

# **United Utilities Water Limited**

## **Annual Report and Financial Statements**

**31 March 2022**

## Strategic report

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## Strategic report

### Non-executive directors

Liam Butterworth  
Stephen Carter  
Kath Cates  
Mark Clare  
Alison Goligher  
Sir David Higgins  
Paulette Rowe  
Doug Webb

### Executive directors

Steve Mogford  
Phil Aspin  
Louise Beardmore

### Secretary

Simon Gardiner

### Auditor

KPMG LLP  
St Peter's Square  
Manchester  
M2 3AE

### Registered office

Haweswater House  
Lingley Mere Business Park  
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WA5 3LP

### Regulatory reporting:

Regulatory reporting information for the year ended 31 March 2022 is contained in the separate Annual Performance Report, which has been prepared in accordance with regulatory reporting guidelines, and will be available separately once filed with Ofwat.

### Terms used in this report:

United Utilities Water Limited's ultimate parent company is United Utilities Group PLC. 'UUG' means United Utilities Group PLC and 'United Utilities' or 'the UUG group' means United Utilities Group PLC and its subsidiary undertakings. The 'group' means United Utilities Water Limited and its subsidiary undertakings. The 'company' or 'Uuw' means United Utilities Water Limited. The 'regulated business' or 'regulated activities' means the licensed water and wastewater activities undertaken by United Utilities Water Limited in the North West of England.

### Cautionary statement:

This 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 include without limitation any projections or guidance relating to the results of operations and financial conditions of the group as well as plans and objectives for future operations, expected future revenues, financing plans, expected expenditure and any strategic initiatives relating to the group, as well as discussions of our business plan and our assumptions, expectations, objectives and resilience with respect to climate scenarios. 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.

## Strategic report

### Our purpose

**To provide great water and more for the North West.**

As the water and wastewater service provider for the North West region of England, our purpose is why we exist and it drives us to focus on what matters to our stakeholders.

**To provide great water...** This means delivering our core water, wastewater and customer services, reliably and to the highest quality. It is what our customers expect and deserve.

**and more...** This means creating value for our stakeholders by understanding what matters to them through strong and constructive relationships. We do this by:

- supporting communities to be stronger;
- caring for customers through trusted relationships;
- creating a great place to work for all our employees;
- protecting and enhancing the environment;
- delivering a sustainable return to investors; and
- innovating in partnership with suppliers.

**for the North West.** We are a part of the region we serve just as that region is a part of who we are as a business, and there are certain characteristics specific to the North West region that influence what we do.

### Our vision

**To be the best UK water and wastewater company.**

This is what motivates us to improve our services and deliver more. To achieve this vision, our strategy has three themes – the best service to customers, at the lowest sustainable cost, in a responsible manner.

### Our strategy

This is how we deliver our purpose and vision, and consists of three strategic themes.

#### **The best service to customers**

We put customers at the heart of everything we do. As well as delivering a reliable service of great tasting water and removing wastewater, we proactively keep customers informed about any work we are doing in their area and communicate with them in ways that meet their individual needs. For example, we now use 'push texts' to send updates and alerts to customers within a specified location.

The best service to customers means being available when they need to contact us, always interacting in a friendly and helpful manner, and offering tailored support and assistance for customers when they need it. As well as these day-to-day interactions, it means consulting on what matters to them. This shapes what we do; for example, we redesigned our bills based on customer research and feedback.

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### **At the lowest sustainable cost**

To run a resilient business, it is important to ensure cost reductions are sustainable so that we can keep them down without compromising on resilience or the quality of service we deliver.

When we develop our plans and assess different options, we look to minimise the whole-life cost. This fits with the total expenditure (totex) model, because the most cost-effective option can vary between traditional operating expenditure (opex) or capital expenditure (capex) solutions.

Our Systems Thinking approach helps us look holistically at all options, and operating our entire network as a system rather than discrete assets opens up new avenues that otherwise would not have been available.

### **In a responsible manner**

We will only deliver our purpose and create and maintain value for our stakeholders if we act in a responsible manner.

This means protecting and enhancing the natural environment, using natural solutions where possible, and reducing our carbon footprint and waste. It means promoting a safe, healthy and engaging workplace for our employees, supporting their physical and mental health. It drives us to support local communities on issues that matter to them, and to work with local schools and training facilities to promote skills for the future.

Above all, it means we are open, honest and transparent in our dealings and in reporting our performance.

## **Our core values and culture**

These are the fundamental values that drive our decision-making

### **Customer-focused**

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

### **Innovative**

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

### **Trustworthy**

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

### **Culture at United Utilities**

As well as our purpose, strategy and core values, we monitor our culture against key categories relating to our people, such as engagement, health and wellbeing, diversity, and development.

## Strategic report

### How we operate



**Collect** - We collect water from open reservoirs, lakes, rivers and boreholes, which we manage in a sustainable way, protecting and enhancing local habitats. We own and manage 56,000 hectares of land, which we open to the public to enjoy access to nature.

**Treat** - The water we extract needs a lot of work in one of our 88 water treatment works before it is safe and clean for customers to drink. We then store the treated water in covered reservoirs ready to be delivered to customers' taps when they need it.

**Deliver** - We maintain over 42,000 kilometres of water pipes and deliver an average of 1.8 billion litres of water each day to 7.4 million people across the North West. Our main Haweswater Aqueduct uses gravity to transfer water from Cumbria to Manchester, and our integrated supply network enables us to move water around the region.

**Remove** - Wastewater from customers' drains and rain water from roads and rooftops flows into our combined sewers to be taken for cleaning. In excessive rainfall, when sewer capacity is overloaded, storm overflows allow rain water, mixed with wastewater, to flow directly into rivers or the sea through a separate pipe to help prevent flooding of streets, homes and businesses.

**Clean** - We maintain over 78,000 kilometres of wastewater pipes to transport wastewater from sewers to one of our 566 wastewater treatment works, where it requires separation and treatment before it is returned to the natural environment.

**Generate** - We waste nothing, turning sludge byproduct into compost for farmers and capturing gas to generate renewable energy from bioresources. United Utilities self-generates around 25 per cent of its energy, helping to reduce our carbon footprint and energy costs.

**Return** - Once the water is clean enough to meet stringent environmental consents, we return it to the natural environment through rivers and streams so that the water cycle can begin again.

## Strategic report

### Our key resources (the six capitals)

#### Natural capital

We rely on natural resources to supply water and take back wastewater after treatment, as well as to generate renewable energy.

#### Human capital

We rely on skilled and engaged employees and suppliers to deliver our services, and skills must be maintained through training and development.

#### Manufactured capital

We invest to maintain and enhance our assets and build long-term resilience, and we use telemetry to monitor and control many assets remotely.

#### Financial capital

Efficient financing allows us to preserve intergenerational equity for customers while funding necessary long-term capital investment projects.

#### Social capital

The constructive relationships we have built with regulators, suppliers, and other stakeholders are fundamental to our ability to deliver our purpose.

#### Intellectual capital

Innovation helps us continually improve, and understanding performance trends in our network helps us spot potential issues early and fix them proactively.

### Our external drivers

#### Natural environment

We must be resilient to changes such as climate change and population growth, and ensure our impact on the natural environment is positive.

#### Stakeholders

Our work and the huge areas of land we manage impacts a wide variety of stakeholders and we consult them to help develop and execute our plans.

#### Technology and innovation

New technology and innovations create opportunities for improvements in service and efficiency, but can also create risks such as cyber-attacks.

#### Economic environment

The economy impacts our financing through market rate movements such as interest rates and inflation, and our customers' ability to pay their bills.

#### Regulatory environment

Environmental and drinking water standards set by our regulators drive what we do, both now and in the long term through future market reforms.

#### Political environment

This includes regional and national politicians as well as policymakers, and we must understand the key policy issues affecting our industry.

## Strategic report

### Our regulatory environment

**To provide great water and more for the North West, we must consider our economic, quality and environmental regulation and create medium and long-term plans that meet the priorities of each of our regulators.**

Most customers in England and Wales are served by one of 11 large water and wastewater companies or smaller companies providing only water services.

United Utilities Water Limited is the second largest company as measured by Regulatory Capital Value (RCV). RCV represents the net value of accumulated investment in the company's asset base. We serve over seven million people, with over three million household customers making up around two-thirds of our revenue, and over 200,000 businesses. In the non-household marketplace, we provide wholesale services to retailers.

As a monopoly provider of essential services, we are regulated by various bodies (as set out below), and we are subject to sector-specific legislation alongside this regulation.

Our regulators assess our comparative operating performance against the other water and wastewater companies in England and Wales, with the Drinking Water Inspectorate (DWI) assessing performance in water, the Environment Agency (EA) assessing performance in wastewater, and Ofwat assessing customer satisfaction. Both Ofwat's customer satisfaction assessment and the EA's annual performance assessment are included in our operational key performance indicators (KPIs).

Ofwat sets total revenues, service levels that must be provided, and the incentive package for companies for five-year periods, known as Asset Management Plan periods (AMPs).

These packages are based on Ofwat's methodology, which reflects stakeholder and customer priorities, and are confirmed following detailed scrutiny of business plans proposed by the companies. We must, therefore, engage constructively with Ofwat on future priorities and its methodology development and submit high-quality plans to help ensure we receive a determination that targets the best outcomes for us to continue creating value for customers and all our stakeholders, and effectively incentivises us to continue improving performance.

To ensure our plan is robust and balanced, we consult with customers and other stakeholders (including quality and environmental regulators) and factor in long-term planning and resilience needs.

This was the second year of AMP7, covering the 2020–25 period, and our focus has been on delivering and trying to outperform our final determination through:

- achieving higher customer satisfaction than our peers;
- beating the outcome delivery incentive (ODI) targets for operational performance;
- delivering efficient total expenditure (totex); and
- raising debt finance at a cost below the industry allowed cost of debt.

Our vision is to be the best UK water and wastewater company, so we regularly benchmark our performance against our peers, and we benchmark our customer service performance against other leading service providers in our region.

Since privatisation, the water industry has invested a significant amount, contributing to improvements in public health and environmental standards, better quality of services, and superior quality drinking water. In its final determinations for AMP7, Ofwat allowed a further £51 billion across the industry to deliver further improvements, and since this, Ofwat has allowed a further £2.7 billion for green economic recovery.

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### Our regulators

We are subject to regulation of our price and performance by economic, quality and environmental regulators, as shown in the diagram.



\* RAPID is a partnership made up of Ofwat, the Environment Agency and DWI.

These bodies exist to help protect the interests of customers and the environment, but they can have competing interests. For example, in agreeing environmental improvements and over what time frame these will be delivered, we must consider how much it will cost and the need to protect customers from bill shocks. Balancing these interests requires open and continuous dialogue.

The regulatory framework can change significantly in the long term and we have seen substantial tightening of laws and regulations since privatisation.

While much is outside our direct control, maintaining good relationships enables us to engage positively with regulators to influence future policy, aiming to achieve the best outcome for all our stakeholders.

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### The North West

**Our purpose is singularly focused on the North West, and what we do is influenced by several key factors that make our region unique. We are committed to understanding and actively responding to these.**

#### Economic factors

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

- 7.4 million population expected to grow significantly in the next 25 years
- 22,700 jobs actively supported by our work, with over 5,000 direct employees
- Tourism relied on by the Lake District, Manchester, Liverpool and coastal areas

#### Social factors

We are leading the sector on supporting customers with affordability and vulnerability.

- 54 per cent of the most deprived areas in the country
- 47 per cent of households have less than £100 savings to cope with unexpected bills
- 12 per cent of households are affected by water poverty, more than 50 per cent higher than the national average

#### Environmental factors

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

- 30 per cent of land is National Park or Area of Outstanding Natural Beauty or Sites of Special Scientific Interest
- 25 designated coastal bathing waters
- 830mm rainfall each year, higher than the UK average

## Strategic report

### Engaging with our stakeholders

**We actively engage with stakeholders to understand what matters most to them through strong and constructive relationships.**

To create longer-term value for all it is essential that we identify and engage with our stakeholders to understand what matters most to them.

We do not operate in isolation and it is not for us alone to determine what the region needs us to deliver. Engaging with stakeholders across the North West enables us to identify shared solutions to shared challenges. We value the diverse perspectives that a broad range of stakeholders, representing different and often competing interests, can bring to our decision-making.

Understanding what matters to stakeholders will only be achieved by building strong, constructive relationships and engaging regularly. This is important to building and maintaining trust. These relationships are subject to robust governance to ensure the insights generated are taken into account in decision-making at executive and board level. The board’s corporate responsibility committee meets four times a year, with stakeholder engagement as one of its standing agenda items, and the chair of the independent customer challenge group (YourVoice) attends board meetings to provide its perspective.

Pages 30 to 32 of our United Utilities Group PLC annual report and financial statements detail how we engage with, and are influenced by, each of our key stakeholder groups. Our analysis of what matters most to stakeholders, and how these issues affect our ability to create long-term value, is set out in our material issues matrix on page 12.

As shown below, there are nine key stakeholder groups that influence our planning and activities, and six of these groups benefit from the value we create. Our approach to engagement extends across all of these stakeholders.



## Strategic report

### What matters most to our stakeholders

We continuously challenge ourselves to make sure we understand what matters most regarding our role in society, the impact that we have and the value we create.

### Our materiality assessment process

1. **Define** - We reviewed current best practice in materiality reporting. The assessment criteria for stakeholder interest and our ability to create value was confirmed. Building on our existing matrix we brought in more stakeholder views and evolved the matrix design. We committed to provide more detailed commentary on the most material issues.
2. **Engage** - Views were obtained from across all our stakeholder groups. Insight from consultations and data was made available through the engagement processes described on pages 30 to 32 of the United Utilities Group PLC Annual Report and Financial Statements. Key internal subject matter experts and stakeholder relationship managers provided further insight on issues.
3. **Assess** - Comments and data were drawn together to form an initial view of the issues. The rationale for issue selection and its significance was presented to senior management for discussion. This included potential new issues, removal of issues and movement of existing issues.
4. **Align** - We cross-referenced and aligned identified issues with our principal risks and uncertainties, as set out on pages 50 to 73. Matrix visuals were then created to easily communicate the prioritisation of issues. For the first time an indication of how issues have moved since the previous review has been included.

### Our approach to materiality

Understanding what matters most to our stakeholders is fundamental to being a purpose-driven organisation. 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.

This stakeholder materiality assessment informs decisions about what we report in documents such as the group's 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 and employees) and there can be external value (for customers, communities, investors, suppliers and the environment). Value may be financial or non-financial.

### Our 2021/22 assessment

This year we carried out a thorough review of our material issues and matrix design.

Striking the right balance between different interests and views is not easy but our assessment process consolidated feedback based on a balance of views obtained from all our stakeholders.

The assessment process identified 28 material issues. More information about the most material issues can be found on pages 36 to 39 of the United Utilities Group PLC Annual Report and Financial Statements, where we describe the issue, provide our response to managing the issue, explain how the issue links to our strategic themes and how it is included in our plans for the future.

Issues are plotted on the matrix from lower to higher in terms of level of interest to stakeholders and how much it can affect our ability to create value.

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Our approach has been reviewed by responsible business consultancy Corporate Citizenship, which commented that “United Utilities has set out the orderly, balanced and comprehensive process by which it has arrived at its refreshed materiality assessment. The detailed coverage of the six most material issues fosters public understanding. It sets out the links to strategic themes, risks and future actions. It shows how United Utilities recognises the most important issues and acts upon them”.

## Material issues matrix



Material issue	Movement relative to previous review	Material issue	Movement relative to previous review
1 Trust, transparency and legitimacy	=	15 Health, safety and wellbeing	↗
2 Resilience	=	16 North West regional economy	=
3 Customer service and operational performance	=	17 Land management, access and recreation	↗
4 Climate change	↗	18 Sewage sludge to land	N
5 Political and regulatory environment	=	19 Energy management	=
6 Affordability and vulnerability	=	20 Environmental impacts	=
7 Drinking water quality	N	21 Data security	=
8 Sewer flooding and storm overflows	↗	22 Diverse and skilled workforce	↗
9 Water resources and leakage	↘	23 Responsible supply chain	=
10 Financial risk management	=	24 Employee engagement	↗
11 Corporate governance and business conduct	=	25 Supporting communities	↗
12 Nature capital and biodiversity	=	26 Competitive markets	=
13 Innovation	=	27 COVID-19	↘
14 Cyber security	=	28 Human rights	=

## Strategic report

### S172(1) Statement

#### Our key decisions during the year to 31 March 2022.

Throughout the United Utilities Group PLC Annual Report and Financial Statements, we provide examples of how we have thought about the likely consequences of long-term decisions and how we:

- build relationships with stakeholders and balance their needs and expectations with those of the business;
- 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;
- are mindful of the interactions we have with our regulators; and
- understand the importance of behaving responsibly and being consistent with the company's purpose, vision and values.

#### 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 and having regard (amongst other matters) to factors (a) to (f) s172 Companies Act 2006, in the decisions taken during the year ended 31 March 2022 including:

#### Haweswater Aqueduct Resilience Programme

##### The decision

In December 2021, the board agreed delivery of the replacement of six of the existing tunnel sections of the Haweswater Aqueduct (the aqueduct) and connections to existing multiline siphons between the tunnel sections and associated facilities had the potential to be delivered as a Direct Procurement for Customers (DPC) project rather than through the traditional UUW procurement route. Under DPC the CAP<sup>1</sup> will be responsible for the detailed design and build of the project and, crucially, for securing the project finance. The CAP will also be responsible for maintaining and inspecting the new tunnels for a period of 25 years post construction. In November 2020, the replacement of the Hallbank section of the aqueduct was successfully completed by UUW, which was delivered via a traditional approach working with a design and build contractor.

##### How we engaged with stakeholders

Our regulator, Ofwat, has introduced the new DPC approach for companies to consider when delivering large infrastructure projects. (More information on the DPC approach can be found on Ofwat's website.) Ofwat 'believe that by outsourcing the delivery of infrastructure projects using DPC, water companies can achieve significant benefits for customers. This includes both through innovation and lower whole life costs of the project'. The company has been working with Ofwat on developing the detail of the DPC approach for this complex project since proposing the delivery of HARP via DPC in its AMP7 business plan.

In developing this project, we have sought customers' views and worked with their representatives through YourVoice to develop a solution to balance risk reduction and the cost of delivery. We have

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<sup>1</sup> CAP means a limited company which has been competitively appointed to be the provider in accordance with a DPC Procurement Process in respect of a DPC Delivered Project

## Strategic report

completed initial design work and submitted all planning applications taking into account impacts on local communities and the environment, and have sought to minimise this as much as possible. We have actively engaged stakeholders through the planning process, undertaking extensive public engagement including an innovative ‘virtual public exhibition’ when face-to-face interactions were restricted due to the pandemic. We have also completed environmental impact assessments and are seeking a ten per cent biodiversity net gain from the project.

