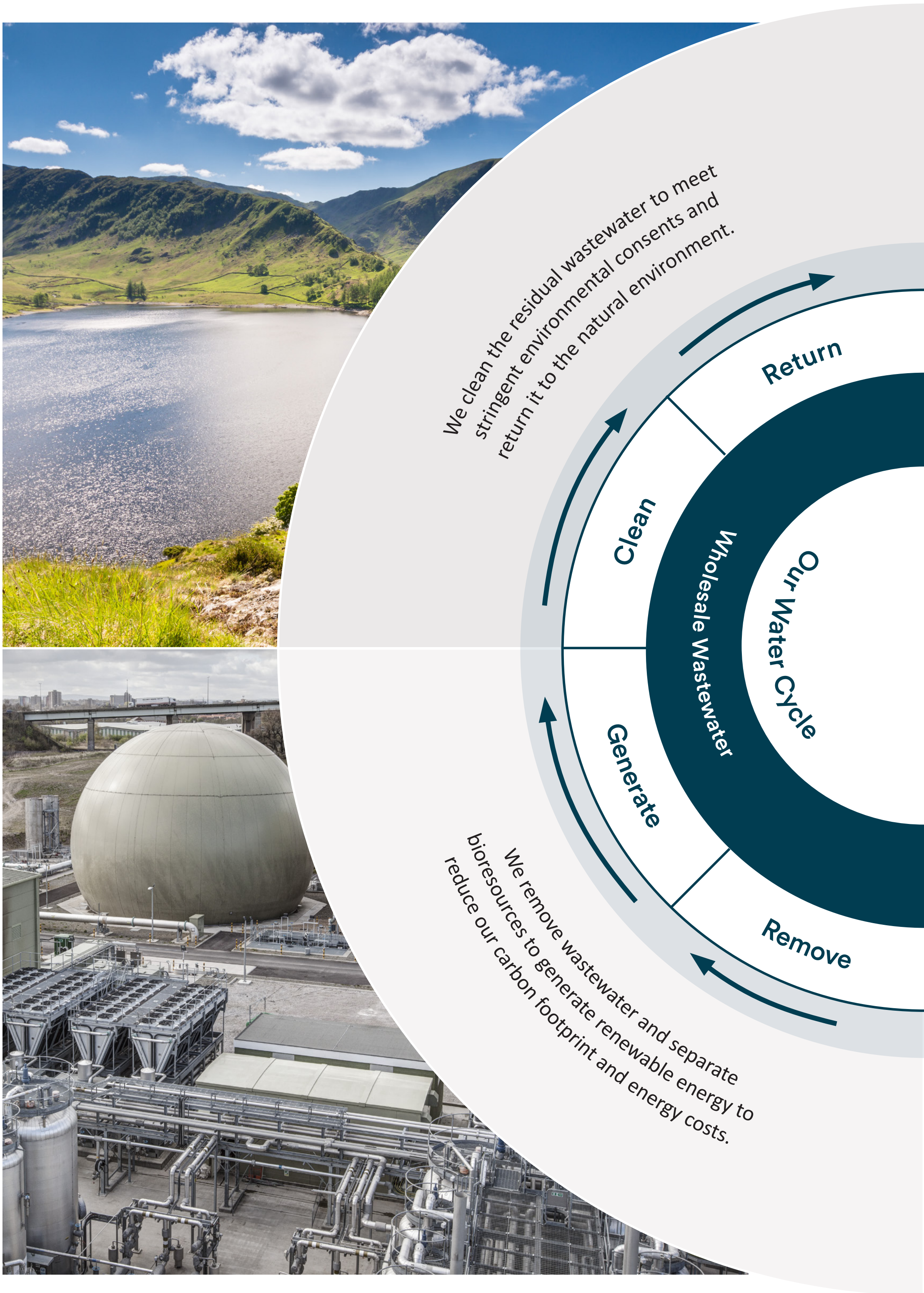
1,300
kilometres of coastline

REMOVING WASTEWATER AND GENERATING ENERGY

77,000
kilometres of wastewater pipes

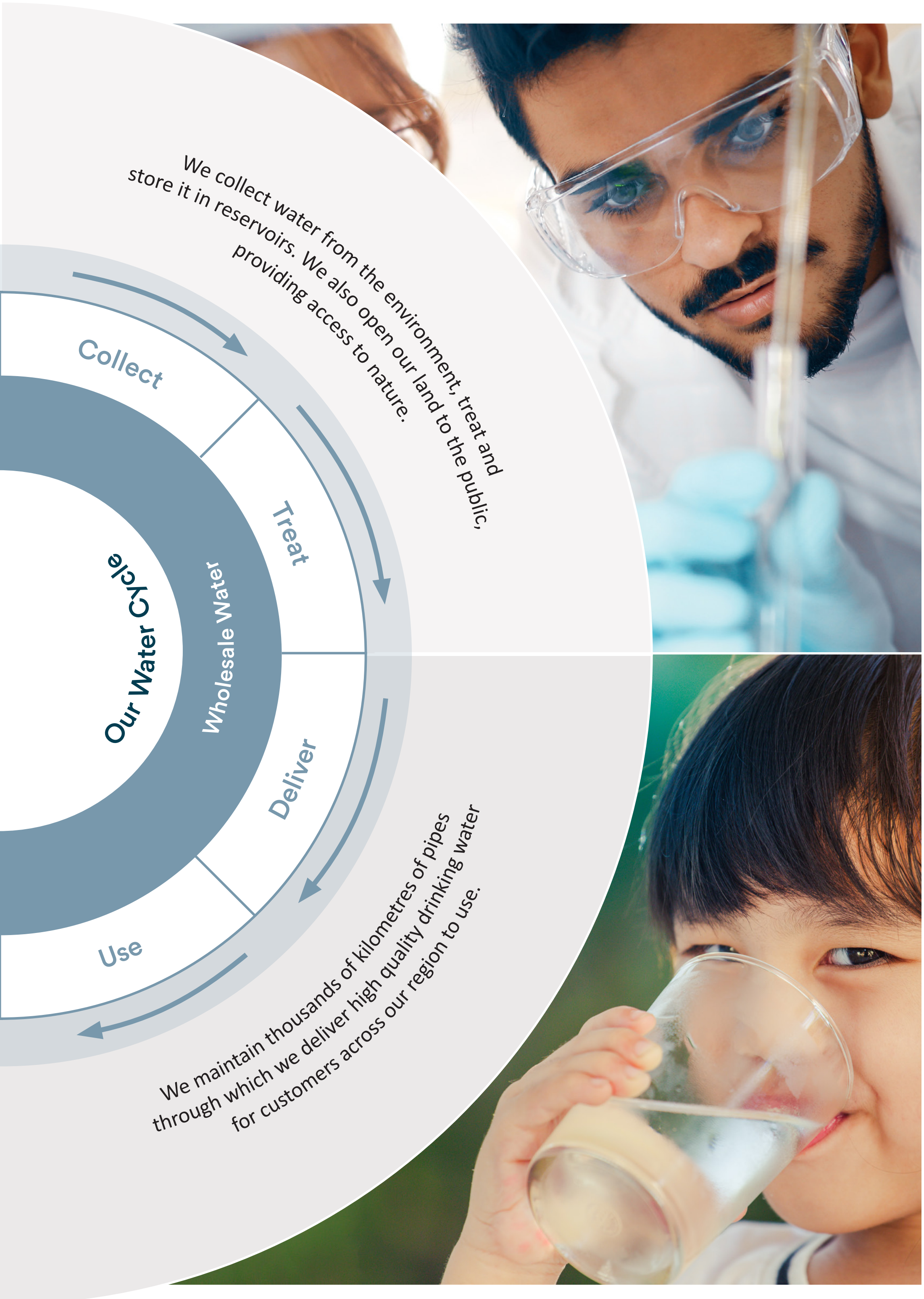
190,000
tonnes of sewage sludge every year

37
renewable energy facilities



Did you know?

We are investing **£3.9 billion** over 2015–20, including **£350 million** additional investment of outperformance earned over the period.



COLLECTING AND TREATING WATER

56,000 hectares of land

165 reservoirs

88 water treatment works

DELIVERING WATER TO CUSTOMERS

42,000 kilometres of water pipes

1.7 billion litres of clean water every day

7.2 million customers served 24 hours a day

What we do

We work in the North West, for the North West. This means understanding the key factors that make our region unique

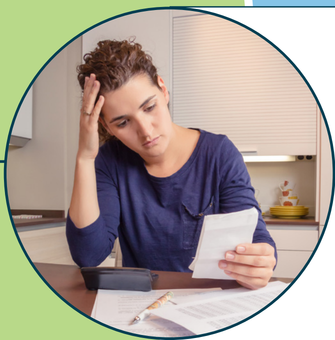
Economic factors

We are building resilience to continue serving our growing population and support jobs and the tourism industry

7.2 million population expected to grow significantly in the next 25 years

17,500 jobs actively supported by our work, with over **5,000** direct employees

Tourism relied on by Lake District, Liverpool and coastal areas



Social factors

We are leading the sector on affordability and vulnerability

41% of the most deprived areas in the country

47% of households have less than £100 savings to cope with unexpected bills

18% of households are affected by water poverty, **20%** higher then the national average

Environmental factors

We have a large coastline, protected rural areas and dense urban areas, all of which create different demands

30% of land is National Park or Area of Outstanding Natural Beauty or Sites of Special Scientific Interest

31 designated bathing waters with **25** 'good' or 'excellent' and **6** 'sufficient'

830mm higher than average UK rainfall each year

Our purpose and strategy

Our core values and strategic themes demonstrate the way we operate in order to work towards our vision and deliver our purpose

We are a purpose-driven organisation. This is the reason we exist, and is what drives us to continually improve our performance and the creation of value.

Read more about how we create value for stakeholders on pages 39 to 46

Our purpose

To provide great service to customers and communities in the North West, creating long-term value for all of our stakeholders.

Our vision

To be the best UK water and wastewater company.

Our strategic themes

- The best service to customers
- At the lowest sustainable cost
- In a responsible manner

Our strategy is broken down into three themes which form the framework for how we work towards our vision. Our operational performance measurement, risk assessment and remuneration policy are all aligned to these strategic themes.

Read more about our operational performance on pages 56 to 61

Read more about how we manage risk on pages 68 to 76

Read more in our remuneration report on pages 116 to 143

Our core values

Customer focus

Customers are at the heart of everything we do, and we aim to provide a great and resilient service at the most efficient cost.

Innovation

We continually look for new ways to make our services better, safer, faster and cheaper.

Integrity

We make promises knowingly and keep them, behaving responsibly towards all of our stakeholders.

Our core values provide the cultural framework we operate in and we encourage our employees to live these values in everything they do in their daily work.

Read more about our values and culture on pages 92 and 93

Our marketplace

We are the water and wastewater provider in the North West of England and are subject to economic, quality and environmental regulation

KEY FACTS

50 million
household and non-household customers in England and Wales

10
licensed water and wastewater companies

>£130 billion
invested in maintaining and improving assets and services since privatisation

Our industry and market

Customers in England and Wales are served by ten licensed water and wastewater companies, making up around 95 per cent of the industry, with the remainder being smaller licensed companies providing water-only services.

Since privatisation in 1989, the water industry has invested over £130 billion and delivered a significant contribution to improvements in public health. This investment has led to improvements in the quality of services, significantly higher environmental standards, and superior quality drinking water.

The advancement of technology and innovation makes way for more improvements as we continue to invest to improve services for the long term. Customer bills have declined in real terms in the current and last regulatory periods.

The water and wastewater companies are split regionally based on river catchment areas. United Utilities Water Limited (UUW) operates in the North West of England, and is the second largest of these companies based on the size of our asset base, measured by Regulatory Capital Value (RCV).

We provide water and wastewater services to a population of over seven million people, with over three million household customers making up around two-thirds of our total revenue, and over 200,000 businesses, ranging in size from large manufacturing companies to small shops.

Our competitive environment

Our main competitors are the other water and wastewater companies in England and Wales. Our vision is to be the best UK water and wastewater company, and so we regularly benchmark our performance against these peers.

Our regulators assess our comparative operational performance against the other water and wastewater companies in England and Wales:

- The Drinking Water Inspectorate (DWI) assesses our performance in the water business;
- The Environment Agency (EA) assesses our performance in the wastewater business; and
- Ofwat assesses our customer service performance through its qualitative and quantitative Service Incentive Mechanism (SIM) scores.

The EA performance assessment and qualitative and quantitative SIM scores are included in our operational key performance indicators (KPIs).

Read more about our **operational KPIs** on pages 52 and 53

As well as assessment against our water peers, we benchmark our customer service performance against other leading service providers in our region. As a FTSE 100 public listed company, the other UK and worldwide utilities are competitors from an investment perspective.

Our political and regulatory environment

We are subject to regulation of price and performance by economic, quality and environmental regulators, as set out in the diagram. These bodies exist to help protect the interests of customers and the environment.

The political and regulatory framework can change significantly in the long term and we have seen substantial tightening of laws and regulations since privatisation of the water industry. To some extent these changes are outside our direct control. Maintaining good relationships with these bodies enables us to engage positively in order to influence future policy with the aim of achieving the best outcome for all of our stakeholders.

Read more about **how we create value for stakeholders** on pages 39 to 46.

Our competitive advantages

Our pioneering Systems Thinking approach and prudent financial risk management give us a clear competitive advantage

Systems Thinking improves efficiency and operational resilience. Prudent financial risk management delivers long-term predictability and resilience to financial shocks. These competitive advantages help us to deliver sustainable long-term value for stakeholders.

Systems Thinking

What do we do?

Systems Thinking looks at how each individual element interacts with the other constituents of the system in which it operates. Instead of isolating smaller and smaller elements of the system, Systems Thinking expands its view to consider larger and larger numbers of interactions over time as a particular issue is being studied.

We use this pioneering approach to operate our business. For a water and wastewater company this means, rather than assessing and operating each asset or individual treatment works in isolation, we use all the data from the telemetry backbone we have installed across our network to analyse the entire system and all its linkages, enabling us to find the best overall long-term solutions.

Our field engineers across the region are linked by an Integrated Control Centre (ICC) at head office, from which we plan, monitor and control our operations. We process enormous amounts of real-time data in the ICC from right across our network, as well as factoring in other source data such as weather forecasts, and we have begun using artificial intelligence and machine-learning to process this data and spot issues so that we can work to resolve them before they impact customers. We allocate resources to production teams with full accountability for asset and system performance, helping to embed this way of thinking within our operational teams.

Read more about the rollout of artificial intelligence across our water network on page 35 — just one example of Systems Thinking in action.

Why is this a differentiator?

The water industry was consolidated into its current regions in 1973 and a lot of our assets were originally built a long time ago when water and wastewater services were managed by local authorities with little coordination at a regional or national level.

It takes considerable time and investment to install the telemetry and interconnections across a water and wastewater network to enable a Systems Thinking approach to be used. No other UK water company does this at the holistic level we do, and we are continuing to extend our lead, with new developments and further rollouts in the pipeline.

What value does it create?

Using network-wide real-time data and operating our network in this way enables us to optimise cost and service performance.

Systems Thinking is improving the reliability and resilience of our assets, reducing unplanned service interruptions, and helping us move away from the traditional reactive approach to address problems proactively before they affect customers.

This approach is helping us deliver operational improvements and £100 million cost savings versus our original business plan for the current regulatory period. Further development of Systems Thinking is embedded into our business plan submission for the 2020–25 period. It is part of our long-term strategy to continue delivering benefits for customers and other stakeholders well into the future.

Prudent financial risk management

What do we do?

Inflation — we maintain around half our debt in index-linked form, offering good relative value and hedging the impact of inflation on a portion of our regulatory capital value (RCV) and revenue. Most of this is RPI-linked, reflecting the current regulatory model. From 2020 Ofwat will transition towards consumer price inflation including owner occupiers' housing costs (CPIH), so we will gradually increase our CPI exposure, subject to cost and availability, as CPI is the best available proxy for CPIH in the absence of a CPIH debt capital market.

Interest rates — we fix the underlying interest cost on our remaining nominal debt out to ten years, on a reducing balance basis. We have previously supplemented this by substantively fixing interest rates for each forthcoming regulatory period when Ofwat publishes the final determination, including the cost of debt allowance. From 2020 Ofwat will apply debt indexation to the portion of debt assumed to be new debt, so this supplement will not be necessary for the 2020–25 period.

Pensions — we adopt an asset-liability matching approach for our defined benefit pension schemes by investing in assets, such as corporate bonds and gilts and the use of interest rate swaps, that perform in line with the liabilities, providing a hedge against changes in swap and gilt yields and therefore stability in our pensions position. The schemes have hedged inflation exposure through RPI gilts and swaps, and in April 2019 we prepaid all remaining deficit repair contributions meaning the schemes are now self-sufficient.

Why is this a differentiator?

Different companies have different levels of risk exposure as a result of preference and/or analysis of the costs and benefits of moving away from a historically different approach. Our prudent approach offers a lower risk exposure than many other companies.

What value does it create?

Effective financial risk management delivers long-term resilience and our clearly articulated policies, covering a variety of market risks, help us reduce our exposure to the economic and regulatory environment, providing more predictable returns to investors.

Our approach to debt financing and interest rate risk management enables us to consistently lock in long-term debt at good relative value, manage uncertainty in Ofwat's approach to setting the cost of debt at each price review, and maintain resilience to financial shocks. Our asset-liability matching approach reduces the volatility of the required funding level of our defined benefit pension schemes, and self-sufficiency means our employees and pensioners are in a very secure position and shareholders are well protected.

All of this underpins our target to maintain gearing (measured as net debt to RCV) within a range of 55 to 65 per cent, which supports a solid A3 credit rating with Moody's for United Utilities Water Limited, and enables us to maintain efficient access to the debt capital markets across the economic cycle.

Our economic regulation

Ofwat sets the regulatory contract that we will deliver in each five-year period

KEY FACTS

5-year
regulatory contracts set by Ofwat for Asset Management Plan (AMP) periods

AMP6
covers 1 April 2015 to 31 March 2020, with four of these five years now delivered

AMP7
covers 1 April 2020 to 31 March 2025, with business plans already well progressed and final determinations due in December 2019

Setting our regulatory contract

Water and wastewater companies in England and Wales operate within five-year regulatory periods known as Asset Management Plan periods (AMPs). Price, service and incentive levels are set by our economic regulator, Ofwat, prior to the start of each regulatory period following a period of consultation and planning known as a price review.

During the price review, Ofwat consults with stakeholders, including water and wastewater companies, and sets out its methodology, which details its key areas of focus and an indication of how prices, service and incentive levels will be set.

Companies consult with customers and other stakeholders, including environmental and quality regulators, and prepare a detailed business plan that sets out the proposed price and service package they will deliver over the period.

These plans are submitted to Ofwat, which scrutinises and challenges them and ultimately sets a regulatory contract for each company, known as the final determination (FD). The FD sets the price, in terms of total expenditure (totex) and customer bills, level of service, and incentive package that companies must deliver over the period. It gives an allowed return companies can earn, which is expressed as a percentage of Regulatory Capital Value (RCV).

We base our plan on continuous customer insight and bespoke research and consultation on customer priorities, factoring in long-term planning as well as what is needed in just that five-year period. This means we can submit a robust and balanced plan to Ofwat. This helps ensure we receive a regulatory contract that targets the best overall outcomes for our customers and all our stakeholders, and which effectively incentivises us to continually improve our performance.

We have just delivered the fourth year of the sixth asset management plan period (AMP6) that covers the 2015–20 regulatory period. The 2019 price review (PR19) that will set the regulatory contract for the 2020–25 period (AMP7) is well under way. Key dates in the PR19 process can be seen on the timeline below.

Delivering that contract

In order to incentivise companies to deliver sustainably better and more efficient performance, Ofwat gives companies the opportunity to earn a higher return where they outperform their regulatory contract, and the risk of earning a lower return where they underperform. The opportunity for outperformance allows us to create further value for customers, shareholders and wider stakeholders. We can outperform through:

- Totex – delivering the agreed outcomes while spending less than the allowed totex through innovation and efficiency initiatives. Totex outperformance is shared roughly 50:50 between customers and the company.
- Outcome delivery incentives (ODIs) – beating the stretching target levels agreed for an assortment of measures, mainly of customer service and environmental performance.
- Customer satisfaction – delivering a great level of customer service that is favourable relative to the other water and wastewater companies, currently measured through Ofwat's quarterly service incentive mechanism (SIM) surveys.
- Financing – raising debt finance at a cost below the industry allowed cost of debt, which forms part of the overall allowed return.
- Household retail – minimising the cost to serve our household customers relative to the allowed revenue for household retail activities.

We include our performance against each of the above areas in our operational KPIs, including our targets for the 2015–20 regulatory period. Since the start of AMP6 we have published an Annual Performance Report (APR), which reports our regulatory performance in a format that helps customers and other stakeholders understand it and compare it with other companies in the sector. This includes reporting of Return on Regulated Equity (RoRE), which is made up of the base allowed return and any outperformance/underperformance in the above areas.

Our APRs are published in July each year at **unitedutilities.com/corporate/about-us/performance**

Information on companies' regulatory performance can also be found at **discoverwater.co.uk**

3 Sept 2018
Submission of company business plans to Ofwat

31 Jan 2019
Publication of Ofwat's initial assessment of company business plans

11 Apr 2019
Publication of draft determinations for fast-track companies

AMP7 Planning and preparation

AMP6 Delivery – Year 4 of 5 | AMP6 Delivery

31 March 2018 → **31 March 2019**

Our business plan submission for 2020–25

Meeting the high hurdle to achieve a fast-track assessment

Overview

We submitted our business plan for the 2020–25 period in September 2018, and Ofwat published its initial assessment (IAP) on 31 January 2019, in which we were one of only three companies to achieve a fast-track assessment. This achievement reflects the transformation we have delivered in recent years as well as the quality of our plan.

Our plan received the highest overall grades for the sector, as can be seen in the table below. It was commended as high quality and industry-leading in many areas, including innovation, affordability and vulnerability, customer engagement, and resilience. We committed to deliver more for less for customers, with stretching service level targets alongside a significant bill reduction in real terms.

As part of the IAP, all three fast-track companies accepted targeted actions from Ofwat. There were areas of our plan where we were asked to commit to even more stretching targets, such as reducing leakage, a further 3 per cent reduction in total expenditure, and provide more information on our proposals. We will continue to work constructively with Ofwat through to our final determination in December 2019.

A fast-track assessment brings reputational, financial and procedural benefits. Most importantly, it gives us greater clarity earlier in the process, and we have committed a further £100 million investment in 2019/20 to make a flying start in delivering our plan.

Ofwat published its latest annual Company Monitoring Framework assessment, in which we retained the highest category of 'self-assurance'. We have achieved this three years in a row – the only company to do so – demonstrating the consistently high level of trust and confidence that customers and other stakeholders can have in the quality and transparency of our reporting.

Ofwat's assessment of company performance against key test areas

	Water and sewerage companies											Water only companies					
Test Area	Anglian Water	Dwr Cymru	Hafren Dyfrdwy	Northumbrian Water	Severn Trent Water	South West Water	Southern Water	Thames Water	United Utilities Water	Wessex Water	Yorkshire Water	Affinity Water	Bristol Water	Portsmouth Water	South East Water	South Staffs Water	SES Water
Engaging customers	A	B	C	B	B	B	C	C	B	B	B	C	B	C	C	B	C
Addressing affordability and vulnerability	B	B	D	B	B	B	B	C	A	B	C	C	C	C	B	C	B
Delivering outcomes for customers	B	C	D	C	C	B	C	C	C	C	C	C	C	C	B	C	C
Securing long-term resilience	C	C	D	C	C	B	D	D	B	C	C	D	C	C	C	D	C
Targeted controls, markets and innovation	B	C	C	C	C	C	C	C	B	B	B	C	C	C	B	C	C
Securing cost efficiency	D	D	B	C	B	B	D	D	B	C	C	C	C	B	C	C	D
Aligning risk and return*	C	C	D	B	C	B	C	C	C	D	C	D	C	C	C	C	C
Accounting for past delivery*	B	C	D	C	B	D	D	D	B	B	B	C	D	C	D	B	B
Securing confidence and assurance	D	A	C	C	B	C	C	C	B	C	C	C	C	C	B	C	D

* Highest possible assessment for these test areas was B

Source: Ofwat, PR19 Initial assessment of plans: Summary of test area assessment

A = High-quality, ambitious and innovative plan with evidence that overall is sufficient and convincing

B = High-quality plan, not sufficiently ambitious and innovative to be exceptional with evidence that overall is sufficient and convincing

C = Concerns with the plan: Plan falls short of high quality and/or evidence is insufficient and/or unconvincing in some areas

D = Substantial concerns with the plan: Plan falls significantly short of required quality and/or little or no evidence, or no convincing evidence

KEY FACTS

Fast-track
rating received for our high quality and ambitious plan

Lower bills
for customers in real terms to 2025

£100 million
additional investment in 2019/20 to facilitate a flying start to AMP7

18 July 2019
Publication of draft determinations for slow-track and significant scrutiny companies, and update on Ofwat cost of capital assessment

11 Dec 2019
Publication of final determinations for all companies

Jan 2020
Companies announce whether they accept their final determination

April 2020
Start of AMP7 period

AMP7 Delivery – Year 1 of 5

– Year 5 of 5

31 March 2020

Our business plan submission for 2020–25

High quality and sector leading across a range of areas

Innovation

Our approach to innovation is deeply embedded throughout the entire organisation and we were the only company to receive the highest possible grade in the sub-test for innovation. We are delivering technology and processes that are not seen elsewhere in the industry.

We have delivered enhanced capabilities through our pioneering Systems Thinking approach, which has delivered both efficiency and improved performance, underpinning the transformation we have delivered in recent years. Our business plan includes significant savings to be delivered from our innovation initiatives.

We are actively working with global innovators, from small start-ups to large, established corporations, reaching far beyond the water sector. Through our Innovation Lab, we have gained unprecedented access to very small businesses with very big ideas – companies across the world that would normally struggle to interact with a large utility.

Read more about **our Innovation Lab** on page 37

We will exit the current regulatory period as a high-performing and efficient company, and we have achieved this in part by being at the frontier of innovation and technology.

"United Utilities shows the most embedded innovation culture, with an ambitious and sector-leading approach to innovation capability"

Source: Ofwat, PR19 IAP – Overview of company categorisation

Affordability and vulnerability

Our ambitious and innovative approach to addressing affordability and vulnerability is seen by Ofwat as sector-leading and we received the highest available grade in this key test area.

Our plan represents a strong value for money proposition, supported by over 80 per cent of customers. Average customer bills are lower with a real reduction of over 10 per cent between 2020 and 2025 supported by targeted financial assistance for those who need it most, while service and environmental quality continue to improve.

Our region is home to some of the most deprived communities in England and Wales. We have worked hard to put in place some of the most innovative and ambitious affordability schemes in the industry, and have taken a lead on transforming the sector's approach to supporting customers in vulnerable circumstances. Our plan will push the industry frontier through innovative affordability schemes, such as our Lowest Bill Guarantee, which gives confidence to customers that a meter would save money, as well as water.

This year we hosted the second North West Affordability Summit, working alongside charities, local authorities and support agencies to find ways to help customers in need. At this second summit we launched the North West Hardship Hub, a one-stop-shop portal for cross-sector information and financial assistance schemes to help the money advice community find the right support for vulnerable people.

Read more about this **North West Hardship Hub** on page 57

"United Utilities' plan includes ambitious, innovative and sector-leading proposals to make customers' bills affordable and on providing support for vulnerable customers"

Source: Ofwat, PR19 IAP: United Utilities company categorisation

Customer engagement

Our high-quality approach to customer engagement was recognised by Ofwat in its assessment, as was our ambition and innovation in bringing research findings together with other sources of customer data to gauge customer support for our plan. One test area Ofwat asked us to improve was delivering outcomes for customers, with more evidence on some performance commitments and commit to more challenging targets to align with the results of customer feedback and the industry frontier.

Our plan reflected unprecedented engagement with customers, regulators and other stakeholders. Over 140,000 people from all walks of life were involved in informing our plan through over 90 bespoke engagement exercises. We used a range of research techniques, including online surveys, co-creation events and online panels tailored to the target audience. Our use of new techniques, such as immersive research and behavioural economics, to get better insight into customers' preferences and to supplement stated preference approaches, was highlighted by Ofwat as ambitious and innovative. Over 2 million individual data points, from day-to-day interaction with customers, were used to create our plan.

The independent customer challenge group, YourVoice, monitored our performance during the current regulatory period and was deeply involved in challenging our plan for 2020–25.

Read more on pages 22 and 23 about **how we used this engagement to help shape our business plan**

"United Utilities' plan reflects high-quality customer engagement and participation. It uses a range of research techniques . . . tailored to the target audience"

Source: Ofwat, PR19 IAP – Overview of company categorisation

Resilience in the round

We have seen record-breaking extremes of weather in the last few years that have tested the industry. Learning from this, we have already made significant progress in enhancing operational resilience, and we are investing an additional £250 million in the current regulatory period to improve this further.

Read more about **our response to these challenges** on page 30

We were assessed as an industry leader in our approach to securing long-term operational, corporate and financial resilience. Our Systems Thinking approach has been fundamental to this assessment, and our robust capital structure, appropriate level of gearing, prudent financial risk management and strong pensions position contribute to the strength of our long-term resilience.

Our plan proposed a major water resilience scheme in Manchester and the Pennines, which will mitigate the most significant operational risk that we face. Ofwat recognises the need for investment to deliver resilience and welcomed the fact that we have embraced the direct procurement approach in our proposal. Given its scale and complexity, this will be addressed outside the constraints of the fast-track timetable.

As a contribution to national resilience, we devised a large-scale north-south water transfer scheme some time ago. Ofwat is proposing to allow up to £25.7 million to further investigate this scheme in collaboration with two other water companies to determine whether it would be a strong value-for-money proposition.

"United Utilities has a sector-leading approach to resilience . . . and set the standard for other companies to reach"

Source: Ofwat, PR19 IAP – Overview of company categorisation

Aligning risk and return

Our plan provides for a fair balance of risk and return, with rewards available for the delivery of stretching performance. We have a responsible corporate structure aligned with industry-leading environmental performance and strong financial resilience, and we provided strong evidence about the financeability of our proposed business plan.

We committed to provide £71 million of company funding over the period toward financial assistance schemes for customers in need, building on our sector-leading approach to affordability and vulnerability.

In addition, we proposed a clearly defined benefit sharing mechanism through our 'CommUnity Share' scheme, which offers to match benefits for customers if dividends are much higher than assumed in our business plan. We will consult with customers and stakeholders, under the supervision of the independent customer challenge group, YourVoice, about how this funding will be used, with transparency about how this funding would be used for customer benefit.

This builds on the voluntary reinvestment of over £600 million that we have already committed across the current and previous regulatory periods. Ofwat recognises that this approach puts us among the leading companies in terms of voluntary benefit sharing with customers.

"United Utilities' plan demonstrates high quality and ambition in its approach to aligning the interests of the company and its investors with customers"

Source: Ofwat, PR19 IAP – Summary of test area assessment

Stretching service levels and efficient cost

Driving efficiency is a key focus for management and Ofwat found ours to be one of the most efficient plans when compared with its own view of efficient costs.

Our business plan represented a reduction of over £1 billion in expenditure compared with AMP5 (covering 2010–15), driven by innovation, use of market mechanisms, and the significant improvement that we have made in efficiency in recent years. All three fast-track companies were asked to reduce their cost proposals by about 3 per cent. This compares with the industry average that was 15 per cent above Ofwat's view of efficient costs.

In household retail, we have substantially reduced our cost base in recent years, primarily through tackling levels of household bad debt, and we were pleased to see that our cost projections aligned with Ofwat's own assessment.

There are 14 common Outcome Delivery Incentives (ODIs) for the industry, where targets are based on upper quartile performance expectations, alongside a suite of innovative, company-specific measures. The targets for common ODIs were updated with Ofwat's latest view based on plan submissions, and may change further as the price review process continues for all companies.

"United Utilities provides a high-quality plan and made strides towards cost efficiency compared to the last price review"

Source: Ofwat, PR19 IAP – Summary of test area assessment

If it matters to you, it matters to us

We asked over 140,000 customers and stakeholders across our region what matters most to them, and used this feedback to help shape our business plan for 2020–25. These are just a few examples of what they told us and how we responded.

Read more online at unitedutilities.com/corporate/about-us/our-future-plans/our-proposed-business-plan/

YOU TOLD US...
Providing extra support for those in need matters

THAT'S WHY...
We've introduced payment breaks and pledged to help 250,000 customers out of water poverty

YOU TOLD US...
Replacing old pipes matters

THAT'S WHY...
We've committed to a long-term aim of eliminating lead pipes across the network

YOU TOLD US...
Protecting the environment matters

THAT'S WHY...
We're playing our part in improving the quality of the region's river and bathing waters

YOU TOLD US...
Reducing leaks matters

THAT'S WHY...
We've increased our team of leak detectives across the region – including our team of leak detection sniffer dogs

YOU TOLD US...
Lower bills matter

THAT'S WHY...
We've proposed our largest ever bill reduction of over 10 per cent, reducing average bills in real terms by 2025

YOU TOLD US...
Reducing internal flooding matters

THAT'S WHY...
We've pledged to drive down the amount of internal sewer flooding incidents over the next five years

Our business model

We consult and plan for short, medium and long-term horizons

We provide essential water and wastewater services to millions of customers every day, and this relies on a variety of key resources. How we manage these is influenced by external drivers and relationships with a variety of stakeholders.

Consultation with customers and other stakeholders forms an integral part of our planning process across the short, medium and long term, and our work delivers a range of long-term benefits for many different stakeholder groups. This value creation feeds back into the continuous cycle of what we do.

Read more about our key resources and the impact of external drivers on pages 28 to 34

Read more about our planning horizons on pages 48 to 50

Our external drivers and relationships

Natural environment

- The natural environment is constantly changing, and we must adapt and prepare for future impacts such as climate change and population growth. Our use and return of water to the environment is a continuous cycle, and returning water cleanly and safely, as well as managing our catchment land effectively, allows this cycle to begin again from the best starting point.

Technology and innovation

- New technologies and innovative ideas present opportunities for us to make things faster, better, safer and cheaper. These can come from all over, which is why we encourage innovation externally and internally at all levels of the business, from our annual CEO Challenge and dedicated innovation team to our Innovation Lab.

Stakeholders

- Our work and the huge areas of land we manage puts us at the heart of communities in our region, and impacts a large variety of stakeholders. We build relationships and consult with them in developing and executing our plans.

Regulatory environment

- Sustainable business means preparing for future market reforms as well as meeting current regulatory commitments. We place great value on our relationships with economic, quality and environmental regulators, engaging actively and influencing where we can.

Our key resources

Natural resources

- We rely on natural sources of water that we collect for treatment, and manage large areas of catchment land in a sustainable way. We rely on watercourses where we return wastewater safely and cleanly to the environment, and we process bioresources from wastewater to generate renewable energy, which helps to reduce our carbon footprint and energy costs.

Assets

- Our significant capital investment programme helps to grow our business while building resilience and maintaining and enhancing sustainable long-term assets. We use telemetry across the network to manage our assets as one integrated network from our Integrated Control Centre as part of our Systems Thinking approach.

People

- We rely on employees and suppliers to deliver our services to customers. We are committed to attracting, developing, training and motivating a diverse and skilled workforce. We build effective relationships and work with suppliers who share our values. We have management incentives based on performance and a long-term incentive plan.

Financing

- Financing allows us to preserve intergenerational equity for customers while funding long-term capital investment. We maintain a robust capital structure with an appropriate level of gearing level and prudent risk management. We have long-term debt locked in at good relative value and maintain access to a range of markets. We proactively engage with equity and credit investors.

Political environment

- We engage with regional and national politicians as well as policy makers, through regular meetings and conferences, in relation to areas such as our local investment schemes, our economic contribution to the North West, and key policy issues affecting the water industry.

Economic environment

- We are impacted by market rate movements, such as interest rates and inflation, and seek to manage these prudently to reduce risk as far as practical. We operate in an area with high levels of extreme deprivation, so helping vulnerable customers is particularly important for us.

We deliver the outcomes set out in our regulatory contract

What we do is set out in our regulatory contract, which details the price and service package we will deliver in each five-year period split out by price control areas – wholesale water, wholesale wastewater and household retail. The fourth price control, non-household retail, sits within our joint venture, Water Plus.

How we do it is set out in our strategic themes, and everything we do is underpinned by our values and culture, and our governance and risk management. Our pioneering Systems Thinking approach to operating our business is a competitive advantage.

We review progress on outcomes we have promised to deliver for customers in the regulatory period, and we measure our performance against operational KPIs as well as financial measures.

These outcomes and KPIs fit within the framework of our three strategic themes.

How we operate

What we do

Read more about what is involved in the provision of wholesale and retail services in our water cycle on pages 12 and 13

How we do it

Read more about our strategy on page 15, and more about our competitive advantages on page 17

Our outcomes and KPIs

The best service to customers

Outcomes

- Provide great water;
- Dispose of wastewater; and
- Deliver a service customers can rely on.

KPIs

- Wholesale ODI composite;
- SIM – qualitative; and
- SIM – quantitative.

At the lowest sustainable cost

Outcomes

- Value for money; and
- Improved efficiency.

KPIs

- Totex outperformance;
- Financing outperformance; and
- Household retail cost to serve.

In a responsible manner

Outcomes

- Protect and enhance the environment;
- Support local communities; and
- Support employees in a safe workplace.

KPIs

- Leakage;
- EA performance assessment; and
- Dow Jones Sustainability Index.

We review and measure our progress

We create long-term value for a range of stakeholders

The work we do delivers a wide range of benefits to a variety of stakeholders, creating long-term sustainable value for many people.

Responsible business runs through everything we do, as evidenced by our business principles.

Read more on pages 39 to 46

Read more at unitedutilities.com/corporate/responsibility/our-approach

For shareholders

- Many of our shareholders are pension funds and charities and the income that we provide is relied on by millions of people every day. We manage risk prudently and provide an appropriate return, investing in our assets for growth and sustainability

For customers

- Through innovation and efficiency we provide a great service at a lower cost. We support thousands of vulnerable customers through a wide range of assistance schemes

For employees

- We focus on attracting, developing and retaining a diverse workforce, and ensuring that we look after their health, safety and wellbeing. To help ensure the next generation of skilled employees, we run graduate and apprenticeship programmes

For the environment

- We maintain and enhance reservoirs, catchment land, rivers and bathing waters that provide a home for wildlife, areas for recreation, and a major pull for tourism. We strive to reduce our environmental impact and generate renewable energy

For communities

- We build partnerships and work with schools to develop skills and help people back to work. We encourage employee volunteering programmes to help create better places, stronger communities, and accomplish more to address local issues together

For suppliers

- We invest in the North West's infrastructure and generate jobs, skills and income through our supply chain that supports the local economy. We treat all suppliers fairly and are a signatory to the Prompt Payment Code

Open the flap to see our business model in full

Our business model
Key resources and the impact of external drivers

Natural resources
We rely on a variety of natural resources to deliver water and wastewater services, and we impact those natural resources through our operations, such is the circular nature of the water cycle. We also generate renewable energy from the sun and wind.

We rely on natural sources of water to supply customers. We hold abstraction licences for a number of reservoirs, rivers and boreholes that permit us to take water from the environment in a safe and sustainable way, which we then treat, store and transport across the region.

Nearly half the water we abstract originates from land we own and manage. Run-off from this land impacts the quality of the water, so managing it well helps us provide reliable and clean water, reducing risk and increasing our resilience. We help protect habitats and species designated as nationally and internationally important, many of which make their homes on this land.

We rely on watercourses to take effluent back into the environment after extensive cleaning to ensure it meets environmental consents. This protects the health of the natural environment, which enhances recreational value for our communities, protects rare species and wildlife habitats, and provides economic benefits such as underpinning the local tourism industry.

We extract bioresources from wastewater, using anaerobic digestion to break it down into biogas and biosolids. Biogas is used to generate renewable energy through combined heat and power plants, reducing our energy costs and carbon footprint. Biosolids are treated to provide a valuable source of nutrients and organic matter as high-quality fertiliser for farmers.

Impact of external drivers
Natural environment
Our long-term planning looks far into the future to ensure we are prepared for the challenges of a changing natural environment. The most significant anticipated impact comes from climate change, and in particular the long-term changes in average temperature and rainfall. Water companies must adapt to meet the challenges climate change presents, and this creates both risks and opportunities.

The main opportunity is the potential for water sharing. Our region typically receives higher average rainfall than other parts of the country, meaning the availability of raw water tends to be less constrained than in the comparatively drier south. Ofwat indicated in its initial assessment of company business plans for 2020–25 that it would provide us with £25.7 million funding for feasibility and planning work with respect to a potential north-south transfer of water as part of the development of strategic water resources options for the south and south east.

The main risks are the impact of prolonged severe dry periods, which constrain water resources, and intense periods of heavy rainfall, which increase the risk of flooding and pollution incidents.

Our response to climate change risk can be split into two areas: mitigation and adaptation.

- Mitigation – reducing carbon emissions to minimise our contribution to climate change.

The key contributor to climate change is an increase in greenhouse gases. There is global scientific agreement that as a result of human activity the amount of greenhouse gases in the atmosphere is increasing and affecting the global climate. We have been driving down our carbon footprint (net operational emissions in 2018/19 were over 70 per cent lower than 2005/06) and have plans to reduce it further, mainly through our energy strategy.

We have assessed our operational sites for their potential to generate renewable energy through either solar panels or wind turbines. We are working on plans to substantially increase our renewable energy production across the current regulatory period to 2020, mainly from solar, and this year we generated the equivalent of over 20 per cent of our electricity consumption through renewable energy. This provides environmental benefits as well as energy cost savings.

The anaerobic digestion of bioresources reduces our carbon emissions as well as saving energy costs and producing a high-quality fertiliser. Our advanced digestion facility at Davyhulme wastewater treatment works is one of the largest of its type, making the site energy self-sufficient, with surplus energy exported to the national grid.

- Adaptation – improving the resilience in our water and wastewater business.

The potential effect of climate change on our future water resources is considered in our 25-year Water Resources Management Plan, and we published two adaptation reports in 2011 and 2015 outlining our holistic, integrated and partnership approach to a range of short, medium and long-term challenges including climate change.

Read more about our **long-term planning** on page 48

It is predicted that climate change will result in the North West experiencing higher daily temperatures all year, and a shift in our rainfall from summer to winter. More occurrences of heavy rainfall are expected, with higher rainfall in winter but more frequent and/or severe drought events predicted in summer.

We have first-hand experience of the impacts of extreme weather events on our operations and customers – during 2018 we experienced two weather extremes, with a deep freeze followed by rapid thaw in the early part of the year, and then extremely hot, dry weather coupled with significantly increased demand for water over the summer.

Read more about these **weather extremes in our business insight** on page 30

Coping with extreme hot, dry periods requires action in relation to both supply and demand.

Supply is managed by ensuring we continue to have resilient water resources and infrastructure capable of moving water efficiently around the region. We have an integrated supply zone covering the majority of our region operated using our Systems Thinking approach. This helps us to manage water supply and demand and, where there is any potential shortfall, we bring more supplies online to meet demand. Generally this system is proficient, but there are areas that require further improvements to deal with future challenges. Our West East Link Main pipeline runs between Manchester and Liverpool, allowing transfer of water across our region, and the extreme dry weather in 2018 gave us cause to increase the capacity of this pipeline, as well as bringing additional groundwater sources online, both of which increased our resilience.

Demand is managed by encouraging and supporting customers to use water efficiently. We have increased our efforts in this area and ran a number of high profile campaigns in summer 2018 when demand was much higher than normal. We encourage customers to save water through education initiatives to raise awareness, sharing water saving tips on our website and through social media, and providing free water-saving devices. We work with external partners to expand our messaging further afield, and have increased the number of water meters installed, with 44 per cent of households in our region now fitted with meters.

Coping with periods of intense heavy rainfall requires action to cope with excess surface water drainage while minimising the risk of sewer flooding, pollution and spills.

Traditional interventions, such as storage tanks and enlarging sewers, are costly and subject to constraints for space, particularly in urban areas with little permeable ground. Innovation is needed to find new solutions, which is why we have increased our focus on the use of sustainable drainage solutions in recent years, working with partners to transform hard-grey areas into living planted places.

Our operations produce sludges, excavated materials and general office waste, which we are committed to managing in a sustainable way. Less than five per cent of our waste goes to landfill, we use recycled products where practical, and are working to reduce the use of plastics. We look for ways to reduce our use of raw materials to minimise our environmental impact and increase efficiency.

Stakeholders

Our catchment land is open to the public with an estimated nine million visits a year, providing access to the beauty and recreational benefits that the natural environment offers, and boosting the local tourism industry.

Much of our catchment land is managed by tenant farmers, or in partnership with other organisations such as the RSPB and Wildlife Trusts. We are increasingly looking at integrated catchment solutions, taking a holistic view of issues and solutions within catchments, working with others to improve the lakes, rivers and coastal waters in our region, and often utilising the natural environment as part of the solution. We have a long history of doing this through our award-winning sustainable catchment management programme (SCaMP), which has shown we can manage our catchment land to protect and enhance water quality and to provide other benefits such as an improving biodiversity.

We are one of many organisations with a role to play in boosting the quality of bathing water along the North West coast. With strict bathing water standards, we continue to work with partners to improve the quality of rivers and coastal waters, and we give the public real-time information on bathing water quality.

Technology and innovation

Innovation is one of our core values, and we embrace new treatment technologies and efficient approaches that use less resources. The development of connected technologies and Systems Thinking enables greater control and flexibility to operate our networks and assets to reduce our environmental impact.

Regulatory environment

Our regulatory framework shapes the way we manage natural resources and our interaction with the environment, and we work with our environmental regulators to agree long-term plans. The Environment Agency (EA) assesses water companies' performance across a basket of measures including regulatory compliance, pollution incidents and improvement plans.

Political environment

Many of our environmental regulations are based on EU legislation; therefore, there may be changes after the UK leaves the EU. The UK government published its 25-year Environment Plan for England and Wales in 2017, setting out its environmental ambitions. This plan, subject to any changes following exit from the EU, influences our activities and long-term investment plans.

The influence of devolved metro mayors in our region is starting to impact development and spatial planning, including the natural environment. Maintaining a close working relationship helps us work together to improve the natural environment in the region.

Global politics also has an impact on what we do. See page 46 for how we are contributing to the UN's Sustainable Development Goal to 'Ensure access to water and sanitation for all'.

Management and measurement

We have an ISO-accredited environment management system that covers the whole business, and is externally certified through six-monthly surveillance visits.

We have a comprehensive set of environmental strategies covering our approach to carbon management, waste and resources, biodiversity and water use.

Our environmental policy is available on our website at: **unitedutilities.com/corporate/responsibility/environment**

We manage our own woodland in a sustainable way to protect water quality, conservation, access, recreation and timber, and have been Forest Stewardship Council® (FSC®) certified since 2003.

A number of our operational KPIs are directly linked to the protection and enhancement of the natural environment, such as leakage, EA performance assessment, and some of our wholesale outcome delivery incentives, such as measures of our contribution to improving rivers and bathing waters, and pollution incidents.

See how we are **performing against our operational KPIs** on pages 52 and 53

We measure and report on our wider environmental performance. Those most relevant to our stakeholders can be found on page 55, and information is available on our website at: **unitedutilities.com/corporate/responsibility/environment/environment-performance**

The principal risks and uncertainties that relate to this key resource are 'Health, safety and environmental risk', 'Water service risk' and 'Wastewater service risk'.

Read more about **how we manage risk** on pages 68 to 76.

Link to our strategic themes

The best service to customers

Customers have told us they value the natural environment and want us to protect and enhance the region's natural resources as part of our activities, and this was one of the outcomes that we committed to deliver as part of our business plan for the 2015–20 regulatory period. Many of our outcome delivery incentives are directly linked to the environmental impacts of our water and wastewater services and to protecting and enhancing the environment. We help customers do their bit for the environment and save money on their bills through our water-saving initiatives and 'what not to flush' campaigns to prevent sewer blockages.

At the lowest sustainable cost

Our embedded innovation culture helps us find new ways of working that simultaneously reduce costs and protect natural resources. Our approach to catchment management aims to address issues at source rather than through increasingly expensive treatment methods. This approach, as well as our renewable energy generation, makes us less reliant on power and chemicals, which reduces treatment costs as well as carbon emissions and use of natural resources. The work we do to prepare our network to sustainably cope with extreme weather and the challenges of climate change can save repair and recovery costs as well as ensuring a more resilient service for customers.

In a responsible manner

Managing our dependency, use and impact on natural resources is a key expectation of many of our stakeholders. Our monitoring and management of leakage from our water network is a crucial part of responsible water management. We comply with abstraction licences and environmental discharge consents set by independent regulators to safeguard the responsible management of the environmental impact of the water and wastewater services we provide. In addition, our efforts to reduce our carbon footprint and use of plastics makes an important contribution to protecting and enhancing the natural environment and mitigating climate change.

Business insight

Responding to extreme weather conditions

Keeping the taps flowing during a year when weather conditions swung from blizzards to the longest heatwave since 1976

From sub-zero temperatures, high winds and blizzards to the longest heatwave since 1976, 2018 was a year of extreme weather challenges. As we worked to maintain water supplies, tackle leakage and encourage customers to play their part by using water wisely, we faced intense media scrutiny.

Between May and August 2018 there was significantly lower rainfall than average, and this was felt most acutely in North West England. It was the driest start to the summer since modern records began in 1961 and soaring temperatures contributed to a huge demand for water. At the height of the hot weather in June the demand for water rose by 500Ml/d – 25 per cent more than usual.

At one stage there was a possibility that we might have had to impose a temporary use ban if the extreme dry weather and increased demand had continued. Due to our own efforts, and those of our customers who responded to our calls to use water efficiently, this was avoided and we successfully maintained an unrestricted service.

The high demand caused localised problems with low pressure which we overcame using our fleet of alternative supply vehicles (ASVs). From the end of May to the beginning of September our ASVs worked 24 hours a day to pump into the supply network and help maintain water pressure.

These intense hot and dry conditions had followed on from several weeks of freezing conditions during the 'Beast from the East' in March. Pipe movements caused by the frozen ground resulted in high levels of background leakage, and as the ground continued to dry out over the summer this exacerbated the issue further. Customer calls about leaks increased as they became easier to spot against the dry ground. In response to the rising levels of leakage we had already recruited additional leak detection and repair crews and by mid-July we were repairing 750 leaks a week with double the number of teams working 24 hours a day.

To minimise any impact on customers we invoked our Drought Management Plan which sets out a series of pre-agreed actions that must be followed once certain trigger levels are crossed in our impounding reservoirs.

This included pumping water from the south of our region through the West East Link Main to ease pressure on our key reservoir at Haweswater. We also carried out a number of capital projects to bring back into service borehole supplies that had not been used for many years. We increased communication with customers to ask them to use water wisely, through regional and national media, and we applied to the Environment Agency for drought permits so that we could increase levels of water abstraction.

Our mitigation plan continued through the winter – by March 2019 reservoir levels had recovered to normal levels and we met our leakage target.

“Intense hot and dry conditions followed on from several weeks of freezing conditions during the Beast from the East”

Our business model

Key resources and the impact of external drivers

Assets

Our network assets and treatment works are essential to delivering water and wastewater services to customers and protecting public health, and our energy assets enable us to generate energy, which helps reduce costs and minimise our environmental impact.

We are investing around £3.9 billion across the 2015–20 period, and we expect to continue with a substantial investment programme for the foreseeable future to meet increasingly stringent environmental standards and to maintain and improve our assets and services.

Impact of external drivers

Natural environment

We must build increased resilience into all our assets to cope with the anticipated impacts of a changing climate in the long term, including improvements to flood defences. Our assets must be prepared to continue to comply with increasingly challenging environmental constraints in areas such as water abstraction and wastewater treatment levels.

Economic environment

When making strategic investment decisions we must consider the impact on customers' bills and ensure we maintain affordability. A phased, long-term approach to address all of the concerns and interests of our many stakeholders, including environmental regulators, ensures that the necessary work can be delivered without the costs placing too much pressure on customer bills. For example, we have agreed to spread some of the environmental spend required by current legislation over the next 15 years.

Regulatory environment

Many of our assets are very long-term in nature, such as our impounding reservoirs that can last hundreds of years. Through our economic regulation framework we earn a return, received through revenue, based on a measure of the value of our capital asset base, Regulatory Capital Value (RCV). This mechanism allows us to share the cost of building these long-term assets between the generations that will benefit from them.

Our RCV is over £11 billion, but the gross replacement cost of our fixed assets (including all our reservoirs, treatment works and pipes), i.e. the estimated amount it would cost for another company to build similar assets and networks, is around £90 billion.

Stakeholders

Many of our reservoirs are areas of natural beauty and we permit the public to enjoy access to this land, bringing recreational and health benefits. Other assets, such as our wastewater treatment plants, are close to residential areas and we work hard to minimise odours and other impacts.

New infrastructure projects, such as our West Cumbria pipeline, can impact local communities and we go to great lengths to consult in the planning stage.

Political environment

UK government priorities, including those of the National Infrastructure Commission, will impact the planning of large infrastructure projects. We anticipate an increase in the North West's population of around one million by 2045 (more than the population of a large city such as Liverpool). We are planning to ensure our services and infrastructure are able to meet the needs of this growing population, including new connections and higher demand on our water and wastewater networks.

See page 46 for how we are contributing to the UN's Sustainable Development Goal to **'Build resilient infrastructure, promote sustainable industrialisation and foster innovation'**

Technology and innovation

It is important we have the right systems and procedures in place to monitor and control our assets efficiently and effectively. We embrace the opportunity that new technology and innovation presents. This is at the heart of our Systems Thinking approach.

The new Nereda process has transformed the wastewater treatment process, our use of robots in managing the water network has improved efficiency and customer service, and we are using drones to inspect assets with restricted access, which improves health and safety as well as reducing time and costs.

We use technology for renewable energy self-generation, for example our Davyhulme sludge recycling centre employs a groundbreaking configuration of thermal hydrolysis to maximise energy generation from sludge; and we built Europe's largest floating solar array on our reservoir in Godley, Greater Manchester.

Technological advances can give rise to new risks as well as opportunities. Cyber crime has been on the increase in recent years and, as the holder of customer information, is a threat we take very seriously.

Read more about our approach to **'Mitigating the risk of cyber crime'** on page 71

Management and measurement

Our asset management policy, available to all employees on our intranet, details how we will operate, maintain and invest in our assets with the aim of delivering our customer promises and associated outcomes, as agreed at the price review for the current regulatory period.

We monitor the condition and performance of our assets and assess the risk to service provision. Our proactive and reactive maintenance programmes, and focus on asset health performance measures, ensure we are managing our assets in the most efficient way. Our wholesale outcome delivery incentives, which feature as one of our operational KPIs, include measures of asset health such as the resilience of our impounding reservoirs and maintaining our wastewater treatment works.

The principal risks and uncertainties that relate to this key resource are 'Security risk', 'Water service risk', 'Wastewater service risk', 'Compliance risk', and 'Supply chain and programme delivery'.

Read more about **how we manage risk** on pages 68 to 76

Link to our strategic themes

The best service to customers

Maintaining and enhancing our assets is essential in order for us to provide the best service to customers. Since privatisation in 1989, we have invested billions in our assets and this has provided substantial benefits to customers, including reduced supply interruptions, reduced sewer flooding incidents, and improved water quality.

At the lowest sustainable cost

We manage our assets in a holistic way that seeks to minimise whole life costs, helping us deliver efficient total expenditure (totex) without compromising on quality of service or long-term resilience. This approach helps us to save future operating costs, reduce future customer bills, and continue to operate in a sustainable manner.

In a responsible manner

We are committed to managing and operating our assets in a way that continues to create long-term value for all our stakeholders. Effective capital investment helps us to meet increasingly stringent environmental standards, which helps to enhance the region's environment, improving bathing waters and protecting indigenous wildlife and habitats.

Our business model

Key resources and the impact of external drivers

People

We support thousands of jobs in the North West, including a growing graduate programme and we have been named one of the top 100 apprenticeship employers, helping to secure a legacy for the future in our region. We believe that the most effective decision-making comes from access to a diverse range of people with a broad set of viewpoints.

Fundamental to the performance we deliver is a skilled, engaged and motivated team of employees, suppliers and contractors. We provide comprehensive training and development opportunities for our employees. Competitive wages, benefits and long-term incentives have been shown to enhance quality of work, increase employee retention, and reduce absenteeism, as well as providing societal benefits. Employee retention also helps ensure efficient and effective training and higher levels of performance.

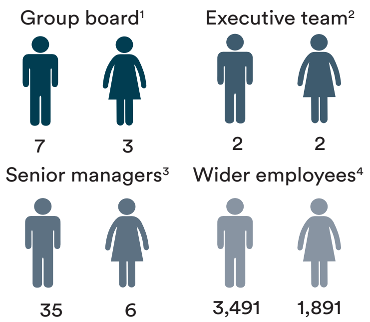
Impact of external drivers

Stakeholders

We are committed to protecting the health, safety and wellbeing of our people. This is fundamental to their welfare and to the reputation and performance of the company, and remains an area of focus as we strive for continuous improvement. We have implemented a number of initiatives over recent years to improve health and safety conditions for our employees, and have been awarded the workplace wellbeing charter.

We promote diversity and equal opportunity to drive a comprehensive and balanced skill set, and we recruit and promote employees on the basis of merit. Over the last few years, we have been striving to improve diversity across all types of role and all levels within our business. We established a Gender Equality Network in 2015 to provide role models, mentoring and opportunities. We target diverse shortlists and attraction campaigns for our apprentice and graduate schemes.

Women are represented at all levels of our company. Over a third of our combined board and executive team is female. See chart.



1) Group board as at 31 March 2019.
2) Executive team excludes CEO, CFO and COO, who are included in group board figures.
3) As at 31 March 2019, there were 11 male and 3 female employees appointed as statutory directors of subsidiary group companies but who do not fulfil the Companies Act 2006 definition of 'senior managers'.
4) Employees of each sex as at 31 March 2019.

Further information on **diversity** can be found on page 98

Applicants with disabilities are given equal consideration in our application process, and disabled colleagues have equipment and working practices modified for them as far as possible where it is safe and practical to do so.

See page 46 for how we are contributing to the UN's Sustainable Development Goal to **'Promote inclusive and sustainable economic growth, employment and decent work for all'**

Economic environment

The availability of skilled engineers depends on economic and social conditions. Our award-winning apprentice scheme and graduate programme help ensure we can continue to attract and train a high calibre of engineers, in a profession which has seen declining numbers in the UK in recent years. Our employees are paid a competitive base salary plus benefits and the opportunity to join the employee healthcare scheme and our share incentive plan.

We work with suppliers and contractors whose business principles, conduct and standards align with our own. Our key suppliers have committed to our sustainable supply chain charter. We support the appointment of a small business commissioner to investigate companies who do not treat suppliers fairly, are a signatory to the Prompt Payment Code, and will fully comply with rules on reporting payments to suppliers.

Technology and innovation

We have an embedded culture of innovation, and it is one of our core values. We encourage ideas from our people as well as from outside our business, both ad hoc and formally through programmes such as our annual CEO challenge.

Management and measurement

We measure employee engagement through an annual survey, and regularly achieve engagement levels higher than the UK norm. We monitor and measure employee performance through annual reviews, and employees at all levels of the company participate in the bonus scheme, so they benefit from company success. The bonus performance measures are the same for all employees as those for the executive directors, and can be found on page 132.

We maintain a comprehensive A–Z suite of policies, which are available to all employees on our intranet. Our policies on maternity, paternity, adoption, personal and special leave go beyond the minimum required by law. For disabled applicants, and existing employees, we are committed to fulfilling our obligations in accordance with the relevant legislation.

We convened a cross-company working group to draft our human rights policy statement and assess risks and potential impacts on our stakeholders. These are mapped to, and managed within, our corporate risk register. Our human rights policy can be found on our website, and this has links to other related policies including our modern slavery policy and slavery and human trafficking statement, and sustainable supply chain charter.

Read more at **unitedutilities.com/corporate/responsibility/our-approach/human-rights**

The principal risks and uncertainties that relate to this key resource are 'Health, safety and environmental risk' and 'Resource risk'.

Read more about **how we manage risk** on pages 68 to 76

Link to our strategic themes

The best service to customers

Our employees and our supply chain act as the face of our business, and therefore are a crucial part of delivering the best service to customers across our entire business. Customer focus is one of our core values that we encourage our people to live by, and we recognise great customer service from individuals, such as through participation in the WOW! Awards.

At the lowest sustainable cost

Comprehensive training and development opportunities for our employees help to improve our internal skills base and therefore quality of work at an efficient cost, as well as creating a more engaged workforce. Management has a range of incentives that focus on performance over a number of years, rather than just the current year, to encourage the delivery of benefits over the longer term.

In a responsible manner

We work with schools, including encouraging the next generation of women into science, technology, engineering and mathematics careers, and with our supply chain partners to give young people not in education, employment or training the chance to gain hands-on experience and basic skills training in the workplace. We are a signatory to the Prompt Payment Code for our suppliers.

Creating a healthy workplace

Working hard to improve the wellbeing of our employees

In January we were named one of Britain's Healthiest Workplaces 2018, following the largest and most comprehensive workplace wellbeing survey in the UK.

Britain's Healthiest Workplace 2018 incorporated data from 129 organisations and 26,432 employees, and ranked United Utilities as the third most improved organisation. The award recognised our increased efforts over the past four years to improve the wellbeing of our employees. This includes helping employees quit smoking, offering discounted gym membership, nutritional programmes, and training mental health champions and first aiders.

In 2018 we were reaccredited with the Workplace Wellbeing Charter, reflecting our continued commitment to health and wellbeing. We fully met 90 of the 95 standards set out in the charter, which are based on best practice, research and commercial benefit.

We picked up two employee wellbeing accolades at the Reward and Employee Benefits Association (REBA) awards. We won the award for Physical Wellbeing for our "superb reductions in inactivity rates" among employees, made possible by initiatives including standing desks and walking meetings. At our Warrington headquarters we have an onsite gym, health kiosks so staff can accurately measure their weight and blood pressure, incentives for employees who stay smoke-free for six months, and we organised activity challenges including a Mighty Hike, Billion Step and Walking Home for Christmas.

We won the prize for Best Mental Wellbeing, for a company with 5,000 employees or more, for identifying specific issues in our workforce, setting out a clear approach to building a supportive culture, and for putting good data analytics in place to measure progress. The judges praised our 'mental health selfies' as an excellent way of encouraging staff to engage with their own mental wellbeing, and were impressed by the support network we have built for mental health first aiders.

In May 2018 we joined other businesses, including Barclays, PwC and BNFL Sellafield, along with football clubs and mental health charities in an initiative aimed at ending the stigma of talking about mental health in the workplace. 'This is Me' launched in Manchester to coincide with the start of Mental Health Awareness Week. The campaign challenges the stigma around mental health at work aiming to break the culture of silence by supporting people to tell their own personal stories.

Approximately one in four people in the UK experience a mental health problem each year. As a responsible business, we have an obligation to get involved and take an active interest in the wellbeing of our staff and create an environment where those in need can get help and support.

"In 2018 we were also reaccredited with the Workplace Wellbeing Charter"

Our business model

Key resources and the impact of external drivers

Financing

As a result of the long-term nature of our assets and the need to spread the cost between the generations of customers that benefit from them, it is necessary to raise financing in order to fund this investment.

We adopt a prudent approach to managing financial risks, with clear and transparent hedging policies, and our debt portfolio has a very long average life. We maintain a robust and sustainable capital structure, balancing both equity and debt financing, which helps us maintain a strong and stable investment grade credit rating. This enables efficient access to the debt capital markets across the economic cycle, long-term financial resilience, and reduces our exposure to fluctuating market conditions and regulatory changes.

Impact of external drivers

Economic environment

Changes in economic conditions and financial markets can influence our ability to create value through financing. We mitigate some of the impact through our financial hedging strategies, including our approach to hedging inflation and interest rates.

Interest rates have been comparatively low in recent years, and through our interest rate hedging policy we have progressively locked in these lower rates on our debt portfolio, benefiting our future cost of debt.

Our revenue and regulatory capital value (RCV) are linked to RPI inflation during the current regulatory period. Our inflation hedging policy aims to maintain around half our net debt in index-linked form (where it is economic to do so), as this provides a partial economic offset for our inflation exposure. Periods of lower inflation mean lower growth in revenue and the RCV, but also lower finance costs, and the reverse is true in periods of higher inflation.

Market sentiment can impact our financing. While much of this can be outside of our direct control, we can help inform and influence investor opinion through regular engagement.

Regulatory environment

Our ability to raise efficient financing at a cost cheaper than many of our peers provides the potential to outperform the industry-allowed cost of debt, and we have a long track record of aligning our financial risk management policies with the regulatory model.

We maintain an appropriate level of gearing, measured as net debt to regulatory capital value (RCV), within a target range of 55–65 per cent, which is broadly in line with regulatory assumptions for the ‘notional company’.

Our inflation hedging policy aligns with the current RPI-linked regulatory framework, and we have evolved our policy and began introducing CPI-linked debt in line with Ofwat's transition towards CPIH inflation for the 2020–25 period. We issued the first ever CPI-linked notes by a UK utility in 2017 and have continued to increase our CPI exposure where there are good relative value opportunities, but we expect our index-linked debt to remain mostly in RPI-linked form until CPI or CPIH debt and swaps become available in sufficient size at an economic cost.

Our interest rate hedging policy is to fix nominal debt out to 10 years on a reducing balance basis, reducing our exposure to market fluctuations while managing uncertainty in Ofwat's approach to setting the cost of debt at future price reviews. For 2015–20 we also substantively fixed all our nominal debt to the end of the period once the cost of debt was known, but we will not do this for 2020–25 as a result of Ofwat's introduction of indexation on new debt.

Stakeholders

As a FTSE 100 listed company, we have open and transparent reporting around all of our equity and debt financing arrangements, which helps to build trust with long-term investors as well as our regulator.

We have proactive engagement programmes with equity and debt investors, through which we update them on developments in our business and seek their views, which we consider in our strategic planning.

Technology and innovation

New innovative ways of raising finance often emerge, for example accessing pockets of untapped investor demand via our Euro Medium Term Note (EMTN) programme, CPI-linked financing, and green bonds have become more prevalent in recent years. We monitor and assess these developments and continue to maintain access to a broad and diverse range of sources of finance in a number of markets, across which we seek the best relative value when issuing new debt.

Management and measurement

We have clearly articulated financial risk management policies, covering credit, liquidity, interest rate, inflation and currency risk.

Read more about our **financial risk management policies** on pages 190 to 197

We maintain relationships with a diverse range of banks, and we periodically refresh our EMTN programme to enable efficient debt issuance under pre-agreed contractual terms. The board delegates authority to the CFO, allowing us to respond quickly to attractive financing opportunities.

We aim to avoid a concentration of refinancing in any one year, and fund long-term where possible. We monitor liquidity forecasts, with a policy of having available resources to cover the next 15–24 months of projected cash flows to ensure forward funding needs are met.

As part of our planning process, we review key credit ratios against required thresholds for our target credit ratings. Performance against these ratios is regularly monitored, and we maintain relationships with the credit rating agencies to understand methodology changes.

The principal risk that relates to this key resource is ‘Financial risk’.

Read more about **how we manage risk** on pages 68 to 76

Link to our strategic themes

The best service to customers

Customers benefit from receiving service improvements earlier as a result of our ability to pre-fund investment in long-term assets, and keeping finance costs down helps us to ensure bills remain affordable. The financial resilience we build through our financial risk management helps to ensure we can continue to provide great service long into the future.

At the lowest sustainable cost

Locking in long-term debt and swaps at good relative value helps keep our finance costs low, and we monitor liquidity and headroom regularly to maintain adequate funding. Our approach and financial risk management reduce our risk exposure and help ensure the sustainability of our ability to efficiently finance our business.

In a responsible manner

Our environmental, social and governance performance and robust capital structure give equity and debt investors confidence in the long-term sustainability of our business, which reduces their investment risk. We do not use offshore financing vehicles, and our open and transparent reporting is trusted by Ofwat who rated us ‘self-assurance’ three years in a row.

Introducing artificial intelligence to our network

Using self-learning technology to bring to life the benefits of Systems Thinking

We are the first water company in the UK to introduce large-scale artificial intelligence into operational systems.

Every day we pump water from our service reservoirs to customers. The calculation of pump schedules (when to turn pumps on and off) is manually intensive and requires skilled analysts for several hours a day. This manual process cannot cope with the many variables required to make balanced decisions, and energy use is too complex to calculate manually. Our water leadership team recognised the need to find a better solution and this was set as one of the challenges in our Innovation Lab.

We worked with a Canadian start-up company, EMAGIN, through our Innovation Lab last year to apply HARVI (Hybrid Adaptive Real-time Virtual Intelligence), a real-time analytics dashboard, to our water network pump scheduling.

HARVI uses artificial intelligence and machine learning to assess vast amounts of data on a wide range of factors such as weather, demand for water, pump performance and electricity prices.

This is used to help our system operators make decisions on the most cost-effective and efficient way to run water pumps, detect burst pipes and minimise the risk of discoloured water.

We tested this innovative technology in Oldham, Greater Manchester – one of the 33 zones in our region. Oldham was chosen as we needed a test site that was large enough to deliver real benefit to customers, had an identified opportunity for delivering further efficiencies, and already had Systems Thinking capability. Oldham District Metered Zone produces 55 mega litres of drinking water a day for over 180,000 domestic customers, has Systems Thinking capability by way of remote monitoring and control technology, and is one of our high energy intensive zones. In the 12-week trial, taking into account the optimum times to pump water across our network, HARVI demonstrated it could achieve energy savings of 22 per cent.

Water networks are complex systems, and technology like this is going to play an integral role in the further development of our Systems Thinking approach, helping us make more sense and better use of large amounts of data. It will also free up our people to be more proactive, which will have a direct impact on levels of service for customers. Water companies need to be thinking in this way and embracing new technology if we are to meet customers' expectations on value and reliability.

HARVI has shown huge potential to help reduce our operational costs through the Innovation Lab pilot phase. We are now working with EMAGIN to develop a plan to roll this technology out in phases to the rest of our water network.

> "HARVI has shown huge potential to help reduce our operational costs"

Our business model

Internal drivers

Systems Thinking

Our pioneering approach to operating our business, which we call Systems Thinking, is one of our competitive advantages and we set out more detail on this on page 17.

Systems Thinking is one of the main drivers of the operational performance improvements we have delivered in recent years, as well as helping us achieve significant cost savings.

We have embedded this way of thinking throughout our business, to put in place the telemetry backbone across our network, to gather and analyse data, and to set up our Integrated Control Centre (the 'digital brain' of our network) to remotely monitor and control our assets from our head office. This time and investment has given us a significant advantage.

The best way to demonstrate what Systems Thinking means in practice and the benefits it delivers is to give detailed operational examples.

Since 2015, we have included business insights in each year's annual report covering our integrated control centre, our network sensors and telemetry backbone, our system-wide approach to sludge treatment, and our use of artificial intelligence to deliver advanced water network management.

This year, read more on page 35 about how we are rolling out artificial intelligence across our entire water network through a platform that can assess vast amounts of data on a wide range of factors such as weather, demand for water, pump performance and electricity prices. This was an idea developed through our Innovation Lab, and helps make decisions on the most cost-effective and efficient way to run water pumps, detect burst pipes, and minimise the risk of discoloured water.

Governance and risk management

Good governance lies at the heart of all successful organisations and leads to better management decisions. We strive to operate in a manner that reflects the highest standards of corporate governance, accountability and transparency. Our company structure and governance standards are designed to ensure our board continues to observe sound and prudent governance in compliance with the UK Corporate Governance Code.

Read more about our approach to governance in our **Governance report** on pages 80 to 144

Our board members have diversity in terms of experience, skills and personal attributes, and in terms of age, gender and ethnicity, helping to bring a breadth of views in considering strategic decisions and priorities.

We have an anti-bribery policy that all our employees must follow, and processes in place to monitor compliance with the policy. We operate an independently provided, confidential reporting helpline and web portal for employees to raise matters of concern in relation to fraud, dishonesty, corruption, theft, security and bribery, and all claims are fully investigated. Our audit committee has oversight of the policies and procedures in relation to anti-bribery and fraud.

Our anti-bribery policy is available to view online at: **unitedutilities.com/corporate/about-us/governance**

Our employees and representatives of our suppliers must comply with our sustainable supply chain charter. This explains that we will not tolerate corruption, bribery or anti-competitive actions, and we expect our suppliers to comply with applicable laws and regulations and, in particular, never to offer or accept any undue payment or other consideration, directly or indirectly, for the purposes of inducing any person or entity to act contrary to their prescribed duties.

Given the complex legal and regulatory environment within which we operate, and the critical nature of our infrastructure and service provision, we are exposed to a broad variety of risks. Mitigating exposure to potential risks helps us improve our resilience.

Accepting some level of risk is a normal and necessary consequence for a commercial organisation in order to run the business in a cost-effective way. However, as you would expect of the provider of an essential service, we adopt a prudent approach to managing risks to our business.

See pages 68 to 76 for what we consider to be **our principal risks and uncertainties**, and how we manage and mitigate these

Values and culture

Our core values of customer focus, integrity and innovation start at the top and cascade through all levels of our business. They are interrelated – innovating to improve our services and acting with integrity in the way we conduct our activities helps us to continually improve customer service.

Customer focus

We have instilled a customer-centric approach right across our organisation, and this has been a key driver of the major improvement in customer service. Putting customers at the heart of what we do has helped deliver benefits for shareholders and wider stakeholders.

Integrity

Acting with integrity, both at board level and as a company, underpins our approach to responsible business and building trust. We actively encourage our employees to express their opinions and ideas through various engagement and social channels, such as our employee engagement surveys, intranet, and social media collaboration tool 'Yammer'.

Innovation

Innovation is a critical enabler in creating value. We welcome new ideas and technologies from all levels of our business with employees given the opportunity to develop and present ideas to senior management, from our supply chain, and from industries across the world, including via our Innovation Lab, as detailed on the next page.

See how our core values underpin our strategic themes and contribute towards delivering our purpose and working towards our vision on page 15.

The culture of our company is a combination of our values, attitudes and behaviours, manifested in our operations and relations with all our stakeholders.

Read more about **how we create value for stakeholders** on pages 39 to 46

See how we are contributing to the UN's Sustainable Development Goal to 'Promote just, peaceful and inclusive societies and institutions' on page 46.

The United Utilities way of doing things is to behave as a responsible business and is set out in our 'Business Principles' document, which can be found on our website at: **unitedutilities.com/corporate/about-us/governance/business-principles**

Read more about our board's approach to **values and culture** on page 92 and 93

Accelerating the drive for new ideas

Running our Innovation Lab is helping us find new ways of improving services

Water companies have been challenged to push the boundaries of 'business as usual' during the price review process for the next regulatory period. To deliver more for less, we have to do things differently.

The biggest challenge is how to find new innovations when, historically, it has been difficult for new entrants to implement their ideas in the water industry. Our procurement processes are set up to define the scope of the services we want very precisely, which can be counterproductive to creativity. To address this, last year, we ran the UK water industry's very first Innovation Lab, working with technology accelerator partner L Marks.

Our first challenge was to loosen the procurement constraints. We used EU Innovation Partnership Procedure legislation to develop a revolutionary new procurement framework for the industry, which won the Utility Week award for Supply Chain Excellence. This allowed us to procure ideas rather than specific services. The Innovation Lab did not look for fully formed new services or technologies. We were clear from the outset that we wanted ideas that could be nurtured and co-created with and for the water industry.

We defined five areas where we had identified a challenge in need of a solution:

- **Connected customer:** such as smart devices and 'Internet of Things' – water is lagging behind other utilities in this area.
- **Proactive customer:** providing better and more timely updates for customers when they need to hear from us.
- **Predictive asset maintenance:** finding less invasive ways to monitor performance of our assets without needing to dig them up or switch them off.
- **Safe and healthy worker:** protecting our employees when they are working alone, at night, or in dangerous locations.
- **Future of water:** this final category was intended to be a 'catch all' to attract ideas, however radical, that could have applications for the water industry.

The Innovation Lab provided a safe, supportive environment for the shortlisted suppliers to access our sites, data, systems, experts and experienced senior employees. It helped foster a culture where we work together to bring these ideas to fruition.

We advertised the Lab to some 1,500 fledgling, small and large businesses and received applications from 80 organisations. We narrowed that down to a shortlist of 22 ideas from UK and international applicants. Seven finalists joined us at our head office for an intensive 10-week Lab process. Five of these suppliers were new entrants to the UK water sector.

So far, we have signed contracts with three of the suppliers. UK-based firm Typhon is installing a power-efficient LED UV system for water treatment. Canadian firm EMAGIN is rolling out its artificial intelligence platform HARVI to all of our water pumping stations across the North West. Manchester-based Datatecnics is rolling out its intelligent pipe system that uses printed electronics and artificial intelligence to report pipe integrity and predict pipe failures.

This process has proved so successful for finding and proving new innovations that we are repeating it. We launched our second Innovation Lab in April 2019 to find more great ideas that we can co-create with their originators for the benefit of our company, our customers and other stakeholders, and the water industry as a whole.

"The process has proved so successful for finding and proving new innovations that we are repeating it."

Business insight

Alerting communities to what not to flush

Local campaign delivered dramatic results in drive to reduce sewer flooding

Every year there are 25,000 sewer blockages across the North West and around 1,000 homes and 6,000 gardens are affected by sewer flooding.

Things like wipes and nappies do not just disappear down the u-bend and dissolve, they clump together and can cause havoc in the sewers, causing distress for people whose homes and gardens have been flooded by blocked sewers.

As well as blocking sewers, many of these items can end up in our rivers and on our beaches, which has far-reaching impacts on nature and the environment.

In 2018 we trialled a new community-focused approach to reducing sewer flooding in Burscough, Lancashire, an area with flooding issues mainly due to sewer blockages caused by wet wipes.

For a six-month period, our customer team went out and about meeting customers and working with the community to spread the message about what not to flush and showing them how we can all do our bit to help.

The campaign delivered excellent results, with an impressive 90 per cent reduction in wet wipes and other non-flushable items entering our sewers.

As part of the campaign we:

- Sent a ‘Burscough Better Together’ leaflet to 6,000 residents in the area;
- Held a number of events in supermarkets, a Christmas fayre, and a heritage weekend in the summer;
- Engaged with local children by holding ‘Mad Science’ assemblies in primary schools and a talk at the village holiday club;
- Visited food outlets to talk to owners about their methods of dealing with fats, oil and grease;
- Provided local nurseries and baby groups with potty training packs containing advice and information about not flushing wipes;
- Placed adverts in local magazines about the importance of not flushing wet wipes; and
- Worked closely with other agencies, such as West Lancashire District Council and the Environment Agency, to discuss local flooding issues and future developments in Burscough.

Our network teams carried out regular cleaning across the area and looked at ways to reduce the risk of further flooding.

The Burscough project worked so well that we are planning to roll it out to other problem areas, engaging with customers and communities to help change behaviours around ‘what not to flush’.

> “In 2018 we trialled a new community-focused approach to reducing sewer flooding”

How we create value for stakeholders

Identifying who our stakeholders are and engaging to understand what matters to them helps enable us to create long-term value

Why stakeholder engagement matters

Our purpose is to provide great service to customers and communities in the North West, creating long-term value for all of our stakeholders. To create this value, it is important to understand our stakeholders and what matters to them.

The provision of water and wastewater services creates a deep connection between the company and the communities we serve. Our work generates value for the North West economy, for example through job creation and delivering environmental improvements, which underpin the region's tourist economy.

We rely on shareholders to finance our activities, and we agree commitments with economic, quality and environmental regulators about what we will deliver within given time frames.

Politicians and the media can influence our priorities and the perceptions of our stakeholders. During the year there has been increased focus on the water sector, from several perspectives including corporate governance, resilience and levels of leakage.

We recognise that we do not operate in isolation and it is not our decision alone to determine what the region needs us to deliver. This is why it is essential we engage with stakeholders across the North West, so we can identify shared solutions to shared challenges.

Understanding what matters to stakeholders will only be achieved by building strong, constructive relationships and engaging regularly. We value the diverse perspectives that a broad range of stakeholders, representing different and often competing interests, can bring to our decision-making.

The relationships we build are subject to robust governance to ensure the insights generated are taken into account in decision-making at executive and board level. Read more on page 152. This is important to building trust. The board's corporate responsibility committee meets four times a year and stakeholder engagement is one of its standing agenda items. The chair of the independent customer challenge group, YourVoice, attends board meetings to provide its perspective.

The following pages detail how we engage with, and are influenced by, each of our key stakeholder groups, and the value we create for them. Our analysis of what matters most to stakeholders, and how these issues affect our ability to create long-term value in line with our purpose statement, is set out in our material issues matrix on page 45.

How we create value for stakeholders

Shareholders

How we engage with and are influenced by shareholders

It is important that shareholders have confidence in the company and how it is managed, given their investment in the business. By providing updates on our strategy and performance, we can assist in their understanding and decision-making. Similarly, engagement with shareholders gives us a broad insight into their priorities, which influences our own decision-making and our strategic direction.

Through our investor relations programme, we actively engage with shareholders and sell-side analysts who write research reports on our company and industry. Details of this can be found on page 99. Regular engagement activities are supplemented by ad hoc events, such as the webcasts held this year in relation to the price review process for the 2020–25 period. We complete several investor-led indices on environmental, social and governance matters, such as the Dow Jones Sustainability Index.

