



Tax, plain and simple.

Our annual tax report

2019 REPORT

Introduction

Our total contribution to public finances for 2019 was in excess of £240 million and this is a typical amount paid by United Utilities each and every year.

United Utilities group ('the group') is fully committed to paying its fair share of tax and acting in an open and transparent manner in relation to its tax affairs.

As part of this commitment, we are constantly looking at ways to further improve the communication and transparency of our approach to tax.

I am delighted to introduce our inaugural annual tax report: **'Tax, plain and simple'**

In preparing our main, statutory Annual Report, we work hard to ensure that it contains relevant information for all stakeholders. The Annual Report contains a comprehensive disclosure of our tax related information but we felt that stakeholders would welcome a report just focused on tax.

In producing this new tax report, we want to reach a broad range of stakeholders. Accordingly, the main body of the report presents a summary but there is also more detailed information included via the **#MORE** links to the relevant appendix or other hyperlinks to information elsewhere in the report or online.

In addition, at the end of the report we have included a **GLOSSARY** of key tax terms used.

Our report addresses the following three key themes:

1. **How much tax do we pay?**
2. **How do we ensure we pay the right amount of tax at the right time?**
3. **How do we ensure our tax affairs are transparent?**



From next year, we intend to publish this annual tax report at the same time as our main, statutory Annual Report. We expect the contents of this report to evolve over time and we would welcome any feedback on this inaugural edition.

Russ Houlden
Chief Financial Officer



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1. How much tax do we pay?

Business rates

£95m

Business rates are chargeable on all non-domestic property unless subject to a relief. To deliver our services, we have 56,000 hectares of land, 165 reservoirs, 88 water treatment works, 569 wastewater treatment works and many support buildings.



Corporation tax

£28m



We are primarily a UK based group with only a few minor overseas interests. You can read more about this at [#MORE7](#)

Employment taxes

Company
£23m



Employees
£50m



We have around 5,000 employees and we support thousands of jobs via our supply chain, making us one of the biggest employers in the North West.



Environmental taxes / other duties

£17m



Our energy strategy is to use less and generate more renewable energy. We are subject to a number of taxes on our carbon footprint and the energy we use including carbon emissions tax, climate change levy and fuel duty. As part of providing water and wastewater services, we produce waste such as sludge, excavated materials and general office waste. We are committed to managing this in a sustainable way, with around five per cent of our waste going to landfill which is subject to the landfill tax.

Regulatory service fees

£28m



We hold licences with the Environment Agency that permit us to abstract water from the natural environment – we treat this and supply drinking water to seven million people in the North West every day. We also hold permits with the Environment Agency to enable us to discharge treated water back into the environment in a controlled manner.

“ £190 million of the total represents a cost borne by the group with the balance of £50 million being taxes borne by employees and collected by the group on their behalf. ”

TOTAL
£241m



2. How do we ensure we pay the right tax at the right time?

We have a formal set of tax policies and objectives that are approved by the board of directors on an annual basis, covering three main pillars:

1. We do not engage in aggressive or abusive tax avoidance; we do look to structure commercial activities efficiently both within the letter and spirit of the law **#MORE1**

2. We maintain a robust governance and risk management framework to ensure our tax policies are applied throughout the group **#MORE2**

3. We are committed to open, transparent and professional relationships with all relevant tax authorities based on mutual trust and collaborative working **#MORE4**

We have a specialist tax team that monitors delivery against the tax policies and objectives, working with colleagues to ensure we have a sustainable approach to tax risk management **#MORE3**