Read more at [ofwat.gov.uk/regulated-companies/markets/directprocurement/direct-procurement-forcustomers/](https://ofwat.gov.uk/regulated-companies/markets/directprocurement/direct-procurement-forcustomers/)

### The board’s view

The aqueduct is a critical asset in being able to deliver our purpose to provide great water and more for the North West. It is a major part of our water supply network serving our customers in parts of Cumbria, Lancashire and Greater Manchester. The board does not underestimate the complexities of the project to replace six sections of tunnel in some remote stretches of countryside and with sections of the tunnel at a depth of up to 370 metres. As well as the technical challenges, the complexities of the new and untested DPC approach have added to the challenge of a project estimated to require investment of over £1 billion and take circa 9–10 years to complete.

The board has been kept fully apprised of progress at key stages of the project through regular presentations at board meetings, ‘deep-dive’ sessions and as part of strategy discussions.

The board approved the submission of the Outline Business Case to Ofwat under DPC having evaluated and considered the DPC approach and identified, and sought to mitigate as far as possible, the known and likely risks associated with the DPC approach. The board is cognisant of the many challenges ahead including amongst other things: the appointment of the CAP through a new DPC tender process, the implications for the group of the different commercial construct and financing of the project, and the critical nature of the aqueduct to the business.

Under the current circumstances, the board considers that the DPC delivery approach has the potential to be most likely to promote the long-term success of the company for the benefit of its members as a whole. This is based on the information currently available, which suggests that the DPC route has the potential to offer the best value for customers and, therefore, supports the position that this should be tested through the market through progressing HARP through a DPC procurement process.

In April 2022, Ofwat gave its consent for UUW to procure HARP through a DPC procurement process under Condition U of its licence.

### Hybrid working

#### The decision

The COVID-19 pandemic has changed the world of work. United Utilities is an organisation where, pre-pandemic, the majority of our employees routinely travelled to work on a daily basis to attend one of the group’s offices or sites. As the pandemic progressed, the need to evolve our ways of working to face the future became evident. The board was fully involved in the development of the group’s next ways of working, including the pilot project prior to rolling out the hybrid way of working for roles which fulfilled specific criteria within the organisation.

#### How we engaged with stakeholders

Weekly online webinars were established during the early stages of the pandemic in order to communicate with line managers prior to the cascade of information to their teams, and with these resources being made available to all employees via the intranet. Our Employee Voice panel has been a valuable mechanism for employees to provide feedback, particularly on how they felt they have been supported during the pandemic. Over 1,000 employees, including those based out in the field or at one of our many operational sites, provided their views, which were taken into account when formulating the

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plans for our next ways of working. Feedback from the teams involved in the pilot project have helped shape our current approach to hybrid working.

### The board's view

Our employees are fundamental to fulfilling our purpose of providing great water and more for the North West. We have seen a number of positive benefits relating to work during the pandemic including: reductions in employee sickness absences; improvements in engagement and wellbeing; improvements in operational performance; and reduced travel costs and carbon emissions. Increased hybrid working provides opportunities including: the ability to attract employees from a wider and potentially more diverse talent pool; being the catalyst to improve our digital capabilities and in time shape the workplace of the future; and potentially make savings on accommodation.

Our plans have seen 2,000 employees adopting hybrid ways of working. In terms of the non-hybrid roles which are typically directly supporting our customers and critical operations, we are continuing to look at providing additional flexible opportunities and changing workplace practices to retain, attract and stay aligned to the employment market. The board concluded that the incorporation of a hybrid way of working alongside the traditional approach would be most likely to promote the long-term success of the company for the benefit of its members as a whole. This way of working will be monitored closely to ensure it remains efficient and effective.

## River health

### The decision

The group has committed to deliver £230 million in environmental improvements within our base capital programme, supporting at least a one-third sustainable reduction in the number of spills recorded from our storm overflows by 2025 compared to the 2020 baseline, leading to 184 kilometres of improved waterways across the region.

### How we engaged with stakeholders

There has been much negative press coverage regarding river health and bathing water quality aimed primarily at the wastewater sector, with the Environment Agency (EA) and Ofwat currently investigating whether wastewater companies' treatment works have been operated in line with their environmental permits. We have written to all our stakeholders including the EA, Ofwat, The Consumer Council for Water and MPs in our region. We announced that we would be launching a community fund to support local rivers initiatives, work alongside The Rivers Trust, RSPB and local authorities to deliver projects, and launch a new partnership to protect watercourses with farmers to incentivise farming practices that reduce impact to river health.

### The board's view

The group has co-operated fully with the EA/Ofwat investigation. The board is cognisant that United Utilities needs to do more to play its part in improving river health in the North West, and amongst other things, we will:

- aim to publish investigations and plans for all overflows that operate frequently;
- ensure all storm overflows are monitored by 2023;
- aim to provide near real-time data when an overflow operates and ensure this data is easily accessible by 2023;
- aim to deliver a significant reduction in impact caused by storm overflows and sewage treatment works by 2030; and
- aim for there to be no serious pollution incidents from our assets.

The board, in committing to playing its part in improving river health, believes this would be most likely to promote the long-term success of the company for the benefit of its members as a whole.

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### Non-financial information statement

The table below constitutes the company's non-financial information statement, produced to comply with sections 414CA(1) and 414CB(1) of the Companies Act 2006. Our purpose-driven approach, as described on pages 3 to 4, sets out how we act as a responsible business and is applicable to the areas of disclosure required by s414CB(1). The performance tables we publish for each stakeholder that we create value for, so that we can demonstrate we are fulfilling our purpose (see pages 52 to 75 of the United Utilities Group PLC Annual Report and Financial Statements), include data in relation to the areas of disclosure required by s414CB(1).

Read more about our purpose on our website at: [unitedutilities.com/corporate/about-us/what-we-do/our-vision](https://unitedutilities.com/corporate/about-us/what-we-do/our-vision)

The composition of the U UW Board mirrors that of the UUG Board and therefore the non-financial information statement should be read in conjunction with the UUG 2022 Annual report and financial statements. Page references in the below table are to the relevant areas of the UUG Annual report and financial statements, with much of the information also incorporated within the U UW Annual report and financial statements.

Reporting requirement	Information necessary to understand our business and its impact; policies and due diligence activities; and outcomes	Policies, guidance and standards which govern our approach (some of which are only published internally)
<b>Environmental matters</b>	Reflecting the needs of the environment: <ul style="list-style-type: none"> <li>• Natural resources – see page 24</li> <li>• Natural environment – see pages 26 and 31</li> <li>• Reducing our carbon footprint – see pages 86 to 97</li> </ul>	<ul style="list-style-type: none"> <li>• Waste and resource use policy</li> <li>• Environmental policy – see the responsibility pages on our website</li> <li>• Water Resources Management Plan – see page 48</li> <li>• Emissions target – see pages 86 to 97</li> </ul>
<b>Employees</b>	Reflecting the needs of our employees: <ul style="list-style-type: none"> <li>• Health and safety – see page 62</li> <li>• Mental wellbeing – see pages 61 to 62</li> <li>• Competitive base salaries and benefits – see page 183</li> <li>• Gender pay report 2021 – see page 44</li> <li>• Engagement – see pages 7, 30, 60 to 62 and 196</li> <li>• Board diversity – see pages 133 to 134</li> </ul>	<ul style="list-style-type: none"> <li>• Health and safety policy</li> <li>• Mental wellbeing policy</li> <li>• Equality, diversity and inclusion policy</li> <li>• Flexible working arrangements</li> <li>• Agency worker policy</li> <li>• Human rights policy – see page 36</li> <li>• Board diversity policy – see pages 133 to 134</li> </ul>
<b>Respect for human rights</b>	Reflecting the needs of our stakeholders: <ul style="list-style-type: none"> <li>• Suppliers – see page 31</li> <li>• Diversity within our workforce – see pages 7, 44 to 45, 60 to 63, 133 to 134, and 137 to 138</li> </ul>	<ul style="list-style-type: none"> <li>• Employee data protection policy</li> <li>• Slavery and human trafficking statement</li> <li>• Human rights policy – see page 36</li> </ul>
<b>Social matters</b>	Reflecting the needs of our stakeholders: <ul style="list-style-type: none"> <li>• Customers – see page 30</li> <li>• Communities – see page 30</li> <li>• Environment – see pages 31 and 86</li> <li>• Suppliers – see page 31</li> <li>• Regulators – see page 32</li> </ul>	<ul style="list-style-type: none"> <li>• YourVoice – see page 29</li> <li>• Charitable matched funding guidance</li> <li>• Volunteering policy</li> <li>• United Supply Chain – see pages 36 and 73</li> <li>• Commercial procurement policy</li> </ul>
<b>Anti-corruption and anti-bribery</b>	Reflecting the needs of employees and suppliers: <ul style="list-style-type: none"> <li>• Employees – see pages 61 and 154</li> <li>• Suppliers – see page 73</li> </ul>	<ul style="list-style-type: none"> <li>• Anti-bribery policy</li> <li>• Fraud investigation and reporting processes</li> <li>• Whistleblowing policy</li> <li>• Internal financial control processes</li> <li>• Commercial procurement policy</li> </ul>

## Strategic report

### Our approach

#### Systems Thinking

Our Systems Thinking approach enables us to better manage our end-to-end water and wastewater systems, optimising our decision-making and helping us move away from the traditional reactive approach to address problems proactively before they affect customers. This creates long-term value, improving our asset reliability and resilience, reducing unplanned service interruptions, and delivering cost savings.

We assess new opportunities against five capability maturity levels. At the lower levels there is a high degree of human intervention and reactive behaviour. At the higher levels there is a high degree of predictive analytics, use of artificial intelligence to process vast amounts of data, joined up decision-making across the system, and higher levels of automation. It requires time and investment to reach the higher levels, and we are at different levels in different areas of our business as we continue to embed and progress our approach.

Systems Thinking involves looking at the entire system and all of its linkages, rather than individual assets or sites in isolation, to find the best all-round solutions. Our digital backbone sends vast amounts of real-time data to our Integrated Control Centre (ICC), from which we plan, monitor and control our operations. We also factor in other source data such as weather forecasts and customer demand, and at the higher capability maturity levels we use artificial intelligence and machine-learning to identify trends and anomalies that could signal potential issues.

#### Diversity and inclusion

We want our workforce to reflect the communities we serve by reaching and recruiting from every part of our community, and we want all employees to feel valued and included, regardless of their gender, age, race, disability, sexuality or social background.

Our customer services and people director sponsors our overall diversity and inclusion plan and tracks its progress with the executive team. We have completed a further maturity audit with our specialist inclusion partner, the Clear Company, who has independently measured progress against our plans and recognised our strong focus on education.

We again ranked in the top 1 per cent of over 850 companies across Europe in the Financial Times' Statista Survey for Diversity and Inclusion Leadership, and were the leading utility company in the Top 50 Inclusive UK Employers Index. We have been included in the Bloomberg Gender Equality Index 2022, showing our commitment to more equal and inclusive workplaces.

More information on diversity and inclusion across the business can be found on pages 44 and 45 of the United Utilities Group PLC Annual Report and Financial Statements.

## Strategic report

### How we plan for the future

**Our approach and long, medium and short-term planning horizons help us continue fulfilling our purpose in a sustainable and resilient way.**

We take an integrated approach to everything we do. To help us create and prioritise our plans, we consider:

- what the material issues are, both in terms of the level of interest to stakeholders and the effect they may have on our ability to create value;
- our assessment of principal risks and uncertainties;
- our environmental, social and governance (ESG) commitments; and
- how our plans will fit with our Systems Thinking approach.

We undertake planning for long, medium and short-term horizons.

Long-term (25+ years) planning helps us identify what we need to do to address challenges and opportunities that may arise, building resilience so that we can ensure we are able to provide our essential services to customers far into the future.

These long-term plans influence our medium-term (five to ten years) planning, which sets out how we will deliver the commitments of our final determination for each regulatory period, as well as our non-regulatory activities.

Short-term (one year) planning enables us to monitor and measure progress against our five-year plans and regulatory targets. We retain flexibility in our one-year plans to meet our five-year targets in the most effective and efficient way as circumstances change.



#### Long-term planning (25+ years)

Our approach to long-term planning ensures we are responding to challenges and opportunities that may arise far into the future.

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.

## Strategic report

This involves looking at a lot of current and predictive data from various sources, such as economic forecasts, expectations for population growth, climate and weather predictions, legal and regulatory consultations and changes, as well as the age and condition of our assets, and keeping track of innovations and technological advancements. We review this information as part of our long-term planning and risk management processes.

Over the next 25+ years we have identified many challenges and opportunities that we are likely to be faced with, including:

- Climate change;
- Population growth;
- A more open, competitive market;
- Water trading;
- More stringent environmental regulations;
- Developments in technology; and
- Combining affordable bills with a modern, responsive service.

There is a section of our website dealing with our future plans, where we examine these challenges and how we will focus our resources and talents to meet them.

Our 25-year Water Resources Management Plan (WRMP) covering the 2020–45 period, was developed and published in 2019 following consultation with stakeholders. We will publish our new WRMP in 2024 covering the next period.

Our last Drought Plan was published in 2018. We have a new draft on which we have consulted with stakeholders, and the final plan will be made available on our website once approved by Defra and the Environment Agency.

We will publish a Drainage and Wastewater Management Plan (DWMP) for the first time in 2024, and more information will be made available on our website as we launch this.

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, the actions we will take to manage the risk of a drought, and the risks around flooding, pollution, storm overflows, and wastewater treatment.

We create long-term value for stakeholders by:

- Systems Thinking and innovation;
- long-term planning and responding to challenges and opportunities;
- 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.

Read more at: [unitedutilities.com/corporate/about-us/our-future-plans](https://unitedutilities.com/corporate/about-us/our-future-plans)

## Strategic report

### Medium-term planning (5-10 years)

Our medium-term planning aligns with delivery of our plans as set out in Ofwat's final determination.

The majority of the group's activities sit within our regulated water and wastewater business, therefore, our medium-term planning predominantly sets out how we will deliver against the final determination (FD) we receive from Ofwat for each five-year period. Historically, we have submitted business plans which were focused mainly on the subsequent five-year asset management plan (AMP) period, while providing a high level view of the following AMP. This provided medium-term planning visibility of between five and ten years at any one point in time, although Ofwat is proposing a longer-term planning approach for the next business plan submission in 2023.

It is important that our plans deliver for all stakeholders including customer preferences and environmental requirements. We, therefore, align our plans to these priorities in line with key published methodologies in order to deliver the best overall approach to stakeholder value.

Our business plans are designed to help us work towards our long-term plans, build and maintain resilience, and ultimately fulfil our purpose. We engage in extensive research to ensure the plans we put forward are robust and balanced, targeting the best overall outcomes for all our stakeholders.

Following scrutiny and challenge from Ofwat, we receive the final determination (FD), which sets the price (in terms of total expenditure and customer bills), level of service, and incentive package that we must deliver over the five-year period, and an allowed return we can earn.

Our business plan submission for 2020–25 was awarded fast-track status by Ofwat and we were given one of the lowest cost challenges in the sector, reflecting the efficient total expenditure (totex) proposals we put forward.

The acceleration of our capital programme during the 2015–20 period helped us deliver improvements early and we are adopting the same strategy in this regulatory period, with around £500 million of total expenditure brought forward over the first three years of the AMP, helping us make a strong start to our 2020–25 plans.

Our total expenditure for this period will be extended by £765 million beyond the scope of the FD, with this investment delivering improvements in environmental performance, accelerating delivery of the new Environment Act, and providing an enhanced level of service that will deliver better performance against customer outcome delivery incentives (ODIs).

Our strategy helps us create value for our stakeholders by delivering or outperforming the FD. Since 2015, 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 comprises the base allowed return and any out/underperformance, on an annual and cumulative basis for each AMP.

Our APR is published in July each year at: [unitedutilities.com/corporate/about-us/performance/annual-performancereport](https://unitedutilities.com/corporate/about-us/performance/annual-performancereport)

Information on companies' regulatory performance can be found at: [discoverwater.co.uk](https://discoverwater.co.uk)

### Short-term planning (1 year)

In the short term we set annual, measurable targets, but we retain flexibility to enable us to respond to challenges that may arise.

Short-term planning helps us work towards our medium and long-term goals and provides us with measurable targets so that we can continually monitor and assess our progress, which helps us ensure the long-term resilience and sustainability of our business.

## Strategic report

Before the start of each financial year, which runs from 1 April to 31 March, we develop a business plan for that year, and this is reviewed and approved by the board. This business plan 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 our five-year and longer-term goals.

Performance against these annual targets determines the annual bonus percentage that is awarded. Executive directors and employees right through the organisation are remunerated against these same bonus targets.

As well as these annual bonus targets, in order to avoid encouragement of short-term decision-making and ensure management is focused on the long-term performance of the company, executive directors are remunerated through long-term incentive plans (LTP). The LTP assesses three-year performance, and is measured during the 2020–25 period through RoRE and a basket of customer measures.

See details of the annual bonus and Long Term Plan arrangements on pages 178 to 182 of the United Utilities Group PLC Annual Report and Financial Statements.

The executive directors hold quarterly business review meetings with senior managers across the business to monitor and assess 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.

The challenges presented by COVID-19 were a clear example of why this flexibility is crucial. We enacted our robust contingency plans, enabling us to quickly and efficiently move thousands of our people to home working and introduce additional safeguarding measures for those that remained on sites or in the field, while maintaining reliable water and wastewater services that were especially critical for public health at this time.

## Strategic report

### How we measure our performance

To measure progress on delivering our purpose and creating value for our stakeholders, we monitor and measure our performance against each of the stakeholder groups that we create value for.

#### Our key performance indicators

We measure our performance against a selection of key performance indicators (KPIs), both operational and financial. These are unchanged from last year.

Bonuses (for executive directors and employees right through the business) and long-term incentives for executive directors, are closely aligned to many of our operational and financial KPIs.

**Operational KPIs** - Our purpose drives us to create long-term value for all our stakeholders, and we report against one operational KPI for each of the six stakeholders for whom we create value. More detail on these operational KPIs, including our targets and performance this year, can be seen on page 27.

**Financial KPIs** - We have selected financial KPIs that assess both profitability and sustainability of our business from a financial perspective. These are monitored and measured at the UUG level.

More detail on these financial KPIs, including our targets and performance this year, can be seen on pages 10 to 11 of the UUG Annual report and financial statements.