Top three material issues for shareholders*

- Customer service and operational performance
- Political and regulatory environment
- Financial risk management

Customers

How we engage with and are influenced by customers

To deliver a great service in a way that customers value, we need to listen and engage with them in building new solutions. We engage with customers through a variety of channels, including webchat, text and social media. We get feedback on customer interactions every day, and conduct more detailed weekly research on key themes that are important to them. We have changed how we communicate and deliver services based on customer feedback, such as the introduction of our customer app and redesign of customer bills. Our business plan for 2020–25 was shaped by unprecedented levels of customer engagement.

Read more on pages 19 to 23

The independent customer challenge group, 'YourVoice', aims to ensure customers are at the heart of our business planning engagement, and the Chair regularly attends our board meetings. YourVoice continues to provide challenge and critical support on our delivery of commitments for the 2015–20 period as well as contributing to our business plan for 2020–25.

Top three material issues for customers*

- Customer service and operational performance
- Affordability and vulnerability
- Leakage and water efficiency

Communities

How we engage with and are influenced by communities

Our work puts us at the heart of local communities, places where customers and employees live and work. When communities come together, whether that is around a particular issue or location, they can often make powerful representations to the company. We seek to develop strong relationships based on mutual trust, respect and an understanding of the impact our work has on everyday lives. We play a constructive role in tackling issues through engagement and investment, and by identifying the water-related issues that matter most to communities we can develop solutions in partnership with them.

We engage through facilitated workshops and community partnerships, such as the North West Hardship Hub to help customers in vulnerable circumstances. Read more on page 57. Issues raised by communities can present opportunities to improve what we do or to help others, while others can be complex and difficult to handle, with competing interests between different stakeholder groups, and require time and effort to work through.

Top three material issues for communities*

- Land management and access
- Community investment
- Trust, transparency and legitimacy

* Read about how we manage our material issues on page 45

Strategic themes

- Best service to customers
- At the lowest sustainable cost
- In a responsible manner

Material issues

- External factor
- Internal factor
- Both an external and internal factor

How we create value for shareholders

Short-term

- Since many of our shareholders are pension funds, charities and employees, the income we provide through dividends is relied on by millions of people every year
- We are committed to high ethical standards of business conduct, strong corporate governance and acting with integrity so shareholders can have confidence in the way we do business
- We maintain a high level of quality and transparency, enabling shareholders to have trust and confidence in what we report. This was recognised by Ofwat, which has rated us in its top 'self-assurance' category three years in a row

Long-term

- Our shareholders have placed their money into our business as a long-term investment and we provide an appropriate sustainable return through a combination of short-term dividend income and long-term growth
- We plan far into the future and invest in our infrastructure to ensure the sustainability of the business and the services we provide
- We manage risk prudently so shareholders can have confidence in our stability and resilience in the round
- Our innovation culture drives continuous improvements, enabling us to be at the frontier of our industry and ahead of peers

Link to strategic themes

Our regulatory return varies dependent on our performance for customers, aligning shareholders' interests with delivering the best service to customers

By reducing costs in a sustainable way through innovation and efficiency, we can target outperformance of our allowed expenditure in the long term without compromising operational performance

Our strong corporate governance, prudent risk management, and clear and transparent reporting help create a lower risk investment and build trust

How we create value for customers

Short-term

- We focus on delivering a reliable service so customers can simply get on with their lives and not have to worry about their water and wastewater services
- When they do need to contact us, we provide a helpful service, talking and listening to customers so we can understand and meet their expectations
- We maintain bills that are good value for money through innovation and efficiency
- Where customers are struggling with affordability and vulnerability, we provide tailored support through Priority Services and payment assistance schemes

Long-term

- Our water and wastewater services make a major contribution to the long-term health and wellbeing of customers in our region
- Through long-term financing and the regulatory framework, we are delivering multi-million pound infrastructure projects, to improve our services and resilience for the long term. We ensure the cost of this is shared fairly and affordably between those that benefit now and in the future
- We focus on earning the trust of customers, for example by keeping personal details safe and through transparent reporting, to ensure they can have complete peace of mind

Link to strategic themes

Engaging with customers helps us understand what they value most so that we can target our services accordingly

By achieving sustainable cost reductions we can provide an efficient service, keeping bills low and enabling us to help vulnerable customers

Customers value a company they can trust, and they care about protecting vulnerable people in society. They value the support we provide through our many assistance schemes

How we create value for communities

Short-term

- We look after beautiful landscapes and beaches and open our land to the public, which supports the regional tourism industry and gives communities the health and wellbeing benefits through access to relaxation and recreation
- We encourage employees to volunteer on projects that address local issues, helping to create better places and stronger communities
- Working in partnership with others means we can accomplish more together to tackle mutual issues, such as partnering to develop employability skills for those who need it most

Long-term

- The health and wellbeing benefits through our provision of access to nature for recreation and relaxation helps reduce the burden on health services
- We make a significant contribution to the regional economy through our activities, the people we employ, and the money we spend in our supply chain
- We work with teachers and children to raise awareness about water and the natural environment, giving the next generation an understanding of the true value water brings and how we can all play our part in protecting the services nature provides

Link to strategic themes

Customers live and work in the local communities we serve and so they value the work we do to tackle issues together

By operating at the lowest sustainable cost we are able to continue investing in local communities for the long term

As they encompass a breadth and depth of people, communities bring a variety of views and issues to our attention, helping us find the most balanced approach in the best interests of all

How we create value for stakeholders

Employees

How we engage with and are influenced by employees

Our employees are the face of the company and we could not deliver our services without them. It is essential we build productive relationships based on trust, develop our employees and keep them engaged and motivated so we can meet the stretching objectives we set ourselves. Employees know our business better than anyone, with a diverse range of views and experience, making them well placed to identify opportunities for improvement.

We have a highly engaged workforce who take pride in their work, value opportunities to learn new skills, and maintain an open and honest dialogue with unions and the business. Line managers play a vital role in supporting employees, with regular one-to-one meetings, and our engagement survey regularly scores above the UK norm. Our new 'employee voice' will ensure their perspective is heard by the board. We have employee-led networks such as for gender, LGBT and disability, and encourage employees to share innovative ideas via many forums.

Top three material issues for employees*

- Health, safety and wellbeing
- Diverse and skilled workforce
- Employee relations

Environment

How we engage with and are influenced by the environment

We rely on the environment as one of our key resources so it is important for the sustainability of our business that we protect and enhance it. For example, climate change will affect how much water is available and stakeholders are concerned about the resilience of supplies and look to water companies to adapt and take the necessary steps to reduce flood risk.

Given the environment has no voice of its own, we engage with interested groups such as environmental regulators, non-governmental organisations, customers and communities. We conduct facilitated workshops with stakeholders to understand their priorities and have undertaken a large number of customer research projects. We work with environmental partners across the North West to identify new ways to deliver improvements, and engage with several groups to explore opportunities to deliver shared environmental outcomes.

Top three material issues for the environment*

- Resilience
- Environmental impacts
- Climate change

Suppliers

How we engage with and are influenced by suppliers

As well as employees, we rely on suppliers to deliver our services, and the availability of goods and services in the market influences our strategy and how we operate. Good relationships with suppliers help ensure projects are delivered on time, to good quality, at efficient costs, and can bring innovative approaches and solutions that create shared value.

We engage through supplier workshops, including targeted sessions on innovation, and suppliers sign up to our sustainable supply chain charter and support the commitments set out within it, as they recognise the importance of acting responsibly. They often suggest new ways we can meet some of our own responsible business targets. Feedback from suppliers revealed it can be difficult to access the company, especially when they have new products and services that could help us be more efficient and deliver better service. We established our Innovation Lab to help address this issue.

Read more on page 37

Top three material issues for suppliers*

- NW regional economy
- Responsible supply chain
- Human rights

* Read about **how we manage our material issues** on page 45

Strategic themes

- Best service to customers
- At the lowest sustainable cost
- In a responsible manner

Material issues

- External factor
- Internal factor
- Both an external and internal factor

How we create value for employees

Short-term

- We have a strong focus on health, safety and wellbeing. We firmly believe that nothing we do is worth getting hurt for, and we aim to ensure all employees go home safe and well at the end of the day
- We invest in training and development to enable our employees to grow their skills and to help keep them motivated
- Listening to our employees helps create an engaged workforce, increasing job satisfaction, and through employee communications and conferences we update our people on business developments so they feel part of a team

Long-term

- Looking after the health, safety and wellbeing of our employees in the short term, by encouraging them to lead fitter and healthier lives and work in ways that reduce accidents, creates long-term health benefits which, in turn, reduces the burden on healthcare services
- Health, safety and wellbeing extends to mental as well as physical health, and we promote awareness of stress and other mental health issues, promoting an all-round healthy lifestyle in the long term
- We provide pension offerings that help support employees in later life

Link to strategic themes

Well-trained, engaged and motivated employees who take pride in their work have the ability and drive to deliver the best service to customers

Encouraging innovative ideas from employees can lead to cost reductions, and improving employee satisfaction reduces turnover which ensures training and development costs are efficient

We take a responsible approach to protecting the health, safety and wellbeing of our employees

How we create value for the environment

Short-term

- We meet increasingly stringent environmental consent levels, which help to improve the quality of rivers and bathing waters and so support tourism in the region
- We manage our land in a way that safeguards habitats for indigenous wildlife, as well as protecting wildlife that makes its home in rivers and other water bodies
- We have invested in new infrastructure, such as our West East Link Main, to allow us to transfer water around the region more efficiently to avoid depletion of individual water sources

Long-term

- Our investment in renewable energy generation is reducing our carbon footprint and contribution to climate change
- We innovate and invest in new technologies to solve environmental challenges for future generations
- We are working on campaigns to educate the public and younger generations on water usage to protect this valuable resource and reduce usage over time
- We plan far ahead to ensure our activities and investment enhance the long-term resilience of the environment

Link to strategic themes

Customers care about the environment so providing the best service to customers involves protecting the places they live and love

Many of the ways we protect the environment also help us reduce cost, for example renewable energy generation reduces our energy costs as well as our carbon footprint

We manage water and wastewater in a responsible way that protects the environment and enhances its resilience

How we create value for suppliers

Short-term

- We spend significant amounts with our suppliers each year to help deliver maintenance and enhancement projects across our asset base, and this helps support thousands of jobs in our region
- By investing in our infrastructure we are helping to keep the economy flowing. We generate jobs through our capital programme and provide income for workers in the region
- While our operations and suppliers are mainly UK and European, they work closely with us to address human rights, in particular modern slavery

Long-term

- Supporting jobs through our supply chain in the short term catalyses the development of skills and jobs in the North West, providing a stimulus to benefit the regional economy in the long term
- Working together to develop innovations and new technologies means we can identify solutions that will make our services better in the future
- We act with integrity, giving suppliers confidence in the way we do business, which translates to transparency and fairness for our suppliers

Link to strategic themes

Working on our behalf, suppliers are a face for our business. Ensuring they are motivated to deliver good quality work is enormously important to us when delivering the best service to customers

Ensuring our suppliers deliver efficient cost is integral to delivering a sustainable low cost for customers, and the shared value of developing innovations together with suppliers can assist with this

Working with responsible suppliers helps us achieve more and succeed together in tackling environmental and social issues

How we create value for stakeholders

Politicians

How we engage with and are influenced by politicians

Politicians influence the long-term national water strategy and environmental priorities, as well as other matters that affect how all businesses operate. Engagement with national and local government, as well as elected representatives and devolved administrations, on topics of public interest helps us to understand their issues so we can seek solutions to shared environmental, social, economic and governance issues.

We engage with regional and national politicians in different political parties on topics of shared interest. We play an active role in trade association Water UK.

Top three material issues for politicians

- Political and regulatory environment
- Leakage and water efficiency
- Trust, transparency and legitimacy

Regulators

defra
Department for Environment Food and Rural Affairs

Environment Agency

OFWAT

dwi

WATRS
Water Redress Scheme

NATURAL ENGLAND

CONSUMER COUNCIL FOR Water

How we engage with and are influenced by regulators

Through proactive, constructive engagement with economic, quality and environmental regulators, we agree to deliver commitments over specified time frames. Read more about our regulatory environment on page 16. We actively engage to shape the policy and regulatory framework within which we operate, covering customer, economic, environmental, social and governance matters. These priorities need to be balanced and viewed over a long-term horizon and maintaining relationships is key to this. The priorities and objectives of regulators can change over time so active engagement to provide our perspective around future policy is important to us.

We hold regular meetings with all our regulators, including working on joint projects such as Natural Course, which aims to build capacity to protect and improve the North West water environment.

Read more at naturalcourse.co.uk

Top three material issues for regulators

- Political and regulatory environment
- Resilience
- Trust, transparency and legitimacy

Media

How we engage with and are influenced by the media

The media is intrinsically linked with all our other stakeholders, being influenced by the issues that matter to those stakeholders as well as influencing them through what it reports. It is through the media, and increasingly its social media platforms, that many of our stakeholders receive their information about us and our activities.

Given the essential nature of our services, it is important that coverage is fair, balanced and accurate, and this requires effective two-way dialogue between the company and the media. This is achieved through proactive engagement by our media team, which is available 24/7, providing content to media outlets, as well as dedicated resources to drive proactive messaging on social media channels.

Top three material issues for the media

- Political and regulatory environment
- Leakage and water efficiency
- Social media

Material issues External factor · Internal factor · Both an external and internal factor

Managing our material issues

Our approach to materiality

Understanding what matters most to our stakeholders is a fundamental part of our planning and day-to-day service delivery. We consider these stakeholder priorities alongside our own assessment of what has the biggest impact on the company and its ability to create value, and the output is presented in the material issues matrix below.

This stakeholder materiality assessment informs decisions about what we report in documents such as this Annual Report. Setting out issues in this way helps ensure we understand key stakeholder priorities and consider their interests in strategic decision-making, helping us create long-term value.

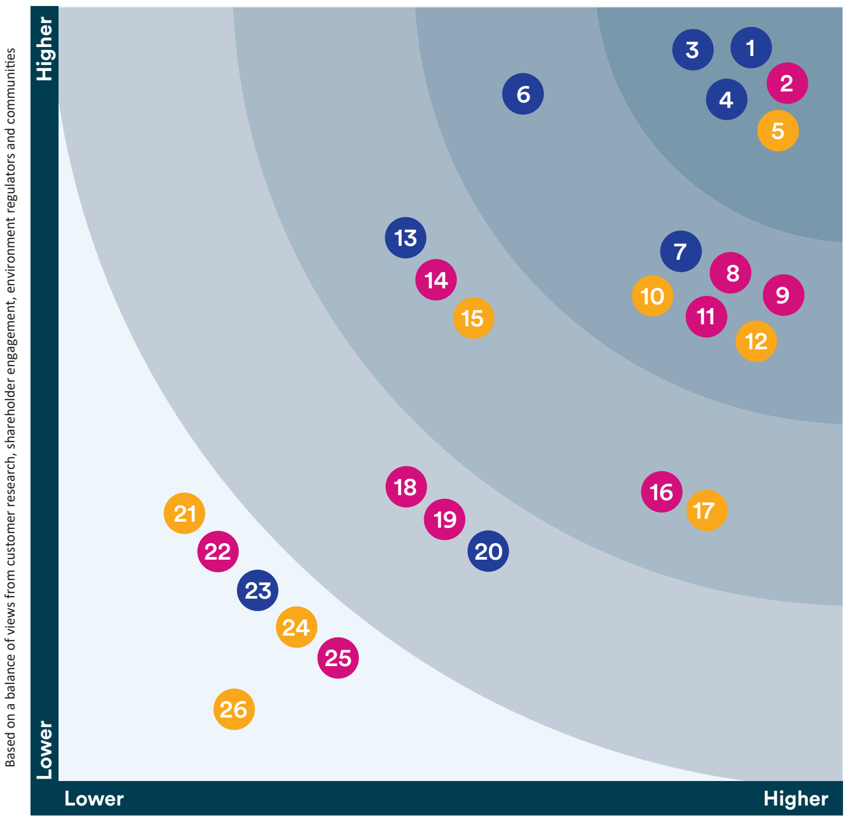
In defining the strategic relevance of an issue to the company, we have adopted the integrated reporting framework definition of materiality, which states: “A matter is material if it could substantively affect the organisation’s ability to create value in the short, medium or long term”. Value, in this context, may be created internally (for the company, shareholders and employees) and there can be external value (for customers, communities, suppliers and the environment). Value may also be financial or non-financial.

Our assessment of the level of interest to stakeholders is based on a balance of views obtained from customers, shareholders, regulators, communities, and subject matter experts from the company on an ongoing basis, as well as the extensive insights gathered for the regulatory price review process.

We have cross-referenced and aligned these issues with our principal risks and uncertainties, and our approach was reviewed by responsible business consultancy Corporate Citizenship, which commented that “alignment with UU’s way of creating value gives life and credibility to the materiality matrix” and this sends a very distinctive message about our business model and what we value.

Material issues matrix

We consolidated feedback from our various stakeholder groups, as detailed above, which resulted in a list of 26 material issues. These issues are impacted by factors that may be external, internal or both — for example, affordability and vulnerability affects customers due to external social and economic factors, and the support services we provide those customers with are an internal factor, so this issue is impacted by both. The 26 issues are plotted on the matrix below, from lower to higher in terms of level of interest to stakeholders and how much it can affect our ability to create value.



Effect on our ability to create value

Based on the potential effect on our ability to create value over the short, medium and long term. Value can be created for UU, shareholders, regulators, employees, the public, and/or the environment. Value can be financial and non-financial.

External factors

- 5 Political and regulatory environment
- 10 Climate change
- 12 Cyber security
- 15 NW regional economy
- 17 Natural resources
- 21 Social media
- 24 Land management and access
- 26 Human rights

Internal factors

- 2 Resilience
- 8 Financial risk management
- 9 Corporate governance and business conduct
- 11 Innovation
- 14 Data security
- 16 Energy use
- 18 Responsible supply chain
- 19 Health, safety and wellbeing
- 22 Employee relations
- 25 Community investment

Both external and internal factors

- 1 Trust, transparency and legitimacy
- 3 Customer service and operational performance
- 4 Leakage and water efficiency
- 6 Affordability and vulnerability
- 7 Sewer flooding
- 13 Environmental impacts
- 20 Competitive markets
- 23 Diverse and skilled workforce

Read **our stakeholder metrics table** on page 55

Read about how the board considers stakeholders in its decision-making in our **section 172 statement** on page 152

How we create value for stakeholders

UN Sustainable Development Goals

KEY FACTS

17

global goals adopted by the United Nations to be achieved by 2030

5

identified where we contribute most as a business

The Sustainable Development Goals (SDGs) are a collection of 17 global goals to be achieved by the year 2030, and were adopted by a summit of the United Nations (UN) in 2015. They are designed to be the blueprint to achieve a better and more sustainable future for all, aiming to end poverty, fight inequality and tackle climate change.

Since they were published, stakeholder interest has increased in the contributions companies are making to the UN SDGs.

While our work contributes across all of the goals, we have identified five goals that are the most material to our business and the nature of the essential services that we provide. Our approach to operating in a responsible manner aligns quite naturally with these goals. We will increasingly need to work in partnership with all our stakeholders in order to achieve these goals.

The following details show the steps we are taking to meet each of these five SDGs.

Read more at unitedutilities.com/sdgs

Clean water and sanitation – Ensure availability and sustainable management of water and sanitation for all

This is our core function and the reason we exist – providing safe, resilient and affordable water and wastewater services to customers across the North West of England.

Part of this goal is about avoiding wasting water, and we promote water efficiency through campaigns, advice, education and free water-saving gadgets for customers.

We protect and enhance water-related ecosystems across our region.

Decent work and economic growth – Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all

Our daily operations provide direct and indirect employment for thousands of people, and we are a big contributor to the North West economy.

We provide training and development opportunities in safe, secure working environments, graduate and apprentice opportunities, offer equal opportunities to all and value diversity among our employees. Read more on page 98.

Industry, innovation and infrastructure – Build resilient infrastructure, promote inclusive and sustainable industrialisation and foster innovation

We invest heavily in infrastructure, including £250 million additional investment in 2015–20 to increase our resilience. Read more about our approach to resilience on pages 50.

Ensuring the region where we operate has reliable, sustainable and resilient infrastructure for the long term requires innovation to keep pace with an increasingly digital world. Read about our Innovation Lab on page 37.

Sustainable cities and communities – Make cities and human settlements inclusive, safe, resilient and sustainable

We use our understanding of customer needs and priorities to deliver services that meet their expectations and engage with communities to enhance participation in what we do. We plan far into the future to prepare for increases in the population and new housing that will need connections for water and wastewater services.

To find out more about our community activity see

https://www.unitedutilities.com/globalassets/documents/pdf/community-activity-booklet.pdf

Peace, justice and strong institutions – Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels

We run our business with integrity, and this is one of our core values.

We have high levels of transparency in our reporting and ethical standards of business conduct and corporate governance – those systems and processes through which our organisation is managed, controlled and held accountable.

Collaborating with the community to improve reservoir safety

Throwlines have been installed around reservoirs across Greater Manchester and Lancashire and dedicated to the memory of someone who lost their life.

We have 180 reservoirs across the North West, many in beautiful locations. The land around our reservoirs is a wonderful natural resource and we want to do everything possible to encourage people to visit and enjoy the health and wellbeing benefits of being out in the countryside.

But while reservoirs are wonderful places to visit for a picnic or walk, they are one of the worst possible places to take a swim. As well as dangerous hidden machinery under the surface and no lifeguard on duty, the water can be deceptively cold. If you jump in, the chances are you won't be able to get out. The water is so cold it can literally take your breath away and force your body into a spasm known as 'cold water shock'.

Despite our best efforts to raise awareness of the dangers, there are always a few who will take a chance. Sadly, in the last two years four people have lost their lives swimming in reservoirs in the North West alone.

As a responsible business, we want to do more to prevent these needless tragedies. That's why we've been working with bereaved families, water safety campaigners and representatives from the North West's fire and rescue services to identify what can be done to help reduce the number of drowning incidents in the region's reservoirs.

Together we've come up with a new pilot scheme which will help prevent loss of life. New throwlines have been installed at 20 locations around eight reservoirs across Greater Manchester and Lancashire as part of a special pilot. The throwlines can buy valuable time and help people keep their head above the water until firefighters arrive to help. Each throwline also has an information board with advice on how to help in an emergency and accurate location details for the fire and rescue services.

The scheme has received widespread media coverage and praise. Water safety campaigner Beckie Ramsay has been raising awareness of the dangers of open water swimming following the death of her son, Dylan, in 2011. She said: "I hope when people see the throwlines and the dedications written by the bereaved families it will make them think twice. If it stops just one youngster taking that chance it will be a success."

Mark Hutton, from Lancashire Fire and Rescue Service, added: "We are really pleased to see a major utility provider deciding to install water safety boards and by doing so recognising just how important they can be in preventing loss of life, both in terms of the important safety messages they convey, and also their life-saving function in the event of an emergency."

If the throwline pilot scheme is a success we will consider rolling it out to other reservoir sites around the North West.

> "Together we've come up with a new pilot scheme which will help prevent loss of life."

Our planning horizons

Our approach to planning

Our three business areas – wholesale water, wholesale wastewater, and household retail – align with the distinct price controls in Ofwat's regulatory model. Each area undertakes long, medium and short-term planning.

Long-term (25+ years) planning identifies requirements to cope with challenges and opportunities in line with our strategy. This influences our medium-term planning, which sets out how we will deliver the commitments agreed for each five-year regulatory period.

Short-term (one year) planning enables us to monitor and measure progress towards those regulatory commitments. We retain flexibility in these short-term plans to ensure we meet those commitments in the most effective and efficient way as circumstances change.

25+ years – reflecting the long-term nature of our business, which provides an essential service to customers, and helping us to define what we need to deliver in each five-year regulatory period to ensure long-term resilience

5 years – reflecting the regulatory review periods within which our revenue allowances are set, and helping us move towards achievement of our long-term goals

1 year – reflecting the annual targets we set to help move us towards achievement of our five-year goals

Our plans take into account the internal and external drivers and relationships shown in our business model, and we consult with and consider the interests of all our stakeholders.

Read more about how we create value for stakeholders on pages 39 to 46

We continuously assess our performance against our plans using key performance indicators (KPIs) and other performance metrics of interest to our stakeholders.

Read more about how we measure our performance on pages 51 to 55

Long-term planning (25+ years)

In order to maintain a reliable, high-quality service for customers far into the future, we have to look a long way ahead to anticipate and plan for the changes and core issues that are likely to impact on our activities.

Over the next 25+ years we will face many challenges and opportunities, including:

- Climate change;
- Population growth;
- The UK's exit from the European Union;
- A more open, competitive market;
- More stringent environmental regulations;
- Developments in technology; and
- Combining affordable bills with a modern, responsive service.

There is a section of our website that deals with our future plans, where we examine the challenges ahead and how we will focus our resources and talents in order to meet them.

Read more online at unitedutilities.com/corporate/about-us/our-future-plans

This includes our 25-year Water Resources Management Plan (WRMP). Our current plan was published in 2015 covering the 2015–40 period, and we consulted with stakeholders during the year on our new draft WRMP covering the 2020–45 period. These long-term plans set out the investment needed to ensure we have sufficient water to continue supplying our customers, taking into account the potential impact of climate change.

We create long-term value for stakeholders by:

- Systems Thinking and innovation;
- Long-term planning and responding to challenges and opportunities, including management of water resources;
- Sustainable catchment management;
- Disciplined investment, based on a sustainable whole-life cost modelling approach, to ensure the resilience of our assets and network;
- Investing in our employees to maintain a skilled, healthy and motivated workforce;
- Close collaboration with suppliers; and
- Maintaining a robust and appropriate mix of debt and equity financing.

2020+

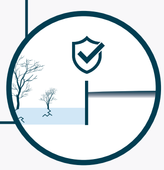
We will continue to contribute to improving bathing water quality

2022

We will extend our integrated water supply network into West Cumbria

2025

We will halve the risk of requiring drought permits to augment supply



Medium-term planning (5 years)

Each five-year business plan aims to help us work towards our long-term plans and ultimately to achieve our vision.

We submit a balanced plan to Ofwat in order to agree a regulatory contract that allows for the best overall outcomes for our customers, shareholders and the environment.

Read more about our economic regulation on page 18

Once each regulatory contract is set, we create value principally by delivering, or outperforming, that contract by providing the best service to customers, at the lowest sustainable cost, in a responsible manner.

In the 2015–20 period we are delivering:

The best service to customers

- Improving customer service further, fixing issues proactively before they impact customers, reducing the number of complaints, and improving our communication channels

At the lowest sustainable cost

- Minimising our total costs on a sustainable basis, enhancing debt collection activities to deliver a more efficient retail service, raising low-cost finance and managing financial risk to reduce volatility

In a responsible manner

- Meeting regulatory commitments to protect and enhance the environment, increasing our renewable energy generation to reduce our carbon footprint, and providing the best support for vulnerable customers

Wholesale water

Our wholesale water team are:

- Maintaining high levels of reliability and water quality, and reducing the number of times customers need to contact us;
- Making better use of technology for remote monitoring and control of assets;
- Maintaining leakage at or below the sustainable economic level;
- Limiting the customer impact of increases in operating costs, such as chemicals and rates, by making cost savings elsewhere through continuous improvement in operational efficiency; and
- Linking 150,000 customers in West Cumbria to Thirlmere reservoir to protect sensitive ecology in their previous water source and ensure a long-term, reliable supply of drinking water.

Wholesale wastewater

Our wholesale wastewater team are:

- Making better use of technology, automation and control to drive better customer service at lower costs;
- Reducing the number of customers' properties exposed to sewer flooding, working in partnerships to deliver cost-effective schemes and promoting the use of more sustainable drainage systems;
- Improving bathing water quality and working with other organisations to support them in delivering improvements to our region's beaches;
- Improving water quality in rivers and lakes and engaging with others in our innovative catchment management approach;
- Increasing the production of renewable energy from waste; and
- Constraining the costs of taking responsibility for all private sewers and private pumping stations in the region.

Household retail

Our household retail team are:

- Continuing to improve the customer experience by being more proactive, anticipating problems before they materialise, and improving our communication channels in line with customer preference;
- Further reducing the number of customer complaints, and resolving them whenever we can to avoid the need for referral to the Consumer Council for Water;
- Reducing the debt burden for customers and the company by engaging with those who are struggling to pay, helping them return to sustained payment behaviour;
- Expanding our assistance offerings, including the social tariff, and contributing to our trust fund, 'Restart', which has proven effective in helping customers in difficulty return to regular payment; and
- Reducing the cost to serve our customers.

Our plans for the 2020–25 period are set out in our business plan submission.

Read more on pages 19 to 23

2025+ – We will work to enable future national water trading

2030 – We will work with others to achieve 'Blue Flag' beaches along our coastline

2045 – We will install additional water meters to achieve coverage of around 75 per cent of households

Our planning horizons

Short-term planning (1 year)

Short-term planning helps us work towards our medium and long-term goals and is important to monitor and assess our progress against these. This approach helps us ensure the long-term resilience and sustainability of our business through short and medium-term goals that we can monitor and measure our progress against.

Before the start of each financial year, we develop a business plan for that year, which is reviewed and approved by the board. This sets our annual targets, which are designed to help deliver further improvements in service delivery and efficiency, and to help move us towards achievement of the five-year goals.

Performance against these annual targets determines annual bonuses for executive directors and employees right through the organisation. To avoid short-term decision-making and ensure management is focused on the long-term performance of the company, as well as these annual targets executive directors are also assessed against three-year performance, covering total shareholder return, sustainable dividends and customer service, through long-term incentive plans. Details of the 2018/19 annual bonus and vested long-term incentive plans for our executive directors are shown on pages 132 and 135.

The executive directors hold quarterly business review meetings with senior managers across the business to monitor and assess our performance against our annual targets, helping to ensure that we are on track to deliver our targets for the year, and longer term.

It is vital that we retain flexibility within this short-term planning so we can adapt to meet challenges that may arise during each year, and deliver high-quality and resilient services to customers in the most effective and cost-efficient way possible.

This may involve bringing enhancements forward to deliver improvements for customers early, investing further into the business to maintain service or delaying projects to occur later in the regulatory period in order to prioritise expenditure and allow our people to spend their time dealing with any unexpected challenges that arise.

For example, during 2018/19 we needed to allocate additional resources to deal with the impact of extreme weather events. We entered the year having experienced a deep freeze followed by a rapid thaw, which had an impact on our levels of leakage, and it was not long before we entered a period of intense hot, dry weather that depleted reservoir levels and saw a surge in water demand.

In response, we substantially increased our leak detection teams and allocated resources to bring additional water resources into operation and increase pumping around the region to balance risk and support the worst affected areas. This resulted in us needing to commit to additional expenditure, as detailed on page 62, but was managed in a way that maintained service for customers and we successfully met our leakage target for the year despite these challenges.

Our approach to resilience

As detailed on page 21, in its initial assessment of our business plan for 2020–25, Ofwat commended our approach to resilience as sector-leading and said we set the standard for other companies to aspire to.

Innovation is a critical enabler for resilience, and our Systems Thinking approach gives us an advantage. Sensors across our network and remote monitoring and control from the Integrated Control Centre at head office allows us to spot issues and respond proactively before customers are impacted and/or the issue becomes more serious. For example, spotting changes in pressure in the network to identify issues so that we can send a team out to repair them before customers are affected.

As well as our use of innovation, we have enhanced our approach to resilience through lessons learned from previous events. We introduced new incident management procedures with detailed contingency plans and a director-led incident review board in response to events in 2015 and 2016. This was instrumental in the way we coped with extreme weather events in 2018, including both the freeze-thaw and the hot, dry summer.

Read more about **how we responded to the challenges of climate-change** on page 30

Another development in our approach as a result of lessons learned was the introduction of Priority Services, which offers tailored support to the more vulnerable members of society in emergencies.

Operational resilience

The main risks to the resilience of our operational assets are the potential for failure of ageing infrastructure and the challenges presented by predictions for climate change and population growth.

Our business plan submission for 2020–25 contains proposals to address our biggest operational asset risk, the Haweswater Aqueduct that transports water from the Lake District to Greater Manchester. Read more on page 21.

Our draft 2019 Water Resources Management Plan considered a range of future challenges, including:

- Extreme drought, freeze-thaw, and flooding;
- Climate change (100 scenarios under the latest UK climate projections at the time of creating the plan, UKCP09); and
- Demand (population growth, economic trends and patterns of water use).

We assessed risks over the 2020–45 planning period and looked beyond this into the 2080s. We published two adaptation reports, in 2011 and 2015, which outline our holistic, integrated and partnership approach to a range of short and long-term challenges, including a changing climate.

Read more online at **unitedutilities.com/corporate/responsibility/environment/climate-change/**

Skills resilience

We have some key highly skilled roles, and our talent succession pipeline is critical to the seamless transfer of skills from one generation of employees to another.

We have active graduate and apprenticeship programmes, we have partnered with Teach First, and we are an active participant in the STEM (science, technology, engineering and mathematics) programme encouraging the younger generation to study and pursue careers in these fields.

Corporate and financial resilience

As a public listed company, we consistently adhere to the highest levels of governance, accountability and transparency.

Long-term financial resilience starts with a strong and robust balance sheet and a prudent risk management approach, and we believe we are at the frontier in this respect. We have maintained a responsible level of gearing and well-controlled pension position for many years, and our prudent financial risk management is one of our competitive advantages.

Read more about **our competitive advantages** on page 17

How we measure our performance

Key performance indicators and other stakeholder metrics

We have a range of key performance indicators (KPIs) encompassing the important areas of customer service and environmental performance, as well as financial indicators. Our operational KPIs are aligned with our strategic themes, and our financial KPIs assess both the profitability and sustainability of our business.

Further detail on our performance against our regulatory commitments is published in July of each year in our Annual Performance Report.

In addition to our KPIs and regulatory commitments, we monitor our performance against an assortment of metrics that are of interest to our many stakeholders, and report against these within this report and on our corporate website.

Our key performance indicators (KPIs)

To help measure progress on how well we are delivering the outcomes described in our business model and adding value for all our stakeholders, we focus on a range of financial and operational KPIs. Our executive bonuses and long-term incentives are closely aligned to our financial and operational performance KPIs, as highlighted in the remuneration report on page 123.

We set operational KPIs for the five-year regulatory period. These align with our three strategic themes, and reflect the outcomes we have committed to deliver for customers and other stakeholders, including the environment. A description of these operational KPIs, our targets for each, and our performance against these targets can be seen on the following pages. These operational KPIs remain consistent with last year.

We set financial KPIs that assess both the profitability and sustainability of our business from a financial perspective. A description of these financial KPIs and our performance against these targets can be seen on page 54. We set internal budgets for financial KPIs but we do not have externally declared targets for these.

This year we have changed one of our financial KPIs. We have removed revenue from the list, recognising that the movements in revenue are dependent on the regulatory mechanism rather than management control, and replaced this with total shareholder return, a measure of movements in the share price plus dividends over the year, which is more important for shareholders. This measure is used for our executive remuneration through the long-term plan, although the time frame of calculation and comparators are different for the one-year KPI and the three-year incentive plan.

Annual Performance Report (APR)

Performance against our regulatory contract is monitored and assessed each year, and reported within an Annual Performance Report (APR). This has been a requirement from Ofwat for all water companies since the start of the current regulatory period in financial year 2015/16, when this replaced the previous ‘regulatory accounts’.

The majority of our operational KPIs relate to this regulatory performance on a high level, and it is within the APR that more detail can be found on the components within these measures, as well as narrative detail about our performance during the year.

There is also financial information contained within the APR. This relates only to the regulated company and its appointed activities, and is calculated and prepared in accordance with the regulatory accounting framework, which differs from IFRS reporting; however, a reconciliation to IFRS reporting is provided in our APR. For the purposes of clarification, our financial KPIs relate to our performance at the group level, and are calculated in line with the definitions given in this report.

Our APRs for previous years are available on our external website, and the APR for 2018/19 will be published in July 2019.

Read more online at **unitedutilities.com/corporate/about-us/performance**

Other performance indicators

Our KPIs provide a snapshot of our performance across a variety of areas, but these are by no means the only metrics by which we monitor and assess our performance on a regular basis, and we report against other metrics both internally and externally.

As discussed on pages 39 to 45, we engage with a variety of stakeholders and this gives us a view of what matters most to them. We report on a selection of other stakeholder metrics on page 55 of this report, based on the measures shown to be of highest interest to our stakeholders.

For example, on customer service our KPIs are Ofwat’s measures, the qualitative and quantitative Service Incentive Mechanism (SIM), but our stakeholder metrics table also reports on the level of customer complaints, use of digital communication channels, customers helped through assistance schemes, and the impact of water efficiency measures.

On environmental performance, our KPIs include performance against our leakage target and the overall assessments by the Environment Agency and Dow Jones Sustainability Index, but our stakeholder metrics table also reports on more specific environmental performance indicators, such as carbon footprint, proportion of waste going to beneficial use rather than landfill, and measures of natural capital.

We also regularly report on numerous corporate responsibility performance measures on our external website.

Read more online at **unitedutilities.com/corporate/responsibility/our-approach/cr-performance**

How we measure our performance

Our operational KPIs

The best service to customers

Wholesale outcome delivery incentive (ODI) composite

Definition

Net reward/(penalty) accrued across United Utilities' 19 wholesale financial ODIs, more detail of which can be found in our Annual Performance Report.

Target

End the 2015–20 regulatory period with around £30 million cumulative net ODI reward.

Link to bonus/LTP

Bonus – direct
LTP – indirect

Status

Achieved/confident of achieving target

Performance

2018/19: £19.2 million reward (cumulative £21.4 million reward)

2017/18: £7.0 million penalty (cumulative £2.2 million reward)

2016/17: £6.7 million reward (cumulative £9.2 million reward)

2015/16: £2.5 million reward

At the lowest sustainable cost

Total expenditure (totex) outperformance

Definition

Progress to date on delivering our promises to customers within the cumulative 2015–20 wholesale totex final determination allowance.

Target

To outperform Ofwat's final determination totex allowance by £100 million over the 2015–20 regulatory period.

Link to bonus/LTP

Bonus – indirect
LTP – indirect

Status

Achieved/confident of achieving target

Performance

2015–20: Confident of outperforming the final determination allowance by £100 million over the 2015–20 regulatory period

Totex was a new measure for the 2015–20 period, hence no prior years' comparators

In a responsible manner

Leakage – average annual leakage

Definition

Average annual water leakage from our network quantified in megalitres (Ml) per day.

Target

To meet our regulatory leakage target of 462.65 Ml per day for each year in the 2015–20 regulatory period, as set by Ofwat.

Link to bonus/LTP

Bonus – indirect

Status

Achieved/confident of achieving target

Performance *

2018/19: Met target
2017/18: Met target
2016/17: Met target
2015/16: Met target
2014/15: Met target

* Final figure for leakage will be reported in our Annual Performance Report, available on our website in July

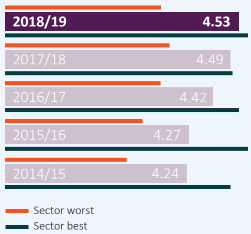
Service incentive mechanism (SIM) – qualitative

Definition
Ofwat-derived index based on quarterly customer satisfaction surveys, measuring the absolute and relative performance of the 18 water companies. Each company receives a score in the range of zero to five, with five being the best attainable score.

Target
To move towards the upper quartile in the medium term.

Link to bonus/LTP
Bonus – direct
LTP – direct

Status
Achieved/confident of achieving target

Performance


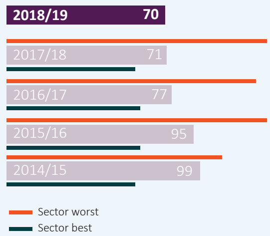
Service incentive mechanism (SIM) – quantitative

Definition
Ofwat-derived composite index based on the number of customer contacts, assessed by type, measuring the absolute and relative performance of the 18 water companies. Each company receives a SIM point total, where the lowest score represents the best performance.

Target
To move towards the upper quartile in the medium term.

Link to bonus/LTP
Bonus – direct
LTP – direct

Status
Achieved/confident of achieving target

Performance *


* Sector best and worst figures for quantitative SIM are not yet available for 2018/19

Financing outperformance

Definition
Progress to date on financing expenditure outperformance secured versus Ofwat's industry allowed cost of debt of 2.59 per cent real over the 2015–20 period.

Target
To beat Ofwat's industry allowed cost of debt.

Link to bonus/LTP
LTP – indirect

Status
Achieved/confident of achieving target

Performance
2015–20: On track to beat Ofwat allowance

2010–15: Exceeded our £300 million target outperformance

Household retail cost to serve

Definition
Cost to serve in our household retail business compared with Ofwat's revenue allowance (including margin).

Target
To minimise costs compared with Ofwat's revenue allowance.

Link to bonus/LTP
Bonus – indirect
LTP – indirect

Status
Achieved/confident of achieving target

Performance
2018/19: £5 million outperformance

2017/18: £9 million outperformance

2016/17: £14 million outperformance

2015/16: £10 million outperformance

Environment Agency performance assessment

Definition
Composite assessment produced by the Environment Agency, measuring the absolute and relative performance of the 10 water and wastewater companies across a broad range of areas, including pollution.

Target
To be a first quartile performer (i.e. at least 4th) on a consistent basis.

Link to bonus/LTP
Bonus – indirect

Status
Achieved/confident of achieving target

Performance*
2017: Joint 1st
2016: Joint 1st
2015: Joint 2nd
2014: 2nd
2013: 2nd

* Assessment for the 2017 calendar year was published in July 2018 and is the most recent available.

Dow Jones Sustainability Index rating

Definition
Independent rating awarded using sustainability metrics covering economic, environmental, social and governance performance.

Target
To retain 'World Class' rating each year

Status
Achieved/confident of achieving target

Performance
2018/19: 'World Class'
2017/18: 'World Class'
2016/17: 'World Class'
2015/16: 'World Class'
2014/15: 'World Class'

How we measure our performance

Our financial KPIs

Underlying operating profit

Definition

The underlying operating profit measure excludes from the reported operating profit any restructuring costs and significant non-recurring items. The group determines adjusted items consistently in the calculation of its underlying operating profit measure against a framework which considers significance by reference to profit before tax, in addition to other qualitative factors such as whether the item is deemed to be within the normal course of business, its assessed frequency of reoccurrence, and its volatility, which is either outside the control of management and/or not representative of the current year performance. A reconciliation is shown on pages 66 to 67.

Link to bonus/LTP

Bonus – direct
LTP – indirect

Status

Close to achieving target but more work to be done

Performance

2018/19	£685m
2017/18	£645m
2016/17	£623m
2015/16	£604m
2014/15	£664m

Underlying earnings per share

Definition

This measure deducts underlying net finance expense and underlying taxation from underlying operating profit to calculate underlying profit after tax and then divides this by the average number of shares in issue during the year. Underlying net finance expense makes consistent adjustments to the reported net finance expense, including the stripping out of fair value movements. Underlying taxation strips out any prior year adjustments, exceptional tax or any deferred tax credits or debits arising from changes in the tax rate from reported taxation. Reconciliations to the underlying measures above are shown on pages 66 to 67.

Link to bonus/LTP

LTP – indirect

Status

Achieved/confident of achieving target

Performance

2018/19	55.5p
2017/18	44.7p
2016/17	46.0p
2015/16	47.7p
2014/15	51.9p

Dividend per share

Definition

This measure divides total dividends declared by the average number of shares in issue during the year.

Link to bonus/LTP

LTP – direct

Status

Achieved/confident of achieving target

Performance

2018/19	41.28p
2017/18	39.73p
2016/17	38.87p
2015/16	38.45p
2014/15	37.70p

Gearing: net debt to RCV

Definition

Group net debt (including derivatives) divided by UUW's regulatory capital value (RCV). From 2016/17 onwards this uses shadow RCV, adjusted for actual spend, while prior years used Ofwat's published RCV in out-turn prices as per previous methodology.

Target

Maintain gearing within a range of 55 per cent to 65 per cent.

Status

Achieved/confident of achieving target

Performance

2018/19	61%
2017/18	61%
2016/17	61%
2015/16	61%
2014/15	59%

Total shareholder return

Definition

This measure calculates the return to shareholders based on the movement in the share price plus dividends over each financial year.

Link to bonus/LTP

LTP – direct

Status

Close to achieving target but more work to be done

Performance

2018/19	120%
2017/18	75%
2016/17	119%
2015/16	102%
2014/15	121%

Note 1: For both our Operational and Financial KPIs, where we have declared external targets we assess our performance against the most recent public targets. Where there are no externally declared targets we assess our performance against our internal budget; however, our internal budget is not disclosed. Green status indicates that we have achieved or are confident of achieving our target. Amber status indicates that we are close to achieving our target but there remains some work to be done. Red status indicates that we are missing our target.

Note 2: In some instances the remuneration committee has used metrics with similar names but calculation methodologies which they consider more appropriate for executive remuneration, as set out in the remuneration report on pages 116 to 143.

Stakeholder metrics table

We have a wide range of stakeholders who take an interest in the way we do business. The following table provides a broad set of performance measures covering Environmental, Social and Governance issues that are of interest to our stakeholders. Further information on how we manage our business in a responsible manner can be found in the responsibility pages of our corporate website.

Theme	Area	Measure	Data metric	Further information
Shareholders	Compliance	2016 UK Corporate Governance Code	Compliant	Directors' report – statutory and other information
		Dow Jones Sustainability Indices	World Index	Our performance - in a responsible manner section
Customers	Complaints	Total number of domestic customer complaints	7,007	Our performance - best service to customers section
		Average speed of complaint resolution	3 days	Our performance - best service to customers section
	Fines	Drinking Water Inspectorate (DWI) fines	2 (£150,000 and £50,000)	Related to two drinking water incidents at Sweetloves water treatment works in 2015
	Digital	Number of customers using online services – My Account	860,648	Our performance - best service to customers section
	Customer assistance	Number of customers assisted by Priority Services	74,505	Our performance - best service to customers section
	Customer water efficiency	Total customer water savings from measures promoted by United Utilities	4.43 Ml/d	Our key resources section
Environment	Carbon and energy	Carbon footprint	167,856 tCO_2e	Directors' report – energy and carbon
		Energy used	976 GWh	Directors' report – energy and carbon
	Waste	Total waste	694,846 tonnes	Responsibility pages of our website
		Waste to beneficial use	96%	Responsibility pages of our website
	Leakage	Total leakage at or below target of 462.65 Ml/d	Met target	Annual Performance Report published in July
	Fines	Number of incidents resulting in fines	0	Our performance - in a responsible manner section
		Enforcement undertakings	5 (£1.5m)	Our performance - in a responsible manner section
	Natural capital	Number of trees planted on catchment land	27,190	Responsibility pages of our website
		No net loss of biodiversity across capital programme	100%	Responsibility pages of our website
Employees	Employee engagement	Overall employee engagement	81%	Our performance - in a responsible manner section
		Percentage of employees with trade union membership*	45%	Our key resources section
	Workforce profile	83% White 2% BAME 15% Non-disclosed 65% Male 35% Female <1% Disability (including long-term health conditions)		
	Gender pay reporting	Mean gender pay gap	13.1%	Gender Pay Report on our website
		Median gender pay gap	15.3%	Gender Pay Report on our website
	Employee development	Average number of days of training per FTE per year	3.57 days	Our performance - in a responsible manner section
	Health and safety	Employee Accident Frequency Rate (per 100,000 hours)	0.152	Our performance - in a responsible manner section
		Contractor Accident Frequency Rate (per 100,000 hours)	0.092	Our performance - in a responsible manner section
Suppliers	Payment statistics	Average time taken to pay invoices	25 days	Suppliers pages of our website
		Suppliers paid on time	98.57%	Suppliers pages of our website
Communities	Charity	Match funding to charity through employee efforts	£157,046	Responsibility pages of our website
	Community investment (LBG data)	How investment was made: Cash £2,717,856 Time £52,409 Management costs £161,214 Total £2,931,479 Type of support: Charitable gift £159,545 Community investment £2,610,719 Commercial initiative £0		
	Employee volunteering	Number of hours' employee volunteering	2,620	Responsibility pages of our website

*Based on employees who pay their union subscriptions via their payroll.

Our performance in 2018/19

Operational performance

The best service to customers

Customer service – sitting at the core of everything we do, our strong focus on customer service has helped us deliver substantial improvements in recent years, becoming the most improved company in the 2010–15 regulatory period with a reduction of over 70 per cent in the overall number of customer complaints.

We have continued to improve at a faster rate than the industry average in AMP6, positioning us as one of the leading water and wastewater companies. This year, we have again gone from strength to strength in our customer satisfaction performance, achieving our highest ever scores against Ofwat's qualitative Service Incentive Mechanism (SIM) measure and finishing fourth out of the water and wastewater companies for the year overall. This performance is mirrored in the number of complaints that we receive. Since 2015/16 we have seen a 30 per cent reduction in complaints and a 64 per cent reduction in repeat complaints.

During AMP6, we have developed new services that increase the speed and quality of the customer service we provide. These include a new system that enables us to proactively keep customers informed of events on our network, increasing the hours we are available for customers to contact us, and increasing the channels by which they can contact us so they do not always need to call.

We have driven an increase in digital engagement through a new customer-centric website, the introduction of an easy-to-use mobile app and a substantially enhanced social media presence on commonly used platforms such as Facebook and Twitter. In support of our most vulnerable customers we launched our Priority Services proposition, setting up dedicated teams for those that need it most. In January, we hosted the second North West Affordability Summit, engaging with customers and key stakeholders.

We have received external recognition for the improvements made in the quality of service we deliver to customers. We are the first water company to receive Shaw Trust Accessibility status for our website, we received the Service Mark with Distinction from the Institute of Customer Service and we won three gold awards at the UK Complaint Handling Awards.

Leading North West service provider – we are consistently ranked third out of ten leading organisations in the North West, through an independent brand tracker survey which is undertaken three times per year. This covers key attributes such as reputation, trustworthiness and customer service and in the most recent survey, we have been ranked first for being environmentally responsible. We are behind only Marks & Spencer and Aldi, and ahead of seven other major organisations across utilities, telecoms, media and banking.

Robust water supply – customers benefit from our robust water supply and demand balance, along with high levels of water supply reliability. Our overall water quality continues to be good with an improvement in our water quality service index compared with the prior year. It is tracking above our historical average with plans in place to deliver further improvements going forward. We have delivered a reliable water service and although we inevitably experience some water no-supply incidents, our Systems Thinking approach is helping us to reduce the frequency and severity of such events and respond to them in a way that minimises customer impact.

During 2018/19, the UK experienced unprecedented extremes of weather beginning with a deep freeze and rapid thaw followed by the driest summer for our region since modern records began. Thanks to interventions that we were able to make, alongside the support of customers and regulators, we were able to minimise the impact of these events and maintain unrestricted service to customers.

Reducing sewer flooding – we have continued to invest heavily in schemes, projects and programmes of work designed to reduce the risk of flooding of customers' homes, including incidence-based targeting on areas more likely to experience flooding and defect identification through CCTV sewer surveys and other innovative technologies. Our plan for the 2015–20 regulatory period includes a target of reducing sewer flooding incidents by over 40 per cent, in line with customers' affordability preferences, and we are making good progress. We achieved our best ever five-year performance on our repeat flooding and internal operational flooding measures.

Our wastewater network will continue to benefit from significant investment going forward and we will continue to seek to work in collaboration with other external flood authorities and associated partners to address the widespread flooding events that hit our region, as we aim to help mitigate the effect of changing weather patterns likely to result from climate change.

Key performance indicators:

› **Outcome delivery incentives (ODIs)**

We have 19 wholesale financial ODIs, of which ten provide the potential to earn a reward in the 2015–20 regulatory period. In 2018/19 we have delivered our best annual performance against ODIs resulting in a net reward of £19.2 million, reflecting great operational performance across the board.

Overall, performance was again good against our wastewater measures, and significantly improved against our water measures with a net reward achieved in both areas.

We are pleased with our cumulative performance over the first four years of the current regulatory period, which have resulted in a net reward of £21.4 million, exceeding our initial expectations. WhilE a number of our ODI measures are susceptible to one-off events and, on the whole, our ODI targets get tougher each year, our strong performance to date coupled with continued targeted investment, alongside our Systems Thinking and innovative approach to the way we operate, gives us confidence that we will achieve a cumulative net ODI outcome over the 2015-20 regulatory period of around £30 million.

Our main areas of reward to date have come through our performance in the areas of private sewers, pollution and leakage. Our main penalty has been on reliable water service and water quality service, although particularly pleasing this year was a significantly improved performance against our reliable water service index where we are seeing the benefit of our targeted investment and Systems Thinking approach.

› **Service incentive mechanism (SIM)**

We have previously stated our target was to move towards the upper quartile in the medium term, and we are particularly pleased with the progress we have made over AMP6, ending the four-year period to 2018/19 in fourth place overall for the water and wastewater companies. This means we should be eligible for a reward of around £16 million assuming that Ofwat applies the same methodology as at PR14.

Qualitative: Ofwat has undertaken the four surveys for 2018/19 and we have improved our score to 4.53 points, compared with 4.49 points in 2017/18, putting us in fifth position for the year out of the 18 water companies, and fourth position out of the 11 companies providing both water and wastewater services. In particular, customers scored us highly for our billing services.

Quantitative: the quantitative assessment measures customer contacts, and performance is assessed on both an absolute and relative basis. WhilE relative performance can only be assessed in full following the end of each financial year when the other companies publish their respective results, on absolute performance for 2018/19, our score of 70 points represents a further improvement on our 2017/18 score of 71 points. For the first nine months of the year, of the companies that share data on quantitative SIM, we were first of the seven water and wastewater companies and fourth of the 11 water companies.

Business insight

Working together to support those in need

North West Hardship Hub gives advisers one-stop-shop for local assistance schemes

With recent reports showing household debt is pushing millions of UK families into the red, we met with organisations who deal with customers in challenging circumstances to discuss what more can be done to support those struggling financially. We believe that a collaborative regional partnership can go way beyond what any one organisation can do alone.

In 2018 and 2019, we held Affordability Summits on ‘Blue Monday’ in January, which is typically the most financially depressing calendar date of the year. These events were attended by over 100 representatives from across the North West, including debt advice charities, food banks, credit unions and housing associations.

At this year’s Affordability Summit, which was held in Manchester and opened by the Mayor of Greater Manchester, we launched the North West financial Hardship Hub. This is a valuable new resource for the money advice community in our region and the first of its kind in the country.

The Hardship Hub is simple to use and has been developed in conjunction with experts including Citizens Advice and housing associations. It has been dubbed a ‘TripAdvisor’ for financial advice, and advisers can use it to search for all the available help in their local area and can also rate schemes and recommend them to colleagues.

Providing support for customers in vulnerable circumstances is more important than ever and, as a responsible business, we have a duty to continually strive to improve our services in order to help those who need it most.

Some customers need additional support at times. This could be due to age, ill health, disability, mental health problems, financial worries or language barriers. Our Priority Services scheme allows us to respond quickly and considerately to their particular needs. Priority Services free benefits are available to all eligible customers living in the North West.

At present, Priority Services are provided by both water and energy companies across the UK, and from April 2020 a joint water and energy sector project will align all existing Priority Services arrangements in the two sectors so that customers benefit from consistent support without needing to register with each of their utility providers separately.

In 2018 we became the first water company to share consented Priority Services data with the energy sector, and successfully completed a pilot with Electricity North West that tested single registration, as well as the legal and operational principles that support the joint UK project. This successful trial will continue up to commencement of the joint UK project in 2020.

Read more about all the financial assistance we provide at **unitedutilities.com/difficulty-paying-bill**

“A valuable new resource for the money advice community in our region and the first of its kind in the country”

Our performance in 2018/19

Operational performance

At the lowest sustainable cost

Power and chemicals – our asset optimisation programme continues to provide the benefits of increased and more effective use of operational site management to optimise power and chemical use and the development of more combined heat and power assets to generate renewable energy. In addition to the electricity we generate from bioresources, we are developing other renewable energy facilities. This is primarily in the area of solar, where we have invested £59 million in the first four years of the 2015–20 regulatory period. We have also substantially locked in our power commodity costs across 2015–20, providing greater cost certainty for the regulatory period.

Proactive network management – through our Systems Thinking approach we are more proactive in the management of our assets and networks. We have improved our predictive modelling and forecasting through better use of sensors in our network and better analysis of other data, such as weather forecasting, enabling us to address more asset and network problems before they affect customers. This reduces the level of reactive work and improves our performance and efficiency.

Debt collection – our region suffers from high levels of income deprivation and we offer wide-ranging schemes to help customers struggling to pay. We now have over 100,000 customers on affordability schemes, almost double the commitment we made at the start of AMP6. Notwithstanding our industry-leading debt management processes, deprivation remains the principal driver of our higher than average bad debt and we expect this to continue to be a challenging area for us.

Reflecting our ongoing focus on bad debt through initiatives such as our affordability schemes, our household bad debt expense has reduced to 2.1 per cent of revenue from 2.3 per cent last year.

Pensions – United Utilities has taken progressive steps to de-risk its pension provision. The group had an IFRS retirement benefit surplus of £484 million as at 31 March 2019, compared with a surplus of £344 million as at 31 March 2018. Further details of the group's pension provision are provided in the pensions section on pages 197 to 201.

From 1 April 2018, the majority of active members in the defined benefit sections of the United Utilities Pension Scheme (UUPS) transitioned to a hybrid section comprising a capped defined benefit element and a top-up defined contribution component. Pension benefits under the defined benefit element of the new UUPS hybrid section that became effective for pensionable service from 1 April 2018 are linked to CPI rather than RPI.

Capital delivery and regulatory commitments – we are strongly focused on delivering our commitments efficiently and on time, and have a robust commercial capital delivery framework in place. Across the 2015–20 regulatory period, we are working with a single engineering partner and four design and construction partners to deliver our regulatory capital investment programme of around £3.9 billion. We are involving our partners much earlier in project definition and packaging projects by type, geography and timing in order to deliver efficiencies. Projects are allocated on an incentive or competitive basis leading to our partners presenting a range of solutions, innovations and pricing.

We have accelerated our 2015–20 investment programme in order to improve services for customers and deliver early operational and environmental benefits. Regulatory capital investment in 2018/19 was £821 million. This includes £165 million of underlying IRE, £40 million additional capex and IRE associated with the dry weather in the summer of 2018 and £60 million of additional investment made available through sharing our net outperformance. This, combined with £2.4 billion invested in the first three years of the regulatory period, brings our total spend to around £3.2 billion of our expected £3.9 billion capital investment across the 2015–20 regulatory period.

We are also driving more effective and efficient delivery of our capital programme and applying a tougher measurement mechanism to our Time: Cost: Quality index (TCQi) score for this regulatory period. Despite this tougher approach, our TCQi score remains high at 95 per cent, representing very good performance.

Key performance indicators:

› **Total expenditure (totex) performance**

Our totex allowance for the 2015–2020 regulatory period represented a significant challenge compared with the costs we originally submitted as part of our business plan. We have not only closed the gap to our allowance but we are now also confident of outperforming that allowance by £100 million. This has been achieved through a combination of driving efficiency into our capital programme and also through Systems Thinking.

› **Financing outperformance**

The low cost of debt we have already locked in places United Utilities in a strong position to deliver significant outperformance for the 2015–20 regulatory period compared with the industry allowed cost.

› **Household retail cost to serve**

We continue to deliver against a challenging benchmark set for AMP6. Our target is to minimise our costs compared with our revenue allowance and we have delivered a good performance in 2018/19, outperforming this year's revenue allowance (including margin) by around £5 million. By 2020, we are forecasting a cost to serve in line with the regulatory cost allowance and we are confident that our cost plans will move us towards upper quartile performance in AMP7.

Pioneering UV LED treatment technology

Game-changing innovation for water and wastewater treatment

We have been working with Typhon Treatment Systems on a game-changing innovation for water and wastewater treatment since 2015. In the last year we have supported their technology to develop it at a faster pace and move it out of the laboratory and into a commercial product.

Typhon, a start-up business based in Penrith, has developed a UV LED water treatment reactor that significantly reduces the power and chemical consumption of traditional water treatment techniques – non-LED UV light disinfection and activated carbon – which have been the mainstay of water and wastewater treatment processes for the last 20 years.

UV light is used to protect the water we use from dangerous microscopic organisms and hazardous chemical pollutants such as pesticides or pharmaceuticals. Activated carbon is used for issues that can lead to taste and smell problems in water treatment. While both technologies are reliable and scalable, they are difficult to control and can be extremely costly for customers, as they have high energy needs and carbon emissions.

We started working with Typhon to accelerate the development of the technology by building and providing access to a test facility on a live operational site, giving them access to our expert asset management, engineering, scientific and innovation skills and supplying equipment and services to allow the field testing to be carried out in the most efficient manner possible. The aim of the trial was to prove whether energy-efficient LED bulbs could be used for UV treatment and whether these would outperform traditional solutions.

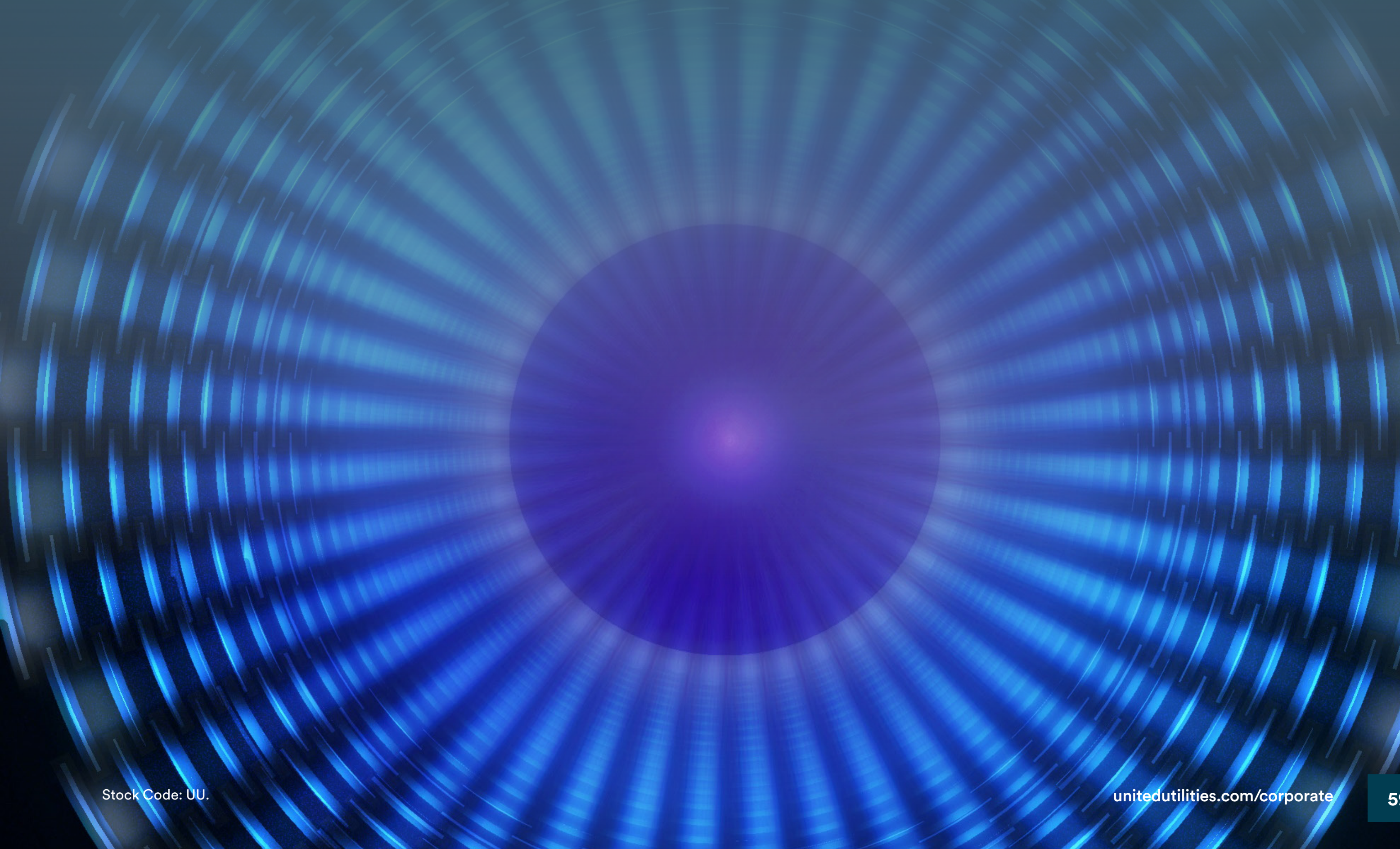
Our work with Typhon enabled them to take a theory and apply it across two trials over a 12-month period, which is significantly faster than traditional water sector technology development. The trials proved the viability of the UV LED rig for advanced oxidation to remove taste and smell compounds as an alternative to conventional treatment processes.

Now proven for water treatment, we are working hard to find the best site for our first full-scale implementation – and encouraged to work with Typhon to further develop and apply this technology into wastewater applications. The Typhon system uses smart computing to optimise the system locally. Our Systems Thinking vision is to have all our Typhon installations remotely monitored, controlled and optimised.

Working together, United Utilities and Typhon accelerated the technological development of LED UV systems for municipal scale applications and delivered the world's first validated LED UV system.

We firmly believe in this technology and our collaboration has helped prove its viability for the benefit of the global water industry.

"Our collaboration has helped prove its viability for the benefit of the global water industry"



Our performance in 2018/19

Operational performance

In a responsible manner

Behaving responsibly is fundamental to the manner in which we undertake our business, and the group has for many years included corporate responsibility factors in its strategic decision-making. Our environmental, social and governance performance across a broad front has received external recognition. Earlier in the 2018/19 financial year, United Utilities retained a World Class rating in the Dow Jones Sustainability Index for the 11th consecutive year, again achieving industry-leading performance status in the multi-utility/ water sector. We look at our performance across a range of other Environmental, Social and Governance (ESG) indices, where we also perform well.

Leakage – we have continued our strong operational focus on leakage, alongside our network resilience improvements and a range of initiatives such as active pressure management, satellite technology and the UK's first leakage sniffer dogs, specially trained to pinpoint the exact location of leaks.

One of the consequences of the extreme weather events that we faced during 2018/19 was an increased level of pipe movements in the ground. We significantly increased our leakage detection and repair efforts in order to combat the higher levels of background leakage that resulted from this. This has delivered good performance against our leakage targets in what has been a very challenging year.

Additionally, we continue to encourage customers to save water through water efficiency programmes as this not only enables them to help preserve this precious resource but can also save money on their water bill. We are particularly grateful for customer support in protecting our water resources through the dry weather period.

Environmental performance – this is a high priority for United Utilities and we were delighted to have retained our Industry Leading Company status in the Environment Agency's latest performance metrics, as described in the KPIs section below. This is a result of our approach to managing our assets in an integrated way to minimise the number of environmental incidents.

Carbon footprint – by 2020, we aim to reduce our carbon footprint by 50 per cent compared with a 2005/06 baseline. This year our carbon footprint has reduced to 167,856 tonnes of carbon dioxide equivalent, a reduction of 71 per cent since 2005/06 and we have therefore achieved our emissions target early. This has been as a result of purchasing certified renewable electricity, with over 95 per cent of the electricity we use having zero emissions.

In addition, we generated the equivalent of 173 gigawatt hours, an increase of 6 gigawatt hours on the previous year. This illustrates good progress in our energy strategy to use less and generate more renewable energy.

Employees – we continue to work hard to engage all of our employees in the transformation of the group's performance. Employee engagement was at 81 per cent this year, higher than the UK norm. We remain focused on maintaining high levels of employee engagement.

We have been successful in attracting and retaining people and have continued with our apprentice and graduate programmes for 2018/19. We now have a total of 39 graduates and 116 apprentices across the business. Our investment in recruiting graduates and apprentices is already benefiting the company, with 214 employees who have previously been on either the graduate or apprentice scheme having secured permanent roles across our business.

Over the last year, we have continued our sustained focus on health, safety and wellbeing. We've started our new campaign, Home Safe and Well, which includes a significant focus on employee behaviour and organisational culture in relation to Health and Wellbeing, Personal Safety and Process Safety. In 2018/19, we retained our Gold award status with the Royal Society for the Prevention of Accidents for the seventh year and our status under the UK workplace wellbeing charter. We have also won REBA awards for our work on Mental and Physical Health and been recognised by Britain's Healthiest Workplace for all the improvements we have made over the last year.

Our employee accident frequency rate for 2018/19 increased to 0.152 accidents per 100,000 hours, compared with a rate of 0.101 in 2017/18. For the same period, our contractor accident frequency rate remained the same at 0.092 per 100,000 hours. While it is disappointing that these accident frequency rates have not improved since last year, they still demonstrate an improved performance against our historical average. We recognise that there is always more to do, and health, safety and wellbeing will continue to be a significant area of focus as we strive to ensure that everyone gets home safe and well.

Communities – we continue to support partnerships, both financially and in terms of employee time through volunteering with other organisations across the North West. Our approach to integrated catchments helps to tackle water quality issues in lakes, rivers and coastal waters across the North West, and our LoveMyBeach contribution includes employees volunteering to help to keep our region's beaches tidy. We continue to support local communities through contributions and schemes such as providing debt advisory services, and our community partnership with Youth Focus North West has addressed one of our region's major issues of affordability through co-creating the 'managing your money' training module.

Key performance indicators:

› **Leakage**

Although leakage is included within our outcome delivery incentives, we intend to continue publishing our leakage position separately, with it being an important measure from a corporate responsibility perspective. In 2018/19 we have again met our regulatory leakage target of 463 megalitres per day.

› **Environmental performance**

On the Environment Agency's latest annual assessment, published in July 2018, we were awarded Industry Leading Company status across the range of operational metrics for the third year running. This indicates we were in joint first position among the nine water and wastewater companies assessed, and aligns with our medium-term goal of being a first quartile company on a consistent basis.

› **Corporate responsibility**

United Utilities has a strong focus on operating in a responsible manner and is the only UK water company to have a World Class rating as measured by the Dow Jones Sustainability Index. In 2018/19, United Utilities retained its World Class rating for the 11th consecutive year.

Co-ordinating our efforts to fight moorland fires

Joining forces with regional stakeholders to limit damage to affected areas

In June 2018 there was extensive media coverage of two large moorland fires in the hills above Manchester, showing images of the fires, the ecological devastation they caused, and the brave and exhausted firefighters tackling the blaze.

Between them, the fires at Stalybridge and Winter Hill covered a huge area – the equivalent of 2,300 football pitches. Over half of the affected area is designated as a Site of Special Scientific Interest. Both sites are also popular recreational spots for local communities, and much of the area is catchment land for drinking water supplies.

The response during the fires was impressive with emergency services, local authorities, landowners and tenants all working together to limit the damage as best they could. Our own land management, emergency response and grounds maintenance teams, along with three helicopters we hired, added to the firefighting effort being coordinated by Greater Manchester Fire and Rescue Service.

The fires caused significant damage to surface vegetation and to the infrastructure used to protect and manage the area, including fences and access routes. The aftermath was distressing for the organisations whose efforts to restore these valuable landscapes had been left in ashes.

Nature itself can be quite resilient, as the green shoots present a few weeks after the fires showed, but the longer-term recovery and resilience of these areas will take time to secure and achieve.

The visible surface damage is only part of the story. Many of the benefits we all derive from these special habitats will take longer to re-establish. Deep burns across areas of peat caused serious releases of sequestered carbon. The amount of CO_2 released is estimated at over 26,000 tonnes, with an estimated value of more than £1.5 million. To restore this peatland to a point where it is again actively locking up carbon will take time, effort and investment.

A wide range of stakeholders have an interest in the recovery of the moorland. Government funding has been made available to help the restoration and efforts to make the moorland more resilient.

The immediate response to the wildfires and the subsequent recovery have required unprecedented levels of partnership working and will continue to need well-coordinated and consistent management and communications for the foreseeable future.

We hope that restoration of 'blanket bog' can be achieved so that once again it can provide the wide range of benefits to all stakeholders. Just as important is making sure any activities improve the resilience of this wonderful habitat.

> "A wide range of stakeholders have an interest in the recovery of the moorland"

Our performance in 2018/19

Financial performance

Strategic report

United Utilities delivered a strong set of financial results for the year ended 31 March 2019.

Revenue

Revenue was up £83 million, at £1,819 million, largely reflecting our allowed regulatory revenue changes.

As a result of Ofwat's annual wholesale revenue forecasting incentive mechanism (WRFIM), we have reduced revenue by £8 million in 2018/19 and will reduce revenue by a further £14 million in 2019/20 (out-turn prices). This consists of two components; firstly reflecting actual volumes being higher than our original assumptions during AMP6, and secondly reductions relating to the 2014/15 'AMP5 blind year', which are £4 million in 2018/19 and £5 million in 2019/20.

Operating profit

Underlying operating profit at £685 million was £40 million higher than last year. This reflects our allowed regulatory revenue changes, partly offset by an £18 million increase in IRE and a £16 million increase in depreciation. The remaining cost base has increased by £9 million as a result of small increases in employee costs, materials, bad debts and property rates, partly offset by a credit resulting from the settlement of an historical commercial claim.

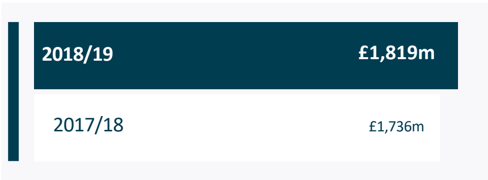
Reported operating profit decreased by £1 million, to £635 million, reflecting the increase in underlying operating profit being more than offset by an increase in adjusted items. Adjusted items for 2018/19 included £36 million of costs associated with the dry weather of 2018, £7 million associated with the equalisation of pension benefits between males and females in relation to Guaranteed Minimum Pension (GMP) benefits, and £7 million of restructuring costs. Adjusted items in the prior year amounted to £9 million, of which £6 million related to restructuring costs.

Investment income and finance expense

The underlying net finance expense of £231 million was £46 million lower than last year, mainly due to the impact of lower RPI inflation on the group's index-linked debt.

Interest of £84 million on non-index-linked debt was £8 million lower than last year, due to the lower rates locked in, including the full year impact of re-couponing a portion of the group's regulatory swap portfolio in the prior year. The indexation of principal on index-linked debt amounted to a net charge in the income statement of £98 million, compared with a net charge of £138 million last year. As at 31 March 2019, the group had approximately £3.8 billion of index-linked debt at an average real rate of 1.3 per cent.

Revenue



Underlying operating profit [1]

Reported operating profit

61%
RCV gearing[2] (%)

41.28p
Total dividend per share ordinary share (pence)

(1) Underlying profit measures have been provided to give a more representative view of business performance and are defined in the underlying profit measure tables on pages 66 and 67.

(2) Regulatory capital value (RCV) gearing calculated as group net debt/United Utilities Water Limited shadow RCV (out-turn prices).

The lower RPI inflation charge compared with last year contributed to the group's average underlying interest rate of 3.3 per cent being lower than the rate of 4.2 per cent for the year ended 31 March 2018. The average underlying interest rate represents the underlying net finance expense divided by average debt.

Reported net finance expense of £205 million was broadly in line with the £207 million expense in 2017/18, principally reflecting a decrease in the fair value gains on debt and derivative instruments, from a £47 million gain in 2017/18 to a £9 million gain in 2018/19 offset by the £39 million decrease in the indexation charge in the year.

The group has fixed the interest rates on most of its non-index-linked debt for the 2015–20 regulatory period.

Profit before tax

Underlying profit before tax was £460 million, £90 million higher than last year, primarily reflecting the £40 million increase in underlying operating profit and the £46 million decrease in underlying net finance expense. This underlying measure excludes the adjusted items, as outlined in the underlying profit measures table on pages 66 and 67.

Reported profit before tax increased by £4 million to £436 million reflecting the £1 million reduction in reported operating profit more than offset by a £1 million reduction in reported net finance expense including fair value movements and a £4 million increase in our share of profits from joint ventures.

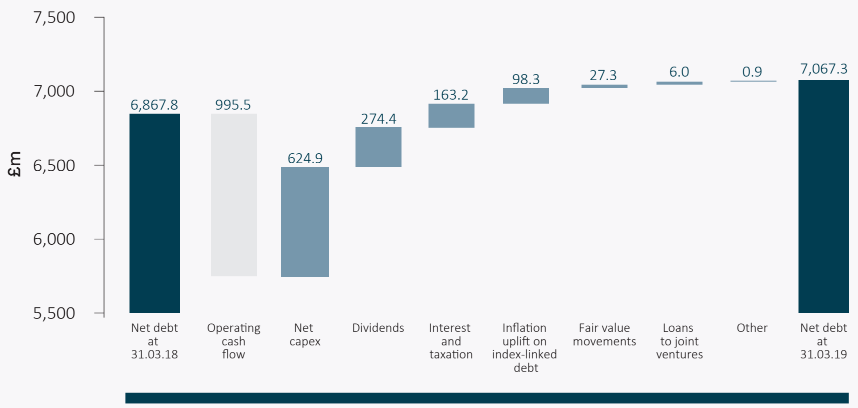
Tax

In addition to corporation tax, the group pays significant other contributions to the public finances on its own behalf as well as collecting and paying further amounts for its 5,000 strong workforce. The total payments for 2018/19 were around £241 million and included business rates, employment taxes, environmental taxes and other regulatory service fees such as water abstraction charges as well as corporation tax.

In 2018/19, we paid corporation tax of £28 million, which represents an effective cash tax rate on underlying profits of 6 per cent, which is 13 per cent lower than the headline rate of corporation tax of 19 per cent. We have expressed the effective cash tax rate in terms of underlying profits as this measure excludes fair value movements on debt and derivative instruments and thereby enables a medium-term cash tax rate forecast.

Our normal effective cash tax rate on underlying profits is around 11 per cent with the key reconciling items to the headline rate of corporation tax (currently at 19 per cent) being allowable tax deduction on capital investment and pension payments, these being deductions put in place by successive governments to encourage such investment and thus reflecting responsible corporate behaviour in relation to taxation.

Summary of net debt movement



In the current year the effective rate is further reduced as a result of the phasing of quarterly tax payments and also the impact of increased underlying profits as the relevant quarterly payments relate to 2017/18 whereas the underlying profits relate to 2018/19. This phasing of tax payments will not be an issue going forward, as from next year the quarterly instalment tax payment rules are being amended to ensure that payments become aligned with financial years.

The total tax charge for 2018/19 was £73 million as compared to a total tax charge of £78 million for 2017/18. For both periods, the total effective underlying tax rate remains in line with the headline rate (currently at 19 per cent) and subject to any legislative or tax practice changes, we would expect this to continue for the medium term.

The current tax charge was £42 million in 2018/19, compared with £25 million in the previous year; the main differences relating to timing with a corresponding equal and opposite adjustment to deferred tax. There were current tax credits of £3 million in 2018/19 and £7 million in 2017/18, following agreement of prior years' tax matters.

For 2018/19, the group recognised a deferred tax charge of £35 million, compared with a charge of £52 million for 2017/18. In addition, the group recognised a deferred tax credit of £1 million in 2018/19 and a deferred tax charge of £7 million in 2017/18 relating to prior years' tax matters.

Profit after tax

Underlying profit after tax of £379 million was £74 million higher than last year, principally reflecting the £90 million increase in underlying profit before tax.

The approach used to derive underlying profit after tax is not consistent across the industry, with the most significant difference relating to the treatment of deferred tax. Having considered whether to change our calculation of underlying profit after tax to exclude the impact of deferred tax, we have decided to retain our current methodology, therefore retaining comparability with our past performance and most FTSE companies but not our listed water peers. We will reassess this position once we have clarity of Ofwat's final determination, by which time it is also possible that there could be further clarity on the direction of travel of the IASB's rate-regulated activities project which could also have an impact on the underlying profit measures.

Reported profit after tax was £363 million, compared with £355 million in the previous year, largely reflecting the £4 million increase in the reported profit before tax.

Earnings per share

Underlying earnings per share increased from 44.7 pence to 55.5 pence. This underlying measure is derived from underlying profit after tax.

As noted above, we have considered whether to change our calculation of underlying profit after tax to exclude the impact of deferred tax and we have decided to retain our current methodology.

Basic earnings per share increased from 52.0 pence to 53.3 pence for the same reasons that caused the increase in profit after tax.

Dividend per share

The board has proposed a final dividend of 27.52 pence per ordinary share in respect of the year ended 31 March 2019. Taken together with the interim dividend of 13.76 pence per ordinary share, paid in February, this results in a total dividend per ordinary share for 2018/19 of 41.28 pence. This is an increase of 3.9 per cent, compared with the dividend relating to last year, in line with the group's dividend policy of targeting a growth rate of at least RPI inflation each year through to 2020. The inflationary increase of 3.9 per cent is based on the RPI element included within the allowed regulated revenue increase for the 2018/19 financial year (i.e. the movement in RPI between November 2016 and November 2017).

The final dividend is expected to be paid on 1 August 2019 to shareholders on the register at the close of business on 21 June 2019. The ex-dividend date is 20 June 2019.

Our dividend policy targets a growth rate of at least RPI inflation each year through to 2020, with further details set out below.

Policy period – the dividend policy aligns with the five-year regulatory period which runs from 1 April 2015 to 31 March 2020.