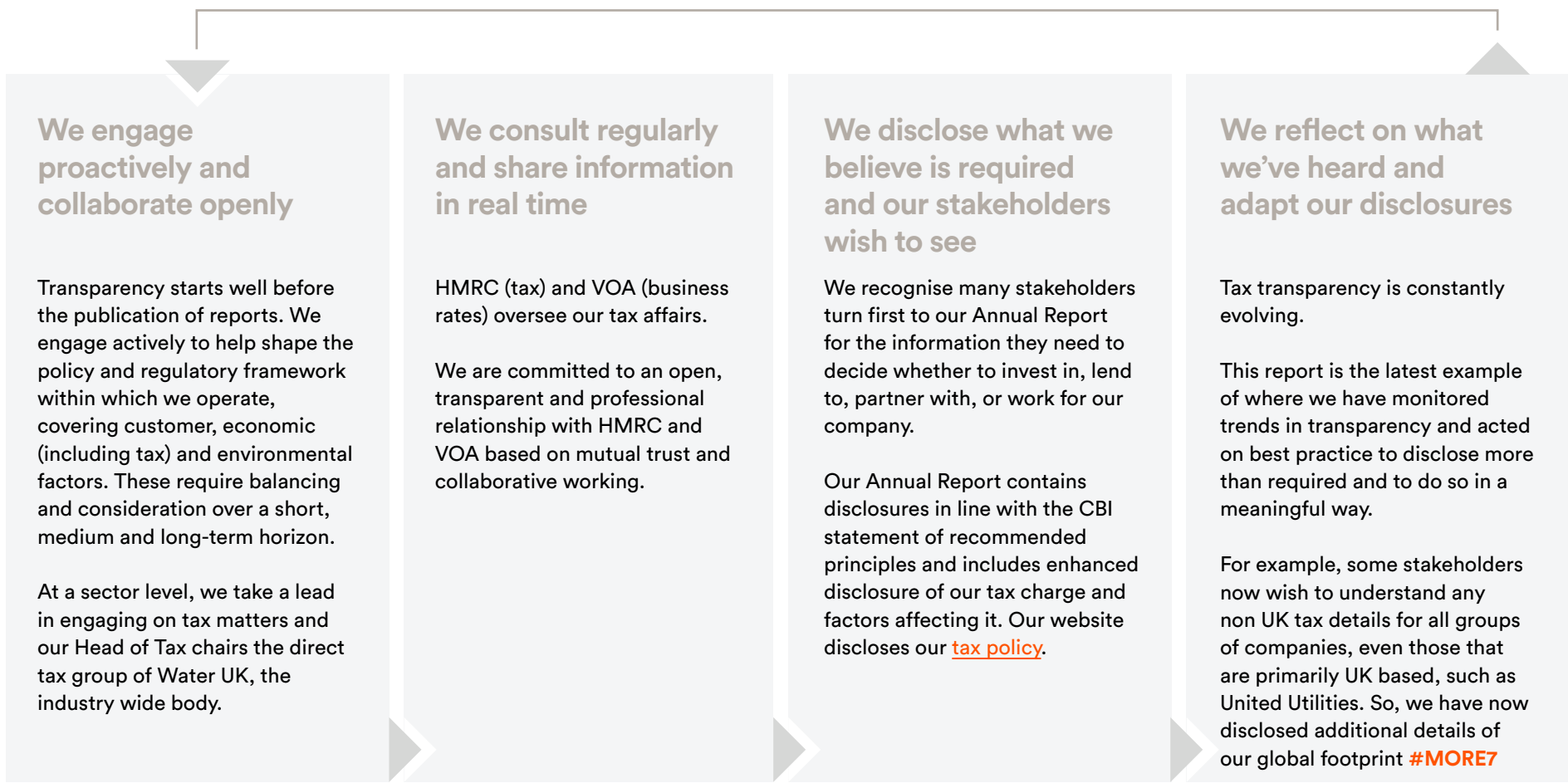
We are subject to detailed regulation in terms of price and performance. 97 per cent of group revenue comes from this regulated business. **#MORE5**


We monitor and claim relevant tax incentives and reliefs **#MORE6**

“ Our tax policies have been fully complied with for many years, including the 2019 period. ”



3. How do we ensure our tax affairs are transparent?



An aerial photograph of a complex industrial facility, likely a power plant or refinery. The scene is filled with a dense network of silver-colored pipes, some wrapped in grey insulation, and various mechanical components. In the lower right foreground, a worker wearing a white hard hat, a high-visibility yellow safety vest over a dark jacket, and black pants is walking across the concrete floor. The overall lighting is somewhat dim, suggesting an indoor or shaded industrial environment.