#### Our other performance indicators

Our KPIs are by no means the only metrics by which we monitor and assess our performance. We report against many other metrics both internally and externally. As discussed on pages 29 to 33 of the UUG Annual Report and Financial Statements, our stakeholder engagement gives us a view of what matters most to them. We report on a selection of other metrics on pages 52 to 75 of the UUG Annual Report and Financial Statements, based on the measures shown to be of highest interest to our stakeholders.

For example, on performance for customers, our KPI is Ofwat's measure of customer experience, C-MeX, but we also report on Ofwat's measure of developer satisfaction, D-MeX, the level of customer complaints, vulnerability support, customers lifted out of water poverty, and the impact of water efficiency measures.

We regularly report on numerous corporate responsibility performance measures on our external website as detailed on page 50 of the UUG Annual Report and Financial Statements.

All these performance indicators have received an appropriate level of assurance, such as independent third-party verification, regulatory reporting assurance processes, or through our own internal audit team.

#### Our Annual Performance Report (APR)

Performance against our regulatory contract is monitored and assessed each year, and reported within the annual performance report (APR), as required by our economic regulator Ofwat.

We cover several regulatory performance measures within this report. Our APR provides more details, as well as further narrative, about our regulatory performance during the year.

There is financial information contained within the APR. This relates only to the regulated company and its appointed activities, and is calculated in accordance with the regulatory accounting framework. This differs from IFRS reporting, and a reconciliation to IFRS reporting is provided in the APR.

Our APRs for previous years are available on our external website, at: [unitedutilities.com/corporate/about-us/performance/annualperformance-report](https://unitedutilities.com/corporate/about-us/performance/annualperformance-report) and the APR for 2021/22 will be published in July 2022.

## Strategic report

### Operational performance

We are helping over 200,000 households currently struggling with their bills, and maintaining a high level of service for customers. We are earning higher outperformance thanks to strong operational performance against customer outcome delivery incentives as well as financial outperformance. As a responsible company we are sharing our success with customers, like we did in 2010-20, by investing an additional £765 million to help accelerate further enhancements for customers and the environment.

Our team has sustained a strong level of operational performance this year, delivering value for all our stakeholders. Customer satisfaction and employee engagement remain high, and we have achieved our best ever performance against customer outcome delivery incentives (ODIs). We are on track to deliver our AMP7 environmental improvement programme, which will improve river and bathing water quality in the North West, and have made good progress against our carbon pledges. We are upper quartile across a suite of environmental, social and governance (ESG) indices, and our robust balance sheet provides long-term financial resilience.

#### Helping customers struggling with bills

Many people across the country are facing real challenges as we emerge from a global pandemic and are faced with significant rises in the cost of living. We serve many of the most deprived areas in England and Wales, so it is more important than ever that we are doing what we can to help customers.

Our average household bill for 2022/23 is not increasing, and we are offering more support than ever before through our extensive range of affordability and vulnerability schemes, helping over 200,000 households this year and providing around £280 million<sup>2</sup> of affordability support over AMP7.

There is still more we would like to be able to do, and we are a passionate supporter of the Consumer Council for Water's drive to introduce a national social tariff, which would help deliver a more equitable sharing of support for customers struggling to pay their bill regardless of where they live in the country.

#### Sustained high levels of operational and environmental performance

We were a sector leading company on outcome delivery in Ofwat's Service Delivery Report for 2020/21, with nine of 11 outcomes<sup>3</sup> being at or better than target, and were recognised as a top performer on supply interruptions and pollution incidents – two areas where we are now seeing the benefits of targeted investment we made in AMP6. On the two outcomes where our performance was below target we have plans in place to improve this.

Our customer ODI performance has been strong across the board this year, meeting or beating over 80 per cent of our performance commitments. Based on our anticipated reward this year, we will have earned rewards in both the first two years of AMP7 against Ofwat's customer satisfaction measure, C-MeX, and we have achieved our lowest ever level of written complaints this year.

We were pleased to achieve a four star rating in the 2020 Environmental Performance Assessment from the Environment Agency (EA), meaning we were categorised as an industry leading company in the most recent annual assessment by the EA, taking into account performance across a broad range of environmental metrics. It reflected our best ever performance, and we were the first water company to achieve green status across all measures since 2015.

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<sup>2</sup> 50 per cent company funded

<sup>3</sup> Excluding per capita consumption, which Ofwat will be revisiting at the next price review once there is a better understanding of the impact of COVID 19 and any enduring effects

## Strategic report

We continue to be at the sector frontier on pollution performance, having reduced overall pollution by a third since the start of the AMP. Our treatment works compliance remains strong and we expect to remain green on this measure in the EA's assessment for 2021.

### Performance improvements earning outperformance

We earned a reported return on regulated equity (RoRE) of 7.9 per cent<sup>4</sup> for 2021/22, driven by our continued improvements in operational performance together with high levels of inflation, which increases financing outperformance, and tax outperformance. Underlying RoRE is slightly lower at 7.7 per cent, and excludes the tax that will be recovered through the regulatory sharing mechanism. Cumulative RoRE for the first two years of AMP7 is 6.2 per cent on both a reported and underlying basis.

Our strong performance this year earned a £25 million<sup>5</sup> reward against customer ODIs, the highest annual reward we have achieved to date. We anticipate earning total customer ODI rewards over AMP7 of £200 million, a third higher than we estimated in last year's report.

We consistently issue debt at efficient rates, and we earned financing outperformance of 1.6 per cent of regulated equity this year. We also performed strongly on tax as a result of optimising government tax incentives.

The economic environment as we emerge from a global pandemic, as well as the war in Ukraine, has driven higher costs in our supply chain and we are starting to see significant cost increases in power and chemicals. We continue to seek efficiencies and exploit technology and innovation to help us deliver our total expenditure (totex) efficiently.

### Sharing our success with customers

As a responsible company it is right that we should share our success with customers, and we feel the best way for us to create more value for customers and other stakeholders is through investing to accelerate improvements in performance. This is in line with the approach we have taken historically, sharing over £600 million over the 2010-20 period.

We have increased the investment we are making by a further £400 million meaning that, over the 2020–25 period, we are investing £765 million beyond the scope of our final determination allowance to help us accelerate environmental and customer outcomes.

### Investing to improve service for customers

£250 million of the additional investment is helping us deliver further improvements to service for customers and better performance against our customer ODIs.

As mentioned above, our performance has been strong across the majority of our customer outcomes, but this investment is targeted at delivering sustainable improvements for customers in two specific areas where we want to do better – sewer flooding and water quality (specifically discolouration).

It includes investment in Dynamic Network Management (DNM), an advancement of Systems Thinking in our wastewater network that will help us reduce sewer flooding and pollution incidents using real-time performance data from a network of sensors to enable predictive and preventative optimisation.

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<sup>4</sup> On a real, RPI/CPIH blended basis

<sup>5</sup> Excluding per capita consumption, which Ofwat will be revisiting at the next price review once there is a better understanding of the impact of COVID 19 and any enduring effects

## Strategic report

### Investing outperformance for environmental improvements

A further £250 million of the additional investment is being used to deliver environmental outcomes. This includes delivering elements of the new Environment Act requirements earlier, and improving the health of rivers across the North West.

In July 2021, we launched a collaborative partnership with The Rivers Trust, a first for any water company in the United Kingdom. To help kickstart a river revival in the North West we published 'Better Rivers: Better North West', our plan to improve the health of rivers across our region in the next three years. We are delivering improvements that support at least a one-third sustainable reduction in the number of spills recorded from our storm overflows between 2020 and 2025, with all storm overflows monitored by 2023 and real time data on their operation made publicly available. Our plans will lead to 184 kilometres of improved waterways across the region. We also continue to engage with the ongoing industry-wide investigations by Ofwat and the Environment Agency into possible unpermitted sewage discharges.

The remaining £265 million of the £765 million of additional investment is for projects where regulatory allowances and mechanisms have been secured, much of which will deliver further environmental benefits. For example, around £90 million will fund a project in Bolton that is part of our Water Industry National Environment Programme (WINEP), and £65 million will go towards supporting the country's green economic recovery in the wake of the pandemic.

### Long-term investment needs for the environment

Protecting and enhancing the natural environment has always been a key priority for us and many of our stakeholders. In the last 12 months this has received increased public interest, particularly the health of rivers and the part the water industry can play in helping to improve this.

New and emerging requirements reflect the increased importance being given by the Government to the environmental agenda and we share the Government's ambitious improvement plans.

The Environment Act 2021 introduces several new challenges for the sector, including a requirement for water companies to secure a progressive but very substantial reduction in the average number of spills from storm overflows, and controlling nutrient pollution by reducing phosphate release from wastewater treatment works. The Industrial Emissions Directive broadens the scope of activities covered by compliance requirements, and the Environment Agency's recent interpretation of Farming Rules for Water restricts the application of biosolids to land in certain areas at certain times, requiring more storage capacity or alternative means of disposal.

We have delivered significant improvements in environmental performance in recent years, and through our original plans for AMP7 we will deliver further improvements, with good progress already having been made. The additional investment we are making will help accelerate improvements, but there is more that the industry will need to do.

Specific targets for the next regulatory period have not yet been agreed, but it is already clear that there is an ambition to deliver a fundamental change in the way drainage network systems were originally configured. The investment needed to deliver these changes will be significant for the industry as a whole, but particularly for the North West, where we have a much higher proportion of combined sewers. We are working with the Government and regulators to determine how these bold ambitions can be met and by when, recognising that the pace of change must consider customer affordability.

Resilience to climate change and population growth remains a material issue for many stakeholders, even more so since COP26, and this is something that will need to be addressed by water companies both regionally and nationally. Our Systems Thinking approach and investment are helping to deliver increased resilience across the North West, and longer-term we are involved in strategic planning for a national water transfer scheme.

## Strategic report

We have committed to achieve net zero by 2030 with six pledges to reduce our carbon footprint, underpinned by ambitious science-based targets for reducing our greenhouse gas emissions, and we are making good progress against these. We are linking executive remuneration more tightly to our carbon commitments with four targets added to the Long Term Plan, and in this year's report we also include nature-related financial disclosures.

### **Haweswater Aqueduct Resilience Programme (HARP)**

We have continued to develop HARP, an industry-first Direct Procurement for Customers (DPC) programme to design and build six replacement tunnel sections of the Haweswater Aqueduct, which transports water from Cumbria to Manchester.

We have undertaken extensive market engagement throughout the process – challenging for a project of this scale during the pandemic – and used innovative ways to manage stakeholder engagement including the use of digital channels and a virtual exhibition giving people access to information and the ability to ask questions remotely.

We developed the initial design following extensive ground investigation work to plot the best route, and planning applications have all been submitted with decisions expected later this year. During early 2022, we have been finalising tender documents, and we expect to start procurement in the summer of 2022.

### **Supported by a diverse and highly motivated workforce**

We pride ourselves on being a quality employer, and are committed to maintaining a diverse and inclusive team of people, recruiting from every part of our community. We scored equal to the UK high performance norm with 87 per cent employee engagement this year, are rated 4.6 out of five by Glassdoor, and were the leading utility company in The Inclusive Top 50 UK Employers List 2021/22.

We believe in the importance of developing younger generations to keep the talent pool flowing. We have active graduate and apprentice schemes, including 30 green apprentices helping us work towards our climate and environmental ambitions. We support young people not in education, employment or training (NEETs), as well as being part of the government's Kickstart scheme providing opportunities to unemployed 16-24 year olds claiming universal credit.

Our commitment to health, safety and wellbeing has been recognised with our 10th consecutive Royal Society for the Prevention of Accidents (RoSPA) gold standard medal, meaning we have achieved the RoSPA President's award.

### **Thank you to our stakeholders**

We are grateful to our employees for their continued hard work, and as we look forward at the many new challenges we and the rest of the sector will be meeting in the next AMP and beyond, we are delighted to have such a great team behind us. We would also like to extend our gratitude to our customers and other stakeholders for their continued support.

## Strategic report

### Our key performance indicators (KPIs)

Our purpose, to provide great water and more for the North West, means we aim to create long-term value for all our stakeholders and, as such, for AMP7 we are reporting against operational KPIs that are linked to each stakeholder group for whom we create value. Our performance against these operational KPIs is reported below.

**Communities** - Our key performance indicator to measure value created for communities over AMP7 is the level of community investment, and we target increasing this by at least 10 per cent over 2020 to 2025, compared with the average of £2.56 million per annum between 2010 and 2020. This year, our direct community investment was £2.8 million (calculated using the B4SI method).

**Customers** - Our key performance indicator to measure customer satisfaction over AMP7 is Ofwat's customer measure of experience (C-MeX), in which we target being in positive reward territory. In 2021/22 we expect to earn a £2.3 million reward and we continue to be the highest performing listed company.

**Employees** - Our key performance indicator to measure value created for our employees over AMP7 is our engagement score, in which we target being upper quartile against the UK Utilities Norm benchmark. Our overall engagement is at 87 per cent, 5 per cent higher than the UK Utilities Norm and equal to UK High Performance levels, which we have now been equal to or above for the last three years.

**Environment** - Our key performance indicator to measure value created for the environment over AMP7 is our performance against the Environment Agency's annual performance assessment, in which we target being an upper quartile performer. The most recent assessment was for 2020, in which we achieved our best ever performance, green across all measures – the first water company to achieve this level of performance since 2015 – and were awarded the maximum 4 star industry leading company status. The Environment Agency will publish its annual performance assessment for 2021 in July 2022.

**Investors** - Our key performance indicator to measure value created for our investors over AMP7 is Return on Regulated Equity (RoRE), and we will update our targets for individual components of this measure as we progress through the period. Reported RoRE for 2021/22 was 7.9 per cent on a real, RPI/CPIH blended basis, double the base return. Underlying RoRE was slightly lower at 7.7 per cent, and excludes the tax that will be recovered through the regulatory sharing mechanism.

**Suppliers** - Our key performance indicator to measure value created for our suppliers over AMP7 is payment within 60 days, and we target at least 95 per cent of invoices to be paid within this timeframe. In 2021/22, we have continued to exceed our target performance, with over 99 per cent of our invoices paid within 60 days, and our average time to pay is 13 days.

**Financial KPIs** – We monitor six financial key performance indicators (underlying operating profit, underlying earnings per share, dividend per share, gearing, total shareholder return, and a low dependency pension scheme), for which we set targets and assess performance at the UUG level. As United Utilities Water Limited makes up 99 per cent of UUG assets and around 97 per cent of revenues/operating profit, the company KPIs are aligned to those of UUG and the outcomes are materially the same. We met our expectation/target on five of these six measures, being close to meeting our expectation/target on total shareholder return as UUG's total shareholder return was higher than the FTSE 100 average but not as high as some listed peers in the utility sector. More detail on these KPIs can be found on pages 10 and 11 of the UUG Annual report and financial statements.

## Strategic report

### Financial performance

Revenue for the year to 31 March 2022 increased by 3 per cent, mainly driven by higher non-household consumption as business activity has returned to pre-pandemic levels. Household bad debt has returned to 1.8 per cent of regulated revenue, lower than the 2.2 per cent last year and consistent with the level we were achieving prior to the pandemic, helped by our wide ranging affordability schemes and effective approach to managing cash collection. Operating profit was broadly in line with the prior year as the increase in revenue was largely offset by inflationary increases in power and other core costs.

While inflation has increased our operating costs and net finance expense this year, it has also led to a higher level of financing outperformance and, together with the £765 million additional investment we have announced beyond the scope of our final determination, will deliver higher regulatory capital value (RCV) growth over the 2020-25 period.

We have doubled our base return on regulated equity (RoRE) for 2021/22, delivering strong performance on financing, tax and customer ODIs.

We benefit from having one of the strongest balance sheets in the sector, with an industry-leading, fully funded pension scheme on a low dependency basis, a low level of customer debtor risk, and RCV gearing supporting a stable A3 credit rating with Moody's.

#### Revenue

	£m
Year to 31 March 2021	1,797.6
Regulatory revenue changes -1.5 per cent real reduction in allowed wholesale revenues and 0.6 per cent uplift in line with CPIH inflation	(13.5)
Non-household consumption increase	105.9
Household consumption decrease	(57.7)
Other	12.3
<b>Year to 31 March 2022</b>	<b>1,844.6</b>

Revenue was up £47 million, at £1,845 million, largely reflecting higher consumption as business activity returns to pre-pandemic levels.

In 2021/22 we have had a £14 million reduction in the revenue cap, incorporating a 1.5 per cent real reduction in allowed wholesale revenues partly offset by a 0.6 per cent CPIH-linked increase.

With many more businesses able to operate compared with last year, when the impact of the initial lockdown was significant, non-household revenue has increased by £106 million. In contrast, consumption from households, although higher than pre-pandemic norms, has decreased £58 million this year. This is due to significantly higher consumption particularly during the first half of last year reflecting the initial impact of people being locked down at home through the warm weather of late spring 2020.

## Strategic report

### Operating profit

	£m
Underlying and Reported – year to 31 March 2021	601.7
Revenue increase	47.0
COVID-related costs in prior year	8.0*
Costs driving ODI performance	(17.0)
Power cost increase	(16.2)
Other costs, largely due to inflation	(16.3)
SaaS costs treated as operating expenses	(5.8)
<b>Underlying and Reported – year to 31 March 2022</b>	<b>601.4</b>

\* £8m COVID-related costs was an estimate in the year ended 31 March 2021 because, with the passage of time and as conditions brought about by the pandemic have become embedded into normal business processes, the usefulness of tracking COVID-related costs specifically has diminished.

Underlying and reported operating profit at remained broadly stable year on year. The £47 million increase in revenue was mostly offset by higher power costs and inflationary pressures increasing our underlying cost base, predominantly in respect of materials and labour.

We have a reduction of around £8 million in operating costs as last year saw additional one-off costs incurred in adapting to operate through the pandemic.

The £17 million of additional costs driving ODI performance are targeted at improving performance against specific customer ODIs, such as spend associated with Dynamic Network Management.

Power costs have increased by £16 million this year, largely in relation to higher prices. Power is a significant cost for our business, which is why we manage this risk through a progressive policy of hedging the commodity price element of power costs to minimise short term volatility (commodity price makes up around half of our annual power costs, with the other half relating to the use-of-system charge and other levies). Through this hedging policy and self-generation, we locked in the cost on the majority of the group's consumption for 2021/22 before the most recent energy price rises, securing an average rate of £65 per megawatt hour (MWh) for the year, which is significantly lower than the current market rate of over £200 per MWh for next year and has been fundamental to our ability to minimise the impact on our cost base. The group is also locked-in on over 90 per cent of expected consumption for 2022/23, and around two-thirds of expected consumption across the final two years of AMP7, at rates that compare favourably to the current market rate.

Cost increases of £16 million largely stem from higher inflation in the period. We are not immune to the impact of the current high inflation environment, but through hedging, constructive cost challenge and commercial negotiations, we have managed to mitigate much of the cost increase to date.