Policy approval process – the dividend policy was considered and approved by the United Utilities group board in January 2015, as part of a comprehensive review of the 2015–20 regulatory final determination in the context of a detailed business planning process, with due regard for the group's financial metrics, credit ratings and long-term financial stability, and is reviewed at least annually.

Distributable reserves – as at 31 March 2019, the company had distributable reserves of £3,139 million. The total external dividends relating to the 2018/19 financial year amounted to £282 million. The company's distributable reserves support over 11 times this annual dividend.

Financing headroom – supporting the group's cash flow, we adopt a funding/liquidity headroom policy of having available resources to cover the next 15–24 months of projected cash outflows on a rolling basis.

Cash flows from subsidiaries – the directors consider that the group's principal operating subsidiary, United Utilities Water Limited, has sufficient resources to pay dividends to United Utilities Group PLC for the duration of the current dividend policy period to support the external payment of dividends to shareholders.

Financial stability – the water industry has invested significant capital since privatisation in 1989 to improve services for customers and provide environmental benefits, a large part of which is driven by legislation. Water companies have typically raised borrowings to help fund the capital investment programme. Part of total expenditure is additive to the regulatory capital value, or RCV, on which water companies earn a return allowed by the economic regulator, Ofwat. RCV gearing is useful in assessing a company's financial stability in the UK water industry and is one of the key credit metrics that the credit rating agencies focus on. We have had a relatively stable RCV gearing level over the last nine years, always comfortably within our target range of 55 to 65 per cent, supporting a solid A3 credit rating for United Utilities Water Limited (UUW) with Moody's. RCV gearing at 31 March 2019 was 61 per cent and the movement in net debt is outlined in the cash flow section below.

Our performance in 2018/19

Financial performance

Dividend sustainability – in approving the policy, the board is satisfied that across the current regulatory period the projected dividend is adequately covered by underlying profit after tax. Separately, during the current regulatory period the executive directors' long-term incentive awards have been directly linked to a measure of sustainable dividends. While specific targets are not disclosed in advance, for commercial sensitivity reasons, there is a major focus on the creation of strong earnings that ensure the sustainability of dividends.

Viability statement – the dividend policy is underpinned by the group's long-term viability statement (contained within the group's annual report and financial statements). Assurance supporting this statement is provided by the review of: the group's key financial measures; the key credit financial metrics; the group's liquidity position; the contingent liabilities of the group; and the key risks of the group together with the associated mitigating actions.

Annual dividend approval process – the group places significant emphasis on strong corporate governance, and before declaring interim and proposing final dividends, the United Utilities group board undertakes a comprehensive assessment of the group's key financial metrics.

Policy sustainability

2015–20

- The policy is considered by the board to be sufficiently robust to withstand reasonable changes in assumptions, such as inflation, opex, capex and interest rates; and
- Extreme economic, regulatory, political or operational events, which could lead to a significant deterioration in the group's financial metrics during the policy period, may present risks to policy sustainability.

2020–25

- A dividend policy for the 2020-25 regulatory period will be formulated after Ofwat announces the outcome of the regulatory price review (currently expected in December 2019).

Cash flow

Net cash generated from continuing operating activities for the year ended 31 March 2019 was £832 million, and therefore broadly consistent with £816 million in the previous year. The group's net capital expenditure was £625 million, principally in the regulated water and wastewater investment programmes. This excludes infrastructure renewals expenditure which is treated as an operating cost under IFRS. Cash flow capex differs from regulatory capex, since regulatory capex includes infrastructure renewals expenditure and is based on capital work done in the period, rather than actual cash spent.

Net debt including derivatives at 31 March 2019 was £7,067 million, compared with £6,868 million at 31 March 2018. This increase largely reflects regulatory capital expenditure, payments of dividends, interest and tax, the inflationary uplift on index-linked debt and fair value movements, partly offset by operating cash flows.

Gross debt – total carrying value £7,815.7 million

Yankee bonds (USD)	£373.9m
Euro bonds (EUR)	£619.8m
GBP bonds	£1,801.1m
GBP RPI-linked bonds	£2,045.2m
GBP CPI-linked bonds	£171.0m
EIB and other RPI-linked bonds	£1,559.5m
Other EIB loans	£606.2m
Other borrowings	£639.0m

Fair value of debt

The group's gross borrowings at 31 March 2019 had a carrying value of £7,816 million. The fair value of these borrowings was £8,905 million. This £1,089 million difference principally reflects the significant fall in real interest rates compared with the rates at the time we raised a portion of the group's index-linked debt. This difference has decreased from £1,140 million at 31 March 2018 due primarily to an increase in credit spreads.

Debt financing and interest rate management

Gearing, measured as group net debt divided by UUW's shadow (adjusted for actual spend) regulatory capital value, was 61 per cent at 31 March 2019. This is the same level of gearing as at 31 March 2018 and remains comfortably within our target range of 55 to 65 per cent.

UUW's senior unsecured debt obligations are rated A3 from Moody's Investors Service (Moody's), A- from Standard & Poor's Ratings Services (S&P) and A- from Fitch Ratings (Fitch), all on stable outlook. United Utilities PLC's (UU PLC's) senior unsecured debt obligations are rated Baa1 from Moody's, BBB from S&P and A- from Fitch, all on stable outlook.

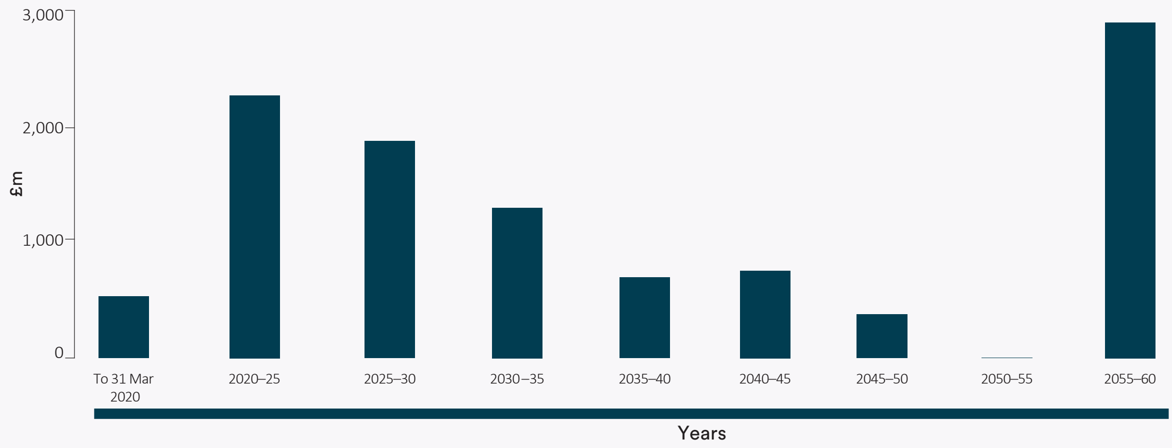
The group has access to the international debt capital markets through its €7 billion euro medium-term note (EMTN) programme. The EMTN programme does not represent a funding commitment, with funding dependent on the successful issue of the notes.

Cash and short-term deposits at 31 March 2019 amounted to £339 million. Over 2015–20 we have financing requirements totalling around £2.5 billion to cover refinancing and incremental debt, supporting our five-year investment programme, and we have now raised all of this requirement.

In January 2019, UUW's financing subsidiary, United Utilities Water Finance PLC (UUWF), raised around £32 million of term funding, via the issue of HKD320 million private placement notes, with a seven-year maturity, off our EMTN programme. Also in January 2019, UUWF increased the amount outstanding on its £350 million public bond with a maturity date in February 2025 by an additional £100 million, taking the total size to £450 million. In February 2019, UUWF raised £250 million fixed rate notes in the public bond market with a 12-year maturity.

UUW remains one of the sector leaders in the issuance of CPI-linked debt having previously raised £165 million, in response to Ofwat's decision to transition away from RPI inflation linkage. In April 2019, we have increased the CPI-linkage in our debt portfolio by a further £200 million by executing a new £100 million bank loan with a 10-year maturity, and entering into inflation swaps against three existing RPI-linked bonds with a notional value of around £100 million, swapping cash flows from RPI to CPI-linkage. As both the CPI-linked loan and inflation swaps were executed subsequent to the year end, neither are included in the statement of financial position as at 31 March 2019.

Term debt maturity per regulatory period



Since September 2018, the group has renewed £100 million of committed bank facilities for an initial five-year term, extended a further £50 million by one year to 2024 and signed £50 million of new committed bank facilities with a five-year term. The group has sufficient headroom to cover its financing needs into late 2020.

Long-term borrowings are structured or hedged to match assets and earnings, which are largely in sterling, indexed to UK retail price inflation and subject to regulatory price reviews every five years.

Long-term sterling inflation index-linked debt provides a natural hedge to assets and earnings. At 31 March 2019, approximately 53 per cent of the group's net debt was in index-linked form, representing around 32 per cent of UUW's regulatory capital value, with an average real interest rate of 1.3 per cent. The long-term nature of this funding also provides a good match to the company's long-life infrastructure assets and is a key contributor to the group's average term debt maturity profile, which is just under 20 years.

Our inflation hedging policy is to target around 50 per cent of net debt to be maintained in index-linked form. This reflects a balanced assessment across a range of factors.

Where nominal debt is raised in a currency other than sterling and/or with a fixed interest rate, the debt is generally swapped to create a floating rate sterling liability for the term of the debt. To manage exposure to medium-term interest rates, the group fixes underlying interest costs on nominal debt out to ten years on a reducing balance basis. Historically, this has been supplemented by fixing substantially all remaining floating rate exposure across the forthcoming regulatory period around the time of the price control determination. In line with this, the group has fixed interest costs for substantially all of its floating rate exposure over the 2015-20 regulatory period, locking in an average annual interest rate of around 3.2 per cent nominal (inclusive of credit spreads).

Recognising Ofwat's intention to apply debt indexation for new debt raised during the 2020–25 regulatory period, we will retain the hedge to fix underlying interest costs on nominal debt out to ten years on a reducing balance basis, but we will no longer supplement this with the additional 'top-up' fixing at the start of each new regulatory period.

Liquidity

Short-term liquidity requirements are met from the group's normal operating cash flow and its short-term bank deposits and supported by committed but undrawn credit facilities. The group's €7 billion EMTN programme provides further support.

Available headroom at 31 March 2019 was £357 million based on cash, short-term deposits and committed bank facilities, net of short-term debt as well as committed facilities and term debt falling due within 12 months.

We consider that we operate a prudent approach to managing banking counterparty risk. Counterparty risk, in relation to both cash deposits and derivatives, is controlled through the use of counterparty credit limits. Our cash is held in the form of short-term money market deposits with prime commercial banks.

We operate a bilateral rather than a syndicated approach to our core relationship banking facilities. This approach spreads maturities more evenly over a longer time period, thereby reducing refinancing risk and providing the benefit of several renewal points rather than a large single refinancing requirement.

Pensions

As at 31 March 2019, the group had an IAS 19 net pension surplus of £484 million, compared with a net pension surplus of £344 million at 31 March 2018. This £140 million increase mainly reflects the favourable impact of updating mortality assumptions and updating membership data based on the 2018 funding valuations. The scheme-specific funding basis does not suffer from volatility due to inflation and credit spread movements as it uses a prudent, fixed credit spread assumption. Therefore, any inflation and credit spread movements have not had a material impact on the deficit calculated on a scheme-specific funding basis or the level of deficit repair contributions.

The most recent pension scheme valuation was signed off as at 31 March 2018 and confirmed the existing schedule of contributions which aimed to eliminate the funding deficit by December 2021 for the United Utilities Pension Scheme (UUPS) and by September 2024 for the United Utilities PLC group of the Electricity Supply Pension Scheme (ESPS). As of April 2019, the group has prepaid at a discount the agreed deficit recovery contributions, resulting in a one-off contribution of around £100 million, and has therefore eliminated any deficit on a scheme-specific funding basis. As this took place subsequent to the year end, it has had no impact on the financial statements for the year ended 31 March 2019.

Further detail on pensions is provided in notes 18 and A5 ('Retirement benefit surplus') of these financial statements.

Our performance in 2018/19

Financial performance

Strategic report

Guide to Alternative Performance Measures (APMs)

The underlying profit measures in the table opposite represent the group's alternative performance measures (APMs) under the definition given by the European Securities and Markets Authority (ESMA). These measures are linked to the group's financial performance as reported under International Financial Reporting Standards (IFRSs) as adopted by the European Union in the group's consolidated income statement, which can be found on page 162. As such, they represent non-GAAP measures.

These APMs are reviewed internally by management and reported to the board, and have been presented in order to provide a more representative view of business performance. The group determines adjusted items in the calculation of its underlying measures against a framework which considers significance by reference to profit before tax, in addition to other qualitative factors such as whether the item is deemed to be within the normal course of business, its assessed frequency of reoccurrence and its volatility which is either outside the control of management and/or not representative of current year performance.

Adjustments in arriving at underlying profit measures

Flooding incidents	Two significant flooding incidents in the year ended 31 March 2016 caused extensive damage to localised parts of our infrastructure, resulting in significant levels of remedial operating expenditure and a large claim under the group's insurance cover. Management's view is that these were significant and infrequent events and, as such, were not part of the normal course of business.
Non-household retail market reform	The group has incurred significant costs since the year ended 31 March 2015 relating to the non-household retail market opening to competition in April 2017. This represents a one-off event and, as such, is not considered part of the normal course of business.
Dry weather event	An extreme period of hot and dry weather during the summer of 2018 led to significant strain being placed on our water resources and network and as a result our reservoir levels ran extremely low. Activities were carried out to safeguard supplies, generating significant costs which would not have been incurred under normal conditions. Given the infrequent nature of periods of dry weather of this severity, this event is not considered part of the normal course of business.
GMP equalisation	The group has recognised an additional part service cost in respect of its defined benefit pension schemes. This reflects a change in benefits following a legal ruling during the year relating to the equalisation of Guaranteed Minimum Pension (GMP) benefits between males and females. This is a one-off adjustment, which is not representative of costs incurred in the normal course of business, is a direct consequence of the ruling and is not expected to reoccur in future years.
Restructuring costs	The group has incurred restructuring costs in the past in relation to a number of discrete underlying events which can cause volatility in the reported results. Management adjusts internally for these costs to provide an underlying view of performance which it views as being more representative of the normal course of business and more comparable period to period.
Net fair value gains on debt and derivative instruments	Fair value movements on debt and derivatives can be both very significant and volatile from one period to the next. These movements are determined by macroeconomic factors which are outside the control of management and these instruments are purely held for funding and hedging purposes (not for trading purposes). Taking these factors into account, management believes it is useful to adjust for this to provide a more representative view of performance.
Interest on derivatives and debt under fair value option	Net fair value gains on debt and derivative instruments includes interest on derivatives and debt under fair value option. In adjusting for net fair value gains on debt and derivatives, it is appropriate to add back interest on derivatives and debt under fair value option to provide a view of the group's cost of debt which is better aligned to the return on capital it earns through revenue.
Net pension interest income	This item can be very volatile from one period to the next and it is a direct function of the extent to which the pension scheme is in an accounting deficit or surplus position. Management believes it is useful to adjust for this to provide a more representative view of performance.
Capitalised borrowing costs	Accounting standards allow for the capitalisation of borrowing costs in the cost of qualifying assets. Management believes it is appropriate to adjust for these significant costs to provide a representative cost of borrowings and current year performance which is better aligned to the return on capital it earns through revenue.
Agreement of prior years' tax matters	The agreement of prior years' tax matters can be significant, volatile and often related to the final settlement of numerous prior year periods. Management adjusts for this to provide a more representative view of current year performance.
Tax in respect of adjustments to underlying profit before tax	Management adjusts for the tax impacts of the above adjusted items to provide a more representative view of current year performance.

Underlying profit

Operating profit	Year ended 31 March 2019 £m	Year ended 31 March 2018 £m
Reported operating profit	**634.9**	636.4
Flooding incidents (net of expected insurance proceeds)	–	1.7
Non-household retail market reform	–	1.0
Dry weather event	**36.1**	–
GMP equalisation	**6.6**	–
Restructuring costs	**7.2**	6.0
Underlying operating profit	**684.8**	645.1

Net finance expense	£m	£m
Finance expense	**(222.5)**	(218.6)
Investment income	**17.1**	12.0
Reported net finance expense	**(205.4)**	(206.6)
Adjustments:		
Net fair value gains on debt and derivative instruments	**(9.5)**	(47.3)
Interest on derivatives and debt under fair value option	**30.6**	23.5
Net pension interest income	**(9.5)**	(7.1)
Adjustment for capitalised borrowing costs	**(37.4)**	(39.7)
Underlying net finance expense	**(231.2)**	(277.2)

Profit before tax	£m	£m
Share of profits of joint ventures	**6.7**	2.3
Reported profit before tax	**436.2**	432.1
Adjustments:		
Flooding incidents	–	1.7
Non-household retail market reform	–	1.0
Dry weather event	**36.1**	–
GMP equalisation	**6.6**	–
Restructuring costs	**7.2**	6.0
Net fair value gains on debt and derivative instruments	**(9.5)**	(47.3)
Interest on derivatives and debt under fair value option	**30.6**	23.5
Net pension interest income	**(9.5)**	(7.1)
Capitalised borrowing costs	**(37.4)**	(39.7)
Underlying profit before tax	**460.3**	370.2

Profit after tax	£m	£m
Underlying profit before tax	**460.3**	370.2
Reported tax charge	**(72.8)**	(77.5)
Agreement of prior years' UK tax matters	**(4.2)**	0.4
Tax in respect of adjustments to underlying profit before tax	**(4.6)**	11.8
Underlying profit after tax	**378.7**	304.9

Earnings per share	£m	£m
Reported profit after tax (a)	**363.4**	354.6
Underlying profit after tax (b)	**378.7**	304.9
Weighted average number of shares in issue, in millions (c)	**681.9m**	681.9m
Reported earnings per share, in pence (a/c)	**53.3p**	52.0p
Underlying earnings per share, in pence (b/c)	**55.5p**	44.7p

Dividend per share	**41.28p**	39.73p

Our risk management

Principal risks and uncertainties

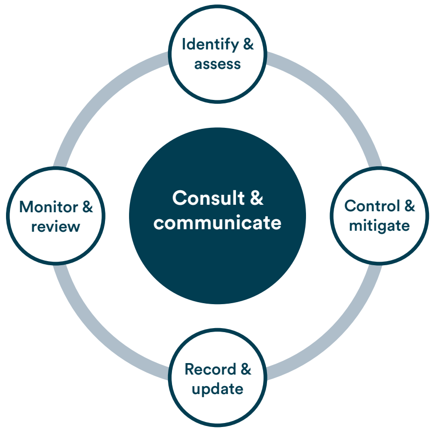
Our management of risk underpins the delivery of our purpose and strategy and enables us to focus on providing a sustainable and resilient service for all customers and stakeholders for years to come

In delivering our group-wide activity we are faced with a range of risks which can threaten the quality of the services we provide, introduce delays and ultimately increase cost and damage the reputation of the group. We anticipate and mitigate these risks through an embedded risk management framework which includes:

- A consistent and reliable enterprise-wide risk management process;
- A governance and reporting structure which enables the board to oversee and direct the control of risk;
- Definition of risk appetite by the board with an overarching general risk appetite supplemented where appropriate by specific risk appetites for certain risks;
- An ISO 31000:2018 aligned assessment and mitigation process; and
- Policies, practical guidance and training programmes to enable our people to identify, quantify and manage risk effectively.

Our risk identification and management activities are continuous and ongoing, with each functional area responsible for assessing, articulating and controlling relevant risks.

Figure 1: Assessment and management process adapted from ISO 31000:2018



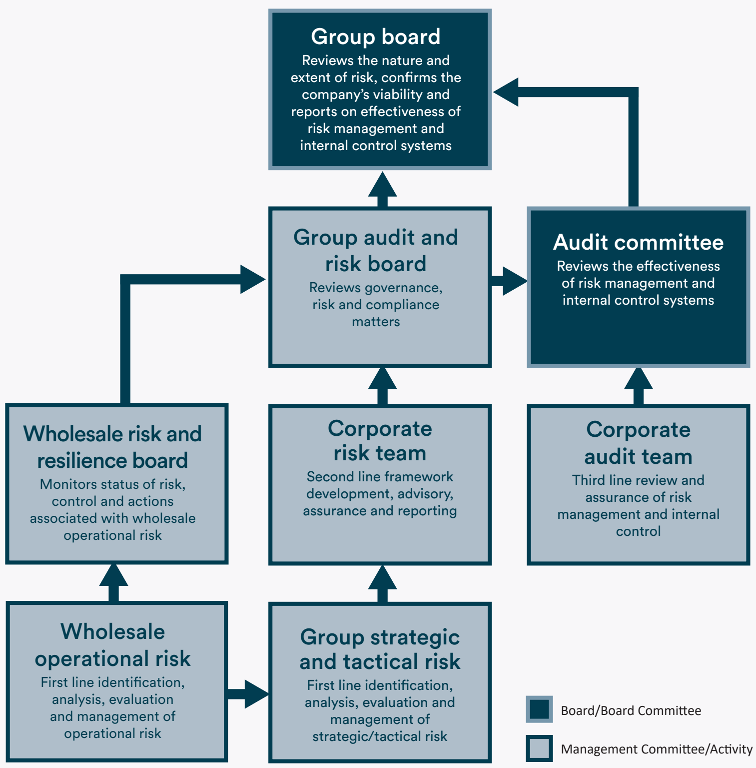
This includes horizon scanning of the internal and external business environment, to identify and review new and emerging risks that could lead to a future impact or emerging circumstances of existing risk that could affect the exposure in the short to medium term.

Risk events are assessed in their current state for the likelihood of occurrence based on the level of threat and the vulnerability of controls, together with the financial and reputational impacts should the identified events materialise. Where we are not satisfied that the current state is consistent with our general risk appetite, or where it could present an unacceptable risk in relation to a specific risk appetite, we determine an appropriate risk exposure as a target state and develop further mitigating controls to deliver this position within an appropriate time frame.

In order to maintain adequate oversight of risk, there are various steering groups and governance forums that focus on individual risks which then escalate and share progress to the group audit and risk board either directly or via the wholesale risk and resilience board.

A complete oversight of our enterprise-wide profile is presented every six months to the group board to highlight the nature and extent of the current risk exposure with focus on the most significant risks relative to the group's principal risks.

Figure 2: Governance and reporting process



Our approach is in accordance with the UK Corporate Governance Code and incorporates reporting to the group board for every full and half year statutory accounting period. This enables the board to:

- Determine the nature and extent of the principal risks it is willing to take in achieving its strategic objectives;
- Oversee the management of those risks and provide challenge to executive management where appropriate;
- Express an informed opinion on the long-term viability of the company; and
- Monitor risk management and internal control systems and review their effectiveness.

We categorise the nature of our principal risks to cover potential issues within the following four categories: Regulatory and legal; Core operations and service provision; Functional service and support; and Hazard-based.

Reports to the board highlight major risks based on the highest impact business risks across the group and wholesale operational risks. These comprise the ten highest scoring risks assessed on the basis of likelihood and financial impact for each of the two categories. In addition, the report covers risks which were scored highly for the severity of their impacts in their current state (net of control effectiveness) but remote on likelihood. The board report also highlights risks where there could be significant reputational impact or which relate to significant new or emerging risks or issues, but which are not encompassed within the other reported categories.

Key developments

Ofwat's Initial Assessment of Plans (IAP) following the price review submission recognised our leading approach to risk and resilience. Our approach is a combination of top-down assessment, where we consider the impacts on strategic delivery, and bottom-up where we consider localised operational performance, asset health and operational hazards. We have an established approach for the two elements, but continue to drive improved maturity through various initiatives which focus on improved appreciation of related data and information to understand our long-term risk profile, to support decision-making and to deliver a cost-effective and proportionate risk management response which drives resilience.

These initiatives include:

- Continuation of our focus on cross-business consideration of strategic and tactical risks, for example an in-depth cyber risk assessment that took place throughout the year (see risk feature at page 71) and Brexit contingency planning below;
- Improvement of our maturity in relation to risk appetite – we have commenced reporting against a general risk appetite boundary and, where appropriate, specific risk appetite boundaries enabling more targeted discussions over the last year (an approach we intend to continue to develop and embed);
- Development of the assessment and reporting of the full distribution of impacts, including possible maximum and minimum outcomes as well as more likely occurrences. This supports our focus on long-term resilience and tests our response and recovery plans and expectations;
- Ongoing development of our wholesale risk and asset planning process to prioritise investment and operational management through the identification of risks and issues and monitoring of strategic performance requirements; and
- An assurance-based strategy within the engineering and programme management team introducing programme and portfolio risk responsibilities and improving capability by focusing on reliable risk information, ownership and learning from risk events.

Profile features

Our risk profile, which currently consists of around 100 event-based risks is enterprise-wide, covering risk across the entire group and considering both internal and external drivers. By their nature, these risks will include many combinations of high to low likelihood and high to low impact.

Political and regulatory risk and uncertainty feature prominently within the profile, notably with the outcome of PR19 being delivered this calendar year. The possibility of 'renationalisation' is a key area of uncertainty as is the opening up to competition of wholesale operations (including the current focus on possible competition in bioresources and water abstraction) and the potential for competition covering domestic retail activities.

Our operations continue to be substantially UK-based, but the potential impacts of Brexit remain under review and have been reported to the group board. In common with other UK companies, a significant issue is the uncertainty surrounding the effects of any Brexit deal that the UK Government may ultimately deliver. Our review has considered the availability of European funding, the availability of critical goods (including chemicals and spare parts) through our supply chain, the price of goods and services due to tariff changes, exchange rate changes and potential inflationary shifts outside current predicted parameters, the effect to the labour resource of both the company and our delivery partners and our ability to collect cash were there to be an economic downturn. For each of these consequences, the impact assessment considers a range of possible impact scenarios and we have developed a contingency plan (in collaboration with Water UK) which has involved discussing the implications of Brexit with our key suppliers and capital delivery partners, as well as considering mitigation measures such as stockpiling and using alternative suppliers, a large proportion of which is already built into our multi-party frameworks.

Following the launch of non-household retail competition in April 2017, we have continued to monitor our operations in the market to review compliance risks and to ensure that we continue to operate in a manner that complements and promotes the 'level playing field'.

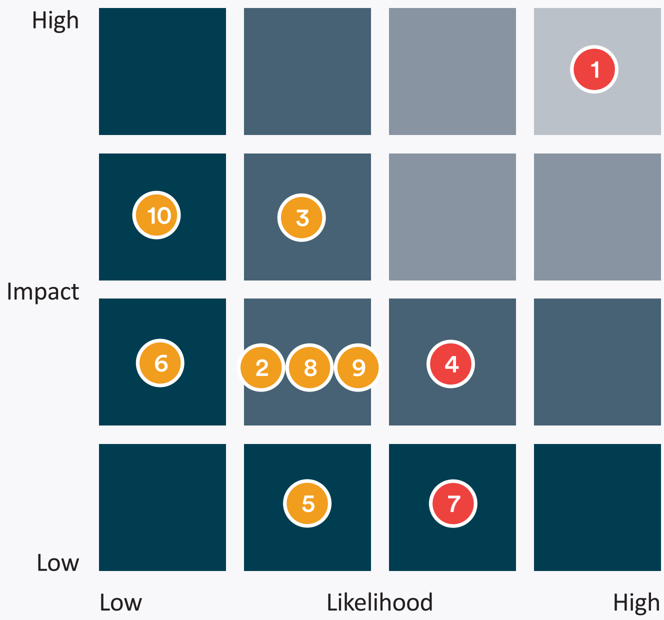
From an operational risk perspective, the dominance of the penalty element of Ofwat's outcome delivery incentive mechanism and the continuing effects of changes to the Environmental Sentencing Guidelines continue to be key features of evolving exposure. Reputationally, our core operations/service provision (notably water service) and health, safety and environmental risks have the highest focus for monitoring and reviewing control effectiveness based on the potential impact should the risk event occur.

We continue to adapt to and plan for climate change and its significant and permanent impacts on the water cycle, our operations and the broader operating environment. This includes consideration of the long-term viability of water and wastewater services such as water abstraction, drinking water supply and treatment capability, drainage and sewer capacity, wastewater treatment and its discharge efficiency and effectiveness. The recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) support and reinforce the need to consider climate-related risks and uncertainties. These continue to be factored into risk management and the likely effects of future changes are a critical consideration in our long and medium-term risk, operational and financial planning (see also Key resources on pages 28 to 34 and Our approach to resilience on page 50). Our water service and wastewater service risks (summarised on page 73) also reflect current key risks including the potential for extreme weather and climate change.

TCFD TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

Our risk management
Principal risks and uncertainties

Figure 3: Risk map



1. Political and regulatory
2. Conduct and compliance risk
3. Water service
4. Wastewater service
5. Retail and commercial
6. Financial
7. Supply chain and programme delivery
8. Resources
9. Security
10. Health, safety and environmental

- Risk increased
- Risk decreased
- Risk stable

The risk map provides an indicative only view of the current exposure of each of the principal risks relative to each other: illustrating the likelihood of occurrence relative to the associated internal or external drivers; whether the risk is believed to have increased, decreased or remained stable over the last 12 months; and the most likely impact should an event occur.

Material litigation

The group robustly defends litigation where appropriate and seeks to minimise its exposure by establishing provisions and seeking recovery wherever possible. Litigation of a material nature is regularly reported to the group board.

Beyond that reported in previous years on the Argentina multiparty 'class action' and the Manchester Ship Canal Company matters (to which there have been no material developments), there is nothing specific to report on material litigation.

Principal risks

The ten principal risks (combinations of relevant event-based risks) identified in the risk map and described in more detail in the tables which follow, illustrate where value can be lost or gained and could have a material impact on the group's business model, future performance, solvency or liquidity. For each principal risk the nature and the extent of exposure is recorded, with alignment to our strategic themes and mitigating controls identified. Also described are key risks worthy of note, together with current issues and areas of uncertainty. These reflect changing/emerging circumstances which could affect the risk exposure of future activities and are therefore considered as part of the ongoing mitigation.

Mitigating the risk of cyber crime

Taking a holistic approach to our control framework

The threat

Malicious cyber activity is well publicised and we see continuous attempts from state-sponsored and criminal groups to breach our protective controls to steal data. As a water utility and operator of critical national infrastructure (CNI) we are further exposed to the increased risk of targeted attacks intended to cause disruptive impact to the UK.

We also need to consider the threat posed by a complex partner ecosystem that supports our increasing reliance upon new technologies and cloud services that underpin our digital strategy. Equally, the advancements in technology that make our lives more efficient and interconnected also start to blur work/personal boundaries, thereby increasing the threat.

The risks

The most significant cyber risks for our organisation are:

- Breach of customer, employee or sensitive business data resulting in the data reaching the public domain or unauthorised groups;
- Critical service, technology or data unavailability resulting in disruption to business processes and system failures;
- Loss of data integrity leading to operational/customer impacts and exposure to the risk of fines and penalties; and
- Compromise of operational resources by malicious groups, leading to service disruptions, loss of supply or environmental breaches.

Cyber risk mitigation

We take a holistic view of the risks and mitigation options to define the strategy, control framework and plan by which we protect our data and information assets. We deliver this through our governance framework, which includes executive level engagement and regular reporting to our group board.

Our security controls framework includes the following:

- Through the integration of our IT and Operational Technology (OT) functions within our Digital Services business unit, we have integrated our security operational management practices and implemented a single delivery programme for our security strategy.
- A security strategy covering all areas of our business that provides the baseline for our compliance with the Network and Information Systems Directive (NISD). Our strategy is underpinned by our security investment plan, which has been set to deliver the required control capabilities.
- A cyber incident response plan that includes the services of third party specialist forensic responders, including government agencies, who provide support in the event of a critical cyber incident.
- A suite of testing options to validate control effectiveness, e.g. penetration testing, audits and scans. We periodically take this testing a stage further and employ specialist 'Brand Damage' experts to simulate a real attack on our business.
- Through our Information Security team we undertake assurance activities across the full life cycle of all technology and data solutions.
- To provide the most secure environments possible for customer data and services, we undertake comprehensive, always-on monitoring of all critical IT systems for any unexpected security events.
- Through proactive government and industry engagement we have developed good practice guidance and created support communities to foster collaboration. Our staff currently hold the chair positions of the Water Sector Strategic Security Board and the Water Security Information Exchange.
- We have an extensive employee cyber education and awareness programme that highlights areas of risk, policies and controls to provide the guidance and understanding of the cyber threat. Beyond employee education, we have also invested in specialist training and certification for our Information Security team who hold internationally recognised accreditations.

"We have an extensive employee cyber education and awareness programme"

Our risk management
Principal risks and uncertainties

Risk exposure:
An indication of each category's current exposure relative to the previous year is shown by the coloured disc surrounding the risk number.

- Increased
- Decreased
- Stable

Strategic themes:
- The best service to customers
- At the lowest sustainable cost
- In a responsible manner

Regulatory and legal

1 Political and regulatory risks
Potential change in the political and regulatory environment and/or frameworks

Main strategic theme:

Principal/significant impacts:
Potential for increased costs of administration, reduction in income, margin and greater uncertainty of returns.

Potential that reduced confidence among equity investors and difficult debt market conditions lead to funding pressures in the context of raising finance and refinancing debt on an ongoing basis.

In the event of renationalisation the business could be acquired below fair value.

Management and mitigation:
We regularly engage in relevant government and regulatory consultations which may affect policy and regulation in our industry as well as consulting with the opposition. We also consult our customers to better understand their requirements and proactively consider opportunities and threats associated with any potential change, exploiting opportunities and mitigating risks where appropriate. We keep customers and the public informed. We also provide information to the government, regulators, customers and the public as appropriate to help them to make informed decisions.

Current key risks, issues and uncertainties:
› Potential renationalisation of the water sector

› Further market reform including upstream competition in water resources and bioresources, as well as additional markets in future, and the potential for the introduction of domestic competition

› Final determination of PR19 and associated tougher regulatory targets

› Brexit and potential changes to the regulatory regime

2 Conduct and compliance risk
The failure to meet all legal and regulatory obligations and responsibilities

Main strategic theme:

Principal/significant impacts:
The detrimental impact to customers and other stakeholders through inappropriate culture, behaviour or decisions and the potential to receive penalties of up to 10 per cent of relevant turnover and ultimately revocation of our licence or the appointment of a special administrator.

Management and mitigation:
Corporate social responsibility features prominently within the group. We work in collaboration with landowners, environmental organisations, community groups and other stakeholders to deliver enhanced environmental outcomes and engage with the community and support agencies regarding vulnerable customers and ensure diversity and equality of employees and an ethical supply chain.

Legislative and regulatory developments are continually monitored as is the governance framework utilised by the group. Risk-based training of employees is undertaken and we participate in consultations to influence legislative and regulatory developments. Allowance for any material additional compliance costs in the regulated business is sought as part of the price determination process. The group also robustly defends litigation where appropriate and seeks to minimise its exposure by establishing provisions and seeking recovery wherever possible.

Current key risks, issues and uncertainties:
› The effects of Brexit on legislation/laws, enforcement and the regulatory regime

› Competition law requirements in relation to the non-household retail market and other competitive markets

› Current material litigation

› Continuing high fines for environmental offences

› Data management and governance (GDPR)

Core operations and service provision

3

Water service risk

A failure to provide a secure supply of clean, safe drinking water and the potential for a negative impact on public confidence in water supply

Main strategic theme:

Principal/significant impacts:

The potential for public health issues associated with poor water quality.

The potential for supply interruptions that could affect large populations within the region for long durations.

Management and mitigation:

Mitigation is provided through core business processes, including centralised planning and control, quality assurance procedures, risk assessments and rigorous sampling/testing regimes. Optimisation of operational and maintenance tasks together with targeted capital interventions help to ensure services to customers are maintained.

Our 25-year Water Resources Management Plan defines our strategy to achieve a long-term, best-value and sustainable plan for water supplies in the North West including consideration of multiple different climate change scenarios including a 2 degree (Celsius) global warming scenario (assessing systems resilience).

We continue to develop innovative solutions and invest in resilience to further support the delivery of water and wastewater services in the long term.

Current key risks, issues and uncertainties:

- Population growth
- Extreme weather, climate change and drought
- Expected change to the abstraction licensing regime
- Drinking water safety and security
- Critical asset failure
- Brexit, in particular the effects of a no-deal scenario on the chemicals supply chain

4

Wastewater service risk

A failure to remove and treat wastewater

Main strategic theme:

Principal/significant impacts:

The potential for sewer flooding or serious pollution to air, soil or water leading to harm or disruption to the public, businesses and the environment (wildlife, fish and natural habitats) resulting in fines and reputational damage.

Management and mitigation:

Mitigation is provided through core business processes, including centralised planning and control, quality assurance procedures, risk assessments, rigorous sampling/testing regimes and close management of discharge consent requirements. Optimisation of operational and maintenance tasks together with targeted capital interventions help to ensure services to customers are maintained.

Current key risks, issues and uncertainties:

- The effects of extreme weather on overloading the sewer network
- Pollution incidents
- Population growth
- Increased regulatory scrutiny and penalties
- Higher fine levels for environmental offences
- Climate change
- Brexit, in particular the effects of a no-deal scenario on the chemicals supply chain

5

Retail and commercial risk

Failing to provide good and fair service to domestic customers and third-party retailers or a failure of or issue in relation to non United Utilities Water operations or businesses (including Water Plus)

Main strategic theme:

Principal/significant impacts:

The potential for significant losses, regulatory penalties and long-term reputational damage associated with poor customer satisfaction. The potential for a significant increase in the bad debt charge, reducing profitability.

Management and mitigation:

For domestic retail there is a wide range of initiatives and activities focused on improving customer satisfaction, including proactive incident communication, complaints handling and use of appropriate tariffs. Bad debt risk is managed through the adoption of best practice collection techniques, segmentation of customers based on their credit risk profile and the use of data sharing to better understand customers' circumstances to determine the most appropriate collection and support activities. Our wholesale business maintains processes, systems, data and organisational capacity and capability to deal fairly with market participants and the central market operator in the Business Retail market in order to generate and collect revenue. Similarly strong governance applies to non United Utilities Water operations and businesses.

Current key risks, issues and uncertainties:

- Socio-economic deprivation in the North West
- Economic downturn (due to welfare reform, Brexit or other factor) and the effect on domestic bad debt
- Competition in the water and wastewater market and competitor positioning
- Non-household retail competition and the ability to treat other participants equally
- The challenges associated with being involved in a joint venture water retail business operating in a competitive environment

Our risk management
Principal risks and uncertainties

Functional service and support

6

Financial risk
Potential inability to finance the business appropriately

Main strategic theme:

Principal/significant impacts:
The potential for worse credit ratings, associated funding costs or reduced access to debt capital markets leading to lower liquidity and adversely impacting the economic return on the regulatory capital value (RCV).

Tax inefficiencies, under or overpayment of tax, market fluctuations in inflation, interest rates and energy prices and a potential worsening of the pension scheme funding position could all lead to a significant increase in costs to the group.

Management and mitigation:
Refinancing is long-term with staggered maturity dates to minimise the effect of short-term downturns. Counterparty credit exposure and settlement limits exist to reduce any potential future impacts. These are based on a number of factors, including the credit rating and the size of the asset base of the individual counterparty. The group also employs hedging strategies to manage the impact of market fluctuations for inflation, interest rates and energy prices. Sensitivity analysis is carried out as part of the business planning process, influencing the various financial limits employed. Continuous monitoring of the markets takes place including movements in credit default swap prices and movements in equity levels.

Current key risks, issues and uncertainties:
› Inflation/deflation
› Financial market conditions, interest rates and funding costs due to economic uncertainty (e.g. Brexit)
› Paying an appropriate amount of tax

7

Supply chain and programme delivery
Potential ineffective delivery of capital, operational and change programmes/processes

Main strategic theme:

Principal/significant impacts:
The potential failure to meet our obligations and customer outcomes resulting in an impact at future price reviews, negative reputational impact with customers and regulators.

Management and mitigation:
Supply chain management is utilised to deliver an end-to-end contract management service, including contract strategy, tendering and category management, which provides a risk-based approach and relationship management programmes for suppliers. We prioritise our investment programmes, projects and integrated business and asset plans. We have created better alignment and integration between our capital delivery partners and engineering service providers including alignment with our operating model.

Our programmes and project management capabilities are well established with strong governance and embedded processes to support delivery, manage risks and achieve business benefits. We utilise a time, cost and quality index (TCQi) as a key performance indicator and enhance our performance through a dedicated programme change office to deliver change in a structured and consistent way.

Current key risks, issues and uncertainties:
› New partnership structure and arrangement in AMP 7
› Direct procurement for customers (DPC)
› Technical quality and innovation
› Brexit and increased uncertainty of availability of materials sourced from Europe

8

Resources risk
Failing to provide appropriate resources (human, technological or physical resource) required to support business activity

Main strategic theme:

Principal/significant impacts:
The potential inability to recruit, retain or deploy knowledge and/or expertise.

The potential inability to respond and recover due to ineffective non resilient business activity.

Management and mitigation:
Developing our people with the right skills and knowledge, combined with delivering effective technology are important enablers to support the business to meet its objectives. Employees are kept informed regarding business strategy and progress through various communication channels. Training and personal development programmes exist for all employees in addition to talent management programmes and apprentice and graduate schemes. We focus on change programmes and innovative ways of working to deliver better, faster and more cost-effective operations.

Current key risks, issues and uncertainties:
› Delivering required employee engagement
› Personal development, talent management and succession planning
› Optimising technology and innovation

Hazard-based

9

Security risk

Potential for malicious activity (physical or technological) against people, assets or operations

Main strategic theme:

Principal/significant impacts:

The potential for a loss of data/information and the consequent effect on service provision.

The potential for catastrophic damage to UU property, infrastructure and non-infrastructure and the consequent effect on service provision.

Management and mitigation:

Physical and technological security measures and awareness training combined with strong governance and inspection regimes aim to protect infrastructure, assets and operational capability. Externally, we work closely with our industry peers, the Centre for the Protection of National Infrastructure (CPNI), the National Cyber Security Centre (NCSC), the Drinking Water Inspectorate (DWI) and Defra to shape the sector approach to security, particularly cyber security, and to understand how we can best deliver the appropriate levels of protection to our business and in compliance with the new Network and Information Systems Directive (NIS). Ongoing system and network integration improves operational resilience and we maintain robust incident response, business continuity and disaster recovery procedures. We also maintain insurance cover for loss and liability, and the licence of the regulated business also contains a ‘shipwreck’ clause that, if applicable, may offer a degree of recourse to Ofwat/customers in the event of a catastrophic incident.

Current key risks, issues and uncertainties:

- Cyber crime (see page 71)
- Terrorism
- Fraud
- Ownership of critical national infrastructure and national infrastructure

10

Health, safety and environmental

Potential harm to people (employees, contractors or the public) and the environment

Main strategic theme:

Principal/significant impacts:

The potential for serious injury or loss of life in remote, extreme circumstances.

The potential for catastrophic damage to private, public or commercial property/infrastructure including the consequent effect on water and wastewater service provision.

The potential for serious impact on wildlife, fish or natural habitats resulting in significant fines and reputational damage.

Management and mitigation:

Supported by strong governance and management systems certified to OHSAS 18001 we have developed a strong health and safety culture where ‘nothing we do at United Utilities is worth getting hurt for’. We actively seek to improve health, safety and wellbeing across the group through targeted improvements and benchmarking against our peers. Also certified to ISO 14001, we seek to protect and improve the environment through the responsible delivery of our services. This includes helping to support rare species and habitats through targeted engagement and activity and commitment to reducing our carbon emissions by designing out waste from our operations, generating our own energy and looking at ways to reduce our use of raw materials. We also recognise the impact the environment can have on our service provision with extreme weather and climate change being integrated into our risk, planning and decision-making processes.

Current key risks, issues and uncertainties:

- Impounding reservoirs containing significant volumes of water
- Other critical asset failure
- Multiple hazards including process safety, use or accidental release of chemicals, excavation, tunnelling and construction work
- Fluvial and coastal flooding associated with climate change

Risk exposure:

An indication of each category’s current exposure relative to the previous year is shown by the coloured disc surrounding the risk number.

- Increased
- Decreased
- Stable

Strategic themes:

- The best service to customers
- At the lowest sustainable cost
- In a responsible manner

Our risk management

Emerging risks and issues

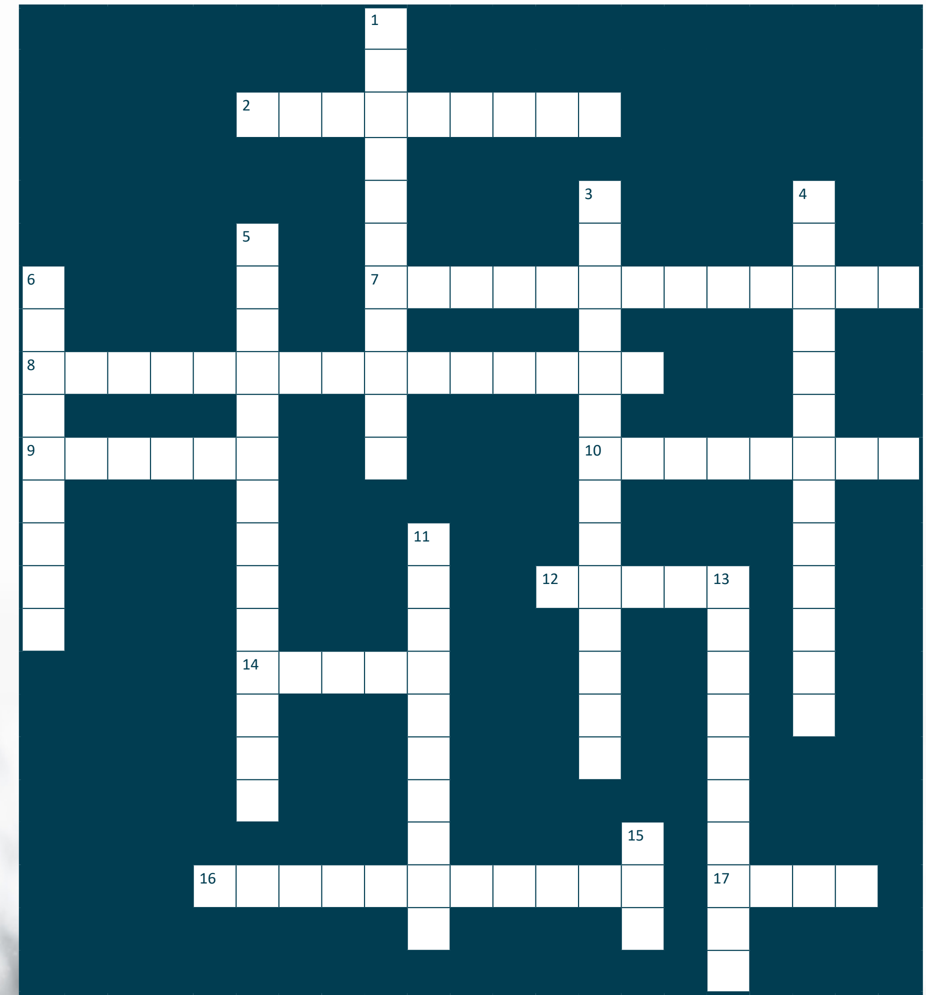
We monitor the internal and external business environment, to identify and review new and emerging risks to our strategy or operations and emerging circumstances of existing risk that could affect our risk exposure in the short to medium term. If new and emerging risks or circumstances are too far into the future or we lack sufficient detail to make a reliable quantification, they are summarised as a watching brief and reported to the corporate responsibility committee and to the board in the six-monthly reporting cycle.

Some new and emerging risks of note are listed below, with emerging circumstances of existing risk included within the list of current key risks, issues and uncertainties in the principal risks table on pages 72 to 75.

Emerging risk/issue	Strategic theme	Description
Climate change		While not new as a risk/issue, climate change is an ever emerging risk in terms of understanding the extent of extreme weather and the return frequency of such events. As an organisation responsible for essential services and infrastructure, we are required under the Climate Change Act 2008 to prepare for a changing climate and understand and consider how we intend to manage material risks to which climate change contributes including: › More frequent and/or higher magnitude drought events in summer; › Higher rainfall in winter; and › More occurrences of heavy rainfall.
Water scarcity		The Environment Agency has warned of water supply shortages in England by 2050. In particular, London's demand is expected to exceed supply in the next decade due to relatively low rainfall, growing population and drier summers. United Utilities has been proactive in the opportunity for the strategic transfer of water from the North West to the South East of England, incorporating an option in the 2019 Water Resources Management Plan (WRMP) for onward transfer in the 2030s. While this is an opportunity, it also brings a number of service, commercial and reputational risks which we will continue to consider, monitor and manage.
Plastics		There is currently considerable attention on single-use plastics and microplastic pollution. The water industry has a role to play in understanding how this material gets into the water environment and this may present potential operational and reputational risks. We will continue to keep a watching brief on the situation and are involved in research projects to better understand any risks to human health or the environment regarding this, and will continue to monitor developments carefully.
Biosolids		Biosolids to agriculture is currently recognised by the government as the best practicable environmental option, but other jurisdictions adopt different approaches to biosolids disposal creating a potential risk that this could extend to the UK in the long term. We do not currently expect any change in this regard but will continue to keep a watching brief on the situation, noting that several research projects are underway to understand these risks and identify solutions.

Time for a tea break

As a bit of fun, we've included a little test with the crossword below. All the answers can be found within this Strategic Report, so please feel free to refer to the pages referenced if you are unsure of any of the answers.



Across

2 Independent customer challenge group whose chair attends our board meetings
Read more on page 39

7 Intensive process where we welcome co-creation of new ideas
Read more on page 37

8 Pioneering operational approach that gives us a competitive advantage
Read more on page 17

9 Company with whom we have been trialling the use of UV LED for water treatment
Read more on page 59

10 Mental health campaign we promoted in the year
Read more on page 33

12 Our economic regulator
Read more on page 16

14 Self-learning artificial intelligence we are rolling out across our water network
Read more on page 35

16 Furry friends helping us detect leaks
Read more on page 23

17 Directive that sets the framework for our security strategy
Read more on page 71

Down

1 One-stop-shop for cross-industry assistance schemes we have set up to help the money advice community
Read more on page 57

3 Campaign we used in Burscough to tackle sewer flooding by changing behaviours
Read more on page 38

4 Top rating we have received three years in a row reflecting our transparent reporting
Read more on page 19

5 Benefit-sharing mechanism we have proposed to help communities in 2020–25
Read more on page 21

6 Rating our 2020–25 business plan received in the initial assessment
Read more on page 19

11 Aeronautical machine we hired three of to help tackle the moorland fires
Read more on page 61

13 Pilot scheme has installed these in 20 locations to help with reservoir safety
Read more on page 47

15 Acronym for the fleet of vehicles we used to cope with demand over the extremely hot, dry summer
Read more on page 30

Governance

The corporate governance report presents information on the board of United Utilities and its activities, and those of the various committees. It also sets out how the board demonstrates leadership, effectiveness and its accountability to the company's stakeholders and its approach to the remuneration of the directors.

Formby beach, after colleagues in our treasury department had spent a day cleaning it — photograph taken by our finance colleague Ian Edwards

Corporate governance report
Board of directors

Dr John McAdam
Chairman

N

Responsibilities: Responsible for the leadership of the board, setting its agenda and ensuring its effectiveness on all aspects of its role.

Qualifications: BSc (Hons) Chemical Physics, Diploma Advanced Studies in Science, PhD.

Appointment to the board: Appointed as a non-executive director in February 2008 and as Chairman in July 2008.

Committee membership: Nomination (chair).

Skills and experience: With over 19 years' service as a board director in a wide range of companies, and as a current non-executive director serving on a number of other boards and across different sectors, John has a wealth of past and current experience on which to draw in his role as Chairman and leader of the board.

Career experience: Joined the board of ICI plc in 1999 and became chief executive in 2003, a position held until ICI's takeover by Akzo Nobel. Previous non-executive roles: senior independent director J Sainsbury plc; non-executive director Rolls-Royce Holdings plc; senior independent director Electra Private Equity PLC; and chairman of Rentokil-Initial plc until 8 May 2019.

Current directorships/business interests: Non-executive and senior independent director of Cobham plc and appointed as non-executive director of Wilmcote Holdings plc on 1 October 2018. He is also Chairman of United Utilities Water Limited.

Independence: John met the 2016 UK Corporate Governance Code's independence criteria on his initial appointment as Chairman.

Specific contribution to the company's long-term success: During his final year as Chairman, John has continued to help drive the considerable progress made by the business throughout the tenure of his leadership.

Steve Mogford
Chief Executive Officer (CEO)

C

Responsibilities: To manage the group's business and to implement the strategy and policies approved by the board.

Qualifications: BSc (Hons) Astrophysics/ Maths/Physics.

Appointment to the board: January 2011.

Committee membership: Corporate responsibility.

Skills and experience: Steve's experience of the highly competitive defence market and complex design, manufacturing and support programmes has driven forwards the board's strategy of improving customer service and operational performance at United Utilities. His perspective of the construction and infrastructure sector provides valuable experience and insight to support United Utilities' capital investment programme.

Career experience: Previously chief executive of SELEX Galileo, the defence electronics company owned by Italian aerospace and defence organisation Finmeccanica, chief operating officer BAE Systems PLC and a member of its PLC board. His early career was spent with British Aerospace PLC.

Current directorships/business interests: Non-executive and senior independent non-executive director G4S PLC. He is also Chief Executive Officer of United Utilities Water Limited.

Specific contribution to the company's long-term success: As chief executive, Steve has driven a step change in the company's operational performance, leading to fast-track status in the PR19 price review process for the 2020–25 asset management period.

Russ Houlden
Chief Financial Officer (CFO)

T

Responsibilities: To manage the group's financial affairs and to contribute to the management of the group's business and to the implementation of the strategy and policies approved by the board.

Qualifications: BSc (Hons) Management Sciences, Fellow of the Chartered Institute of Management Accountants, Chartered Global Management Accountant and a Fellow of the Association of Corporate Treasurers.

Appointment to the board: October 2010.

Committee membership: Treasury.

Skills and experience: Russ's skills and experience in accounting in other commercial and regulated companies, along with his extensive experience of driving performance improvement, provides the group with valuable expertise in pursuing its strategy of improving customer service and in providing our services at the lowest sustainable cost.

Career experience: Previously chief financial officer at Telecom New Zealand and finance director of: Lovells; BT Wholesale; BT Networks and Information Services; ICI Polyurethanes; and ICI Japan.

Current directorships/business interests: Member of the supervisory board and chairman of the audit committee Orange Polska SA. Chairman of the financial reporting committee of the 100 Group. He is also Chief Financial Officer of United Utilities Water Limited.

Specific contribution to the company's long-term success: Russ helps to drive the transformation of the operational performance of the business, delivers the group's competitive advantage in financial risk management and ensures excellence in reporting to shareholders and other stakeholders.

Board role

- Chairman
- Executive Director
- Senior independent non-executive director
- Independent non-executive director

Committees membership

- (N) Nomination committee
- (C) Corporate responsibility committee
- (T) Treasury committee
- (R) Remuneration committee
- (A) Audit committee
- ● Chair of the committee

Steve Fraser

Chief Operating Officer (COO)

Responsibilities: To develop the strategy for, and to manage, the group's operations.

Qualifications: BA (Hons) Management Studies, MSc Engineering Management, AMP Harvard University.

Appointment to the board: August 2017.

Committee membership: None.

Skills and experience: Steve brings a strong commercial acumen and operations focus to the wider business. He has a proven track record in managing networks and using his change management skills and broad experience across all aspects of utilities construction, and programme and operations management.

Career experience: Steve has a wide range of project and contract management experience within the infrastructure sector. Prior to joining United Utilities in 2005, he was operations director of Bethell plc, the power and construction group.

Current directorships/business interests: He is also Chief Operating Officer of United Utilities Water Limited.

Specific contribution to the company's long-term success: Steve is responsible for addressing all operational activities. Through the close scrutiny and monitoring of these activities he ensures that adjusting actions are taken in order that the company's overall operational performance continues to improve.

Mark Clare

Senior independent non-executive director

(N) (R)

Responsibilities: Responsible, in addition to his role as an independent non-executive director, for discussing any concerns with shareholders that cannot be resolved through the normal channels of communication with the Chairman or Chief Executive Officer.

Qualifications: Chartered Management Accountant (FCMA).

Appointment to the board: November 2013.

Committee membership: Nomination and remuneration.

Skills and experience: Through his previous roles at British Gas and BAA, Mark has a strong background operating within regulated environments. His extensive knowledge of customer-facing businesses is particularly valuable for United Utilities in the pursuit of our strategy to improve customer service.

Career experience: Previously chief executive Barratt Developments plc. A former trustee of the Building Research Establishment and the UK Green Building Council. Senior executive roles held in Centrica plc and British Gas. Former non-executive director: BAA plc and Ladbrokes Coral PLC.

Current directorships/business interests: Non-executive chairman Grainger plc and non-executive director Premier Marinas Holdings Limited. He is also an independent non-executive director of United Utilities Water Limited.

Specific contribution to the company's long-term success: As senior independent non-executive director, Mark has led a robust selection process culminating in the appointment of Sir David Higgins as the next Chairman of the company.

Sara Weller

Independent non-executive director

(N) (R)

Responsibilities: To challenge constructively the executive directors and monitor the delivery of the strategy within the risk and control framework set by the board and to lead the board's activities concerning directors' remuneration.

Qualifications: MA Chemistry.

Appointment to the board: March 2012.

Committee membership: Nomination and remuneration (chair).

Skills and experience: Sara's experience of customer-facing businesses, together with her knowledge of operating within a regulated environment, provides the board with valuable perspective as the company improves its service to customers.

Career experience: Previously managing director of Argos; senior executive roles at Mars, Abbey National and J Sainsbury plc. Former non-executive and senior independent director Mitchells and Butlers plc and chair of the remuneration committee. Other non-executive roles: the Department for Communities and Local Government; the Higher Education Funding Council for England; and the Planning Inspectorate.

Current directorships/business interests: Non-executive director Lloyds Banking Group plc; lead non-executive Department of Work and Pensions; and council member at Cambridge University. She is also an independent non-executive director of United Utilities Water Limited.

Specific contribution to the company's long-term success: As chair of the remuneration committee, Sara has played a key role in revising the directors' remuneration policy being presented for approval by shareholders as this year's annual general meeting.

Corporate governance report
Board of directors

Brian May
Independent non-executive director

N A T R

Responsibilities: To challenge constructively the executive directors and monitor the delivery of the strategy within the risk and control framework set by the board and to lead the audit committee.

Qualifications: BSc (Hons) Actuarial Science, Chartered Accountant FCA.

Appointment to the board: September 2012.

Committee membership: Nomination, audit (chair), treasury (chair) and remuneration.

Skills and experience: Brian joined Bunzl plc in 1993 as head of internal audit before becoming group treasurer, then finance director (Europe and Australasia). Brian's background and the various finance roles that he has held are major assets to the board in chairing both the audit and the treasury committees. Brian has been chair of the audit committee for nearly five years and has considerable knowledge of the company and the specifics of the utilities sector.

Career experience: Finance director Bunzl plc, since 2006. Prior to joining Bunzl, Brian qualified as a chartered accountant with KPMG.

Current directorships/business interests: Finance director Bunzl plc, he intends to retire from this role on 31 December 2019. He is also an independent non-executive director of United Utilities Water Limited.

Specific contribution to the company's long-term success: Brian contributes his considerable expertise in finance to the company primarily through the important position of chair of the audit committee. The industry knowledge he has gained during the six years as a board member, and his involvement in the second regulatory price review of his tenure, have provided continuity and knowledge to this vital long-term decision-making process.

Stephen Carter CBE
Independent non-executive director

N A C

Responsibilities: To challenge constructively the executive directors and monitor the delivery of the strategy within the risk and control framework set by the board and to lead the board's agenda on acting responsibly as a business.

Qualifications: Bachelor of Laws (Hons).

Appointment to the board: September 2014.

Committee membership: Nomination, audit and corporate responsibility (chair).

Skills and experience: As the chief executive of a FTSE 100 listed company, Stephen brings current operational experience to the board. His public sector experience provides additional insight in regulation and government relations. His day-to-day experience in the information and technology industries ensures that the board is kept abreast of these areas of the company's operating environment.

Career experience: Previously held senior executive roles at Alcatel Lucent Inc. and a number of public sector/service roles, including serving a term as the founding chief executive of Ofcom. Former chairman Ashridge Business School. A Life Peer since 2008.

Current directorships/business interests: Group chief executive Informa plc and non-executive director Department for Business, Energy and Industrial Strategy. He is also an independent non-executive director of United Utilities Water Limited.

Specific contribution to the company's long-term success: Stephen's experience as a current chief executive and his work in the public sector and government provides valuable insight.

Alison Goligher
Independent non-executive director

N R C

Responsibilities: To challenge constructively the executive directors and monitor the delivery of the strategy within the risk and control framework set by the board.

Qualifications: BSc (Hons) Mathematical Physics, MEng Petroleum Engineering.

Appointment to the board: August 2016.

Committee membership: Nomination, remuneration and corporate responsibility.

Skills and experience: Alison has strong technical and capital project management skills, having been involved in large projects and the production side of Royal Dutch Shell's business. This experience of engineering and industrial sectors provides the board with additional insight into delivering United Utilities' capital investment programme.

Career experience: Royal Dutch Shell (2006 to 2015), her most recent executive role was Executive Vice President Upstream International Unconventionals. Prior to that she spent 17 years with Schlumberger, an international supplier of technology, integrated project management and information solutions to the oil and gas industry.

Current directorships/business interests: Non-executive director Meggitt PLC, part-time executive chair Silixa Ltd and a board member of Edinburgh Business School. She is also an independent non-executive director of United Utilities Water Limited.

Specific contribution to the company's long-term success: Alison's understanding of large capital projects and operational challenges provides valuable insight into the longer-term strategic risks faced by the business. Her role as the designated non-executive director for workforce engagement will provide the board with a first-hand understanding of the views of employees and the culture of the company.

Paulette Rowe

Independent non-executive director

N A

Responsibilities: To challenge constructively the executive directors and monitor the delivery of the strategy within the risk and control framework set by the board.

Qualifications: MEng (Hons) Mechanical Engineering and Management, MBA.

Appointment to the board: July 2017.

Committee membership: Nomination and audit.

Skills and experience: Paulette has spent most of her career in the regulated finance industry and so provides the board with additional perspective and first-hand regulatory experience. Her experience of technology-driven transformation will contribute to United Utilities' customer experience programme and its Systems Thinking approach.

Career experience: Previously held roles include: managing director Barclaycard Payments Solutions; strategy director NBNK Investments plc; commercial and marketing director Tesco Personal Finance; chief executive, European Consumer Finance and managing director Royal Bank of Scotland. Former board member Prince's Youth Business Trust and former trustee and chair of children's charity The Mayor's Fund for London.

Current directorships/business interests: EMEA Executive Facebook Inc. since July 2018. She is also an independent non-executive director of United Utilities Water Limited.

Specific contribution to the company's long-term success: Paulette shares her experience as a senior leader in financial services, and her current role in the technology sector, where technological innovations have driven improved customer service.

Sir David Higgins

Independent non-executive director

N

Responsibilities: To challenge constructively the executive directors and monitor the delivery of the strategy within the risk and control framework set by the board and, in time, assume the role and responsibilities of Chairman.

Qualifications: BEng Civil Engineering, Diploma Securities Institute of Australia, Fellow: the Institute of Civil Engineers and the Royal Academy of Engineering.

Appointment to the board: 13 May 2019.

Committee membership: Nomination.

Skills and experience: Sir David has spent his career overseeing high profile infrastructure projects including: the delivery of the Sydney Olympic Village and Aquatics centre; Bluewater Shopping Centre, Kent; and the delivery of the 2012 London Olympic Infrastructure Project. He joined Network Rail in 2011, overseeing the operation of the rail network during the 2012 Olympic and Paralympic Games and the major redevelopment of stations including Birmingham New Street and London King's Cross.

Career experience: Former chief executive of: Network Rail Limited; The Olympic Delivery Authority; and English Partnerships. Previous non-executive roles: chairman of High Speed Two Limited and Sirius Minerals plc.

Current directorships/business interests: Chairman of Gatwick Airport Limited. Non-executive director of Commonwealth Bank of Australia and chair of the remuneration committee and a member of the risk committee, he will step down in December 2019. He is also an independent non-executive director of United Utilities Water Limited.

Specific contribution to the company's long-term success: Sir David's experience of major infrastructure projects will be invaluable in meeting the challenges of the next regulatory period and beyond. He will take over as Chairman on 1 January 2020.

Board role

- Chairman
- Executive Director
- Senior independent non-executive director
- Independent non-executive director

Committees membership

- N Nomination committee
- C Corporate responsibility committee
- T Treasury committee
- R Remuneration committee
- A Audit committee
- Chair of the committee

Corporate governance report
Letter from the Chairman

As the board of directors, we recognise our responsibilities to our different but mainly interrelated stakeholder groups and our wider societal responsibilities.

Quick facts

- Dr John McAdam met the independence criteria as set out in the 2016 UK Corporate Governance Code (the Code) when he was appointed as Chairman.
- The Code requires that at least half of the board is made up of independent non-executive directors (the test excludes the Chairman). At United Utilities, seven out of the remaining ten directors are independent non-executive directors.
- The company secretary attends all board and committee meetings and advises the Chairman on governance matters. The company secretariat team provides administrative support.
- The directors' biographies (see pages 80 to 83) include specific reasons why each director's contribution is, and continues to be, important to the company's long-term sustainable success.
- All directors are subject to annual election at the annual general meeting (AGM) held in July. Following the completion of the annual evaluation process all the non-executive directors were considered by the board to be independent and making a valuable and effective contribution to the board (see page 91). As a result, the board recommends that shareholders vote in favour of those standing for a further term at the forthcoming AGM, as they will be doing in respect of their individual shareholdings.

Quick links

The details of the matters that the board has reserved for its own decision are set out in the 'Schedule of matters reserved for the board'.

A copy can be found at unitedutilities.com/corporate-governance

A copy of the Financial Reporting Council's 2016 UK Corporate Governance Code can be found at **frc.org.uk**

Dear Shareholder

Our year

We have reported strong financial performance and sustained our improvement in operational performance contributing towards achieving our strategic targets during 2018/19. Our 2020–25 draft business plan for UUW was awarded fast-track status in Ofwat's initial assessment. Our plan reflects our strategy of providing the best service to customers, at the lowest sustainable cost and in a responsible manner, and in accordance with our core values. Ofwat commended our plan in a number of areas, including customer engagement, affordability and vulnerability, resilience and innovation. We believe our plan demonstrates the regard the board has for our various stakeholder groups in its decision-making. Our plan is designed to promote the group's long-term success and customers' interests as well as creating value for shareholders.

During the year, we have also had our challenges. In particular, the prolonged hot and dry weather last summer, resulting in exceptional demand from customers, impacted many areas of our operations.

Our approach

Our role as the board is to set the strategy of the group and ensure that management operates the business in accordance with this strategy. Details of the strategy and purpose are set out in the strategic report (see page 15). We believe this approach will promote the group's long-term success, our customers' interest, create value for shareholders and take account of our other stakeholders. The board's intention is to hand over the business to our successors in a better and more sustainable position for the future. Within our region, our activities often have multiple touch points on individuals' lives. United Utilities is a monopoly supplier of water and wastewater services to domestic households. Many customers are also our shareholders, either directly or indirectly holding shares through pension scheme investments. Indeed, many of our employees are also customers, shareholders and future pensioners and have an interest in the group's long-term success. As individual directors we are mindful of our statutory duty to act in the way each of us considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, as set out in s172 of the Companies Act 2006 (the Act). There are times when difficult decisions must be taken requiring each of us to exercise independent judgement and apply reasonable care, skill and diligence in the decision-making process. As the board of directors, we recognise our responsibilities to our different but mainly interrelated stakeholder groups and our wider societal responsibilities. For the first time this year, we have included, as required by s414CZA of the Act, a s172(1) Statement (see page 152).

Our governance structure

We held eight scheduled board meetings during the year; in addition, there were a number of other board meetings held which directors attended either in person or via telephone conferencing facilities.
A diagram showing the interrelationships of the various board committees can be found on page 87 and reports from each of the committee chairs about their work can be found on the following pages. The diagram also describes some of the group's principal management committees.

Our people

At 31 March 2019, we had maintained our gender target that at least 25 per cent of the board comprised of women with three out of ten directors on the board being women. The board aspires to achieve 33 per cent by 2020. Our current gender balance places us 33rd in the FTSE 100 in the '2018 Hampton Alexander Women on Boards Leadership Index'. With regards to diversity more generally, I am satisfied that we have an appropriately diverse board in terms of experience, skills and personal attributes and in terms of age and ethnicity among our board members. During the year, we have updated our board diversity policy, and included an ethnicity objective (see page 97).

As directors, both individually and collectively, we have many years of experience gained across a variety of industries and regulated businesses, and so are familiar with the particular challenges of a regulated operating environment. Although there are time constraints for non-executive directors who also have an executive role, these individuals bring valuable current market experience and thinking to the board table. Similarly, we encourage our executive directors to serve as non-executive directors elsewhere to help broaden their experience, although this is normally limited to one other directorship in a company in an industry which does not conflict with United Utilities' business.

Twenty-nine per cent of our executive team is made up of women. We are keen to develop our succession pipeline of female senior managers so that, over time, they can be considered for executive board appointments or as potential candidates for non-executive directorships in other companies. Our current talent programme at a senior level is well embedded and we believe a non-executive appointment for senior managers provides an excellent opportunity for both personal and career development. It is a way of gaining valuable experience that may be applied at United Utilities so long as no conflicts of interest occur. Our graduate and apprentice programmes are thriving and we are focusing more effectively on middle/junior management succession. Our gender pay data can be found on page 98. Historically, our industry has been male dominated, but we have measures in place to increase diversity in broad terms, including gender among our employees.

The board considered the requirement in the 2016 UK Corporate Governance Code (the Code) that the "audit committee as a whole shall have competence relevant to the sector in which the company operates". It concluded that, when taking into account the skills, knowledge, experience and professional qualifications of committee members (see the directors' biographies on pages 80 to 83), the Code requirement was fulfilled. Furthermore, all members of the audit committee are independent non-executive directors.

Our values and culture

Our aim is to behave as a responsible business, and our business principles can be found on our website (see page 93). Our core values of acting with integrity and focusing on our customers provide both the framework for our business culture and the way in which our employees go about their daily work. Behaving responsibly has been part of the United Utilities ethos for many years.

The company has complied fully with the main and subsidiary principles and provisions of the 2016 Code (the details of which are contained within this corporate governance report), with which we are required to report by the Financial Conduct Authority's Listing Rules for the year ended 31 March 2019. The board is working towards addressing the details of the 2018 Code, against which it will report next year.

Our approach to risk

Our approach toward risk is very much aligned with our culture. We are an organisation that provides a vital service to its customers and we recognise the responsibilities of this, and our intention is to act responsibly towards our stakeholders, in particular our customers, in the provision of our services to them. As a board, we must take long-term decisions to ensure our successors are able to operate the business efficiently for customers, and we need to build our assets to meet future demand and circumstances. We are a commercial organisation operating within a regulated framework and accepting some level of risk is a normal consequence of doing business. It is the board's and the executive team's role to understand the risks associated with each activity of the business and ensure that actions are taken to mitigate these risks.

Our investors

We are in regular contact with our large investors through a regular scheduled programme of meetings attended by either our CEO or CFO or both of them. The programme is also supported by the activities of our investor relations team who are readily available to address investors' queries. Feedback is regularly shared with board colleagues.

Ensuring that the directors' remuneration packages align the directors' and senior managers' interests with the long-term interests of the company and its shareholders is always a key area of interest for investors. The directors' remuneration policy was most recently put to the shareholder vote at the AGM in 2017, when over 98 per cent of the vote was cast in favour of the policy. At this year's AGM we are renewing our directors' remuneration policy, a year earlier than expected in order to align performance targets with the new five-year asset management period starting on 1 April 2020. Further information and the proposed new policy can be found on pages 124 to 130.

Looking forward

Having served on the board for over 11 years, and as the company is preparing for the start of its new regulatory period in April 2020, I felt now was a good time for me to hand over the reins, and I will leave the board on 31 December 2019. The company announced on 13 May 2019 the appointment of Sir David Higgins as a non-executive director and Chairman designate. I am grateful to Mark Clare, senior independent non-executive director, who led a thorough search process on behalf of the nomination committee, identifying Sir David as my successor. Sir David is an excellent appointment, his approach and experience will fit well with the culture at United Utilities. I have very much enjoyed my time as a member of the board and am confident that the company is well placed as it goes into the 2020–25 asset management period.

As always, any feedback you may have on this annual report is welcome – please email any comments you may have to: secretariat@uuplc.co.uk

Dr John McAdam
Chairman

Corporate governance report

Governance

Code principles

Leadership

Read more about Leadership on page 86

Effectiveness

Read more about Effectiveness on page 90

Relations with shareholders

Read more about Relations with shareholders on page 99

Accountability

Read more about Accountability on page 100

Remuneration

Read more about Remuneration on page 116

Code principle – Leadership

Introduction by Dr John McAdam

"The penultimate year in an asset management period is always a crucial one. The extent of the challenge and the complexities of the decisions taken in the construction of the business plan for the next asset management period should not be underestimated. We believe that in the plan we submitted to Ofwat on 3 September 2018, we have fulfilled our individual statutory duties, to act in the way that would be most likely to promote the long-term success of the company."

Overview of the board's responsibilities

- Sets the strategy of the group, ensuring the long-term success of the group for customers, investors and wider stakeholders and in creating shareholder value;
- Is responsible for challenging and encouraging the executive team in its interpretation and implementation of how it manages the business, and that it is doing so in accordance with the strategic goals the board has set;
- Has responsibility for ensuring the company's internal control systems (including financial, operational and compliance) and processes are sound and fit for purpose. See the 'accountability' section of this report on pages 100 to 111 for more detail;
- Must ensure that the company has the necessary financial resources and people with the necessary skills to achieve its objectives. It also reviews managerial performance annually; and
- Has oversight of major capital expenditure projects within UUW which exceed £150 million, and any project which materially increases the group's risk profile or is not in the ordinary course of the group's business.

Full details of the matters that the board has reserved for its own decision-making, due to their importance to the business or the working of the board, can be found on our website at unitedutilities.com/corporate-governance

Governance structure for our board and our committees

In line with the Code, the board delegates certain roles and responsibilities to its principal board committees, as shown in the diagram opposite. While the board retains overall responsibility, a sub-committee structure allows these committees to probe the subject matters more deeply and gain a greater understanding of the detail. The committees then report back to the board on the matters discussed, decisions taken, and where appropriate, make recommendations to the board on matters requiring its approval. The reports of the principal board committees required by the Code can be found on the subsequent pages. Minutes of the board and principal board committee meetings (with the exception of the remuneration committee) are tabled at board meetings and the chairs of each of the board committees report verbally to the board on their activities. The Chairman chairs the nomination committee; all other principal board committees are chaired by independent non-executive directors who have particular skills or interests in the activities of those committees.

The executive team is chaired by the CEO, and its members are the senior managers who have a direct reporting line to the CEO. Our executive team meets monthly; it is responsible for the day-to-day running of the business and other operational matters and implementing the strategies that the board has set. Short biographies of the executive team can be found on our website at unitedutilities.com/executive-team

The diagram shown opposite also shows the principal management committees and a brief description of their roles. These committees enable senior management to understand and, if necessary, challenge the business in its interpretation of the implementation of the strategies the board has set. The board received reports from the CEO and CFO at every scheduled board meeting, providing the board with an updated overview of the business and its financial performance and position. Operational updates are also provided to board meetings by the COO.

Governance structure of the board and its principal committees and the principal management committees

Group board
Chair: Dr John McAdam

Chief Executive Officer
Steve Mogford

Principal board committees

Audit committee
Chair: Brian May

Read more on pages 103 to 111

Remuneration committee
Chair: Sara Weller

Read more on pages 116 to 143

Nomination committee
Chair: Dr John McAdam

Read more on pages 94 to 98

Corporate responsibility committee
Chair: Stephen Carter

Read more on pages 112 to 115

Treasury committee
Chair: Brian May

The committee considers and approves borrowing, leasing, bonding and other banking facilities within limits set by the board. The CFO and treasurer are also members. Some powers are sub-delegated, within certain limits, to the CFO and treasurer.

Principal management committees

Executive team
Chair: Steve Mogford, CEO

This forum is responsible for implementing the board's strategy and the day-to-day operation of running the business and the CEO will cascade decisions made by the board to the business via this forum.

Group audit and risk board
Chair: Steve Mogford, CEO

Read more on page 68

Quarterly business review
Chair: Steve Mogford, CEO

This forum is responsible for the quarterly review of operational and financial performance.

Political and regulatory steering group
Chair: Gaynor Kenyon, corporate affairs director

This forum is responsible for discussing political and regulatory issues affecting the company, where any 'horizon scanning' issues are raised and business responses to consultations are agreed.

Capital investment committee
Chair: Steve Mogford, CEO

The committee is responsible for authorising expenditure relating to the capital investment programme.

Key:
- The best service to customers
- At the lowest sustainable cost
- In a responsible manner

Corporate governance report

Summary of board activity in 2018/19

	Cross reference	Link to strategic themes
Leadership and employees		
› Review of health, safety and well-being activities and consideration of health and safety incidents of employees and contractors reinforcing the company's belief that 'nothing we do is worth getting hurt for' and an update on the progress of developing and implementing an improved health and safety culture within the business branded as 'home safe and well';	See page 33	
› Considered board succession planning and the appointment of Sir David Higgins as an independent non-executive director and Chairman designate;	See page 96	
› Monitored progress on key aspects of the employee succession and development plans, identifying leadership potential at all levels, developing our employer brand and our aspiration for a multi-generational and diverse workforce;	See page 98	
› Reviewed and discussed: executive team succession plans and the needs of the business; the ongoing progress in the development of our talent pipeline of senior talent to address business challenges identified in the 2020–25 asset management period and beyond; and other emerging employee issues;	See page 95	
› Discussed the results of the annual employee voice and engagement survey. Reviewed and endorsed the introduction of new workforce engagement mechanisms to ensure an accurate representation of employees' views are provided to the board. Alison Goligher was identified as the non-executive director designated for engagement with the workforce;	See page 115	
› Reviewed and amended the board diversity policy; and	See page 97	
› Approved the changes to the all-employee share incentive plan to comply with the General Data Protection Regulation.	–	
Strategy		
› Reviewed the group's corporate responsibility activities focusing on reputation management, particularly in our communications with stakeholders;	See page 112	
› Received regular updates at each meeting of items with a strategic component, such as emerging changes to regulation, major capital expenditure and business structuring decisions;	–	
› Discussed the context of the next price review the key issues to be addressed and considered the expectations of our key stakeholders;	See page 6	
› Discussed the group's preparations in relation to Brexit; and	See page 72	
› Discussed the impact of any renationalisation of the water sector.	See page 69	
Governance		
› Reviewed and debated the risk profile of the group, and in particular the principal risks and our risk appetite, including a review of the most significant operational risks;	See page 68	
› Reviewed the effectiveness of the risk management systems, including financial, operational and compliance controls and reviewed the effectiveness of the internal control systems;	See page 109	
› Reviewed and discussed developments in cyber crime and the activities undertaken to enhance the effectiveness of the group's security controls;	See page 71	
› Reviewed the terms of reference for the audit, remuneration, treasury and corporate responsibility committees and received post-meeting reports from the chairs of each committee summarising discussions and actions;	–	
› Reviewed biannual updates on changes and developments in corporate governance and the implementation of any changes required particularly relating to the 2018 Code;	See page 92	
› Reviewed and discussed the external evaluation of the board, its committees and individual directors and conflicts of interest;	See page 90	
› Reviewed the performance of the external auditor and recommendation for reappointment;	See page 106	
› Reviewed and approved the new directors' remuneration policy to be presented to shareholders for approval at the 2019 AGM; and	See page 118	
› Reviewed the approach and progress of work to identify areas where there is any risk of modern slavery occurring in our supply chain and approval of the 2019/20 slavery and human trafficking statement.	See page 150	

Summary of board activity in 2018/19

	Cross reference	Link to strategic themes
United Utilities Water Limited (UUW) regulated business and its stakeholders		
› Regular review and monitoring of the progress with the business plan submission for the 2020–25 regulatory period as submitted to Ofwat on 3 September 2018, and the ongoing preparations towards final determination in December 2019;	See page 19	
› Monitored the ongoing progress of the customer experience programme and resulting improvements to customer service. During the year, new initiatives for customers in vulnerable circumstances were incorporated into our accessible affordability schemes, contributing to our improved performance scores against Ofwat's qualitative Service Incentive Mechanism (SIM); and	See page 57	
› Regular updates in relation to the 2018 extreme weather events and group's operational response and performance.	See page 30	
Other group business		
› Reviewed progress on the group's renewable energy generation capabilities and opportunities for expansion and innovation including the construction of a 7.2MW ground mounted solar panel array at Huntington water treatment works and a 4.5MW array at Preston Clifton Marsh wastewater treatment works; and	See page 23	
› Regular reviewed of progress of Water Plus, the group's joint venture with Severn Trent serving commercial customers, and approved the renewal of working capital arrangements.	See page 109	
Shareholder relations		
› Received and discussed a presentation by Rothschild Investor Advisory on investors' views and perceptions of the group in relation to, among other things: strategy; the group's unique selling proposition; dividend policy; and how the company compares with other listed water and wastewater companies; and	See page 99	
› Regularly received and discussed feedback from road shows, presentations and face-to-face meetings between investors and the CEO and/or the CFO and other communications received from large investors.	See page 99	
Financial		
› Reviewed the 2020–25 business plan and approved the 2019/20 budget;	–	
› Reviewed and approved the half and full-year results and associated announcements;	–	
› Reviewed and approved the going concern and long-term viability statement;	See page 101	
› Reviewed and approved the company's 2018/19 UK tax strategy;	See page 144	
› Reviewed and approved: the annual pensions update and the guaranteed minimum payment pension charge to address the equalisation of benefits between men and women reflecting the outcome of a recent legal case;	See page 108	
› Reviewed and approved the company's treasury policies; the group's funding requirements for the year and the potential sources to meeting these funding requirements; and managing the group's interest rate and other market risk exposures including the impact of Brexit;	See page 100	
› Approved annual insurance arrangements for 2019/20;	–	
› Reviewed progress with material litigation involving the group; and	See page 70	
› Reviewed, discussed and approved proposals in principle relating to actuarial valuations of the United Utilities Pension Scheme and the United Utilities PLC group of the Electricity Supply Pension Scheme.	See page 5	

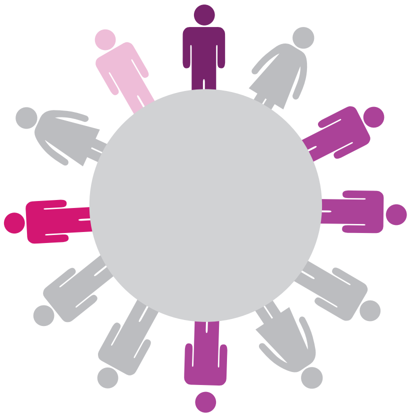
Key:

The best service to customers · At the lowest sustainable cost · In a responsible manner

Governance

Corporate governance report

The board table



- Chairman
- Executive director
- Senior independent non-executive director
- Independent non-executive director
- Company secretary

Attendance at board and committee meetings

Eight scheduled board meetings were planned and held during the year (2018: eight). A number of other board meetings and telephone conferences were also held during the year, as the need arose. The table below shows the actual number of scheduled meetings attended and the maximum number of scheduled meetings which the directors could have attended. Only in exceptional circumstances would directors not attend board and committee meetings. Similarly, every effort is made to attend ad hoc meetings either in person or via the use of video or telephone conferencing facilities if needs be. None of our non-executive directors have raised concerns over the time commitment required of them to fulfil their duties.