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We do not engage in
aggressive or abusive
tax avoidance.”

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We know the question of tax, and paying our ‘fair share’ is important to stakeholders and society more generally. It is a subject that goes beyond just the tax team, with a tax strategy approved by the board that is promoted across the business to ensure that all of our people act consistently with our agreed values and objectives.

We only engage in reasonable tax planning. In other words, we ensure that commercial activities and transactions are structured tax efficiently in compliance with what we consider to be both the letter and the spirit of the law. Our directors have a duty to promote the success of the company and that includes not paying more tax than a company is obliged to do.

What does that actually mean?

An example would be when we’re planning a major capital investment programme, we are mindful of the different rates of allowances that may be available for energy efficient assets which may influence our choice of equipment.

We do therefore claim reliefs, such as allowances in relation to our capital spend and manage our tax as a cost of business, like any other. However, we believe we operate a sustainable and responsible approach to tax planning that balances the interests of all our stakeholders.

Taking corporation tax alone, we’ve paid £28 million this year and over a quarter of a billion pounds in respect of the previous five years, making us consistently one of the highest payers of corporation tax in the UK water sector.



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We maintain a
robust risk and
governance
framework and we
work within it. ”



Our strategy sets out our approach to tax and to deliver it we have a framework to ensure that its values are embedded in everything that we do.

Risk Framework

Consistent with the group's general risk management framework, all tax risks are assessed for the likelihood of occurrence and the financial or reputational impact on the group and its objectives, should the event occur. As a consequence of the sector's five-year regulatory cycle, 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 engaging actively with relevant authorities to manage any such risk. We proactively lobby, both at a company and an industry level where appropriate, to minimise the impact of any proposed changes in tax law or

HMRC practice which could materially impact on the group. For example, when the OTS announced it was considering abolishing the capital allowance regime in favour of new rules based around accounting depreciation, we actively engaged with the OTS, both as a company and through sector wide tax groups, to put our views across.

Governance framework

Our governance process is the basis by which we ensure our tax returns are right and can be traced right through the group's accounting systems and processes. We are required to certify on an annual basis that we've taken reasonable steps to ensure that our tax accounting arrangements are fit for purpose and this is managed via the involvement of our specialist tax team.



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One specialist tax team.
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With an overarching strategy agreed by the board and a strong risk framework established to support that, both require monitoring by people well equipped to understand the tax risks and how to manage them.

Ultimately, our CFO is responsible for tax governance with oversight from the board. He is our Senior Accounting Officer and, as such, is required to certify on an annual basis that each relevant company in the group has taken reasonable steps to ensure that its tax accounting arrangements are fit for purpose for all major tax related risk areas.

The CFO is supported by a specialist team of tax professionals with more than 50 years of tax experience within the water sector. Led by the Head of Tax, the team includes people with specific responsibilities for different taxes, such as corporation tax, employment taxes and VAT.

The Head of Tax has ‘day to day’ responsibility for managing the group’s tax affairs and engages regularly with colleagues to ensure tax risk is proactively managed. For example, he speaks regularly with the legal team to ensure that tax is always considered for the many transactions and projects they are involved with.

The team engages with both external advisers and HMRC to obtain additional advice and certainty with the aim of ensuring that any residual risk is typically low. The Head of Tax is chair of Water UK’s direct tax group, keeping track of key sector wide tax issues and leading the Industry’s collective response.

All significant tax issues are reported to the board regularly. They have agreed the strategy and take a keen interest in ensuring it is faithfully applied.



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We are committed to open, transparent and professional relationships with all tax authorities based on mutual trust and collaborative working. **”**



Our tax team has the job of delivering the tax strategy and developing strong, professional relationships with the key authorities who monitor our compliance with relevant rules and regulations.