During the year, the IFRS Interpretations Committee (IFRIC) published clarifications on how arrangements in respect of a specific part of cloud technology – Software as a Service – should be accounted for, resulting in £6 million of costs that would previously have been accounted for as fixed asset additions now being treated as operating costs.

Household bad debt is back at our lowest ever level of 1.8 per cent of regulated revenue, having reduced from 2.2 per cent in the year to 31 March 2021 as we return to pre-pandemic levels.

## Strategic report

### Profit before tax

	<b>£m</b>
Underlying – year to 31 March 2021	454.4
Underlying operating profit increase	(0.3)
Underlying net finance expense increase	(166.5)
<b>Underlying – year to 31 March 2022</b>	<b>287.6</b>
Adjusted items *	138.0
<b>Reported – year to 31 March 2022</b>	<b>425.6</b>

\* Adjusted items are set out on pages 38 to 40.

Underlying profit before tax was £288 million, £166 million lower than last year. This reflects the £166 million increase in underlying net finance expense.

Reported profit before tax decreased by £80 million to £426 million reflecting the £80 million increase in reported net finance expense (including fair value movements).

- Net finance expense

The underlying net finance expense of £314 million was £167 million higher than last year, mainly due to the non-cash impact of significantly higher inflation on our index-linked debt.

The indexation of principal on index-linked debt, excluding the impact of inflation swaps, amounted to a net charge in the income statement of £228 million, compared with a net charge of £53 million last year, resulting in an increase of £175 million. Interest on non index-linked debt of £81 million is consistent with last year, while foreign exchange gains of £44 million compare with foreign exchange losses of £15 million last year. Various smaller year-on-year increases and decreases broadly offset against one another when considered together.

The £314 million underlying net finance expense included in the income statement for the year compares with £120 million net cash interest paid included in the statement of cash flows. This £194 million difference is predominantly due to non-cash inflation uplifts on index linked debt and derivatives of £256 million, less capitalised borrowing costs of £53 million and net pension interest income of £11 million, both of which are non-cash items.

Reported net finance expense of £176 million was £80 million higher than last year, reflecting the £167 million increase in underlying net finance expense, offset by an £87 million increase in net fair value gains on our debt and derivative portfolio, excluding interest on derivatives and debt under fair value option, from £51 million last year to £138 million this year.

## Strategic report

### Profit/(loss) after tax

	<b>PAT</b> <b>£m</b>
Underlying – year to 31 March 2021	379.4
Underlying profit before tax decrease	(166.7)
Tax credit relating to research and development tax allowances	72.5
Underlying tax decrease, including the impact of capital allowance 'super deductions'	83.8
<b>Underlying – year to 31 March 2022</b>	<b>369.0</b>
Adjusted items *	(445.7)
<b>Reported – year to 31 March 2022</b>	<b>(76.7)</b>

\* Adjusted items are set out on pages 38-40.

Underlying profit after tax of £369 million was £10 million lower than last year as the £167 million reduction in underlying profit before tax is partly offset by £142 million lower underlying tax (moving from a charge of £78 million last year to a net credit of £82 million this year). The reduction in underlying tax reflects a £73 million tax credit relating to optimising the available research and development UK tax allowances on innovation-related expenditure we had incurred in prior years, and the impact of the capital allowance 'super deductions' announced in the March 2021 Chancellors Budget, which lowers the current tax charge significantly in the current period.

The group has a reported loss after tax of £77 million this year, compared with a £410 million reported profit after tax last year. This £487 million difference reflects the £80 million decrease in reported profit before tax, and a £584 million increase in deferred tax largely due to a one-off charge to restate the brought forward deferred tax liability at the new 25 per cent future headline rate, partially offset by a £156 million positive movement in current tax primarily as a result of adjustments in respect of optimising available tax incentives on our innovation-related expenditure in prior years.

- Tax

The group continues to be fully committed to paying its fair share of tax and acting in an open and transparent manner in relation to its tax affairs and the United Utilities group was delighted to have retained the Fair Tax Mark independent certification for a third year, having been only the second FTSE 100 company to be awarded the Fair Tax Mark in July 2019.

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 over further amounts for its over 5,000 strong workforce. The total payments for 2021/22 were around £230 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 2021/22, we paid corporation tax of around £37 million, which represents an effective cash tax rate on underlying profits of 13 per cent, which is 6 per cent lower than the headline rate of corporation tax of 19 per cent. The key reconciling item to the headline rate of corporation tax continues to be allowable tax deductions on capital investment including the new temporary capital allowance 'super deductions'. We expect a similar tax benefit from the temporary super deduction regime for 2023 as well.

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

## Strategic report

medium-term cash tax rate forecast. We expect the average cash tax rate on underlying profits to remain below the headline rate of tax for the medium term.

For 2021/22, the group recognised an overall current tax credit of £82 million in 2021/22. This includes a current tax charge relating to 2021/22 of £nil million this year, compared with £78 million in the previous year, key reconciling items being the lower taxable profits and the availability of capital allowance 'super deductions' for 2021/22. In addition, in the current year, there were prior period tax credits of £82 million, compared with £nil million in 2020/21. The current year credit mainly relates to optimising the available research and development UK tax allowances on our innovation-related expenditure for multiple prior years.

For 2021/22, the group recognised a deferred tax charge of £584 million, compared with £17 million for 2020/21. For 2021/22, £404 million relates to the government's planned increase in the rate of corporation tax from 19 per cent to 25 per cent from 1 April 2023. Subject to any legislative or tax practice changes, we would expect the total effective tax rate to continue to be broadly in line with the headline rate of corporation tax for the medium term.

In 2021/22, there are £107 million of tax adjustments recorded within other comprehensive income, primarily relating to remeasurement movements on the group's defined benefit pension schemes. As in the prior year the rate at which the deferred tax liabilities are measured on the group's defined benefit pension scheme is 35 per cent, being the rate applicable to refunds from a trust.

### Dividend per share

The Board has not proposed a final dividend in respect of the year ended 31 March 2022. Interim dividends totalling £339.2 million were paid during the year, results in a total dividend per ordinary share for 2021/22 of 1.48 pence. No dividends were paid by the company in the prior year.

### Cash flow

Net cash generated from continuing operating activities for year to 31 March 2022 was £868 million, £73 million lower than £941 million last year. The group's net capital expenditure was £627 million, principally in the regulated water and wastewater investment programmes. This excludes infrastructure renewals expenditure, which is treated as an operating cost.

### Pensions

As at 31 March 2022, the group had an IAS 19 net pension surplus of £771 million, compared with a surplus of £531 million at 31 March 2021. This £240 million increase principally reflects an increase in credit spreads during the year, partially offset by a higher inflation assumption. The group has de-risked its pension schemes through hedging strategies applied to the underlying interest rate and future inflation. The IAS 19 position remains volatile to changes in credit spread and changes in mortality, neither of which have been hedged at this current time. This is primarily due to difficulties hedging against credit spread volatility over long durations, and, for mortality, there is lower volatility in the short term and relatively high hedging costs. The scheme specific funding basis does not suffer volatility due to credit spread movements to the same extent as it uses a prudent, fixed credit spread assumption.

Further detail on pensions is provided in note 15 ('Retirement benefit surplus') of these financial statements.

## Strategic report

### Financing

Net debt	£m
At 31 March 2021	7,664.8
Cash generated from operations	(1,025.8)
Net capital expenditure	626.4
Dividends	339.2
Indexation	228.6
Interest	120.0
Fair value movements	24.4
Tax	37.4
Other	4.5
<b>At 31 March 2022</b>	<b>8,019.5</b>

Net debt at 31 March 2022 was £8,020 million, compared with £7,665 million at 31 March 2021. This comprises gross borrowings with a carrying value of £8,350 million net of cash and short-term deposits of £161 million and net derivative assets hedging specific debt instruments of £169 million.

Underlying movements in net debt are largely a result of net operating cash inflows offset by our net capital expenditure, dividends, indexation and cash interest.

Gearing, measured as group net debt divided by UUW's shadow (adjusted for actual spend and timing difference) regulatory capital value of £12.4 billion, was 61 per cent at 31 March 2022. This is slightly lower than gearing of 62 per cent as at 31 March 2021, and remains comfortably within our target range of 55 to 65 per cent.

- Cost of debt

As at 31 March 2022, the group had approximately £3.2 billion of RPI-linked instruments and £0.4 billion of CPI or CPIH-linked instruments held as debt. In recent years, in response to Ofwat's decision to transition away from RPI inflation linkage, the group has entered into a number of transactions swapping RPI-linked cash flows to CPI-linked cash flows or swapping floating rate cash flows to CPI-linked cash flows. As a result, including these swaps, the group has RPI-linked debt exposure of £3.1 billion at an average real rate of 1.3 per cent, and £1.1 billion of CPI or CPIH-linked debt exposure at an average real rate of -0.6 per cent.

A significantly higher RPI inflation charge compared with the same period last year contributed to the group's average effective interest rate of 4.8 per cent being higher than the rate of 2.9 per cent last year. The average underlying interest rate represents the underlying net finance expense adjusted for capitalised borrowing costs and net pension interest income, divided by average notional debt. More information on this can be found on page 40.

The UUG group has fixed the interest rates on its non index-linked debt in line with its 10-year reducing balance basis at a net effective nominal interest rate of 2.2 to 2.4 per cent for the remainder of the AMP7 regulatory period.

- Credit ratings

UUW's senior unsecured debt obligations are rated A3 with Moody's Investors Service (Moody's), A- with Fitch Ratings (Fitch) and BBB+ with Standard & Poor's Ratings Services (S&P)

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and all on stable outlook. United Utilities PLC's (UU PLC's) senior unsecured debt obligations are rated Baa1 with Moody's, A- with Fitch and BBB- with S&P, all on stable outlook.

- Debt financing

The group has access to the international debt capital markets through its £10 billion medium-term note (MTN) programme. The MTN programme is updated at least annually and this year's update was completed in November 2021, at which time the previous €7 billion euro programme limit was increased and redenominated to £10 billion. The MTN programme does not represent a funding commitment, with funding dependent on the successful issue of the notes.

In total over 2020-25, we expect to raise around £2.7 billion to cover refinancing and incremental debt, supporting our five-year investment programme. So far in AMP7, we have raised around £1.4 billion, taking advantage of attractive rates available and extending our liquidity position (as at 31 March 2022) out to February 2025.

In November 2020, we published our new sustainable finance framework, through which we expect to raise financing based on our strong ESG credentials alongside conventional issuance. This replaces the green funding we have previously secured through the European Investment Bank (EIB), which is no longer available post-Brexit. We issued our debut sustainable bond in January 2021, raising £300 million maturing in October 2029 and subsequently swapped to CPI-linkage.

In August 2021, we raised around £74 million of term funding via the issue off our MTN programme of a JPY11 billion privately placed note swapped to GBP with a 9-year maturity, and in September 2021 we priced a £100 million fixed note with a 7-year maturity, the proceeds of which were received in early October.

In April 2022, we raised £100 million of term funding with an 8-year maturity via a bilateral loan with Export Development Canada (EDC). AAA-rated EDC is the Canadian Government's Export Development Agency that looks to promote trade with Canadian firms worldwide. This follows collaboration with EDC in relation to some of the innovation activities that we have undertaken, and we expect such collaboration to continue.

Since March 2021, we have extended £100 million of revolving credit facilities for a further year, renewed £100 million of revolving credit facilities for a further 5-year term and entered into £40 million of new revolving credit facilities for a 5-year term. The group has also amended the documentation for all of its existing revolving credit facilities to remove references to LIBOR and replace with SONIA.

- Interest rate management

Long-term borrowings are structured or hedged to match assets and earnings, which are largely in sterling, indexed to UK 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 2022, approximately 41 per cent of the group's net debt was in RPI-linked form, representing around 25 per cent of UUW's regulatory capital value, with an average real interest rate of 1.3 per cent. A further 15 per cent of the group's net debt was in CPI or CPIH-linked form, representing around nine per cent of UUW's RCV, with an average real rate of -0.6 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 around 18 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.

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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.

- 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. Our MTN programme provides further support.

At 31 March 2022, we had liquidity out to February 2025, comprising cash and short-term deposits, plus committed undrawn revolving credit facilities. This gives us flexibility in terms of when and how further debt finance is raised to help refinance maturing debt and support the delivery of our regulatory capital investment programme. In October 2021, U UW prepaid a £100 million floating rate loan a year ahead of its scheduled maturity, this being efficient use of our available liquidity.

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.

### Return on Regulated Equity (RoRE)

Reported RoRE for 2021/22 was 7.9 per cent on a real, RPI/CPIH blended basis.

This comprises the base return of 3.9 per cent (including our 11 basis point fast track reward that we receive in each of the five years of the AMP), tax outperformance of 2.7 per cent, financing outperformance of 1.6 per cent, and customer ODI outperformance of 0.5 per cent, partially offset by the total expenditure (totex) impact on RoRE of -0.8 per cent as a result of our additional investment.

Underlying RoRE was slightly lower at 7.7 per cent, and excludes the tax that will be recovered through the regulatory sharing mechanism.

- Totex performance

The totex impact on RoRE of -0.8 per cent, on both a reported and underlying basis, largely reflects the year two impact of the additional investment we are making outside the scope of our Final Determination (FD), for example our investment in Dynamic Network Management.

Our AMP7 business plan was assessed by Ofwat as being amongst the most efficient in the sector, and our performance improvements over AMP6 meant we started AMP7 at a totex run rate that supported delivery of the stretching efficiency challenge in our FD allowance. We are not immune to the impact of inflation, both directly and indirectly through our supply chain, with many of our costs rising above the headline rate. Our totex allowance does increase with inflation, which helps to mitigate some of this cost pressure, and we continue to exploit technology and innovation to help us deliver our investment efficiently.

In this second year of AMP7, we have invested £645 million in net regulatory capital expenditure (excluding infrastructure renewals expenditure), representing the continued acceleration of our AMP7 investment programme and early expenditure against the extension to our original totex plans as set out above. Cumulatively, this is £1.3 billion in the first two years of the period, which represents a good start to the delivery of our AMP7 programme. We have been able to deliver this expenditure effectively, maintaining our high performance scores against our Time, Cost and Quality index (TCQi) at over 95 per cent.

Our investment strategy delivers long-term efficiency and sustainable performance improvements, and the additional £765 million investment we are making beyond the scope of

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our FD will drive further enhancements for customer and environmental performance. £265 million of this investment we expect to be fully recovered through regulatory mechanisms, including Green Recovery and projects that form part of our Water Industry National Environment Programme (WINEP). £250 million of this investment is improving environmental outcomes, funded through investment of outperformance, and subject to regulatory sharing mechanisms. The final £250 million of this investment will drive improved performance against customer outcomes and is supported on a business case basis, delivering improved customer ODI performance.

While we continue to strive to deliver our investment efficiently, as we have demonstrated through this additional investment, we will invest where we are confident we can deliver improved customer or environmental outcomes and better customer ODI performance.

- Customer outcome delivery incentives (ODIs)

Customer ODI outperformance of 0.5 per cent, on both a reported and underlying basis, reflects a net reward of £25 million<sup>6</sup>. This is our highest ever one-year net reward against customer ODIs, reflecting our continued improvements in performance for customers.

Our customer ODI performance has been strong across the board, meeting or beating over 80 per cent of our performance commitments, giving us the confidence to increase our total AMP7 ODI guidance by a third, targeting a cumulative net ODI reward over the five-year period of around £200 million.

The additional investment we are making will help improve performance in areas where we want to do better. This includes £100 million investment in Dynamic Network Management, which will help us improve performance on sewer flooding, and around £100 million investment in improving water quality.

Customer ODI rewards and penalties in AMP7 will be adjusted in revenues on a two-year lag, therefore the net reward earned this year will be reflected in an increase to revenues earned in 2023/24 through allowed increases in the rates charged to customers in that financial year, in accordance with the regulatory mechanism.

- Financing outperformance

We earned financing outperformance this year of 1.6 per cent, on both a reported and underlying basis, compared with 1.2 per cent last year. This increase mainly results from recent high levels of inflation, which increases the benefit of the roughly £3 billion fixed rate debt we have locked in.

We have consistently issued debt at efficient rates that compare favourably with the industry average, thanks to our leading treasury management, clear and transparent financial risk management policies, and ability to act swiftly to access pockets of opportunity as they arise. This delivered significant financing outperformance during AMP6 and the rates we have locked-in for AMP7 compare favourably with the price review assumptions.

- Tax outperformance

The 2.7 per cent outperformance on tax on a reported basis reflects our optimisation of available government tax incentives, including research and development tax allowances and the temporary capital allowance 'super deductions', net of the tax impact of financing outperformance. The 2.5 per cent outperformance on tax on an underlying basis excludes the tax that will be recovered through the regulatory sharing mechanism.

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<sup>6</sup> Excluding per capita consumption, which Ofwat will be revisiting at the next price review once there is a better understanding of the impact of COVID 19 and any enduring effects

## Strategic report

### OUTLOOK

We have delivered another good year of performance, maintaining high levels of customer satisfaction underpinned by our Systems Thinking approach, improving operational performance, and long-term financial resilience, giving us confidence in our ability to continue to create value for customers, the environment, and other stakeholders.

We are accelerating our AMP7 capital programme and investing an additional £765 million over the regulatory period to help us deliver even more sustainable improvements in customer and environmental performance, and to get ahead of the requirements coming into force through the Environment Act. This investment, together with latest views of inflation, contributes to RCV growth over AMP7 of 21 per cent on a nominal basis, more than 10 per cent higher than we expected at the beginning of the period.

Our sustained high level of operational performance is earning outperformance, and we have increased our target of cumulative net outperformance against customer ODIs by a third to around £200 million in total over AMP7. As a consequence of our performance in AMP7 and the additional investment we are making, we are generating around £750 million of value that we expect to receive through an RCV uplift and additional revenues in AMP8.

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### Guide to Alternative Performance Measures (APMs)

The underlying profit measures in the following table represent alternative performance measures (APMs) as defined by the European Securities and Markets Authority (ESMA). These measures are linked to the group's financial performance as reported in accordance with UK-adopted international accounting standards and the requirements of the Companies Act 2006 in the group's consolidated income statement, which can be found on page 146. As such, they represent non-GAAP measures.

These APMs 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.

In addition, a reconciliation of the group's average effective interest rate has been presented, together with a prior period comparison. In arriving at net finance expense used in calculating the group's effective interest rate, underlying net finance expense is adjusted to add back net pension interest income and capitalised borrowing costs in order to provide a view of the group's cost of debt that is better aligned to the return on capital it earns through revenue.