On the evening before most scheduled board meetings all the non-executive directors meet either by themselves, or together with just the CEO, or with the entire board and the company secretary, and this time is usefully spent enabling board colleagues to share views and consider issues impacting the company. Time together also helps to build relationships on a personal level, which contributes to better relationships and decision-making around the board table.

	Board meetings	Audit committee	Remuneration committee	Nomination committee	Corporate responsibility committee	Treasury committee
Dr John McAdam	8/8	–	–	2/2	–	–
Steve Mogford	8/8	–	–	–	4/4	–
Russ Houlden	8/8	–	–	–	–	3/3
Steve Fraser	8/8	–	–	–	–	–
Mark Clare	8/8	–	6/6	2/2	–	–
Sara Weller	7[(1)]/8	–	6/6	1[(1)]/2	–	–
Brian May	8/8	4/4	6/6	2/2	–	3/3
Stephen Carter	7[(2)]/8	4/4	–	2/2	4/4	–
Alison Goligher	8/8	4/4	5[(3)]/6	2/2	4/4	–
Paulette Rowe	8/8	4/4	–	1[(4)]/2	–	–

Actual number of meetings attended/maximum number of scheduled meetings which the directors could have attended during the financial year ended 31 March 2019.

(1) Sara Weller was unable to attend a meeting of the board and a meeting of the nomination committee due to unforeseen circumstances.
(2) Stephen Carter was unable to attend a meeting of the board due to a conflicting commitment.
(3) Alison Goligher was unable to attend a meeting of the remuneration committee due to a conflicting commitment.
(4) Paulette Rowe was unable to attend a meeting of the nomination committee due to a conflicting commitment.

Code principle – Effectiveness

Introduction by Dr John McAdam

"Board colleagues have approached the evaluation process with resolve this year, ahead of the challenges and changes posed by a new five-year asset management period."

Evaluation of the board and board committees

Our board evaluation was conducted internally this year; our last external evaluation was conducted by Lintstock consultants in 2018.

The evaluation process was facilitated by the company secretary and his team. It was based on the completion of questionnaires (including questions to be scored and free text questions) by board members assessing both the performance of the board and each of its principal committees, as well as that of the Chairman and each of the individual non-executive directors.

Board members were also asked to provide a view on how well the actions identified in the 2017/18 evaluation had been addressed.

In addition to board members, other members of the executive team who regularly attend and support the various committee meetings were also asked to complete the questionnaires.

The results, once reviewed by the company secretary, were then discussed with the Chairman and the chair of the relevant committee, tabled at a meeting of the relevant committee, and then presented to the board. The Chairman reviewed the performance of the individual directors. Mark Clare, as the senior independent non-executive director, in discussion with the other non-executive directors, led the review of the Chairman's performance.

A summary of the internal analysis of the 2018/19 evaluation is as follows:

2018/19 areas of assessment	Commentary and actions
Board composition and expertise	The composition of the board was considered to be a diverse group of high-quality non-executive and executive directors, with a variety of skills, expertise and knowledge.
Board agenda	The board was well informed about the regulatory environment within which the company operates and had a good understanding of the views of customers, regulators and investors. The agendas were well balanced, and site visits were welcomed and added significant value.
Board dynamics	The relationship between the board members was appropriate. Board meetings were conducted in an atmosphere with open communication, meaningful participation and the proper resolution of issues.
Board support	The timeliness of the distribution of board documentation was satisfactory, but could be improved. Executive summaries of board papers were used effectively although board packs were sometimes considered to be too lengthy.
Wider strategic oversight	The involvement of the board in the development of the strategic direction of the group was considered to be appropriate and they were fully involved in the requirements of the price review process.
Risk management and internal control	The board's approach to the management of risk and to its systems of internal control were considered to be appropriate. The information received relating to risk management was rated highly with good visibility of operational and reputational risks, and board members welcomed the opportunity for discussion on risk.
Succession planning and human resource management	Succession plans for the board were in place with outline timescales, with the Chairman's succession being addressed. Succession for senior executive positions was considered to be satisfactory.
Committees	The composition and performance of the audit, remuneration, nomination, corporate responsibility and treasury committees were considered to be appropriate. The feedback to the board by committee chairs was full and transparent and meetings chaired effectively. Specific comments/actions were identified as follows: › Nomination committee: more regular meetings would be required over the next year within agreed timescales; › Remuneration committee: overall, colleagues felt the committee was very effective; › Audit committee: the balance between detail and simplification in audit papers should continue to be reviewed; and › Corporate responsibility committee: the implications of the outcome for the business plan submission for the committee's agenda should be kept under review.
Individual directors	The individual performance of all the directors was assessed: all the non-executive directors were considered to be independent and effective, and all directors demonstrated the expected level of commitment to their roles. The review of the Chairman's performance (led by the senior independent director) concluded that Dr McAdam continued to demonstrate an effective and unbiased perspective, notwithstanding that he would have served for over ten years as a board director by 31 March 2019. It was agreed that Dr McAdam fulfilled the expected commitment to the role and was an effective leader of the board. All directors would be offering themselves for reappointment/election at the 2019 AGM.

Corporate governance report

2017/18 evaluation recommendations	Actions taken during 2018/19
The board would benefit from more opportunities to gain better understanding of the views of employees across the group.	During the year, the board agreed its preferred approach for strengthening the employee voice in the boardroom with Alison Goligher appointed as the designated non-executive director.
Allow more time for discussion of key strategic topics at the board strategy awayday and involving experts to further the debate.	A strategy awayday was not held during the year, due to the demands of the price review process.
Nomination committee: maintain the focus on senior board succession over the next 12 months and ensure it was managed proactively.	The nomination committee has reviewed board succession in accordance with the succession plan, and undertaken the recruitment of the Chairman's successor.
Remuneration committee: consider the way in which incentives should address the transition to the next asset management period.	During the year, the remuneration committee decided to accelerate its review of the directors' remuneration policy. A comprehensive shareholder consultation process was undertaken covering a wide range of elements, including incentive arrangements and performance measures for directors, a new directors' remuneration policy will be presented to shareholders for approval at the 2019 AGM.
Audit committee: ensure the committee was kept abreast of reporting changes.	The audit committee received updates on the implications for the company on the adoption of IRFS 9, IFRS 15 and IRFS 16.
Corporate responsibility committee: ensure the committee contributed to the PR19 business plan submission process, particularly in terms of customer priorities.	The corporate responsibility committee reviewed the draft business plan from for the 2020–25 asset management period from a responsible business perspective prior to submission to Ofwat. The committee endorsed management's approach particularly the emphasis towards affordability and vulnerability and the impact that this would have on the communities served.

Board development

Board directors regularly receive updates to improve their understanding and knowledge about the business and in particular its regulatory environment. As part of the individual directors' element of the board evaluation exercise (see page 91), directors are asked to identify any skills or knowledge gaps they would like to address.

Consideration of environmental and social issues are fundamental to the way in which we operate as a responsible business at United Utilities; such matters are central to board discussions (see the summary of board activity on pages 88 to 89). The board's approach to these matters is reflected in our strategic theme, and our corporate culture, of behaving in a responsible manner as reflected throughout the strategic report. Through presentations and discussions with representatives of YourVoice, the independent customer challenge group, the board has been kept fully aware of in-region environmental and social matters.

In addition to this less formal approach to board development, during the year the board also received briefings from both Slaughter and May (legal and governance matters) and KPMG (governance changes relating to reporting requirements) along with a number of other advisers.

Our non-executive directors are conscious of the need to keep themselves properly briefed and informed about current issues and to deepen their understanding of the business. During the year, Sara Weller and Alison Goligher visited the group's offices in Warrington to attend different meetings with representatives of YourVoice, the independent customer challenge group. As part of the ongoing work to ensure the board has direct link to understand the views of employees (see page 115) Alison spent time meeting employees in different areas of the business to gain an understanding of everyday life and the culture of the business.

Induction programmes are designed and arranged for any new director.

Values and culture

The best service for customers | At the lowest sustainable cost | In a responsible manner

Core value: Customer focus

Customers are at the heart of everything we do, and we aim to provide a great and resilient service at the most efficient cost.

Core value: Innovation

We continually look for new ways to make our services better, safer, faster and cheaper.

Core value: Integrity

We make promises knowingly and keep them, behaving responsibly towards all of our stakeholders.

Values and culture

Our values underpin our strategic themes as shown in the diagram on the opposite page. The United Utilities way of doing things is to behave as a responsible business, and is set out in our business principles document. A copy can be found at: **unitedutilities.com/corporate/about-us/governance/business-principles/**

The board leads by example; behaving responsibly is at the root of the board's decision making processes and it operates in an environment conducive to open and frank discussions. Culture, as defined by the FRC (see below), is cultivated and cascaded throughout the business by the CEO and his executive team. Our employees play a vital role in bringing our values to life, particularly in relation to fulfilling the company's purpose of providing great service to customers in the North West, creating long-term value for all of our stakeholders. Our culture, of behaving responsibly, is treated as business as usual.

Board decisions and culture are interlinked. The culture of the business is impacted by the decisions taken by the board, and the board takes decisions in light of its understanding of the culture of the business.

During the year, the board has a number of opportunities to consider cultural indicators and metrics particularly in relation to reporting on: employees, customer matters and risk. While such reporting provides the board with a good opportunity to monitor the cultural health of the business, management is working to improve the presentation of the information to better facilitate the board's monitoring and assessment of culture.

The management team continues to drive the focus on customers and ensure this value is deeply embedded in our culture and the way we operate. Through the ongoing work of Alison Goligher, the designated non-executive director for engagement with the workforce, the board will benefit from Alison's first hand assessment of the culture of the business.

A stakeholder metrics table (see page 55) provides data on a number of stakeholder and cultural indicators.

Examples of how we aim to behave responsibly towards our different stakeholders are shown in the table below. Further information on our stakeholder engagement can be found on pages 39 to 47.

How we behave responsibly towards our customers	How we behave responsibly towards our employees	How we behave responsibly towards our other stakeholders (shareholders, environment, communities, and regulators)
Customers are at the heart of everything we do, and we aim to provide great and resilient service at the most efficient cost. Our offering to customers includes: › 'Priority Services' that customers can register for if they require extra support due to such things as age, ill health, disability, mental health problems, financial worries or language barriers; › 'Moving Home' services are designed to provide an easy way for customers in our region to get in touch with us when they move house; › improved communications with customers – including making our bills easier to understand and removing technical jargon; › a user-friendly customer website and mobile app enabling customers to easily access their account at any time; and › through the regular contact with representatives of YourVoice the independent customer challenge group, the board receives a direct channel of communication and customers' views to inform its decision making.	At the heart of our operations is our ethos of 'nothing we do is worth getting hurt for'. We believe the safety of our employees and contractors is paramount. Our offering to employees includes: › a competitive base salary; › employee benefits; › family friendly employment policies that go beyond the statutory minimum; › the opportunity to express their views about the company in the annual employee voice survey; › an internal network of mental health awareness supporters; › employees are encouraged to improve their well-being through exercise. Corporate or reduced rate gym membership has been arranged with providers across the company's region; and › the company funds an employee assistance support programme providing a confidential counselling and information service 24/7 to assist employees with personal or work-related problems that may be affecting their health, well-being or performance.	Our engagement with our wider stakeholders is business as usual through a number of specialist functions/teams such as: › our investor relations team provides a point of contact for equity investor queries; › the sustainability team champions sustainability issues with the business; › our stakeholder teams provide support for communities where we are undertaking major capital projects; › our communications teams raise awareness and respond to press and media queries; › our corporate affairs team provides information to public organisations; › teams within our business are in constant communication with our various regulators in relation to customer, economic and environmental factors; and › our treasury team provides a point of contact for credit investor queries.

The culture of a company is defined by the FRC as 'a combination of the values, attitudes and behaviours manifested by a company in its operations and relations with its stakeholders. These stakeholders include shareholders, employees, customers, suppliers and the wider community and environment which are affected by a company's conduct.' FRC's 'Corporate Culture and the Role of Boards' July 2016.

Corporate governance report
Nomination committee

Further embedding our Systems Thinking approach and increased digitalisation continues to underpin our succession pipeline for board and senior management

Pictured: (back row, left to right) Alison Goligher, Stephen Carter, Brian May, Sara Weller; (front row, left to right) Paulette Rowe, Dr John McAdam, Mark Clare

Quick facts

- All members of the committee are independent, thus fulfilling the Code requirement that a "majority of members of the nomination committee should be independent non-executive directors".
- The role of the committee is to make recommendations to the board on its composition, balance and membership and on refreshing the membership of the board committees.
- The company secretary attends all meetings of the committee;
- The customer services and people director, has responsibility for human resources, and regularly attends meetings and is responsible for engaging with executive search recruitment advisers.
- The CEO is not a member of the committee, but from time to time is invited to attend. Neither the Chairman nor the CEO would participate in the recruitment of their own successor.

Quick links

Terms of reference – unitedutilities.com/corporate-governance

Nomination committee members

Dr John McAdam (chair)	Sir David Higgins
Stephen Carter	Brian May
Mark Clare	Paulette Rowe
Alison Goligher	Sara Weller

Dear Shareholder

This year the focus for the nomination committee has been on the search for my successor, and so this will be my last report on behalf of the nomination committee. This process was led by Mark Clare in his role as senior independent director, and was in accordance with our previously agreed board succession plans. Further information can be found on page 96.

Our succession plan aims to ensure that the board and senior management have the appropriate balance of skills and experience to support the group's strategic objectives. Our senior management succession plans take into account the views of all board members to ensure our plans encompass the benefit of all their skills and experience. During the year the board has reviewed the people and organisational capability plan ensuring that our internal talent is identified and developed to support the delivery of our next five-year asset management period. Further embedding our Systems Thinking approach and increased digitalisation continues to underpin our succession pipeline for board and senior management. In our succession planning we aim to ensure both our board directors and members of the executive team and other senior managers, who are potential successors to the board and/or the executive team or board, are well equipped with the right skills and experience to address the challenges of our business and, where necessary, address any developmental needs. They also need to be in tune with the culture of the company.

In support of these board discussions, the nomination committee has responsibility for considering the detailed recruitment process for executive and non-executive board appointments and members of the executive team. All the non-executive directors are members of the nomination committee and participate in meetings and in the recruitment process for new board colleagues. During a board recruitment process, the nomination committee would be supported by Louise Beardmore, customer services and people director, as part of her human resources responsibilities. During the year, the committee formally met twice. The meetings discussed and reviewed our board and executive level succession plans. Our plans address both contingency planning needs and requirements in the short to medium term, and incorporate a reasonable degree of certainty on timescales for key board positions.

Historically, independent non-executive directors at United Utilities have served a term of between seven and nine years, a pattern which has facilitated the refreshing of the board in recent years almost on an annual basis, along with ensuring a high degree of continuity. Notwithstanding this, the specifics of each of the non-executive directors' time of departure has been driven by their own personal circumstances. Serving beyond a nine-year term is identified in the Code as being one of the reasons which could affect a non-executive director's independence, although the 2016 Code, under which we are reporting, excludes a board chairman from this nine-year rule. The 2018 Code specifies that board chairmen are now subject to the nine-year rule.

Our updated board diversity policy (see page 97) is taken into account during every candidate selection process. Ultimately, we do strive to appoint the person we believe is best matched to the role in terms of what they have to offer the company and to make a positive contribution to the board conversation and board dynamics. Diversity of outlook and interest is essential to ensuring we have a variety of views to contribute to discussions and the decision-making process.

Dr John McAdam
Chair of the nomination committee

Main responsibilities of the committee

- Lead the process for board appointments and make recommendations to the board about filling vacancies on the board, including the company secretary;
- Consider the succession planning of directors and members of the executive team;
- Make recommendations to the board on refreshing the membership of the board's principal committees;
- Review directors' conflict authorisations;
- Consider the request from executive directors for election to the boards of other companies and make a recommendation to the board; and
- Consider requests from non-executive directors for the election to the boards of other companies; this role has been delegated to the Chairman (other than in respect of his own position).

What has been on the committee's agenda during the year?

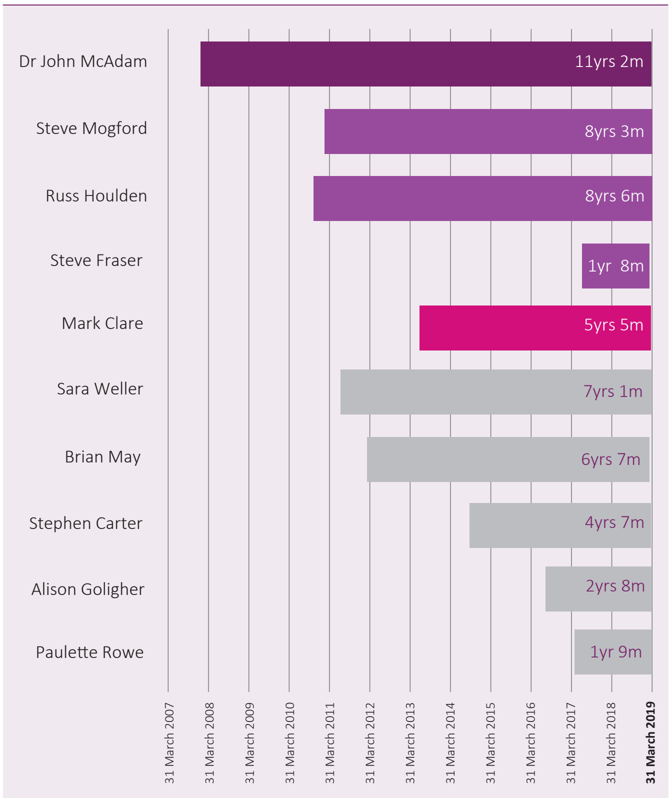
Board succession

The committee has further developed the board succession plans during the year, taking into account more granularity around timescales for key board positions, the likely evolution of the business and the changing shape and increasingly competitive nature of the industry expected from 2020 onwards. A succession planning matrix tool (incorporating the skills matrix, see page 96) for board directors is used to support the planning process for board appointments. The succession planning matrix highlights the Code governance requirements; existing directors' terms of appointment and a forecast/anticipated time frame when an individual might leave the business; the projected strategic needs of the business and resulting preferred experience of any potential new board member; existing potential internal successors to a role (where identified) and those who could act as an interim should the need arise. A candidate suitable for the role of CEO would need to demonstrate that their management approach would fit with the company's culture of behaving responsibly. The committee would seek to consult with the incumbent CEO, given his unique knowledge and perspective of the group, on his view of the needs of the business going forwards. Neither the Chairman nor the CEO would be involved in the appointment process of their successor.

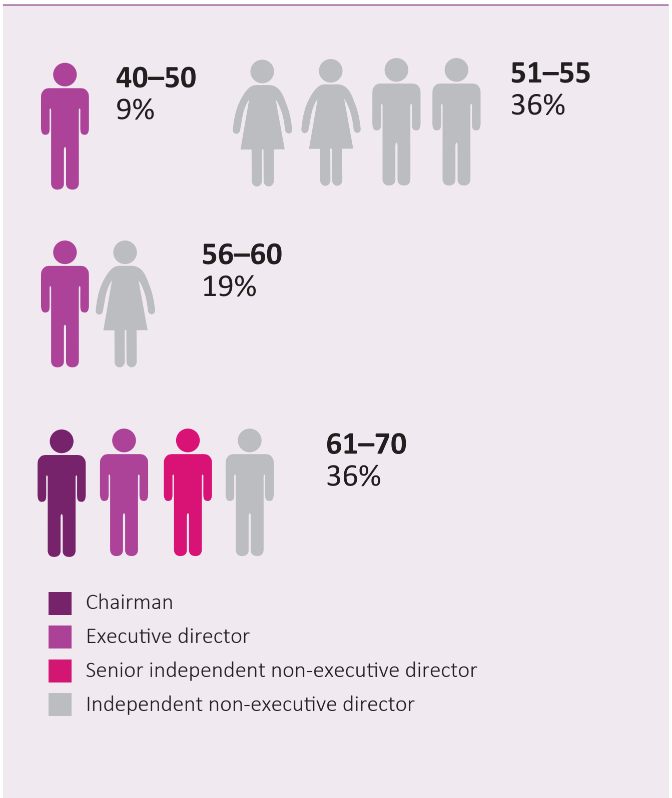
Board appointment process

Typically, following board discussions, the nomination committee will be responsible for drafting a brief, setting out the attributes and experience of a preferred candidate supported by the customer services and people director as part of the human resources function of the role. The brief would be shared with a number of executive search agencies (all of which would be signatories to the voluntary code of conduct on gender diversity for executive search firms) who would be invited to present their understanding of the role and attributes required. One of these firms would be engaged to conduct the search. A longlist of candidates would then be reviewed by the nomination committee and those identified for a shortlist would be invited for interview, initially with the Chairman, the CEO and the customer services and people director. Thereafter, a number of candidates would be invited to meet other non-executive directors and the CFO. Following the interview process, the nomination committee would meet to review and discuss the candidates (with the support of the customer services and people director) taking into account the views of the CEO/CFO and assess the 'best fit' with the succession planning and skills matrix and then make a recommendation to the board. References would be sought and reviewed by the Chairman prior to an appointment being taken up. A preferred candidate would also meet with representatives of Ofwat.

Directors' tenure as at 31 March 2019



Age profile



Corporate governance report
Nomination committee

Report by Mark Clare (senior independent non-executive director) on the appointment of Sir David Higgins as non-executive director and Chairman designate

The focus for the nomination committee this year has been to identify a suitable successor to John as Chairman. The brief was to find a candidate with the skills, experience and capability to take on the leadership of the board as the company prepares to implement its business plan for the next five year period and beyond, against a backdrop of an operating environment that continues to change.

The process to identify a new Chairman started with the appointment of a recruitment partner, the Lygon Group in November 2018 (other than providing executive search services on previous occasions, Lygon Group have no other connection with the company). The brief made it clear that we were very keen to ensure we considered and saw a diverse range of candidates. From an extensive and diverse longlist, seven candidates were seen in the first stage, two of whom were female.

Following a rigorous process involving all members of the board and including a meeting with our regulator, Ofwat we decided to appoint Sir David to succeed Dr John McAdam as Chairman. John will step down from the board on 31 December 2019. On his initial appointment as a non-executive director, Sir David will become a member of the nomination committee. He will also be appointed as a non-executive director of United Utilities Water Limited.

In recruiting Sir David, the board believes his substantial infrastructure experience, engineering background and understanding of regulated businesses make him an excellent appointment. We are delighted that he has accepted the position and the board looks forward to working under his leadership to deliver the company's 2020–25 business plan and beyond.

Sir David is currently chairman of Gatwick Airport Limited and a non-executive director of Commonwealth Bank of Australia, where he chairs the remuneration committee and is a member of the risk committee. Sir David will step down from the Commonwealth Bank of Australia in December 2019. Previously, he was chief executive of Network Rail Limited and The Olympic Delivery Authority. Sir David's full biography can be found on page 83 .

Having served on the Board for over 11 years, I would like to thank John for the pivotal role he has played in helping drive the considerable progress made by the business during that time, and for his wider contribution to the sector. His commitment and contribution to the company will be much missed and we wish him well for the future.

Membership of the principal board committees

No changes were made to the membership of the principal board committee during the year. On his appointment, Sir David Higgins became a member of the nomination committee.

Board diversity

The board diversity policy (see page 97) is to "ensure the selection process for board appointments provides access to a range of candidates. Any appointments will be made on the basis of merit and objective criteria, and within this context, should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths, but with due regard for the benefits of diversity on the board, including gender diversity." The objective of the policy is for new directors to bring something different to the board table, be it in terms of experience, skills, perspective, interests or other attributes. As referred to above, our board diversity policy would be brought to the attention of any executive search firm used as part of the selection and appointment process for a board position. Feedback would be sought from the search firm in terms of their success in attracting potential candidates with diversity of attributes and from any interview process conducted by other board members and taken into consideration in identifying suitable candidates. During the year, we have updated our board diversity policy, reflecting the recommendation of the review of the ethnic diversity of UK boards led by Sir John Parker and published in October 2017. We recognise the benefits of diversity, and its contribution to the effectiveness of the board decision-making process, and to the benefits of diversity across our entire employee population with initiatives in place to support women in the workplace and the ethnic imbalance of our workforce (see page 98).

Skills matrix of board directors

	Finance/ accounting	Utilities	Regulation	Government	Construction/ engineering	Industrial	Customer-facing	FTSE companies
Dr John McAdam		✓				✓	✓	✓
Steve Mogford		✓			✓		✓	✓
Russ Houlden	✓	✓	✓			✓	✓	✓
Steve Fraser		✓			✓	✓	✓	
Mark Clare	✓	✓	✓		✓		✓	✓
Sara Weller			✓	✓			✓	✓
Brian May	✓					✓	✓	✓
Stephen Carter		✓	✓	✓			✓	✓
Alison Goligher					✓	✓		✓
Paulette Rowe			✓		✓		✓	
Sir David Higgins			✓	✓	✓			

Summary of board diversity policy

- Ensure the selection process for board appointments provides access to a range of candidates. Any such appointments will be made on the basis of merit and objective criteria, and within this context, should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths.
- Ensure that the policies adopted by the group will promote diversity in the broadest sense among senior managers who will in turn aspire to a board position.
- In selecting candidates for board positions, only use the services of executive search firms who have signed up to the voluntary code of conduct for executive search firms as recommended by the Davies Report.
- Adopt measurable objectives from time to time for achieving gender diversity at board level – which shall be to maintain at least 25 per cent, and aspire to 33 per cent female representation by 2020 and to have at least one director of non-white ethnicity by 2021.

A typical induction programme

- Meet with members of the executive team discussing our business and regulation;
- Meet with the company secretary to gain an understanding of the group's governance arrangements and associated processes;
- Visit the integrated control centre based in Warrington, to meet staff, and gain an understanding of the digital monitoring and control of the group's water and wastewater network and assets;
- Meet with the corporate affairs director and head of sustainability;
- Meet with the customer services and people director to discuss the actions undertaken by the business to improve service to customers and the group's employee agenda;
- Meet with the wastewater network director and the water and scientific services director to gain an understanding of the wholesale operating model; and
- Visit the water and wastewater testing laboratories where regulatory and operational samples are analysed daily providing essential quality and compliance data.

Conflicts of interest and time commitment

The company's articles of association contain provisions which permit unconflicted directors to authorise conflict situations. Each director is required to notify the Chairman of any potential conflict or potential new appointment or directorship, and the board reviews the position of each director annually. No changes were recorded which would impact the independence of any of the directors.

The board does not specify the precise time commitment it requires from its non-executive directors in taking on the role as they are expected to fulfil it and manage their diaries accordingly. The board is content that none of its directors are overcommitted and unable to fulfil their responsibilities as a board director for United Utilities and are not overboarded. Each individual's circumstances are different, as is their ability to take on the responsibilities of a non-executive directorship role. Should a director be unable to attend meetings on a regular basis, not be preparing appropriately or not contributing appropriately to board discussions, the Chairman would be responsible for discussing the matter with them and agreeing a course of action.

Induction of new non-executive directors

An induction programme is devised for each new non-executive director. It would include one-to-one meetings with the Chairman and each of the existing non-executive directors. They will have one-to-one meetings with the CEO, CFO, COO and the company secretary along with other members of the executive team. They will also meet members of the operational teams and visit some of the key operational sites and capital projects to ensure they get a first-hand understanding of the water and wastewater business. New directors receive a briefing on the key duties of being a director of a regulated water company, including the role of the regulated company's holding company. They will also meet with the strategy and regulation director and are required to meet with representatives of Ofwat.

Wider succession pipeline and talent management

For a number of years, we have had a written succession plan for our executive directors and other members of the executive team, which now includes outline timescales. This plan identifies an interim internal successor to fill a role in the short term should the need arise, and the longer-term development needs of potential successors to be able to fulfil a role on a more permanent basis. As with all our board appointments, we would always aim to appoint the best person to fulfil a role. It would be common, when recruiting for a senior role, for an external search to be conducted alongside an internal candidate recruitment process.

Any changes that are required to the profile of the management team to reflect the changing needs of the business are considered by the board in the executive succession plan. Succession and development initiatives for senior executives include executive mentoring and coaching and participating in an executive business school programme. Leadership development centres have been delivered to identify and validate potential for future director and senior leader positions and develop a number of role-ready diverse candidates to provide the group with leadership capacity in an increasingly complex environment. Senior managers are encouraged to take on a non-executive directorship role as part of their personal development, but it is recognised that this is very much a personal commitment for each individual. We continue to work towards improving our gender balance across our employee population as part of our ongoing diversity and inclusion plan (see page 98).

During the year, board directors have a number of opportunities to meet with members of the executive team, both formally when senior managers are required to present at board meetings on matters related to their responsibilities, and on more informal occasions. From time to time, board members also have the opportunity to attend events and meet with members of the apprentice and graduate population and other employees identified as potential talent within the business.

Corporate governance report
Nomination committee

What we have done to improve diversity and inclusion in 2018/19

Gender

Our workforce profile has remained quite static at 65 per cent male and 35 per cent female. This is primarily due to the limited supply of females with the relevant skills available in the market and the legacy of a traditional male-orientated bias in science, technology, engineering and maths (STEM) careers.

At board level, 70 per cent are male and 30 per cent are female; the position is similar at the executive team level of 71 per cent male:29 per cent female. Encouragingly, there is a greater female representation in the direct reports to the executive team of 64 per cent male:34 per cent female. The overall number of female graduates is 41 per cent. We offer predominantly STEM based programmes and we are encouraged to see a more gender balanced pool of future talent. The apprentice population is 18 per cent female, an increase from nine per cent since 2014/15, and this compares favourably compared to the sector.

We are:

- celebrating the success of those of our senior and emerging female leaders included in the Northern Women Power List;
- continuing to look for targeted development for our future female leaders with cross company mentoring schemes and targeted personal development to support future progression;
- actively encouraging employees to join the gender equality network within the business;
- part of the 30 per cent Club campaign to achieve the target of 30 per cent female representation in senior leadership teams by 2020; and
- members of the EU skills diversity network and have signed a diversity pledge alongside 32 other businesses in the sector, with the aim of improving diversity business-wide.

Disability

In the North West, 19 per cent of the working age population are disabled or live with a long-term health condition; less than one per cent of our employees have declared a disability or long-term health condition. Our ability network aims to support employees with, or those who support, people with a disability or long-term health condition. In 2017 we gained the government recognised Disability Confident status, and are aiming to achieve Disability Leader status over the next 18 months. We are committed to guarantee interviews and making reasonable adjustments for people who are registered with a disability, and will continue to promote this to attract candidates from the widest talent pool.

Our Time to Change campaign, normalising the stigma of mental health and providing support to employees through our network of trained mental health first aiders, is sponsored by Steve Fraser, COO. Similarly, Louise Beardmore, customer services and people director, sponsors and raises awareness of dyslexia across the business. We will participate and promote National Dyslexia week to encourage awareness and support employees with the condition.

Ethnicity

The Black Asian Minority Ethnic (BAME) representation of our workforce is two per cent; 15 per cent of our workforce choose not to disclose ethnicity. We hold Bronze status in the Business in the Community Race for Opportunity programme. Attracting a future pipeline of employees from multi-cultural backgrounds remains a priority. We are in the second year of partnership with Teach First as a way to gain access to talented young people from diverse cultural communities in our region, particularly in areas where English is a second language. We have strategic partnerships with universities and other education providers, with higher levels of BAME presence in their student population in order to improve the ethnicity of our workforce profile.

We are members of the National Apprenticeship Champions Diversity Network Forum, which works alongside other companies in the UK, to address the challenge of recruiting more apprentices from BAME backgrounds. We have joined the Energy and Utility Skills Diversity Forum to enable us to promote and contribute to the agenda in our sector.

Social mobility

During the year we signed up to the UK Government's social mobility pledge, committing to provide support to people from communities with low social mobility. Youth unemployment in the North West is higher than the national average at 11.2 per cent. We recognise that our region's young people come from a range of socio-economic backgrounds which can contribute, along with personal challenges, to the difficulties of finding work.

In collaboration with our partners, we have continued to lead our youth programme, started in 2014, supports young people from across our region who are not in education, employment or training (NEET) become work ready. This collaboration has supported over 80 young people, with 79 per cent of participants obtaining paid employment after the programme. The Prince's Trust measure the social value of the programme at £150,000 per person.

Flexible working

We comply with, and often exceed, our statutory obligations to provide flexible and part-time working patterns for our employees to reflect stages in their individual lifecycle. We provide the opportunity for money and credit management advice to the under 30s through to financial management and budgeting in retirement. We are committed to considering modifying working practices and policies to reflect what is important to employees at different points in the employment lifecycle.

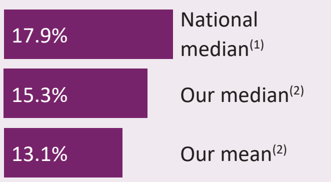
LGBT+

Identity+, our lesbian, gay, bisexual and trans employee network, has over 500 members. Plans are in place to gain external recognition for the excellent colleague support provided by the network, which has an active presence in our communities often being involved, in annual pride events across our region. We hope to encourage those involved in our LGBT+ network to play an active role in their own communities to promote United Utilities as an employer of choice.

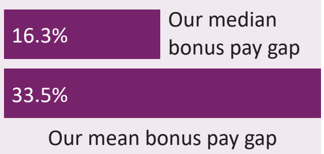
Gender pay

At present, we have a higher proportion of men at more senior levels within our organisation and more men in higher-skilled and higher-paid roles which contributes to the gender pay gap. We have an action plan in place which focuses on how we challenge tradition and attract more women into these currently male dominated roles; how we develop our female talent to increase the number of women in senior positions and strengthen succession pipelines; and leading from the top on a commitment to change. Our gender equality network (GENEq) aims to support, mentor, develop, inspire and promote both men and women in United Utilities to realise the benefits of gender equality. Our gender pay gap figures are shown below. Further details can be found in the full report; a copy can be found at **unitedutilities.com/corporate/responsibility/employees/diversity/**

Median and mean gender pay gap



Median and mean bonus gender pay gap(3)



93.3 per cent of males and 96.2 per cent of females received a bonus payment. Levels are less than 100 per cent as the eligibility criteria requires a minimum level of service to be completed during the bonus year and therefore some new starters may not be eligible.

(1) Source: Office for National Statistics October 2018.
(2) Source: company payroll data for the month of April 2018.
(3) Source: company payroll data, bonus paid in the 12 months period preceding 30 April 2018.

Code principle – Relations with shareholders

Introduction by Dr John McAdam

"We welcome the opportunity to engage with investors. Face-to-face meetings are particularly useful in gaining a better understanding of investors' views. Feedback from investor meetings is regularly shared with board colleagues."

The board as a whole accepts its responsibility for engaging with shareholders and is kept fully informed about information in the marketplace including:

- The investor relations adviser produces an annual survey of investors' views and perceptions about United Utilities, the results of which are presented and discussed by the board;
- The board receives regular updates and feedback on investor meetings involving the CEO, CFO and/or investor relations team and reports from sector analysts to ensure that the board maintains an understanding of investors' priorities; and
- The executive and non-executive directors are available to meet with major shareholders and institutional investors; this is also one of the specific roles of the senior independent director. Feedback from any such meetings would be shared with all board members.

Institutional investors

We are always keen to engage with our shareholders, hear their views and update them on developments in our business. As well as current investors, we engage actively with institutional investors who do not currently hold shares in United Utilities, as we are keen to ensure our business is well understood across the investment community, and to hear and discuss the views of all investors.

We have an active investor relations programme, which includes:

- A regular schedule of face-to-face meetings between the CEO and CFO and representatives from our major shareholders, supplemented with meetings hosted by our investor relations team;
- Presentations by the CEO and CFO to groups of institutional investors, both on an ad hoc basis and linked to our half and full-year results announcements;
- The programme covers a range of major global financial centres, typically including the UK, Europe, North America and the Asia Pacific region;
- Regular feedback is provided to the board on the views of our institutional investors following these meetings; and
- Close contact is also maintained between the investor relations team and a range of City analysts that conduct research on United Utilities.

In 2018/19, through our investor relations programme, we met or offered to meet with 78 per cent, by value, of the overall shareholder base, of the targetable institutional shareholder base (after adjusting for shareholders who do not typically meet with companies, such as indexed funds).

Frequent areas of common interest arising in meetings with investors include operational and environmental performance, customer service, capital investment, efficiency initiatives, regulatory performance, regulatory changes and political risk. Investors are always keen to observe financial stability and are interested in: the level of gearing versus regulatory assumptions; cost of finance; our debt portfolio and debt maturity profile; future financing requirements; and dividends. The performance against the final determination for the 2015–20 period is a key area of interest, and investors are also keen to understand how the company is performing relative to the price review allowances and targets each year, along with the potential implications of regulatory change and political risk. Furthermore, investors are keen to hear how we are progressing with our plans for the 2020–25 regulatory period and beyond.

Retail shareholders

Despite the privatisation process being around 30 years ago, we have retained a large number of individual shareholders with registered addresses in the North West of England – in fact, over 50 per cent of registered shareholdings on the share register. We have historically always held our AGM in our region in Manchester, which enables our more local shareholders, many of whom are also our customers, to attend the meeting. We endeavour to hold the meeting at a venue which is both centrally located in the city (to enable shareholders to use public transport should they so wish) while being mindful of the costs.

There is a considerable amount of information on our website, including our online report which provides information on our key social and environmental impacts and performance during the year. Together with the annual and half-yearly results announcements, our annual report and financial statements are also available on our website; these are the principal ways in which we communicate with our retail shareholders. Our company secretariat and investor relations teams, along with our registrar, Equiniti, are also on hand to help our retail shareholders with any queries. Information for shareholders can also be found on the inside back cover of this document, with a number of useful website addresses.

Outcome of 2018 AGM

At the 2018 AGM, votes were cast in relation to approximately 65 per cent of the issued share capital. All 21 resolutions were passed by the required majority.

Votes were cast in favour of the reappointment of the board directors as follows:

Dr John McAdam	99.73%	Russ Houlden	99.29%
Steve Mogford	99.73%	Brian May	99.72%
Stephen Carter	99.74%	Paulette Rowe	99.74%
Mark Clare	99.73%	Sara Weller	99.51%
Alison Goligher	99.72%		

Steve Fraser was elected with 99.55% of the votes.

Sir David Higgins will stand for election by shareholders for the first time at the 2019 AGM as a non-executive director and Chairman designate.

Corporate governance report

Relations with banks and credit investors

Running a water and wastewater business, by its very nature, requires a long-term outlook. Our regulatory cycle is based on five-year periods, and we raise associated funding in order to build and improve our water and wastewater treatment works and associated network of pipes for each five-year cycle and beyond. We are heavily reliant on successfully acquiring long-term funding from banks and credit investors to fund our capital investment programme and refinance upcoming debt maturities.

This requires long-term support from our credit investors who invest in the company by making term funding available in return for receiving interest on their investment and repayment of principal on maturity of the loans or bonds. We arrange term debt finance in the bond markets (with maturities typically ranging from seven years to up to 50 years at issue). Debt finance is raised via the group's London listed multi-issuer Euro Medium Term Note Programme, which gives us access to the sterling and euro public bond markets and privately arranged note issues. Committed credit facilities are arranged with our relationship banks on a bilateral basis. Additionally, the European Investment Bank (EIB), which is the financing arm of the European Union (EU), is our single biggest lender, currently providing around £1.8 billion of loan funding to support our capital investment programmes (past and present).

Following the 2016 referendum regarding the UK exiting the EU (Brexit), it is likely that the EIB will significantly curtail new lending into the UK once Brexit has been effected. We therefore expect that post-Brexit, further loans from the EIB will not be available and our existing loan portfolio with the EIB will enter into 'run-off' in line with the scheduled maturities of each loan. The group is therefore likely to access the debt capital markets on a more regular basis post-Brexit.

The group currently has gross borrowings of *circa* £7,816 million. Given the importance of debt funding to our group, we have an active credit investor programme coordinated by our group treasury team, which provides a first point of contact for credit investors' queries and maintains a dedicated area of the company's website. One-to-one meetings are held with credit investors through a programme aimed at the major European fund managers known to invest in corporate bonds that may be existing holders of the group's debt or potential holders. Regular mailings of company information are sent in order to keep credit investors informed of significant events. The treasury team has regular dialogue with the group's relationship banks and the EIB and the credit rating agencies. More information can be found on our website at **unitedutilities.com/corporate/investors/credit-investors**

During the year, the rating agency services provided to the group were reviewed. Moody's Investors Service Limited, S&P Ratings Europe Limited and Fitch Ratings Ltd were appointed to provide credit rating services to the group for an initial three-year term. Future debt capital market issuance by the group will benefit from solicited ratings from all three rating agencies.

Code principle – Accountability

Introduction by Dr John McAdam

"Risk and viability reporting are an area of key interest for investors. Management has recommended, and the board has approved a more detailed and informative long-term viability statement, in line with the FRC's guidance in its letter to audit committee chairs and finance directors published in October 2018."

Board's approach to risk management and internal control

The board discharges its responsibility for determining the nature and extent of the risks that it is willing to take to achieve its strategic objectives through the risk appetite framework. As a key part of the risk management framework, risk appetite captures the board's desire to take and manage risk relative to the company's obligations, stakeholder interests and the capacity and capability of our key resources.

The board is also responsible for ensuring that the company's risk management and internal control systems are effectively managed across the business and that they receive an appropriate level of scrutiny and board time. The group's risks predominantly reflect those of all regulated water and wastewater companies. These generally relate to the failing of regulatory performance targets or failing to fulfil our obligations in any five-year planning cycle, potentially leading to the imposition of fines and penalties, in addition to reputational damage. Political risk is also closely monitored.

Review of the effectiveness of the risk management and internal control systems

During the year, the board reviewed the effectiveness of the risk management systems and internal control systems, including financial, operational and compliance controls. Taking into account the principal risks and uncertainties set out on pages 72 to 75 , and the ongoing work of the audit committee in monitoring the risk management and internal control systems on behalf of the board (and to whom the committee provides regular updates, see pages 109 and 111), the board:

- Is satisfied that it has 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; and
- Has reviewed the effectiveness of the risk management and internal control systems including all material financial, operational and compliance controls (including those relating to the financial reporting process) and no significant failings or weaknesses were identified. After review, it was concluded that through a combination of the work of the board, the audit committee and the UUW board (which has particular responsibility for operational and compliance controls), the company's risk management and internal controls were indeed effectively monitored throughout the year.

In the review of the effectiveness of risk management and internal controls systems, the board also took into account the:

- Biannual review of significant risks (see page 68);
- Outcome of the biannual business unit risk assessment process (see page 110);
- Activities and review of the effectiveness of the internal audit function (see page 110);
- Opinion provided by internal audit in relation to their work, that "the governance, risk management and internal control framework was suitably designed and effectively applied within the areas under review";
- Self-assessment provided by management confirmed compliance with a range of key internal policies, processes and controls (see page 111);
- Review of reports from the group audit and risk board (see page 110);
- Oversight of treasury matters in particular debt financing and interest rate management (see page 64); and
- Review of the business risk management framework and management's approach and tolerance towards risk (see page 110).

Going concern and long-term viability

The board, following the review by the audit committee, concluded that it was appropriate to adopt the going concern basis of accounting (see page 68). Similarly, in accordance with the principles of the Code, the board concluded, following the recommendation from the audit committee, that it was appropriate to provide the long-term viability statement (see below). Assurance supporting these statements was provided by the review of: the group's key financial measures and contingent liabilities; the key credit financial ratios; and the group's liquidity and ongoing ability to meet its financial covenants. As part of the assurance process, the board also took into account the principal risks and uncertainties facing the company, and the actions taken to mitigate those risks, and include emerging and more topical risks.

These principal risks and uncertainties are detailed on pages 72 to 75, as are the risk management processes and structures used to monitor and manage them. Biannually, the board receives a report detailing management's assessment of the most significant risks facing the company. The report gives an indication of the level of exposure, subject to the mitigating controls in place, for the risk profile of the group, while also highlighting the reputational and customer service impact. This provides the board with information in two categories: group-wide business risks; and wholesale operational risks. The board also receives information during the year from the treasury committee (to which the board has delegated matters of a treasury nature – see the structure diagram on page 87) including such matters as liquidity policy, the group's capital funding requirements and interest rate management. The board has reconsidered its viability assessment period. In line with the work undertaken to support the financial resilience element of the UUW draft business plan, as submitted to Ofwat on 3 September 2018, the board believes that under the current regulatory and statutory framework a period of seven years to assess the group's long-term viability is appropriate. After review, the board concluded that among other things, because of the nature of the regulatory regime of the water sector and the clarity of Ofwat's business plan assessment process contributing to the longer-term planning horizon for the sector, it was comfortable with the extension of the period from a five-year to a seven-year term.

Long-term viability statement

The directors have assessed the viability of the group, taking account of the group's current position, the potential impact of the principal risks facing the business in severe but reasonable scenarios, and the effectiveness of any mitigating actions. This assessment has been performed in the context of the group's prospects as considered over the longer term. Based on this viability assessment, the directors have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the seven year period to March 2026.

Basis of assessment

The long-term planning detailed on page 48 assesses the group's prospects and establishes its strategy over a 25-year time horizon consistent with its rolling 25-year licence and its published long-term strategy. This provides a framework for the group's strategic planning process, and is key to achieving the group's aim of providing the best service to customers at the lowest sustainable cost and in a responsible manner over the longer term, underpinning our business model set out on pages 24 to 36.

In order to achieve this aim and promote the sustainability and resilience of the business, due consideration is given to the management of risks over the long term that could impact on the business model, future performance, credit ratings, solvency and liquidity of the group. An overview of our risk management approach that supports the group's long-term planning and prospects, together with the principal risks and uncertainties facing the business, can be found on pages 68 to 75.

Fundamental assumptions

This viability statement is based on the fundamental assumption that the current regulatory and statutory framework does not substantively change, for example a change that facilitated the compulsory purchase of the shares or assets of either UUW or the company for the renationalisation of the water sector.

Viability assessment: resilience of the group

The viability assessment is based upon the group's medium-term business planning process, which sits within the overarching strategic planning process and considers:

- the group's current liquidity position – with £1.0 billion of available liquidity at March 2019 covering funding requirements through to 2021, this provides a significant buffer to absorb short-term cash flow impacts;
- the group's robust capital solvency and credit rating positions – with a debt to regulatory capital value (RCV) ratio of around 60 per cent, a robust pension position and current credit ratings of A3/A-/A- with Moody's, S&P and Fitch respectively, this provides considerable headroom supporting access to medium-term liquidity where required;
- the group's expected performance, underpinned by its historical track-record – Ofwat's Initial Assessment of Plans, published in January 2019, scored the group's business plan the highest across the industry and has given good early visibility of expected cash flows for the 2020–25 period; and
- the current regulatory framework within which the group operates – which provides a high degree of cash flow certainty over the regulatory period and the broader regulatory protections outlined below.

The group has a proven track-record of being able to raise new forms of finance in most market conditions, and expects to continue to do so into the future. This is despite the likely inability to secure future EIB funding should the UK exit from the EU.

Corporate governance report

From a regulatory perspective, the group benefits from a rolling 25-year licence and a regulatory regime in which regulators – including the economic regulator, Ofwat – are required to have regard to the principles of best regulatory practice. These include that regulation should be carried out in a way that is transparent, accountable, proportionate, consistent and targeted. Ofwat's primary duties provide that it should protect consumers' interests, by promoting effective competition wherever appropriate; secure that the company properly carries out its statutory functions; secure that the company can finance the proper carrying out of these functions – in particular through securing reasonable returns on capital; and secure that water and wastewater supply systems have long-term resilience and that the company takes steps to meet long-term demands for water supplies and wastewater services.

In addition, from an economic perspective, given the market structure of water and wastewater services, threats to the group's viability from risks such as reduced market share, substitution of services and reduced demand are low compared to those faced by many other industries.

Viability assessment: resilience to principal risks facing the business

The directors have assessed the group's viability based on the resilience of the group and its ability to absorb a number of 'severe but reasonable' scenarios, derived from the principal risks facing the group, as set out on pages 72 to 75. Such risks include: environmental risks such as the occurrence of extreme weather events; political and regulatory risks; the risk of critical asset failure; significant cyber security breaches; and the potential for a restriction to the availability of financing resulting from a capital markets crisis. Specifically in relation to a 'no deal' Brexit scenario, while this may have adverse operational and financial impacts on the group, this risk does not represent a significant risk to the ongoing viability of the group.

The assessment has considered the impact of these scenarios on the group's business model, future performance, credit ratings, solvency and liquidity over the course of the viability assessment period. This assessment has demonstrated the group's ability to absorb the impact of all severe but reasonable scenarios modelled, without the need to rely on the key mitigating actions detailed below.

As part of the assessment, reverse stress testing of extreme theorectical scenarios has been performed to understand the headroom in the group's ability to absorb all severe but reasonable scenarios.

Viability assessment: key mitigating actions

In the event of more extreme but low likelihood scenarios occurring, there are a number of key mitigations available to the group, the effectiveness of which are underpinned by the strength of the group's capital solvency position.

As well as the protections that exist from the regulatory environment within which the group operates, a number of actions are available to mitigate more severe scenarios, which include: the raising of new finance; capital programme deferral; the closeout of derivative asset positions; the restriction of dividend payments; and access to additional equity.

Extending the viability period to seven years

Recognising the group's expected performance underpinned by its historical track-record, Ofwat's positive assessment of its 2020–25 business plan which was awarded fast-track status and the protections provided by the regulatory framework, the board considers it appropriate to extend the viability statement to cover a seven-year period.

In determining this period, the board had regard for the increasing level of uncertainty as the duration of the assessment period is extended and the desire to maintain a robust viability assessment.

Governance

The analysis underpinning this assessment has been through a robust internal review process, which has included scrutiny and challenge from the audit committee and board, and has been reviewed by the group's external auditor, KPMG, as part of their normal audit procedures.

Going concern

The directors also considered it appropriate to prepare the financial statements on the going concern basis, as explained in the basis of preparation paragraph in note 1 to the accounts.

Read more about **Our business model** on pages 24 to 38

Read more about the **Principal risks and uncertainties** on pages 68 to 75

Read more online at **unitedutilities.com/corporate/about-us/our-future-plans/**

Corporate governance report
Audit committee

During the year, the committee reviewed and agreed with management's proposal to extend the company's 2019 long-term viability period to cover a seven-year period.

Pictured: Paulette Rowe, Brian May and Stephen Carter

Quick facts

- Brian May has chaired the committee since July 2013. He is a serving finance director of a FTSE 100 company and chartered accountant and is considered by the board to have recent and relevant financial experience.
- All members of the committee are independent non-executive directors and the Board is satisfied that the committee as a whole has competence relevant to the sector and its members have an appropriate level of experience of corporate financial matters.
- Other regular attendees at meetings at the invitation of the committee include the Chairman of the board, the CEO, the CFO, the company secretary, the head of audit and risk, the group controller, and representatives from the external auditor KPMG LLP (KPMG). None of these attendees are members of the committee.
- The representatives from KPMG and the head of audit and risk are each afforded time with the committee and the company secretary to raise freely any concerns they may have without management being present.
- The committee is authorised to seek outside legal or other independent professional advice as it sees fit, but has not done so during the year.

Quick links

Terms of reference –
unitedutilities.com/corporate-governance

Audit committee members

- Brian May (chair)
- Paulette Rowe
- Stephen Carter

Dear Shareholder

In my report this year I have sought to provide shareholders with an understanding of the work we have done as the audit committee to provide assurance on the integrity of the 2018/19 annual report and financial statements. All directors have a duty to act in a way they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and have regard to other stakeholders as set out in s172 of the Companies Act 2006. The directors' responsibility statement in respect of the annual report and financial statements can be found on page 153.

The particular role of the audit committee is to ensure that the interests of shareholders are properly protected in relation to the company's financial reporting and internal control arrangements and to provide challenge to the decisions and approach made by the management team relating to the content and disclosures within the company's financial reports. As articulated in both the 2016 and 2018 versions of the Code, "the board should present a fair, balanced and understandable assessment of the company's position and prospects". The board asks the audit committee to advise on whether in fact "the annual report and accounts, taken as a whole, is fair balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy". The audit committee's role is to ensure that management's disclosures reflect the supporting detail or challenge them to explain and justify their interpretation and, if necessary, re-present the information. The committee is supported in this role by using the expertise of the external auditor, who in the course of the statutory audit, reviews the accounting records kept by the company to test whether information is being recorded in line with agreed accounting practices. The external auditor presents its findings to the shareholders as the owners of the business, and their report is set out on pages 156 to 161. The committee reports its findings and makes recommendations to the board accordingly.

The audit committee is responsible for ensuring that the three-way relationship between the committee, the auditor and the company's management is appropriate. The external auditor must be independent of the company. Independence is a key focus for both the external auditor, whose staff must comply with their firm's own ethics and independence criteria which must be consistent with the FRC's Revised Ethical Standard 2016, and the committee, in order to ensure the integrity of the auditing process and the annual report and financial statements. Information on how the committee assesses the independence of the external auditor is set out on page 107.

In June 2018 the FRC published the 2017/18 versions of its audit quality inspection reports (AQIRs) of the 'big four' audit firms, including KPMG. The FRC, as the competent authority for audit regulation in the UK, were critical of the firms for different reasons, but their overall view was that there was a decline in audit quality. In response to its AQIR, KPMG have set in place an audit quality transformation plan and invested in face-to-face training courses for all their audit professionals, and have expressed their commitment to continue their focus on audit quality. The committee invited KPMG, at its meeting in September 2018, to explain their audit quality transformation plan and the initiatives being applied to their plans and strategy for our 2018/19 audit (see page 106). The committee welcomes this commitment and will review the evidence of the enhancements to the processes later in the year.

Corporate governance report
Audit committee

During the year, the committee reviewed and agreed with management's proposal to extend the company's 2019 long-term viability statement to cover a seven-year period (see page 109), rather than the five-year period as in previous years. It was agreed that such an approach was appropriate given the nature of the regulatory regime in the water sector and the clarity of Ofwat's business plan assessment contributing to the longer-term planning horizon for the sector.

This is the last year when my report contains an overview of the company's whistleblowing arrangements (see page 111), as this work in future will be the direct responsibility of the board, reflecting the 2018 Code; however, the committee will act upon any relevant findings impacting its areas of responsibility as appropriate.

As chair of the committee I reiterate the board's view (see page 85) that the committee as a whole has competence relevant to the sector, as disclosed in the biographies of the relevant committee members (see pages 80 to 83). All members contribute to the work of the committee and have the skills and necessary degree of financial literacy. As non-executive directors, my colleagues and I are of an independent mindset and would have no hesitation in seeking clarification and a full explanation from management or the external auditor on any matter we feel necessary.

Much of the work of the committee is necessarily targeted at the regulated activities of UUW, which represent over 98 per cent of group revenues and is a reflection of our commitment to safeguarding the interests of our stakeholders, particularly our shareholders and customers.

We continue to be committed to providing meaningful disclosure of the committee's activities. As chair of the audit committee, I am intent on ensuring that the committee's agenda is kept under review and keeps abreast of relevant developments. The details of the annual evaluation process of the committee's performance can be found on page 91.

The following report was approved by the committee at its meeting held on 14 May 2019.

Brian May
Chairman of the audit committee

Main responsibilities of the committee

- Make a recommendation to the board for the appointment or reappointment of the auditor, and to be responsible for the tender of the audit from time to time and to agree the fees paid to the auditor.
- Establish policies for the provision of any non-audit services by the auditor.
- Review the scope and the results of the annual audit and report to the board on the effectiveness of the audit process and how the independence and objectivity of the auditor has been safeguarded.
- Review the half-year and annual financial statements and any announcements relating to financial performance, including reporting to the board on the significant issues considered by the committee in relation to the financial statements and how these were addressed.
- Review the scope, remit and effectiveness of the internal audit function and the group's internal control and risk management systems.
- Review the group's procedures for whistleblowing (up until 31 March 2019), reporting fraud and other inappropriate behaviour and to receive reports relating thereto.
- Report to the board on how it has discharged its responsibilities.

What has been on the committee's agenda during the year?

The committee has an extensive agenda of items of business focusing on the audit, assurance and risk processes within the business which it deals with in conjunction with senior management, the auditor, the internal audit function and the financial reporting team. In doing so it ensures that high standards of financial governance, in line with the regulatory framework as well as market practice for audit committees going forward, are maintained. There were four scheduled meetings of the committee during the year. Items of business considered by the committee during the year are set out in the table below.

	Cross reference
– Considered the issues and findings brought to the committee's attention by the internal audit team and satisfied itself that management has resolved or is in the process of resolving any outstanding issues or concerns.	See page 109
– Reviewed and discussed the reports from the financial reporting team on the financial statements, considered management's significant accounting judgements, and the policies being applied and how the statutory audit contributed to the integrity of the financial reporting.	See page 108
– Reviewed the regulatory reporting process relating to the annual performance report for UUW as required to be submitted to Ofwat and noted the differences between the regulatory and statutory accounts.	–
– Reviewed the company's approach to the adoption of International Financial Reporting Standards (IFRS) IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts With Customers which was a particular focus for the committee. Updates on the adoption of IFRS 16 Leases, which would first impact the 31 March 2020 financial statements, were received.	See page 168
– Reviewed the proposed audit strategy for the 2018/19 statutory audit, including the level of materiality applied by KPMG, audit reports from KPMG on the financial statements and the areas of particular focus for the 2018/19 audit, and tasked management to resolve any issues relating to internal controls and risk management systems.	See page 156
– Reviewed the basis of preparation of the financial statements as a going concern (prior to making a recommendation to the board) as set out in the accounting policies.	See page 101
– Reviewed the long-term viability statement, in particular the extension of the period from a five-year to a seven-year term, prior to making a recommendation to the board.	See page 101
– Reviewed the results of the committee's assessment of the effectiveness of the 2017/18 external audit along with receiving a presentation from KPMG on the proposals for their Audit Quality Transformation Plan and confirmation of the independence of the auditor and made a recommendation to the board on the reappointment of KPMG as the external auditor at the forthcoming annual general meeting.	See page 106
– Reviewed the 2018/19 annual report and financial statements and provided a recommendation to the board that they complied with the Code principle to be 'fair, balanced and understandable'.	See page 106
– Reviewed KPMG's proposed audit quality improvement plan applicable to the 2018/19 statutory audit.	See page 106
– Approved revised terms of reference, which would be applied from 1 April 2019, reflecting the 2018 UK Corporate Governance Code prior to making a recommendation to the board.	See page 103
– Reviewed the effectiveness of the risk management and internal control systems prior to making a recommendation to the board.	See page 109
– Negotiated and agreed the statutory audit fee for the year ended 31 March 2019 and agreed the fee approach for subsequent years.	See page 107
– Reviewed and approved the non-audit services and related fees provided by the external auditor for the year 2018 and approved the policy on non-audit services provided by the auditor for 2019/20.	See page 107
– Monitored fraud reporting and incidents of whistleblowing.	See page 111
– Biannual oversight and monitoring of the group's compliance with the Bribery Act which the board then reviews annually.	See page 111
– Approved the strategic internal audit planning approach and reviewed reports on the work of the internal audit function from the head of audit and risk.	See page 110
– Reviewed the quality and effectiveness of internal audit and the effectiveness of the current co-source arrangements.	See page 110
– Reviewed and approved the approach and internal audit plan for 2019/20.	See page 110
– Reviewed the conclusions of the committee's annual evaluation. The internally facilitated evaluation was undertaken as part of the overall board evaluation. The review explored: time management, the composition of the committee and the management of the meetings; the committee's processes and support; the agenda and work of the committee; and the priorities for change. All elements of the workings of the committee reviewed scored well. It was concluded that the committee continued to be effective.	See page 91

Corporate governance report
Audit committee

How we assessed whether "the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy"

The committee, further to the board's request, has reviewed the annual report and financial statements with the intention of providing advice to the board on whether, as required by the Code, "the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy".

To make this assessment, the committee received copies of the annual report and financial statements to review during the drafting process to ensure that the key messages being followed in the annual report were aligned with the company's position, performance and strategy being pursued and that the narrative sections of the annual report were consistent with the financial statements. The significant issues considered by the committee in relation to the financial statements were consistent with those identified by the external auditor in their report on pages 156 to 159.

The committee received regular updates on the calculation of underlying operating profit measures as one of the principal alternative performance measures (APMs). A guide to APMs can be found on page 66. APMs are used in accordance with the ESMA guidelines and management highlights any impact on APMs as a result of changes to accounting methods/transactions.

The key performance indicators included in the strategic report (see pages 51 to 54) were, among others, those used by management and some of which reflect the regulatory measures to be monitored by either Ofwat, the DWI or the EA during the 2015–20 period.

Additionally, the committee was satisfied that all the key events and issues which had been reported to the board in the executive team's monthly board reports during the year, both good and bad, had been adequately referenced or reflected within the annual report.

How we assessed the effectiveness of the external audit process

The committee, on behalf of the board, is responsible for the relationship with the external auditor, and part of that role is to examine the effectiveness of the audit process. Audit quality is a key requirement of the external audit process.

In June 2018, the FRC, as the competent authority for audit regulation in the UK, published its 2017/18 Audit Quality Inspection Reports (AQIRs) for each of the 'big four' audit firms, including KPMG. Such reports are published annually. In the AQIRs, the FRC identified areas of improvement for all four firms. KPMG was asked to make improvements in the following areas: to ensure that the extent and rigour of challenge of management in areas of judgement fully demonstrates professional scepticism; to strengthen the involvement of the group audit team in component audits; to improve the consistency and quality of audit work over pension scheme assets and liabilities; and to enhance the audit of management review controls, in particular for entities with long-term contracts. KPMG was identified as having made good progress in ensuring that its policies and procedures on independence complied with the requirements of the FRC Revised Ethical Standard 2016 (FRC's Ethical Standard).

It was reported in the 2018 audit committee report that KPMG had expressed its commitment to the committee to improve audit quality, providing extra resource to supplement the usual audit team in order to ensure additional oversight and review of the 2017/18 audit. Consequently, KPMG provided an overview of its updated Audit Quality Transformation Plan (AQTP) to address the improvements identified by the FRC, in its AQIRs, to the committee in September 2018. Their AQTP included: a more standardised audit approach; their intention to hold companies to account for the quality of the information provided to them in the audit process; their intention to provide more feedback to companies on the findings of their audit and provide additional senior level support to the KPMG audit teams during the audit. The committee will review the evidence of the enhancements to the external audit processes later in the year.

KPMG presented the strategy and scope of the external audit for the forthcoming financial year at the meeting of the committee held in September, highlighting any areas which would be given special consideration. KPMG report against this audit scope at subsequent committee meetings, providing an opportunity for the committee to monitor progress and raise any questions. Private meetings are also held at each committee meeting between the audit committee and representatives of the external auditor without management being present in order to encourage open and transparent feedback by both parties.

On completion of the external audit process at the full-year, all members of the committee, as well as key members of the senior management team and those who regularly provide input into the audit committee or have regular contact with the external auditor, complete a feedback questionnaire seeking their views on how well KPMG performed the year-end audit.

Views of the respondents were sought in terms of:

- the robustness of the external audit process and degree of challenge to matters of significant audit risk and areas of management subjectivity;
- whether the scope of the audit and the planning process were appropriate for the delivery of an effective and efficient audit;
- the quality of the delivery of the audit;
- the expertise of the audit team conducting the audit;
- that the degree of professional scepticism applied by the external auditor was appropriate;
- the appropriateness of the communication between the committee and the external auditor in terms of technical issues;
- the quality of the service provided by the external auditor;
- their views on the quality of the interaction between the audit partner, the audit senior manager and the company; and
- whether the statutory audit contributed to the integrity of the group's financial reporting.

The feedback was collated and presented to the committee's meeting in November 2018, at which the conclusions were discussed and any opportunities for improvement brought to the attention of the external auditor.

In summary, the committee concluded, that given KPMG's commitment to make improvements to its policies and processes impacting audit quality, and in relation to the additional oversight provided in relation to the 2017/18 audit, it was agreed that the external audit process and services provided by KPMG were satisfactory and effective.

How we assessed the independence of our external auditor

There are two aspects to auditor independence that the committee monitors to ensure that the external auditor remains independent of the company.

Firstly, in assessing the independence of the auditor from the company the committee takes into account the information and assurances provided by the external auditor confirming that all its partners and staff involved with the audit are independent of any links to United Utilities. KPMG confirmed that all its partners and staff complied with their ethics and independence policies and procedures which are fully consistent with the FRC's Ethical Standard including that none of its employees working on our audit hold any shares in United Utilities Group PLC. KPMG is also required to provide written disclosure at the planning stage of the audit about any significant relationships and matters that may reasonably be thought to have an impact on its objectivity and independence and that of the lead partner and the audit team. The lead audit partner must change every five years and other senior audit staff rotate at regular intervals.

Secondly, the committee develops and recommends to the board the company's policy on non-audit services and associated fees that are paid to KPMG. The EU Audit Directive (2014/56/EU) and Audit Regulation (537/2014) (the Regulation) came into force in the UK on 17 June 2016. Associated guidance was included in the FRC's Ethical Standard, which prohibits the statutory auditor from providing certain non-audit services to public interest entities (i.e. United Utilities Group PLC) as such services could impede their independence. The FRC's Ethical Standard clarified that non-audit services would be subject to a fee cap of no more than 70 per cent of the average annual statutory audit fee for the three consecutive financial periods preceding the financial period in which the cap will apply.

The cap will first apply for the group in the year ending 31 March 2021 and, as such, our year ended 31 March 2018 will be the first year of the initial three-year rolling period over which the annual statutory audit fee will be measured for this purpose. The committee revised the non-audit services policy incorporating the 70 per cent fee cap as described above with effect from 1 April 2017. Furthermore, a limit of £10,000 is applied for individual items that the CFO can approve, with individual items in excess of £10,000 requiring the approval of the committee.

Fees for non-audit services are shown in the bar chart below (2019: £65,000) and represent 15 per cent of the total audit fees. Non-audit services fees (2018: £80,000; 2017: £201,000) in 2017 were considerably higher reflecting the inclusion of fees paid to Makinson Cowell, a subsidiary of KPMG, which provided investor relations services to the group until 31 March 2017. Investor relations services are regarded as a prohibited service under the Regulation. Fees paid to KPMG also include the cost of the UUW regulatory assurance work they undertake which is separate to the regulatory audit. While this work could be performed by a different firm, the information is in fact more granular breakdowns of data that form part of the statutory audit, and by KPMG undertaking the work it reduces duplication and saves considerable cost.

Work undertaken by KPMG in auditing management's methodology and processes in the implementation of the new international financial reporting standards and related disclosures and judgements is included in the statutory audit fee.

Taking into account our findings in relation to the effectiveness of the audit process and in relation to the independence of KPMG, the committee was satisfied that KPMG continue to be independent, and free from any conflicting interest with the group.

Governance

External auditor reappointment

We last undertook a formal tender process for statutory audit services in 2011. KPMG commenced their appointment as auditor and presented their first report to shareholders for the year ended 31 March 2012. The lead audit partner must change every five years. Bill Meredith, who has considerable audit experience of other FTSE 100 utility companies, is in his third year in the role. The 2018/19 year-end audit has been KPMG's eighth consecutive year in office as statutory auditor. As previously reported, the most recent audit tender review was undertaken in September 2015, when it was concluded that the committee would next undertake a competitive tender for statutory audit services for the year ended 31 March 2022, most probably during 2020. This was felt to be an appropriate point in the regulatory cycle, due to the benefits of having an experienced audit team in place in the run-up to the 2019 price determination for the regulatory period commencing on 1 April 2020. United Utilities has complied fully with the provisions of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 for the year ended 31 March 2019.

As a result, the committee recommended to the board that KPMG be proposed for reappointment at the forthcoming AGM in July 2019. There are no contractual obligations that restrict the committee's choice of external auditor; the recommendation is free from third-party influence and no auditor liability agreement has been entered into.

Significant issues considered by the committee in relation to the financial statements and how these were addressed

In relation to the group's financial statements, the committee reviewed the following principal areas of judgement (as noted in the accounting policies where applicable):

Capitalisation of fixed assets

Fixed assets (see page 178) represent a subjective area, particularly in relation to costs permitted for capitalisation and depreciation policy.

- In considering the work performed by KPMG during the year in this area, the committee assessed the reasonableness of the group's capitalisation policy and the basis on which expenditure is determined to relate to the enhancement or maintenance of assets. These were both deemed to be appropriate; and
- The committee also reviewed the recovery of the capital overhead rate which management has applied during the year and which the committee had approved in the year ended 31 March 2015 for the five year regulatory period ending 31 March 2020. The committee concluded that the rate still remained appropriate.

Revenue recognition and allowance for doubtful receivables

Due to the nature of the group's business, the extent to which revenue is recognised and doubtful customer debts are provided against is an area of considerable judgement and estimation.

- The committee reviewed the current levels of doubtful debt and credit note provisioning (see page 181 for more detail). The committee challenged management over the appropriateness of the overall levels of provisioning following these reviews and were satisfied that the resulting net debtor balance was appropriate.

Retirement benefits

The group's defined benefit retirement schemes are an area of considerable judgement, the performance and position of which is sensitive to the assumptions made. In addition, during the current year the impact of the equalisation of Guaranteed Minimum Pension (GMP) payments between males and females was reflected in the financial statements as a significant one-off past service cost recognised in the income statement.

- The committee sought from management an understanding as to the factors which led to the increase in the IAS 19 net retirement benefit surplus during the period and noted that the scheme specific funding basis had not been impacted by this volatility. Management presented an explanatory note (see pages 197 to 201) in order to communicate most effectively what is a complex area for the benefit of the group's stakeholders. The committee was satisfied with the explanations provided by management and following a review of the explanatory note approved its inclusion in the financial statements;
- The committee reviewed the methodology and assumptions used in calculating the defined benefit scheme surplus (see page 197 for more details). The group employs the services of an external actuary to perform these calculations and determine the appropriate assumptions to make. KPMG presented a report showing how the assumptions applied compared to their client base. After considering the above, the committee concluded that the approach taken and assumptions made – including changes to the basis on which mortality assumptions are set – were appropriate and fairly balanced in determining the net retirement benefit surplus; and
- The committee also reviewed the methodology used in calculating the impact of GMP equalisation reflected in the financial statements, which was performed by the group's external actuary. Having considered this together with the audit work KPMG performed in relation to this significant past service cost, the committee concluded that the approach taken was appropriate and in accordance with the relevant legal requirements.

Provisions and contingencies

The group makes provisions for contractual and legal claims which, by their nature, are subjective and require management to arrive at a best estimate as to the probable outcomes and costs associated with each individual case.

- The committee received regular updates on new and existing claims being made against the group and the extent to which these have been provided for (see page 184 for details). The committee focused their attention on the more significant items and discussed the judgements made by management in arriving at appropriate provisions in relation to these matters.
- Having assessed management's provisioning methodology and rationale, and having challenged the views taken by management where necessary, the committee concluded that the provisions management had made were appropriate. The committee reached this conclusion based on the facts behind each provision, taking account of any relevant legal advice that may have been received as well as the past experience of management in making such provisions and assurance provided by KPMG who cover these as part of their audit.

Carrying value of loans to and investments in the Water Plus joint venture

The group has interests relating to its Water Plus joint ventures in the form of investments (see page 179) and loans receivable (see page 202), the recoverability of which are considered with reference to the estimated future cash flows of the joint ventures. Management tests whether any impairment exists in relation to the equity investments and loans receivable if adverse changes in conditions associated with the joint venture suggest that this is appropriate. The committee scrutinised the impairment assessments performed by the management of Water Plus which the group considers when making its own assessment (see page 179). This involved reviewing the valuations that underpin the carrying values of these amounts and challenging the methodology and assumptions used. In reviewing these assumptions the committee met with the Water Plus executive team in order to understand the business plan underpinning the Water Plus valuation and consider whether it was appropriate for management to base its impairment assessment on this. Following robust discussion on this issue, the committee confirmed that it was satisfied that the carrying values of these interests at the reporting date were recoverable.

Derivative financial instruments

The group has a significant value of swap instruments, the valuation of which is based upon models which require certain judgements and assumptions to be made (see page 196). Management performs periodic checks to ensure that the model-derived valuations agree back to third-party valuations and KPMG check a sample against their own valuation models. It was confirmed to the committee that such testing had been undertaken during the year and there were no significant issues identified.

Taxation

The committee considered the tax risks that the group faces and the key judgements made by management underpinning the provisions for potential tax liabilities and deferred tax assets. In addition, the committee took account of KPMG's assessment of these provisions. Based upon the above, the committee was satisfied with the judgements made by management.

Underlying profit adjustment

During the year the committee considered and challenged management's treatment of items as adjustments to underlying profit measures and satisfied itself that those items being reported as adjustments met the requirements of the group's policy (see pages 66 to 67). In doing this the committee specifically scrutinised and satisfied itself over the appropriateness of management's decision to include costs associated with the dry weather event experienced during the year as an adjusting item when calculating underlying profit measures.

Going concern and long-term viability

The committee challenged and scrutinised management's detailed assessment of the group's long-term viability and its ability to continue as a going concern. In doing this the committee took into account the risks facing the business, including those associated with the possibility that the UK could leave the European Union without a Brexit deal, and its ability to withstand a number of severe but reasonable scenarios. Having considered management's assessment the committee approved the Long-term viability statement set out on page 101, including the increase in the period over which the assessment is given from five years to seven years and recommended it to the board for approval.

In reading the above significant issues considered by the committee, shareholders might also wish to examine the auditor's report and their assessment of risks of material misstatement on pages 156 to 159.

Read more about **Our business model** on pages 24 to 26

Read more about the **Principal risks and uncertainties** on pages 68 to 75

Read more online at **unitedutilities.com/corporate/about-us/our-future-plans/**

The main features of the group's internal controls and risk management systems are summarised below:

Internal audit function

The internal audit function is a key element of the group's corporate governance framework. Its role is to provide independent and objective assurance, advice and insight on governance, risk management and internal control to the audit committee, the board and to senior management. It supports the organisation's vision and objectives by evaluating and assessing the effectiveness of risk management systems, business policies and processes, systems and key internal controls. In addition to reviewing the effectiveness of these areas and reporting on aspects of the group's compliance with them, internal audit makes recommendations to address any key issues and improve processes and, as such, provides an indication of the behaviours being exhibited by employees in the areas under review. Once any recommendations are agreed with management, the internal audit monitors their implementation and reports to the committee on progress made at every meeting.

A five-year strategic audit planning approach is applied. This facilitates an efficient deployment of internal audit resource in providing assurance coverage over time across the whole business, as well as greater variation in the nature, depth and breadth of audit activities. This strategic approach supports the annual audit plan, which is then endorsed by management, and which the committee also approves. The plan focuses the team's work on those areas of greatest risk to the business. Building on the strategic planning approach, the development of the plan considers risk assessments, issues raised by management, areas of business and regulatory change, prior audit findings and the cyclical review programme. The purpose, scope and authority of internal audit is defined within its charter which is approved annually by the audit committee.

Corporate governance report
Audit committee

The in-house team is expanded as and when required with additional resource and skills sourced from external providers – primarily PwC at present. The committee keeps the relationship with PwC under review to ensure the independence of the internal audit function is maintained and there is a documented process to manage possible conflicts of interest with the co-sourced resource. Ensuring that PwC remain independent in the course of its work is crucial to the integrity of its work.

The internal audit function also liaises with the statutory auditor, discussing relevant aspects of their respective activities which ultimately supports the assurance provided to the audit committee and board. During the year, the committee reviewed the current operating model, in particular the balance of in-house versus co-sourced resource, and concluded that, while minor improvements were identified, the current approach was satisfactory.

Assessing the effectiveness of the internal audit function

The effectiveness of the internal audit function's work is continually monitored using a variety of inputs including the ongoing audit reports received, the audit committee's interaction with the head of audit and risk, an annual review of the department's internal quality assurance report, a quarterly summary dashboard providing a snapshot of the progress against the internal audit plan tabled at each committee meeting as well as any other periodic quality reporting requested.

An annual stakeholder survey in the form of a feedback questionnaire is circulated to committee members, senior management and other managers who have regular contact with the internal audit function, including representatives from the external auditor KPMG and the co-source audit provider PwC. The responses were anonymous to encourage open and honest feedback, and were consistently favourable, as were previous surveys.

Periodically, the quality and effectiveness of the internal audit function is also assessed externally, with the most recent review being undertaken early 2019. Taking all these elements into account, the committee concluded that the internal audit function was an effective provider of assurance over the organisation's risks and controls and appropriate resources were available as required.

Internal audit, led by the head of audit and risk, covers the group's principal activities and reports to the committee and functionally to the CFO. The head of audit and risk attends all scheduled meetings of the audit committee, and has the opportunity to raise any matters with the members of the committee at these meetings without the presence of management. He is also in regular contact with the chair of the committee outside of the committee meetings.

Risk management systems

The committee receives updates and reports from the head of audit and risk on key activities relating to the company's risk management systems and processes at every meeting. These are then reported to the board, as appropriate. The group designs its risk management activities in order to manage rather than eliminate the risk of failure to achieve its strategic objectives.

The CFO has executive responsibility for risk management and is supported in this role by the head of audit and risk and the corporate risk manager and his team. The group audit and risk board (GARB) is a sub-committee of the executive team. The GARB meets quarterly and reviews the governance processes and the effectiveness and performance of these processes along with the identification of emerging trends and themes within and across the business. The work of the GARB then feeds into the information and assurance processes of the audit committee and into the board's assessment of risk exposures and the strategies to manage these risks.

Supplementing the more detailed ongoing risk management activities within each business area, the biannual business unit risk assessment process (BURA) seeks to identify how well risk management is embedded across the different teams in the business. The BURA involves a high level review of the effectiveness of the controls that each business unit has in place to mitigate risks relating to activities in their business area, while also identifying new and emerging risks and generally to facilitate improvements in the way risks are managed. The outcome of the BURA process is communicated to the executive team and the board. This then forms the basis of the determination of the most significant risks that the company faces which are then reviewed by the board. The group utilises risk management software to underpin the company's risk management process. The maturity of the risk management framework and its application across the business is assessed on an annual basis against a defined maturity model. This assessment provides an objective appraisal of the degree of maturity in how the risk management system is being applied and the quality of each risk in terms of quantification and management. The results of the maturity assessment are reported to the GARB, and actions agreed with business units.

An external assessment of the risk management process last took place in 2015/16.

Internal controls

The committee reviews the group's internal control systems and receives updates on the findings of internal audit's investigations at every meeting, prior to reporting any significant matters to the board. Internal control systems are part of our 'business as usual' activities and are documented in the company's internal control manual which covers financial, operational and compliance controls and processes. Internal control systems are the responsibility of the CFO, with the support of the GARB, the financial control team and the internal audit team, although the head of audit and risk and his team are directly accountable to the audit committee.

Confirmation that the controls and processes are being adhered to throughout the business is the responsibility of managers, but is continually tested by the work of the internal audit team as part of its annual plan of work which the committee approves each year as well as aspects being tested by other internal assurance providers. Compliance with the internal control system is monitored annually by the completion of a self-assessment checklist by senior managers in consultation with their teams. The results are then reviewed and audited on a sample basis by the internal audit team and reported to the committee.