HMRC

We are committed to having an open and professional relationship with HMRC which includes operating on full disclosure. For the various tax compliance processes, we meet regularly with HMRC to agree key risk areas and share how our risk framework identifies and manages these risks. We do in-year testing to flag up any issues in real time and share the results with them. We also operate a system of real time disclosure with HMRC whereby we discuss significant proposed transactions so that any concerns can be discussed in advance of returns being formally submitted.

Valuation Office Agency

Given our largest single tax outflow is business rates, where we pay nearly £100m each year, we hold regular meetings with the VOA team in charge of the UK water sector, typically every six months. We provide respective business updates and discuss the latest business rates issues relevant to us.



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We operate in a
complex regulatory
environment. ”



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 and secure that the company can finance carrying out of these functions – in particular through securing reasonable returns on capital, ensuring 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.

How is it determined whether our strategy and tax forecasting is fair?

By submitting a robust, balanced plan to Ofwat prior to the start of each five-year regulatory period, our aim is to agree a regulatory contract that allows for the best overall outcomes for our customers, shareholders and the environment.

Ofwat scrutinises and challenges these business plans, and sets the five-year price, service and incentive package. This becomes the regulatory contract that company performance is measured against. It ensures all interactions between the regulatory entities and the group are undertaken at arm's length.

What does that mean for tax?

As part of that plan, we provide detailed tax calculations which are independently reviewed

by Ofwat. As Ofwat sees all the different regulated water companies' tax calculations, not only are the details closely scrutinised against our wider financial plan and best assumptions, they are benchmarked across the whole industry.

Detailed work is undertaken on an annual basis and reviewed by the regulator to assess how we are performing against the contract. Given the regulatory contract is set five years in advance, we use our best estimates but sometimes changes outside of our control can occur. For example, in the past five years the UK's headline corporation tax rate has dropped from 21 per cent to 19 per cent.

Recognising that these matters are outside of management's control, the impact of changes to tax rates and capital allowances will now be passed back to customers under the terms of the regulatory contract commencing in financial year 2020/21.



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**We monitor and
claim relevant tax
incentives and reliefs.**

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Tax is a cost of doing business and just like any other, it needs to be planned for, budgeted and managed efficiently so that we pay our fair share.

Our group's overall effective tax rate on underlying profits will typically broadly match the UK headline rate, currently at 19 per cent. However the actual effective cash tax rate may fluctuate from the headline UK rate year by year due to the way statutory tax relief works for items such as capital investment, pensions, R&D and financing:

An important element of the group's tax liability position is tax allowances on our capital spend. We spent £800 million on capital items in 2019, so any changes to the allowances can significantly affect our tax bill. From 1 April 2019, the rate of tax allowance on the majority of our infrastructure spend reduced from 8 per cent to 6 per cent and will result in an

estimated additional annual tax liability of around £10 million. We invest in R&D to make our processes and operations more efficient. We claim reliefs on this expenditure where applicable.

The above tax deductions are achieved as a result of statutory reliefs, or utilising tax incentives which have been explicitly put in place by successive governments precisely to encourage such investment in infrastructure and innovation. The impact of this is set out in our [detailed tax disclosures](#).

We are largely a UK group and our funding comes from non-related parties. We have not been negatively impacted by the recent changes

to the tax deductibility of interest rules which were generally targeted at groups that had a disproportionate amount of debt in the UK as compared with their overall group position. Our interest costs remain deductible in the UK. Managing our financial position is complex and the movement on unrealised profits and losses on our debt and derivatives portfolio can be significant. The tax treatment of some of this follows the accounts and for others is based on specific tax rules. As such, the impact can be volatile but all profits and losses remain subject to tax in the UK.



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For the relatively small amount of overseas income we receive, we pay tax at the UK rate or higher. ”



The group is committed to paying its fair share of tax and this includes a commitment not to use tax havens for tax avoidance purposes.