Adjusted item	Rationale
Fair value (gains)/losses on debt and derivative instruments, excluding interest on derivatives and debt under fair value option	Fair value movements on debt and derivative instruments can be both very significant and volatile from one period to the next, and are therefore excluded in arriving at underlying net finance expense as they are determined by macro-economic factors which are outside of the control of management and relate to instruments that are purely held for funding and hedging purposes (not for trading purposes). Included within fair value movement on debt and derivatives is interest on derivatives and debt under fair value option. In making this adjustment 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. Taking these factors into account, management believes it is useful to adjust for these fair value movements to provide a more representative view of performance.
Deferred tax adjustment	Management adjusts to exclude the impact of deferred tax in order to provide a more representative view of the group's profit after tax and tax charge for the year given that the regulatory model allows for cash tax to be recovered through revenues, with future revenues allowing for cash tax including the unwinding of any deferred tax balance as it becomes current. By making this adjustment, the group's underlying tax charge does not include tax that will be recovered through revenues in future periods, thus reducing the impact of timing differences.
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.

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### Underlying profit

	Year ended 31 March 2022	Year ended 31 March 2021
	£m	£m
<b>Operating profit</b>		
<b>Operating profit per published results</b>	<b>601.4</b>	601.7
<b>Underlying operating profit</b>	<b>601.4</b>	601.7
<b>Net finance expense</b>		
Finance expense	(188.0)	(114.6)
Investment income	12.2	18.6
<b>Net finance expense per published results</b>	<b>(175.8)</b>	(96.0)
Net fair value gains on debt and derivative instruments, excluding interest on swaps and debt under fair value option	(138.0)	(51.3)
<b>Underlying net finance expense</b>	<b>(313.8)</b>	(147.3)
<b>Profit before tax</b>		
<b>Profit before tax per published results</b>	<b>425.6</b>	505.7
Adjustments in respect of operating profit	–	–
Adjustments in respect of net finance expense	(138.0)	(51.3)
<b>Underlying profit before tax</b>	<b>287.6</b>	454.4
<b>(Loss)/Profit after tax</b>		
<b>(Loss)/Profit after tax per published results</b>	<b>(76.7)</b>	410.1
Adjustments in respect of profit before tax	(138.0)	(51.3)
Deferred tax adjustment	584.3	18.4
Tax in respect of adjustments to underlying profit before tax	(0.6)	2.2
<b>Underlying profit after tax</b>	<b>369.0</b>	379.4

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### Average effective interest rate

In arriving at net finance expense used in calculating the group's effective interest rate, management adjusts underlying net finance expense to add back pension income and capitalised borrowing costs in order to provide a view of the group's cost of debt that is better aligned to the return on capital it earns through revenue.

	31 March 2022	31 March 2021
<b>Underlying net finance expense</b>	<b>(313.8)</b>	(147.3)
Net pension interest income	<b>(11.1)</b>	(13.4)
Adjustment for capitalised borrowing costs	<b>(52.7)</b>	(30.4)
<b>Net finance expense for effective interest rate (a)</b>	<b>(377.6)</b>	(191.1)
Average notional net debt (b)	<b>(8,031)</b>	(7,852)
<b>Average effective interest rate (a/b)</b>	<b>4.7%</b>	2.4%

## Strategic report

### Our approach to climate change

#### Task Force on Climate-related Financial Disclosures (TCFD)

Climate change and extreme weather events are critical to our service delivery because of our reliance on a stable climate and the natural environment. Here we report on our latest progress and plans on cutting emissions to reduce future climate change, known as climate mitigation, and how we are maintaining and improving our resilience to climate change, known as climate adaptation.

Our business, and the communities we serve, has already experienced the impacts of climate change, including several record-breaking weather events that caused impacts such as flooding, power cuts and travel disruption. Risks associated with flooding are heightened in the North West because it is the wettest region in the country, and this is projected to increase with climate change. There is overwhelming evidence that we need to prepare for more severe weather events more often, as well as gradual trends for wetter winters, hotter drier summers and rising sea levels. We integrate past and projected climate data throughout our plans to ensure an effective and evolving response. We are committed to playing our part in securing the global goal to curb climate change to no more than 1.5oC.

In the following pages we share our greenhouse gas emissions (GHGs) and progress towards meeting our six carbon pledges and science-based targets (SBTs). We present our six most sensitive climate risks and our new adaptation report. In this section, supported with content elsewhere in this integrated report and on our website, we include disclosures consistent with the TCFD Recommended Disclosures all sector guidance.

#### Where to find our TCFD recommended disclosures

N.B. Where followed by “UUG” page references relate to the Group Annual Report and Financial statements.

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<b>Governance</b>	<b>Pages</b>	<b>Topic</b>
Board's oversight of climate-related risks and opportunities.	44	TCFD governance
Management's role in assessing and managing climate-related risks and opportunities.	120 UUG	Governance structure
<b>Strategy</b>	<b>Pages</b>	<b>Topic</b>
Climate-related risks and opportunities identified over the short, medium, and long term.	24–25 UUG 11–12	Creating value Our approach to materiality
Impact of climate-related risks and opportunities on our businesses, strategy, and financial planning.	18–21 42–43	Business planning horizons Pledges and targets
Resilience of our strategies, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.	46–49 91–93 56–57 66–68	Climate sensitive risks TCFD strategy TCFD metrics and targets Our risk management
<b>Risk management</b>	<b>Pages</b>	<b>Topic</b>
Processes for identifying and assessing climate-related risks.	45–49	TCFD risk management
Processes for managing climate-related risks.	63–85	Our risk management
How processes identifying, assessing, and managing climate-related risks are integrated into the organization's overall risk management		
<b>Metrics and targets</b>	<b>Pages</b>	<b>Topic</b>
Metrics used to assess climate-related risks and opportunities in line with our strategy and risk management processes.	64–67 UUG 42–43	Our performance Pledge progress
Scope 1, Scope 2, and Scope 3 GHG emissions, and related risks.	61–63	TCFD metrics and targets
Targets used to manage climate related risks and opportunities and performance against targets.	94–97 UUG 161–191 UUG	Energy and carbon report Remuneration

### **Pledge 1 - Reduce scope 1 & 2 emissions**

#### **Down 2.2% compared to baseline**

We are making good progress towards our science-based target to reduce scope 1 and 2 emissions by 42 per cent from our baseline by 2030.

2021/22: 135,936 tCO<sub>2</sub>e

2019/20: 138,961 tCO<sub>2</sub>e (baseline year)

### **Pledge 2 - 100% of electricity used from renewable sources**

#### **We achieved this pledge from October 2021**

From October 2021 the electricity we purchased was from guaranteed renewable sources. In addition, we generated a record 210 GWh of renewable energy in 2021/22, equivalent to 26 per cent of our total electricity consumption.

### **Pledge 3 - 100% green fleet by 2028**

#### **27 fully electric vehicles (EV) now deployed in our fleet with plans for 200 low carbon vehicles by 31 March 2025**

We have installed advanced telematics to improve understanding of travel patterns and are trialling options for larger vehicles. We are enabling employees to shift to EV through changes to the company car policies and launch of a salary sacrifice scheme 'EVolve'.

## Strategic report

### **Pledge 4 - 1,000 hectares of peatland restoration by 2030**

#### **Restoration activity well underway**

We have restoration projects across the North West at different stages of maturity. As well as continuing our site work to completion, we aim to become an early pioneer in applying the Peatland Code at scale to independently verify the carbon benefits.

### **Pledge 5 - Create 550 hectares of woodland by 2030**

#### **9 hectares planted and validated to the Woodland Carbon Code**

Planting in 2021 was postponed due to weather and tree disease. The remaining 541 hectares have been planned and the funding identified.

### **Pledge 6 - Set scope 3 science-based target**

#### **Targets verified by SBTi**

Emissions from our value chain are the most challenging to address so we are working with our supply chain. We are exploring how to improve our calculation methods for scope 3 emissions so that we can consider and openly report the impact of our management choices.

### **Transparency and disclosures**

We have a long track record of public carbon and climate change disclosures having estimated and reported our carbon footprint since 2006 and participated in CDP's Climate Change Programme for 12 years. Our reporting is fully compliant with UK Government Environmental reporting guidelines and applies international best practice such as Greenhouse Gas Protocol Corporate Accounting and Reporting Standards (2015). The Science Based Targets initiative (SBTi) assessed and verified our four science-based targets in July 2021 and commended our ambitious 1.50C aligned scope 1 and 2 target.

We confirm that our annual report includes all climate-related financial disclosures required to be consistent with the TCFD recommendations and recommended disclosures and is in line with the current Listing Rules requirements (as referred to in Listing Rule 9.8.6R(8)). Corporate Citizenship, a leading sustainability consultancy, has reviewed this disclosure and provided an ISAE assurance against the Principles of Effective Disclosure to ensure that consistency with TCFD recommendations including the implementation guidance published in the 2021 Annex.

### **2021 performance**

CDP is known for setting the standard for companies on their environmental leadership. In 2021 we achieved an overall B rating, with category scores of A in targets, governance and risk management. We are working to improve the other categories towards achieving an overall A list rating. We were proud to be recognized as a 2021 Supplier Engagement Leader, raising the level of climate action across our value chain.

### **Examples of our activities to respond to climate change**

#### **Haweswater Aqueduct Resilience Programme (HARP)**

The Haweswater Aqueduct plays an important role in moving large volumes of water from the Lake District to supply Greater Manchester. The aqueduct was originally completed in 1950 and since 2005 we have been planning how to secure its continued and long-term resilience.

Following extensive planning and stakeholder engagement we are ready to start delivery of a solution designed to meet future demand whilst maintaining a gravity-fed, low carbon water supply. The proposed tunnelling solution has been assessed as having one of the lowest environmental and carbon impacts of all options considered, with further opportunities identified to recycle materials to local sites thus reducing impacts from vehicle movements.

## Strategic report

### Surface water separation – Blackpool south

We have invested over £30 million to address the combined challenges of climate change, an ageing Victorian sewer network, and increasing urbanisation in Blackpool.

The primary objective of this project was to separate surface water from the combined sewer system. New infrastructure was constructed, including a storm water interception tank, pumping stations, and a new sea outfall to provide a sustainable discharge point for surface waters. This will prevent over 800,000m<sup>3</sup> of surface water from entering the combined sewer system during wet weather. By diverting the surface water away, the flooding risks posed by storms due to the resulting excess volume of wastewater have been significantly reduced.

### Governance

#### TCFD definition

The organisation's governance around climate-related risks and opportunities.

#### Progress this year

- Oversight and scrutiny of climate change matters by the board and its committees, including approval of our new science-based targets, and review of the adaptation progress report and carbon commitments risk.
- Strengthened governance by expanding our director-led climate change mitigation steering group and introduced six new cross-business working groups.
- Introduced carbon measures into the executive remuneration framework.
- Expanded our internal carbon and climate change teams.
- Supplemented public disclosures through conversations with investors and participation in new climate-related indices and assessments.

#### Future focus

- Communication and engagement programme with all stakeholder groups.
- Deploy whole-life carbon costing using an internal carbon price aligned to government carbon values.

### Board oversight of climate-related risk and opportunities

2021 saw increased global attention on the climate change emergency culminating at the COP26 climate summit in Glasgow. As board members, our Chief Executive Officer and Chief Financial Officer both show personal leadership for the impact of climate change on our capacity and capability to deliver our services. Climate change-related matters have always been of interest to the corporate responsibility committee in its role to scrutinise environmental topics and initiatives. This year, climate change matters have also been discussed by the audit committee (review of carbon commitments risk) and remuneration committee (linking long-term incentive outcomes to the delivery of carbon pledges).

### Management role

CEO Steve Mogford has ultimate responsibility for the group's preparedness for adapting to climate change and driving our mitigation strategy. CFO Phil Aspin has executive responsibility for risk management and is supported in this role by the head of audit and risk and the corporate risk manager. Along with the executive team, they are tasked with managing the risks and mitigating actions, for example by ensuring the company has the necessary financial resources and skilled people are in place to achieve its climate-related objectives.

## Strategic report

Our climate change mitigation strategy starts with ‘vision and visibility’, reflecting that consideration of climate is becoming an essential factor in both day-to-day and strategic decision-making and behaviours. All of the principal management committees have discussed climate-related matters this year. For example, our leadership team has tracked the delivery of our carbon pledges as part of the quarterly business reviews and initiated a trial of a low emission fuel HVO as a result. The capital investment committee is working to integrate climate issues into its decision-making processes including a carbon reduction incentive for capital programme delivery partners.

In 2021/22, we held two deep-dive workshops to build executive team knowledge and awareness of carbon. This resulted in a refresh of our climate change mitigation governance and the creation of new director-led working groups. These focus on maturing our decision-making and delivering reductions of all greenhouse gas (GHG) emissions while developing our future climate-related strategy and engagement.

### Introducing carbon to our executive remuneration

Four carbon measures have been agreed by the remuneration committee for the three-year period ending 31 March 2025, together forming ten per cent of the Long Term Plan (LTP) against which stretching targets have been set. These measures are:

- green fleet vehicles;
- woodland creation;
- peatland restoration; and
- supply chain engagement.

Including targets within our executive remuneration arrangements recognises the importance of our carbon commitments. We have designed these measures to reinforce delivery of our ambitious carbon pledges and science-based targets. We are working to mature these incentive measures in future years, ultimately to align with our science-based emission reduction targets for 2030 and beyond.

## Risk management

### TCFD definition

How the organisation identifies, assesses and manages climate-related risks.

### Progress this year

- Published our third adaptation report, including the outcome of a progress review of climate-related risks across the organisation.
- Greater recognition of transitional risks in our corporate risk management system, in particular the investment needed to meet our carbon commitments and the potential costs to the business if we do not.

### Future focus

- Produce our PR24 business plan with full integration of carbon reduction and climate resilience priorities.
- Finalise and publish our 2022 Drought Plan.
- Improve our long-term strategic plans for water resources and drainage, integrating advanced climate change analysis to shape our investment and operational approaches in the short, medium and long term (up to 80 years).
- Embed climate change impacts into corporate decision-making tools and processes.

## Strategic report

### Climate risk identification and assessment

We have a mature risk and resilience framework for the identification, assessment and mitigation of risks, as described on pages 66 to 71. This framework is used to identify and assess climate-related risks. We consider both physical risks, identified as those related to climate change impacts on our operations or assets, and transitional risks, which are those associated with the necessary transition to a low-carbon economy (e.g. changes to policies, regulation and legislation).

We use a variety of approaches to assess risks, such as risk breakdown structures and PESTLE. We use complex modelling of the physical impacts of climate change in our water resources and drainage management planning, and incorporate Met Office UK climate projections. In our assessment of materiality we recognise that some risk events may happen multiple times so we compare impacts over a long-term (40-year) horizon. This accentuates where climate change, and other demographic changes, influence the frequency of events as well as the consequences.

We have found that horizon scanning for industry research and emerging legal and regulatory changes are particularly useful when considering transitional risks. In our revision of the carbon commitments risk, we incorporated the updated carbon values provided by the department for Business, Energy and Industrial strategy (BEIS). Applying these values resulted in an escalation of the risk to the executive team and board who re-evaluated our response to ensure we continue to effectively manage the risk. Incorporating longer-term climate change impacts explicitly in our corporate risk framework has raised the profile of climate change, allowing the board to consider our appetite and capacity to mitigate and control the risks from within existing risk management processes and with the same thresholds for materiality.

### Managing climate-related risks

By recognising the causes and consequences, and assessing the likelihood and the severity of impact (both financial and reputational) should the event occur, we are able to prioritise climate-related risks and take proactive and early action to reduce the frequency and severity.

As climate change is a common causal factor for our principal risks (see pages 68 to 82), a review of all event-based risks in our business risk profile was undertaken to assess their sensitivity to climate change. The most sensitive risks are outlined on page 46 to 50 and more details, including discussion and examples of activities to mitigate and control for these risks, can be found in our latest adaptation progress report.

### Organisational resilience to climate change

In preparing each of our three adaptation progress reports, we assessed the organisation's resilience to specific outcomes of climate change, such as hotter, drier summers and more extreme weather events. We identified over 90 risks that could impact a single business area, for instance wastewater, but we also noted business-wide risks, interdependencies and transitional risks. The outcome of the latest assessment was 79 new or existing mitigating actions listed in our adaptation report along with an update on what has been done to manage the risk to date.

We are maturing our understanding of risk and uncertainty to build and maintain long-term resilience across the corporate, financial and operational structures of the group. Looking ahead, we will explore how innovation can help us to learn more about the profile of risk events, their causes and consequences, and to identify opportunities to improve our capacity and capability. This will help us to identify where climate risks remain uncertain or where existing controls might be inadequate to manage the risk in the long term. This will help us to be better prepared by prioritising issues.

### Our risks most sensitive to climate change

Last year, we presented the outcome of a special risk assessment on the sensitivity of all our event-based risks to climate change. We have updated this assessment through our corporate risk process and the results are shown below. Likelihood and impact are based on the Met Office climate projections using the most likely global emissions scenario known as RCP 6.0, in which emissions peak around 2080 and average temperatures will have risen to between 3 and 3.5°C by 2100.

## Strategic report

### Risk categorisation



Chronic physical risk – changing trends in weather patterns, such as rising temperatures, sea level and rainfall.



Acute physical risk – chance of severe weather events, such as storms, heat waves and floods.

\* One of the most significant event-based group risks

### Control effectiveness

Controls are the activities we undertake to reduce risk or realise an opportunity.



Largely insufficient to mitigate risk



Somewhat sufficient



Mostly sufficient

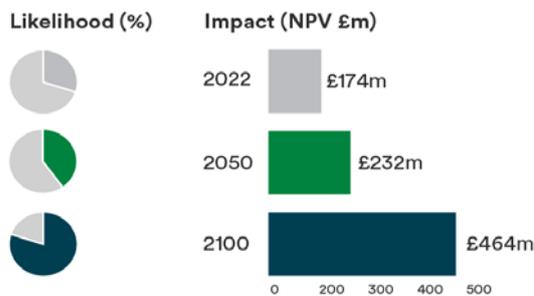
## Strategic report

### Water sufficiency event

Prolonged dry periods can cause supply challenges. Warmer temperatures intensify these pressures because of increased water usage and evapo-transpiration.

#### Controls

- Reduce leakage.
- Support customers to use less water.
- Install more meters in domestic properties.
- Develop new sources of water, particularly boreholes.
- Long-term water resources management planning.
- Facilitate water trading between the North West and other regions of the UK.