Whistleblowing, anti-fraud and anti-bribery

For the year ended 31 March 2019 the audit committee was responsible for reviewing the group's arrangements for individuals to raise concerns and the arrangements for investigation of such matters; and for the company's procedures for detecting fraud; and the systems and controls for preventing other inappropriate behaviour. The group's whistleblowing policy supports the culture within the group where genuine concerns may be reported and investigated without reprisals for whistleblowers. From 1 April 2019, the committee no longer has the responsibility for overseeing the group's whistleblowing arrangements, and the board has assumed this responsibility, reflecting the 2018 Code.

The company operates an independently provided confidential reporting telephone helpline and web portal for employees to raise matters of concern in relation to fraud, dishonesty, corruption, theft, security and bribery. Furthermore, employees are encouraged to raise any matters relating to health and safety and any activities of the business which have caused or may cause damage to the environment, such as pollution or other contamination. Alternatively, any matters of concern can also be raised with their manager, their human resources business partner or another senior manager. Employees can remain anonymous if they wish. All concerns are investigated fully, whether they are raised with a manager, or via the confidential helpline/web portal.

In the first instance of an incident being reported, a summary of the allegations is passed to the fraud and whistleblowing committee (consisting of the company secretary, customer services and people director, commercial director and head of internal audit and risk) to decide on the appropriate course of action and investigation and by whom.

During the year, the audit committee was kept fully appraised in regular updates on the progress and findings of investigations of cases of whistleblowing and alleged fraud and any remedial actions taken. A number of employees have been selected and received specialist training in order to conduct investigations of cases of whistleblowing and alleged fraud.

The company has an anti-bribery policy to prevent bribery being committed on its behalf, which all employees must follow, and processes in place to monitor compliance with the policy. As part of the anti-bribery programme, employees are also required to comply with the group's hospitality policy. The hospitality policy permits employees to accept proportionate and reasonable hospitality for legitimate business purposes only. Our employees and representatives of our suppliers must also comply with the group's sustainable supply chain charter which explains that we will not tolerate corruption, bribery and anti-competitive actions and we expect our suppliers to comply with applicable laws and regulations, and in particular never to offer or accept any undue payment or other consideration, directly or indirectly, for the purposes of inducing any person or entity to act contrary to their prescribed duties.

As part of the internal control self-assessment checklist (part of the group's internal control processes), senior managers in consultation with their teams are required to confirm, among other things, that they have complied with the group's anti-bribery and hospitality policies. The anti-bribery programme is monitored and reviewed biannually by the committee.

The anti-bribery policy is available on the company's website at **unitedutilities.com/corporate/about-us/governance**

The sustainable supply chain charter is available at **unitedutilities.com/corporate/responsibility/stakeholders/suppliers**

Corporate governance report
Corporate responsibility committee

The company's long-standing commitment to corporate responsibility has provided a solid foundation upon which to evolve existing programmes, or develop new initiatives, in response to the growing complexity of managing responsible business issues.

Pictured: Steve Mogford, Stephen Carter and Alison Goligher

Quick facts

- The committee comprises three directors appointed by the board, two of whom are independent non-executive directors
- The company secretary, corporate affairs director and customer services and people director attend all meetings of the committee
- Senior operational directors attend the committee to report on the environmental and social impact of particular topics and initiatives
- The corporate responsibility committee has existed for over eleven years
- Terms of reference – **unitedutilities.com/corporate-governance**

Quick links

Terms of reference – **unitedutilities.com/corporate-governance**

Corporate responsibility committee members

- Stephen Carter (chair)
- Alison Goligher
- Steve Mogford

Dear Shareholder

I am pleased to report on the work of the corporate responsibility committee in 2018/19.

The company's long-standing commitment to corporate responsibility has provided a solid foundation upon which to evolve existing programmes, or develop new initiatives, in response to the growing complexity of managing responsible business issues. In recognition of the company's comprehensive corporate responsibility agenda, the committee increased the frequency of its meetings to four times a year. This has provided it with the extra time it needs to consider the company's effectiveness in delivering its responsible business commitments in a rapidly changing external environment and how it is continuing to build legitimacy among the opinions of customers, regulators, government and other stakeholders.

Twelve months ago, the committee agreed to a comprehensive forward agenda of topics covering environmental, social and governance matters. I am pleased to report on a year where the committee discussed over 50 papers covering these topics, including papers specific to its own governance. To prioritise topics for discussion, members agreed to categorise items into those with a mandatory driver, those with regulatory interest, stimulus from items of best practice and committee governance topics.

In a year when water companies submitted their business plans for the 2020–2025 regulatory period to Ofwat, the committee reviewed those plans from a responsible business perspective. It concluded that the company's approach put much emphasis on communities, the environment and the importance of working in partnership, especially around catchment management. The committee welcomed the company's plans on affordability and vulnerability support, encouraging it to do more to promote the good work it is already doing and the benefits this brings to the communities it serves.

There has been considerable external interest in the water sector from a variety of stakeholders and at each meeting the committee has discussed the interaction between corporate responsibility, communications and reputation. As well as reviewing key reputational matters, the committee has considered the current debate on nationalisation and reversing the privatisations of several sectors, including water. In addition, it explored how the company is acting in the best interests of customers and particularly welcomed efforts to connect with customers in a different way, such as the #NWMatters campaign with the message 'if it matters to you, it matters to us'.

The committee blended items specific to the moment, most notably the implications of Brexit on environmental and employment legislation and the company's approach to one of the most pressing environmental issues, plastic, with those items with a longer term dimension, such as gender pay reporting and natural capital. Several papers addressed the emerging topic of valuation, exploring how wider benefits, such as those generated by the services provided by nature, might be woven into decision-making.

The committee also returned to issues of continued significance to North West England, most notably the support given to customers on lower incomes given the ongoing social and economic challenges in the region. In addition to the regular review of the dashboard tracking actions to support customers in vulnerable circumstances, the committee was pleased to see that a further affordability summit was convened. This second event brought together the region's affordability stakeholders to launch the UK's first affordability hub, to report on progress and to identify new initiatives where groups can work collaboratively.

It has been pleasing to see the progress made in building relationships with the metropolitan mayors in the North West, especially in Greater Manchester. Senior managers are engaged at several levels, including a recently established infrastructure group, holding the vice-chair of the natural capital group and in securing support for the Manchester-Pennine resilience scheme.

Governance remained topical and the committee discussed the company's response to the 2018 UK Corporate Governance Code's recommendation on workforce engagement. The committee looks forward to the regular updates it will receive on progress and greater visibility of the work of the company's employee networks.

The committee discussed the company's second gender pay report and its approach to diversity and inclusion. It acknowledged that there will be short-term fluctuations in the statistics and that, ultimately, success will only be evidenced by a sustained downward trend over time. The committee welcomed progress on the company's action plan, such as the introduction of a mentoring scheme to support more female talent on succession plans for senior leader positions, and the increasing percentage of female apprentices, standing at 23 per cent compared to a national average of between five per cent and seven per cent.

The committee reviewed the company's responsible business scorecard, used to track progress against company objectives to provide the best service to customers, at the lowest sustainable cost, in a responsible manner. We were delighted to retain world class status in the Dow Jones Sustainability index for the 11th consecutive year and 77 per cent of the stretching targets tracked by the committee to measure the company's corporate responsibility performance were achieved.

As a listed company, United Utilities complied with the 2016 UK Corporate Governance Code and continues to drive for the highest standards of board leadership, transparency and governance.

Stephen Carter
Chair of the Corporate Responsibility Committee

Main responsibilities of the committee

The board approved an updated set of terms of reference for the committee in May 2019. Minor amendments were made to take into account the 2018 UK Corporate Governance Code and the evolution of corporate reporting with greater emphasis on integrated reporting.

The main duties are to:

› consider and recommend to the board the broad approach to corporate responsibility taking into account the company's desired corporate responsibility positioning;
› keep under review the group's approach to corporate responsibility and ensure it is aligned with the group strategy;
› review corporate responsibility issues and objectives material to the group's stakeholders and identify and monitor the extent to which they are reflected in group strategies, plans and policies;
› monitor and review the status of the company's reputation and examine the contribution the group's corporate responsibility activities make towards protecting and enhancing this;
› monitor and review compliance with the board's approach to corporate responsibility and scrutinise the effectiveness of the delivery of the policy requirements;
› develop and recommend to the board corporate responsibility targets and key performance indicators and receive and review reports on progress towards the achievement of such targets and indicators;
› monitor and review the steps taken by the company to support customers in vulnerable circumstances; and
› review all approved specific giving where the aggregate financial contribution exceeds £100,000 over the period of the proposed funding and to review all community giving expenditure annually.

Corporate governance report
Corporate responsibility committee

The committee's agenda during the year:

Environmental
Climate change mitigation
With the current carbon strategy coming to an end in 2020, the committee was updated on proposed priorities up to 2025. This included the company's intention to set a new science-based emissions target and to evolve its reporting in line with expectations to achieve net zero emissions. In addition, the strategy will include continued focus on delivering solutions to reduce operational carbon emissions, enhancing climate-related disclosure and, as a last resort, purchasing green credits to achieve emissions targets. It was particularly impressed with work to develop an organisational capability matrix for carbon, which incorporates components from existing frameworks such as HM Treasury Infrastructure Carbon Review and the Taskforce for Climate-related Financial Disclosure recommendations. The updated carbon strategy, objectives and targets will be finalised later in 2019.

Climate change adaptation
The committee welcomed the instigation of an independent review of the company's approach to climate change adaptation whose scope includes a critique of the approach taken to assess the risk for drought, peak demand, sewer flooding and pollution and flooding of assets; a review of other potential approaches to better assess the risk, incorporating the findings of UKCP18; and a recommendation of which method should be adopted for each risk. The findings of this study will feed into the third round climate adaptation report to be submitted to Defra in the autumn of 2020.

Valuing natural capital
Some of the steps necessary to adapt to climate change were covered as part of discussions examining how to better value the services provided by nature. The committee was presented with an overview of how the company is developing a strategic plan to implement a natural capital approach. This takes into account the identification of specific organisational barriers and challenges in implementing a natural capital approach, such as explaining the relevance of natural capital; an action plan to address these challenges, including how natural capital is measured and adopted through policies and projects, such as the company's approach to catchment management; and the identification of external factors and changes.

Approach to plastics
The committee reviewed the steps being taken by the company to tackle this high profile issue. It heard how a multi-functional 'task and finish' group has been established to assess the company's touchpoints with plastic, creating a 'water-cycle map' of potential impacts. The committee supported the review of the existing evidence base and the company's research project with the University of Manchester to understand how plastics interact with the wastewater treatment process. It was explained that single use plastic had been removed from the company's catering outlets and that dialogue was under way with suppliers to examine how plastic use could be reduced, in particular for delivery of materials, water sample bottles and bottled water used in emergency response. The company was actively supporting the refill campaign, focusing to begin with in Greater Manchester.

Social
Affordability and vulnerability
The committee covered this topic extensively in 2018/19, reviewing performance against 22 measures used to track progress in assisting lower income groups. It welcomed an update on the second North West affordability summit, where the North West hardship hub was officially launched. Delegates were updated on the company's new payment break scheme where bill payments can be delayed for a set period of time under specific circumstances, such as a temporary drop in income, to help customers avoid falling into debt.

Diversity and inclusion, including gender pay
It was reported to the committee that there had been good progress implementing the company's gender plan, part of its diversity and inclusion action plan. The committee shared the company's ambition to increase diversity of thought and to build a diverse workforce representative of all the communities served. In its review of the company's second gender pay gap report, the committee commented that the report would benefit from a clearer explanation that the gap will close through the successful implementation of the company's diversity and inclusion strategy.

Update on community strategy
The committee was briefed on the company's intention to revisit its community strategy in the context of, among other issues, what the 25-year natural environment plan means for access and recreation; the impact of the PR19 business plan and its emphasis on building a positive connection with the communities of the North West; and that opportunities exist to enhance reputation through more targeted and effective engagement on current activities.

Early careers and developing young people
The committee was updated on the positive impact of current initiatives such as the graduate and apprentice programmes, youth employment programme and focus on STEM subjects. Because of the demands, skills and diversity gaps of the company, coupled with the expectations from a future workforce, the company's review had prompted several new initiatives including degree apprentices, a partnership with Teach First to gain access to talented young people from diverse communities across the region and the launch of an engineering master class with high schools in Warrington.

Governance

Corporate governance

- **Corporate Governance Code** – In response to the introduction of a new requirement on how companies should engage with their workforces, the committee discussed a number of options. It agreed that existing communication channels, such as the annual employee opinion survey, the network of over 200 employee engagement champions and 80 health, safety and well-being champions, and the 920 employees involved in inclusion networks that provide peer-to-peer support for different employee communities, should be at the heart of the approach. The committee recommended to the board that a non-executive director act as the designated lead for workforce engagement and establish an employee voice panel, supported by subgroups built from existing employee networks and forums.
- **Committee evaluation** – In its annual evaluation, the committee requested that it be presented with a paper examining trends from other companies and non-governmental organisations and to calibrate this against the company's current approach. This will be discussed later in 2019.
- **Reporting** – The committee was updated on plans to include a stakeholder materiality matrix in the 2019 Annual Report and noted the company's proposal to adopt the International Integrated Reporting Council's definition of materiality where "A matter is material if it could substantively affect the organisation's ability to create value in the short, medium or long term". Read more on page 45.

Reputation and engagement

- **Reputation** – This topic remained a standing agenda item for committee, allowing it time to examine the relationship between responsible business topics and reputation. An assessment of the company's key reputational risks also remained a standing item.
- **Engagement** – The committee discussed several papers on the company's approach to stakeholder engagement, including an analysis of levels of trust following the summer's dry weather and stakeholder reaction to the PR19 business plan.
- **Measuring and reporting CR performance** – The committee reviewed the company's 2017/18 corporate responsibility scorecard with 77 per cent of targets achieved. It noted that some measures were likely to remain 'red' – a predicted shortfall in the sewer flooding index and the challenging target for the water quality service index – and the amber status given for the number of volunteering hours due to fewer volunteering opportunities and the switch towards the use of agencies at customer roadshows.

Cross cutting

Brexit and regulatory convergence – environmental and employment legislation

The committee was provided with an assessment of the likely effects of Brexit on environmental and water regulation and employment legislation. It focused its discussions on waste management and agriculture, noting that company opinions were being heard in the appropriate forums and that it would be important to continue engagement with Defra. A limited number of employment issues caused by Brexit were being addressed and implications for the supply chain would be kept under review, particularly in terms of labour availability post Brexit.

Social media policy

A paper was presented to the committee describing how the social media landscape is ever changing with impacts on consumer behaviour and opinion as well as the way brands interact with customers. It discussed how the company is making use of social media and how it governs social media with employees. The committee supported a number of next steps including the proposed review of the company's social media policy and strategy.

Implementing a value framework

The committee discussed natural capital and social value approaches which seek to place a value on what a company does beyond traditional economic parameters. Demonstrating this can provide proof that a company is delivering on its 'purpose'. It supported the proposed approach for the company to articulate more comprehensively the value it brings to the communities it serves, to place a monetary value on existing and new measures and to seek to incorporate value into decision-making processes and tools.

Looking to the next year, the committee will:

- in the context of discussing and agreeing the company's corporate responsibility commitments for the period 2020 to 2025, take stock of the company's corporate responsibility journey so far, its current status and its ambition;
- consider new and emerging issues which, in some cases, will be discussed by the committee for the first time, such as digital and responsible business, air quality, sustainable drainage, access and recreation and green finance;
- return to issues previously discussed to examine progress such as the company's efforts to support customers on low incomes, what Brexit means for environmental and employment legislation, human rights, sustainable supply chain, plastics, talent and young people, progress on carbon strategy, community strategy and diversity and inclusion;
- discuss progress on high profile initiatives such as employee voice and gender pay;
- continue its focus on the interaction between corporate responsibility, communications and reputation, including brand; and
- consider matters of governance such as the committee's terms of reference.

Corporate governance report
Annual statement from the remuneration committee chair

Our executive remuneration arrangements align to the business plan for the new regulatory period, incentivising high standards of delivery for customers and the creation of long-term value for all of our stakeholders.

Pictured: Alison Goligher, Mark Clare, Brian May, Sara Weller (seated)

Quick facts

- The Code requires that "the board should establish a remuneration committee of at least three independent non-executive directors";
- The role of the committee is to set remuneration terms for all executive directors, other senior executives and the Chairman; and
- By invitation of the committee, meetings are also attended by the Chairman, the CEO, the company secretary, the customer services and people director, the head of reward and pensions and the external adviser to the committee.

Quick links

Terms of reference – unitedutilities.com/corporate-governance

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Read more about the Review of the directors' remuneration policy on pages 118 to 120

Read more about the At a glance summary: executive directors' remuneration on pages 121 to 123

Read more about the Directors' remuneration policy on pages 124 to 130

Read more about the Annual report on remuneration on pages 131 to 142

Remuneration committee members

Sara Weller (chair)
Alison Goligher
Mark Clare
Brian May

Code principle – Remuneration

Introduction by Dr John McAdam

"Our remuneration policy has been designed to promote the long-term success of the company, with a significant proportion of senior executives' pay being performance-related."

Dear Shareholder

After what has been a particularly busy year for the remuneration committee, I am pleased to introduce the directors' remuneration report for the year ended 31 March 2019. This includes my statement, an 'at a glance' summary, a revised directors' remuneration policy which is intended to take effect from the date of our 2019 AGM (subject to shareholder approval) and the annual report on remuneration for the year ended 31 March 2019.

Remuneration policy review

Although the current directors' remuneration policy was approved by shareholders in 2017 and was intended to run until the 2020 AGM, during the summer of 2018 the committee decided to accelerate its review of the executives' remuneration arrangements (and the incentive elements in particular) to make sure that they would be well aligned with the proposed business plan for the new regulatory period from 2020–25 and the expectations of investors and Ofwat. It was also important for the committee to consider how various aspects of good governance which stem from the latest UK Corporate Governance Code and investors' guidance on pay might be embraced.

Between December 2018 and April 2019 we consulted directly with major shareholders and other key stakeholders about our proposals. That process was valuable, and allowed the committee to thoroughly consider views on a range of areas.

Following the company's business plan being accorded fast-track status by Ofwat in January 2019 in its initial assessment, our draft determination was published in April. Together with positive feedback from stakeholders this led the committee to finalise its policy review earlier than required. This enables us to propose a new directors' remuneration policy at the 2019 AGM, ready for the start of the new regulatory period in April 2020, which fully supports the business plan goals, aligns the interests of the executive directors with those of shareholders, and responds to the regulator's desire for even greater engagement to link remuneration with delivery of outcomes that are important to customers, whilst recognising ever-evolving standards of corporate governance.

Further information about the policy review, along with full details of the proposed policy, are shown on pages 118 to 120 and pages 124 to 130.

Implementation of the current directors' remuneration policy during 2018/19

Salary

The committee believes that executive directors' salaries remain appropriately positioned relative to the market. While our policy is that executive directors will normally receive a salary increase broadly in line with the increase awarded to the general workforce, Steve Mogford, Russ Houlden and Steve Fraser each received a base salary increase of two per cent with effect from 1 September 2018, whereas the headline increase applied across the wider workforce was higher, at three per cent. Salaries will next be reviewed in September 2019.

Annual bonus

Employees throughout the company participate in the annual bonus scheme, alongside the executive directors, to ensure shared focus on the business plan at all levels. The current bonus measures reflect the importance of the targets set by our regulators for the period 2015–20.

Despite the challenges presented by the extreme dry weather conditions during the year we have seen another very good year of customer service, operational and financial performance in 2018/19.

New approaches introduced in recent years that improve the speed and quality of our delivery, alongside a focus on helping customers communicate easily with us in ways that best suit their lifestyles, have seen us continue to set ever higher standards of customer service. The Priority Services programme and our efforts to ensure that customers in difficult financial circumstances are supported are recognised by many, including Ofwat, as being market-leading. Achieving our best ever score against Ofwat's qualitative service incentive mechanism demonstrates the continued success of our approach to customer service and it is satisfying that having started the regulatory period with performance levels in the lower quartile and potentially facing financial penalties, we are now in a position where we anticipate being eligible for a regulatory reward.

We also achieved our best ever annual performance against the outcome delivery incentives (ODIs), reflecting good all-round operational performance. Overall, performance was good against our wastewater measures and significantly improved against our water measures with a net reward achieved in both areas. ODI performance across the whole regulatory period remains ahead of the business plan.

Underlying operating profit was better than in 2018/19 and the efficient and effective delivery of the capital programme is reflected in our Time, Cost and Quality index (TCQi) score which remains high at 95.4 per cent.

When considering the personal contributions of the executive directors, amongst other achievements during the year, Ofwat's fast-track rating of our business plan and commendation of our high quality and industry leading approach in many areas is testament to their performance, and to their leadership of the wider team.

Overall company results, together with the strong personal performance of the executive directors, has resulted in annual bonus out-turn of around 79 per cent of maximum (compared to the 2017/18 outcome of around 75 per cent of maximum) and a company-wide bonus pool totalling £17 million (compared to £16 million in the prior year). Half of the annual bonuses earned by the executive directors will be deferred into shares for a period of three years.

Long-term incentives

The final outcome of the Long Term Plan awards, which were granted in 2016 and whose performance is measured over the three years to 31 March 2019, is expected to be confirmed as 60 per cent later in the summer of 2019. Again, this reflects the continued delivery of high standards of customer service set in recent years, and the achievement of the stretch level of sustainable dividend performance. Ongoing uncertainty about the water sector continues to affect the share price, and the threshold target set for relative total shareholder return over the period was not achieved so there will be zero pay-out in relation to that measure. The awards for the executive directors will actually vest only after the completion of a further two-year holding period, during which the shares will remain subject to withholding provisions. This approach aligns the interests of the executive directors with those of shareholders and customers.

Agenda for 2019/20

While it is clearly important for the executives and wider workforce to remain focused on the delivery of the current plan in the final year of the regulatory period, it is also important to look towards the new regulatory period and make transitional steps where appropriate.

The annual bonus plan will therefore operate in a similar way to 2018/19, except the measures based on Ofwat's service incentive mechanism will be replaced by measures based on Ofwat's new C-MeX approach. Details are shown on page 134.

The 2019 LTP awards will also be based on a similar structure to that used in recent years, although the committee is considering whether it might begin to reflect the performance measures included in the proposed directors' remuneration policy in the construct of the 2019 LTP awards, and major shareholders will be consulted on the proposed approach before the awards are made. The committee will continue to focus on setting stretching targets that drive excellent customer service, operational and financial performance and enhance long-term shareholder value.

Later in the year the annual bonus measures and targets for the new regulatory period will be agreed, to ensure that, alongside the proposed LTP structure, all incentives continue to support the business strategy and provide appropriately stretching goals.

The committee will also continue to review how the developing corporate governance and remuneration environment, in particular the changes to the UK Corporate Governance Code, might be reflected in the way the committee operates.

I hope we will receive your support for the resolutions relating to remuneration at the forthcoming AGM.

Sara Weller
Chair of the remuneration committee

Corporate governance report
Review of the directors’ remuneration policy

Around seven million people in the North West of England rely on United Utilities to provide reliable and affordable year-round water supplies to their homes, businesses and recreational spaces.

Over the five-year regulatory period from 2020-25, our business plan commits us to delivering affordable bills and excellent service to customers, alongside a programme of careful investment to sustain the region’s water quality, reduce leakage and ensure reliability of water supply. At the same time the company must lay foundations for longer-term resilience and the provision of water in an environmentally sensitive and sustainable way.

When setting the remuneration arrangements for executive directors, the committee has always adopted a prudent and responsible approach, which aligns to company strategy.

This continues under the proposed remuneration policy, where the potential maximum quantum of reward available is unchanged, for both the annual bonus (which operates at all levels throughout the company) and for the Long Term Plan (LTP). The proposed policy also ensures that incentives for the executive directors are related to the delivery of key business plan goals for customers, and returns for shareholders, and operates over four and five year periods respectively when bonus deferral and LTP holding periods are taken into account.

The proposed changes to our current policy mainly affect the way we structure the LTP element of the executive directors’ remuneration package. New measures are proposed, to assess performance in a way that reflects the financial and service priorities of shareholders, regulators and customers, while recognising the importance of both long-term sustainability and dividend certainty.

Further details of the two equally weighted measures proposed for the LTP are described in more detail on page 127.

Some other small changes to the policy are also proposed to reflect recent shareholder guidance, notably in the commitment to align pension contributions for new executive director appointments with those that apply to the wider workforce.

The proposed policy has been developed taking careful account of shareholder views that were sought during a comprehensive consultation exercise between December 2018 and April 2019, involving major shareholders and other key stakeholders. A summary of the key elements of the review and its outcome are shown on pages 119 to 120, with full details of the proposed policy provided on pages 124 to 130.

If approved by shareholders the new policy will take effect from the July 2019 AGM, so it will be in place ready to support both the annual bonus and Long Term Plan at the start of the new regulatory period in spring 2020.

Pictured: Liverpool waterfront

Element of policy	Focus of/rationale for review	Position following consultation
Long Term Plan – introduction of Return on Regulated Equity (RoRE) as a performance measure	The committee proposes to replace Relative Total Shareholder Return as the financial LTP measure with RoRE. RoRE is the return that the company is expected to earn relative to the equity portion of its Regulatory Capital Value. The committee considers RoRE to be a better incentive measure than relative TSR because it: more effectively incentivises management in that they have strong line of sight to the outcome; allows stretching but achievable targets to be set, including across regulatory periods; captures financial, operational and customer performance; is aligned to shareholder value creation, without the volatility of share price; and is recognised as a relevant measure for the sector, evaluated by the analyst community. Additionally, RoRE is used by Ofwat to assess each water and wastewater company's performance and is published annually as part of each company's Annual Performance Report, so it is comparable across companies.	Shareholders were supportive of the use of RoRE instead of TSR as a performance measure in the LTP. RoRE will therefore be used as a performance measure in the LTP, with a weighting of 50 per cent. See page 127 for further details.
Long Term Plan – introduction of a 'customer basket' of performance measures	Ofwat has made it clear that during the next regulatory period, financial rewards and penalties available to companies should be directly linked to customer service delivery. The committee believes it is therefore appropriate for a substantial part of the executive directors' long-term incentive to be based on the performance of a number of customer service measures. This 'customer basket' will include measures which demonstrate the long-term health of our assets and services and ensure the long-term resilience of our water networks.	Shareholders understood the rationale for ensuring that Ofwat's focus on customer service delivery was reflected in executive incentives. A customer basket of measures will therefore be used as a performance measure in the LTP, with a weighting of 50 per cent. The basket of customer measures will include both service measures and resilience measures, so will capture delivery of performance for customers across a broad range of criteria. For the service measures, we will use the new C-MeX and D-MeX metrics being introduced by Ofwat as replacements for SIM. Using our online research panel of nearly 8,000 customers, we will also ask customers to prioritise outcomes that they think we should focus on (e.g. reducing leakage). For the resilience measures, we will focus on metrics that capture the long-term health and serviceability of our networks and assets, thereby aligning executive performance pay with building long-term resilience of our water and wastewater services. Customers will benefit from long-term reliability in the quality of their water supplies, and ways of working that protect and improve the environment. See page 127 for further details.
Long Term Plan – use of a dividend delivery underpin	The committee recognises that providing dividend sustainability to shareholders is important and that the current sustainable dividends measure used in the LTP has been effective. However, setting robust targets that can cross into a new regulatory period poses a significant challenge.	The committee's use of dividends under the LTP will be modified in the proposed framework by making delivery of our dividend policy an overall underpin. Vesting under the proposed LTP structure will be dependent on the delivery of the company's declared dividend policy during the respective performance period (alongside the existing underpin of the committee being satisfied that the company's performance on these measures is consistent with underlying business performance).
Balance between annual bonus and LTP quantum	The committee considered whether, in order to be able to set the mix of incentives each year in consideration of relevant developments in the external environment, it would be advantageous to have the flexibility to vary the mix of annual bonus and Long Term Plan awards annually within the respective overall maximum quantums.	Based on shareholder feedback the committee did not progress further with this element and it does not feature in the proposed policy.

Review of the directors' remuneration policy

Element of policy	Focus of/rationale for review	Position following consultation
Alignment of executive pension contributions with those applying to the wider workforce	There have been growing calls from investors and proxy bodies for pension provision for executive directors to be aligned to the wider workforce, and this expectation of pension alignment has now been included in the revised UK Corporate Governance Code (Code).	Shareholders were supportive of the committee's decision to align pension provisions for new executive to those applying to the wider workforce, with the maximum company pension contribution for new executive directors set at 14 per cent of salary, or a cash allowance of 12 per cent of salary (which is of broadly equivalent cost to the company). The current executive directors will receive a cash allowance of 22 per cent of salary and will no longer have the option to take any level of pension contribution instead.
Use of discretion	Shareholders expect that remuneration committees have the authority to exercise discretion diligently and in a manner that is aligned with shareholders' interests.	The committee already has sufficient power to exercise discretion, and in fact has exercised and disclosed the use of such in recent years, by applying downward adjustments to the executive directors' bonus outcomes in 2015/16 and 2017/18. The potential use of discretion is articulated more clearly in the proposed policy.
Recovery and withholding provisions	The committee is aware that the revised Code reminds remuneration committees of the expectation that incentive schemes will include recovery and withholding provisions in certain specified circumstances, and the guidance to the Code lists examples: payments based on erroneous or misleading data, misconduct, misstatement of accounts, serious reputational damage and corporate failure. Our incentive scheme rules already contain recovery and withholding provisions that can be used in cases of misstatement of accounts, error in calculations and gross misconduct. The rules also provide for withholding (but not recovery) to be applied in cases of serious reputational damage, serious failure of risk management, and such other circumstances where the committee determines they should apply.	The current provisions already go beyond what is typical market practice and provide flexibility including, for example, the ability to apply the provisions in the event of corporate failure. Importantly, the committee is satisfied that the provisions are fully enforceable. The potential use of the recovery and withholding provisions is articulated more clearly in the proposed policy.
Post-employment shareholding requirements	The policy review commenced some months ago before the current positions held on this topic by some stakeholders were published. Our current approach to incentives ensures that executive directors would continue to have significant shareholdings for at least two years after departure, because under our current policy they are not entitled to accelerated vesting of their unvested share awards. This means that long-term incentive awards within the two-year holding period do not vest until the end of that holding period; long-term incentive awards still in the performance period vest no sooner than two years after departure; and deferred bonuses do not vest until the end of the deferral period (which could potentially be up to three years after departure) so a former executive director could still have a material value in unvested share awards two or three years after departure.	Having carefully considered this area, including the context of the current political uncertainty impacting our industry, we do not intend to introduce additional post-employment shareholding requirements as part of this policy review. The post-employment vesting provisions that apply currently to the incentive plans already require unvested awards to be held after departure, and ensures they remain subject to robust recovery and withholding provisions. It was clear during the consultation process that some shareholders are keen for such provisions to be introduced, but the committee's rationale for not doing so at the current time was understood. The approach will be considered again in the next policy review, and market practice will be monitored in the meantime.

Corporate governance report
At a glance summary: executive directors' remuneration

Remuneration philosophy

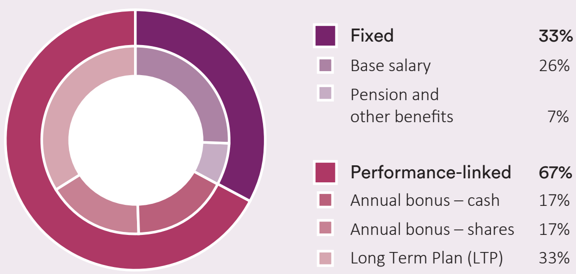
There are three key principles of our approach to executive remuneration.

Align	Incentivise	Create long-term value
to our purpose, vision and strategy	great customer service	for all of our stakeholders

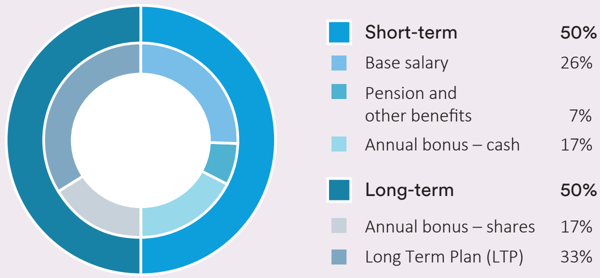
Executive directors' remuneration policy
Elements of executive directors' pay

A significant proportion of executive directors' pay is performance-linked, long-term and remains 'at risk' (i.e. subject to withholding and recovery provisions for a period over which the committee can withhold vesting or recover sums paid):

Fixed vs performance-linked (%)(1)

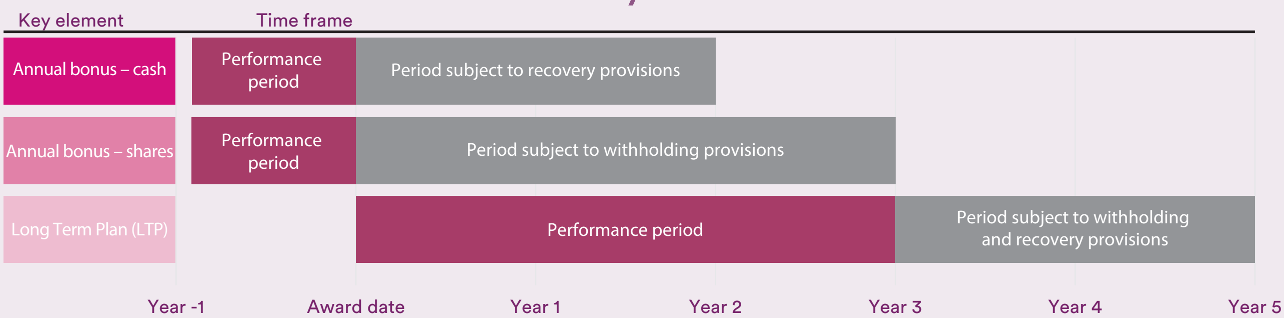


Short-term vs long-term (%)(1)



(1) Based on maximum pay-out scenario for executive directors assuming the normal maximum award level of 130 per cent of salary for the Long Term Plan (LTP).

Pay at risk



Further details on what triggers the withholding and recovery provisions can be found on pages 125 to 126.

Implementation of directors' remuneration policy in 2018/19

The table below summarises the implementation of the directors' remuneration policy for executive directors in 2018/19. For further details see the annual report on remuneration on pages 131 to 142.

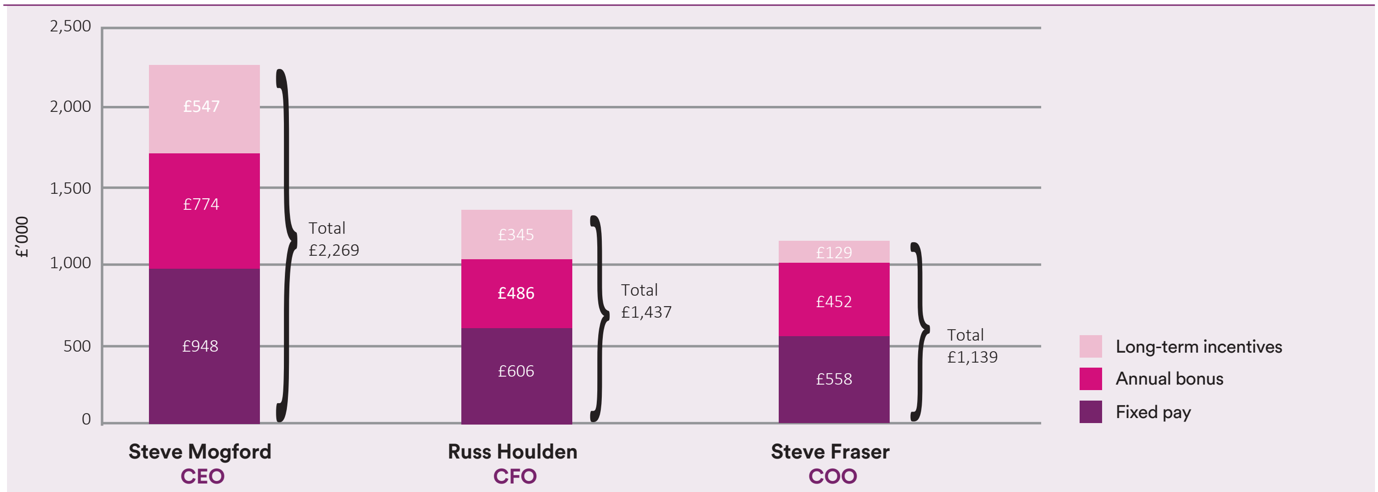
Key element	Implementation of policy in 2018/19
Base salary	› Salary increase of 2.0 per cent from 1 September 2018 (the general employee base salary increase in 2018 was 3.0 per cent).
Benefits and pension	› Market competitive benefits package. › Cash pension allowance of 22 per cent of base salary.
Annual bonus	› Maximum opportunity of 130 per cent of base salary. › 2018/19 annual bonus outcome of around 79 per cent of maximum. › 50 per cent of 2018/19 annual bonus deferred in shares for three years. › Withholding and recovery provisions apply.
Long Term Plan	› Award of 130 per cent of base salary. › Estimated long-term incentive vesting of 60 per cent for the performance period 1 April 2016 to 31 March 2019. These awards will vest after an additional two-year holding period. › Withholding and recovery provisions apply.
Shareholding guidelines	› Personal shareholdings for Steve Mogford and Russ Houlden remain above the 200 per cent of salary minimum guideline. Steve Fraser is expected to reach the minimum guideline within five years of his appointment to the board.

Corporate governance report

At a glance summary: executive directors' remuneration

Single total figure of remuneration for executive directors for 2018/19

Fixed pay comprises base salary, benefits and pension. There is no share price appreciation attributable to the value of the long-term incentives. Further information on the single figure of remuneration can be seen on page 131.



Key performance indicators (KPIs) performance

Annual bonus – Year ended 31 March 2019					Long Term Plan – Three years ended 31 March 2019		
Underlying operating profit[1]	SIM qualitative ranking versus other WASCs	SIM quantitative score	Wholesale outcome delivery incentive (ODI) composite	Time, Cost and Quality index (TCQi)	Total shareholder return (TSR)[2]	Underlying dividend cover[3]	SIM ranking versus other water companies[4]
🟠	🟠	🟢	🟠	🟠	🔴	🟢	🟠
£838.9m	4th out of 10	69.8	£19.2m	95.4%	2.7%	1.22	5th out of 18

Key:

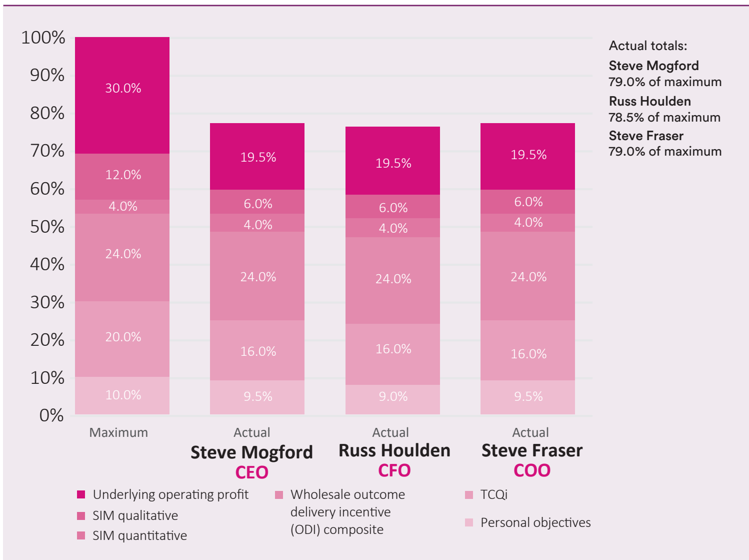
🟢 At or above stretch target 🟠 Between threshold and stretch targets 🔴 Below threshold target

(1) For the purpose of annual bonus, underlying operating profit excludes infrastructure renewals expenditure and property trading.
(2) Below threshold versus the comparator group. See page 135 for further details.
(3) Average underlying dividend cover over 2016/17, 2017/18 and 2018/19.
(4) The estimated SIM combined score ranking for 2018/19.

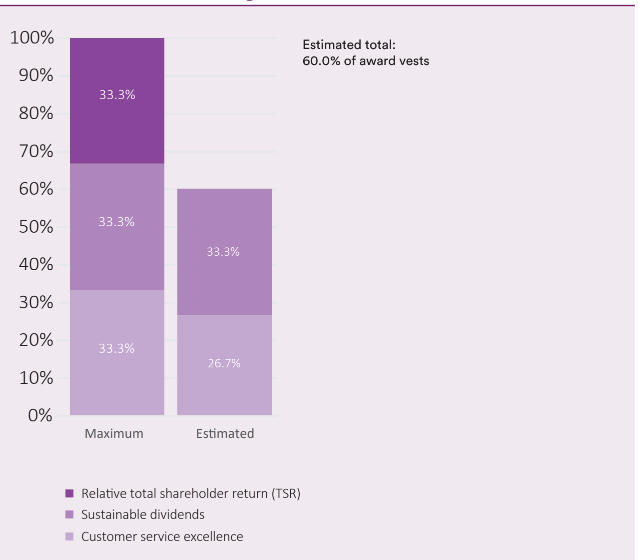
Annual bonus and Long Term Plan (LTP) outcomes

The charts below show the results of the performance against targets for the annual bonus and LTP schemes. Further information on the annual bonus can be seen on page 132 and on the LTP on page 135.

2018/19 Annual bonus outcome



Estimated 2016 Long Term Plan (LTP) outcome



Aligning our remuneration philosophy to business strategy

Our remuneration philosophy is aligned to our purpose, vision and strategy, thereby incentivising great customer service and the creation of long-term value for all of our stakeholders.

The following table provides a summary of how our incentive framework in 2018/19 aligned with our business strategy and the results that it delivers. Many of the performance measures are key performance indicators (KPIs) for the regulatory period 2015–20 (see pages 52 to 53).

	Alignment to strategy	Link to strategic themes	A long-term approach to creating sustainable value
Annual bonus			
Underlying operating profit	Key measure of shareholder value.		✓
Customer service in year[1] › Service incentive mechanism – qualitative › Service incentive mechanism – quantitative	Delivering the best service to customers is a strategic objective. Ofwat can apply financial incentives or penalties depending on our customer service performance.		✓
Maintaining and enhancing services for customers › Wholesale outcome delivery incentive (ODI) composite › Time, cost and quality of the capital programme (TCQi)	Delivering the best service to customers is a strategic objective. There is a direct financial impact on the company of Ofwat incentives and penalties for delivery/non-delivery of customer promises. Keeping tight control of our capital programmes ensures we can provide a reliable service to our customers at the lowest sustainable cost.		✓
Personal	Focused on specific areas of individual contribution.		✓
Compulsory deferral of bonus	Deferral of part of bonus into shares aligns the interests of executive directors and shareholders.		✓
Long Term Plan (LTP)			
Relative total shareholder return (TSR)	Direct measure of delivery of shareholder returns, rewarding management for the outperformance of a comparator group of companies.		✓
Sustainable dividends	Direct measure of return to shareholders through dividend payments, while focusing on the creation of strong earnings that ensure the sustainability of dividends.		✓
Customer service excellence	This is fundamental to delivering our vision of becoming the best UK water and wastewater company. This measure has a direct financial impact on the company as Ofwat can apply financial incentives or penalties depending on our customer service performance.		✓
Additional two-year holding period	Ensures continued alignment with shareholder interests and provides an additional period over which withholding can be applied.		✓
Shareholding guidelines	It is important that a significant investment is made by each executive director in the shares of the company to provide alignment with shareholder interests.		✓

Key:

The best service to customers · At the lowest sustainable cost · In a responsible manner

(1) As Ofwat transitions from using the service incentive mechanism (SIM) to C-MeX as its primary assessment of customer service, for the 2019/20 annual bonus the two SIM measures will be replaced by measures based on performance related to the new C-MeX approach. See page 134 for details.

Corporate governance report
Directors' remuneration policy

Governance

Directors' remuneration policy

This part of the directors' remuneration report sets out the remuneration policy for the company and has been prepared in accordance with the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. The policy in this report will be put to a binding shareholder vote at the 2019 AGM on 26 July 2019 and will take formal effect from that date, subject to shareholder approval. It is intended that the policy will formally apply for three years beginning on the date of approval.

Overview of remuneration policy

The company's remuneration arrangements are designed to promote the long-term success of the company. The company does not pay more than is necessary for this purpose. The committee recognises that the company operates in the North West of England in a regulated environment and therefore needs to ensure that the structure of executive remuneration reflects both the practices of the markets in which its executives operate, and stakeholder expectations of how the company should be run.

The committee monitors the remuneration arrangements to ensure that there is an appropriate balance between risk and reward and that the long-term performance of the business is not compromised by the pursuit of short-term value. There is a strong direct link between incentives and the company's strategy and if the strategy is delivered within an acceptable level of risk, senior executives will be rewarded through the annual bonus and long-term incentives. If it is not delivered, then a significant part of their potential remuneration will not be paid.

The committee also understands that listening to the views of the company's key stakeholders plays a vital role in formulating and implementing a successful remuneration policy over the long term. The committee thus actively seeks the views of shareholders and other key stakeholders to inform the development of the remuneration policy, particularly where any changes to policy are envisaged.

Although employees are not consulted directly on executive remuneration policy, employee engagement surveys are carried out annually and regular discussion takes place with union representatives on matters of pay and remuneration for employees covered by collective bargaining or consultation arrangements. The committee takes into account the general base salary increase and remuneration arrangements, including pension provision, for the wider employee population when determining remuneration policy for the executive directors. Processes are in place for the committee to review and consider any remuneration-related matters that may arise from the activities undertaken by the board to take account of the 'employee voice'.

Future policy table for directors

Base salary	
Purpose and link to strategy: To attract and retain executives of the experience and quality required to deliver the company's strategy.	
Operation	**Maximum opportunity**
Normally reviewed annually, typically effective 1 September. Significant increases in salary should only take place infrequently, for example where there has been a material increase in: › the size of the individual's role; › the size of the company (through mergers and acquisitions); or › the pay market for directly comparable companies (for example, companies of a similar size and complexity). On recruitment or promotion to executive director, the committee will take into account previous remuneration, and pay levels for comparable companies, when setting salary levels. This may lead to salary being set at a lower or higher level than for the previous incumbent.	Current salary levels are shown in the annual report on remuneration. Executive directors will normally receive a salary increase broadly in line with the increase awarded to the general workforce, unless one or more of the conditions outlined under 'operation' is met. Where the committee has set the salary of a new hire at a discount to the market level initially, a series of planned increases can be implemented over the following few years to bring the salary to the appropriate market position, subject to individual performance. **Performance measures** None.

Pension	
Purpose and link to strategy: To provide a level of benefits that allow for personal retirement planning.	
Operation	**Maximum opportunity**
Executive directors are offered the choice of: › a company contribution into a defined contribution pension scheme; › a cash allowance in lieu of pension; or › a combination of a company contribution into a defined contribution pension scheme and a cash allowance.	The maximum opportunity is aligned to the approach available to the wider workforce, currently: › up to 14 per cent of salary into a defined contribution scheme; › cash allowance of broadly equivalent cost to the company (up to 14 per cent of salary less employer National Insurance Contributions at the prevailing rate, i.e. up to 12 per cent of base salary for 2019/20); or › a combination of both such that the cost to the company is broadly the same. For executive directors appointed to role before 26 July 2019 a cash allowance of 22 per cent of salary is payable. **Performance measures** None.

Benefits	
Purpose and link to strategy: To provide market competitive benefits to help recruit and retain high-calibre executives.	
Operation	**Maximum opportunity**
Provision of benefits such as: › health benefits; › car or car allowance; › relocation assistance; › life assurance; › group income protection; › all employee share schemes (e.g. opportunity to join the ShareBuy scheme); › travel; and › communication costs. Any reasonable business-related expenses can be reimbursed (and any tax thereon met if determined to be a taxable benefit). Executives will be eligible for any other benefits which are introduced for the wider workforce on broadly similar terms and additional benefits might be provided from time to time if the committee decides payment of such benefits is appropriate and in line with emerging market practice.	As it is not possible to calculate in advance the cost of all benefits, a maximum is not predetermined. **Performance measures** None.

Annual bonus	
Purpose and link to strategy: To incentivise performance against personal objectives and selected financial and operational KPIs which are directly linked to business strategy. Deferral of part of bonus into shares aligns the interests of executive directors and shareholders.	
Operation	**Maximum opportunity**
A maximum of 50 per cent of bonus awarded paid as cash. A minimum of 50 per cent of bonus awarded deferred into company shares under the Deferred Bonus Plan (DBP) for a period of at least three years. DBP shares accrue dividend equivalents. Not pensionable. Bonuses and DBP shares are subject to recovery provisions in certain negative circumstances including: material misstatement of audited financial results; an error in the calculation; or gross misconduct. Additionally, withholding provisions can also apply to DBP shares in cases of: serious reputational damage; serious failure of risk management; or other circumstances that the committee may determine.	Maximum award level of up to 130 per cent of salary, for the achievement of stretching performance objectives. **Performance measures** Payments predominantly based on financial and operational performance, with a minority based on achievement of personal objectives. Targets and weightings set by reference to the company's financial and operating plans. Bonus outcomes are subject to the committee being satisfied that the company's performance on the measures is consistent with underlying business performance and individual contributions. The committee will exercise discretion on bonus outcomes if it deems necessary. 100 per cent of maximum bonus potential for stretch performance; up to 50 per cent of maximum for target performance; and up to 25 per cent of maximum for threshold performance. No payout for below-threshold performance.

Long Term Plan (LTP)	
Purpose and link to strategy: To incentivise long-term value creation and alignment with the long-term interests of shareholders, customers, and other stakeholders.	
Operation	**Maximum opportunity**
Awards under the Long Term Plan are rights to receive company shares, subject to certain performance conditions. Each award is measured over at least a three-year performance period. An additional holding period applies after the end of the three-year performance period so that the total vesting and holding period is at least five years. Vested shares accrue dividend equivalents. Shares under the LTP are subject to recovery and withholding provisions in certain negative circumstances, including: material misstatement of audited financial results; an error in the calculation; or gross misconduct. Additionally, withholding provisions can also apply in cases of: serious reputational damage; serious failure of risk management; or other circumstances that the committee may determine.	The normal maximum award level will be up to 130 per cent of salary per annum. The overall policy limit is 200 per cent of salary. It is not anticipated that awards above the normal level will be made to current executive directors and any such increase on an ongoing basis will be subject to prior consultation with major shareholders. **Performance measures** The two performance conditions are Return on Regulated Equity and a basket of customer measures. The weighting of each of these two components is 50 per cent. Any vesting is also subject to the delivery of the dividend policy during the respective performance period, and the committee being satisfied that the company's performance on these measures is consistent with underlying business performance. The committee will exercise discretion on LTP outcomes if it deems necessary. The committee retains discretion to set alternative performance measures for future awards but will consult with major shareholders before making any changes to the currently applied measures. 100 per cent of awards vest for stretch performance; and up to 25 per cent of awards vest for threshold performance. No awards vest for below-threshold performance.

Non-executive directors' fees and benefits	
Purpose and link to strategy: To attract non-executive directors with a broad range of experience and skills to oversee the development and implementation of our strategy.	
Operation	**Maximum opportunity**
The remuneration policy for the non-executive directors (with the exception of the Chairman) is set by a separate committee of the board. The policy for the Chairman is determined by the remuneration committee (of which the Chairman is not a member). Fees are reviewed annually taking into account the salary increase for the general workforce and the levels of fees paid by companies of a similar size and complexity. Any changes are normally effective from 1 September. Additional fees are paid in relation to extra responsibilities undertaken, such as chairing certain board sub-committees, and to the senior independent non-executive director. In exceptional circumstances, if there is a temporary yet material increase in the time commitments for non-executive directors, the board may pay extra fees on a pro rata basis to recognise the additional workload. No eligibility for bonuses, long-term incentive plans, pension schemes, healthcare arrangements or employee share schemes. The company repays any reasonable expenses that a non-executive director incurs in carrying out their duties as a director, including travel, hospitality-related and other modest benefits and any tax liabilities thereon, if appropriate.	Current fee levels are shown in the annual report on remuneration. The value of benefits may vary from year to year according to the cost to the company. **Performance measures** Non-executive directors are not eligible to participate in any performance-related arrangements.

Notes to the policy table

Selection of performance measures and targets

Performance measures for the annual bonus are selected annually to align with the company's key strategic goals for the year and reflect financial, operational and personal objectives. 'Target' performance is typically set in line with the business plan for the year, following rigorous debate and approval of the plan by the board. Threshold to stretch targets are then set based on a sliding scale on the basis of relevant commercial factors. Only modest rewards are available for delivering threshold performance levels, with rewards at stretch requiring substantial outperformance of the business plan. Details of the measures used for the annual bonus are given in the annual report on remuneration.

The proposed Long Term Plan (LTP) measures were selected by the committee following an extensive review and shareholder consultation in 2018/19, to align with the company's key strategic goals as we look towards the new regulatory period in 2020, and be closely linked to the creation of long-term shareholder value as follows:

Measure	What is it?	Key reasons for selection
Return on Regulated Equity (RoRE)	RoRE is the return that the company is expected to earn relative to the equity portion of its Regulatory Capital Value. The return is comprehensive in that it is composed of the company's performance on expenditure, investment and financing decisions, and operational and customer initiatives undertaken over the regulatory period. Outperformance (or underperformance) in these areas will result in an increase (or reduction) to RoRE which should translate into higher (or lower) returns for shareholders through share price performance.	› Increasingly used by investors and analysts as it is a good proxy for value (i.e. premium to Regulatory Capital Value) in the sector. › Directly linked to the allowable return set by the regulator, and is comparable across the sector. › Captures financial, operational and customer performance. › Motivates management as they have strong line of sight to the outcome, for which stretching but achievable targets can be set. › Outperformance will result in an increase to RoRE which should translate into higher returns for investors through share price performance.
Customer basket	A basket of customer measures comprising operational measures, service measures and resilience measures to capture the delivery of performance for customers. Customers have a say on which measures they consider the most important priorities for the Company, and the regulator's measures of customer service are included.	› Investors will be impacted by financial rewards resulting from delivery on service commitments, and through investments made to ensure the long-term health and sustainability of our assets. › Customers will benefit from improvements in key performance areas of importance to them, and from long-term reliability in the quality of their water supplies, and ways of working that protect and improve the environment.

The policy provides for committee discretion to alter the LTP measures and weightings to ensure they continue to facilitate an appropriate measurement of performance over the life of the policy (taking into account any evolution of the strategic goals of the company). LTP targets are set taking into account a number of factors, including reference to market practice, the company business plan and analysts' forecasts where relevant. The LTP will only vest in full if stretching business performance is achieved.

Annual bonus and long-term incentives – flexibility, discretion and judgement

The committee will operate the company's incentive plans according to their respective rules and consistent with normal market practice, the Listing Rules and HMRC rules where relevant, including flexibility in a number of regards.

These include making awards and setting performance criteria each year, dealing with leavers, and adjustments to awards and performance criteria following acquisitions, disposals, changes in share capital and to take account of the impact of other merger and acquisition activity. The committee also retains discretion within the policy to adjust the targets, set different measures and/or alter weightings for the annual bonus plan, pay dividend equivalents on vested shares up to the date those shares can first reasonably be exercised and, in exceptional circumstances, under the rules of the long-term incentive plans to adjust performance conditions to ensure that the awards fulfil their original purposes (for example, if an external benchmark or measure is no longer available). All assessments of performance are ultimately subject to the committee's judgement. Any discretion exercised, and the rationale, will be disclosed in the annual remuneration report.

Historic awards

All historic awards that were granted under any current or previous share schemes operated by the company and remain outstanding remain eligible to vest based on their original award terms.

Corporate governance report
Directors' remuneration policy

Alignment of executive director remuneration with the wider workforce

The remuneration approach is consistently applied at levels below the executive directors. Key features include:

- market competitive levels of remuneration, incentives and benefits to attract and retain employees;
- employees at all levels participate in a bonus scheme with the same corporate performance measures as for executive directors; and
- all employees have the opportunity to participate in the HMRC-approved share incentive plan, ShareBuy.

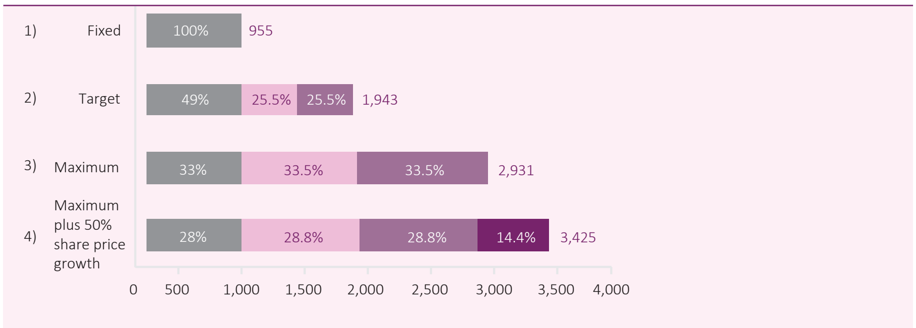
At senior levels, remuneration is increasingly long-term, and 'at risk' with an increased emphasis on performance-related pay and share-based remuneration.

Scenarios for total remuneration

The charts below show the payout under the remuneration policy for each executive director under four different scenarios.

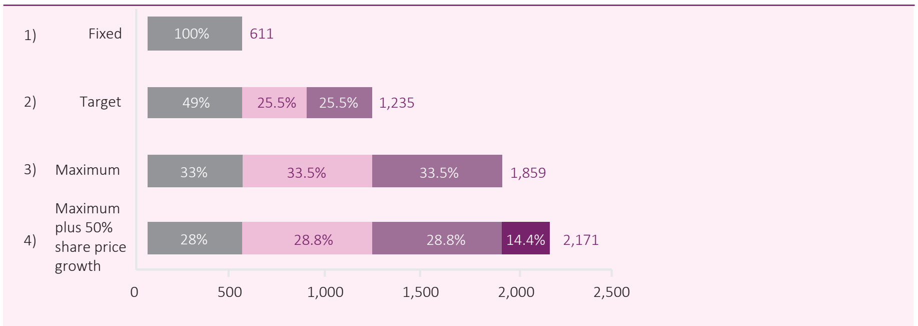
Steve Mogford CEO

£000s



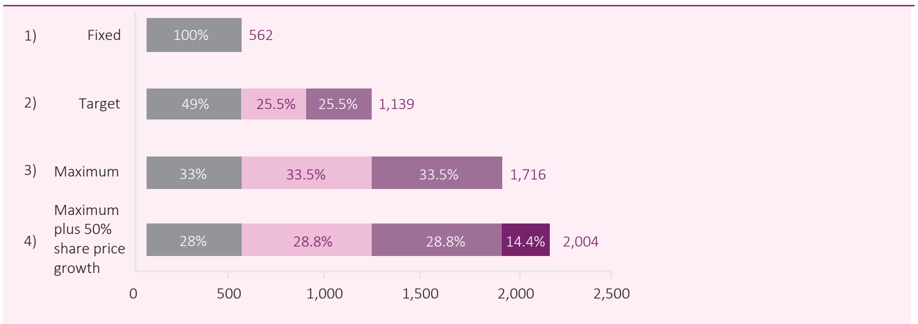
Russ Houlden CFO

£000s



Steve Fraser COO

£000s



Fixed

Annual bonus

Long Term Plan

Additional Long Term Plan value if share price grows by 50%

Notes on the scenario methodology:

- 'Fixed' is base salary effective 31 March 2019 plus cash allowance in lieu of pension of 22 per cent of salary and the value of benefits as shown in the single total figure of remuneration table for 2018/19;
- 'Target' performance is the level of performance required for the annual bonus and Long Term Plan to pay out at 50 per cent of maximum;
- 'Maximum' performance would result in 100 per cent vesting of the annual bonus and Long Term Plan (i.e. 260 per cent of salary in total);
- 'Maximum performance plus 50 per cent share price growth' shows maximum performance plus the impact on the Long Term Plan of a hypothetical 50 per cent increase in the share price;
- Annual bonus includes amounts compulsorily deferred into shares;
- Long Term Plan is measured at face value, i.e. no assumption for dividends or changes in share price (except in the fourth scenario); and
- Amounts relating to all-employee share schemes have, for simplicity, been excluded from the charts.

Shareholding guidelines
The committee believes that it is important for each executive director to build and maintain a significant investment in shares of the company to provide alignment with shareholder interests. Shareholding guidelines are therefore operated and the details of how these are currently applied are provided in the annual report on remuneration.

External directorships
The company recognises that its executive directors may be invited to become non-executive directors of other companies outside the company and exposure to such non-executive duties can broaden experience and knowledge, which would be of benefit to the company. Any external appointments are subject to board approval (which would not be given if the proposed appointment was with a competing company, would lead to a material conflict of interest or could have a detrimental effect on a director's performance). Directors will be allowed to retain any fees received in respect of such appointments.

Service contracts and letters of appointment
Executive directors' service contracts are subject to up to one year's notice period when terminated by the company and at least six months' notice when terminated by the director.

The policy on payments for loss of office is set out in the next section.

The Chairman and other non-executive directors have letters of appointment rather than service contracts. Their appointments may be terminated without compensation at any time. All non-executive directors are subject to re-election at each AGM.

Copies of executive directors' service contracts and non-executive directors' letters of appointment are available for inspection at the company's registered office during normal hours of business and will be available at the company's AGM. Copies of non-executive directors' letters of appointment can also be viewed on the company's website.

Approach to recruitment remuneration
The remuneration package for a new executive director would be set in accordance with the terms of the company's approved remuneration policy in force at the time of appointment.

Buy-out awards
The committee may offer additional cash and/or share-based elements (on a one-time basis or ongoing) when it considers these to be in the best interests of the company (and therefore shareholders). Any such payments would be limited to a reasonable estimate of value of remuneration lost when leaving the former employer and would reflect the delivery mechanism (i.e. cash and/or share-based), time horizons and whether performance requirements are attached to that remuneration. Shareholders will be informed of any such payments at the time of appointment.

Maximum level of variable pay
The maximum level of long-term incentives which may be awarded to a new executive director will be limited to the maximum Long Term Plan limit of 200 per cent of salary per annum on an ongoing basis. Therefore, the maximum level of overall variable pay that may be offered will be 330 per cent of salary (i.e. 130 per cent annual bonus plus 200 per cent Long Term Plan) per annum on an ongoing basis. These limits are in addition to the value of any buy-out arrangements which are governed by the policy above.

In the case of an internal appointment, any variable pay element awarded in respect of the prior role would be allowed to pay out according to its terms, adjusted as relevant to take into account the appointment. In addition, any other previously awarded entitlements would continue, and be disclosed in the next annual report on remuneration.

Base salary and relocation expenses
Base salary levels for new executive directors will be set in accordance with the policy, taking into account the experience of the individual recruited. The committee has the flexibility to set the salary of a new appointee at a discount to the market level initially, with a series of planned increases implemented over the following years to bring the salary to the appropriate market position, subject to individual performance in the role.

The committee may agree that the company will meet certain relocation and/or incidental expenses as appropriate.

Annual bonus performance conditions
Where a new executive director is appointed part way through a financial year, the committee may set different annual bonus measures and targets for the new executive director from those used for other executive directors (for the initial part-year only).

Appointment of non-executive directors
For the appointment of a new Chairman or non-executive director, the fee arrangement would be set in accordance with the approved remuneration policy in force at that time. Non-executive directors' fees are set by a separate committee of the board; the Chairman's fees are set by the remuneration committee.

Corporate governance report
Directors' remuneration policy

Payment for loss of office

The circumstances of the termination, including the individual's performance and an individual's duty and opportunity to mitigate losses, are taken into account in every case. Our policy is to stop or reduce compensatory payments to former executive directors to the extent that they receive remuneration from other employment during the compensation period. A robust line on reducing compensation is applied and payments to departing employees may be phased in order to mitigate loss. Our policy is shown in the table below:

Provision	Summary terms
Compensation for loss of office	› An executive director's service contract may be terminated without notice and without any further payment or compensation, except for sums earned up to the date of termination, on the occurrence of certain contractually specified events such as gross misconduct. › No termination payment if full notice is worked. › Otherwise, a payment in respect of the period of notice not worked of basic salary, plus pension and car allowance for that period. › Half of the termination payment will be paid within 14 days of date of termination. › The other half will be paid in monthly instalments over what would have been the second half of the notice period. This will be reduced by the value of any salary, pension contribution and car allowance earned in new paid employment in that period.
Treatment of annual bonus on termination	› A time prorated bonus may be payable for the period of active service; however, there is no automatic entitlement to payments under the bonus scheme. Any payment is at the discretion of the committee and is subject to recovery and withholding provisions as detailed in the policy table. › Performance targets would apply in all circumstances.
Treatment of deferred bonus on termination	› Determined on the basis of the relevant plan rules. Full details can be found on the company's website. › Deferred bonuses are subject to recovery and withholding provisions as detailed in the policy table. › The default treatment is that any outstanding awards will vest in full on the normal vesting date with no time prorating applying.
Treatment of unvested long-term incentives on termination	› Determined on the basis of the relevant plan rules. Full details can be found on the company's website. › Normally, any outstanding awards will lapse on date of cessation of employment (if that occurs during the performance period). › However, under the rules of the plans, in certain prescribed circumstances, such as death, disability, mutually agreed retirement or other circumstances at the discretion of the committee, 'good leaver' status can be applied. In these circumstances, a participant's awards vest on a time prorated basis subject to the satisfaction of relevant performance criteria, with the balance of awards lapsing. The committee retains the discretion not to time prorate if it is inappropriate to do so in particular circumstances. The committee will take into account the individual's performance and the reasons for their departure when determining whether 'good leaver' status can be applied.
Treatment of pensions on termination	› On redundancy, an augmentation may apply in relation to benefits accrued under a United Utilities defined benefit pension scheme, in line with the trust deed and rules of the appropriate section.

Outplacement services, reimbursement of legal costs and any other incidental expenses may be provided where appropriate. Any statutory entitlements or compromise claims in connection with a termination of employment would be paid as necessary. Outstanding savings/shares under all-employee share plans would be transferred in accordance with the terms of the plans as approved by HMRC.

Change of control

On a change of control, executive directors' incentive awards will be treated in accordance with the rules of the applicable plans. In summary:

- Bonus payments will take into account the extent to which the performance measures have been satisfied between the start of the performance period and the date of the change of control, and the value will be prorated to reflect the same period.
- Deferred bonuses will generally vest on the date of a change of control, unless the committee permits (or requires) awards to roll over into equivalent shares in the acquirer.
- Long Term Plan awards will generally vest on the date of a change of control taking into account the extent to which any performance condition has been satisfied at that point. Time prorating will normally apply unless the committee determines otherwise.

Executive directors' remuneration for the year ended 31 March 2019

Single total figure of remuneration for executive directors (audited information)

	Fixed pay						Variable pay					
	Base salary £'000		Pension £'000		Benefits £'000		Annual bonus £'000		Long-term incentives £'000		Total £'000	
Year ended 31 March	**2019**	2018	**2019**	2018	**2019**	2018	**2019**	2018	**2019**(1)	2018(2)	**2019**	2018
Steve Mogford	**754**	737	**166**	162	**28**	29	**774**	718	**547**	521	**2,269**	2,167
Russ Houlden	**476**	466	**105**	102	**25**	25	**486**	450	**345**	329	**1,437**	1,372
Steve Fraser(3)	**440**	278	**97**	61	**21**	15	**452**	277(4)	**129**	102	**1,139**	733

(1) The long-term incentive amount is in respect of the Long Term Plan award which was granted in June 2016 and which will vest based on performance over the three-year period from 1 April 2016 to 31 March 2019. The Long Term Plan amount is estimated as the vesting percentage for the one-third relating to customer service excellence will not be known until later in 2019, and the award for Steve Mogford and Russ Houlden will not vest until the end of an additional two-year holding period. Steve Fraser's award was granted prior to his appointment to the board and so no holding period applies. There is no share price appreciation attributable to these awards. See page 135 for further details.

(2) The long-term incentive amount for the year ended 31 March 2018 is in respect of the Long Term Plan award which was granted in June 2015 and whose performance period ended on 31 March 2018. The figures for Steve Mogford and Russ Houlden have been restated to reflect the additional dividend equivalents accrued to 31 March 2019. Their awards are not due to vest until April 2020 following an additional two-year holding period and for the purposes of this table have been valued on the basis of the average share price over the three-month period from 1 January 2019 to 31 March 2019 of 824.5 pence per share.

(3) Salary, benefits, pension and annual bonus figures for Steve Fraser in 2018 reflect part-year earnings and are for the period from 1 August 2017, when he was first appointed to the board.

(4) A bonus of around £74,000 was earned by Steve Fraser in respect of the period from 1 April 2017 to 31 July 2017 prior to him joining the board. This is not included in the table.

Base salary

	Base salary £'000	
Executive director	**Current salary**	1 September 2017
Steve Mogford	**760.0**	745.0
Russ Houlden	**480.0**	470.5
Steve Fraser	**443.7**	405.0

Executive director salaries were increased by 2.0 per cent with effect from 1 September 2018. This is lower than the 3.0 per cent increase applying to the general workforce in 2018. The committee judged that the increase was supported by very good individual and business performance.

On his appointment as COO on 1 August 2017, Steve Fraser's salary was set at £405,000 in consideration of the organisational structure and the level of responsibilities he assumed at that time, and also took account of internal and external market benchmarks. As stated in last year's report, on 1 January 2018 there was a material change in the size and scope of the COO role as a result of a reorganisation, and his salary was increased to £435,000 from the same date in recognition of this. His current salary reflects the 2.0 per cent increase applied to the executive directors on 1 September 2018.

Pensions

The executive directors receive a cash allowance of 22 per cent of base salary in lieu of pension. No changes are expected to the pensions cash allowance percentage for the current executive directors during the year commencing 1 April 2019.

Benefits

For executive directors, benefits include: a car allowance of £14,000; health, life cover and income protection insurance; travel costs; and communication costs.

No material changes are expected to benefits during the year commencing 1 April 2019.

External appointments

Steve Mogford is the senior independent director of G4S PLC for which he received and retained an annual fee of £78,500. Russ Houlden is an independent member of the supervisory board, and audit committee chairman, of Orange Polska SA for which he receives and retains annual fees of around £80,000.

Annual bonus

Annual bonus in respect of financial year ended 31 March 2019 (audited information)

The performance measures, targets and outcomes in respect of the executive directors' annual bonus for the year ended 31 March 2019 are set out below. The table on page 123 summarises how these performance measures are linked to our business strategy.

Measure	Threshold (25% vesting)	Target	Stretch (100% vesting)	Vesting as a % of maximum	Steve Mogford weighting (% of award) **Outcome**	Russ Houlden weighting (% of award) **Outcome**	Steve Fraser weighting (% of award) **Outcome**
Underlying operating profit[1]							
	£806.4m	£831.4m	£856.4m	65%	30.0%	30.0%	30.0%
	Actual: £838.9m				**19.5%**	**19.5%**	**19.5%**
Customer service in year							
Service incentive mechanism – qualitative	5th position v other WASCs	4th position v other WASCs	3rd position v other WASCs	50%	12.0%	12.0%	12.0%
	Actual 4th position v other WASCs				**6.0%**	**6.0%**	**6.0%**
Service incentive mechanism – quantitative	73.5	73.0	72.5	100%	4.0%	4.0%	4.0%
	Actual: 69.8				**4.0%**	**4.0%**	**4.0%**
Maintaining and enhancing services for customers							
Wholesale outcome delivery incentive (ODI) composite	(£25.1m)	(£4.7m)	£17.8m	100%	24.0%	24.0%	24.0%
	Actual: £19.2m				**24.0%**	**24.0%**	**24.0%**
Time, cost and quality of capital programme (TCQi)[2]	85.0%	91.5%	98.0%	80%	20.0%	20.0%	20.0%
	Actual: 95.4%				**16.0%**	**16.0%**	**16.0%**
Personal objectives (see page 133 for further detail)							
Steve Mogford				95%	10.0%		
	Actual: 95%				**9.5%**		
Russ Houlden				90%		10.0%	
	Actual: 90%					**9.0%**	
Steve Fraser				95%			10.0%
	Actual: 95%						**9.5%**
Total:							
Actual award (% of maximum)					**79.0%**	**78.5%**	**79.0%**
Maximum award (% of salary)					130%	130%	130%
Actual award (% of salary)[3]					**102.7%**	**102.1%**	**102.7%**
Actual award (£'000 – shown in single figure table)[3]					**774**	**486**	**452**

(1) The underlying operating profit figure for bonus purposes is based on the underlying operating profit on page 67 and excludes infrastructure renewals expenditure and property trading. The vesting percentage shown in the table above is the figure after this adjustment.
(2) TCQi is an internal measure which measures the extent to which we deliver our capital projects on time, to budget and to the required quality standard. It is expressed as a percentage, with a higher percentage representing better performance.
(3) Under the Deferred Bonus Plan, 50 per cent of the annual bonus will be deferred in shares for three years.

Further detail of achievement against personal objectives

Personal objectives represent 10 per cent of the total bonus opportunity. Assessment of outcomes against personal objectives is summarised in the table below:

Steve Mogford	
Personal objectives related to:	**Performance summary**
› Preparations for the new regulatory period (2020–2025); › Operational performance for the benefit of customers; › Analyst and investor engagement; and › Organisation culture.	The committee assessed that Steve Mogford's performance warranted an outcome of 95 per cent in respect of the personal objective element of his bonus, including: › Led the formulation of the company's PR19 business plan for the period 2020–25, rewarded by the award of fast-track status to the plan by Ofwat, yielding a significant reward in AMP7. › Drove a further step-change in company performance with significant financial rewards related to ODI and SIM performance. › Provided strong leadership of the company's response to the exceptional weather conditions during the summer of 2018. › Engaged actively with investors and analysts in the communication of our strategy, performance and plan. › Continued to develop a strong and cohesive executive team and organisation culture.

Russ Houlden	
Personal objectives related to:	**Performance summary**
› Financial preparations for the new regulatory period 2020–25; › Financing activities; and › Cyber security.	The committee assessed that Russ Houlden's performance warranted an outcome of 90 per cent in respect of the personal objective element of his bonus, including: › Strong contribution to the formulation of the company's PR19 business plan for the period 2020–25. › Led the enhancement of our financing competitive advantage, with low cost financing raised within the context of a low risk hedging strategy delivering significant value to customers and shareholders, benefitting service resilience and the environment. › Strengthened our cyber security strategy to defend against increasing cyber threats, covering information technology and operational technology.

Steve Fraser	
Personal objectives related to:	**Performance summary**
› Operational preparations for the new regulatory period 2020–25; and › Operational performance for the benefit of customers.	The committee assessed that Steve Fraser's performance warranted an outcome of 95 per cent in respect of the personal objective element of his bonus, including: › Strong contribution to the formulation of the company's PR19 business plan for the period 2020–25. › Achievement of our best ever annual ODI result. › Established a new network maintenance function and implemented a revised contracting framework, delivering a marked improvement in network performance and best ever customer satisfaction scores. › Strong leadership of the company's operational teams in addressing the impact of the exceptional weather conditions.

Corporate governance report
Annual report on remuneration

Deferred Bonus Plan awards made in the year ended 31 March 2019 (audited information)

Bonuses are earned by reference to performance in the financial year and paid in June following the end of the financial year. Fifty per cent of any bonus is deferred into shares under the Deferred Bonus Plan. These awards vest after three years and are subject to withholding provisions. There are no service or additional performance conditions attached.

The table below provides details of share awards made on 18 June 2018 in respect of bonus payments made to executive directors in 2018/19.

Executive Director	Type of award	Basis of award	Number of shares	Face value of award[(1)] (£'000)	End of deferral period
Steve Mogford	Conditional shares	50% of bonus	47,057	£359	18.06.2021
Russ Houlden	Conditional shares	50% of bonus	29,517	£225	18.06.2021
Steve Fraser	Conditional shares	50% of bonus[(2)]	22,043	£168	18.06.2021

(1) The face value has been calculated using the closing share price on 15 June 2018 (the dealing day prior to the date of grant), which was 762.8 pence per share.

(2) As stated in last year's report, a bonus of around £277,000 was earned by Steve Fraser in respect of the period 1 August 2017 to 31 March 2018 (following his appointment to the board), along with a bonus of around £74,000 in respect of the period 1 April 2017 to 31 July 2017 (prior to his appointment to the board). He received one overall Deferred Bonus Plan award in respect of both bonus payments, where the overall award value was based on 50 per cent of the bonus earned since his appointment to the board plus 40 per cent of the bonus earned prior to his appointment.

Annual bonus in respect of the financial year commencing 1 April 2019

The maximum bonus opportunity for the year commencing 1 April 2019 will remain unchanged at 130 per cent of base salary.

The annual bonus will operate in a similar way as that for the year 2018/19, except in relation to the 'Customer service in year' measures. As Ofwat transitions from using the service incentive mechanism (SIM) to C-MeX as its primary assessment of customer service, the two SIM measures will be replaced by measures based on performance related to the new C-MeX approach.

The table below summarises the measures, weighting and targets for the 2019/20 bonus. Targets that are considered commercially sensitive will be disclosed in the 2019/20 annual report on remuneration.

	Targets			
Measure	Threshold (25% vesting)	Target (50% vesting)	Stretch (100% vesting)	Weighting (% of award)
Underlying operating profit[(1)]		Commercially sensitive		30.0%
Customer service in year				
C-MeX – customer service survey (out of 10 WASCs)	6th	4th	3rd	12.0%
C-MeX – quantitative	16.62	16.06	15.50	4.0%
Maintaining and enhancing services for customers				
Wholesale outcome delivery incentive (ODI) composite		Commercially sensitive		24.0%
Time, cost and quality of capital programme (TCQi)[(2)]	85%	91.5%	98%	20.0%
Personal objectives		Commercially sensitive		10.0%
Total				**100%**

(1) Underlying operating profit for bonus purposes excludes infrastructure renewals expenditure and property trading.

(2) TCQi is an internal measure which measures the extent to which we deliver our capital projects on time, to budget and to the required quality standard. It is expressed as a percentage, with a higher percentage representing better performance.

Long-term incentives

Performance for Long Term Plan awards

2016 Long Term Plan (LTP) awards with a performance period ended 31 March 2019 (audited information)

The 2016 LTP awards were granted in June 2016 and performance was measured over the three-year period from 1 April 2016 to 31 March 2019. Executive directors' awards will normally vest in April 2021, following an additional two-year holding period. The unvested shares will remain subject to withholding provisions over this two-year holding period.

Note that the final outcome for the customer service excellence measure (which forms one-third of the award) will not be known until Ofwat publishes the combined service incentive mechanism scores for the company and its comparator water companies (expected to be published in late summer 2019). The values of the 2016 LTP awards in the single total figure of remuneration table are therefore estimated and will be restated in next year's report once the final outcome is known.

The table below shows how the long-term incentive amount in respect of the 2016 LTP was calculated:

Measure	Threshold (25% vesting)	Intermediate	Stretch (100% vesting)	Vesting as a % of maximum	Steve Mogford weighting (% of award) **Outcome**	Russ Houlden weighting (% of award) **Outcome**	Steve Fraser weighting (% of award) **Outcome**
Relative total shareholder return (TSR)							
TSR versus median TSR of FTSE 100 companies (excluding financial services, oil and gas, and mining companies)[1]	Median TSR	Straight-line between threshold and stretch	Median TSR × 1.15	0%	33.3%	33.3%	33.3%
	Actual: Less than median TSR				**0%**	**0%**	**0%**
	Company TSR of 2.7% was below threshold TSR of 17.9%						
Sustainable dividends		**(50% vesting)**					
Average underlying dividend cover over the three-year performance period	1.05	1.13	1.15	100%	33.3%	33.3%	33.3%
			Actual: 1.22		**33.3%**	**33.3%**	**33.3%**
Underpin: Dividend growth of at least RPI in each of the years 2016/17, 2017/18 and 2018/19[2]	✓ Met						
Customer service excellence		**(80% vesting)**					
Ranking for the year ended 31 March 2019 versus 17 other water companies using Ofwat's service incentive mechanism (SIM) combined score[3]	Median rank	Upper quartile rank	Upper decile rank	80.0%	33.3%	33.3%	33.3%
	Estimate: 5th out of 18				**26.7%**	**26.7%**	**26.7%**
Overall underpin							
Overall vesting is subject to the committee being satisfied that the company's performance on these measures is consistent with underlying business performance	✓ Assumed met. The committee will make a final assessment of the company's performance once the combined SIM score is known.						
Estimated vesting (% of award)					**60.0%**	**60.0%**	**60.0%**
Number of shares granted					98,763	62,333	23,397
Number of dividend equivalent shares					11,733	7,404	2,778
Number of shares before performance conditions applied					110,496	69,737	26,175
Estimated number of shares after performance conditions applied					66,297	41,842	15,705
Three-month average share price at end of performance period (pence)[4]					824.5	824.5	824.5
Estimated value at end of performance period (£'000 – shown in single figure table)					**547**	**345**	**129**

(1) For the purposes of calculating TSR, the TSR index is averaged over the three months prior to the start and end of the performance period. TSR is independently calculated by New Bridge Street.
(2) Subject to approval of the final dividend by shareholders at the 2019 AGM.
(3) This is an estimate as the final outcome will not be known until the combined scores are published later in 2019.
(4) Average share price over the three-month period from 1 January 2019 to 31 March 2019.