Whilst we are now primarily a UK business, we do still have some small legacy commercial operations overseas. The registered address of each of the entities noted below is also the place of incorporation

Estonia

We hold a 35.3 per cent interest in AS Tallinna Vesi, a listed Estonian water company. Profits are taxed on a distribution basis in Estonia. The net distributed income for 2018/19 was €2.5 million with associated Estonian tax payments of €635k, representing a tax rate of 25%. Once distributed, all of our share of profits from AS Tallinna Vesi will typically be fully taxed in Estonia.

Netherlands

We hold a 100 per cent interest in United Utilities Tallinn BV, a Dutch holding company which holds our shares in AS Tallinna Vesi. For 2018/19, it received a dividend of €2.5 million from profits that have been fully taxed in Estonia and paid on a dividend of €2.4 million, the balance of around €100k being retained to cover its costs. It had no other income.

Thailand

We hold a 100 per cent interest in Manta Management Services Limited, a company resident in Thailand where the group used to have operations. This company has no operating income or profit and is in the process of being dissolved.

Bahrain/Dubai

We hold interests in four companies involved in Muharraq sewage treatment plant in Bahrain. The cumulative net group income for the eight years to 2018/19 was around £5 million and was fully taxed in the UK.

India

We hold a 1 per cent interest in Mahindra Water Utilities Limited, an Indian trading company. Our only source of income from this shareholding is dividend income of which we have received a total of £10 thousand over the last six years and this income will have been subject to Indian tax at above the UK rate.



GLOSSARY

Accounting depreciation

Is an accounting method of allocating the cost of a tangible asset over its useful life and is used to account for declines in value.

Arm's length

Refers to the pricing of a transaction between two parties and indicates that it is equivalent to that which would occur between independent parties.

Business rates

Set by the government and collected by local authorities, these are the means by which those who occupy non-domestic property contribute towards the cost of local services.

Capital allowances

The tax equivalent of accounting depreciation, allowing a company to obtain tax relief on tangible capital expenditure at rates and over periods of time set within the tax legislation.

CBI

The Confederation of British Industry is the premier lobbying organization for UK businesses on national and international issues.

CFO

Our Chief Financial Officer is the board member responsible for managing the financial risks of the group.

Corporation Tax

Is tax levied on the profits of a company.

Effective tax rate

Is the tax charged as a percentage of the accounting profits.

Employment taxes

Everyone who earns income or works in the UK is typically liable to pay UK income tax and social security. This term covers all forms of employer's and employees' liabilities.

Environment Agency

Is a public body set up to protect and improve the environment.

Environmental taxes/other duties

These are designed to internalize environmental costs and provide economic incentives for people and businesses to promote ecologically sustainable activities.

Headline tax rate

The prevailing rate for UK companies (currently 19 per cent).

HMRC

Her Majesty's Revenue and Customs is a non-ministerial department of the UK Government responsible for the collection of taxes.



Ofwat

The Water Services Regulation Authority, or Ofwat, is the body responsible for economic regulation of the privatised water and sewerage industry in England and Wales.

OTS

Office of Tax Simplification, they provide advice to the UK government on simplifying the UK tax system.

R&D

Research and development is applying innovation to develop a new service/product or to improve an existing service/product.

Related entities

Means any business, partnership, limited liability company or other entity in which the company, a parent or a subsidiary holds a substantial ownership interest, directly or indirectly.

Senior Accounting Officer (SAO)

Responsible to personally certify that their companies' systems are fit for the purpose of reporting taxes.

Stakeholder

Anyone who is affected by our business in one way or another.

Statutory tax relief

This is tax relief that is required, permitted or enacted by statute and which reduces the amount of tax owed by a taxpayer.

Tax Liability

This is the total amount of tax owed by a company to HMRC.

VAT

Value Added Tax is a consumption tax placed on a product whenever value is added at each stage of the supply chain, from production to the point of sale.

VOA

Valuation Office Agency is an agency of Her Majesty's Revenue and Customs. It values properties for the purpose of Council Tax and business rates in England and Wales.

Water UK

The sector organisation that engages with companies and regulators to ensure customers receive high quality tap water at a reasonable price and that our environment is protected and improved.





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