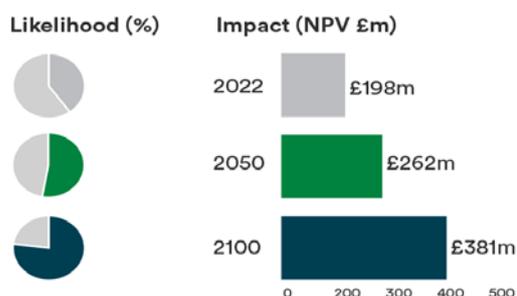


### Failure of wastewater network (sewer flooding) \*

More frequent and intense storms can overload the wastewater network and lead to severe sewer flooding. Urbanisation makes this worse due to quick run-off from hard surfaces.

#### Controls

- Implement and encourage 'slow the flow' and sustainable drainage solutions.
- Support customers to use sewers responsibly.
- Increase sewer capacity and build storm water holding tanks.
- Use technology to monitor and better control flows in the sewer system.
- Install flood protection devices to at-risk properties.



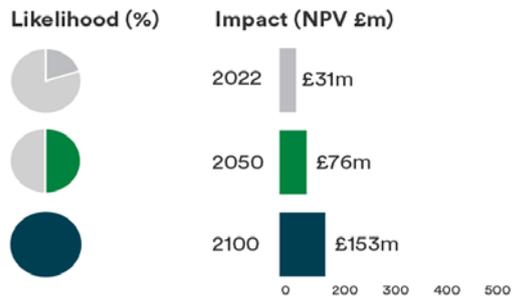
# Strategic report

## Land management \*

Deterioration in land quality due to climate change has both direct and indirect impacts. Hotter, drier summers lead to fire, flood, subsidence and landslip events which in turn have associated health, safety and environmental impacts.

### Controls

- Catchment Systems Thinking and proactive land management, including nature-based solutions.
- Deliver net gain in biodiversity from our construction projects.
- Directly restore peatland and woodland.
- Work in partnership with farmers, regulators and others to improve upland watercourses.

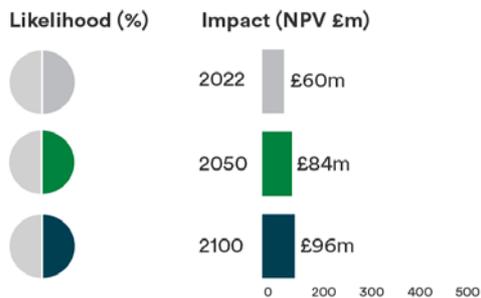


## Failure to adequately treat wastewater

Extremely heavy rainfall, which is projected to happen more often, can exceed our wastewater treatment works capacity and result in use of overflows to prevent flooding of assets, streets and homes.

### Controls

- Investment to meet legislated environment and treatment capacity requirements.
- Inclusion of climate change growth parameters in long-term adaptive plans.
- Controls for failure of wastewater network will support this risk.



## Strategic report

### Failure of above-ground water and wastewater assets



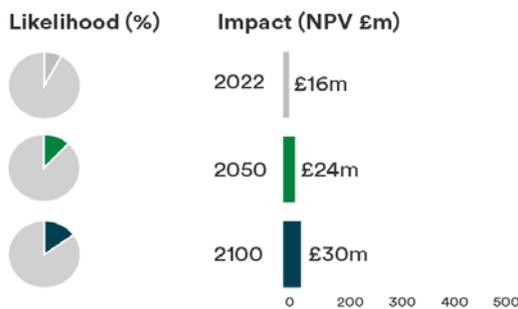
(flooding)

Average winter rainfall is projected to rise, increasing the frequency of extreme events where operational sites are flooded from sea, river or surface water sources.

#### Controls



- Install permanent flood defences at most flood-prone sites.
- Improve flood forecasting capabilities.
- Build better network connectivity to maintain water supplies during floods.
- Invest in quick recovery once flooding subsides.



### Recycling biosolids to agriculture \*



Water logging resulting from more persistent rainfall will limit options for recycling biosolids to land for a greater part of the year. Uncovered sludge stores and stockpiles will be more vulnerable in persistent wet, winter weather, increasing the risk of environmental pollution from run-off.

We are currently updating our assessment of this risk following recently proposed legislative changes included within the Farming Rules for Water. We expect this will significantly restrict the window of permitted recycling of biosolids to agriculture, and therefore exceed the climate change impact we have previously assessed.

### Strategy

#### TCFD definition

How climate-related risks and opportunities impact the organisation's businesses, strategy and financial planning.

#### Progress this year

- Built relationships with key suppliers to reduce environmental impact by sharing best practice and collaborating on how to reduce GHGs.
- Further developed our multi-capital approach to enhance decision-making processes, integrating both GHG impact and attributes of climate resilience.
- Implemented climate change resilience plans (both physical and transitional) across AMP7, incorporating natural capital solutions.

## Strategic report

### Future focus

- Further develop our mitigation and adaptation strategies and delivery plans.
- Include low carbon and climate adjustable approaches in our PR24 business plan.
- Assess and limit the carbon impact of our PR24 business plan.



### Our climate change mitigation strategy

#### Planning horizons

Our assets typically have long, even very long, lifespans so we are vulnerable to physical climate risks over the long term, and we are already experiencing the impacts of climate change in the North West. We undertake planning for long (25+ years), medium (5–10 years), and short-term (one year) horizons, enabling us to account for external drivers including climate change, while continuing to fulfil our purpose in a resilient and adaptable way. Our planning horizons are further described on pages 48 to 49 of the UUG Annual report and financial statements.

#### Short-term climate issues

Extreme weather events such as periods of hot and dry weather, cold snaps and heavy rain events impact our ability to deliver our services. Climate change is already increasing the frequency of these events (see page 53), exacerbating the impact of existing risks such as sewer flooding, asset flooding and asset deterioration as can be seen in the current top ten event-based risks shown on pages 82 to 85.

## Strategic report

The North West has felt the significant damage caused by numerous extreme storms over recent years. The region has 28 per cent more rainfall than the average for England and Wales and climate change will further increase the likelihood and severity of intense storms. There is also a significantly higher proportion of combined sewers so, together, this means more pressure on sewerage and treatment infrastructure, and relatively more risk from sewer flooding and/or pollution from storm overflows. Managing the risk of flooding is a priority for us and other agencies in the North West.

### Medium and long-term impact of climate change

Predicting the effects of climate change is complex, with greater uncertainty about how our infrastructure will respond to the challenges presented by both climate and demographic changes. We considered the implications of climate change to our business risk profile to ascertain which risks were sensitive to climate change in that climate change would increase their likelihood or severity. To quantify the risk we used the highly respected and relevant Met Office UK Climate Projections 2018 (UKCP18) for weather in the North West. There are four main pathways used for climate modelling and research, each describing climate futures related to the volume of greenhouse gases emitted. For our climate sensitivity assessment we chose the Met Office climate projections for the representative concentration pathway, RCP 6.0, which has an emissions peak occurring in 2080 and an expected 3.0–3.5°C increase in global mean temperatures from pre-industrial levels.

### Impact of climate-related risks and opportunities on our business strategy and planning

We have taken a twin track approach to addressing climate change in our business strategy and planning (see page 53). We account for the costs and benefits, of both mitigation and adaptation and in this way manage both physical and transitional climate risks as we deliver our services in a sustainable and resilient way.

### Adapting to physical risks

All six of the risks most sensitive to climate change are physical risks, meaning they are disruptive or destructive to our operations or assets. This means there are tangible controls that can be put in place to improve our resistance to weather events, enhance our response and recovery preparations and realise opportunities.

We are applying a systems thinking approach which recognises the complex interdependencies within our business functions and externally across society. This means that interventions to address one risk have multiple benefits. For instance, sustainable drainage systems (SuDS) to slow down or divert rainwater run-off both reduce the risk of sewer flooding and optimise wastewater treatment capacity. Green infrastructure solutions such as SuDS provide an opportunity to deliver wider social value in the community and local environment.

### Strategies for a changing climate

Alongside our focus to address the climate-related risks to our service delivery, we recognise the critical need to secure a stable climate and minimise the need for adaptation over the long term. We are part of the global leadership community that is working to encourage everyone to contribute to achieving the global goal to curb emissions.

In response, our climate change mitigation strategy has four pillars (see page 51 to 52). Our focus this year has been to consolidate our ambition and commitments and to enhance the visibility and understanding of climate impacts both within the organisation and to our external stakeholders. We were proud to be the first UK water company to have its targets verified by the Science Based Targets initiative (SBTi) and used this to drive communication and engagement. We held deep-dive sessions with the executive team, developed and launched an employee e-learning module, and had net zero as a theme in our latest Innovation Lab, in which we challenge and collaborate with new suppliers.

## Strategic report

Climate change was a topic in our CEO graduate challenge. A team of graduates focused on helping mature plans towards a net zero future by developing a tool to estimate process emissions on a site-by-site basis, promoting our carbon pledges to employees through a social media campaign, and compiling a database of over 200 potential emission reduction opportunities that we are now exploring as part of our mitigation delivery plans.

### Resilience of our strategies

Weather is fundamental to how our water, wastewater and bioresources operations function so it is critical we make our assets, systems and strategies climate-ready. More frequent extreme weather events increase the risk of cascade impacts. Multiple different extreme weather events can occur in a single short time frame, such as storms Dudley, Eunice and Franklin in February 2022. Our ability to recognise the compound physical impacts to our system, and have various recovery tactics, is increasingly vital in effective climate change adaptation.

Our public Water Resources Management Plan (WRMP) and Drainage and Wastewater Management Plan (DWMP) are examples of where adaptive planning, incorporating climate change scenarios and advanced modelling, are used to shape our plans for the long term (25+ years) whilst staying aligned with our short-term needs. In these plans we describe how we have used complex models to test how resilient our services would be against a range of possible future climate change and demand scenarios (population growth and movement, economic trends and patterns of water use). Understanding these impacts allows us to adapt our plans to improve performance and resilience across key topic areas such as water supply, leakage, sewer flooding and pollution. For example, we have decided to invest to ensure certain drought options are always available, minimising the time it takes to bring them online during dry weather conditions. This will enable us to react more quickly and make supplies more resilient during dry weather. Together with reducing demand through leakage and water efficiency, this has reduced the likelihood of requiring drought permits and temporary use bans.

As well as targeted scenario analysis in WRMP and DWMP, we have developed three company-wide alternative scenarios for 2050, incorporating combinations of key factors that are both highly relevant and uncertain. These scenarios, named 'climate chaos', 'green guardianship' and 'public purpose', have associated metrics to define possible futures for water and wastewater services in the North West. The scenarios recognise climate change as one of the most critical factors shaping future services and use RCPs 2.6, 4.5 and 8.5 (GHG concentration pathways adopted by the Intergovernmental Panel for Climate Change) to describe how well climate change has been mitigated by society in each case. These different scenarios have provided a simple way to understand the interaction of multiple factors so we can enhance resilience, help manage future uncertainty and shape long-term decisions.

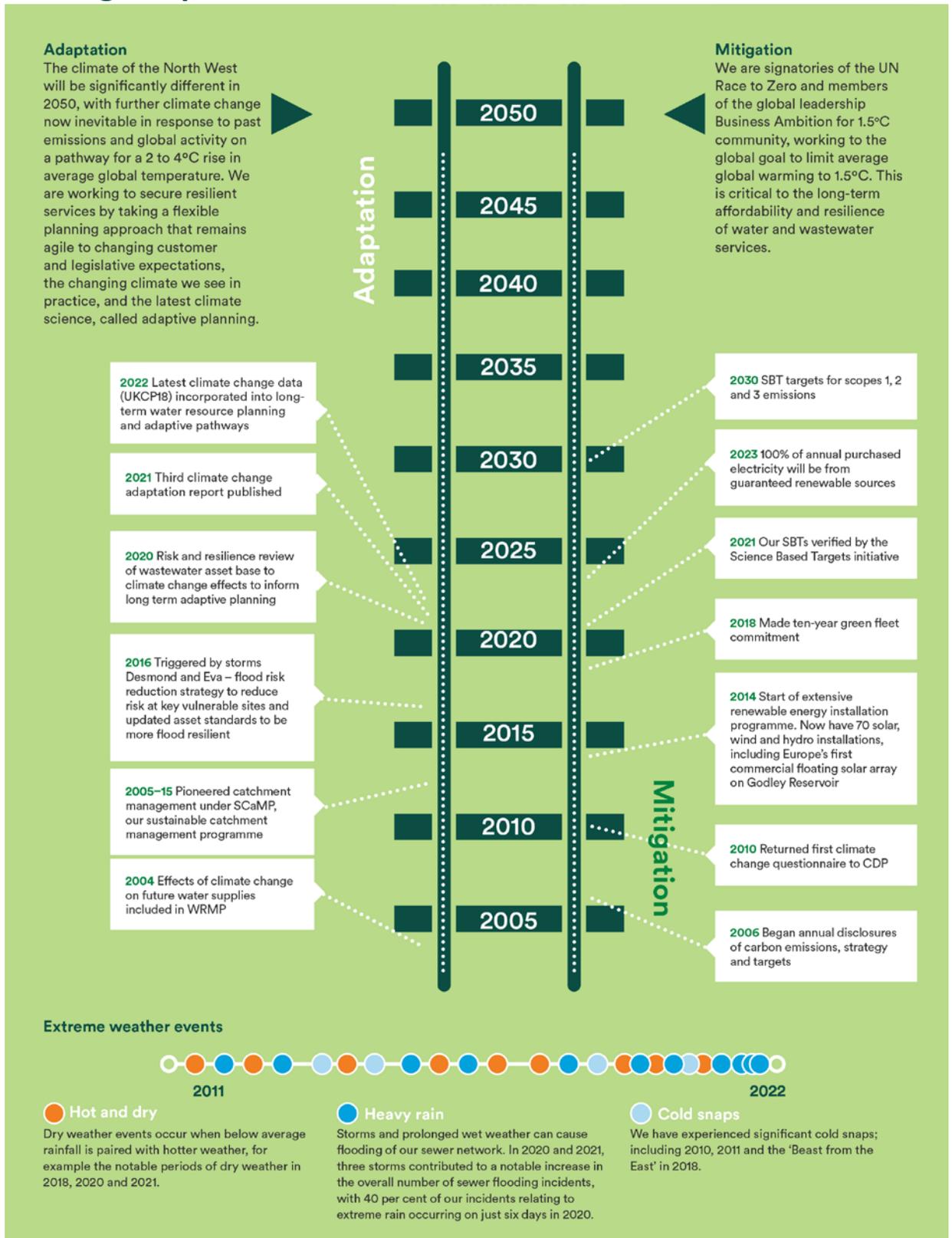
Note: The forward-looking scenario analyses above reflect uncertainties about the timing and magnitude of climate change in specific contexts and efforts to mitigate and adapt to climate change, which are without historical precedent. Scenarios are hypothetical constructs and are not intended or designed to represent a full description of the future or deliver precise outcomes; they are not forecasts or predictions, nor are they sensitivity analyses.

## Strategic report

### **Twin track approach to climate change**

We have been managing adaptation and mitigation for many years, aligning our approach to become more efficient and effective in our response. Our twin track approach to climate change is central to our purpose to provide great water and more for the North West.

# Strategic report



## Strategic report

### Metrics and targets

#### TCFD definition

The metrics and targets used to assess and manage climate-related risks and opportunities.

#### Progress this year

- The first UK water company to have targets verified by the SBTi, including for scope 3 emissions. Achieved our pledge 6.
- Delivered pledge 2: 100 per cent of electricity purchased has been renewable since October 2021.
- Reduced scope 1 and 2 emissions by 2.2 per cent (gross) and 3.5 per cent (net) compared to our baseline year 2019/20.
- Improved data collection and tracking of fuel use enabling targeted interventions.

#### Future focus

- Data improvements for scope 3 emissions with more supplier and product-based estimates, rather than spend-based.
- Work to validate our long-term net zero ambition to the new SBTi Net Zero Standard.
- Use BEIS carbon values as an internal carbon price in our planning for medium and long-term investments, including PR24 (e.g. for 2030 we use the low case value of £140/tCO<sub>2</sub>e).

#### Metrics to assess climate-related risks

Our vulnerability to climate-related risks is determined by two factors: the physical and transitional impacts we experience and the control measures we have put in place to manage the risks and realise opportunities. To manage our physical risks effectively we must track and understand patterns of weather, and weather events, and learn how they can affect us operationally. To do this we have been working with the Met Office to use both their short-term forecasts and longer-term projections, planning for up to a 4°C change in global temperature. We monitor factors relating to transitional risks, including energy pricing (of both fossil fuels and low carbon alternatives), carbon pricing (through purchasable credits, offsets and certificates), and the marketplace for the availability and cost of alternative fuelled vehicles, batteries and for emerging technologies to reduce process and fugitive emissions.

#### Metrics to manage climate-related risks

We manage our climate-related risks by putting in place controls such as those as set out on page 47 to 50 and in Appendix A.3 of the climate change adaptation report. The effectiveness of these controls is seen in our operational performance metrics. The following metrics are recognised as key to our resilience to a changing climate and are reported in the annual performance report:

- External flooding incidents;
- Hydraulic external flood risk resilience;
- Hydraulic internal flood risk resilience;
- Internal sewer flooding;
- Leakage;
- Per capita consumption;
- Raising customer awareness to reduce the risk of flooding;

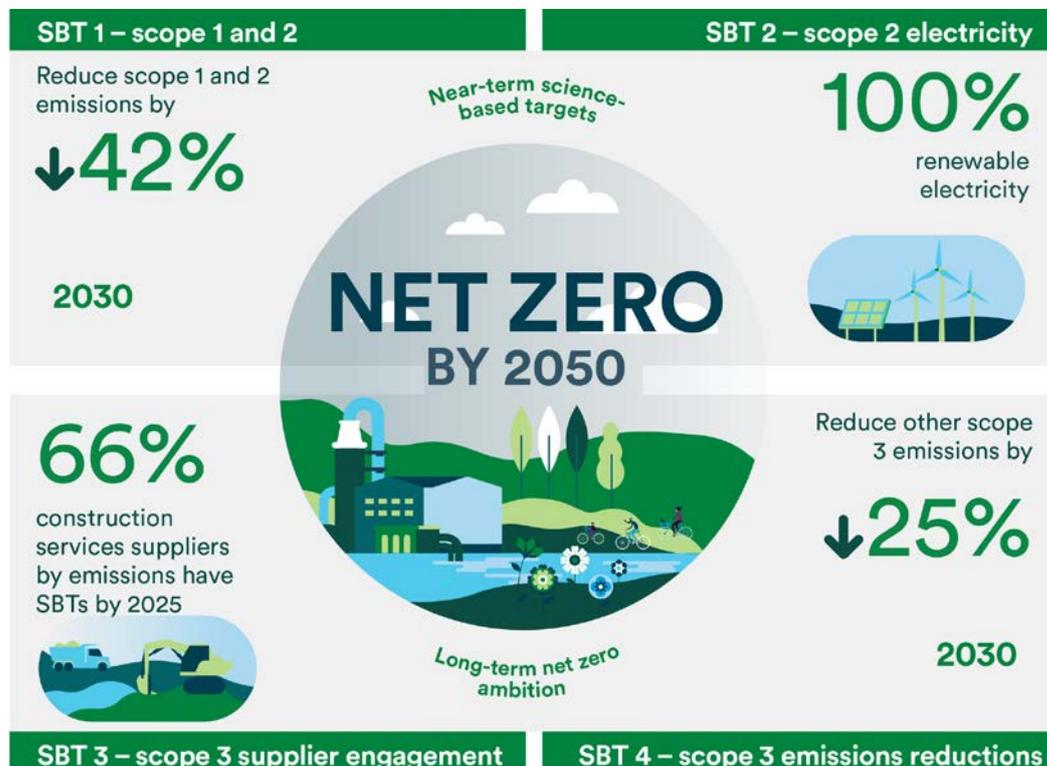
## Strategic report

- Areas of low water pressure;
- Risk of severe restrictions in a drought;
- Risk of sewer flooding in a storm;
- Sewer collapses;
- Unplanned outages;
- Water service resilience; and
- Water supply interruptions.