Long Term Plan awards granted in the year

2018 LTP awards with a performance period ending 31 March 2021 (audited information)

The table below provides details of share awards made to executive directors on 25 June 2018 in respect of the 2018 LTP:

Executive Director	Type of award	Basis of award	Face value of award (£'000)[1]	Number of shares under award	% vesting at threshold	End of performance period[2]
Steve Mogford	Conditional shares	130% of salary	£968	129,030	25%	31.03.2021
Russ Houlden	Conditional shares	130% of salary	£612	81,488	25%	31.03.2021
Steve Fraser	Conditional shares	130% of salary	£565	75,339	25%	31.03.2021

(1) The face value has been calculated using the closing share price on 22 June 2018 (the dealing day prior to the date of grant) which was 750.6 pence per share.
(2) An additional two-year holding period applies after the end of the three-year performance period.

Details about the 2018 LTP performance measures and targets are shown in the following table. Performance is measured over the three-year period 1 April 2018 to 31 March 2021. The table on page 123 summarises how these performance measures are linked to our business strategy.

	Targets		
Measure	Threshold (25% vesting)	Stretch (100% vesting)	Weighting
Relative total shareholder return (TSR)			
TSR versus median TSR of FTSE 100 companies (excluding financial services, oil and gas, and mining companies) [1] measured over the three-year performance period	Median TSR	Median TSR × 1.15	33.3%
Sustainable dividends			
Average underlying dividend cover over the part of the performance period up to the end of the regulatory period (31 March 2020)	The targets are considered commercially sensitive and so are not disclosed in this report. However, actual targets, performance achieved and awards made will be published retrospectively so that shareholders can fully understand the basis for any vesting		33.3%
Underpin:	Dividend growth of at least RPI in each of the years 2018/19 and 2019/20		
Customer service excellence [2]			
Ranking for the year ending 31 March 2021 versus ten other water and wastewater companies using Ofwat's service incentive mechanism (SIM) combined score	Median rank (5th out of 10)	Upper quartile rank (3rd out of 10)	33.3%
Overall underpin			
Overall vesting is subject to the committee being satisfied that the company's performance on these measures is consistent with underlying business performance			

(1) For the purposes of calculating TSR, the TSR index is averaged over the three months prior to the start and end of the performance period. TSR is independently calculated by New Bridge Street.
(2) The committee retains the discretion to adjust the customer service measure and targets once Ofwat's approach to assessing customer service for the regulatory period 2020–25 is agreed.

Straight-line vesting applies between the threshold and stretch targets, with nil vesting below threshold performance. The committee will have the flexibility to make appropriate adjustments to the performance targets in exceptional circumstances, to ensure that the award achieves its original purpose.

Performance targets for future Long Term Plan awards

2019 LTP awards with a performance period ending 31 March 2022

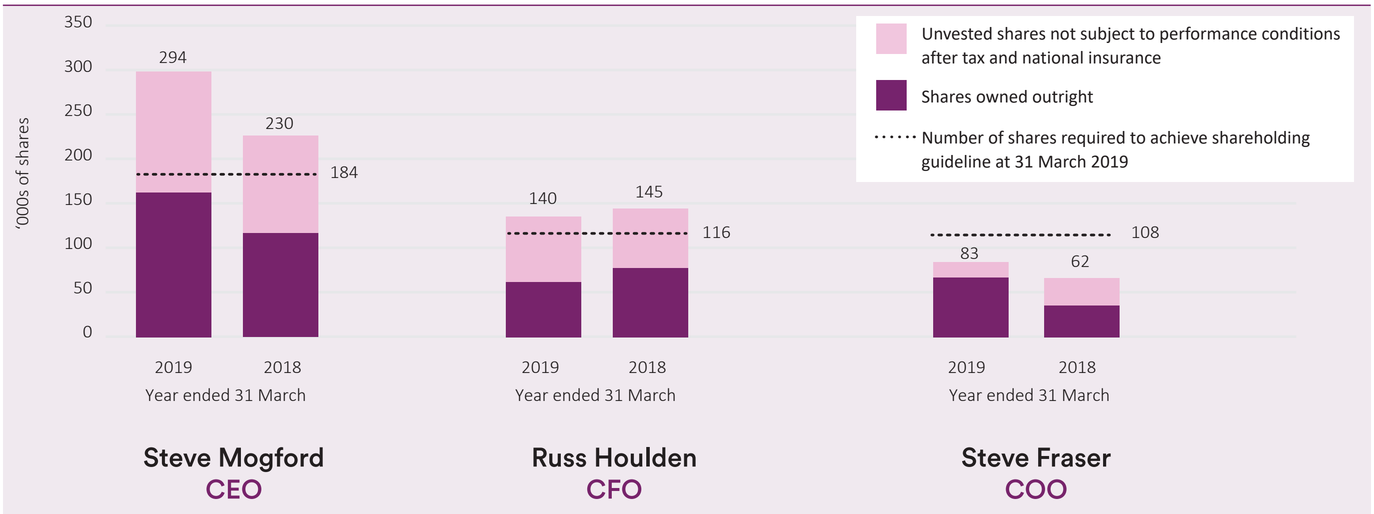
Awards are expected to be made in late June 2019 and the award level for executive directors will remain unchanged at 130 per cent of base salary. Setting appropriate targets against the current performance measures is challenging given that two of the three years of the performance period will be in the new regulatory period. The committee is considering whether it might begin to reflect the performance measures included in the proposed directors' remuneration policy in the construct of the 2019 LTP awards, and major shareholders will be consulted on the proposed approach before the awards are made.

Executive directors’ interests in shares

Executive directors’ shareholding (audited information)

Executive directors are expected to reach a shareholding guideline of 200 per cent of salary, normally within five years of appointment. There is no additional requirement in the current guidelines for post-employment shareholding requirements as outlined on page 120.

Details of beneficial interests in the company’s ordinary shares as at 31 March 2019 held by each of the executive directors and their connected persons are set out in the charts below along with progress against the target shareholding guideline level. Steve Mogford and Russ Houlden have both exceeded the target shareholding guideline level of 200 per cent of salary. Steve Fraser is expected to reach his shareholding guideline of 200 per cent of salary within five years of his appointment to the board.



Further details of the executive directors’ shareholdings and their share plan interests are given in the table below and in the appendix on page 143.

Director	Shareholding guideline (% of salary)	Number of shares required to meet shareholding guideline[1]	Number of shares owned outright (including connected persons) 2019	2018	Unvested shares not subject to performance conditions[2] 2019	2018	Total shares counting towards shareholding guidelines[3] 2019	2018	Shareholding as % of base salary at 31 March 2019[1] 2019	Shareholding guideline met at 31 March 2019 2019	Unvested shares subject to performance conditions[4] 2019	2018
Steve Mogford[5] [6]	200%	184,354	**158,299**	110,119	**255,366**	225,615	**293,665**	229,713	**319%**	**Yes**	**352,738**	318,589
Russ Houlden[5] [6]	200%	116,434	**55,040**	69,435	**160,669**	142,088	**140,217**	144,760	**241%**	**Yes**	**222,701**	201,117
Steve Fraser[5]	200%	107,629	**60,608**	46,905	**43,069**	29,027	**83,457**	62,310	**155%**	**No**	**129,081**	75,479

(1) Share price used is the average share price over the three months from 1 January 2019 to 31 March 2019 (824.5 pence per share).
(2) Unvested shares subject to no further performance conditions such as matching shares under the ShareBuy scheme. Includes shares subject only to withholding provisions such as Deferred Bonus Plan shares in the three-year deferral period and Long Term Plan shares in the two-year holding period.
(3) Includes unvested shares not subject to performance conditions (on a net of tax and national insurance basis), plus the number of shares owned outright.
(4) Includes unvested shares under the Long Term Plan.
(5) In the period 1 April 2019 to 21 May 2019, additional shares were acquired by Steve Mogford (37 ordinary shares), Russ Houlden (37 ordinary shares) and Steve Fraser (38 ordinary shares) in respect of their regular monthly contributions to the all-employee ShareBuy scheme. These will be matched by the company on a one-for-five basis. Under the scheme, matching shares vest one year after grant provided the employee remains employed by the company.
(6) On 1 April 2019, shares granted on 30 June 2014 under the Long Term Plan vested for Steve Mogford and Russ Houlden following their additional two-year holding period. Steve Mogford had 66,415 shares vesting, of which 31,294 shares were sold to cover tax and national insurance. Steve retained the remaining balance of 35,121 shares. Russ Houlden had 41,920 shares vesting, of which 19,752 shares were sold to cover tax and national insurance. Russ retained the remaining balance of 22,168 shares.

Dilution limits

Awards granted under the company’s share plans are satisfied by market purchased shares bought on behalf of the company by United Utilities Employee Share Trust immediately prior to the vesting of a share plan. The company does not make regular purchases of shares into the Trust nor employs a share purchase hedging strategy and shares are bought to satisfy the vesting of share plans. The rules of the Deferred Bonus Plan do not permit awards to be satisfied by newly issued shares and must be satisfied by market purchased shares. The rules of the Long Term Plan permit the awards to be satisfied by newly issued shares but the company has decided to satisfy awards by market purchased shares.

Should the company’s method of satisfying share plan vestings change (i.e. issuing new shares) then the company would monitor the number of shares issued and their impact on dilution limits set by The Investment Association in respect of all share plans (10 per cent in any rolling 10-year period) and executive share plans (five per cent in any rolling 10-year period).

No treasury shares were held or utilised in the year ended 31 March 2019.

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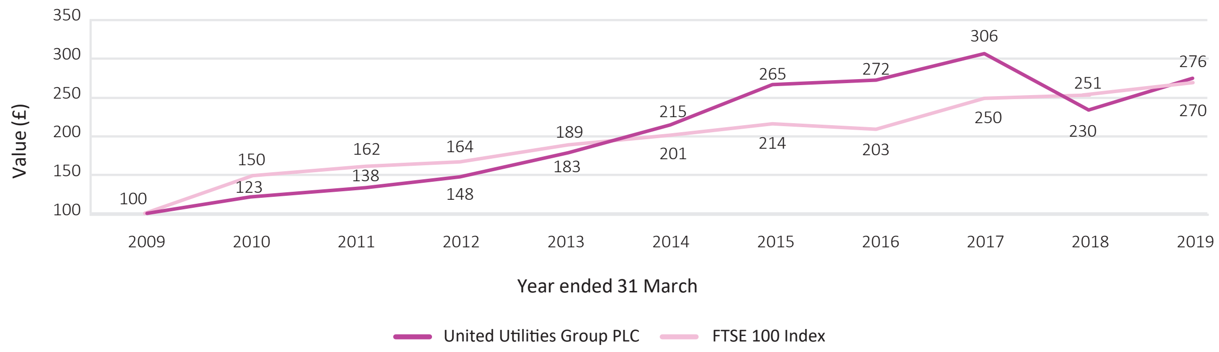
Other information

Performance and CEO remuneration comparison

This graph illustrates the company's performance against the FTSE 100 over the past ten years. The FTSE 100 has been chosen as the appropriate comparator as the company is a member of the FTSE 100 and it is considered to be the most widely published benchmark for this purpose. The table below the TSR chart shows the remuneration data for the CEO over the same ten-year period as the TSR chart.



Year ended 31 March		2010	2011	2012	2013	2014	2015	2016	2017	2018	**2019**
CEO single figure of remuneration (£000)	Steve Mogford	n/a	377	1,421	1,549	2,378	2,884	2,760[1]	2,233[2]	2,167[3]	**2,269**
	Philip Green	1,992	3,073	n/a	n/a	n/a	n/a	n/a	n/a	n/a	**n/a**
Annual bonus payment (% of maximum)	Steve Mogford	n/a	90.6	72.0	84.4	78.2	77.4	54.5	83.7	74.9	**79.0**
	Philip Green	89.2	90.8	n/a	n/a	n/a	n/a	n/a	n/a	n/a	**n/a**
LTP vesting (% of maximum)[4]	Steve Mogford	n/a	n/a[5]	n/a[5]	n/a[5]	93.5	97.5	33.6	54.5	55.4	**60.0**[7]
								100[6]			
	Philip Green	0[8]	28.1[10]	n/a	n/a	n/a	n/a	n/a	n/a	n/a	**n/a**
		12.5[9]	100[11]								

(1) This includes the pay-out from the 2013 Long Term Plan (LTP) as well as £1.028 million in respect of Steve Mogford's one-off Matched Share Investment Scheme which ended on 5 January 2016.
(2) The pay-out from the 2014 LTP, which vested on 1 April 2019 after the end of a two-year holding period, has been updated to reflect the additional dividends accruing on this award and the closing share price on the date of vesting of 813 pence per share.
(3) The pay-out from the 2015 LTP has been restated to reflect the additional dividend equivalents accruing on these awards, final vesting outcome and updated share price. See page 131 for further details.
(4) For performance periods ended on 31 March, unless otherwise stated.
(5) Steve Mogford was not a participant in any long-term incentive plans that had performance periods ending during 2011 to 2013. For those who did participate in those plans, the vesting as a percentage of maximum was 37.5 per cent for those vesting in 2012 and 35.3 per cent for those vesting in 2013.
(6) The retention period applicable to Steve Mogford's Matched Share Investment Scheme ended on 5 January 2016.
(7) The 2016 Long Term Plan amount vesting percentage is estimated. See page 135 for further details.
(8) 2007 Performance Share Plan (PSP).
(9) 2007 Matching Share Award Plan (MSAP).
(10) 2008 PSP and MSAP.
(11) The retention period applicable to Philip Green's Matched Share Investment Scheme ended on 12 February 2011.

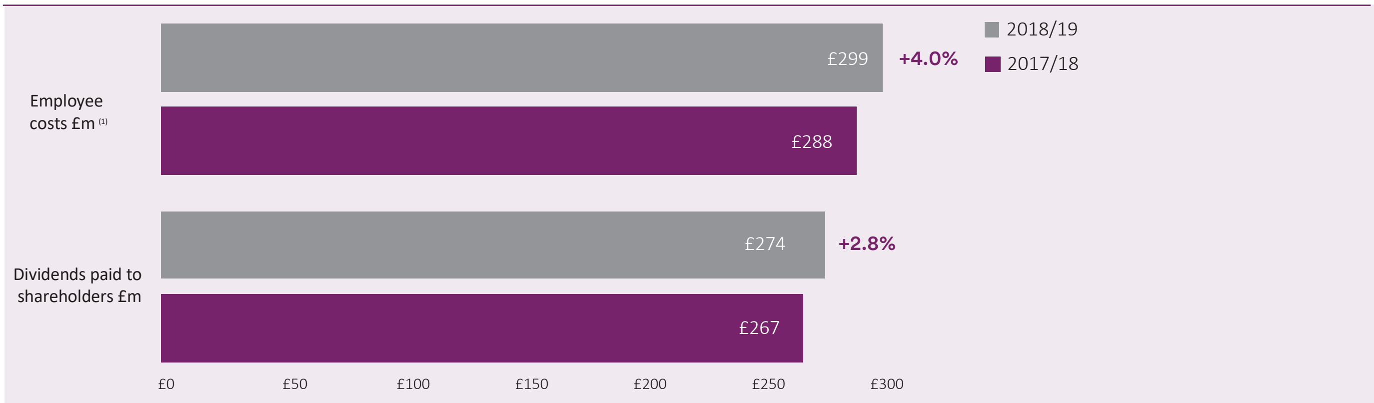
Date of service contracts

Executive directors	Date of service contract
Steve Mogford	5.1.11
Russ Houlden	1.10.10
Steve Fraser[1]	1.8.17

(1) Steve Fraser joined the company on 23 May 2005.

Relative importance of spend on pay

The table below shows the relative importance of spend on pay compared to distributions to shareholder.



(1) Employee costs includes wages and salaries, social security costs, and post-employment benefits.

Alignment of wider workforce pay

Percentage change in CEO's remuneration versus the wider workforce

The figures below show how the percentage change in the CEO's salary, benefits and bonus earned in 2017/18 and 2018/19 compares with the percentage change in the average of each of those components for a group of employees.

Change in CEO remuneration

Base salary(1)	Bonus(2)	Benefits(2)
+2.0%	+7.8%	-3.6%

Change in employee remuneration(3)

Base salary(4)	Bonus	Benefits(5)
+4.3%	+11.3%	+16.9%

(1) On 1 September 2018, Steve Mogford received a base salary increase of 2.0 per cent.
(2) See page 132 for further details.
(3) To aid comparison, the group of employees selected by the committee are all those members of the workforce who were employed over the complete two-year period.
(4) Includes promotional increases. The headline salary increase for employees was 3.0 per cent.
(5) The increase in benefits for employees mainly relates to the alignment of life assurance benefits with effect from 1 April 2018, which improved the value of the benefit package for a large number of employees. Additionally, a large number of employees became eligible for group income protection benefits with effect from 1 April 2018.

Cascade of remuneration through the organisation

	Executive directors	Executive committee	Senior leaders	Management	Wider workforce	Graduates	Apprentices
Base salary	✓	✓	✓	✓	✓	✓	✓
Annual bonus – cash	✓	✓	✓	✓	✓	✓	✓
Annual bonus – deferred shares	✓	✓	×	×	×	×	×
Long Term Plan(1)	✓	✓	✓	×	×	×	×
Pension	✓	✓	✓	✓	✓	✓	✓
Life cover and ill health benefits	✓	✓	✓	✓	✓	✓	✓
Company-funded healthcare	✓	✓	✓	✓	✓	✓	✓
ShareBuy	✓	✓	✓	✓	✓	✓	✓
Other benefits	✓	✓	✓	✓	✓	✓	✓

(1) Long Term Plan grants for senior leaders are made annually on a selective basis.

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Non-executive directors

Single total figure of remuneration for non-executive directors (audited information)

	Salary/fees £'000		Taxable benefits £'000		Total £'000	
Year ended 31 March	**2019**	2018	**2019**	2018	**2019**	2018
Dr John McAdam	**307**	300	**1**	2	**308**	302
Stephen Carter	**78**	76	**0**	0	**78**	76
Mark Clare	**80**	78	**0**	2	**80**	80
Alison Goligher	**66**	65	**0**	0	**66**	65
Brian May	**82**	81	**0**	2	**82**	83
Paulette Rowe[1]	**66**	49	**0**	0	**66**	49
Sara Weller	**80**	78	**0**	0	**80**	78

(1) Paulette Rowe joined the board on 1 July 2017.

Fees

Non-executive director annual fee rates were reviewed and increased with effect from 1 September 2018 as shown below. Base fees were increased by 2.0 per cent which is lower than the 3.0 per cent increase applying to the general workforce in 2018. Additional fees for the senior independent non-executive director and the chairs of committees were not increased.

	Fees £'000	
Role	**1 Sept 2018**	1 Sept 2017
Base fee: Chairman[1]	**309.0**	303.0
Base fee: other non-executive directors[2]	**66.9**	65.6
Senior independent non-executive director[2]	**13.5**	13.5
Chair of audit and treasury committees[2]	**16.0**	16.0
Chair of remuneration committee[2]	**13.5**	13.5
Chair of corporate responsibility committee[2]	**12.0**	12.0

(1) Approved by the remuneration committee.
(2) Approved by a separate committee of the board.

Non-executive directors' shareholding (audited information)

Details of beneficial interests in the company's ordinary shares as at 31 March 2019 held by each of the non-executive directors and their connected persons are set out in the table below.

Non-executive directors	Date first appointed to the board	Number of shares owned outright (including connected persons) at 31 March 2019[1]
Dr John McAdam	4.2.08	1,837
Stephen Carter	1.9.14	3,075
Mark Clare	1.11.13	7,628
Alison Goligher	1.8.16	3,000
Brian May	1.9.12	3,000
Paulette Rowe	1.7.17	3,000
Sara Weller	1.3.12	11,000

(1) From 1 April 2019 to 21 May 2019 there have been no movements in the shareholdings of the non-executive directors.

The remuneration committee

Summary terms of reference

The committee's terms of reference were last reviewed in November 2018 and are available on our website: **corporate.unitedutilities.com/corporate-governance**

The committee's main responsibilities include:

- determining and recommending to the board the policy for executive director remuneration, having reviewed and taken into account workforce remuneration and related policies and the alignment of incentives and reward with culture;
- setting the individual employment and remuneration terms for executive directors and other senior executives, including: recruitment and severance terms, bonus plans and targets, and the achievement of performance against targets;
- approving the general employment and remuneration terms for selected senior employees;
- setting the remuneration of the Chairman;
- proposing all new long-term incentive schemes for approval of the board, and for recommendation by the board to shareholders; and
- assisting the board in reporting to shareholders and undertaking appropriate discussions as necessary with institutional shareholders on aspects of executive remuneration.

Composition of the remuneration committee

Member	Member since	Member to
Sara Weller (chair since 27.7.12)	1.3.12	To date
Mark Clare	1.9.14	To date
Alison Goligher	1.8.16	To date
Brian May	16.5.17	To date

The committee's members have no personal financial interest in the company other than as shareholders and the fees paid to them as non-executive directors.

Support to the remuneration committee

By invitation of the committee, meetings are also attended by the Chairman of the company, the CEO, the company secretary (who acts as secretary to the committee), the customer services and people director and the head of reward and pensions, who are consulted on matters discussed by the committee, unless those matters relate to their own remuneration. Advice or information is also sought directly from other employees where the committee feels that such additional contributions will assist the decision-making process.

The committee is authorised to take such internal and external advice as it considers appropriate in connection with carrying out its duties, including the appointment of its own external remuneration advisers.

During the year, the committee was assisted in its work by the following external adviser:

Adviser	Appointed by	How appointed	Services provided to the committee in year ended 31 March 2019	Fees paid by company for these services in respect of year and basis of charge
New Bridge Street	Committee	Reappointed following committee review in 2013	General advice on remuneration matters and support for the directors' remuneration policy review	£205,000 on a time/cost basis
Other services provided to the company: Benchmarking of roles not under the committee's remit, provision of market information relevant to the price review submission and advice on non-executive director remuneration				

The independent consultants New Bridge Street (a trading name of Aon Hewitt Limited, an Aon PLC company) are members of the Remuneration Consultants Group and, as such, voluntarily operate under the Code of Conduct in relation to executive remuneration consulting in the UK. The committee is satisfied that the advice they received from external advisers is objective and independent.

In addition, during the year the law firm Eversheds Sutherland provided advice on the company's share schemes to the company.

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Key activities of the remuneration committee over the past year

The committee met seven times in the year ended 31 March 2019.

Regular activities

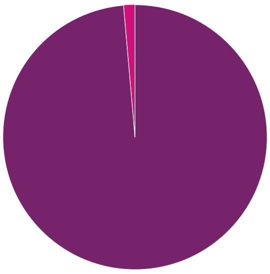
- Approved the 2017/18 directors' remuneration report;
- Reviewed the pay comparator group;
- Reviewed the base salaries of executive directors and other members of the executive team;
- Reviewed the base fee for the Chairman;
- Assessed the achievement of targets for the 2017/18 annual bonus scheme, reviewed progress against the targets for the 2018/19 annual bonus scheme, and set the targets for the 2019/20 annual bonus scheme;
- Assessed the achievement of targets for the Long Term Plan (LTP) awards made in 2015 and set the targets for LTP awards made in 2018;
- Reviewed and approved awards made under the annual bonus scheme, Deferred Bonus Plan (DBP) and LTP;
- Monitored progress against shareholding guidelines for executive directors and other members of the executive team;
- Reviewed the committee's performance during the period;
- Amended the committee's terms of reference, taking account of best practice and changes introduced by the 2018 UK Corporate Governance Code, including the committee assuming responsibility for the setting of remuneration for all members of the executive team;
- Considered governance developments and market trends in executive remuneration, including in the wider utilities sector; and
- Noted progress on the company's gender pay gap reporting.

Other activities

- Reviewed the executive pay arrangements and consulted with shareholders on the proposed remuneration policy;
- Reviewed the shareholding guidelines; and
- Agreed to align pension arrangements for future executive directors with those of the wider workforce.

2018 AGM: Statement of voting

At the last Annual General Meeting on 27 July 2018, votes on the 2017/18 directors' remuneration report (other than the part containing the directors' remuneration policy) were cast as follows:



Votes for **438,000,676**
(98.64% of votes cast)

Votes against **6,060,476**
(1.36% of votes cast)

444,061,152
Total votes cast

779,222
Votes withheld (abstentions)

The directors' remuneration report was approved by the board of directors on 21 May 2019 and signed on its behalf by:

Sara Weller
Chair of the remuneration committee

Corporate governance report

Appendix 1: Executive directors' share plan interests 1 April 2018 to 31 March 2019

	Award date	Awards held at 1 April 2018	Granted in year	Vested in year	Lapsed/ forfeited in year	Notional dividends accrued in year[1]	**Awards held at 31 March 2019**
Steve Mogford							
Shares not subject to performance conditions at 31 March 2019							
DBP	16.6.15	41,627	–	41,627	–	–	–
DBP	16.6.16	29,485	–	–	–	1,583	31,068
DBP	16.6.17	42,735	–	–	–	2,296	45,031
DBP[2]	18.6.18	–	47,057	–	–	2,527	49,584
LTP	29.7.13	48,700	–	48,700	–	–	–
LTP	30.6.14	63,029	–	–	–	3,386	66,415
LTP	30.6.15	108,300	–	–	50,073	4,994	63,221
ShareBuy matching shares[3]	1.4.18 to 31.3.19	39	47	39	–	–	47
Subtotal		**333,915**	**47,104**	**90,366**	**50,073**	**14,786**	**255,366**
Shares subject to performance conditions at 31 March 2019							
LTP	28.6.16	104,863	–	–	–	5,633	110,496
LTP	27.6.17	105,426	–	–	–	5,663	111,089
LTP[4]	25.6.18	–	129,030	–	–	2,123	131,153
Subtotal		**210,289**	**129,030**	**0**	**0**	**13,419**	**352,738**
TOTAL		**544,204**	**176,134**	**90,366**	**50,073**	**28,205**	**608,104**
Russ Houlden							
Shares not subject to performance conditions at 31 March 2019							
DBP	16.6.15	26,277	–	26,277	–	–	–
DBP	16.6.16	18,440	–	–	–	990	19,430
DBP	16.6.17	26,816	–	–	–	1,440	28,256
DBP[2]	18.6.18	–	29,517	–	–	1,585	31,102
LTP	29.7.13	30,733	–	30,733	–	–	–
LTP	30.6.14	39,784	–	–	–	2,136	41,920
LTP	30.6.15	68,373	–	–	31,613	3,153	39,913
ShareBuy matching shares[3]	1.4.18 to 31.3.19	38	48	38	–	–	48
Subtotal		**210,461**	**29,565**	**57,048**	**31,613**	**9,304**	**160,669**
Shares subject to performance conditions at 31 March 2019							
LTP	28.6.16	66,183	–	–	–	3,554	69,737
LTP	27.6.17	66,561	–	–	–	3,575	70,136
LTP[4]	25.6.18	–	81,488	–	–	1,340	82,828
Subtotal		**132,744**	**81,488**	**0**	**0**	**8,469**	**222,701**
TOTAL		**343,205**	**111,053**	**57,048**	**31,613**	**17,773**	**383,370**
Steve Fraser							
Shares not subject to performance conditions at 31 March 2019							
DBP	16.6.15	10,197	–	10,197	–	–	–
DBP	16.6.16	8,085	–	–	–	433	8,518
DBP	16.6.17	10,702	–	–	–	574	11,276
DBP[2]	18.6.18	–	22,043	–	–	1,184	23,227
LTP	30.6.15	25,651	–	14,731	11,860	940	–
ShareBuy matching shares[3]	1.4.18 to 31.3.19	43	48	43	–	–	48
Subtotal		**54,678**	**22,091**	**24,971**	**11,860**	**3,131**	**43,069**
Shares subject to performance conditions at 31 March 2019							
LTP	28.6.16	24,842	–	–	–	1,333	26,175
LTP	27.6.17	24,986	–	–	–	1,342	26,328
LTP[4]	25.6.18	–	75,339	–	–	1,239	76,578
Subtotal		**49,828**	**75,339**	**0**	**0**	**3,914**	**129,081**
TOTAL		**104,506**	**97,430**	**24,971**	**11,860**	**7,045**	**172,150**

(1) Note that these are also subject to performance conditions where applicable.

(2) See page 134 for further details.

(3) Under ShareBuy, matching shares vest provided the employee remains employed by the company one year after grant. During the year Steve Mogford purchased 238 partnership shares and was awarded 47 matching shares (at an average share price of 757 pence per share). Russ Houlden purchased 238 partnership shares and was awarded 48 matching shares (at an average share price of 757 pence per share). Steve Fraser purchased 237 partnership shares and was awarded 48 matching shares (at an average share price of 757 pence per share).

(4) See page 136 for further details.

Corporate governance report
Tax policies and objectives

Our tax policies and objectives, which are approved by the board on an annual basis, ensure that we:

- Only engage in reasonable tax planning aligned with our commercial activities and we always comply with what we believe to be both the letter and the spirit of the law;
- Do not engage in marketed, aggressive or abusive tax avoidance;
- Do not use tax havens for tax avoidance purposes;
- Are committed to an open, transparent and professional relationship with HMRC based on mutual trust and collaborative working; and
- Maintain a robust governance and risk management framework to ensure that these policies and objectives are fully complied with and applied at all levels

We expect to fully adhere to the HMRC framework for co-operative compliance.

Our Chief Financial Officer (CFO) has responsibility for tax governance with oversight from the board. The CFO is supported by a specialist team of tax professionals with many years of tax experience within the water sector and led by the Head of Tax. The Head of Tax has day-to-day responsibility for managing the group's tax affairs and engages regularly with key stakeholders from around the group in ensuring that tax risk is proactively managed. Where appropriate, he will also engage with both external advisers and HMRC to provide additional required certainty with the aim of ensuring that any residual risk is typically low. All significant tax issues are reported to the board regularly.

Consistent with the group's general risk management framework, all tax risks are assessed for the likelihood of occurrence and the negative financial or reputational impact on the group and its objectives, should the event occur. In any given period, the key tax risk is likely to be the introduction of unexpected legislative or tax practice changes which lead to increased cash outflow which has not been reflected in the current regulatory settlement. The group is committed to actively engaging with relevant authorities in order to manage any such risk.

In any given year, the group's effective cash tax rate on underlying profits may fluctuate from the standard UK rate due to the available tax deductions on capital investment and pension contributions. These deductions are achieved as a result of utilising tax incentives, which have been explicitly put in place by successive governments precisely to encourage such investment. This reflects responsible corporate behaviour in relation to taxation.

Under the regulatory framework the group operates within, the majority of any benefit from reduced tax payments will typically not be retained by the group but will pass to customers; reducing their bills. For 2018/19, the impact of tax deductions on capital investment alone reduced average household bills by around £25.

The group's principal subsidiary, United Utilities Water Limited (UUW), operates solely in the UK and its customers are based here. All of the group's profits are taxable in the UK (other than profits relating to the group's 35 per cent holding in Tallinn Water which are fully taxable in Estonia).

The investment in Tallinn Water is directly held via United Utilities (Tallinn) BV, a Dutch holding company. There is no tax advantage to this historic intermediate holding company and the only income of the Dutch company is the annual dividends received from Tallinn Water of around £2 million, which are fully taxable within Estonia and wholly paid onto the UK. The group's only other overseas subsidiary is a dormant company resident in Thailand, where the group had historic trading operations. This company is in the process of being dissolved and has no income.

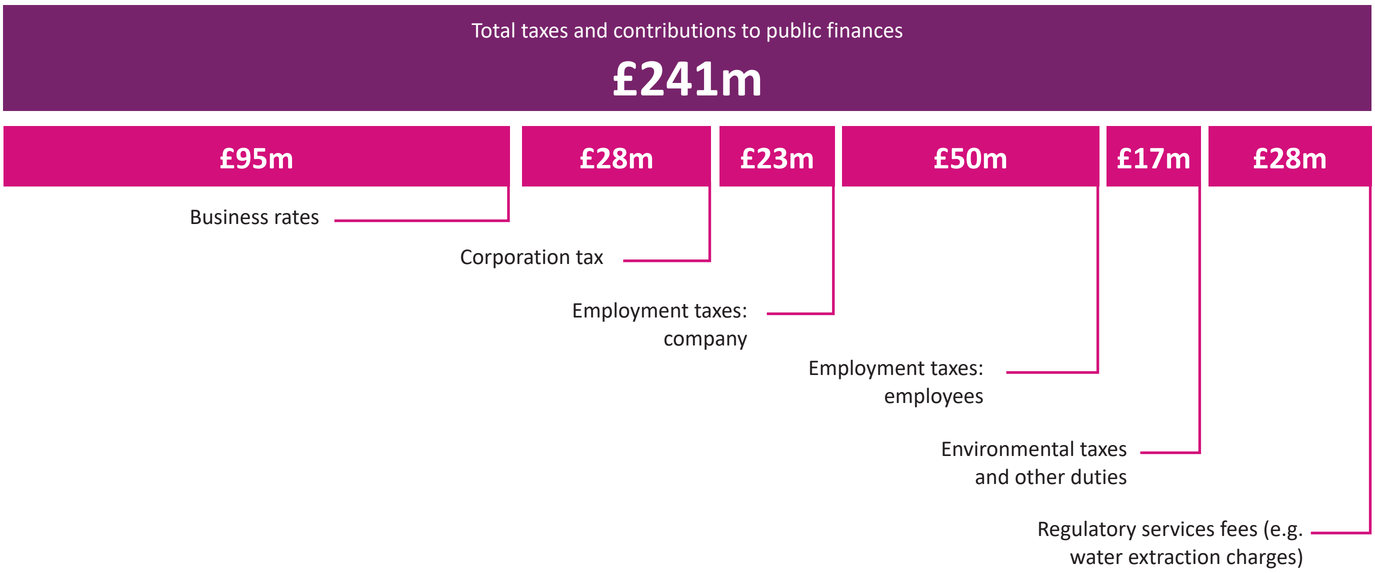
Every year, the group pays significant contributions to the public finances on its own behalf as well as collecting and paying over further amounts for its 5,000-strong workforce. Details of the total payments for 2019 of around £241 million are set out below.

We expect the above details, which apply for the year ended 31 March 2019, to fully comply with the new legislative requirements for 'Publication of Group Tax Strategies' for UK groups.

From summer 2019, the group will also now be publishing a separate dedicated annual tax report on our website, which will include further details in relation to the following key areas:

- How much tax we pay;
- How we ensure that we pay the right tax at the right time; and
- How we ensure our tax affairs are transparent for all our stakeholders.

Taxes/contributions to public finances for 2019



Directors' report
Energy and carbon

Carbon emissions	Operational energy use	Renewable energy generation
167,856	**976GWh**	**173GWh**
tonnes CO_2 equivalent (tCO_2e) 71 per cent below our 2005/06 baseline	underlying energy use that is used to calculate GHG emissions	equivalent to 21 per cent of our electricity consumption

Greenhouse gas emissions reporting

We measure and report our greenhouse gas (GHG) emissions of the six Kyoto Protocol gases that result from all United Utilities' operational activities in the UK. There are no material omissions.

We report as required under the Companies Act 2006 (Strategic Report and Directors' Reports) Regulations. We follow the 2019 UK Government Environmental Reporting Guidelines: Including streamlined energy and carbon reporting guidance and the GHG Protocol Corporate Accounting and Reporting Standard (2015).

In line with the recommendations of the Taskforce on Climate-related Financial Disclosure (TCFD), we are reporting scope 1, 2 and 3 emissions, our methodology and targets.

Our reporting is compliant with the international carbon reporting standard (ISO 14064, Part 1) and assured by the Certified Emissions Measurement and Reduction Scheme (CEMARS).

How we measure our greenhouse gas emissions

A carbon footprint is calculated by converting all emissions of Kyoto Protocol gases into a carbon dioxide equivalent (CO_2e). Emissions are categorised as direct, indirect or avoided emissions.

Direct emissions (scope 1 emissions) are those from activities we own or control including those from our treatment processes, company vehicles, burning of fossil fuels for heating and incineration of sewage sludge.

Indirect emissions, known as scope 2 and 3 emissions, result from operational activities we do not own or control. These include emissions produced as a consequence of electricity we purchase to power our treatment plants (scope 2) and other indirect emissions such as travel on company business (scope 3).

Avoided emissions are reductions from the purchase, or export, of renewable energy.

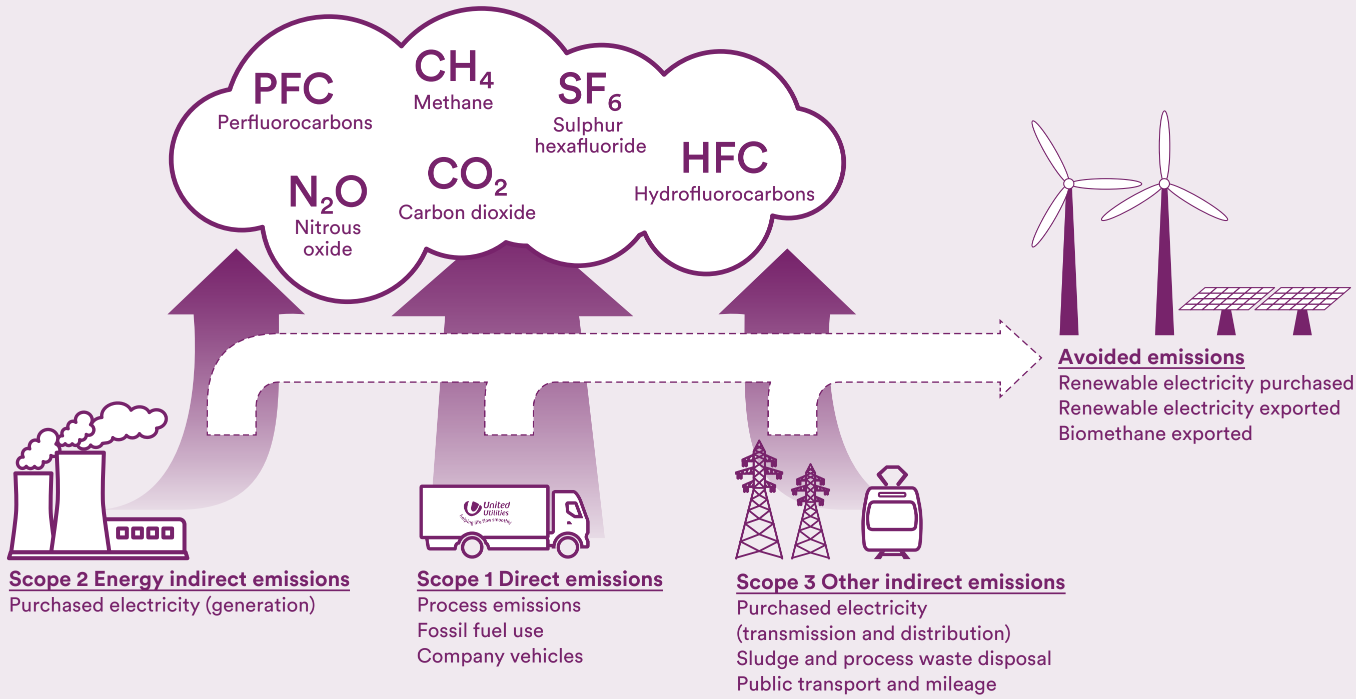
Gross emissions are the sum of all three scopes. Net emissions are the gross emissions minus reductions from avoided emissions.

The GHG Protocol recommends using two methods to quantify emissions – the 'location-based' method which uses average grid electricity emissions factors and the 'market-based' method which is specific to the actual electricity purchased. From this year we will report results using both methods and will adopt the gross 'market-based' figure to report our headline carbon emissions.

Intensity measurement

As in previous years we state our carbon emissions as tonnes CO_2e per £million revenue. This year we have also reported the metric tonnes CO_2e per megalitre (using the location-based method) broken down by clean water and wastewater, as these are common metrics for our industry.

Greenhouse gas emissions by scope



Directors' report
Energy and carbon

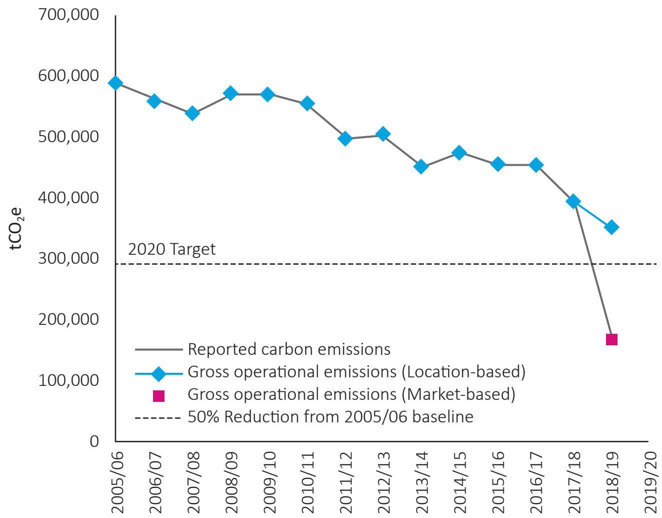
Emissions target

By 2020 we aim to reduce our greenhouse gas emissions by 50 per cent from the 2005/06 baseline and to achieve a 60 per cent reduction by 2035. We are pleased to report that for 2018/19 our carbon emissions were 167,856 tCO_2e, 71 per cent below the 2005/06 baseline.

We have achieved our emission target early as a result of purchasing certified renewable electricity, with over 95 per cent of the electricity we use having zero emissions. We will now focus on our remaining emissions, the majority of which are from processing wastewater and the treatment and disposal of sludge.

In line with our refreshed environmental policy, published in October 2018, we recognise our obligation to mitigate climate change and will continue to explore ways to lower our GHG emissions. We will set a new science based emissions target and evolve our reporting in line with expectations to achieve net zero emissions.

Our carbon footprint since 2005/06



United Utilities' greenhouse gas emissions

		Current year 2018/19 tCO_2e	Previous years 2017/18 tCO_2e[(2)]	2016/17 tCO_2e	Baseline Year 2005/06 tCO_2e
Scope 1 Direct emissions					
Direct emissions from burning of fossil fuels		16,809	14,324	20,848	17,638
Process emissions from our treatment plants – including refrigerants		88,136	91,456	96,019	125,032
Transport: company owned or leased vehicles		14,409	11,803	11,783	7,514
Total Scope 1 Direct emissions		**119,354**	**117,583**	**128,649**	**150,183**
Scope 2 Energy indirect emissions					
Grid electricity purchased – generation	Market-based[(1)]	18,503	28,287		
	Location-based	187,171	230,167	277,726	357,660
Total Scope 2 Energy indirect emissions		**18,503**	**230,167**	**277,726**	**357,660**
Scope 3 Other indirect emissions					
Business travel (public transport and private vehicles)		2,236	2,504	2,889	2,374
Emissions from sludge and process waste disposal		26,186	23,048	17,915	42,712
Grid electricity purchased – transmission and distribution	Market-based[(1)]	1,577	2,644		
	Location-based	15,955	21,520	25,120	33,088
Total Scope 3 Other indirect emissions		**29,999**	**47,072**	**45,924**	**78,174**
GROSS CARBON EMISSIONS[(3)]		**167,856**	**394,822**	**452,301**	**586,017**
Avoided emissions from renewable electricity exported		(3,434)	(2,303)	(4,417)	(1,597)
Avoided emissions from biomethane exported		(8,446)	(8,577)	(3,240)	–
Avoided emissions from renewable electricity purchased	Location based	(168,667)	(173,876)	–	–
Total avoided emissions		**(11,880)**	**(184,756)**	**(7,657)**	**(1,597)**
NET CARBON EMISSIONS[(3)]		**155,976**	**210,066**	**444,644**	**584,420**

(1) Market-based figures for electricity purchased on a standard tariff have been calculated using specific emissions factors from published generator fuel mix disclosures.
(2) 2017/18 figures are restated recognising the purchase of renewable electricity during that year and calculated using the market-based method.
(3) Operational emissions for baseline and previous years use the location-based method and current year uses the market-based method.

United Utilities' greenhouse gas emissions intensity

		Current year 2018/19	Previous year 2017/18	Baseline year 2005/06
Carbon emissions per £m revenue	tCO_2e	**92.3**	225.6	280.9
Operational emissions per megalitre of treated water	Kg CO_2e/Ml	**38.22**	60.43	
Operational emissions per megalitre of sewage treated	Kg CO_2e/Ml	**102.43**	116.75	

Energy use

The underlying energy data used to calculate our carbon emissions includes electricity, gas and other fuels purchased for use on-site and for transport.

This year we used 976GWh of energy. The prolonged dry and warm conditions from January 2018 increased customer demand for water and required more pumping to move water around our integrated network. As a result, we estimate that we used up to 30GWh more electricity.

We generated the equivalent of 173GWh of renewable electricity, an increase of 6GWh on last year. We achieved this with a mix of generation from wind, hydro, solar photovoltaics and energy recovery from bioresources (using sewage sludge to power combined heat and power generators).

We continued to invest in our generation capability with nine new solar installations coming on line during the year. Most of the energy we generate is used to power our operations, but where there is excess or it makes commercial sense to do so we export to the grid. We are exploring emerging technologies such as batteries and electric vehicles and investigating how systems thinking and artificial intelligence might optimise our energy use and generation.

Energy use and generation

	GWh
Energy use	
Electricity	807.8
Gas	33.0
Other fuels (e.g. for transport)[1]	135.0
Total energy use[2]	**975.8**
Electricity purchased	
Renewable 0 CO_2 g/kWh	601.5
Supplier Standard Tariff 310 CO_2 g/kWh	59.7
Total electricity purchased	**661.2**
Renewable energy generated	
CHP	115.7
Solar	34.6
Wind	4.8
Hydro	4.6
Biomethane[3]	13.2
Total renewable energy generated	**172.9**
Renewable energy exported	
Electricity	13.0
Biomethane[3]	13.2
Total renewable energy exported	**26.2**

(1) Energy use for other fuels includes fuel used in processing and transport plus business mileage in private vehicles converted to GWh using UK Government GHG Conversion Factors for Company Reporting.
(2) Underlying energy use that is used to calculate GHG emissions.
(3) Biomethane generated and exported to grid is expressed as an electricity equivalent.

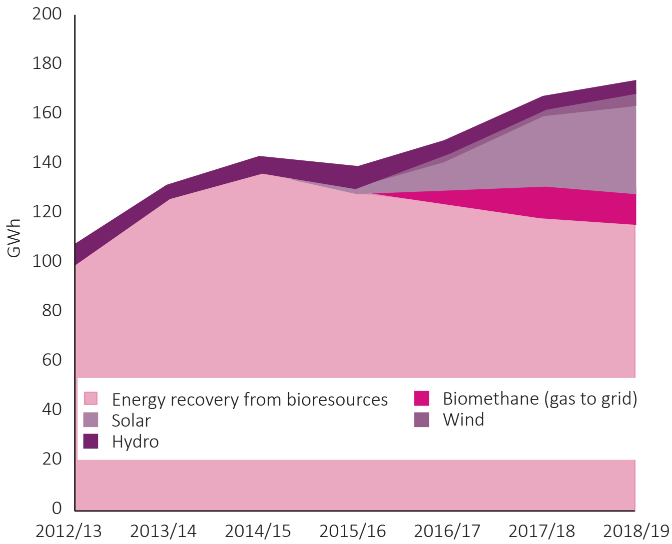
Energy efficiency action taken

Our energy management strategy aims to achieve an appropriate balance between managing our energy consumption, use of renewables and self-generation and being smart about how we operate our assets to get best value while maintaining security of supply.

A key activity in the last year has been assessing and improving energy management planning at both local and regional levels. For instance, at a local level, the United Utilities energy standard has been developed and roll-out is well under way. This is a simple assessment that enables sites to understand current energy management practices and identify where improvements can be made. Supporting this are energy engineers who identify energy efficiency opportunities and share their knowledge of best practice with our teams across the region.

At a regional level, we have increased the weighting that energy consumption has in investment and operational decision-making. This began with raising awareness of actual energy consumption and generation by using the now well-established energy management information portal. With timely, accurate and consistent data, supplemented by trials using energy monitoring and control tools, it has been possible to better understand the local and broader energy impacts of our business decisions and improve how we balance business needs and energy use.

Renewable energy generation by technology



Directors' report
Statutory and other information

Governance

Our directors present their management report, including the strategic report, on pages 10 to 77 and the audited financial statements of United Utilities Group PLC (the company) and its subsidiaries (together referred to as the group) for the year ended 31 March 2019.

Business model	A description of the company's business model can be found within the strategic report on pages 24 to 38.
Dividends	Our directors are recommending a final dividend of 27.52 pence per ordinary share for the year ended 31 March 2019, which, together with the interim dividend of 13.76 pence, gives a total dividend for the year of 41.28 pence per ordinary share (the interim and final dividends paid in respect of the 2017/18 financial year were 13.24 pence and 39.73 pence per ordinary share respectively). Subject to approval by our shareholders at our AGM, the final dividend will be paid on 1 August 2019 to shareholders on the register at the close of business on 21 June 2019.
Directors	The names of our directors who served during the financial year ended 31 March 2019 can be found on pages 80 to 83. Sir David Higgins was appointed on 13 May 2019.
Reappointment	Our articles of association provide that our directors must retire at every annual general meeting following their last election or reappointment by our shareholders which is consistent with the recommendation contained within the 2016 UK Corporate Governance Code ('the Code') that all directors should be subject to annual election by shareholders. This has been the case at all the AGMs since 2011. Information regarding the appointment of our directors is included in our corporate governance report on pages 94 to 97.
Interests	Details of the interests in the company's shares held by our directors and persons connected with them are set out in our directors' remuneration report on pages 116 to 143 which is hereby incorporated by reference into this directors' report.
Corporate governance statement	The corporate governance report on pages 80 to 115 is hereby incorporated by reference into this directors' report and includes details of our compliance with the Code. Our statement includes a description of the main features of our internal control and risk management systems in relation to the financial reporting process and forms part of this directors' report. A copy of the 2016 version of the Code, as applicable to the company for the year ended 31 March 2019, can be found at the Financial Reporting Council's website frc.org.uk. Copies of the matters reserved for the board and the terms of reference for each of the main board committees can be found on our website.
Share capital	At 31 March 2019, the issued share capital of the company was £499,819,926 divided into 681,888,418 ordinary shares of 5 pence each and 273,956,180 deferred shares of 170 pence each. Details of our share capital and movements in our issued share capital are shown in note 23 to the financial statements on page 186. The ordinary shares represented 71.3 per cent and the deferred shares represented 28.7 per cent respectively of the shares in issue as at 31 March 2019. All our ordinary shares have the same rights, including the rights to one vote at any of our general meetings, to an equal proportion of any dividends we declare and pay, and to an equal amount of any surplus assets which are distributed in the event of a winding-up. Our deferred shares convey no right to income, no right to vote and no appreciable right to participate in any surplus capital in the event of a winding-up. The rights attaching to our shares in the company are provided by our articles of association, which may be amended or replaced by means of a special resolution of the company in general meeting. The company renews annually its power to issue and buy back shares at our AGM and such resolutions will be proposed at our 2019 AGM. Our directors' powers are conferred on them by UK legislation and by the company's articles. At the AGM of the company on 27 July 2018, the directors were authorised to issue relevant securities up to an aggregate nominal amount of £11,364,806 and were empowered to allot equity securities for cash on a non-pre-emptive basis to an aggregate nominal amount of £1,704,721.
Voting	Electronic and paper proxy appointment and voting instructions must be received by our registrars (Equiniti) not less than 48 hours before a general meeting and when calculating this period, the directors can decide not to take account of any part of a day that is not a working day.
Transfers	There are no restrictions on the transfer of our ordinary shares in the company, nor any limitations on the holding of our shares in the company, save: (i) where the company has exercised its right to suspend their voting rights or to prohibit their transfer following the omission of their holder or any person interested in them to provide the company with information requested by it in accordance with Part 22 of the Companies Act 2006; or (ii) where their holder is precluded from exercising voting rights by the Financial Conduct Authority's Listing Rules or the City Code on Takeovers and Mergers. There are no agreements known to us between holders of securities that may result in restrictions on the transfer of securities or on voting rights. All our issued shares are fully paid.

Major shareholdings	At 22 May 2019, our directors had been notified of the following interests in the company's issued ordinary share capital in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority:

	Per cent of issued share capital	Direct or indirect nature of holding
Lazard Asset Management LLC	8.03	Indirect
BlackRock Inc.	5.13	Indirect
Norges Bank	3.03	Direct

Purchase of own shares	At our last AGM held on 27 July 2018, our shareholders authorised the company to purchase, in the market, up to 68,188,841 of our ordinary shares of 5 pence each. We did not purchase any shares under this authority during the year. We normally seek such an authority from our shareholders annually. At our 2019 AGM, we will again seek authority from our shareholders to purchase up to 68,188,841 of our ordinary shares of 5 pence each with such authority expiring at the end of our AGM held in 2020.
Change of control	As at 31 March 2019, Equiniti Trust (Jersey) Limited was the trustee that administered our executive share plans and had the ability to exercise voting rights at its discretion which related to shares that it held under the trust deed constituting the trust. In the event of a takeover offer which could lead to a change of control of the company, the trustee must consult with the company before accepting the offer or voting in favour of the offer. Subject to that requirement, the trustee may take into account a prescribed list of interests and considerations prior to making a decision in relation to the offer, including the interests of the beneficiaries under the trust. In the event of a change of control, the participants in our all-employee share incentive plan (ShareBuy) would be able to direct the trustee of ShareBuy, Equiniti Share Plan Trustees Limited, how to act on their behalf.
Information required by UK Listing Rule 9.8.4	Details of the amount of interest capitalised by the group during the financial year can be found in note 6 to the financial statements on page 175. In line with current UK tax legislation, the amount is fully deductible against the group's corporation tax liability, resulting in tax relief of £7.1 million. There are no other disclosures to be made under Listing Rule 9.8.4.
Directors' indemnities and insurance	We have in place contractual entitlements for the directors of the company and of its subsidiaries to claim indemnification by the company in respect of certain liabilities which might be incurred by them in the course of their duties as directors. These arrangements, which constitute qualifying third-party indemnity provision and qualifying pension scheme indemnity provision, have been established in compliance with the relevant provisions of the Companies Act 2006 and have been in force throughout the financial year. They include provision for the company to fund the costs incurred by directors in defending certain claims against them in relation to their duties as directors of the company or its subsidiaries. The company also maintains an appropriate level of directors' and officers' liability insurance.
Political donations	We do not support any political party and do not make what are commonly regarded as donations to any political party or other political organisations. 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 group and our political stakeholders. This includes promoting United Utilities' activities at the main political parties' annual conferences, and occasional stakeholder engagement in Westminster. The group incurred expenditure of £9,338 (2018: £21,662) as part of this process. At the 2018 AGM, an authority was taken to cover such expenditure. A similar resolution will be put to our shareholders at the 2019 AGM to authorise the company and its subsidiaries to make such expenditure.
Trade associations	We are members of a small number of trade associations. Some of these have a national focus, such as Water UK, the representative body of the UK water industry, which considers industry-wide priorities such as development of markets, customer trust, resilience, and legislation and regulation, and the Confederation of British Industry, which provides a policy-making voice for firms at a regional, national and international level. Others focus on specific professions such as the 100 Group representing the views of the finance directors of FTSE 100 and large UK private companies and the GC 100, the voice of general counsel and company secretaries in FTSE 100 companies. The company is also a member of regional bodies, such as the North West Business Leadership Team which encourages engagement across the public and private sectors to promote the sustainable economic development and long-term well-being of the North West. Our total contribution to these associations in 2018/19 was £399,658 (2017/18: £389,743).

Directors' report
Statutory and other information

Employees	Our policies on employee consultation and on equal opportunities for our disabled employees can be found in the 'People' section on page 32. The company's business principles make clear how the company and all our employees must seek to act with integrity and fairness and observe legal requirements. Anyone with serious concerns that the company may not be adhering to these principles is encouraged to speak up via their line manager or through a confidential telephone line. Importance is placed on strengthening employees' engagement (see page 42), measuring their views annually, then taking action to improve how they feel about the company and understand its direction. Employees are provided with information, through briefings and access to other online materials, to enable them to understand the financial and economic factors affecting the company's performance. Furthermore, Alison Goligher has been designated as the non-executive director for leading the board's engagement with the workforce. Amongst other initiatives, an Employee Voice Panel has been established, chaired by Alison; meetings will be held quarterly with the venue rotating around our region. The Panel will consist of *circa* 30 employees elected from across all employee segment groups and geographical areas. Panel members will be re-elected approximately every two years. The objectives of the Panel are to: provide the opportunity for a two-way channel of communication between the board and the workforce; provide insight to the board on how people think and feel about working for the company; and contribute to the monitoring and assessment of the culture of the business. During the year, we have had regard to employee interests, consulting with employees and their representatives and trade union representatives in relation to new pension arrangements introduced on 1 April 2019 and consulting with employee representatives in relation to organisational changes for support and managerial roles. The effect of our regard towards employees in relation to the decisions taken during the financial year is included in our s172(1) Statement on page 152. Employees are encouraged to own shares in the company through the operation of an all employee share incentive plan (ShareBuy). Information on our average number of employees during the year, can be found in note 3 on page 173.
Environmental, social and community matters	Details of our approach, as a responsible business, is set out in our business principles, which can be found on our website at **unitedutilities.com/corporate/about-us/governance/business-principles/**. Our approach to engagement with our environmental stakeholders and those in the communities we serve can be found on pages 40 to 43. The effect of our regard towards the environment, social and community matters in relation to the decisions taken during the financial year is included in our s172(1) Statement on page 152.
Customers and suppliers and key stakeholders	Our approach to engagement with customers, suppliers, regulators and other key stakeholders can be found on pages 39 to 45. The effect of our regard towards customers, suppliers, regulators and other key stakeholders in relation to the decisions taken during the financial year is included in our s172(1) Statement on page 152. Our sustainable supply chain charter sets out how we work with our suppliers, which can be found on our website at: **unitedutilities.com/corporate/about-us/governance/suppliers/how-we-buy/sustainable-supply-chain/**, we are also a signatory to the Prompt Payment Code. We publish key statistics and other information on our payment practices in line with the Duty to Report on Payment Practices and Performance on the Department for Business, Energy & Industrial Strategy's website. Information is published on a six-monthly basis. For the six months to 31 March 2019, our average time taken to pay invoices was 24 days; in the previous six months it was 25 days.
Approach to technology development	We are committed to using innovative, cost-effective and practical solutions for providing high-quality services and we recognise the importance of ensuring that we focus our investment on the development of technology and that we have the right skills to apply technology to achieve sustainable competitive advantage and also that we continue to be alert to emerging technological opportunities.
Financial instruments	Our risk management objectives and policies in relation to the use of financial instruments can be found in note A4 on page 190.
Events occurring after the reporting period	Details of events after the reporting period are included in note 26 on page 186.
Slavery and human trafficking statement	Our statement can be found on our website at: **unitedutilities.com/human-rights**

Annual general meeting

Our 2019 annual general meeting (AGM) will be held on 26 July.

› Full details of the resolutions to be proposed to our shareholders, and explanatory notes in respect of these resolutions, can be found in our notice of AGM. A copy can be found on our website.

At our 2019 AGM, resolutions will be proposed, among other matters:

› to receive the annual report and financial statements; to approve the directors' remuneration report; to approve the directors' remuneration policy; to declare a final dividend; and to reappoint KPMG LLP as auditor; and
› to approve the directors' general authority to allot shares; to grant the authority to issue shares without first applying statutory rights of pre-emption; to authorise the company to make market purchases of its own shares; to authorise the making of limited political donations by the company and its subsidiaries; and to enable the company to continue to hold general meetings on not less than 14 working days' notice.

Information given to the auditor

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

› so far as he or she is aware, there is no relevant audit information of which the company's auditor is unaware; and
› he or she has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the company's auditor is aware of that information. This confirmation is given, and should be interpreted, in accordance with the provisions of s418 of the Companies Act 2006.

Reappointment of the auditor

Our board is proposing that our shareholders reappoint KPMG LLP as our auditor at the forthcoming AGM and authorises the audit committee of the board to set the auditor's remuneration.

Approved by the board on 22 May 2019 and signed on its behalf by:

Simon Gardiner
Company Secretary

Non-financial information statement

The table below constitutes the company's non-financial Information statement ('the statement'), produced to comply with sections 414CA(1) and 414CB(1) of the Companies Act 2006. The statement is incorporated into the strategic report by cross reference. Our business principles set out how we behave as a business and are applicable to the areas of disclosure required by s414CB(1). Our business principles can be found on our website: unitedutilities.com/corporate/about-us/governance/business-principles/. The stakeholder metrics table (see page 55) also includes data in relation to the areas of disclosure required by s414CB(1).

Reporting requirement	Information necessary to understand our business and its impact, policy, due diligence and outcomes	Policies, guidance and standards which govern our approach (some of which are only published internally)
Environmental matters	Reflecting the needs of the environment: › Natural resources – see page 28 › Natural environment – see page 28 › Reducing our carbon emissions – see pages 28-29	› Waste and resource use policy › Environmental policy – see page 29 › Water resources management plan – see page 48 › Emissions target – see page 146
Employees	Reflecting the needs of our employees: › Competitive base salaries and benefits - see page 93 › Health and safety – see page 6 › Mental well being – see page 33 › Gender pay report 2018 – see page 98 › Engagement – see pages 42 and 150 › Board diversity – see page 96	› Health and safety policy › Equality, diversity and inclusion policy › Flexible working arrangements › Agency worker policy › Mental well being policy › Human rights policy – see page 32 › Board diversity policy – see page 97
Respect for human rights	Reflecting the needs of our stakeholders: › Suppliers – see page 43. › Diversity within our workforce – see pages 32 and 98	› Employee data protection policy › Slavery and human trafficking statement › Human rights policy – see page 32
Social matters	Reflecting the needs of our stakeholders: › Customers – see pages 40 and 57 › Community – see page 40 › Environment – see pages 42 and 61 › Suppliers – see pages 42 and 148 › Regulators – see page 44	› YourVoice – see page 40 › Charitable matched funding guidance › Volunteering policy › Sustainable supply chain charter – see page 150 › Commercial procurement policy
Anti-corruption and anti-bribery	› Employees – see pages 36, 41 to 42 › Suppliers – see page 42	› Anti-bribery policy › Fraud investigation and reporting processes › Whistleblowing policy › Internal financial control processes › Commercial procurement policy

Directors' report
Statutory and other information

Introduction
Throughout this annual report, we provide examples of how we: take into account the likely consequences of long-term decisions; build relationships with stakeholders; understand the importance of engaging with our employees; understand the impact of our operations on the communities in our region and the environment we depend upon; and attribute importance to behaving as a responsible business.

Statement by the directors in performance of their statutory duties in accordance with s172(1) Companies Act 2006
The board of directors of United Utilities Group PLC consider, both individually and together, that they have acted in the way they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole (having regard to the stakeholders and matters set out in s172(1)(a-f) of the Act) in the decisions taken during the year ended 31 March 2019 (see pages 88 to 89). In particular, by reference to the approval of our business plan ('our plan') for the period 2020–25, supported by the board assurance statement accompanying our plan:

- Our plan was designed to have a long-term beneficial impact on the company and to contribute to its success in delivering a better quality, more reliable water and wastewater service for customers in the North West of England to 2025 and beyond. We will continue to operate our business within tight budgetary controls and in line with our regulatory targets. Our plan was awarded 'fast-track' status and commended in relation to: customer engagement, affordability and vulnerability, resilience and innovation (see pages 19 to 21).
- Our employees are fundamental to the delivery of our plan. We aim to be a responsible employer in our approach to the pay and benefits our employees receive. The health, safety and well-being of our employees is one of our primary considerations in the way we do business (see page 6).
- Our duty, in accordance with the Water Industry Act 1991, is to provide a safe and secure supply of water and return wastewater safely to the environment. Our plan was informed by extensive engagement with customers, enabling us to gain an understanding of their views and priorities, communicating and listening through new channels and underpinned by working with the independent customer challenge group YourVoice (see page 40). We have made a commitment to share the gains of out-performance with customers. We also aim to act responsibly and fairly in how we engage with: our suppliers (see page 42); our credit investors (see page 100); and co-operate with our regulators (see page 44); all of whom are, integral to the successful delivery of our plan.
- Our plan took into account the impact of the company's operations on the community and environment and our wider societal responsibilities, and in particular how we impact the regions we serve in the North West of England (see page 40). Several of the proposed performance measures in our plan will deliver environmental improvements.
- As the Board of Directors, our intention is to behave responsibly and ensure that management operate the business in a responsible manner, operating within the high standards of business conduct and good governance expected for a business such as ours (see pages 84 to 143) and in doing so, will contribute to the delivery of our plan. The intention is to nurture our reputation, through both the construction and delivery of our plan, that reflects our responsible behaviour.
- As the Board of Directors, our intention is to behave responsibly toward our shareholders and treat them fairly and equally, so they too may benefit from the successful delivery of our plan.

Statement of directors' responsibilities in respect of the annual report and the financial statements

The directors are responsible for preparing the annual report and the group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law they are required to prepare the group financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (EU) (IFRSs as adopted by the EU) and applicable law and have elected to prepare the parent company financial statements on the same basis.

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 group and parent company and of their profit or loss for that period. In preparing each of the group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a strategic report, directors' report, directors' remuneration report and corporate governance statement that comply with that law and those regulations.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility statement of the directors in respect of the annual financial report

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the strategic report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

We consider the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's position and performance, business model and strategy.

Approved by the board on 22 May 2019 and signed on its behalf by:

Dr John McAdam
Chairman

Russ Houlden
Chief Financial Officer

Financial statements

In this section you will find our full audited financial results for the year ended 31 March 2019

Sunrise over Castlerigg, near Keswick - photograph taken by our wastewater data and analytics colleague John King

Independent auditor's report to the members of United Utilities Group PLC only

1. Our opinion is unmodified

We have audited the financial statements of United Utilities Group PLC (the company) for the year ended 31 March 2019, which comprise the Consolidated income statement, the Consolidated statement of comprehensive income, the Consolidated and company statements of financial position, the Consolidated statement of changes in equity, the Company statement of changes in equity, the Consolidated and company statements of cash flows, and the related notes, including the accounting policies on pages 168 to 171 and 203 to 207.

In our opinion:

› the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 March 2019 and of the group's profit for the year then ended;

› the group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);

› the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and

› the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were first appointed as auditor by the shareholders on 22 July 2011. The period of total uninterrupted engagement is for the eight financial years ended 31 March 2019. We have fulfilled our ethical responsibilities under, and we remain independent of the group in accordance with, UK ethical requirements, including the FRC Ethical Standard as applied to listed public interest entities. No non-audit services prohibited by that standard were provided.

2. Key audit matters: including our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

Overview

Materiality: group financial statements as a whole	£20.0m (2018: £19.0m) 4.7% (2018: 4.9%) of normalised group profit before tax	
Coverage	98% (2018: 98%) of group profit before tax	
Risks of material misstatement		vs 2018
Recurring risks	Revenue recognition and allowance for household customer debt	◀ ▶
	Capitalisation of costs relating to the capital programme	◀ ▶
	Retirement benefit obligation valuation	◀ ▶
	Water Plus joint venture investment and loans carrying value	◀ ▶
	Recoverability of parent company's investment in United Utilities PLC	◀ ▶

	The risk	Our response
Revenue recognition and allowance for household customer debt Revenue not recognised: £18.0 million (2018: £20.3 million) Provision for household customer debt: £52.9 million (2018: £63.4 million) *Refer to page 108 (Audit committee report), note A7 and pages 170 and 171 (accounting policies)*	**At each balance sheet date:** › judgement is required to identify properties where there is little prospect that cash will be received for revenue that has been billed due to either the occupier not being able to be identified or a past history of non-payment of bills relating to that property and, therefore, whether the revenue should be recognised; and › assumptions involving a high degree of estimation uncertainty are required to assess the recoverability of trade receivables. The effect of these matters is that, as part of our risk assessment, we determined that the recoverability of trade receivables has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (see pages 170 and 171 accounting policies) disclose the sensitivities estimated by the group.	**Our procedures included:** › **Accounting analysis** – Assessing the recognition of revenue where the collection of consideration is not probable on the date of sale for compliance with relevant accounting standards; › **Control observation** – Testing the group's controls over revenue recognition and provision for household customer debt, including reconciliations between sales and cash receipts systems and the general ledger; › **Methodology choice** – Assessing the appropriateness of the customer debt provisioning policy based on historical cash collections, credits, re-bills and write-off information; and › **Assessing transparency** – Assessing the adequacy of the group's disclosures of its revenue recognition and household customer debt provisioning policies, including the judgement involved in recording revenue and estimation uncertainty of the doubtful debts provision. **Our results:** › We found the amount of revenue recognised to be acceptable; and › We considered the level of provisioning against household customer debt to be acceptable.
Capitalisation of costs relating to the capital programme £726.2 million (2018: £741.3 million) *Refer to pages 108 (Audit committee report), note A7, page 171 (accounting policies) and page 178 (financial disclosures)*	**Subjective classification** The group has a substantial capital programme which has been agreed with the Water Services Regulation Authority (Ofwat) and, therefore, incurs significant annual expenditure in relation to the development and maintenance of both infrastructure and non-infrastructure assets. The determination of project costs as capital or operating expenditure is inherently judgemental. Costs capitalised include an allocation of overhead costs, relating to the proportion of time spent by support function staff, which is based on assumptions involving a high degree of judgement. The effect of these matters is that, as part of our risk assessment, we determined that the costs capitalised has a high degree of judgement, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (see page 171 accounting policies) disclose the sensitivities estimated by the group.	**Our procedures included:** › **Accounting analysis** – Assessing the group's capitalisation policy for compliance with relevant accounting standards; › **Control observation** – Testing controls over the application of the policy in the period, including review of project business case submissions, and attending a sample of capital approval meetings to observe the judgements made and evaluating the documented conclusions; › **Tests of details** – Critically assessing the costs capitalised for a sample of project cost transactions against the capitalisation policy; › **Tests of details** – Identify and assess the impact of existing projects where the capitalisation rate has changed during the year; › **Historical comparisons** – Critically assess the proportion of capitalised overhead costs using historical comparisons and expected changes based on corroborated enquiry and our sector knowledge; and › **Assessing transparency** – Assessing the adequacy of the group's disclosures of its capitalisation policy, including the judgement involved in assessing expenditure as capital and the judgement relating to the allocation of overhead costs. **Our results:** › We found the group's classification of expenditure as capital or operating to be acceptable.

Independent auditor's report to the members of United Utilities Group PLC only

	The risk	Our response
Retirement benefit obligation valuation £3,425.2 million (2018: £3,498.7 million) *Refer to page 108 (Audit committee report), note A7, page 171 (accounting policies), and note A5 (financial disclosures)*	**Subjective valuation:** The valuation of the retirement benefit obligations depends on a number of estimates, including the discount rates used to calculate the current value of the future payments the group expects to pay pensioners, the rate of inflation that must be incorporated in the estimate of the future pension payments, and the life expectancy of pension scheme members. There is a considerable amount of estimation uncertainty involved in setting the above assumptions and a small change in the assumptions and estimates may have a significant impact on the retirement benefit obligations. The effect of these matters is that, as part of our risk assessment, we determined that the gross defined benefit pension obligations has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. The financial statements (see note A5) disclose the sensitivity estimated by the group.	**Our procedures included:** › **Our actuarial expertise** – We used our own actuarial specialists to challenge key assumptions and estimates used in the calculation of the retirement benefit obligations. We also compared the IAS 19 valuation with the triennial funding valuations of the UK schemes, notwithstanding that they were prepared on a different basis and as at different dates; › **Methodology assessment** – We used our own actuarial specialists to assess the appropriateness and consistency of the methodology applied by management in setting the key assumptions; › **Benchmarking assumptions** – We performed a comparison of key assumptions against our own benchmark ranges derived from externally available data and against those used by other companies reporting on the same period › **Assessing external actuary's credentials** – We assessed the competence and independence of the external actuary engaged by the group; and › **Assessing transparency** – We considered the adequacy of the group's disclosure in respect of retirement benefits, in particular, the gross defined benefit obligation and the assumptions used, which are set out in note A5 to the financial statements. **Our results:** › We found the resulting estimate of the retirement benefit obligations to be acceptable.
Water Plus joint venture investment and loans carrying value £36.7 million investment in joint venture and £142.1 million loans to joint venture (2018: £37.3 million and £135.8 million respectively) *Refer to page 109 (Audit commitee report), note A7, page 171 (accounting policies) and pages 179 to 180 (financial disclosures)*	**Forecast-based valuation:** The group's investment in the equity of and loans to Water Plus is significant. The estimated recoverable amount is subjective due to the inherent uncertainty involved in forecasting future cash flows.	**Our procedures included:** › **Assessing methodology** – We assessed whether the principles and integrity of the cash flow model are in accordance with relevant accounting standards; › **Our valuation expertise** – We challenged the assumptions used by the group in the calculation of the discount rates, including comparisons with external data sources and by involving our own valuation specialist to assist us in assessing the discount rate assumptions applied. › **Sensitivity analysis** – We performed our own sensitivity analysis, including a reasonably possible reduction in forecast cash flows and an alternative discount rate assumption, to assess level of sensitivity to these changes; and › **Assessing transparency** – We assessed whether the group's disclosures about the sensitivity of the outcome of the impairment assessment to a reasonably possible change in the discount rate and cash flows reflected the risks inherent in the valuation. **Our results:** › We found the resulting estimate of the recoverable amount of the investment in the equity and loans to Water Plus to be acceptable.

	The risk	Our response
Recoverability of parent company's investment in United Utilities PLC Investment in United Utilities PLC £6,326.8 million (2018: £6,326.8 million). *Refer to note A7, page 203 (accounting policies) and page 180 (financial disclosures)*	**Low risk, high value:** The carrying amount of the parent company's investments in United Utilities PLC represents 99 per cent (2018: 99 per cent) of the company's total assets. The recoverability is not at a high risk of significant misstatement or subject to significant judgement. However, due to the materiality in the context of the parent company financial statements, this is considered to be the area that had the greatest effect on our overall parent company audit.	**Our procedures included:** › **Tests of detail:** Compared the carrying amount of the investment with the draft balance sheet of United Utilities PLC to identify whether the net assets, being an approximation of the minimum recoverable amount, was in excess of the carrying amount and if not, comparing it with the expected value of the business based on a suitable premium to the regulatory capital value. **Our results:** › We found the group's assessment of the recoverability of the investment in United Utilities PLC to be acceptable.

3. Our application of materiality and an overview of the scope of our audit

Materiality for the group financial statements as a whole was set at £20.0 million (2018: £19.0 million), determined with reference to a benchmark of group profit before tax, normalised to exclude net fair value gains or losses on debt and derivative instruments as disclosed in note 5, of £9.5 million, of which it represents 4.7 per cent (2018: 4.9 per cent).

Materiality for the parent company financial statements as a whole was set at £19.5 million (2018: £18.5 million), determined with reference to a benchmark of company total assets, of which it represents 0.30 per cent (2018: 0.29 per cent).

We agreed to report to the audit committee any corrected or uncorrected identified misstatements exceeding £0.5 million, in addition to other identified misstatements that warranted reporting on qualitative grounds.

Of the group’s 34 (2018: 34) reporting components, we subjected seven (2018: six) to full scope audits for group purposes.

The components within the scope of our work accounted for the percentages illustrated opposite.

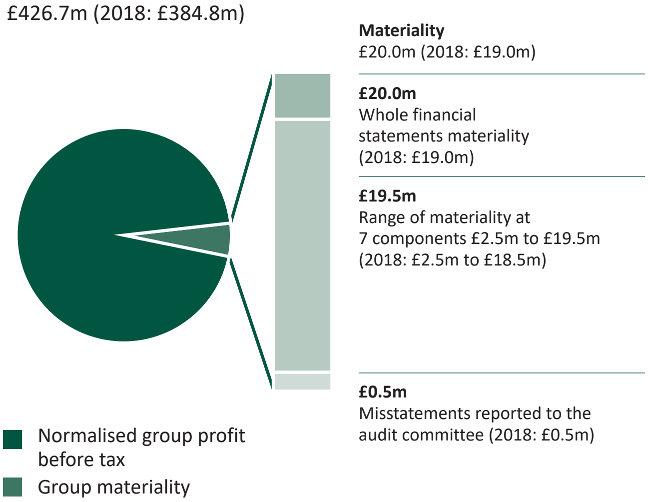
For the residual components, we performed analysis at an aggregated group level to re-examine our assessment that there were no significant risks of material misstatement within these.

The group team approved the component materialities, which ranged from £2.5 million to £19.5 million (2018: £2.5 million to £18.5 million), having regard to the mix of size and risk profile of the group across the components. The work on one of the seven reporting components (2018: one of six) was performed by component auditors and the rest, including the audit of the parent company, was performed by the group team. The group team instructed the component auditor as to the significant areas to be covered, including the relevant risks detailed above and the information to be reported back. The group team performed procedures on the items excluded from normalised group profit before tax.

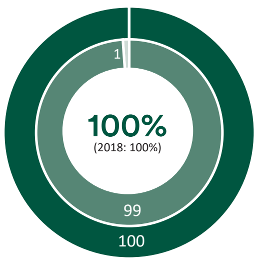
The group team visited none (2018: none) of the component locations to assess the audit risk and strategy. Telephone conference meetings were held with the component auditor. At these meetings, the findings reported to the group team were discussed in more detail and any further work required by the group team was then performed by the component auditor.

Normalised group profit before tax

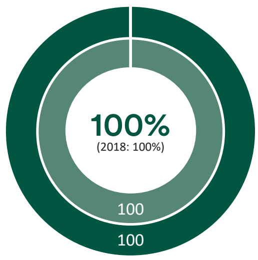
£426.7m (2018: £384.8m)



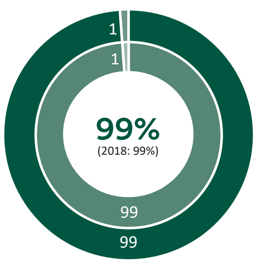
Group revenue



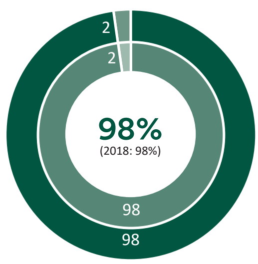
Group normalised profit before tax



Group total assets



Group profit before tax



Full scope for group audit purposes 2019

Full scope for group audit purposes 2018

Residual components

Specified risk-focused audit procedures 2019

Specified risk-focused audit procedures 2018

Independent auditor's report to the members of United Utilities Group PLC only

4. We have nothing to report on going concern

The directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the company or the group or to cease their operations and, as they have concluded, that the company's and the group's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over their ability to continue as a going concern for at least a year from the date of approval of the financial statements ('the going concern period').

Our responsibility is to conclude on the appropriateness of the directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the group and the company will continue in operation.

In our evaluation of the directors' conclusions, we considered the inherent risks to the group's and the company's business model and analysed how those risks might affect the group's and the company's financial resources or ability to continue operations over the going concern period. The risks that we considered most likely to adversely affect the group's and the company's available financial resources over this period were:

› a significant increase required in total expenditure;
› funding to be obtained in line with forecast; and
› the impact of macro-economic factors on household customers' ability to pay.

As these were risks that could potentially cast significant doubt on the group's and the company's ability to continue as a going concern, we considered sensitivities over the level of available financial resources indicated by the group's financial forecasts taking account of reasonably possible (but not unrealistic) adverse effects that could arise from these risks individually and collectively and evaluated the achievability of the actions the directors consider they would take to improve the position should the risks materialise. We also considered less predictable but realistic second-order impacts, such as the impact of Brexit and the erosion of customer or supplier confidence, which could result in a rapid reduction of available financial resources.

Based on this work, we are required to report to you if:

› we have anything material to add or draw attention to in relation to the directors' statement on page 168 of the financial statements on the use of the going concern basis of accounting with no material uncertainties that may cast significant doubt over the group and company's use of that basis for a period of at least 12 months from the date of approval of the financial statements; or
› the related statement under the Listing Rules set out on page 101 is materially consistent with our audit knowledge.

We have nothing to report in these respects and we did not identify going concern as a key audit matter.

5. We have nothing to report on the other information in the Annual Report

The directors are responsible for the other information presented in the Annual Report, together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work, we have not identified material misstatements in the other information.

Strategic report and Directors' report

Based solely on our work on the other information:

› we have not identified material misstatements in the strategic report and the directors' report;
› in our opinion, the information given in those reports for the financial year is consistent with the financial statements; and
› in our opinion, those reports have been prepared in accordance with the Companies Act 2006.

Directors' remuneration report

In our opinion, the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

Disclosures of principal risks and longer-term viability

Based on the knowledge we acquired during our financial statements audit, we have nothing material to add or draw attention to in relation to:

› the directors' confirmation within the Long-term viability statement on pages 101 to 102 that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency and liquidity;
› the Principal risks and uncertainties disclosures describing these risks and explaining how they are being managed and mitigated; and
› the directors' explanation in the Long-term viability statement of how they have assessed the prospects of the group, over what period they have done so and why they considered that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Under the Listing Rules, we are required to review the Long-term viability statement. We have nothing to report in this respect.

Our work is limited to assessing these matters in the context of only the knowledge acquired during our financial statements audit. As we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of anything to report on these statements is not a guarantee as to the group's and company's longer-term viability.

Corporate governance disclosures

We are required to report to you if:

› we have identified material inconsistencies between the knowledge we acquired during our financial statements audit and the directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's position and performance, business model and strategy; or
› the section of the annual report describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee.

We are required to report to you if the Corporate governance statement does not properly disclose a departure from the 11 provisions of the UK Corporate Governance Code specified by the Listing Rules for our review.

We have nothing to report in these respects.

6. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion:

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

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 153, the directors are responsible for: the preparation of the financial statements, including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience and through discussion with the directors and other management (as required by auditing standards), and from inspection of the group's regulatory and legal correspondence and discussed with the directors and other management the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. This included communication from the group to component audit teams of relevant laws and regulations identified at group level.

The potential effect of these laws and regulations on the financial statements varies considerably.

Firstly, the group is subject to laws and regulations that directly affect the financial statements; including financial reporting legislation (including related companies legislation); distributable profits legislation and taxation legislation; and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the group is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation. We identified the following areas as those most likely to have such an effect: Ofwat, Environmental Agency, Drinking Water Inspectorate, health and safety, anti-bribery, employment law, regulatory capital and liquidity and certain aspects of company legislation recognising the financial and regulated nature of the group's activities and legal form. Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors and inspection of regulatory and legal correspondence, if any. Through these procedures, we became aware of actual or suspected non-compliance and considered the effect as part of our procedures on the related financial statement items. The actual or suspected non-compliance was not sufficiently significant to our audit to result in our response being identified as a key audit matter.

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

8. The purpose of our audit work and to whom we owe our responsibilities

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.

William Meredith (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
St Peter's Square, Manchester, M2 3AE
22 May 2019

Consolidated income statement for the year ended 31 March

	Note	2019 £m	2018 £m
Revenue	2	**1,818.5**	1,735.8
Employee benefits expense	3	**(169.6)**	(153.5)
Other operating costs	4	**(449.3)**	(423.4)
Other income	4	**3.6**	3.8
Depreciation and amortisation expense	4	**(393.2)**	(376.8)
Infrastructure renewals expenditure		**(175.1)**	(149.5)
Total operating expenses		**(1,183.6)**	(1,099.4)
Operating profit		**634.9**	636.4
Investment income	5	**17.1**	12.0
Finance expense	6	**(222.5)**	(218.6)
Investment income and finance expense		**(205.4)**	(206.6)
Share of profits of joint ventures	12	**6.7**	2.3
Profit before tax		**436.2**	432.1
Current tax charge	7	**(38.8)**	(18.7)
Deferred tax charge	7	**(34.0)**	(58.8)
Tax	7	**(72.8)**	(77.5)
Profit after tax		**363.4**	354.6
Earnings per share			
Basic	8	**53.3p**	52.0p
Diluted	8	**53.2p**	51.9p
Dividend per ordinary share	9	**41.28p**	39.73p

All of the results shown above relate to continuing operations.

Consolidated statement of comprehensive income for the year ended 31 March

	2019 £m	2018 £m
Profit after tax	**363.4**	354.6
Other comprehensive income		
Items that may be reclassified to profit or loss in subsequent periods:		
Cash flow hedge effectiveness*	**0.4**	–
Tax on items that may be reclassified to profit or loss	**(0.1)**	–
Foreign exchange adjustments	**(0.8)**	0.2
Other comprehensive income that may be reclassified to profit or loss	**(0.5)**	0.2
Items that will not be reclassified to profit or loss in subsequent periods:		
Remeasurement gains on defined benefit pension schemes	**73.0**	50.2
Change in credit assumptions for debt reported at fair value through profit or loss	**6.6**	–
Cost of hedging – cross-currency basis spread adjustment*	**(2.2)**	–
Tax on items that will not be reclassified to profit or loss	**(13.1)**	(8.5)
Other comprehensive income that will not be reclassified to profit or loss	**64.3**	41.7
Total comprehensive income	**427.2**	396.5

* On adoption of IFRS 9, the group has recognised the cost of hedging reserve and the cash flow hedging reserve as new components of equity. A reconciliation of movements in these reserves, including amounts reclassified from other comprehensive income to profit or loss during the year, is included in note 22.

Consolidated and company statements of financial position at 31 March

		Group		Company	
		2019	2018	**2019**	2018
	Note	**£m**	£m	**£m**	£m
ASSETS					
Non-current assets					
Property, plant and equipment	10	**11,153.4**	10,790.5	**–**	–
Intangible assets	11	**202.7**	197.7	**–**	–
Interests in joint ventures	12	**79.0**	75.2	**–**	–
Investments	13	**11.5**	7.1	**6,326.8**	6,326.8
Trade and other receivables	15	**148.1**	141.1	**–**	–
Retirement benefit surplus	18	**483.9**	344.2	**–**	–
Derivative financial instruments	A4	**387.8**	297.8	**–**	–
		12,466.4	11,853.6	**6,326.8**	6,326.8
Current assets					
Inventories	14	**14.9**	16.8	**–**	–
Trade and other receivables	15	**249.5**	260.9	**82.2**	74.2
Current tax asset		**16.4**	24.5	**–**	–
Cash and short-term deposits	16	**339.3**	510.0	**–**	–
Derivative financial instruments	A4	**101.3**	337.7	**–**	–
		721.4	1,149.9	**82.2**	74.2
Total assets		**13,187.8**	13,003.5	**6,409.0**	6,401.0
LIABILITIES					
Non-current liabilities					
Trade and other payables	21	**(697.3)**	(642.7)	**–**	–
Borrowings	17	**(7,115.6)**	(7,072.8)	**(1,718.4)**	(1,690.3)
Deferred tax liabilities	19	**(1,146.0)**	(1,098.8)	**–**	–
Derivative financial instruments	A4	**(66.1)**	(96.8)	**–**	–
		(9,025.0)	(8,911.1)	**(1,718.4)**	(1,690.3)
Current liabilities					
Trade and other payables	21	**(321.2)**	(275.7)	**(14.7)**	(11.3)
Borrowings	17	**(700.2)**	(839.5)	**(0.5)**	(0.5)
Provisions	20	**(16.8)**	(22.1)	**–**	–
Derivative financial instruments	A4	**(13.8)**	(4.2)	**–**	–
		(1,052.0)	(1,141.5)	**(15.2)**	(11.8)
Total liabilities		**(10,077.0)**	(10,052.6)	**(1,733.7)**	(1,702.1)
Total net assets		**3,110.8**	2,950.9	**4,675.4**	4,698.9
EQUITY					
Capital and reserves attributable to equity holders of the company					
Share capital	23	**499.8**	499.8	**499.8**	499.8
Share premium account		**2.9**	2.9	**2.9**	2.9
Capital redemption reserve		**–**	–	**1,033.3**	1,033.3
Other reserves	22	**338.3**	327.9	**–**	–
Retained earnings		**2,269.8**	2,120.3	**3,139.4**	3,162.9
Shareholders' equity		**3,110.8**	2,950.9	**4,675.4**	4,698.9

These financial statements for the group and United Utilities Group PLC (company number: 6559020) were approved by the board of directors on 22 May 2019 and signed on its behalf by:

Steve Mogford
Chief Executive Officer

Russ Houlden
Chief Financial Officer

Consolidated statement of changes in equity for the year ended 31 March

	Share capital £m	Share premium account £m	Other reserves* £m	Retained earnings £m	Total £m
At 31 March 2018	**499.8**	**2.9**	**327.9**	**2,120.3**	**2,950.9**
Adjustment on initial application of IFRS 9	**–**	**–**	**12.7**	**(12.7)**	**–**
Adjustment on initial application of IFRS 15	**–**	**–**	**–**	**5.9**	**5.9**
At 1 April 2018	**499.8**	**2.9**	**340.6**	**2,113.5**	**2,956.8**
Profit after tax	**–**	**–**	**–**	**363.4**	**363.4**
Other comprehensive income/(expense)					
Remeasurement gains on defined benefit pension schemes (see note 18)	**–**	**–**	**–**	**73.0**	**73.0**
Change in credit assumption for debt reported at fair value through profit or loss	**–**	**–**	**–**	**6.6**	**6.6**
Cash flow hedge effectiveness	**–**	**–**	**0.4**	**–**	**0.4**
Cost of hedging – cross-currency basis spread adjustment	**–**	**–**	**(2.2)**	**–**	**(2.2)**
Tax on items taken directly to equity (see note 7)	**–**	**–**	**0.3**	**(13.5)**	**(13.2)**
Foreign exchange adjustments	**–**	**–**	**(0.8)**	**–**	**(0.8)**
Total comprehensive (expense)/income	**–**	**–**	**(2.3)**	**429.5**	**427.2**
Dividends (see note 9)	**–**	**–**	**–**	**(274.4)**	**(274.4)**
Equity-settled share-based payments (see note 3)	**–**	**–**	**–**	**4.0**	**4.0**
Exercise of share options – purchase of shares	**–**	**–**	**–**	**(2.8)**	**(2.8)**
At 31 March 2019	**499.8**	**2.9**	**338.3**	**2,269.8**	**3,110.8**

	Share capital £m	Share premium account £m	Other reserves £m	Retained earnings £m	Total £m
At 1 April 2017	499.8	2.9	327.7	1,991.2	2,821.6
Profit after tax	–	–	–	354.6	354.6
Other comprehensive income/(expense)					
Remeasurement gains on defined benefit pension schemes (see note 18)	–	–	–	50.2	50.2
Tax on items taken directly to equity (see note 7)	–	–	–	(8.5)	(8.5)
Foreign exchange adjustments	–	–	0.2	–	0.2
Total comprehensive income	–	–	0.2	396.3	396.5
Dividends (see note 9)	–	–	–	(267.0)	(267.0)
Equity-settled share-based payments (see note 3)	–	–	–	3.2	3.2
Exercise of share options – purchase of shares	–	–	–	(3.4)	(3.4)
At 31 March 2018	499.8	2.9	327.9	2,120.3	2,950.9

* Other reserves comprise the group's cumulative exchange reserve, merger reserve, cost of hedging reserve and cash flow hedging reserve. The cost of hedging and cash flow hedging reserves were included as separate components of equity for the first time in the year ended 31 March 2019 as a result of the group's adoption of IFRS 9 'Financial instruments' (see pages 168 to 169 accounting policies). A reconciliation of movements in these reserves is included in note 22.

Company statement of changes in equity for the year ended 31 March

	Share capital £m	Share premium account £m	Capital redemption reserve £m	Retained earnings £m	Total £m
At 1 April 2018	**499.8**	**2.9**	**1,033.3**	**3,162.9**	**4,698.9**
Profit after tax	**–**	**–**	**–**	**249.7**	**249.7**
Total comprehensive income	**–**	**–**	**–**	**249.7**	**249.7**
Dividends (see note 9)	**–**	**–**	**–**	**(274.4)**	**(274.4)**
Equity-settled share-based payments (see note 3)	**–**	**–**	**–**	**4.0**	**4.0**
Exercise of share options – purchase of shares	**–**	**–**	**–**	**(2.8)**	**(2.8)**
At 31 March 2019	**499.8**	**2.9**	**1,033.3**	**3,139.4**	**4,675.4**

	Share capital £m	Share premium account £m	Capital redemption reserve £m	Retained earnings £m	Total £m
At 1 April 2017	499.8	2.9	1,033.3	3,183.5	4,719.5
Profit after tax	–	–	–	246.6	246.6
Total comprehensive income	–	–	–	246.6	246.6
Dividends (see note 9)	–	–	–	(267.0)	(267.0)
Equity-settled share-based payments (see note 3)	–	–	–	3.2	3.2
Exercise of share options – purchase of shares	–	–	–	(3.4)	(3.4)
At 31 March 2018	499.8	2.9	1,033.3	3,162.9	4,698.9

At 31 March 2019, 31 March 2018 and 1 April 2017, the company's entire retained earnings balance was distributable to shareholders.

The capital redemption reserve arose as a result of a return of capital to shareholders following the reverse acquisition of United Utilities PLC by United Utilities Group PLC in the year ended 31 March 2009.

As permitted by section 408 of the Companies Act 2006, the company has not presented its own income statement. The result of the company for the financial year was a profit after tax of £249.7 million (2018: £246.6 million).

Consolidated and company statements of cash flows for the year ended 31 March

		Group			Company
		2019	2018	**2019**	2018
	Note	**£m**	£m	**£m**	£m
Operating activities					
Cash generated from operations	A1	**995.5**	989.8	**278.8**	271.2
Interest paid		**(143.0)**	(144.6)	**(28.0)**	(25.1)
Interest received and similar income		**7.3**	5.9	**–**	–
Tax paid		**(27.5)**	(35.5)	**–**	–
Tax received		**–**	–	**10.4**	–
Net cash generated from operating activities		**832.3**	815.6	**261.2**	246.1
Investing activities					
Purchase of property, plant and equipment		**(622.3)**	(698.6)	**–**	–
Purchase of intangible assets		**(39.9)**	(36.1)	**–**	–
Proceeds from sale of property, plant and equipment		**2.1**	1.1	**–**	–
Grants and contributions received	21	**35.2**	23.7	**–**	–
Loans to joint ventures	A6	**(6.0)**	(26.5)	**–**	–
Dividends received from joint ventures	12	**2.2**	3.3	**–**	–
Proceeds from investments	13	**1.0**	1.0	**–**	–
Net cash used in investing activities		**(627.7)**	(723.2)	**–**	–
Financing activities					
Proceeds from borrowings		**568.4**	801.0	**16.0**	24.4
Repayment of borrowings		**(668.6)**	(345.9)	**–**	–
Dividends paid to equity holders of the company	9	**(274.4)**	(267.0)	**(274.4)**	(267.0)
Exercise of share options – purchase of shares		**(2.8)**	(3.4)	**(2.8)**	(3.4)
Net cash generated from/(used in) financing activities		**(377.4)**	184.7	**(261.2)**	(246.0)
Net (decrease)/increase in cash and cash equivalents		**(172.8)**	277.1	**–**	0.1
Cash and cash equivalents at beginning of the year		**497.4**	220.3	**(0.5)**	(0.6)
Cash and cash equivalents at end of the year	16	**324.6**	497.4	**(0.5)**	(0.5)

Guide to detailed financial statements disclosures

In the interest of providing clear and relevant information to the users of our financial statements we have included summary information within the notes to the financial statements, with additional detailed information included in appendices where required. These notes and appendices can be grouped as follows:

Accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. Further detail can be found in note A7.

Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU). They have been prepared on the historical cost basis, except for the revaluation of financial instruments, accounting for the transfer of assets from customers, and the revaluation of infrastructure assets to fair value on transition to IFRS.

The preparation of financial statements, in conformity with IFRS, requires management to make estimates and assumptions that affect the amounts of assets and liabilities at the date of the financial statements and the amounts of revenues and expenses during the reporting periods presented. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results, ultimately, may differ from these estimates.

The financial statements have been prepared on the going concern basis as the directors have a reasonable expectation that the group has adequate resources for a period of at least 12 months from the date of the approval of the financial statements, and that there are no material uncertainties to disclose.

In assessing the appropriateness of the going concern basis of accounting, the directors have reviewed the resources available to the group, taking account of the group's financial projections, together with its liquidity position with regards to available cash and undrawn committed borrowing facilities, as well as consideration of the group's capital adequacy. The board has also considered the magnitude of potential impacts resulting from uncertain future events or changes in conditions, the likelihood of their occurrence and the likely effectiveness of mitigating actions the directors would consider undertaking.

Adoption of new and revised standards

The following standards, interpretations and amendments, effective for the year ended 31 March 2019, are relevant to the group but have had no material impact on the group's financial statements:

› Amendments to IFRS 2 'Classification and Measurement of Share-based Payment Transactions' (issued on 20 June 2016).

The following standards, interpretations and amendments, effective for the year ended 31 March 2019, have had a material impact on the group's financial statements – this impact is discussed further below:

› IFRS 9 'Financial Instruments' (issued on 24 July 2014); and

› IFRS 15 'Revenue from Contracts with Customers' (issued on 28 May 2014) including amendments to IFRS 15: Effective date of IFRS 15 (issued on 11 September 2015).

IFRS 9 'Financial Instruments'

IFRS 9 'Financial Instruments' was adopted by the group on 1 April 2018. The standard replaces IAS 39 'Financial Instruments: Recognition and Measurement', and has been applied retrospectively in accordance with the standard's transition requirements. Comparative periods have not been restated, with any differences arising from retrospective application being recognised as an adjustment to retained earnings at the beginning of the period. This has resulted in retained earnings at the adoption date decreasing by £12.7 million with a corresponding credit of £13.8 million to the cost of hedging reserve, which is a separate component of equity newly recognised under IFRS 9, offset by a corresponding debit of £1.1 million to the cumulative exchange reserve. Further details of these adjustments are set out below.

Under IFRS 9, there is no longer a requirement for cross-currency basis spread adjustments to be incorporated in the test for the effectiveness of a hedge as was the case under IAS 39. IFRS 9 states that when an entity separates the foreign currency basis spread from a financial instrument, and excludes it from the designation of that financial instrument as the hedging instrument, the entity may apply the accounting such that the change in fair value resulting from the foreign currency basis spread can be recognised in other comprehensive income rather than in profit or loss to the extent that it relates to the hedged item. Under the standard this change in fair value relating to the basis spread adjustment, which effectively represents a liquidity charge inherent in foreign exchange contracts for exchanging currencies, shall be accumulated in a separate component of equity. This has been recorded as a cost of hedging reserve.

The group has adopted this accounting treatment under IFRS 9, resulting in the creation of a cost of hedging reserve with a brought forward balance of £13.8 million at 1 April 2018, being the accumulated fair value gains to date at this point relating to the basis spread adjustment on cross-currency swaps in place at the adoption date. The portion of the change in fair value due to changes in the cross-currency basis spread during the period, which has been recognised in other comprehensive income, has been a £2.2 million loss. This would have previously been incorporated within the fair value charge recognised in the income statement under IAS 39.

Where the group has chosen to measure borrowings at fair value through profit or loss, the portion of the change in fair value due to changes in the group's own credit risk, which has been a £6.6 million gain during the period, has been recognised in other comprehensive income rather than within profit or loss, and has been taken directly to retained earnings, meaning no opening retained earnings adjustment has been required.

During the period, fair value foreign exchange gains of £0.5 million have been recognised in the income statement, which would not have been recognised under previous accounting policies. This has resulted from the classification of an investment previously accounted for as an available-for-sale financial asset under IAS 39 'Financial Instruments: Recognition and Measurement' as a financial asset measured at fair value through profit or loss. Under IFRS 9, the available-for-sale category no longer exists and, given that the financial asset does not meet the criteria to be subsequently measured at amortised cost or fair value through other comprehensive income, subsequent measurement at fair value through profit or loss is deemed the most appropriate categorisation. As a result of this change in classification, a credit of £1.1 million in the cumulative exchange reserve, representing cumulative foreign exchange gains on the investment up to the adoption date, was reclassified to retained earnings as an opening balance sheet adjustment.

On adoption of IFRS 9, there were no financial assets or liabilities initially designated at fair value through profit or loss that have subsequently been reclassified out of this category.

The group has reassessed the effectiveness of existing accounting hedges on adoption of IFRS 9 and the documentation that supports any designation. Financial instruments that had been designated in an accounting fair value hedge relationship under IAS 39 continue to be designated as such under IFRS 9; however, the group has reassessed its position with regards to designating non-financial risks in hedge relationships, and has determined that in order to give a more representative view of operating costs it would be appropriate to designate existing and future swaps as being in a cash flow hedge relationship provided they meet the criteria for designation. This means that only the impact of any hedging ineffectiveness is recognised through fair value in the income statement, with movements reflecting the effective part of the swaps being recognised in other comprehensive income. At the maturity date the amounts paid/received will be recognised against operating costs in the income statement, including the effect of any fair value movements reflecting hedge effectiveness previously recognised in other comprehensive income.

Previously, no income relating to these swaps would have been recognised against corresponding operating expenses, with the £4.2 million gain for the year being recognised in full as a fair value movement included as part of finance expense. The treatment under IFRS 9 has led to the settlement of existing swaps in the period giving rise to income of £3.8 million recognised against operating expenses, with a fair value gain of £0.4 million recognised in other comprehensive income together with a corresponding increase in the cash flow hedge reserve as the hedge was fully effective.

A deferred tax charge of £0.8 million has been recognised in other comprehensive income during the period in relation to the above.

On transition to the expected credit loss model for impairing financial assets in accordance with the standard, the group has not been significantly impacted as under IAS 39 the group had always used a model which used historic cash collection rates to form an expectation of the estimated recoverability of trade receivables at a point in time. The simplified approach, whereby the company recognises full lifetime credit losses on initial recognition, has been adopted.

IFRS 15 'Revenue from Contracts with Customers'

The group adopted IFRS 15 on 1 April 2018, applying the standard retrospectively with the cumulative effect of initial application recognised at the date of initial application as an adjustment to retained earnings. Prior period comparatives have therefore not been restated. The group has elected to use the practical expedient whereby any contracts that were completed in accordance with accounting standards as at 31 March 2018 need not be restated on an IFRS 15 basis. This transition approach, which was made in accordance with the IFRS 15 transitional provisions, has resulted in a £2.6 million increase in retained earnings and reduction in deferred income on the adoption date due to a change in the period over which revenue relating to connection activities is recognised. This has also given rise to a tax credit of £3.3 million relating to the adjustment, which has resulted in an increase in retained earnings at the adoption date. The tax credit is greater than the £2.6 million increase in retained earnings on adoption of IFRS 15 due to the different tax treatments of various connection activities that make up the adjustment.

The two main areas of the group's activities considered in the adoption of IFRS 15 are:

› the provision of core water and wastewater services, accounting for more than 96 per cent of the group's revenue; and
› capital income streams relating to diversions work, and activities, typically performed opposite property developers, that facilitate the creation of an authorised connection through which properties can obtain water and wastewater services.

The adoption of IFRS 15 had no impact on the timing or amount of revenue recognised in relation to core water and wastewater services, which are deemed to be distinct performance obligations under the contracts with customers, though following the same pattern of transfer to the customer who simultaneously receives and consumes both of these services over time. No significant judgements are required in identifying customers of these services. In accordance with IFRS 15, revenue relating to these activities will be recognised over time as these performance obligations are satisfied.

There are two categories of capital income, both of which will be impacted by the adoption of IFRS 15:

› Diversions relating to the relocation of water and wastewater assets; and
› Activities that facilitate the creation of an authorised connection through which properties can obtain water and wastewater services.

The adoption of IFRS 15 did not result in any net income statement impact relating to diversions as income was previously recognised in line with the completion of diversion work. However, whereas this income was included in the income statement as a credit within infrastructure renewals expenditure (IRE) due to it representing a contribution towards these costs, under IFRS 15 it is now recognised within revenue, resulting in an increase in both the revenue and IRE expense balances. The adoption of the standard in the year has caused both balances to increase by £11.1 million. As there was no net impact to the income statement, there was also no net impact to earnings per share or diluted earnings per share as a result of this element of the new standard.

Significant judgement is required in relation to accounting for activities that facilitate an authorised network connection through which water and wastewater services can be delivered. Establishing such an authorised connection can involve a number of activities performed opposite developers, which are considered to be neither separable nor distinct and instead form a bundle of activities necessary to establish an authorised connection from which network access can be obtained and water and wastewater services can be provided. Costs incurred by the group in carrying out these activities are capitalised as property, plant and equipment to the extent they result in the creation or enhancement of assets. These activities are considered to form part of the group's ordinary activities associated with the operation, maintenance and expansion of a water and wastewater network and, because they are deemed to result in an exchange transaction, we have determined that they fall within the scope of IFRS 15 as transactions arising from contracts with customers.

In addition, as the group has a legal obligation to keep a connection in place for as long as a property requires water and wastewater services, these initial connection activities are deemed to result in a broader ongoing performance obligation that is not distinct from the ongoing supply of water and wastewater services. The right to benefit from this connection, and obtain water and wastewater services through it, is deemed to be transferable from the initial developer to subsequent occupants of a connected property. Accordingly, under IFRS 15, the element of the performance obligation associated with the connection activities is deemed to be satisfied over the period of time that water and wastewater services are expected to be provided through the connection, compared with the prior treatment under which deferred amounts were released to the income statement over the useful economic life of the related assets or, for certain items, immediately to the income statement. This estimated period is a matter of judgement. We estimate that an average connection will be in place for a period of 60 years and therefore revenue associated with connection activities will be recognised evenly over this period.

Contract liabilities are accounted for within deferred revenue. These contract liabilities relate to the revenue which is held on the balance sheet in respect of connection activities. As stated above, revenue is released and recognised evenly over a period of 60 years; therefore deferred income on the balance sheet will also be reduced evenly over the 60 year period on a connection-by-connection basis. The group will hold no material contract assets, meaning there will be no material impairments to contract assets under IFRS 9 given the new requirement to provide for expected credit losses for contract assets.

As noted above, we have applied IFRS 15 retrospectively, with the cumulative effect of initially applying the standard recognised as an adjustment to the opening retained earnings balance at the date of initial application, resulting in an increase of £2.6 million in retained earnings with the corresponding decrease being to deferred income. In line with the standard, contracts which were completed in accordance with current accounting standards at the date of initial application were not restated on an IFRS 15 basis. The impact of the change on ongoing revenue as a result of the revised period over which income is released to the income statement is that revenue of £13.4 million was recognised in the year relating to the amortisation of deferred income; had IFRS 15 not been adopted, this revenue recognised in the year would have been £9.9 million. The adoption of IFRS 15 has therefore resulted in an increase of revenue of £3.5 million. This has directly impacted the amount of revenue and profit of the group with the corresponding decrease of the adoption of IFRS 15 being in deferred income on the balance sheet. Accordingly, the group's EPS and diluted EPS for the year have also been affected. EPS was 53.3p and diluted EPS was 53.2p; had IFRS 15 not been adopted the EPS and diluted EPS of the group would have been 52.8p and 52.7p respectively.

New and revised standards not yet effective

At the date of authorisation of these financial statements, the following relevant major standards were in issue but not yet effective. The directors anticipate that the group will adopt these standards on their effective dates.

IFRS 16 'Leases'

This standard, which replaces IAS 17 'Leases', IFRIC 4 'Determining Whether an Arrangement Contains a Lease', SIC-15 'Operating Leases – Incentives', and SIC-27 'Evaluating the Substance of Transactions in the Legal Form of a Lease', is effective for periods commencing on or after 1 January 2019. The group therefore adopted the standard on 1 April 2019 with the 31 March 2020 financial statements being the first which will be presented with IFRS 16 being applied. Under the provisions of the new standard, most leases, including the majority of those previously classified as operating leases where the group is the lessee, will be brought onto the statement of financial position as both a right-of-use asset and an offsetting lease liability. The typical items which the group leases include land, buildings, and vehicles. The right-of-use asset and lease liability are both based on the present value of lease payments due over the term of the lease, with the asset being depreciated in accordance with IAS 16 'Property, Plant and Equipment' and the liability increased for the accretion of interest (being the unwinding of the discounting applied to the future lease payments) and reduced by lease payments. The group does not act as a lessor.

The key judgements associated with adoption of this standard relate to the identification and classification of contracts containing a lease within the scope of IFRS 16, and the discount rate to use in calculating the present value of future lease payments on which the reported lease liability and right-of-use asset is based when the rate is not implicit in the lease contract.

The group has reassessed whether contracts it has entered into are, or contain, leases as defined by the new standard, so the new standard is being applied to a different population of contracts to those previously identified as containing leases under IAS 17 and IFRIC 4. Some new contracts have been identified as leases, while other contracts previously identified as operating leases under IAS 17 and IFRIC 4 will not be accounted for as leases under the new standard.

Due to the nature of the group's operations, many of the current operating leases have long remaining terms, which causes the discount rate to be a key factor in determining the value of the lease liability. Where the interest rate is not implicit in the lease, which is the case for materially all of the group's leases recognised under IFRS 16, the discount rate which is used to calculate the lease liability will be based on the relevant group company's nominal incremental borrowing rate adjusted for the payment profile and term of each lease.

The group intends to use the modified retrospective transitional approach permitted by the standard in which the right-of-use asset and lease liability brought onto the balance sheet on the adoption date will be based on the present value of future lease payments at the adoption date calculated using the appropriate discount rate at 1 April 2019. Under this approach there will be no effect on retained earnings recognised on transition. After the initial adoption of the standard, lease liabilities and right-of-use assets for new leases will be based on the corresponding discount rate at the date the new contract is entered into. Prior year comparatives will not be restated.

The group intends to apply recognition exemptions permitted by the standard in relation to short-term leases and leases of low-value items.

Based on the appropriate incremental borrowing rates at 31 March 2019, the right-of-use asset and liability brought onto the balance sheet is estimated to be £54.8 million. Absent new leases being entered into or cancellation of existing leases, the income statement charge in the year of adoption in respect of these leases is estimated to be £3.8 million, split between £2.2 million of depreciation of the assets and £1.6 million in relation to the finance charge recognised on the liabilities. This compares with £3.7 million of operating lease expenses that would have been recognised under IAS 17. The group does not expect the adoption of IFRS 16 to impact its ability to comply with any banking or financing covenants.

The actual impacts of adopting the standard on 1 April 2019 may differ from the figures quoted above as new accounting policies may be subject to change until the group presents its first financial statements that include the date of initial application.

Critical accounting judgements and key sources of estimation uncertainty

In the process of applying its accounting policies set out in note A7, the group is required to make certain estimates, judgements and assumptions that it believes are reasonable based on the information available. These judgements, estimates and assumptions affect the carrying amounts of assets and liabilities at the date of the financial statements and the amounts of revenues and expenses recognised during the reporting periods presented. Changes to these estimates, judgements and assumptions could have a material effect on the financial statements.

On an ongoing basis, the group evaluates its estimates using historical experience, consultation with experts and other methods considered reasonable in the particular circumstances. Actual results may differ significantly from the estimates, the effect of which is recognised in the period in which the facts that give rise to the revision become known.

The following paragraphs detail the estimates and judgements the group believes to have the most significant impact on the annual results under IFRS.

Revenue recognition and allowance for doubtful receivables

Accounting judgement – The group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured. When the group considers that the criteria for revenue recognition are not met for a transaction, revenue recognition is delayed until such time as collectability is reasonably assured. There are two different criteria whereby management does not recognise revenue for amounts which have been billed to the customer on the basis that collectability is not reasonably assured. These are as follows:

- The customer has not paid their bills for a period of at least two years; and
- The customer has paid their bills in the preceding two years; however, has previously had statements de-recognised and has more than their current year debt outstanding.

This two-criteria approach resulted in £18.0 million of amounts billed not being recognised as revenue during the year (net of cash receipts and credits). Had management made an alternative judgement that where customers have paid in the preceding two years, and have more than their current year debt outstanding, the recoverability of the entirety of their debt was deemed to be reasonably assured (i.e. the second criteria were disapplied), the required adjustment to revenue would have been £12.8 million lower. Payments received in advance of revenue recognition are recorded as deferred income.

Accounting estimate – At each reporting date, the company and each of its subsidiaries evaluate the estimated recoverability of trade receivables and record allowances for doubtful receivables based on experience. Judgements associated with these allowances are based on, among other things, a consideration of actual collection history. The actual level of receivables collected may differ from the estimated levels of recovery, which could impact operating results positively or negatively. At 31 March 2019, the allowance for doubtful receivables relating to household customer debt of £52.9 million was supported by a six-year cash collection projection. Based on a five-year or seven-year cash collection projection the allowance for doubtful receivables would have been £50.9 million or £53.5 million respectively.

Accounting estimate – United Utilities Water Limited raises bills in accordance with its entitlement to receive revenue in line with the limits established by the periodic regulatory price review processes. For water and wastewater customers with water meters, the receivable billed is dependent on the volume supplied, including the sales value of an estimate of the units supplied between the date of the last meter reading and the billing date. Meters are read on a cyclical basis and the group recognises revenue for unbilled amounts based on estimated usage from the last billing through to each reporting date. The estimated usage is based on historical data, judgement and assumptions; actual results could differ from these estimates, which would result in operating revenues being adjusted in the period that the revision to the estimates is determined. Revenue recognised for unbilled amounts for these customers at 31 March 2019 was £47.2 million. Had actual consumption been five per cent higher or lower than the estimate of units supplied this would have resulted in revenue recognised for unbilled amounts being £4.2 million higher or lower respectively. For customers who do not have a meter, the receivable billed and revenue recognised is dependent on the rateable value of the property, as assessed by an independent rating officer.

Property, plant and equipment

Accounting judgement – The group recognises property, plant and equipment (PPE) on its water and wastewater infrastructure assets where such expenditure enhances or increases the capacity of the network, whereas any expenditure classed as maintenance is expensed in the period it is incurred. Determining enhancement from maintenance expenditure requires an accounting judgement, particularly when projects have both elements within them. Enhancement spend was 26 per cent of total spend in relation to infrastructure assets during the year. A change of +/- one per cent would have resulted in £2.4 million less/more expenditure being charged to the income statement during the period. In addition, management capitalises time and resources incurred by the group's support functions on capital programmes, which requires accounting judgements to be made in relation to the appropriate capitalisation rates. Support costs allocated to PPE represent 46 per cent of total support costs. A change in allocation of +/- one per cent would have resulted in £0.8 million less/more expenditure being charged to the income statement during the period.

Accounting estimate – The estimated useful economic lives of PPE and intangible assets is based on management's experience. When management identifies that actual useful economic lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively. Due to the significance of PPE and intangibles investment to the group, variations between actual and estimated useful economic lives could impact operating results both positively and negatively. As such, this is a key source of estimation uncertainty, although historically few changes to estimated useful economic lives have been required. The depreciation and amortisation expense for the year was £393.2 million. A 10 per cent increase in average asset lives would have resulted in a £38.9 million reduction in this figure and a 10 per cent decrease in average asset lives would have resulted in a £39.5 million increase in this figure.

Retirement benefits

Accounting estimate – The group operates two defined benefit pension schemes which are independent of the group's finances. Actuarial valuations of the schemes are carried out as determined by the trustees at intervals of not more than three years. Profit before tax and net assets are affected by the actuarial assumptions used. The key assumptions include: discount rates, pay growth, mortality, and increases to pensions in payment and deferred pensions. It should be noted that actual rates may differ from the assumptions used due to changing market and economic conditions and longer or shorter lives of participants and, as such, this represents a key source of estimation uncertainty. Sensitivities in respect of the assumptions used during the year are disclosed in note A5.

Joint ventures – Water Plus

Accounting estimate – The group has an equity investment in Water Plus Group Limited, a joint venture with Severn Trent PLC, the recoverability of which is considered with reference to the present value of the estimated future cash flows of the joint venture. Please see note 12 for details of the significant estimates relating to the recoverable amount of this investment, as well as an assessment of how sensitive the recoverable amount is to reasonably possible downside scenarios.

Derivative financial instruments

Accounting estimate – The model used to fair value the group's derivative financial instruments requires management to estimate future cash flows based on applicable interest rate curves. Projected cash flows are then discounted back using discount factors which are derived from the applicable interest rate curves adjusted for management's estimate of counterparty and own credit risk, where appropriate. Sensitivities relating to derivative financial instruments are included in note A4.

Notes to the financial statements

1 Segmental reporting

The board of directors of United Utilities Group PLC (the board) is provided with information on a single-segment basis for the purposes of assessing performance and allocating resources. The group's performance is measured against financial and operational key performance indicators which align with our three strategic themes to deliver the best service to customers, at the lowest sustainable cost, in a responsible manner. The board reviews revenue, operating profit and gearing, along with operational drivers at a consolidated level (see page 67). In light of this, the group has a single segment for financial reporting purposes and therefore no further detailed segmental information is provided in this note.

2 Revenue

The group's revenue predominantly arises from the provision of services within the United Kingdom, with less than one per cent of external revenue and non-current assets being overseas.

	2019 £m	2018 £m
Wholesale water charges	**767.4**	719.2
Wholesale wastewater charges	**905.8**	875.6
Residential retail charges	**86.7**	91.2
Other	**58.6**	49.8
	1,818.5	1,735.8

In accordance with IFRS 15, revenue has been disaggregated based on what is recognised in relation to the core services of supplying clean water and the removing and treating of wastewater. Each of these services is deemed to give rise to a distinct performance obligation under the contract with customers, though following the same pattern of transfer to the customer who simultaneously receives and consumes both of these services over time.

Residential retail charges relate solely to the margin applied to the wholesale amounts charged to residential customers. The wholesale charges and retail margin are combined in arriving at the total revenues relating to water and wastewater services provided to household customers.

Other revenues comprise a number of smaller non-core income streams, including those relating to energy generation and export, and those associated with activities, typically performed opposite property developers, which impact the group's capital network assets including diversions works to relocate water and wastewater assets, and activities that facilitate the creation of an authorised connection through which properties can obtain water and wastewater services.

3 Directors and employees

Directors' remuneration

	2019 £m	2018 £m
Fees to non-executive directors	**0.8**	0.7
Salaries	**1.7**	1.5
Benefits	**0.4**	0.4
Bonus	**0.9**	0.7
Share-based payment charge	**2.4**	1.8
	6.2	5.1

Further information about the remuneration of individual directors and details of their pension arrangements are provided in the Directors' remuneration report on pages 131 to 142.

Remuneration of key management personnel

	2019 £m	2018 £m
Salaries and short-term employee benefits	**5.2**	5.3
Severance	**–**	0.6
Share-based payment charge	**3.1**	2.4
	8.3	8.3

Key management personnel comprises all directors and certain senior managers who are members of the executive team.

Employee benefits expense (including directors)

Group	2019 £m	2018 £m
Wages and salaries	**234.2**	220.7
Employee-related taxes and levies	**24.1**	22.8
Severance	**4.8**	3.7
Post-employment benefits:		
Defined benefit pension expense (see note 18)	**18.0**	32.2
Defined contribution pension expense (see note 18)	**23.0**	12.1
	41.0	44.3
Charged to other areas including regulatory capital schemes	**(134.5)**	(138.0)
Employee benefits expense	**169.6**	153.5

Within employee benefits expense there were £7.2 million (2018: £6.0 million) of restructuring costs, £6.6 million of costs associated with the equalisation of Guaranteed Minimum Pension (GMP) benefits (2018: nil) and £1.4 million (2018: nil) of costs incurred in relation to the group's response to the severe dry weather event experienced during the year.

The total expense included within employee benefits expense in respect of equity-settled share-based payments was £4.0 million (2018: £3.2 million). The company operates several share option schemes, details of which are given on pages 135 to 137 in the Directors' remuneration report. Further disclosures have not been included as they are considered immaterial to the assessment of the share-based payments charge.

Average number of employees during the year (full-time equivalent including directors):

	2019 number	2018 number
Average number of employees during the year	**5,267**	5,223

Company

The company has no employees.

4 Operating profit

The following items have been charged/(credited) to the income statement in arriving at the group's operating profit:

	2019 £m	2018 £m
Other operating costs		
Hired and contracted services	**112.2**	97.7
Property rates	**94.7**	90.5
Materials	**77.8**	67.3
Power	**72.8**	70.4
Regulatory fees	**32.5**	29.7
Charge for bad and doubtful receivables (see note 15)	**26.5**	20.8
Cost of properties disposed	**4.7**	9.8
Loss on disposal of property, plant and equipment	**3.9**	6.8
Operating leases payable:		
Property	**2.8**	3.5
Plant and equipment	**1.3**	0.7
Compensation from insurers	**–**	(3.6)
Settlement of commercial claims	**(9.9)**	–
Other expenses	**30.0**	29.8
	449.3	423.4
Other income		
Other income	**(3.6)**	(3.8)
	(3.6)	(3.8)
Depreciation and amortisation expense		
Depreciation of property, plant and equipment (see note 10)	**357.3**	348.4
Amortisation of intangible assets (see note 11)	**35.9**	28.4
	393.2	376.8

During the current year, as a result of the group's response to a severe dry weather event, there were £36.1 million of expenses incurred, comprising £24.2 million of other operating costs, £10.5 million of infrastructure renewals expenditure, and £1.4 million of employee costs (see note 3).

During the prior year, as a result of two significant flooding incidents caused by storms Desmond and Eva in December 2015, there were £5.3 million of expenses incurred, comprising £2.9 million of operating costs, £2.4 million of infrastructure renewals expenditure. Insurance compensation of £3.6 million relating to the flooding incidents was recognised as part of a final settlement of the insurance claim. In addition, in the prior year, there were £1.0 million of market reform restructuring costs relating to the non-household retail market opening to competition in April 2017.

Total other operating costs are stated net of £0.2 million (2018: £1.4 million) of costs recharged to Water Plus at nil margin under transitional service agreements.

Research and development expenditure for the year ended 31 March 2019 was £1.2 million (2018: £1.2 million).

Other income relates primarily to property rental income.

During the year, the group obtained the following services from its auditor:

	2019 £'000	2018 £'000
Audit services		
Statutory audit – group and company	**97**	84
Statutory audit – subsidiaries	**340**	295
	437	379
Non-audit services		
Regulatory audit services provided by the statutory auditor	**47**	46
Other non-audit services	**65**	80
	549	505

5 Investment income

	2019 £m	2018 £m
Interest receivable on short-term bank deposits held at amortised cost	**3.3**	1.5
Interest receivable on loans to joint ventures held at amortised cost (see note A6)	**4.3**	3.4
Net pension interest income (see note 18)	**9.5**	7.1
	17.1	12.0

6 Finance expense

	2019 £m	2018 £m
Interest payable		
Interest payable on borrowings held at amortised cost(1)	**232.0**	265.9
	232.0	265.9
Fair value (gains)/losses on debt and derivative instruments		
Fair value hedge relationships:		
Borrowings(2)	**47.4**	(149.2)
Designated swaps(2)(3)	**(29.7)**	159.6
	17.7	10.4
Financial instruments at fair value through profit or loss:		
Borrowings designated at fair value through profit or loss(4)	**32.8**	(27.8)
Associated swaps(5)(6)	**(37.1)**	63.7
	(4.3)	35.9
Fixed interest rate swaps(5)	**19.1**	(87.4)
Electricity swaps(7)	**–**	(8.0)
Net receipts on derivatives and debt under fair value option	**(40.6)**	(20.4)
Other swaps(5)(8)	**–**	2.2
Realisation of fair value loss on settlement of borrowings held at amortised cost(9)	**–**	23.1
Other	**(1.4)**	(3.1)
	(22.9)	(93.6)
Net fair value gains on debt and derivative instruments(10)	**(9.5)**	(47.3)
	222.5	218.6

Notes:

(1) Includes a £98.3 million (2018: £137.8 million) non-cash inflation uplift expense repayable on maturity in relation to the group's index-linked debt.

(2) Includes foreign exchange losses of £37.6 million (2018: £56.5 million gains). These gains/losses are largely offset by fair value losses/gains on derivatives.

(3) Under the provisions of IFRS 9 'Financial instruments', changes in fair value resulting from changes to the foreign currency basis spread (£2.2 million gain) are recognised in other comprehensive income rather than profit or loss as they relate to items designated in an accounting hedge relationship. In the prior year, there was an £8.1 million gain on designated swaps recognised within profit or loss.

(4) Under the provisions of IFRS 9 'Financial instruments', changes in fair value due to changes in the group's own credit risk (£6.6 million gain) are recognised in other comprehensive income rather than within profit or loss. In the prior year, there was a £24.0 million loss, which was recognised within profit or loss.

(5) These swap contracts are not designated within an IFRS 9 hedge relationship and are classed as 'held for trading' under the accounting standard. These derivatives form economic hedges and, as such, management intends to hold these through to maturity.

(6) Includes a £3.8 million gain caused by the settlement of certain cross-currency interest rate swap liabilities.

(7) From 1 April 2018, under the provisions of IFRS 9, electricity swaps have been designated within cash flow hedge relationships. Gains or losses resulting from the effective portion of the hedge are recognised within other comprehensive income in the cash flow hedge reserve. Any other gains or losses are recognised immediately in the income statement. The cash flow hedges are deemed to be fully effective and, therefore, have no impact on net fair value gains in the income statement. In the prior year, the electricity swaps were not designated within a hedge relationship and an £8.0 million gain was recognised in net fair value gains in the income statement.

(8) Includes fair value movements in relation to other economic hedge derivatives relating to debt held at amortised cost, which matured during the year ended 31 March 2018.

(9) The fair value loss in the prior year results from the partial close-out of £50.0 million RPI index-linked notes due April 2043. The portion of the notes closed out had a nominal value of £30.0 million (carrying value £41.3 million), and were purchased at a fair value of £64.4 million resulting in a £23.1 million fair value loss.

(10) Includes £30.6 million income (2018: £23.5 million) due to net interest on derivatives and debt under fair value option.

Interest payable is stated net of £37.4 million (2018: £39.7 million) borrowing costs capitalised in the cost of qualifying assets within property, plant and equipment and intangible assets during the year. This has been calculated by applying a capitalisation rate of 3.1 per cent (2018: 3.6 per cent) to expenditure on such assets as prescribed by IAS 23 'Borrowing Costs'.

7 Tax

	2019 £m	2018 £m
Current tax		
UK corporation tax	**41.6**	25.4
Adjustments in respect of prior years	**(2.8)**	(6.7)
Total current tax charge for the year	**38.8**	18.7
Deferred tax		
Current year	**35.4**	51.7
Adjustments in respect of prior years	**(1.4)**	7.1
Total deferred tax charge for the year	**34.0**	58.8
Total tax charge for the year	**72.8**	77.5

The adjustments in respect of prior years relate to agreement of prior years' UK tax matters.

The table below reconciles the notional tax charge at the UK corporation tax rate to the total tax charge and total effective tax rate for the year:

	2019 £m	2019 %	2018 £m	2018 %
Profit before tax	**436.2**		432.1	
Tax at the UK corporation tax rate	**82.9**	**19.0**	82.1	19.0
Adjustments in respect of prior years	**(4.2)**	**(1.0)**	0.4	0.1
Deferred tax rate adjustment/other	**(5.9)**	**(1.3)**	(5.0)	(1.2)
Total tax charge and effective tax rate for the year	**72.8**	**16.7**	77.5	17.9

The deferred tax rate adjustment/other mainly comprises the deferred tax movement calculated at the future tax rate from April 2020 of 17 per cent rather than the current rate of 19 per cent.

The adjustments in respect of prior years relate to agreement of prior years' UK tax matters.

For the current year, there is also an adjustment for items included in retained earnings, following the adoption of IFRS 15 (see accounting policies for further details).

The table below reconciles the notional tax charge at the UK corporation tax rate to the total current tax charge for the year:

	2019 £m	2018 £m
Profit before tax	**436.2**	432.1
Profit before tax multiplied by the standard rate of UK corporation tax of 19%	**82.9**	82.1
Relief for capital allowances in place of depreciation	**(91.0)**	(88.8)
Disallowance of depreciation charged in the accounts	**64.8**	60.6
Financial transactions timing differences	**1.0**	(13.3)
Pension timing differences	**(11.7)**	(11.0)
Relief for capitalised interest	**(7.1)**	(7.5)
Other timing differences	**4.5**	2.3
Adjustments to tax charge in respect of prior years	**(2.8)**	(6.7)
Joint venture profits	**(1.3)**	(0.4)
(Income not taxable)/expenses not deductible for tax purposes	**(1.8)**	0.4
Depreciation charged on non-qualifying assets	**1.3**	1.0
Current tax charge for the year	**38.8**	18.7

The group's current tax charge is lower than the UK headline rate of 19 per cent, primarily due to the availability of capital allowances; tax deductions in relation to capital expenditure available instead of accounting depreciation and put in place by successive governments to encourage such investment.

There are also various other adjustments where there is a simple timing difference between recognition of the income or expense in the accounts and in the related tax computations submitted to HMRC. These include unrealised profits or losses in relation to financing and related treasury derivatives, pension contributions and capitalised interest.

7 Tax continued

The year-on-year movement in financial transactions timing differences is sensitive to fair value movements on treasury derivatives and can, therefore, fluctuate significantly from year to year.

The joint venture profits are mainly our share of profits relating to AS Tallinna Vesi, which have already been fully taxed in Estonia.

For all of the timing differences, the corresponding deferred tax movements are at 17 per cent as the rate of corporation tax will reduce to 17 per cent from April 2020.

Tax on items taken directly to equity	2019 £m	2018 £m
Deferred tax (see note 19)		
On remeasurement gains on defined benefit pension schemes	**12.4**	8.5
On net fair value gains recognised in other comprehensive income	**0.8**	–
Total tax charge on items taken directly to equity	**13.2**	8.5

8 Earnings per share

	2019 £m	2018 £m
Profit after tax attributable to equity holders of the company	**363.4**	354.6

	2019 pence	2018 pence
Earnings per share		
Basic	**53.3**	52.0
Diluted	**53.2**	51.9

Basic earnings per share is calculated by dividing profit after tax for the financial year attributable to equity holders of the company by 681.9 million, being the weighted average number of shares in issue during the year (2018: 681.9 million). Diluted earnings per share is calculated by dividing profit after tax for the financial year attributable to equity holders of the company by 683.4 million, being the weighted average number of shares in issue during the year including dilutive shares (2018: 683.1 million).

The difference between the weighted average number of shares used in the basic and the diluted earnings per share calculations represents those ordinary shares deemed to have been issued for no consideration on the conversion of all potential dilutive ordinary shares in accordance with IAS 33 'Earnings per Share'. Potential dilutive ordinary shares comprise outstanding share options awarded to directors and certain employees (see note 3).

The weighted average number of shares can be reconciled to the weighted average number of shares, including dilutive shares, as follows:

	2019 million	2018 million
Average number of ordinary shares – basic	**681.9**	681.9
Effect of potential dilutive ordinary shares – share options	**1.5**	1.2
Average number of ordinary shares – diluted	**683.4**	683.1

9 Dividends

	2019 £m	2018 £m
Amounts recognised as distributions to equity holders of the company in the year comprise:		
Ordinary shares		
Final dividend for the year ended 31 March 2018 at 26.49 pence per share (2017: 25.92 pence)	**180.6**	176.7
Interim dividend for the year ended 31 March 2019 at 13.76 pence per share (2018: 13.24 pence)	**93.8**	90.3
	274.4	267.0
Proposed final dividend for the year ended 31 March 2019 at 27.52 pence per share (2018: 26.49 pence)	**187.7**	180.6

The proposed final dividends for the years ended 31 March 2019 and 31 March 2018 were subject to approval by equity holders of United Utilities Group PLC as at the reporting dates, and hence have not been included as liabilities in the consolidated financial statements at 31 March 2019 and 31 March 2018.

10 Property, plant and equipment

Group	Land and buildings £m	Infra-structure assets £m	Operational assets £m	Fixtures, fittings, tools and equipment £m	Assets in course of construction £m	Total £m
Cost						
At 1 April 2017	354.2	5,243.1	7,033.2	496.8	942.3	14,069.6
Additions	2.4	70.7	122.2	10.1	535.9	741.3
Transfers	12.0	72.6	141.8	23.4	(249.8)	–
Disposals	(1.4)	(0.1)	(46.4)	(3.7)	–	(51.6)
At 31 March 2018	**367.2**	**5,386.3**	**7,250.8**	**526.6**	**1,228.4**	**14,759.3**
Additions	**5.5**	**60.8**	**126.3**	**11.6**	**522.0**	**726.2**
Transfers	**(12.1)**	**43.3**	**87.3**	**6.5**	**(125.0)**	**–**
Disposals	**(0.9)**	**–**	**(42.3)**	**(6.5)**	**–**	**(49.7)**
At 31 March 2019	**359.7**	**5,490.4**	**7,422.1**	**538.2**	**1,625.4**	**15,435.8**
Accumulated depreciation						
At 31 March 2017	111.6	345.9	2,870.7	335.9	–	3,664.1
Charge for the year	9.4	39.5	260.9	38.6	–	348.4
Disposals	(1.3)	–	(39.3)	(3.1)	–	(43.7)
At 31 March 2018	**119.7**	**385.4**	**3,092.3**	**371.4**	**–**	**3,968.8**
Charge for the year	**8.3**	**35.4**	**279.3**	**34.3**	**–**	**357.3**
Transfers	**(0.5)**	**0.5**	**–**	**–**	**–**	**–**
Disposals	**(0.6)**	**–**	**(37.7)**	**(5.4)**	**–**	**(43.7)**
At 31 March 2019	**126.9**	**421.3**	**3,333.9**	**400.3**	**–**	**4,282.4**
Net book value at 31 March 2018	247.5	5,000.9	4,158.5	155.2	1,228.4	10,790.5
Net book value at 31 March 2019	**232.8**	**5,069.1**	**4,088.2**	**137.9**	**1,625.4**	**11,153.4**

During the year ended 31 March 2019, there was a transfer of £17.8 million cost and associated £0.5 million accumulated depreciation from land and buildings to infrastructure assets following a data cleanse exercise in respect of the fixed asset register.

At 31 March 2019, the group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £300.7 million (2018: £430.1 million).

In addition to these commitments, the group has long-term expenditure plans which include investments to achieve improvements in performance required by regulators and to provide for future growth.

Company

The company had no property, plant and equipment or contractual commitments for the acquisition of property, plant and equipment at 31 March 2019 or 31 March 2018.

11 Intangible assets

Group	Total £m
Cost	
At 1 April 2017	357.2
Additions	38.4
At 31 March 2018	**395.6**
Additions	**40.9**
At 31 March 2019	**436.5**
Accumulated amortisation	
At 1 April 2017	169.5
Charge for the year	28.4
At 31 March 2018	**197.9**
Charge for the year	**35.9**
At 31 March 2019	**233.8**
Net book value at 31 March 2018	197.7
Net book value at 31 March 2019	**202.7**

The group's intangible assets relate mainly to computer software.

At 31 March 2019, the group had entered into contractual commitments for the acquisition of intangible assets amounting to £1.5 million (2018: £2.8 million).

Company

The company had no intangible assets or contractual commitments for the acquisition of intangible assets at 31 March 2019 or 31 March 2018.

12 Joint ventures

Group	£m
At 1 April 2017	75.2
Share of profits of joint ventures	2.3
Dividends received from joint ventures	(3.3)
Currency translation differences	1.0
At 31 March 2018	**75.2**
Share of profits of joint ventures	**6.7**
Dividends received from joint ventures	**(2.2)**
Currency translation differences	**(0.7)**
At 31 March 2019	**79.0**

The group's interests in joint ventures mainly comprise its interests in Water Plus Group Limited (Water Plus) and AS Tallinna Vesi (Tallinn Water). Water Plus is jointly owned and controlled by the group and Severn Trent PLC under a joint venture agreement. Joint management of Tallinn Water is based on a shareholders' agreement.

As at 31 March 2019, the carrying value of the group's equity interest in Water Plus was £36.7 million (2018: £37.3 million), which includes £16.9 million (2018: £16.9 million) representing the group's 50 per cent share of goodwill included in Water Plus's statement of financial position.

Following a deterioration in the working capital position of Water Plus since the non-household water retail market in England opened to competition on 1 April 2017, the carrying value of the group's interest in the Water Plus joint venture has been assessed relative to its estimated recoverable amount in order to determine whether it is impaired. In performing this assessment, consideration has been given to information provided by Water Plus, including the results of its own impairment testing carried out in respect of its goodwill and intangible assets in accordance with IAS 36 'Impairment of Assets'. Having reviewed and challenged this information, the group estimates that the recoverable amount of the Water Plus joint venture is in excess of its carrying value and therefore no impairment is required.

The recoverable amount has been calculated based on Water Plus's value in use, which is determined by discounting the estimated future cash flows of the Water Plus business to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the business, for which estimates of future cash flows have not been adjusted.

12 Joint ventures continued

The cash flows used in the value in use assessment go out to 31 March 2024, with a terminal growth rate of 2.0 per cent applied at this date based on long-term projections of CPIH, to which Water Plus's cash flows tend to be aligned. These cash flows were based on Water Plus's five-year business plan as agreed with its board, and were discounted using a pre-tax discount rate of 8.0 per cent based on a CAPM model underpinned by observable inputs.

The key assumptions to which the recoverable amount is most sensitive are the forecast future cash flows, which are subject to the delivery of Water Plus's business plan, and the discount rate. These therefore represent key areas of estimation uncertainty. At 31 March 2019, the estimated recoverable amount of the group's interest in the Water Plus joint venture exceeded its carrying amount by £59.5 million. An increase in the discount rate to 10.4 per cent or a reduction in forecast cash flows of 25 per cent, both of which are considered reasonably possible, would have, in isolation, led to an impairment loss being recognised for the year ended 31 March 2019.

In addition to the equity interest in the Water Plus joint venture, the group has issued loans of £142.1 million to Water Plus, further details of which can be found in note A6. At 31 March 2019, these loans were deemed to be fully recoverable.

As at 31 March 2019, the carrying value of the group's 35.3 per cent interest in Tallinn Water was £42.4 million (2018: £38.0 million). Tallinn Water has disclosed a contingent liability of EUR 28.6 million in its latest financial statements relating to possible third-party claims. If this contingent liability materialises in the future, this would impact the group's share of profits of the joint venture and the joint venture's carrying value under the equity method of accounting. In addition, Tallinn Water is currently involved in a regulatory dispute, the outcome of which is currently uncertain. At this stage, the group does not consider this to be an indicator that its interest in Tallinn Water may be impaired.

There are no restrictions on the ability of the group's joint ventures to transfer funds to the group in the form of cash dividends, or to repay loans or advances made by the group.

Details of transactions between the group and its joint ventures are disclosed in note A6.

Company

The company had no investments in joint ventures at either 31 March 2019 or 31 March 2018.

13 Investments

Group	£m
At 1 April 2017	9.0
Reduction in investment stake	(1.0)
Currency translation differences	(0.9)
At 31 March 2018	**7.1**
Change in fair value	**4.4**
Reduction in investment stake	**(1.0)**
Currency translation differences	**1.0**
At 31 March 2019	**11.5**

During the year, the group reduced its investment in Muharraq Holding Company 1 Limited through a £1.0 million (2018: £1.0 million) repayment of a shareholder loan.

At 31 March 2019, the group's investments mainly comprised its investment in Muharraq Holding Company 1 Limited. These investments are held at fair value.

Company

At 31 March 2019, the company's investments related solely to its investments in United Utilities PLC, which was recorded at a cost of £6,326.8 million (2018: £6,326.8 million).

14 Inventories

Group	2019 £m	2018 £m
Properties held for resale	**4.7**	9.0
Other inventories	**10.2**	7.8
	14.9	16.8

Company

The company had no inventories at 31 March 2019 or 31 March 2018.

15 Trade and other receivables

	Group		Company	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Trade receivables	**102.2**	116.7	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**82.2**	74.2
Amounts owed by related parties (see note A6)	**182.9**	179.7	**–**	–
Other debtors and prepayments	**34.4**	40.8	**–**	–
Accrued income	**78.1**	64.8	**–**	–
	397.6	402.0	**82.2**	74.2

At 31 March 2019, the group had £148.1 million (2018: £141.1 million) of trade and other receivables classified as non-current, of which £143.5 million (2018: £137.2 million) was owed by related parties.

The carrying amounts of trade and other receivables approximates to their fair value at 31 March 2019 and 31 March 2018.

Trade receivables do not carry interest and are stated net of allowances for bad and doubtful receivables, an analysis of which is as follows:

Group	**2019 £m**	2018 £m
At the start of the year	**63.4**	85.4
Amounts charged to operating expenses (see note 4)	**26.5**	20.8
Trade receivables written off	**(33.4)**	(44.6)
Amounts charged to deferred income	**–**	1.6
Amounts charged to infrastructure renewals expenditure	**–**	0.2
At the end of the year	**56.5**	63.4

Amounts charged to deferred income relate to amounts invoiced for which revenue has not yet been recognised in the income statement.

Amounts charged to infrastructure renewals expenditure relate to amounts invoiced in relation to contributions towards the cost of infrastructure renewals incurred as a result of carrying out infrastructure diversions works.

At each reporting date, the group evaluates the recoverability of trade receivables and records allowances for doubtful receivables based on experience.

At 31 March 2019 and 31 March 2018, the group had no trade receivables that were past due and not individually impaired.

The following table provides information regarding the ageing of net trade receivables that were past due and individually impaired:

Trade receivables	**Aged less than one year £m**	**Aged between one year and two years £m**	**Aged greater than two years £m**	**Carrying value £m**
At 31 March 2019	**63.8**	**25.6**	**1.8**	**91.2**
At 31 March 2018	77.5	24.4	4.2	106.1

At 31 March 2019, the group had £11.0 million (2018: £10.6 million) of trade receivables that were not past due.

Company

At 31 March 2019 and 31 March 2018, the company had no trade receivables that were past due.

The carrying amount of trade and other receivables approximates to their fair value at 31 March 2019 and 31 March 2018.

16 Cash and cash equivalents

	Group		Company	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Cash at bank and in hand	**4.7**	1.0	**–**	–
Short-term bank deposits	**334.6**	509.0	**–**	–
Cash and short-term deposits	**339.3**	510.0	**–**	–
Book overdrafts (included in borrowings, see note 17)	**(14.7)**	(12.6)	**(0.5)**	(0.5)
Cash and cash equivalents in the statement of cash flows	**324.6**	497.4	**(0.5)**	(0.5)

Cash and short-term deposits include cash at bank and in hand, deposits, and other short-term highly liquid investments which are readily convertible into known amounts of cash and have a maturity of three months or less. The carrying amounts of cash and cash equivalents approximate their fair value.

Book overdrafts, which result from normal cash management practices, represent the value of cheques issued and payments initiated that had not cleared as at the reporting date.

17 Borrowings

Group	**2019 £m**	2018 £m
Non-current liabilities		
Bonds	**4,814.6**	4,723.4
Bank and other term borrowings	**2,301.0**	2,349.4
	7,115.6	7,072.8
Current liabilities		
Bonds	**441.9**	583.2
Bank and other term borrowings	**243.6**	243.7
Book overdrafts (see note 16)	**14.7**	12.6
	700.2	839.5
	7,815.8	7,912.3

For further details of the principal economic terms and conditions of outstanding borrowings see note A3.

Company	**2019 £m**	2018 £m
Non-current liabilities		
Amounts owed to subsidiary undertakings	**1,718.4**	1,690.3
	1,718.4	1,690.3
Current liabilities		
Book overdrafts (see note 16)	**0.5**	0.5
	0.5	0.5
	1,718.9	1,690.8

Borrowings are unsecured and are measured at amortised cost. The carrying amounts of borrowings approximate their fair value.

18 Retirement benefit surplus

Defined benefit schemes

The net pension expense before tax recognised in the income statement in respect of the defined benefit pension schemes is summarised as follows:

Group	**2019 £m**	2018 £m
Current service cost	**6.2**	27.3
Curtailments/settlements	**9.0**	2.3
Administrative expenses	**2.8**	2.6
Pension expense charged to operating profit	**18.0**	32.2
Net pension interest income credited to investment income (see note 5)	**(9.5)**	(7.1)
Net pension expense charged before tax	**8.5**	25.1

Defined benefit pension costs excluding curtailments/settlements included within employee benefit expense were £9.0 million (2018: £29.9 million) comprising current service costs and administrative expenses. Total post-employment benefits expense excluding curtailments/settlements charged to operating profit of £32.0 million (2018: £42.0 million) comprise the defined benefit costs described above of £9.0 million (2018: £29.9 million) and defined contribution pension costs of £23.0 million (2018: £12.1 million) (see note 3).

Included within curtailments/settlements is £6.6 million (2018: £nil) relating to the equalisation of GMP benefits (see note A5 for further details).

18 Retirement benefit surplus continued

The reconciliation of the opening and closing net pension surplus included in the statement of financial position is as follows:

Group	2019 £m	2018 £m
At the start of the year	344.2	247.5
Expense recognised in the income statement	(8.5)	(25.1)
Contributions paid	75.2	71.6
Remeasurement gains gross of tax	73.0	50.2
At the end of the year	**483.9**	344.2

Included in the contributions paid of £75.2 million (2018: £71.6 million) were deficit repair contributions of £66.1 million (2018: £43.0 million), enhancements to benefits provided on redundancy of £1.6 million (2018: £1.5 million), administration expenses of £0.5 million (2018: £0.6 million) and an inflation funding mechanism payment of £nil made during the year (2018: £0.4 million). Following the 2018 actuarial valuation, contributions in relation to current service cost decreased to £7.0 million (2018: £26.2 million; 2016 actuarial valuation).

Remeasurement gains and losses are recognised directly in the statement of comprehensive income.

Group	2019 £m	2018 £m
The return on plan assets, excluding amounts included in interest	58.5	(60.0)
Actuarial (losses)/gains arising from changes in financial assumptions	(160.6)	85.1
Actuarial gains arising from changes in demographic assumptions	70.9	43.2
Actuarial gains/(losses) arising from experience	104.2	(18.1)
Remeasurement gains on defined benefit pension schemes	**73.0**	50.2

For more information in relation to the group's defined benefit pension schemes see note A5.

Defined contribution schemes

During the year, the group made £23.0 million (2018: £12.1 million) of contributions to defined contribution schemes which are included in employee benefits expense (see note 3).

Company

The company did not participate in any of the group's pension schemes during the years ended 31 March 2019 and 31 March 2018.

19 Deferred tax liabilities

The following are the major deferred tax liabilities and assets recognised by the group, and the movements thereon, during the current and prior year:

Group	Accelerated tax depreciation £m	Retirement benefit obligations £m	Other £m	Total £m
At 1 April 2017	1,011.4	42.1	(22.0)	1,031.5
Charged to the income statement (see note 7)	38.5	7.9	12.4	58.8
Charged to equity (see note 7)	–	8.5	–	8.5
At 31 March 2018	1,049.9	58.5	(9.6)	1,098.8
Charged/(credited) to the income statement (see note 7)	26.8	11.3	(4.1)	34.0
Charged to equity (see note 7)	–	12.4	0.8	13.2
At 31 March 2019	**1,076.7**	**82.2**	**(12.9)**	**1,146.0**

Certain deferred tax assets and liabilities have been offset in accordance with IAS 12 'Income Taxes'.

Company

The company had no deferred tax assets or liabilities at 31 March 2019 or 31 March 2018.

20 Provisions

Group	Severance £m	Other £m	Total £m
At 1 April 2017	3.7	22.8	26.5
Charged to the income statement	3.7	1.0	4.7
Utilised in the year	(4.8)	(4.3)	(9.1)
At 31 March 2018	**2.6**	**19.5**	**22.1**
Charged to the income statement	**4.8**	**(0.3)**	**4.5**
Utilised in the year	**(4.6)**	**(5.2)**	**(9.8)**
At 31 March 2019	**2.8**	**14.0**	**16.8**

The group had no provisions classed as non-current at 31 March 2019 or 31 March 2018.

The severance provision as at 31 March 2019 and 31 March 2018 relates to severance costs as a result of group reorganisation.

Other provisions principally relate to contractual, legal and environmental claims against the group and represent management's best estimate of the value of settlement, the timing of which is dependent on the resolution of the relevant legal claims.

Company

The company had no provisions at 31 March 2019 or 31 March 2018.

21 Trade and other payables

	Group		Company	
Non-current	**2019 £m**	2018 £m	**2019 £m**	2018 £m
Deferred grants and contributions	**671.2**	617.0	**–**	–
Other creditors	**26.1**	25.7	**–**	–
	697.3	642.7	**–**	–

	Group		Company	
Current	**2019 £m**	2018 £m	**2019 £m**	2018 £m
Trade payables	**34.4**	27.9	**–**	–
Amounts owed to subsidiary undertakings	**–**	–	**12.4**	9.0
Amounts owed to related parties	**0.6**	1.4	**–**	–
Other tax and social security	**5.4**	5.3	**–**	–
Deferred grants and contributions	**13.3**	8.8	**–**	–
Accruals and other creditors	**232.7**	191.7	**2.3**	2.3
Deferred income	**34.8**	40.6	**–**	–
	321.2	275.7	**14.7**	11.3

The average credit period taken for trade purchases is 25 days (2018: 23 days).

The carrying amounts of trade and other payables approximates to their fair value at 31 March 2019 and 31 March 2018.

Deferred grants and contributions

Group	2019 £m	2018 £m
At the start of the year	**625.8**	579.2
Amounts capitalised during the year	**35.7**	23.7
Transfers of assets from customers	**39.4**	34.2
Credited to retained earnings – impact of adoption of IFRS 15 'Revenue from contracts with customers'	**(2.6)**	–
Credited to the income statement – revenue	**(12.9)**	(3.3)
Credited to the income statement – other operating costs (see note 4)	**(0.5)**	(6.4)
Credited to allowance for bad and doubtful receivables	**(0.4)**	(1.6)
At the end of the year	**684.5**	625.8

22 Other reserves

	Cumulative exchange reserve £m	Merger reserve £m	Cost of hedging reserve £m	Cash flow hedging reserve £m	Total £m
At 31 March 2018	**(1.8)**	**329.7**	**–**	**–**	**327.9**
Adjustment on initial application of IFRS 9	**(1.1)**	**–**	**13.8**	**–**	**12.7**
At 1 April 2018	**(2.9)**	**329.7**	**13.8**	**–**	**340.6**
Other comprehensive income					
Change in fair value recognised in other comprehensive income	**–**	**–**	**(2.2)**	**3.5**	**1.3**
Amounts reclassified from other comprehensive income to profit or loss	**–**	**–**	**–**	**(3.1)**	**(3.1)**
Tax on items taken directly to equity	**–**	**–**	**0.4**	**(0.1)**	**0.3**
Foreign exchange adjustments	**(0.8)**	**–**	**–**	**–**	**(0.8)**
At 31 March 2019	**(3.7)**	**329.7**	**12.0**	**0.3**	**338.3**

	Cumulative exchange reserve £m	Merger reserve £m	Cost of hedging reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2017	(2.0)	329.7	–	–	327.7
Other comprehensive income					
Foreign exchange adjustments	0.2	–	–	–	0.2
Total comprehensive income	0.2	–	–	–	0.2
At 31 March 2018	(1.8)	329.7	–	–	327.9

The merger reserve arose in the year ended 31 March 2009 on consolidation and represents the capital adjustment to reserves required to effect the reverse acquisition of United Utilities PLC by United Utilities Group PLC.

On adoption of IFRS 9, the group has recognised the cost of hedging reserve as a new component of equity during the year. This reserve reflects accumulated fair value movements on cross-currency swaps resulting from changes in the foreign currency basis spread, which represents a liquidity charge inherent in foreign exchange contracts for exchanging currencies and is excluded from the designation of cross-currency swaps as hedging instruments.

On adoption of IFRS 9, the group designated a number of swaps hedging non-financial risks in cash flow hedge relationships in order to give a more representative view of operating costs. Fair value movements relating to the effective part of these swaps are recognised in other comprehensive income and accumulated in the cash flow hedging reserve.

23 Share capital

Group and company	2019 million	2019 £m	2018 million	2018 £m
Issued, called up and fully paid				
Ordinary shares of 5.0 pence each	**681.9**	**34.1**	681.9	34.1
Deferred shares of 170.0 pence each	**274.0**	**465.7**	274.0	465.7
	955.9	**499.8**	955.9	499.8

Details of the voting rights of each category of shares can be found within the directors' report on page 148.

The 170.0 pence deferred shares were created to facilitate a return of capital to shareholders following the reverse acquisition of United Utilities PLC by United Utilities Group PLC in the year ended 31 March 2009 (see company statement of changes in equity on page 165), and represent the amount of a special dividend paid on B shares at that time. The deferred shares convey no right to income, no right to vote and no appreciable right to participate in any surplus capital in the event of a winding up.

24 Operating lease commitments

Group	Property 2019 £m	Plant and equipment 2019 £m	Property 2018 £m	Plant and equipment 2018 £m
Commitments under non-cancellable operating leases due				
Within one year	**2.6**	**0.5**	2.6	0.6
In the second to fifth years inclusive	**9.0**	**0.4**	9.4	0.4
After five years	**279.8**	**–**	279.9	–
	291.4	**0.9**	291.9	1.0

In respect of the group's commitment to significant property leases, there are no contingent rentals payable, or restrictions on dividends, debt or further leasing imposed by these lease arrangements. Wherever possible, the group ensures that it has the benefit of security of tenure where this is required by operational and accommodation strategies. Escalation of rents is via rent reviews at agreed intervals.

The company had no operating lease commitments at 31 March 2019 or 31 March 2018.

25 Contingent liabilities

The group has determined that the possibility of any outflow in respect of performance guarantees issued is remote and, as such, there are no contingent liabilities to be disclosed in respect of these (2018: none).

The company has not entered into performance guarantees as at 31 March 2019 or 31 March 2018.

26 Events after the reporting period

After the reporting period, the group paid accelerated deficit repair contributions of £103.0 million to its defined benefit pension schemes, further details of which are included in note A5. In addition to this, the group increased its CPI-linked debt by executing a £100 million CPI-linked bank loan with a 10-year maturity, and entered into inflation swaps against three existing RPI-linked bonds with aggregate notional value of £100.4 million, swapping cash flows from RPI- to CPI-linkage. None of these events have been included in the financial statements for the year ended 31 March 2019 as they represent non-adjusting events after the reporting period.

Notes to the financial statements – appendices

A1 Cash generated from operations

	Group		Company	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Profit before tax	**436.2**	432.1	**243.8**	241.7
Adjustment for investment income (see note 5) and finance expense (see note 6)	**205.4**	206.6	**30.5**	25.4
Adjustment for share of profits of joint ventures (see note 12)	**(6.7)**	(2.3)	**–**	–
Operating profit	**634.9**	636.4	**274.3**	267.1
Adjustments for:				
Depreciation of property, plant and equipment (see note 10)	**357.3**	348.4	**–**	–
Amortisation of intangible assets (see note 11)	**35.9**	28.4	**–**	–
Loss on disposal of property, plant and equipment (see note 4)	**3.9**	6.8	**–**	–
Amortisation of deferred grants and contributions (see note 21)	**(12.9)**	(6.4)	**–**	–
Equity-settled share-based payments charge (see note 3)	**4.0**	3.2	**–**	–
Other non-cash movements	**–**	(3.3)	**–**	–
Changes in working capital:				
Decrease in inventories (see note 14)	**1.9**	5.6	**–**	–
Decrease in trade and other receivables	**11.7**	27.5	**4.4**	3.5
Increase/(decrease) in trade and other payables	**21.3**	(13.0)	**0.1**	0.6
Decrease in provisions (see note 20)	**(5.3)**	(4.4)	**–**	–
Pension contributions paid less pension expense charged to operating profit	**(57.2)**	(39.4)	**–**	–
Cash generated from operations	**995.5**	989.8	**278.8**	271.2

The group has received property, plant and equipment of £39.4 million (2018: £34.2 million) in exchange for the provision of future goods and services (see notes 21 and A7).

A2 Net debt

Group	**2019 £m**	2018 £m
At the start of the year	**6,867.8**	6,578.7
Net capital expenditure	**624.9**	701.0
Dividends (see note 9)	**274.4**	267.0
Interest	**135.7**	138.7
Inflation uplift on index-linked debt (see note 6)	**98.3**	137.8
Tax	**27.5**	35.5
Loans to joint ventures	**6.0**	26.5
Fair value movements:		
Net fair value gains on debt and derivative instruments recognised in finance expense (see note 6)	**(9.5)**	(47.3)
Net fair value gains on debt and derivative instruments recognised in other comprehensive income (see note 22)	**(4.8)**	–
Less: net receipts on derivatives and debt under fair value option (see note 6)	**40.6**	20.4
Less: foreign exchange gains on investments measured at fair value through profit or loss	**1.0**	–
Other	**0.9**	(0.7)
Cash generated from operations (see note A1)	**(995.5)**	(989.8)
At the end of the year	**7,067.3**	6,867.8

Net debt comprises borrowings, net of cash and short-term deposits and derivatives. As such, movements in net debt during the year reflected in the above reconciliation are impacted by net cash generated from financing activities as disclosed in the consolidated statement of cash flows.

The movements from financing activities is £274.4 million (2018: £267.0 million), which relates solely to dividend movements. Other financing movements in the statement of cash flows, such as proceeds from borrowings and repayment of borrowings, do not affect the total net debt figure as the cash generated or used in these activities offsets against the associated decrease or increase in liabilities.

Of the total increase in net debt in the year, £126.5 million (2018: £110.2 million) relates to non-cash movements.

Notes to the financial statements – appendices

A3 Borrowings

Terms and debt repayment schedule

The principal economic terms and conditions of outstanding borrowings, along with fair value and carrying value, were as follows:

	Currency	Year of final repayment	Fair value 2019 £m	Carrying value 2019 £m	Fair value 2018 £m	Carrying value 2018 £m
Borrowings in fair value hedge relationships			**2,749.3**	**2,765.8**	2,905.9	2,895.3
5.375% 150m bond	GBP	2018	–	–	157.9	150.8
4.55% 250m bond	USD	2018	–	–	181.2	178.8
5.375% 350m bond	USD	2019	–	–	256.5	253.6
4.25% 500m bond	EUR	2020	**449.7**	**441.9**	478.8	466.4
5.75% 375m bond	GBP	2022	**424.5**	**406.2**	435.3	411.5
2.0% 450m bond	GBP	2025	**453.1**	**456.7**	299.6	301.5
2.867% 320m bond	HKD	2026	**31.5**	**32.3**	–	–
2.92% 739m bond	HKD	2026	**72.7**	**74.9**	65.9	66.9
1.129% 52m bond	EUR	2027	**45.2**	**46.0**	45.0	44.5
2.37% 830m bond	HKD	2027	**78.7**	**82.0**	70.6	72.4
5.625% 300m bond	GBP	2027	**390.7**	**393.5**	388.6	393.2
5.02% JPY 10bn dual currency loan	JPY/USD	2029	**92.0**	**99.4**	86.9	95.0
2.058% 30m bond	EUR	2030	**26.9**	**27.9**	27.0	26.7
2.625% 250m bond	GBP	2031	**260.0**	**253.0**	–	–
1.641% 30m bond	EUR	2031	**26.2**	**26.4**	25.7	25.0
2.9% 600m bond	HKD	2031	**58.9**	**56.3**	52.4	48.3
1.707% 28m bond	EUR	2032	**24.3**	**26.0**	23.9	24.7
1.653% 26m bond	EUR	2032	**22.3**	**23.7**	21.9	22.4
1.70% 30m bond	EUR	2033	**25.8**	**27.9**	25.4	26.4
5.0% 200m bond	GBP	2035	**266.8**	**291.7**	263.3	287.2
Borrowings designated at fair value through profit or loss			**373.9**	**373.9**	347.7	347.7
6.875% 400m bond	USD	2028	**373.9**	**373.9**	347.7	347.7
Borrowings measured at amortised cost			**5,781.9**	**4,676.1**	5,798.4	4,669.3
Short-term bank borrowings – fixed	GBP	2019	**152.0**	**152.0**	161.5	161.5
1.61%+RPI 50m EIB IL loan	GBP	2020	**68.5**	**65.3**	67.6	63.7
1.73%+RPI 50m EIB IL loan	GBP	2020	**68.5**	**65.2**	67.8	63.6
1.84%+RPI 50m EIB IL loan	GBP	2020	**68.6**	**65.1**	67.9	63.5
1.90%+RPI 50m EIB IL loan	GBP	2020	**68.6**	**65.1**	67.9	63.4
1.93%+RPI 50m EIB IL loan	GBP	2020	**68.6**	**65.0**	67.9	63.4
1.88%+RPI 50m EIB IL loan	GBP	2020	**68.4**	**64.9**	67.7	63.3
2.10%+RPI 50m EIB IL loan	GBP	2020	**68.6**	**64.8**	68.0	63.2
2.46%+RPI 50m EIB IL loan	GBP	2020	**69.0**	**64.9**	68.6	63.2
0.80%+LIBOR 100m loan	GBP	2022	**102.6**	**100.0**	102.6	100.0
0.47%+RPI 100m IL loan	GBP	2023	**121.3**	**115.0**	117.9	112.2
0.49%+RPI 100m IL loan	GBP	2025	**120.3**	**110.7**	116.2	107.9
0.013%+RPI 25m IL bond	GBP	2025	**29.9**	**27.6**	28.1	26.9
0.1275%+RPI 100m IL loan	GBP	2026	**117.5**	**109.2**	111.7	106.5
0.01%+RPI 20m IL bond	GBP	2028	**23.4**	**23.2**	22.1	22.9
1.23%+RPI 50m EIB (amortising) IL loan	GBP	2029	**48.1**	**44.2**	51.2	47.4
1.29%+RPI 50m EIB (amortising) IL loan	GBP	2029	**50.5**	**46.1**	53.4	49.2
1.12%+RPI 50m EIB (amortising) IL loan	GBP	2029	**49.7**	**45.7**	52.6	48.8
1.10%+RPI 50m EIB (amortising) IL loan	GBP	2029	**49.7**	**45.7**	52.5	48.8
0.75%+RPI 50m EIB (amortising) IL loan	GBP	2029	**50.3**	**46.8**	52.9	49.8
0.76%+RPI 50m EIB (amortising) IL loan	GBP	2030	**50.3**	**46.6**	52.8	49.6
1.15%+RPI 50m EIB (amortising) IL loan	GBP	2030	**51.0**	**46.5**	53.7	49.4
1.11%+RPI 50m EIB (amortising) IL loan	GBP	2030	**51.1**	**46.6**	53.7	49.6
0.178%+RPI 35m IL bond	GBP	2030	**43.3**	**38.6**	40.4	37.6
0.245%+CPI 20m IL bond	GBP	2031	**21.2**	**21.0**	20.3	20.6

A3 Borrowings continued

	Currency	Year of final repayment	**Fair value 2019 £m**	**Carrying value 2019 £m**	Fair value 2018 £m	Carrying value 2018 £m
Borrowings measured at amortised cost (continued)						
0.01%+RPI 38m IL bond	GBP	2031	**44.7**	**43.3**	42.4	42.6
3.375%+RPI 50m IL bond	GBP	2032	**126.2**	**79.5**	122.4	76.9
0.709%+LIBOR 100m EIB (amortising) loan	GBP	2032	**81.0**	**81.2**	86.6	87.5
0.691%+LIBOR 150m EIB (amortising) loan	GBP	2032	**126.0**	**126.6**	134.4	135.9
0.573%+LIBOR 100m EIB (amortising) loan	GBP	2033	**86.4**	**87.5**	92.0	93.8
0.511%+LIBOR 150m EIB (amortising) loan	GBP	2033	**133.6**	**135.9**	141.6	145.3
0.01%+RPI 100m EIB (amortising) IL loan	GBP	2033	**106.7**	**102.2**	109.6	106.4
0.01%+RPI 75m EIB (amortising) IL loan	GBP	2034	**80.0**	**76.6**	82.2	79.7
0.01%+RPI 75m EIB (amortising) IL loan	GBP	2034	**82.3**	**78.7**	81.8	79.3
0.01%+RPI 75m EIB (amortising) IL loan	GBP	2034	**82.3**	**78.7**	81.8	79.3
1.9799%+RPI 100m IL bond	GBP	2035	**217.8**	**148.6**	208.3	143.9
0.873%+LIBOR 100m EIB (amortising) loan	GBP	2035	**100.6**	**100.0**	99.6	100.0
0.840%+LIBOR 75m EIB (amortising) loan	GBP	2035	**75.9**	**75.0**	75.2	75.0
0.01%+RPI 26.5m IL bond	GBP	2036	**31.7**	**33.2**	30.1	31.8
0.379%+CPI 20m IL bond	GBP	2036	**21.3**	**21.0**	20.7	20.6
0.01%+RPI 29m IL bond	GBP	2036	**34.6**	**32.3**	32.9	32.5
0.093%+CPI 60m IL bond	GBP	2037	**60.6**	**62.5**	58.8	61.4
1.66%+RPI 35m IL bond	GBP	2037	**62.9**	**47.7**	61.9	46.5
2.40%+RPI 70m IL bond	GBP	2039	**138.0**	**93.0**	135.9	90.7
1.7829%+RPI 100m IL bond	GBP	2040	**221.9**	**147.0**	219.0	142.4
1.3258%+RPI 50m IL bond	GBP	2041	**102.9**	**73.4**	100.7	71.1
1.5802%+RPI 100m IL bond	GBP	2042	**215.5**	**146.6**	214.7	142.0
1.5366%+RPI 50m IL bond	GBP	2043	**43.6**	**29.2**	43.2	28.3
1.397%+RPI 50m IL bond	GBP	2046	**109.3**	**73.3**	109.1	71.0
0.359%+CPI 32m IL bond	GBP	2048	**32.3**	**32.9**	32.0	32.4
1.7937%+RPI 50m IL bond	GBP	2049	**122.9**	**72.9**	122.9	70.7
Commission for New Towns (amortising) loan – fixed	GBP	2053	**54.6**	**27.4**	56.2	27.9
1.847%+RPI 100m IL bond	GBP	2056	**229.9**	**143.9**	232.2	140.3
1.815%+RPI 100m IL bond	GBP	2056	**228.0**	**143.3**	231.7	139.8
1.662%+RPI 100m IL bond	GBP	2056	**221.6**	**143.0**	222.0	139.5
1.5865%+RPI 50m IL bond	GBP	2056	**109.3**	**71.5**	109.2	69.7
1.591%+RPI 25m IL bond	GBP	2056	**54.6**	**35.6**	54.7	34.8
1.556%+RPI 50m IL bond	GBP	2056	**108.8**	**71.1**	108.6	69.3
1.435%+RPI 50m IL bond	GBP	2056	**106.1**	**70.8**	105.9	69.1
1.3805%+RPI 35m IL bond	GBP	2056	**73.5**	**49.6**	73.5	48.4
1.585%+RPI 100m IL bond	GBP	2057	**215.3**	**137.6**	218.9	134.2
0.387%+CPI 33m IL bond	GBP	2057	**32.3**	**33.6**	33.2	33.0
1.702%+RPI 50m IL bond	GBP	2057	**111.2**	**69.4**	112.9	67.7
Book overdrafts (see note 16)	GBP	2019	**14.7**	**14.7**	12.6	12.6
			8,905.1	**7,815.8**	9,052.0	7,912.3

IL	Index-linked debt – this debt is adjusted for movements in the Consumer or Retail Prices Indices with reference to a base CPI or RPI established at trade date.
CPI	The UK general index of consumer prices (for all items) as published by the Office for National Statistics (May 2015 = 100).
RPI	The UK general index of retail prices (for all items) as published by the Office for National Statistics (Jan 1987 = 100).
EIB	Borrowings that are held with the European Investment Bank.