### Science-based targets

We have a strong track record of playing our part to mitigate climate change and have reduced scope 1 and 2 emissions by over 70 per cent since 2005/06, largely through our substantial investment in renewable power generation and green energy procurement. Our ambition and commitments are based on international guidance and climate science and we were delighted in July 2021 that our four near-term science-based targets were verified by the Science Based Targets initiative (SBTi). In October, the remainder of our purchased electricity switched to a renewable tariff backed by Renewable Energy Guarantees of Origin certificates, meaning that in the future 100 per cent of our purchased electricity will be from renewable sources enabling us to deliver on our carbon pledge and our SBT. The SBTi Net Zero Standard was launched in late 2021 and we have committed to validate our 2050 ambition to this standard when we revise and revalidate our near-term targets in advance of 2025.

As well as our company-specific science-based targets, we share the UK water sector ambition for key operational emissions to be net zero from 2030. Note that this target has a smaller scope than SBTi and allows use of purchased credits, using agreed offsetting principles.



## Strategic report

### Energy and carbon report

The Companies Act 2006 (Strategic Report and Directors' Reports) Regulations require us to publish this energy and carbon report applying the 2019 UK Government Environmental Reporting Guidelines, including the Streamlined Energy and Carbon Reporting Guidance (SECR).

We use the financial control approach so our energy and carbon accounting is aligned with the consolidated financial statements for United Utilities Group PLC for 1 April 2021 to 31 March 2022. This includes subsidiaries listed in section A8 on page 262 of the UUG Annual report and financial statements.

#### Energy strategy

Our energy management strategy has four objectives:

- Efficient use of energy;
- Maximising self-generation and direct supply opportunities;
- Reducing costs (through time of use); and
- Supply resilience to ensure we can deliver our services.

In 2021/22, we set a record for renewable energy generation of 210 GWh through focus on end-to-end performance of our bioresources operations, which produce electricity, heat and biomethane. We completed more solar installations during the year.

Each year we serve a growing population, driving increased energy use as we strive to achieve environmental performance targets. We seek to mitigate this through our energy management programme and in recent years have maintained consistent energy use in the face of these considerable upward pressures.

#### Energy efficiency actions taken

Our approach to energy efficiency is based on continuous improvement of:

- people – optimising ways of working;
- systems – improving visibility of use and analysis of data systems; and
- technology – targeted investment to remove technological inefficiencies.

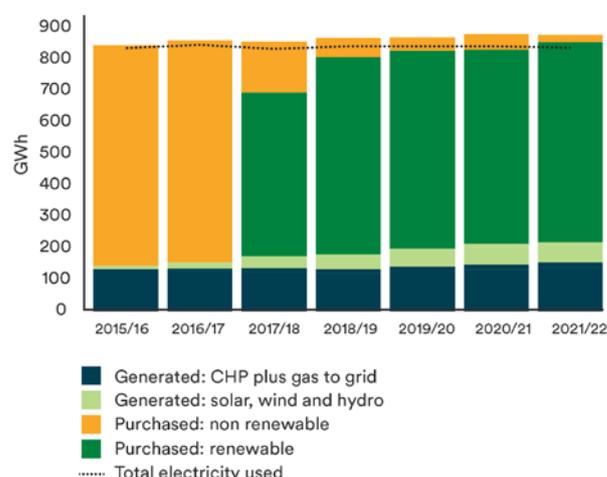
Our Energy Management Programme is now firmly established and working well after activities were restricted during COVID-19. The programme carries out site-based workshops and develops ways of working to optimise operations at sites and local area and is underpinned by e-learning packages and a comprehensive energy performance reporting and analysis capability.

To support reporting and analysis, we have invested over recent years to capture data from our fiscal meters and have installed thousands of sub-meters. The resulting data is used to identify opportunities, assess impacts and benefits of trials and maintain good performance. We are piloting analytics to support pump optimisation interventions.

We have a dedicated investment programme to implement targeted energy saving opportunities for existing operations and we focus on ensuring efficient outcomes from our capital programme. Examples of invest-to-save projects include pump optimisation, time-of-use actions and improved control of wastewater treatment.

## Strategic report

### Electricity use, purchase and self-generation (1)



(1) Electricity purchased plus self-generated is in excess of that used. The difference is what was exported to the grid.

	2021/22	2020/21	2019/20
	GWh	GWh	GWh
<b>Energy use</b>			
Electricity	<b>803.3</b>	807.3	802.3
Natural gas	<b>33.8</b>	40.0	38.3
Other fuels <sup>(1)</sup>	<b>123.1</b>	104.0	116.3
<b>Total energy use</b>	<b>960.2</b>	951.3	956.9
<b>Electricity purchased</b>			
Renewable tariff – half hourly <sup>(2)</sup>	<b>589.4</b>	591.4	602.9
Standard tariff – non-half hourly <sup>(3)</sup>	<b>22.3</b>	47.8	40.8
Renewable tariff – non-half hourly <sup>(3)</sup>	<b>21.6</b>	–	–
<b>Total electricity purchased</b>	<b>633.3</b>	639.2	643.7
<b>Renewable energy generated</b>			
CHP	<b>133.8</b>	127.6	121.5
Solar	<b>47.8</b>	50.7	42.6
Wind	<b>4.8</b>	5.3	5.7
Hydro	<b>7.2</b>	6.9	6.8
Biomethane <sup>(4)</sup>	<b>15.9</b>	14.8	14.2
<b>Total renewable energy generated</b>	<b>209.5</b>	205.3	190.8
<b>Renewable energy exported</b>			
Electricity <sup>(5)</sup>	<b>23.5</b>	22.4	18.1
Biomethane <sup>(4)</sup>	<b>15.9</b>	14.8	14.2
<b>Total renewable energy exported</b>	<b>39.4</b>	37.2	32.3

1. Other fuels includes liquid fuel purchased for processing and transport plus business mileage in private vehicles converted to GWh using 2021 UK Government GHG Conversion Factors for Company Reporting.
2. Half hourly supply has been on a renewable tariff with 0g CO<sub>2</sub>e/kWh emissions since June 2017.
3. Non half hourly metered supplies were on a standard tariff up to the end of September 2021. The emissions were 289g CO<sub>2</sub>e/kWh in 2019/20, 178g CO<sub>2</sub>e/kWh in 2020/21 and 188g CO<sub>2</sub>e/kWh in 2020/21. Non half hourly supplies moved to a new supplier on a 0g CO<sub>2</sub>e/kWh renewable tariff on 1 October 2021.
4. Biomethane generated and exported to grid is expressed as an electricity equivalent.
5. Electricity exported was generated by solar, wind and hydro.

## Strategic report

### Our approach to climate change

#### Greenhouse gas emissions

Our carbon footprint is calculated by estimating the individual greenhouse gases that result from all United Utilities' activities, converted into a carbon dioxide equivalent (tCO<sub>2</sub>e). We report scope 1, 2 and all relevant scope 3 emissions. Emissions have been estimated using the UK water industry Carbon Accounting Workbook v16 (CAW v16), the 2021 UK Government GHG conversion factors for company reporting and CEDA (Comprehensive Environmental Data Archive) factors. Our greenhouse gas inventory has been independently verified and certified by Toitu carbonreduce programme, as aligned to the GHG Protocol Corporate Accounting and Reporting Standard (2015) and the international carbon reporting standard ISO 14064, Part 1:2018.

#### United Utilities' greenhouse gas emissions intensity

As in previous years, we state our emissions as tonnes CO<sub>2</sub> equivalent per £million revenue. We include scope 1 and 2 (market-based) emissions only in this measure. We also report the regulated emissions kilograms CO<sub>2</sub> equivalent per megalitre treated (using the location-based method as calculated in the CAW v16), as these are common metrics for our industry.

##### Regulated emissions per megalitre water treated

2021/22	106.91
2020/21	118.51
2019/20	131.98

##### Regulated emissions per megalitre sewage treated

2021/22	144.21
2020/21	152.26
2019/20	168.51

##### Scope 1 and 2 emissions (gross) per £m revenue

2021/22	73.0
2020/21	78.0
2019/20	74.7

##### Scope 1 and 2 emissions (net) per £m revenue

2021/22	70.7
2020/21	75.7
2019/20	72.6

**Scope 1** - Emissions from activities we own or control, e.g. burning fossil fuels, wastewater and sludge processing.

**Scope 2** - Emissions from purchased electricity.

## Strategic report

		2021/22	2020/21	SBT baseline 2019/20
<b>SCOPE 1 &amp; 2 GREENHOUSE GAS EMISSIONS</b>		<b>tCO<sub>2</sub>e</b>	tCO <sub>2</sub> e	tCO <sub>2</sub> e
<b>Scope 1 Direct emissions</b>				
Direct emissions from burning of fossil fuels		19,207	17,371	15,247
Process and fugitive emissions from our treatment works – including refrigerants		96,020	98,569	96,186
Transport: company-owned or leased vehicles		16,507	16,634	15,739
<b>Total scope 1</b>		<b>131,735</b>	<b>132,574</b>	<b>127,172</b>
<b>Scope 2 Energy indirect emissions</b>				
Grid electricity purchased	Market-based <sup>(1)</sup>	4,201	8,507	11,789
	<b>Location-based<sup>(2)</sup></b>	<b>134,492</b>	<b>149,030</b>	<b>164,521</b>
<b>Total scope 2</b>	Market-based	4,201	8,507	11,789
	<b>Location-based</b>	<b>134,492</b>	<b>149,030</b>	<b>164,521</b>
<b>TOTAL SCOPE 1 &amp; 2 (GROSS)</b>	Market-based	135,936	141,082	138,961
	<b>Location-based</b>	<b>266,226</b>	<b>281,604</b>	<b>291,693</b>
<b>Avoided emissions</b>				
Renewable electricity exported		-4,317	-4,184	-3,979
Biomethane exported	Market-based <sup>(3)</sup>	0	0	0
	<b>Location-based</b>	<b>-10,283</b>	<b>-9,725</b>	<b>-9,302</b>
Green tariff electricity purchased	Market-based	n/a	n/a	n/a
	<b>Location-based</b>	<b>-128,604</b>	<b>-154,095</b>	<b>-136,644</b>
<b>Total avoided emissions</b>		<b>-14,600</b>	<b>-13,909</b>	<b>-13,281</b>
<b>TOTAL SCOPE 1 &amp; 2 (NET)</b>	Market-based <sup>(3)</sup>	131,619	136,897	134,982
	<b>Location-based</b>	<b>118,429</b>	<b>129,680</b>	<b>114,202</b>

1. Market-based figures use emission factors specific to the actual electricity purchased. If electricity is on a standard grid tariff they are calculated using factors from suppliers' public fuel mix disclosures, as shown in energy use table on page 59.

2. Location-based figures use average grid emissions to calculate electricity emissions and are shown in blue.

3. Exported biomethane sold with green gas certificates so has zero avoided emissions in market based accounts. Note in 2022 we have improved disclosure to report both location and market-based methods so the net totals for 2019/20 and 2020/21 have been restated.

### Scope 1 emissions

Wastewater and sludge processes cause 73 per cent of our scope 1 emissions as the gases released, nitrous oxide (N<sub>2</sub>O) and methane (CH<sub>4</sub>) have much greater global warming potentials than carbon dioxide (CO<sub>2</sub>).

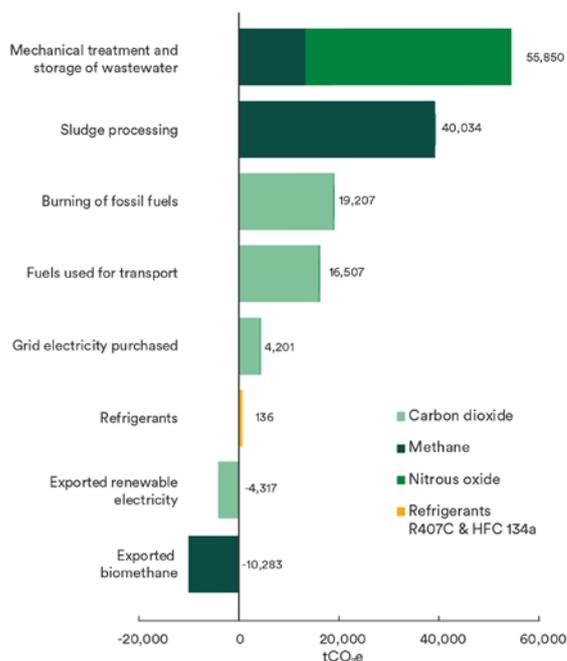
Our process emissions are currently estimated as a direct function of the amount of wastewater we treat. We are undertaking research with other UK water companies to better quantify these emissions from measured values and to find ways to reduce or capture those emissions for beneficial use.

We are investigating and trialling ways to reduce our use of fossil fuels, including for transport, through both efficiencies and use of alternative fuels.

## Strategic report

### Scope 2 emissions

Our market-based scope 2 emissions have halved this year because we switched our remaining non-renewable purchased electricity to a renewable tariff in October 2021. Next year these emissions will be negligible.



**Scope 3** - Emissions from our value chain, e.g. sludge disposal, business travel and products and services.

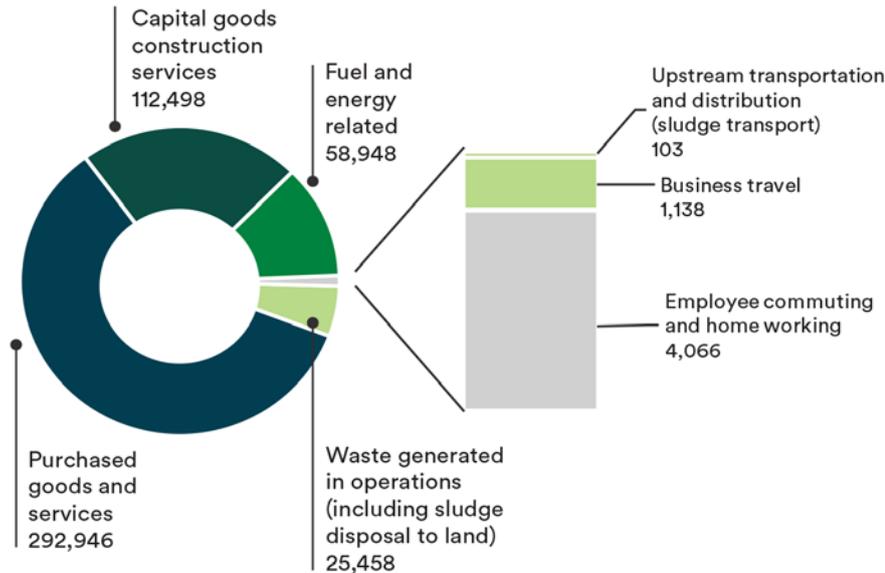
	SBT baseline		
	2021/22	2020/21	2019/20
<b>SCOPE 3 GREENHOUSE GAS EMISSIONS</b>	<b>tCO<sub>2</sub>e</b>	<b>tCO<sub>2</sub>e</b>	<b>tCO<sub>2</sub>e</b>
<b>Scope 3 Other indirect emissions</b>			
Category 1: Purchased goods and services <sup>(1)</sup>	292,946	271,871	213,442
Category 2: Capital goods <sup>(1)</sup>	112,498	95,968	128,286
Category 3: Fuel and energy-related emissions	58,948	42,599	45,262
Category 4: Upstream transportation and distribution (sludge transport)	103	1,119	3,374
Category 5: Waste generated in operations (including sludge disposal to land)	25,458	26,333	27,936
Category 6: Business travel (public transport, private vehicles and hotel accommodation)	1,138	1,226	3,508
Category 7: Employee commuting and home working	4,066	4,108	4,231
<b>TOTAL SCOPE 3</b>	<b>495,145</b>	<b>443,224</b>	<b>426,039</b>
<b>Scope 3 SBT measure (excluding category 2)</b>	<b>382,647</b>	<b>347,256</b>	<b>297,753</b>

1. For Category 1 and 2 we use CEDA (an EEIO (environmentally-extended input-output) inventory) to estimate emissions. Other categories use actual activity records and UK government conversion factors.

## Strategic report

### Scope 3 emissions

Like most organisations, most of our scope 3 emissions are in GHG Protocol category 1 (products and services) and category 2 (capital goods); the latter being those provided by our construction services suppliers. We currently calculate category 1 and 2 emissions using records of the amount we have spent. This provides an indicative estimate but does not show the GHG impact of management choices, instead fluctuating with the scale of our investment programme. This can be seen in our increase in reported emissions this year compared to last. We are working internally and with supply chain partners to enhance relevant data and systems so that we can calculate these emissions based on types and quantities of materials used, thereby showing the full impact of our management choices.



## Our approach to Task Force on Nature-related Financial Disclosures (TNFD)

Launching in 2023, the Task Force on Nature-related Financial Disclosure (TNFD) aims to provide a risk and disclosure framework for organisations interacting with the natural environment. It will adopt a four-pillar approach similar to that of TCFD covering governance, strategy, risk management, metrics and targets.

### Overview

We are dependent upon, and impact, the natural environment from the quality and quantity of water we abstract for treatment and supply of drinking water, through to treated wastewater we return to rivers and biosolids we recycle to land. We are responsible for over 56,000 hectares of water catchment land.

Given the pressures from climate change and population growth on the natural environment, we do not underestimate the contribution we can make in restoring healthy and resilient ecosystems. We need to work collaboratively with like-minded organisations to deliver nature-based solutions as these offer many benefits including carbon sequestration, cleaner water and improved biodiversity. This is at the heart of our Catchment Systems Thinking Approach (CaST).