Borrowings in the above table are unsecured. Funding raised in foreign currencies is swapped to sterling to match funding costs to income and assets.

During the year, the group issued a further £150 million fixed rate notes in addition to the £300 million fixed rate notes issued in the prior year. These notes were issued under the same terms with year of final repayment being 2025 and coupon rate of 2.0 per cent.

In April 2019, the group increased its CPI-linked debt by executing a £100 million CPI-linked bank loan with a 10-year maturity. This has not been recorded in the financial statements at 31 March 2019 as it represents a non-adjusting event after the reporting period.

Notes to the financial statements – appendices

A4 Financial risk management

Risk management

The board is responsible for treasury strategy and governance, which is reviewed on an annual basis.

The treasury committee, a subcommittee of the board, has responsibility for setting and monitoring the group's adherence to treasury policies, along with oversight in relation to the activities of the treasury function.

Treasury policies cover the key financial risks: liquidity risk, credit risk, market risk (inflation, interest rate, electricity price and currency) and capital risk. These policies are reviewed by the treasury committee for approval on at least an annual basis, or following any major changes in treasury operations and/or financial market conditions.

Day-to-day responsibility for operational compliance with the treasury policies rests with the treasurer. An operational compliance report is provided monthly to the treasury committee, which details the status of the group's compliance with the treasury policies and highlights the level of risk against the appropriate risk limits in place.

The group's treasury function does not act as a profit centre and does not undertake any speculative trading activity.

Liquidity risk

The group looks to manage its liquidity risk by maintaining liquidity within a board-approved duration range. Liquidity is actively monitored by the group's treasury function and is reported monthly to the treasury committee through the operational compliance report.

At 31 March 2019, the group had £1,039.3 million (2018: £1,205.0 million) of available liquidity, which comprised £339.3 million (2018: £510.0 million) of cash and short-term deposits and £700.0 million (2018: £695.0 million) of undrawn committed borrowing facilities.

The group had available committed borrowing facilities as follows:

Group	**2019 £m**	2018 £m
Expiring within one year	**100.0**	100.0
Expiring after one year but in less than two years	**50.0**	150.0
Expiring after more than two years	**650.0**	500.0
Total borrowing facilities	**800.0**	750.0
Facilities drawn[1]	**(100.0)**	(55.0)
Undrawn borrowing facilities	**700.0**	695.0

Note:
(1) Facilities expiring after more than two years.

These facilities are arranged on a bilateral rather than a syndicated basis, which spreads the maturities more evenly over a longer time period, thereby reducing the refinancing risk by providing several renewal points rather than a large single refinancing point.

Company

The company did not have any committed facilities available at 31 March 2019 or 31 March 2018.

A4 Financial risk management continued

Maturity analysis

Concentrations of risk may arise if large cash flows are concentrated within particular time periods. The maturity profile in the following table represents the forecast future contractual principal and interest cash flows in relation to the group's financial liabilities on an undiscounted basis. Derivative cash flows have been shown net where there is a contractual agreement to settle on a net basis; otherwise the cash flows are shown gross.

Group At 31 March 2019	Total[(1)] £m	Adjustment[(2)] £m	1 year or less £m	1–2 years £m	2–3 years £m	3–4 years £m	4–5 years £m	More than 5 years £m
Bonds	10,174.4		583.4	129.1	504.9	109.2	110.1	8,737.7
Bank and other term borrowings	3,008.0		293.3	680.4	125.1	356.1	125.4	1,427.7
Adjustment to carrying value[(2)]	(5,366.6)	(5,366.6)						
Borrowings	7,815.8	(5,366.6)	876.7	809.5	630.0	465.3	235.5	10,165.4
Derivatives:								
Payable	1,389.0		510.2	43.7	36.6	32.6	30.1	735.8
Receivable	(1,825.0)		(607.0)	(71.5)	(70.2)	(93.8)	(64.7)	(917.8)
Adjustment to carrying value[(2)]	26.8	26.8						
Derivatives – net assets	(409.2)	26.8	(96.8)	(27.8)	(33.6)	(61.2)	(34.6)	(182.0)

Group At 31 March 2018	Total[(1)] £m	Adjustment[(2)] £m	1 year or less £m	1–2 years £m	2–3 years £m	3–4 years £m	4–5 years £m	More than 5 years £m
Bonds	10,343.8		733.9	585.7	116.7	492.5	96.7	8,318.3
Bank and other term borrowings	3,119.3		289.4	125.2	682.5	124.5	355.3	1,542.4
Adjustment to carrying value[(2)]	(5,550.8)	(5,550.8)						
Borrowings	7,912.3	(5,550.8)	1,023.3	710.9	799.2	617.0	452.0	9,860.7
Derivatives:								
Payable	1,382.5		404.4	475.6	28.6	22.4	19.7	431.8
Receivable	(1,885.7)		(750.0)	(546.9)	(28.7)	(28.7)	(51.6)	(479.8)
Adjustment to carrying value[(2)]	(31.3)	(31.3)						
Derivatives – net assets	(534.5)	(31.3)	(345.6)	(71.3)	(0.1)	(6.3)	(31.9)	(48.0)

Notes:

(1) Forecast future cash flows are calculated, where applicable, using forward interest rates based on the interest environment at year end and are therefore susceptible to changes in market conditions. For index-linked debt it has been assumed that RPI will be three per cent and CPI will be two per cent over the life of each instrument.

(2) The carrying value of debt is calculated following various methods in accordance with IFRS 9 'Financial Instruments' and therefore this adjustment reconciles the undiscounted forecast future cash flows to the carrying value of debt in the statement of financial position.

Company

The company has total borrowings of £0.5 million (2018: £0.5 million), which are payable within one year, and £1,718.4 million (2018: £1,690.3 million), which are payable within one to two years.

Credit risk

Credit risk arises principally from trading (the supply of services to customers) and treasury activities (the depositing of cash and holding of derivative instruments). While the opening of the non-household retail market to competition from 1 April 2017 has impacted on the profile of the group's concentration of credit risk, as discussed further below, the group does not believe it is exposed to any material concentrations that could have an impact on its ability to continue as a going concern or its longer-term viability.

The group manages its risk from trading through the effective management of customer relationships. Concentrations of credit risk with respect to trade receivables are limited due to the majority of the group's customer base being comprised of a large number of unrelated households. The Water Industry Act 1991 (as amended by the Water Industry Act 1999) prohibits the disconnection of a water supply and the limiting of supply with the intention of enforcing payment for certain premises, including domestic dwellings.

Following the non-household retail market opening to competition, credit risk in this area is now concentrated in a small number of retailers to whom the group provides wholesale water and wastewater services. Retailers are licensed and monitored by Ofwat and as part of the regulations they must demonstrate that they have adequate resources available to supply services. The group's retail customers are on 30-day credit terms in respect of trading transactions. As at 31 March 2019, Water Plus was the group's single largest debtor, with amounts outstanding in relation to wholesale services of £39.1 million (2018: £42.2 million). During the year, sales to Water Plus in relation to wholesale services were £454.8 million (2018: £495.4 million). Details of transactions with Water Plus can be found in note A6.

A4 Financial risk management continued

Under the group's revenue recognition policy, revenue is only recognised when collection of the resulting receivable is reasonably assured. Considering the above, the directors believe there is no further credit risk provision required in excess of the allowance for doubtful receivables (see note 15). An allowance is made by the water regulator in the price limits at each price review for a proportion of debt deemed to be irrecoverable.

The group manages its credit risk from treasury activities by establishing a total credit limit by counterparty, which comprises a counterparty credit limit and an additional settlement limit to cover intra-day gross settlement of cash flows. In addition, potential derivative exposure limits are also established to take account of potential future exposure which may arise under derivative transactions. These limits are calculated by reference to a measure of capital and credit ratings of the individual counterparties and are subject to a maximum single counterparty limit. Credit limits are refreshed annually and reviewed in the event of any credit rating action. Additionally, a control mechanism to trigger a review of specific counterparty limits, irrespective of credit rating action, is in place. This entails daily monitoring of counterparty credit default swap levels and/or share price volatility. Credit exposure is monitored daily by the group's treasury function and is reported monthly to the treasury committee through the operational compliance report.

At 31 March 2019 and 31 March 2018, the maximum exposure to credit risk for the group and company is represented by the carrying amount of each financial asset in the statement of financial position:

	Group		Company	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Cash and short-term deposits (see note 16)	**339.3**	510.0	**–**	–
Trade and other receivables (see note 15)*	**397.6**	402.0	**82.2**	74.2
Investments (see note 13)	**11.5**	7.1	**–**	–
Derivative financial instruments	**489.1**	635.5	**–**	–
	1,237.5	1,554.6	**82.2**	74.2

* Included within trade and other receivables is £143.5 million of amounts owed by joint ventures in respect of borrowings, further details of which are disclosed in note A6.

The credit exposure on derivatives is disclosed gross of any collateral held. At 31 March 2019, the group held £52.0 million (2018: £106.7 million) as collateral in relation to derivative financial instruments (included within short-term bank borrowings – fixed in note A3).

Market risk

The group's exposure to market risk primarily results from its financing arrangements and the economic return which it is allowed on the regulatory capital value (RCV).

The group uses a variety of financial instruments, including derivatives, in order to manage the exposure to these risks.

Inflation risk

The group earns an economic return on its RCV, comprising a real return through revenues and an inflation return as an uplift to its RCV. Currently, the group's regulatory assets are linked to RPI inflation; however, following Ofwat's decision to transition to the use of CPIH for inflation indexation for the 2020–25 regulatory period, from 2020 the group's RCV will be 50 per cent linked to RPI inflation and 50 per cent linked to CPIH inflation, with any new additions being added to the CPIH portion of the RCV.

The group's inflation hedging policy aims to have around half of the group's net debt in index-linked form (where it is economic to do so), by issuing index-linked debt and/or swapping a portion of nominal debt. This is expected to remain mostly in RPI-linked form until CPI and/or CPIH debt and swaps become available in sufficient size at an economic cost.

The group believes this is an appropriate inflation hedging policy taking into account a balanced assessment of the following factors: economic hedge of United Utilities Water Limited's (UUW) RCV and revenues; cash flow timing mismatch between allowed cost of debt and the group's incurred cost of debt; the inflation risk premium that is generally incorporated into nominal debt costs; income statement volatility; hedging costs; debt maturity profile mismatch risk; and index-linked hedging positioning relative to the water sector.

As a result of the evaluation of the above factors, the group will continue to identify opportunities to maintain around 50 per cent of the group's net debt being hedged for inflation, which can be evidenced by issuing of CPI index-linked debt since 2017 and the swapping of RPI-linked debt to CPI after the reporting period as described in note 26. Inflation risk is reported monthly to the treasury committee in the operational compliance report.

The carrying value of index-linked debt held by the group was £3,775.8 million at 31 March 2019 (2018: £3,792.8 million).

A4 Financial risk management continued

Sensitivity analysis

The following table details the sensitivity of profit before tax to changes in the RPI and CPI on the group's index-linked borrowings. The sensitivity analysis has been based on the amount of index-linked debt held at the reporting date and, as such, is not indicative of the years then ended. In addition, it excludes the hedging aspect of the group's regulatory assets and post-retirement obligations.

Increase/(decrease) in profit before tax and equity	2019 £m	2018 £m
1% increase in RPI/CPI	(38.2)	(37.7)
1% decrease in RPI/CPI	38.2	37.7

The sensitivity analysis assumes a one per cent change in RPI and CPI having a corresponding one per cent impact on this position over a 12-month period. It should be noted, however, that there is a time lag by which current RPI and CPI changes impact on the income statement, and the analysis does not incorporate this factor. The portfolio of index-linked debt is calculated on either a three- or eight-month lag basis. Therefore, at the reporting date the index-linked interest and principal adjustments impacting the income statement are fixed and based on the annual RPI or CPI change either three or eight months earlier.

Company

The company had no material exposure to inflation risk at 31 March 2019 or 31 March 2018.

Interest rate risk

The group's policy is to structure debt in a way that best matches its underlying assets and cash flows. The group currently earns an economic return on its RCV, comprising a real return through revenues, determined by the real cost of capital fixed by the regulator for each five-year regulatory pricing period, and an inflation return as an uplift to its RCV (see inflation risk section for changes being introduced by Ofwat to inflation indexation from 2020).

In the next regulatory period, Ofwat intends to continue using materially the same methodology in setting a fixed real cost of debt in relation to embedded debt (currently assumed to be 70 per cent of net debt), but will introduce a debt indexation mechanism in relation to new debt (currently assumed to be 30 per cent of net debt).

Therefore, sterling index-linked debt is left unswapped at inception, in accordance with our inflation hedging policy goal to maintain around half of the group's net debt in index-linked form. Conventional nominal debt is hedged as set out below.

Where conventional long-term debt is raised in a fixed-rate form, to manage exposure to long-term interest rates, the debt is generally swapped at inception to create a floating rate liability for the term of the liability through the use of interest rate swaps. These instruments are typically designated within a fair value accounting hedge.

To manage the exposure to medium-term interest rates, the group fixes underlying interest rates on nominal debt out to 10 years in advance on a reducing balance basis, mirroring Ofwat's expected split of 70 per cent embedded and 30 per cent new debt. As such, at the start of each regulatory period, around 30 per cent of the projected nominal net debt for that regulatory period will remain floating until it is fixed via the above 10-year reducing balance basis, which should more closely mirror Ofwat's new debt indexation mechanism.

This interest rate hedging policy dovetails with our revised inflation hedging policy should we need to swap a portion of nominal debt to real rate form to maintain our desired mix of nominal and index-linked debt.

The group seeks to manage its risk by maintaining its interest rate exposure within a board-approved range. Interest rate risk is reported to the treasury committee through the operational compliance report.

Sensitivity analysis

The following table details the sensitivity of the group's profit before tax and equity to changes in interest rates. The sensitivity analysis has been based on the amount of net debt and the interest rate hedge positions in place at the reporting date and, as such, is not indicative of the years then ended.

	Group		Company	
Increase/(decrease) in profit before tax and equity	2019 £m	2018 £m	2019 £m	2018 £m
1% increase in interest rate	130.2	128.1	(17.2)	(16.9)
1% decrease in interest rate	(141.3)	(138.3)	17.2	16.9

The sensitivity analysis assumes that both fair value hedges and borrowings designated at fair value through profit or loss are effectively hedged and it excludes the impact on post-retirement obligations. The exposure largely relates to fair value movements on the group's fixed interest rate swaps which manage the exposure to medium-term interest rates. Those swaps are not included in hedge relationships.

Notes to the financial statements – appendices

A4 Financial risk management continued

Repricing analysis

The following tables categorise the group's borrowings, derivatives and cash deposits on the basis of when they reprice or, if earlier, mature. The repricing analysis demonstrates the group's exposure to floating interest rate risk.

Our largest concentration of floating interest rate risk is with index-linked instruments. This has been classified as repricing in one year or less due to the refixing of the interest charge with changes in RPI and CPI.

Group At 31 March 2019	Total £m	1 year or less £m	1–2 years £m	2–3 years £m	3–4 years £m	4–5 years £m	More than 5 years £m
Borrowings in fair value hedge relationships							
Fixed rate instruments	2,765.8	441.9	–	406.2	–	–	1,917.7
Effect of swaps	–	2,323.9	–	(406.2)	–	–	(1,917.7)
	2,765.8	2,765.8	–	–	–	–	–
Borrowings designated at fair value through profit or loss							
Fixed rate instruments	373.9	–	–	–	–	–	373.9
Effect of swaps	–	373.9	–	–	–	–	(373.9)
	373.9	373.9	–	–	–	–	–
Borrowings measured at amortised cost							
Fixed rate instruments	179.4	152.6	0.6	0.7	0.7	0.7	24.1
Floating rate instruments	720.9	720.9	–	–	–	–	–
Index-linked instruments	3,775.8	3,775.8	–	–	–	–	–
	4,676.1	4,649.3	0.6	0.7	0.7	0.7	24.1
Effect of fixed interest rate swaps	–	(2,330.9)	148.5	50.0	164.5	575.0	1,392.9
Total borrowings	7,815.8	5,458.1	149.1	50.7	165.2	575.7	1,417.0
Cash and short-term deposits	(339.3)	(339.3)	–	–	–	–	–
Net borrowings	7,476.5	5,118.8	149.1	50.7	165.2	575.7	1,417.0

At 31 March 2018	Total £m	1 year or less £m	1–2 years £m	2–3 years £m	3–4 years £m	4–5 years £m	More than 5 years £m
Borrowings in fair value hedge relationships							
Fixed rate instruments	2,895.3	583.2	466.4	–	411.5	–	1,434.2
Effect of swaps	–	2,312.1	(466.4)	–	(411.5)	–	(1,434.2)
	2,895.3	2,895.3	–	–	–	–	–
Borrowings designated at fair value through profit or loss							
Fixed rate instruments	347.7	–	–	–	–	–	347.7
Effect of swaps	–	347.7	–	–	–	–	(347.7)
	347.7	347.7	–	–	–	–	–
Borrowings measured at amortised cost							
Fixed rate instruments	189.4	162.0	0.6	0.6	0.7	0.8	24.7
Floating rate instruments	750.1	750.1	–	–	–	–	–
Index-linked instruments	3,729.8	3,729.8	–	–	–	–	–
	4,669.3	4,641.9	0.6	0.6	0.7	0.8	24.7
Effect of fixed interest rate swaps	–	(3,006.3)	925.4	252.1	50.0	164.5	1,614.3
Total borrowings	7,912.3	4,878.6	926.0	252.7	50.7	165.3	1,639.0
Cash and short-term deposits	(510.0)	(510.0)	–	–	–	–	–
Net borrowings	7,402.3	4,368.6	926.0	252.7	50.7	165.3	1,639.0

A4 Financial risk management continued

Company	2019 Total £m	2019 1 year or less £m	2018 Total £m	2018 1 year or less £m
Borrowings measured at amortised cost				
Floating rate instruments	**1,718.4**	**1,718.4**	1,690.8	1,690.8
Total borrowings	**1,718.4**	**1,718.4**	1,690.8	1,690.8

Electricity price risk

The group is allowed a fixed amount of revenue by the regulator, in real terms, to cover electricity costs for each five-year regulatory pricing period. To the extent that electricity prices remain floating over this period, this exposes the group to volatility in its operating cash flows. The group's policy, therefore, is to manage this risk by fixing a proportion of electricity commodity prices in a cost-effective manner. The group has fixed the price on a substantial proportion of its anticipated net electricity usage out to the end of the AMP in 2020 and has begun fixing prices for the subsequent AMP from 2020 to 2025, partially through entering into electricity swap contracts.

The adoption of IFRS 9 'Financial Instruments' has enabled the group to designate electricity swaps into cash flow hedge relationships. This means that only the impact of any hedging ineffectiveness is recognised through fair value in the income statement, with movements reflecting the effective portion of the swaps being recognised in other comprehensive income. As a result of this, changes in electricity prices are no longer significant sources of volatility in the income statement and therefore sensitivity analysis in this area will no longer be meaningful.

The company has no exposure to electricity price risk.

Currency risk

Currency exposure principally arises in respect of funding raised in foreign currencies.

To manage exposure to currency rates, foreign currency debt is hedged into sterling through the use of cross-currency swaps and these are often designated within a fair value accounting hedge.

The group seeks to manage its risk by maintaining currency exposure within board-approved limits. Currency risk in relation to foreign currency denominated financial instruments is reported monthly to the treasury committee through the operational compliance report.

The group and company have no material net exposure to movements in currency rates.

Capital risk management

The group's objective when managing capital is to maintain efficient access to debt capital markets throughout the economic cycle. The board therefore believes that it is appropriate to maintain RCV gearing, measured as group consolidated net debt (including derivatives) to regulatory capital value (RCV) of UUW, within a target range of 55 per cent to 65 per cent. As at 31 March 2019, RCV gearing was 61 per cent (2018: 61 per cent), which is comfortably within this range.

Assuming no significant changes to existing rating agencies' methodologies or sector risk assessments, the group aims to maintain, as a minimum, credit ratings of A3 with Moody's Investors Service (Moody's) and BBB+ with Standard & Poor's Ratings Services (Standard & Poor's) for UUW and debt issued by its financing subsidiary, United Utilities Water Finance PLC.

In order to maintain its targeted minimum credit ratings, the group needs to manage its capital structure with reference to the ratings methodology and measures used by Moody's and Standard & Poor's. The ratings methodology is normally based on a number of key ratios (such as RCV gearing, adjusted interest cover and Funds from Operations (FFO) to debt) and threshold levels as updated and published from time to time by Moody's and Standard & Poor's. The group looks to manage its risk by maintaining the relevant key financial ratios used by the credit rating agencies to determine a corporate's credit rating, within the thresholds approved by the board. Capital risk is reported monthly to the treasury committee through the operational compliance report.

Further detail on the precise measures and methodologies used to assess water companies' credit ratings can be found in the methodology papers published by the rating agencies.

A4 Financial risk management continued

Fair values

The table below sets out the valuation basis of financial instruments held at fair value and financial instruments where fair value has been separately disclosed in the notes as the carrying value is not a reasonable approximation of fair value.

Group 2019	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at fair value through profit or loss				
Derivative financial assets – fair value hedge	–	329.4	–	329.4
Derivative financial assets – held for trading(1)	–	158.5	–	158.5
Derivative financial assets – cash flow hedge(2)	–	1.2	–	1.2
Investments(3)	–	11.5	–	11.5
Financial liabilities at fair value through profit or loss				
Derivative financial liabilities – fair value hedge	–	(2.3)	–	(2.3)
Derivative financial liabilities –held for trading(1)	–	(75.9)	–	(75.9)
Derivative financial liabilities – cash flow hedge(2)	–	(1.7)	–	(1.7)
Financial liabilities designated as fair value through profit or loss	–	(373.9)	–	(373.9)
Financial instruments for which fair value has been disclosed				
Financial liabilities in fair value hedge relationships	(2,316.9)	(432.4)	–	(2,749.3)
Other financial liabilities at amortised cost	(680.9)	(5,101.0)	–	(5,781.9)
	(2,997.8)	(5,486.6)	–	(8,484.4)

2018	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Available for sale financial assets				
Investments	–	7.1	–	7.1
Financial assets at fair value through profit or loss				
Derivative financial assets – fair value hedge	–	455.7	–	455.7
Derivative financial assets – held for trading(1)	–	179.8	–	179.8
Financial liabilities at fair value through profit or loss				
Derivative financial liabilities – fair value hedge	–	(24.2)	–	(24.2)
Derivative financial liabilities – held for trading(1)	–	(76.8)	–	(76.8)
Financial liabilities designated as fair value through profit or loss	–	(347.7)	–	(347.7)
Financial instruments for which fair value has been disclosed				
Financial liabilities in fair value hedge relationships	(2,192.4)	(713.5)	–	(2,905.9)
Other financial liabilities at amortised cost	(2,425.6)	(3,372.8)	–	(5,798.4)
	(4,618.0)	(3,892.4)	–	(8,510.4)

Notes:

(1) These derivatives form economic hedges and, as such, management intends to hold these through to maturity. Derivatives forming an economic hedge of the currency exposure on borrowings included in these balances were £151.3 million (2018: £151.8 million).

(2) On adoption of IFRS 9 'Financial Instruments', electricity swaps, previously classified as held for trading under IAS 39 'Financial Instruments: Recognition and Measurement', have been designated in cash flow hedge relationships.

(3) Prior to the adoption of IFRS 9 'Financial Instruments' on 1 April 2018, investments were classified as available-for-sale financial assets in accordance with IAS 39 'Financial Instruments: Recognition and Measurement'.

› Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;

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

› Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable).

The group has calculated fair values using quoted prices where an active market exists, which has resulted in £2,997.8 million (2018: £4,618.0 million) of 'level 1' fair value measurements. In the absence of an appropriate quoted price, the group has applied discounted cash flow valuation models utilising market available data in line with prior years. The £1,620.2 million decrease (2018: £1,914.0 million increase) in 'level 1' fair value measurements is largely due to a decrease in the number of observable quoted bond prices in active markets at 31 March 2019.

During the year, changes in the fair value of financial liabilities designated at fair value through profit or loss resulted in a £26.2 million loss (2018: £27.8 million gain). Included within this was a £6.6 million gain (2018: £24.0 million loss) attributable to changes in own credit risk. Following adoption of IFRS 9 'Financial Instruments', this £6.6 million gain has been recognised in other comprehensive income rather than profit or loss. The cumulative amount due to changes in credit spread was £44.8 million profit (2018: £38.2 million profit). The carrying amount is £147.8 million (2018: £145.6 million) higher than the amount contracted to settle on maturity.

A4 Financial risk management continued

Company

The company does not hold any financial instruments that are measured subsequent to initial recognition at fair value or where fair value has been separately disclosed in the notes as the carrying value is not a reasonable approximation of fair value.

A5 Retirement benefits

Defined benefit schemes

The group participates in two major funded defined benefit pension schemes in the United Kingdom – the United Utilities Pension Scheme (UUPS) and the United Utilities PLC group of the Electricity Supply Pension Scheme (ESPS), both of which are closed to new employees. The assets of these schemes are held in trust funds independent of the group's finances.

The trustees are composed of representatives of both the employer and employees. The trustees are required by law to act in the interests of all relevant beneficiaries and are responsible for the investment policy with regard to the assets plus the day-to-day administration of the benefits.

In the year ended 31 March 2019, the majority of active members in the defined benefit sections of the UUPS transitioned to a hybrid section comprising both defined benefit and defined contribution elements. Pension benefits relating to pensionable service before 1 April 2018 were unaffected by the changes. This transition is a consequence of an increase in future service costs and is intended to reduce the overall costs and risk to the group while balancing the interests of employees by maintaining an element of defined benefit pension provision.

The group also operates a series of historic unfunded, unregistered retirement benefit schemes. The costs of these schemes are included in the total pension cost, on a basis consistent with IAS 19 'Employee Benefits' and the assumptions set out below.

Information about the pension arrangements for executive directors is contained in the directors' remuneration report.

Under the schemes, employees are entitled to annual pensions on retirement. Benefits are also payable on death and following other events such as withdrawing from active service. No other post-retirement benefits are provided to these employees.

The defined benefit obligation includes benefits for current employees, former employees and current pensioners as analysed in the table below:

Group	2019 £m	2018 £m
Total value of current employees benefits	**754.3**	913.8
Deferred members benefits	**651.4**	748.6
Pensioner members benefits	**2,019.5**	1,836.3
Total defined benefit obligation	**3,425.2**	3,498.7

The duration of the combined schemes is around 18 years. The schemes' duration is an indicator of the weighted-average time until benefit payments are settled, taking account of the split of the defined benefit obligation between current employees, deferred members and the current pensioners of the schemes.

Funding requirements

The latest finalised funding valuations of the schemes were carried out by independent qualified actuaries as at 31 March 2018, earlier than originally planned due to the aforementioned changes to the pension scheme, and determined that the schemes were both in a deficit position on a funding basis. The basis on which scheme liabilities are valued for funding purposes differs from the basis required under IAS 19, with liabilities on a funding basis being subject to assumptions at the valuation date that are not updated between revaluations. Funding deficits vary significantly from company to company, but neither the deficits, the assumptions on which they are based, the associated sensitivities, nor the risk exposures are disclosed by many companies and, therefore, meaningful cross-company comparisons are not possible. Conversely, scheme liabilities are valued on a consistent basis between companies under IAS 19 and are subject to assumptions and sensitivities that are required to be disclosed. Consequently, the relative economic positions of companies are comparable only on an IAS 19 basis, subject to normalisation of assumptions used between companies.

A retirement benefit surplus was recognised as an asset at both 31 March 2019 and 31 March 2018 as, under both the UUPS and ESPS scheme rules, the group has an unconditional right to a refund of the surplus assuming the full settlement of the plans' liabilities in a single event, such as a scheme wind-up.

Under UK legislation there is a requirement that pension schemes are funded prudently, and that funding plans are agreed by pension scheme trustees. The group had plans in place with the schemes' trustees to address the funding deficits by 31 December 2021 for the UUPS and 30 September 2024 for the ESPS, through a series of deficit recovery contributions. This timescale has been accelerated, with accelerated deficit repair contributions of £97.6 million and £5.4 million made to the UUPS and ESPS respectively in April 2019. These payments represent the final acceleration of deficit repair contributions set out in the schedules of contributions agreed with the schemes' trustees as part of the 31 March 2018 valuation process, and reduce the deficit repair contributions payable, due from the company, to nil.

As the 2018 valuation basis was consistent with a long-term target for self-sufficiency, the expectation is that there should be minimal ongoing reliance on the company by the pension schemes.

The group and trustees have agreed long-term strategies for reducing investment risk in each scheme. This includes an asset-liability matching policy which aims to reduce the volatility of the funding level of the pension plan by investing in assets, such as corporate bonds and gilts, supplemented by swap and gilt long-term hedges of interest and inflation rates, which perform in line with the liabilities so as to hedge against changes in interest and inflation rates.

A5 Retirement benefits continued

In addition, in the year ended 31 March 2019, the investment and risk management strategy continued to evolve with both UUPS and ESPS now fully hedging inflation exposure through external market swaps and gilts. As a consequence, the Inflation Funding Mechanism (IFM), which previously provided an element of inflation hedging directly with the company, has now ceased to apply and, therefore, no IFM payments were made during the year. Further details of the derivatives used in reducing investment risk are disclosed in the 'Further reporting analysis' section of this appendix.

The group expects to make further contributions of £8.4 million in the year ending 31 March 2020, £7.1 million and £0.9 million in respect of current service contributions to UUPS and ESPS respectively, and £0.4 million in respect of expenses to the ESPS.

The schemes' funding plans are reviewed regularly, and the next funding valuation for UUPS and ESPS is due no later than 31 March 2021.

Impact of scheme risk management on IAS 19 disclosures

Under the prescribed IAS 19 basis, pension scheme liabilities are calculated based on current accrued benefits. Expected cash flows are projected forward allowing for RPI and CPI and the current member mortality assumptions. These projected cash flows are then discounted by a high-quality corporate bond rate, which comprises an underlying interest rate and a credit spread.

The group has de-risked its pension schemes through hedging strategies applied to the underlying interest rate and the forecast RPI and CPI. Due to the IFM ceasing to exist, as mentioned above, both UUPS and ESPS are now fully hedging inflation exposure along with underlying interest rates through external market swaps and gilts, the value of which is included in the schemes' assets.

Consequently, the reported statement of financial position under IAS 19 remains volatile due to changes in credit spread which have not been hedged, primarily due to the difficulties in doing so over long durations, and changes in mortality as management has decided, at the current time, not to hedge this exposure due to its lower volatility in the short term and the relatively high hedging costs.

In contrast, the schemes' specific funding bases, which formed the basis for regular deficit repair contributions, are unlikely to suffer from significant volatility due to credit spread, because a prudent, fixed credit spread assumption is applied.

Pension benefits under the defined benefit element of the new UUPS hybrid section, that became effective for pensionable service from 1 April 2018, are linked to CPI rather than RPI.

In the year ended 31 March 2019, the discount rate decreased by 0.2 per cent (2018: 0.05 per cent increase), which includes a 0.1 per cent decrease in credit spreads and a 0.1 per cent decrease in gilt yields over the year. The IAS 19 remeasurement gain of £73.0 million (2018: £50.2 million) reported in note 18 has largely resulted from the favourable impact of updated membership data due to the 2018 funding valuation, changes in mortality assumptions, and growth asset gains, partially offset by the reduction in credit spreads and gilt yields during the year.

Guaranteed Minimum Pensions (GMP) equalisation

On 26 October 2018, the High Court issued its ruling in a landmark case involving Lloyds Banking Group on GMP. The implication of the ruling is that GMP will be equalised for males and females. The impact of GMP equalisation under the chosen C2 method of calculation is £5.5 million (0.2 per cent of liability) for the UUPS and £1.1 million (0.3 per cent of liability) for the ESPS, resulting in an overall increase in the pension liability of £6.6 million as a result of additional benefits being recognised, with a corresponding amount recorded in past service costs in the income statement. Any future true-up costs will be accounted for in other comprehensive income as a change in management estimate.

Reporting and assumptions

The results of the latest funding valuations at 31 March 2018 have been adjusted for IAS 19 in order to assess the position at 31 March 2019, by taking account of experience over the period, changes in market conditions, and differences in the financial and demographic assumptions. The present value of the defined benefit obligation, and the related current service costs, were measured using the projected unit credit method.

Member data used in arriving at the liability figure included within the overall IAS 19 surplus has been based on the finalised actuarial valuations as at 31 March 2018 for both UUPS and ESPS.

Financial assumptions

The main financial and demographic assumptions used by the actuary to calculate the defined benefit surplus of UUPS and ESPS are outlined below:

Group	**2019 % p.a.**	2018 % p.a.
Discount rate	**2.40**	2.60
Pensionable salary growth and pension increases	**3.45**	3.35
Price inflation – RPI	**3.45**	3.35
Price inflation – CPI	**2.05**	1.95

The discount rate is consistent with a high-quality corporate bond rate, with 2.40 per cent being equivalent to gilts plus 90 basis points (31 March 2019: 2.60 per cent being equivalent to gilts plus 100 basis points).

A5 Retirement benefits continued

Demographic assumptions

At both 31 March 2019 and 31 March 2018, mortality in retirement is assumed to be in line with the Continuous Mortality Investigation's (CMI) S2PA year of birth tables, with a scaling factor of 106 per cent and 109 per cent for male pensioners and non-pensioners respectively and 104 per cent and 105 per cent for female pensioners and non-pensioners respectively (2018: 108 per cent for males and 102 per cent for females), reflecting actual mortality experience. At 31 March 2019, mortality in retirement is based on CMI 2018 (2018: CMI 2016) long-term improvement factors, with a long-term annual rate of improvement of 1.50 per cent (2018: 1.75 per cent). The current life expectancies at age 60 underlying the value of the accrued liabilities for the schemes are:

Group	2019 years	2018 years
Retired member – male	**26.4**	27.0
Non-retired member – male	**27.5**	28.7
Retired member – female	**28.6**	29.4
Non-retired member – female	**30.0**	31.1

Sensitivity of the key scheme assumptions

The measurement of the group's defined benefit surplus is sensitive to changes in key assumptions, which are described above. The sensitivity calculations presented below allow for the specified movement in the relevant key assumption, while all other assumptions are held constant. This approach does not take into account the interrelationship between some of these assumptions or any hedging strategies adopted.

- Asset volatility – If the schemes' assets underperform relative to the discount rate used to calculate the schemes' liabilities, this will create a deficit. The schemes hold some growth assets (equities, diversified growth funds and emerging market debt) which, though expected to outperform the discount rate in the long term, create volatility in the short term. The allocation to growth assets is monitored to ensure it remains appropriate given the schemes' long-term objectives.
- Discount rate – An increase/decrease in the discount rate of 0.1 per cent would have resulted in a £73.2 million (2018: £72.7 million) decrease/increase in the schemes' liabilities at 31 March 2019, although as long as credit spreads remain stable this will be largely offset by an increase/decrease in the value of the schemes' bond holdings and other instruments designed to hedge this exposure. The discount rate is based on high-quality corporate bond yields of a similar duration to the schemes' liabilities.
- Price inflation – An increase/decrease in the inflation assumption of 0.1 per cent would have resulted in a £68.4 million (2018: £68.1 million) increase/decrease in the schemes' liabilities at 31 March 2019, as a significant proportion of the schemes' benefit obligations are linked to inflation. However, nearly all of the schemes' liabilities were hedged for RPI in the external market at 31 March 2019, meaning that this sensitivity is likely to be insignificant as a result. As assumptions for pensionable salary growth and pension increases are in line with those for price inflation, sensitivities are also in line.
- Mortality long-term improvement rate – An increase in the mortality long-term improvement rate to 1.75 per cent would have resulted in a £37.5 million decrease in the schemes' liabilities at 31 March 2019.
- Life expectancy – An increase/decrease in life expectancy of one year would have resulted in a £137.1 million (2018: £128.6 million) increase/decrease in the schemes' liabilities at 31 March 2019. The majority of the schemes' obligations are to provide benefits for the life of the member and, as such, the schemes' liabilities are sensitive to these assumptions.

Further reporting analysis

At 31 March, the fair values of the schemes' assets recognised in the statement of financial position were as follows:

Group	Schemes' assets %	2019 £m	Schemes' assets %	2018 £m
Equities	**–**	**0.8**	9.5	363.9
Other non-equity growth assets	**7.7**	**302.5**	5.7	219.1
Gilts	**33.5**	**1,310.2**	47.2	1,813.3
Bonds	**46.2**	**1,805.8**	40.6	1,561.7
Other	**12.6**	**489.8**	(3.0)	(115.1)
Total fair value of schemes' assets	**100.0**	**3,909.1**	100.0	3,842.9
Present value of defined benefit obligations		**(3,425.2)**		(3,498.7)
Net retirement benefit surplus		**483.9**		344.2

The fair values in the table above are all based on quoted prices in an active market, with the exception of £203.8 million (2018: £150.1 million) of assets included in 'Other', which fall within the 'Level 3' fair value categorisation in accordance with IFRS 13 'Fair Value Measurement'.

A5 Retirement benefits continued

The assets, in respect of UUPS, included in the table above, have been allocated to each asset class based on the return the assets are expected to achieve as UUPS has entered into a variety of derivative transactions to change the return characteristics of the physical assets held in order to reduce undesirable market and liability risks. As such, the breakdown shown separates the assets of the schemes to illustrate the underlying risk characteristics of the assets held.

The portfolio contains a proportion of assets set aside for collateral purposes linked to the derivative contracts entered into, as described above. The collateral portfolio, comprising cash and eligible securities readily convertible to cash, provides sufficient liquidity to manage the derivative transactions and is expected to achieve a return in excess of LIBOR.

The fair value of derivatives included within pension scheme asset classification are analysed as follows:

Group	Underlying assets £m	Fair value of derivatives £m	Combined £m
At 31 March 2019			
Equities	**4.8**	**(4.0)**	**0.8**
Other non-equity growth assets	**302.5**	**–**	**302.5**
Gilts	**1,310.2**	**–**	**1,310.2**
Bonds	**1,821.0**	**(15.2)**	**1,805.8**
Other	**370.0**	**119.8**	**489.8**
Total fair value of schemes' assets	**3,808.5**	**100.6**	**3,909.1**
At 31 March 2018			
Equities	357.3	6.6	363.9
Other non-equity growth assets	219.1	–	219.1
Gilts	1,813.3	–	1,813.3
Bonds	1,561.1	0.6	1,561.7
Other	170.1	(285.2)	(115.1)
Total fair value of schemes' assets	4,120.9	(278.0)	3,842.9

The derivative values in the table above represent the net market value of derivatives held within each of these asset categories as follows:

- Derivatives are held within the UUPS equity portfolio to gain economic exposure equivalent to around 4.0 per cent of that scheme's assets, and comprise total return swaps on equity indices with a value of £nil (2018: £4.7 million) and currency forwards with a value of £(4.0) million (2018: £1.9 million).
- Derivatives are used within both the UUPS and ESPS bond portfolio to hedge non-sterling exposure back to sterling:
  - The UUPS total value of £(17.1) million comprises interest rate swaps with a value of £(15.0) million (2018: £(3.9) million) and currency forwards with a value of £(2.1) million (2018: £1.1 million); and
  - The ESPS total value of £1.9 million (2018: £3.4 million) relates to interest rate swaps.
- Derivatives are used within both the UUPS and ESPS 'other' portfolios to manage liability risks. Both schemes use a range of derivatives to target a high level of interest rate and inflation hedging, comprising £112.7 million (2018: £(285.9) million) in the UUPS and £7.1 million (2018: £0.7 million) in the ESPS. These are further broken down as follows:
  - The UUPS net value of £112.7 million (2018: £(285.9) million) comprises asset swaps with a value of £(32.7) million (2018: £(27.3) million), interest rate swaps with a value of £143.6 million (2018: £252.1 million), gilt repurchase agreements with a value of £nil (2018: £(517.2) million) and RPI inflation swaps with a value of £1.8 million (2018: £6.5 million); and
  - The ESPS net value of £7.1 million (2018: £0.7 million) represents gilt repurchase agreements with a value of £7.4 million (2018: £2.3 million) and RPI inflation swaps with a value of £(0.3) million (2018: £(1.6) million).

A5 Retirement benefits continued

The derivatives shown in the tables only cover those expressly held for the purpose of reducing certain undesirable asset and liability risks. The schemes also invest in a number of other pooled funds that make use of derivatives. No allowance is made in the figures above for any derivatives held within these, as these are not held expressly for the purpose of managing risk. The total fair value of pooled funds held within the schemes' assets was £582.0 million (2018: £567.4 million).

Movements in the fair value of the schemes' assets were as follows:

Group	2019 £m	2018 £m
At the start of the year	**3,842.9**	3,863.0
Interest income on schemes' assets	**98.4**	97.7
The return on plan assets, excluding amounts included in interest	**58.5**	(60.0)
Member contributions	**2.9**	4.9
Benefits paid	**(166.0)**	(131.7)
Administrative expenses	**(2.8)**	(2.6)
Company contributions	**75.2**	71.6
At the end of the year	**3,909.1**	3,842.9

The group's actual return on the schemes' assets was a gain of £156.9 million (2018: £37.7 million), principally due to gains on derivatives hedging the schemes' liabilities.

Movements in the present value of the defined benefit obligations are as follows:

Group	2019 £m	2018 £m
At the start of the year	**(3,498.7)**	(3,615.5)
Interest cost on schemes' obligations	**(88.9)**	(90.6)
Actuarial (losses)/gains arising from changes in financial assumptions	**(160.6)**	85.1
Actuarial gains arising from changes in demographic assumptions	**70.9**	43.2
Actuarial (losses)/gains arising from experience	**104.2**	(18.1)
Curtailments/settlements	**(9.0)**	(2.3)
Member contributions	**(2.9)**	(4.9)
Benefits paid	**166.0**	131.7
Current service cost	**(6.2)**	(27.3)
At the end of the year	**(3,425.2)**	(3,498.7)

A6 Related party transactions

Group

Transactions between the company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

The related party transactions with the group's joint ventures and other related parties during the period, and amounts outstanding at the period end date, were as follows:

	2019 £m	2018 £m
Sales of services	**455.8**	496.3
Charitable contributions advanced to related parties	**0.5**	–
Purchases of goods and services	**0.1**	0.7
Costs recharged at nil margin under transitional service agreements	**0.2**	1.4
Interest income and fees recognised on loans to related parties	**4.3**	3.4
Amounts owed by related parties	**182.9**	179.7
Amounts owed to related parties	**0.6**	1.4

Sales of services to related parties during the year mainly represent non-household wholesale charges to Water Plus Group Limited (Water Plus), a joint venture in which the group holds a 50 per cent stake alongside Severn Trent PLC, that were billed during the period. These transactions were on the group's normal trading terms in respect of non-household wholesale charges, which are governed by the wholesale charging rules issued by Ofwat.

Charitable contributions advanced to related parties during the year relate to amounts paid to Rivington Heritage Trust, a charitable company limited by guarantee for which United Utilities Water Limited is one of three guarantors.

At 31 March 2019, amounts owed by joint ventures, as recorded within trade and other receivables in the statement of financial position, were £182.9 million (2018: £179.7 million), comprising £39.4 million (2018: £42.5 million) of trade balances, which are unsecured and will be settled in accordance with normal credit terms, and £143.5 million (2018: £137.2 million) relating to loans. Included within these loans receivable were the following amounts owed by Water Plus:

› £100.0 million outstanding on a £100.0 million revolving credit facility provided by United Utilities Water Limited, which is guaranteed by United Utilities PLC, with a maturity date of 30 September 2020, bearing a floating interest rate of LIBOR plus a credit margin;
› £9.6 million receivable being the fair value of amounts owed in relation to a £12.5 million unsecured loan note held by United Utilities PLC, with a maturity date of 28 March 2027. This is an interest-free shareholder loan with a total amount outstanding at 31 March 2017 of £12.5 million, comprising the £9.6 million receivable held at fair value, and £2.9 million recorded as an equity contribution to Water Plus recognised within interests in joint ventures; and
› £32.5 million outstanding on a £32.5 million revolving credit facility provided by United Utilities PLC, with a maturity date of 30 September 2020, bearing a floating interest rate of LIBOR plus a credit margin.

A further £1.4 million of non-current receivables (2018: £1.4 million) was owed by other related parties at 31 March 2019.

£nil expense or allowance has been recognised for bad and doubtful receivables in respect of amounts owed by related parties (2018: £nil).

During the year, United Utilities PLC provided guarantees in support of Water Plus in respect of certain amounts owed to wholesalers. The aggregate limit of these guarantees was £58.1 million, of which £35.1 million related to guarantees to United Utilities Water Limited.

At 31 March 2019, amounts owed to joint ventures were £0.6 million (2018: £1.4 million). The amounts outstanding are unsecured and will be settled in accordance with normal credit terms (2018: same).

Details of transactions with key management are disclosed in note 3.

Company

The parent company receives dividend income and pays and receives interest to and from subsidiary undertakings in the normal course of business. Total dividend income received during the year amounted to £274.5 million (2018: £267.0 million) and total net interest payable during the year was £30.5 million (2018: £25.4 million). Amounts outstanding at 31 March 2019 and 31 March 2018 between the parent company and subsidiary undertakings are disclosed in notes 15, 17 and 21.

At 31 March 2019 and 31 March 2018, no related party receivables and payables were secured and no guarantees were issued in respect thereof. Balances will be settled in accordance with normal credit terms. No allowance for doubtful receivables has been made for amounts owed by subsidiary undertakings as at 31 March 2019 and 31 March 2018.

A7 Accounting policies

Of the accounting policies outlined below, those deemed to be the most significant for the group are those that align with the critical accounting judgements and key sources of estimation uncertainty set out on pages 168 to 171.

Basis of consolidation

The group financial statements consolidate the financial statements of the company and entities controlled by the company (its subsidiaries), and incorporate the results of its share of joint ventures using the equity method of accounting. The results of subsidiaries and joint ventures acquired or disposed of during the year are included in the consolidated income statement from the date control is obtained or until the date that control ceases, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used under the relevant local GAAP into line with those used by the group. Amounts attributable to non-controlling interests are presented separately in equity and total comprehensive income where material.

Subsidiaries

Subsidiaries are entities controlled by the group. Control is achieved where the group is exposed to, or has the rights to, variable returns from its involvement in an entity and has the ability to affect those returns through its power over the entity. In the parent company accounts, investments are held at cost less provision for impairment.

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. Any deficiency of the cost of acquisition below the fair values of the identifiable net assets acquired is credited to the income statement in the period of acquisition. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Joint ventures

Joint ventures are entities in which the group holds an interest on a long-term basis and which are jointly controlled with one or more parties under a contractual arrangement. The group's share of joint venture results and assets and liabilities is incorporated using the equity method of accounting. Under the equity method, an investment in a joint venture is initially recognised at cost and adjusted thereafter to recognise the group's share of the profit or loss.

On losing control of a subsidiary disposed of to a joint venture, the group recognises the gain or loss attributable to measuring the investment retained in the former subsidiary at its fair value at the date when control is lost.

Revenue recognition

Revenue represents the fair value of the consideration receivable in the ordinary course of business for goods and services provided, exclusive of value added tax and foreign sales tax. Where relevant, this includes an estimate of the sales value of units supplied to customers between the date of the last meter reading and the period end. The group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured. Should the group consider that the criteria for revenue recognition is not met for a transaction, revenue recognition would be delayed until such time as collectability is reasonably assured. Payments received in advance of revenue recognition are recorded as deferred income. This includes the revenue in respect of connection activities which has been impacted by IFRS 15. The revenue in respect of these activities is then released to the income statement over a period of 60 years, which is deemed to be the time over which the performance obligation for providing the connection is satisfied.

Operating profit

Operating profit is stated after charging operational expenses but before investment income and finance expense.

Borrowing costs and finance income

Except as noted below, all borrowing costs and finance income are recognised in the income statement on an accruals basis.

Transaction costs that are directly attributable to the acquisition or issue of a financial asset or financial liability are included in the initial fair value of that instrument.

Where borrowing costs are attributable to the acquisition, construction or production of a qualifying asset, such costs are capitalised as part of the specific asset.

Tax

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Assessing the outcome of uncertain tax positions requires judgements to be made regarding the application of tax law and the result of negotiations with, and enquiries from, tax authorities in a number of jurisdictions. A current tax provision is only recognised when the group has a present obligation as a result of a past event and it is probable that the group will be required to settle that obligation to a taxing authority.

Current tax

Current tax is based on the taxable profit for the period and is provided at amounts expected to be paid or recovered using the tax rates and laws that have been enacted or substantively enacted at each reporting date.

Taxable profit differs from the net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.

Current tax is charged or credited in the income statement, except when it relates to items charged or credited to equity, in which case the tax is also dealt with in equity.

Deferred tax

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are provided, using the liability method, on all taxable temporary differences at each reporting date. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and interests in joint ventures, except where the group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the temporary timing differences are expected to reverse based on tax rates and laws that have been enacted or substantively enacted at each reporting date.

The carrying amount of deferred tax assets is reviewed at each reporting date and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

A7 Accounting policies continued

Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited to equity, in which case the deferred tax is also dealt with in equity.

Property, plant and equipment

Property, plant and equipment comprises water and wastewater infrastructure assets and overground assets.

The useful economic lives of these assets are primarily as follows:

- Water and wastewater infrastructure assets:
  - Impounding reservoirs 200 years;
  - Mains and raw water aqueducts 30 to 300 years;
  - Sewers and sludge pipelines 60 to 300 years;
  - Sea outfalls 77 years;
- Buildings 10 to 60 years;
- Operational assets 5 to 80 years; and
- Fixtures, fittings, tools and equipment 3 to 40 years.

Employee and other related costs incurred in implementing the capital schemes of the group are capitalised where borrowing costs are attributable.

The group is required to evaluate the carrying values of PPE for impairment whenever circumstances indicate, in management's view, that the carrying value of such assets may not be recoverable. An impairment review requires management to make uncertain estimates concerning the cash flows, growth rates and discount rates of the cash generating units under review.

Costs associated with a major inspection or overhaul of an asset or group of assets are capitalised within property, plant and equipment and depreciated over the period of time expected to elapse between major inspections or overhauls.

Water and wastewater infrastructure assets

Infrastructure assets comprise a network of water and wastewater pipes and systems. Expenditure on the infrastructure assets, including borrowing costs where applicable, relating to increases in capacity or enhancements of the network, is treated as additions. Amounts incurred in maintaining the operating capability of the network in accordance with defined standards of service are expensed in the year in which the expenditure is incurred. Infrastructure assets are depreciated by writing off their cost (or deemed cost for infrastructure assets held on transition to IFRS), less the estimated residual value, evenly over their useful economic lives.

Other assets

All other property, plant and equipment is stated at historical cost less accumulated depreciation.

Historical cost includes expenditure that is directly attributable to the acquisition of the items, including relevant borrowing costs, where applicable, for qualifying assets. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

Freehold land and assets in the course of construction are not depreciated. Other assets are depreciated by writing off their cost, less their estimated residual value, evenly over their estimated useful economic lives, based on management's judgement and experience.

Depreciation methods, residual values and useful economic lives are reassessed annually and, if necessary, changes are accounted for prospectively. The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in other operating costs.

Transfer of assets from customers and developers

Where the group receives from a customer or developer an item of property, plant and equipment (or cash to construct or acquire an item of property, plant and equipment) that the group must then use, either to connect the customer to the network, or to provide the customer with ongoing access to a supply of goods or services, or to do both, such items are capitalised at their fair value and included within property, plant and equipment, with a credit of the same amount to deferred grants and contributions. The assets are depreciated over their useful economic lives and the deferred contributions released to revenue over the 60 years, which is the estimated period over which an average connection through which the group provides water and wastewater services is expected to be in place (or where the receipt of property, plant and equipment is solely to connect the customer to the network, the deferred contribution is released immediately to revenue). This accounting treatment has been applied to transfers of assets from customers received on or after 1 July 2009.

Assets transferred from customers or developers are accounted for at fair value. If no market exists for the assets then incremental cash flows are used to arrive at fair value.

Intangible assets

Intangible assets are measured initially at cost and are amortised on a straight-line basis over their estimated useful economic lives. The carrying amount is reduced by any provision for impairment where necessary. On a business combination, as well as recording separable intangible assets already recognised in the statement of financial position of the acquired entity at their fair value, identifiable intangible assets that arise from contractual or other legal rights are also included in the acquisition statement of financial position at fair value.

Internal expenditure is capitalised as internally generated intangibles only if it meets the criteria of IAS 38 'Intangible Assets'.

Intangible assets, which relate primarily to computer software, are amortised over a period of three to 10 years.

Impairment of assets

Where appropriate, assets are reviewed for impairment at each reporting date to determine whether there is any indication that those assets may have suffered an impairment loss. Where the asset does not generate cash flows that are independent from other assets, the group estimates the recoverable amount of the cash generating unit to which the asset belongs.

The recoverable amount is the higher of fair value less costs to sell, and value in use. Value in use represents the net present value of expected future cash flows, discounted on a pre-tax basis, using a rate that reflects current market assessments of the time value of money and the risks specific to the asset, for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash generating unit) is reduced to its recoverable amount. Impairment losses in respect of non-current assets are recognised in the income statement within operating costs.

A7 Accounting policies continued

Where an impairment loss subsequently reverses, the reversal is recognised in the income statement and the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but not so as to exceed the carrying amount that would have been determined had no impairment loss been recognised in prior years.

Non-current assets held for sale

Non-current assets classified as held for sale are measured at the lower of carrying value and fair value less costs to sell. Non-current assets are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as having been met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Financial instruments

Financial assets and financial liabilities are recognised and derecognised on the group's statement of financial position on the trade date when the group becomes/ceases to be a party to the contractual provisions of the instrument.

Cash and short-term deposits

Cash and short-term deposits include cash at bank and in hand, deposits and other short-term highly liquid investments which are readily convertible into known amounts of cash, have a maturity of three months or less from the date of acquisition and which are subject to an insignificant risk of change in value. In the consolidated statement of cash flows and related notes, cash and cash equivalents include cash and short-term deposits, net of book overdrafts.

Financial investments

Investments (other than interests in subsidiaries, joint ventures and fixed deposits) are initially measured at fair value, including transaction costs. Investments classified as financial assets measured at fair value through profit or loss (FVPL) in accordance with IFRS 9 'Financial Instruments' are measured at subsequent reporting dates at fair value. Gains and losses arising from changes in fair value are recognised in the net profit or loss for the period. The business model employed in respect of financial assets is that of a hold-to-collect model.

Trade receivables

Trade receivables are initially measured at fair value, and are subsequently measured at amortised cost, less any impairment for irrecoverable amounts. Estimated irrecoverable amounts are based on historical experience of the receivables balance.

Trade payables

Trade payables are initially measured at fair value and are subsequently measured at amortised cost.

Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the group after deducting all of its liabilities.

Equity instruments

Equity instruments issued by the group are recorded at the proceeds received, net of direct issue costs.

Borrowings

The group's default treatment is that bonds and loans are initially measured at fair value, being the cash proceeds received net of any direct issue costs. They are subsequently measured at amortised cost applying the effective interest method. The difference between the net cash proceeds received at inception and the principal cash flows due at maturity is accrued over the term of the borrowing.

The default treatment of measuring at amortised cost, while associated hedging derivatives are recognised at fair value, presents an accounting measurement mismatch that has the potential to introduce considerable volatility to both the income statement and the statement of financial position. Therefore, where feasible, the group takes advantage of the provisions under IFRS 9 'Financial Instruments' to make fair value adjustments to its borrowing instruments to reduce this volatility and better represent the economic hedges that exist between the group's borrowings and associated derivative contracts.

Where feasible, the group designates its financial instruments within fair value hedge relationships. In order to apply fair value hedge accounting, it must be demonstrated that there is an economic relationship between the borrowing instrument and the hedging derivative and that the designated hedge ratio is consistent with the group's risk management strategy.

Borrowings designated within a fair value hedge relationship

Where designated, bonds and loans are initially measured at fair value, being the cash proceeds received net of any direct issue costs. They are subsequently adjusted for any change in fair value attributable to the risk being hedged at each reporting date, with the change being charged or credited to finance expense in the income statement.

Hedge accounting is discontinued prospectively when the hedging instrument is sold, terminated or exercised, or where the hedge relationship no longer qualifies for hedge accounting.

Under the provisions of IFRS 9 'Financial Instruments', changes in the group's own credit risk are recognised in other comprehensive income.

Borrowings designated at fair value through profit or loss

Designation is made where the requirements to designate within a fair value hedge cannot be met at inception despite there being significant fair value offset between the borrowing and the hedging derivative. Where designated, bonds and loans are initially measured at fair value being the cash proceeds received and are subsequently measured at fair value at each reporting date, with changes in fair value being charged or credited to finance expense in the income statement.

Derivative financial instruments

The group's default treatment is that derivative financial instruments are measured at fair value at each reporting date, with changes in fair value being charged or credited to finance expense in the income statement. The group enters into financial derivatives contracts to manage its financial exposure to changes in market rates (see note A4).

Derivative financial instruments designated within a cash flow hedge relationship

Gains or losses resulting from the effective portion of the hedging instrument are recognised in other comprehensive income and in the cash flow hedge reserve with any remaining gains or losses recognised immediately in the income statement. The cash flow hedge reserve is adjusted to the lower of the cumulative gain or loss on the hedging instrument and cumulative change in fair value of the hedged item. At the maturity date, amounts paid/received are recognised against operating expenses in the income statement.

A7 Accounting policies continued

Upon discontinuation of a cash flow hedge, the amount accumulated in other comprehensive income remains in the cash flow hedge reserve if the hedged future cash flows are still expected to occur. Otherwise the amount is immediately reclassified to the income statement.

Derivatives and borrowings – valuation

Where an active market exists, designated borrowings and derivatives recorded at fair value are valued using quoted market prices. Otherwise, they are valued using a net present value valuation model. The model uses applicable interest rate curve data at each reporting date to determine any floating cash flows. Projected future cash flows associated with each financial instrument are discounted to the reporting date using discount factors derived from the applicable interest curves adjusted for counterparty credit risk where appropriate. Discounted foreign currency cash flows are converted into sterling at the spot exchange rate at each reporting date. Assumptions are made with regard to credit spreads based on indicative pricing data.

The valuation of debt designated in a fair value hedge relationship is calculated based on the risk being hedged as prescribed by IFRS 9 'Financial Instruments'. The group's policy is to hedge its exposure to changes in the applicable underlying interest rate and it is this portion of the cash flows that is included in the valuation model (excluding any applicable company credit risk spread).

The valuation of debt designated at fair value through the profit or loss incorporates an assumed credit risk spread in the applicable discount factor. Credit spreads are determined based on indicative pricing data.

Inventories

Inventories are stated at the lower of cost and net realisable value. For properties held for resale, cost includes the cost of acquiring and developing the sites, including borrowing costs where applicable.

Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Employee benefits

Retirement benefit obligations

The group operates two defined benefit pension schemes, which are independent of the group's finances, for its employees. Actuarial valuations to determine the funding of the schemes, along with future contribution rates, are carried out by the pension scheme actuary as directed by the trustees at intervals of not more than three years. In any intervening years, the trustees review the continuing appropriateness of the funding and contribution rates.

From a financial reporting perspective and in accordance with IAS 19 'Employee Benefits', defined benefit assets are measured at fair value while liabilities are measured at present value, using the projected unit credit method. The difference between the two amounts is recognised as a surplus or obligation in the statement of financial position. Where this difference results in a defined benefit surplus, this is recognised in accordance with IFRIC 14 'IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction', on the basis that the group has an unconditional right to a refund of any surplus that may exist following the full settlement of plan liabilities in a single event.

The pension cost under IAS 19 is assessed in accordance with the advice of a firm of actuaries based on the latest actuarial valuation and assumptions determined by the actuary, which are used to estimate the present value of defined benefit obligations. The assumptions are based on information supplied to the actuary by the company, supplemented by discussions between the actuary and management. The assumptions are disclosed in note A5.

The cost of providing pension benefits to employees relating to the current year's service (including curtailment gains and losses) is included within employee benefits expense, while the interest on the schemes' assets and liabilities is included within investment income and finance expense respectively. Remeasurement gains/losses on scheme assets and liabilities are presented in other comprehensive income.

In addition, the group also operates a defined contribution pension section within the United Utilities Pension Scheme. Payments are charged as employee costs as they fall due. The group has no further payment obligations once the contributions have been paid.

Share-based compensation arrangements

The group operates equity-settled, share-based compensation plans, issued to certain employees. The equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date is expensed on a straight-line basis over the vesting period, based on estimates of the number of options that are expected to vest. Fair value is based on simulation models, according to the relevant measures of performance. The group has the option to settle some of these equity-settled share-based payments in cash. At each reporting date, the group revises its estimate of the number of options that are expected to become exercisable with the impact of any revision being recognised in the income statement, and a corresponding adjustment to equity over the remaining vesting period.

Provisions

Provisions are recognised when the group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Expenditure that relates to an existing condition caused by past operations that does not contribute to current or future earnings is expensed.

Foreign currency translation

Transactions and balances

Transactions in foreign currencies are recorded at the exchange rates applicable on the dates of the transactions. At each reporting date, monetary assets and liabilities denominated in foreign currencies are translated into sterling at the relevant rates of exchange applicable on that date. Gains and losses arising on retranslation are included in net profit or loss for the period.

Exchange differences arising on investments in equity instruments classified as fair value through other comprehensive income are included in the gains or losses arising from changes in fair value which are recognised directly in equity. In order to hedge its exposure to certain foreign exchange risks, the group enters into derivative instruments (see note A4).

Group companies

On consolidation, the statements of financial position of overseas subsidiaries and joint ventures (none of which has the currency of a hyperinflationary economy) are translated into sterling at exchange rates applicable at each reporting date. The income statements are translated into sterling using the average rate unless exchange rates fluctuate significantly, in which case the exchange rate at the date the transaction occurred is used. Exchange differences resulting from the translation of such statements of financial position at rates ruling at the beginning and end of the period, together with the differences between income statements translated at average rates and rates ruling at the period end, are dealt with as movements on the group's cumulative exchange reserve, a separate component of equity. Such translation differences are recognised as income or expense in the period in which the operation is disposed of.

A7 Accounting policies continued

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate. The group has elected to treat goodwill and fair value adjustments arising on acquisitions before the date of implementation of IFRS 3 'Business Combinations' (1 April 1999) as sterling-denominated assets and liabilities.

Grants and contributions

Grants and contributions receivable in respect of property, plant and equipment are treated as deferred income, which is credited to the income statement over the estimated useful economic lives of the related assets.

Leases

Leases are classified according to the substance of the transaction. Operating leases are leases that do not transfer substantially all the risks and rewards of ownership to the lessee.

Operating lease rentals are charged to the income statement on a straight-line basis over the period of the lease.

Notes to the financial statements – appendices

A8 Subsidiaries and other group undertakings

Details of the group's subsidiary undertakings, joint ventures and associates are set out below. Unless otherwise specified, the registered address for each entity is Haweswater House, Lingley Mere Business Park, Lingley Green Avenue, Great Sankey, Warrington, WA5 3LP, United Kingdom. For further details of joint ventures and associates please see notes 12 and 13.

	Class of share capital held	Proportion of share capital owned/voting rights %*	Nature of business
Subsidiary undertakings			
Great Britain			
Halkyn District Mines Drainage Company Limited	Ordinary	99.9	Dormant
Lingley Mere Management Company Limited	Ordinary	90.7	Property management
North West Water International Limited	Ordinary	100.0	Holding company
North West Water Limited	Ordinary	100.0	Dormant
United Utilities (Overseas Holdings) Limited	Ordinary	100.0	Holding company
United Utilities Bioresources Limited	Ordinary	100.0	Wastewater services
United Utilities Energy Limited	Ordinary	100.0	Non-trading
United Utilities Healthcare Trustee Limited	Ordinary	100.0	Corporate trustee
United Utilities International Limited	Ordinary	100.0	Consulting services and project management
United Utilities North West Limited	Ordinary	100.0	Holding company
United Utilities Pensions Trustees Limited	Ordinary	100.0	Corporate trustee
United Utilities PLC	Ordinary	100.0	Holding and management company
United Utilities Property Services Limited	Ordinary	100.0	Property management
United Utilities Renewable Energy Limited	Ordinary	100.0	Renewable energy generation
United Utilities Total Solutions Limited	Ordinary	100.0	Waste treatment
United Utilities Utility Solutions (Industrial) Limited	Ordinary	100.0	Holding company
United Utilities Water Finance PLC	Ordinary	100.0	Financing company
United Utilities Water Limited	Ordinary	100.0	Water and wastewater services
UU (ESPS) Pension Trustee Limited	Ordinary	100.0	Corporate trustee
UU Group Limited	Ordinary	100.0	Dormant
UU Secretariat Limited	Ordinary	100.0	Dormant
YCL Transport Limited	Ordinary	100.0	Non-trading
The Netherlands			
United Utilities (Tallinn) BV	Ordinary	100.0	Holding company
Thailand			
Manta Management Services Limited(1)	Ordinary	49.0	Management company
Joint ventures			
Great Britain			
Lingley Mere Business Park Development Company Limited	Ordinary	50.0	Development company
Selectusonline Limited	Ordinary	16.7	Procurement portal
Water Plus Group Limited(2)	Ordinary	50.0	Water and wastewater non-household retail
Water Plus Limited(2)	Ordinary	50.0	Water and wastewater non-household retail
Water Plus Select Limited(2)	Ordinary	50.0	Water and wastewater non-household retail
Estonia			
AS Tallinna Vesi(3)	Ordinary	35.3	Water and wastewater services
Associated undertakings			
Bahrain			
Muharraq STP Company BSC(c)(4)	Ordinary	20.0	Project company
Muharraq Wastewater Services Company WLL(4)	Ordinary	35.0	Operations and maintenance company
Jebel Ali Free Zone, Dubai, UAE			
Muharraq Holding Company 1 Limited(5)	Ordinary	20.0	Holding company
Muharraq Holding Company 2 Limited(5)	Ordinary	20.0	Holding company

* With the exception of United Utilities PLC, shares are held by subsidiary undertakings rather than directly by United Utilities Group PLC.

(1) Registered address: Unit 2201, No. 1. Soi Chan 2, Yak 3 Chan Road, Thung Wat Don Sub District, Sathorn District, Bangkok, Thailand 10120.
(2) Registered address: Two Smithfield, Leonard Coates Way, Stoke-on-Trent, ST1 4FD, United Kingdom.
(3) Registered address: Adala 10, Tallinn 10614, Estonia.
(4) Registered address: Building 200, Road 13, Block 115, Hidd, Kingdom of Bahrain.
(5) Registered address: Al Tamimi & Company, 9th Floor, Dubai World Trade Centre, Sheikh Zayed Road, Dubai, United Arab Emirates

Five-year summary – unaudited

The financial summary (unaudited) set out below has been derived from the audited consolidated financial statements of United Utilities Group PLC for the five years ended 31 March 2019. It should be read in conjunction with the consolidated financial statements and related notes, together with the strategic report.

Year ended 31 March Continuing operations	**2019** **£m**	2018 £m	2017 £m	2016 £m	2015 £m
Revenue	**1,818.5**	1,735.8	1,704.0	1,730.0	1,720.2
Operating profit per reported results	**634.9**	636.4	605.5	567.9	653.3
Underlying operating profit	**684.8**	645.1	622.9	604.1	664.3
Profit before tax per reported results	**436.2**	432.1	442.4	353.5	341.6
Underlying profit before tax	**460.3**	370.2	389.4	408.1	447.4
Profit after taxation per reported results	**363.4**	354.6	433.9	397.5	271.2
Underlying profit after tax	**378.7**	304.9	313.4	325.3	354.1
Earnings per share (basic) per reported results (pence)	**53.3p**	52.0p	63.6p	58.3p	39.8p
Underlying earnings per share (pence)	**55.5p**	44.7p	46.0p	47.7p	51.9p
Dividend per ordinary share (pence)	**41.28p**	39.73p	38.87p	38.45p	37.70p
Non-current assets	**12,466.4**	11,853.6	11,768.2	11,280.8	10,664.8
Current assets	**721.4**	1,149.9	657.9	626.0	638.8
Total assets	**13,187.8**	13,003.5	12,426.1	11,906.8	11,303.6
Non-current liabilities	**(9,025.0)**	(8,911.1)	(8,914.7)	(8,357.1)	(7,867.7)
Current liabilities	**(1,052.0)**	(1,141.5)	(689.8)	(844.2)	(1,001.5)
Total liabilities	**(10,077.0)**	(10,052.6)	(9,604.5)	(9,201.3)	(8,869.2)
Total net assets and shareholders' equity	**3,110.8**	2,950.9	2,821.6	2,705.5	2,434.4
Net cash generated from operating activities	**832.3**	815.6	820.8	685.6	706.5
Net cash used in investing activities	**(627.7)**	(723.2)	(804.6)	(676.8)	(704.9)
Net cash (used in)/generated from financing activities	**(377.4)**	184.7	22.0	(46.4)	139.2
Net (decrease)/increase in cash and cash equivalents	**(172.8)**	277.1	38.2	(37.6)	140.8
Net debt	**7,067.3**	6,867.8	6,578.7	6,260.5	5,924.0
RCV gearing[1] (%)	**61%**	61%	61%	61%	59%

Note:

(1) Regulatory capital value (RCV) gearing is calculated as group net debt (see note A2), divided by the RCV expressed in out-turn prices, of United Utilities Water Limited.

Shareholder information

Key dates

- **20 June 2019**
  Ex-dividend date for 2018/19 final dividend
- **21 June 2019**
  Record date for 2018/19 final dividend
- **26 July 2019**
  Annual general meeting
- **1 August 2019**
  Payment of 2018/19 final dividend to shareholders
- **20 November 2019**
  Announcement of half-year results for the six months ending 30 September 2019
- **19 December 2019**
  Ex-dividend date for 2019/20 interim dividend
- **20 December 2019**
  Record date for 2019/20 interim dividend
- **3 February 2020**
  Payment of 2019/20 interim dividend to shareholders
- **May 2020**
  Announce the final results for the 2019/20 financial year
- **June 2020**
  Publish the Annual Report and Financial Statements for the 2019/20 financial year

Electronic communications

We're encouraging our shareholders to receive their shareholder information by email and via our website. Not only is this a quicker way for you to receive information, it helps us to be more sustainable by reducing paper and printing materials and lowering postage costs.

Registering for electronic shareholder communications is very straightforward, and is done online via **shareview.co.uk** which is a website provided by our registrar, Equiniti.

Log on to **shareview.co.uk** and you can:

- set up electronic shareholder communication;
- view your shareholdings;
- update your address details if you change your address; and
- get your dividends paid directly into your bank account.

Please do not use any electronic address provided in this notice or in any related document to communicate with the company for any purposes other than those expressly stated.

Why not make life easy and have your dividends paid straight to your bank?

- The dividend goes directly into your bank account and is available immediately;
- No need to pay dividend cheques into your bank account;
- No risk of losing cheques in the post;
- No risk of having to replace spoiled or out-of-date cheques; and
- It's cost-effective for your company.

To take advantage of this, please contact Equiniti via **shareview.co.uk** or complete the dividend mandate form you receive with your next dividend cheque.

If you choose to have your dividend paid directly into your bank account you'll receive one tax voucher each year. This will be issued with the interim dividend normally paid in February and will contain details of all the dividends paid in that tax year. If you'd like to receive a tax voucher with each dividend payment, please contact Equiniti.

Online annual report

Our annual report is available online. View or download the full Annual Report and Financial Statements from:
unitedutilities.com/corporate

Keeping you in the picture

You can find information about United Utilities quickly and easily on our website: **unitedutilities.com/corporate**. Here the Annual Report and Financial Statements, responsible business performance, company announcements, the half-year and final results and presentations are published.

Registrar

The group's registrar, Equiniti, can be contacted on: **0371 384 2041** or textphone for those with hearing difficulties: **0371 384 2255**. Lines are open 8.30 am to 5.30 pm, Monday to Friday excluding public holidays in England and Wales.

The address is:
Equiniti, Aspect House, Spencer Road,
Lancing, West Sussex, BN99 6DA.

Overseas shareholders may contact them on:
+44 (0)121 415 7048

Equiniti offers a share dealing service by telephone: **0345 603 7037** and online: **shareview.co.uk/dealing**

Equiniti also offers a stocks and shares ISA for United Utilities shares: call **0345 300 0430** or go to: **shareview.co.uk/dealing**

Looking after your investment

Our approach to responsible business has again helped us to retain world class status in the Dow Jones Sustainability index for the eleventh consecutive year and in 2018 we achieved the Industry mover award for our sector.

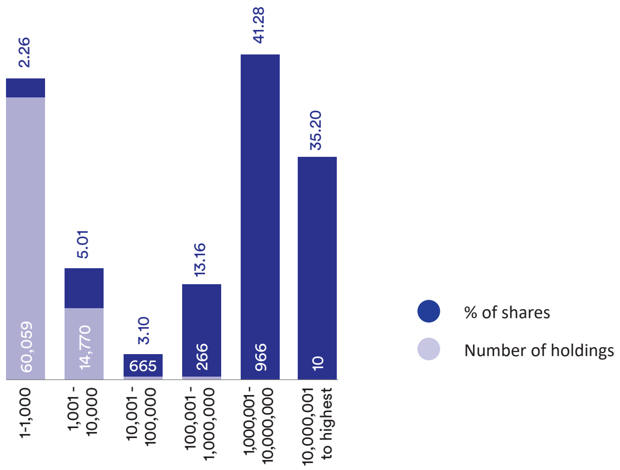
Our membership of the FTSE4Good Index continued for the seventeenth year and we also received a B rating in the Carbon Disclosure Project. We have maintained our position in the Euronext Vigeo index: UK 20 and been reconfirmed as a constituent of the Ethibel Sustainability Index Excellence Europe for our environmental, social and governance performance.

We have retained our Gold award status with the Royal Society for the Prevention of Accidents and been awarded the Chartered Institute of Procurement and Supply Corporate Ethics Mark for our sustainable and ethical approach.

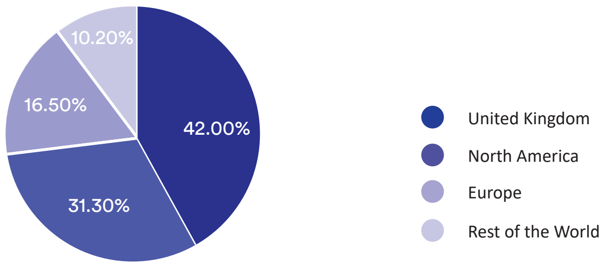
This document is printed on Cocoon Silk 100 which is made from 100% FSC® Recycled pulp and post-consumer waste paper. This reduces waste sent to landfill, greenhouse gas emissions, as well as the amount of water and energy consumed.

Key shareholder facts

Balance analysis as at 31 March 2019



Shareholders by location



Dividend history – pence per share

	2015	2016	2017	2018	**2019**
Interim	12.56	12.81	12.95	12.24	**13.76**
Final	25.14	25.64	25.92	26.49	**27.52**
Total ordinary	37.70	38.45	38.87	39.73	**41.28**

Warning to shareholders

Please be very wary of any unsolicited contact about your investments or offers of free company reports. It may be from an overseas 'broker' who could sell you worthless or high-risk shares. If you deal with an unauthorised firm, you would not be eligible to receive payment under the Financial Services Compensation Scheme. Further information and a list of unauthorised firms that have targeted UK investors is available from the Financial Conduct Authority at: **fca.org.uk/consumers/protect-yourself/unauthorised-firms**

Important information

Cautionary statement:

The Annual Report and Financial Statements (the annual report) contains certain forward-looking statements with respect to the operations, performance and financial condition of the group. By their nature, these statements involve uncertainty since future events and circumstances can cause results and developments to differ materially from those anticipated. The forward-looking statements reflect knowledge and information available at the date of preparation of this annual report and the company undertakes no obligation to update these forward-looking statements. Nothing in this annual report should be construed as a profit forecast. Certain regulatory performance data contained in this annual report is subject to regulatory audit.

Terms used in this report:

Unless expressly stated otherwise, the 'group', 'United Utilities', 'UU' or 'the company' means United Utilities Group PLC and its subsidiary undertakings; the 'regulated business', 'regulated activities' or 'UUW' means the licensed water and wastewater activities undertaken by United Utilities Water Limited (formerly United Utilities Water PLC) in the North West of England.

United Utilities Group PLC
Haweswater House
Lingley Mere Business Park
Lingley Green Avenue
Great Sankey
Warrington
WA5 3LP

Telephone +44 (0)1925 237000

Stock Code: UU.
Registered in England and Wales
Registered number 6559020