We've joined the TNFD forum as a contributing member to help us as we become an early adopter of TNFD reporting.

## Strategic report

### Governance

Our interactions with the natural environment are broad and complex. Overall accountability rests with executive management who strive to comply with the legal and regulatory requirements as set out in our environmental policy. Matters are regularly reviewed at the board's corporate responsibility committee. The environmental advisory group is a management group with a remit to ensure the delivery of the environmental policy commitments including nature-related strategies (e.g. land, catchment, clean air, plastics, waste, water quality, water resources, and natural capital). Governance for these strategies is through cross-departmental working groups comprised of subject matter experts and decision makers to drive implementation. Governance around investment in nature-related risks and opportunities is applied as part of our Internal Control Manual.

### Strategy

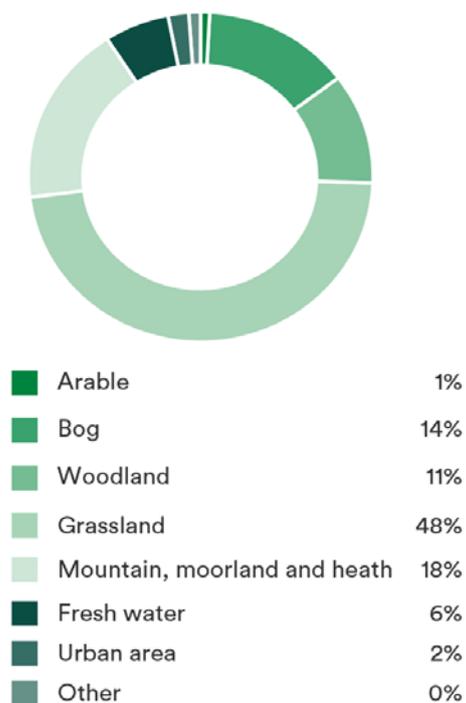
Protecting and enhancing the natural environment is a key part of the 'and more' of our purpose. We protect the environment through maintaining compliance and meeting regulatory requirements. We enhance by driving performance, adopting best asset management practices, and investing in nature-based and other environmental solutions. Our environmental policy is underpinned by a framework of strategies and long term plans in response to nature-related risks and opportunities. Some of these plans are statutory requirements, such as the Water Resources Management Plan, and are reviewed every five years as part of the price review process. Our company business plan details the delivery plans for the five years up to 2025.

Our CaST approach enables individual project decisions to be made in the context of the catchment, or system, in which they are situated. This encourages goals to be set in a collaborative way, maximising the benefits that can be achieved and delivering ecosystem resilience through improvements to water quality, flood risk reduction, access to green space, nature recovery, and carbon sequestration.

Much of the land that we own is designated as Sites of Special Scientific Interest (SSSI), which indicates the importance of the habitat for biodiversity. Ninety-four per cent of SSSIs on our land now meet favourable or unfavourable recovering condition status, in part because we pioneered the use of nature-based solutions to address raw water quality when we started our SCaMP programme in 2005. Designated habitats include blanket bog, moorland and heath and are home to many important species. We recognise our role as a steward of our land and make decisions based on the benefits and impacts our operations have on the natural environment. The land we own is made up of different land cover types, such as grassland and woodland.

## Strategic report

### Land cover types across our land holding



Innovation is embedded in our approach to solving environmental challenges. By understanding and engaging in relevant research we can integrate new technologies and practices to drive environmental enhancements.

### Risk management

Many key risks in our risk management assessments are linked to the natural environment. The risk breakdown structure that underpins our operational risk assessment framework includes consequences related to biodiversity, flooding, drought, water quality, recreational access, carbon storage, air quality and waste. Through our longer-term planning processes, we model a range of environmental risks such as a one in 100-year storm or drought and take appropriate action to include mitigation options in the plans. Read more about our risk and resilience framework on pages 66 to 68.

There is a close link between nature and climate change with many pressures on the natural environment becoming more acute as the climate changes. Our climate change adaptation report highlights key physical risks related to the natural environment. Two of our carbon pledges – on tree planting and peatland restoration – are intrinsically linked to the natural environment.

In 2022, we published a discussion document jointly with The Rivers Trust on barriers to nature-based solutions, entitled PR24: Unlocking nature-based solutions to deliver greater value. This identifies some of the key risks associated with the transition to a nature-positive economy and recommendations for collaborative working with the Government and others to address these barriers. We are working with regulators, other water companies and non-governmental organisations to take forward proposals to address these risks.

### Metrics and targets

To measure our performance we demonstrate delivery against contributing targets from a number of statutory requirements such as the condition of protected sites, biodiversity net gain, environmental performance and supporting strategies. Our long-term nature-based targets align with government expectations such as achieving 75 per cent favourable condition for SSSI locations by 2042. We are committed to improving surface, groundwater and bathing water quality in the immediate term and

## Strategic report

beyond. We will input to the consultation on the Environment Act water targets in 2022 as these will be an important mechanism to drive environmental improvement and meet the objectives for the water environment in the Government's 25-year environment plan.

We are the only water company to set a natural capital outcome delivery incentive in our business plan for 2020–25. This is measured by demonstrating additional value created through ecosystem services for customers and the environment. We achieve this by implementing nature-based solutions where they offer best value compared against a hard-engineered solution (e.g. to improve water quality). Read more about our environmental performance on pages 64 to 67 of the UUG Annual report and financial statements.

We were a key contributor to the North West's first natural capital account developed in collaboration with many regional organisations. By considering this baseline value, we can benchmark the impact of future changes to our natural assets and quantify improvements. It is helping to understand how valuable the region's natural capital assets are. In 2022, we will update our own corporate natural capital account as part of a five-yearly review cycle and we will report on this next year.

### Next steps

In March 2022, the TNFD unveiled the first version of its nature-related risk-management and disclosure framework. The framework, which will be modified over the next 18 months, is designed to align with the International Sustainability Standards Board, which was officially unveiled at COP26. Working with the Taskforce we will continue to develop how we disclose nature-related information.

## Our risk management

### Our risk and resilience framework

We have a robust risk and resilience framework for the identification, assessment and mitigation of risk.

### Our approach to risk and resilience

Successful management of risks and uncertainties enables us to deliver on our purpose to provide great water and more for the North West, and be more resilient across our corporate, financial and operational structures. A key objective of our approach is to support the sustainable achievement of the strategic themes that underpin our vision to be the best UK water and wastewater company delivering:

- the best service to customers;
- at the lowest sustainable cost; and
- in a responsible manner.

Our risk and resilience framework provides the foundation for the business to anticipate threats to delivering an effective service in these challenging times, and to respond and recover effectively when risks materialise. Key components of the framework include:

- an embedded group-wide risk management process, which is aligned to ISO 31000:2018 risk management guidelines;
- a board-led approach to risk appetite, based on strategic goals;
- a strong and well-established governance structure giving the board oversight of the nature and extent of risks the group faces, as well as the effectiveness of risk management processes and controls; and
- a portfolio of policies, procedures, guidance and training to enable consistent, group-wide participation by our people.

## Strategic report

Continuous improvement is a key feature of the framework, which incorporates a maturity assessment model to identify areas to enhance. Based on risk management capabilities relative to five levels of maturity, a recent assessment has supported the development of a road map of improvements. This includes further enhancement to risk appetite and tolerance, greater focus and analysis of cross-cutting themes and improved escalation of data from operational risk management systems.

### Risk appetite and tolerance

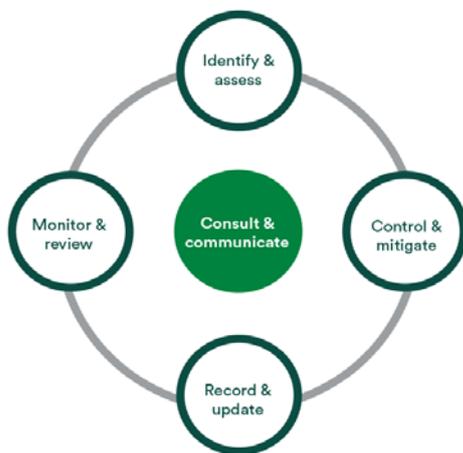
Focused on supporting decision-making, the risk appetite and tolerance framework consists of a package of measures. The General Risk Appetite represents financial limits against which event-based risks are compared at each full and half-year assessment and reporting cycle. In parallel are a series of strategic statements which align directly to the principal risks (see pages 72 to 82). Each statement reflects the strategic intent, strategic theme, relevant stakeholders and governance, but fundamentally emphasises the attitude to risk taking and control relative to four descriptors:

- Averse: A strong opposition to accept risk within business strategy or operational activity.
- Prudent: A reluctance to accept risk within business strategy or operational activity, but careful acceptance within tight boundaries.
- Moderate: Willingness to accept risk with regard to business strategy or operational activity provided this is within reasonable limits.
- Accepting: Willingness to accept risk with regard to business strategy or operational activity.

As a regulated company providing essential public services none of the principal risks have risk accepting as a strategic direction or approach.

Underpinning each strategic statement, and currently under development, are a series of more tangible, tactical statements with specific levels and limits.

### How we identify and assess risk



We have a number of mechanisms in place to identify risk. These include a risk universe, cross-business horizon scanning forums, consultation with third parties and comparison with National Risk Registers.

Each risk is event based and is sponsored by a senior manager who is responsible for the analysis of the corresponding causal factors, consequences and the control effectiveness, taking account of both the internal and external business environment. This process quantifies the likelihood of the event occurring and the full range of potential impacts from a minimum (best case) to a maximum (worst case). Comparing this position against the desired target state, in combination with the strengths, weaknesses and gaps of the control environment, supports the decisions for further mitigation as appropriate. This ongoing analysis culminates in the biannual business unit risk assessment (BURA) which forms part of the governance and reporting process (as outlined opposite) to ensure consistency of approach and a true reflection of the risk facing the company. It also serves to calibrate the most significant risks from a financial and reputational context and to assess how these relate to our risk appetite.

## Strategic report

### Governance and reporting process

The board ensures that its oversight of risk remains effective, and in compliance with the UK Corporate Governance Code, through a number of established reporting routes.

Twice yearly the board receives an extensive update on the risk profile as part of the full and half-year reporting cycle. This provides an overview of the nature and extent of risk exposure in the context of the group's principal risks (as detailed on pages 72 to 82), and emphasises the most significant event-based risks (summarised on pages 82 to 85) in both their current state relative to the risk appetite, and target state of acceptable exposure. The board is also advised of new and emerging risks (see pages 87 to 88). In addition to the biannual risk reporting, specific risk topics are reported to the board to support decision-making. The board is, therefore, able to:

- make decisions on the level of risk it is prepared to manage relative to risk appetite and tolerance in order to deliver on the group's strategy;
- engage with the business to ensure appropriate controls and mitigation are in place, and test the appropriateness of plans;
- report externally on the long-term viability of the company in an informed manner; and
- monitor and review the effectiveness of risk management procedures and internal control systems.

Risk-specific governance and steering groups manage ongoing individual risks. The operational risk and resilience board provides oversight of asset and operational process, risk and resilience capability, escalates risks and issues to the group audit and risk board (GARB) and contributes to the BURA process.

The executive-led GARB focuses on: the adequacy, effectiveness and performance of governance processes; risk management and internal control; monitoring compliance and assurance activities; identification of emerging themes and trends; and resilience across the group.

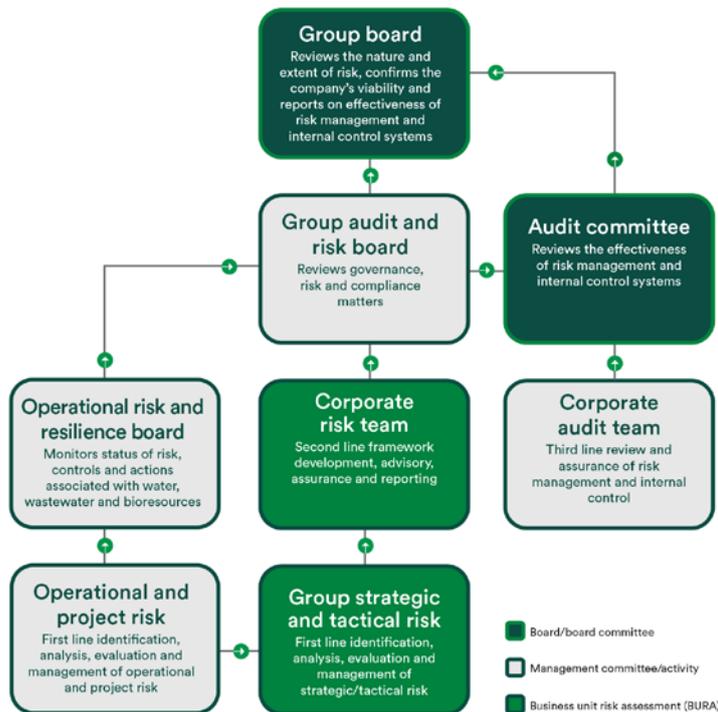
The audit committee is also a fundamental component of the governance structure. Supported by company secretariat and the corporate audit teams, the audit committee reviews the effectiveness of risk management and internal controls before these are agreed by the board.

### Risk profile

The business risk profile is based on the value chain of the company, with the ten principal risks representing inherent risk areas (primary and supportive) where value can be gained, preserved or lost relative to the performance, future prospects or reputation of the company. Underpinning the principal risks, the profile consists of approximately 100 event-based risks, each of which is allocated to one of the ten inherent risk areas based on the context of the event, enabling the company to consider interdependency and correlation of common themes (see pages 70 to 71) and control effectiveness.

## Strategic report

### The governance and reporting process



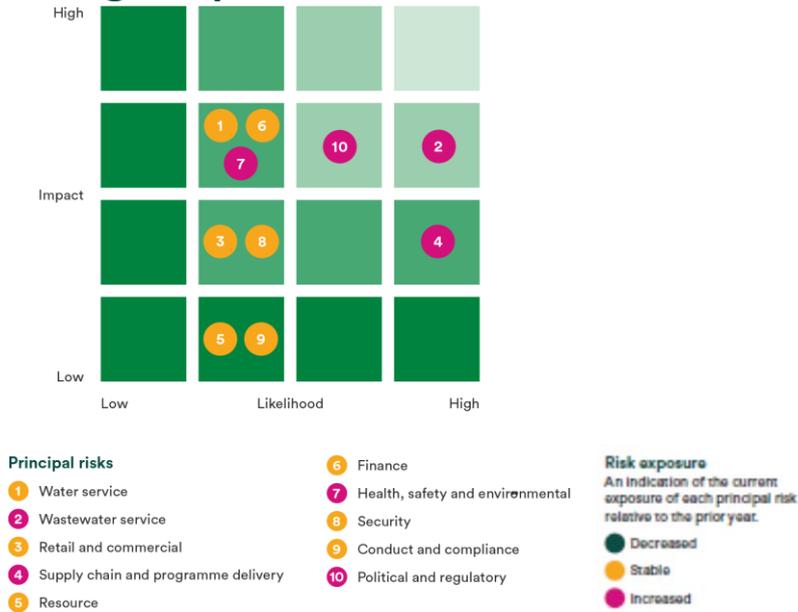
### Principal risk heat map

The heat map provides an indicative only view of the current risk exposure (likelihood of occurrence and most likely impact) of each of the principal risks relative to each other.

Six of the principal risks have remained relatively stable in the last twelve months with the following four demonstrating an increase in exposure:

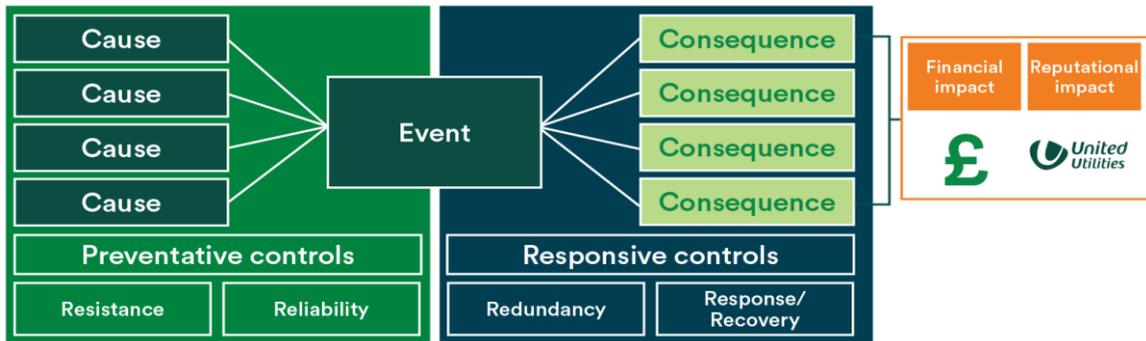
- Wastewater service associated with change in legislation
- Supply chain and programme delivery due to economic conditions
- Health, safety and environmental due to the uncertainty of achieving the net zero carbon commitments
- Political and regulatory due to the challenge of delivering customer and environmental improvements whilst maintaining fair value to customers

## Strategic report



### Common themes

As illustrated in the bow-tie diagram below, each of the event-based risks has multiple causes and consequences, which in turn lead to financial and/or reputational impact. Preventative and responsive controls, which incorporate the four components of resilience (resistance; reliability; redundancy; and response/recovery), are applied to reduce the likelihood of the event occurring and limit the impact if the event were to materialise. New and emerging circumstances in respect of causes, consequences and controls make the profile multifaceted and dynamic. Analysis of the profile highlights common themes, notably associated with the causes and consequences. These common themes can then be considered more holistically, which combined with the analysis of the strengths, weaknesses, gaps and interdependency of control across the business, enables a more integrated approach to risk mitigation.



### Common causal themes

The event-based risks include multiple causal factors, which individually or in combination, could trigger the risk event to occur. Categorisation illustrates six common causal themes:

- Extreme weather/climate change:** In the majority of cases our water resources, asset base and operations can cope with extreme weather conditions, although these can become overwhelmed in intense situations. Climate change projections highlight increased temperatures, rainfall, wind and more frequent extreme variations in weather patterns. This means that climate change remains a key focus for us, because of its impact on our capacity and capability for service delivery, and because of the effect on the environment that we strive to protect and enhance. We are committed to the principles set by the Financial Stability Board’s Task Force on Climate-related Financial Disclosures (TCFD) – see pages 41 to 62.

## Strategic report

- **Demographic changes:** Demographic changes, including population growth and evolving age profiles, can impact the capacity and capability of water and wastewater treatment and network assets; can affect demand on water resources; and increase uncertainty in relation to pension obligations.
- **Legislative and regulatory change:** Changes in legislation and/or regulation can have implications for the business model, asset base and ways of working. For example: post-Brexit changes in law bring an element of uncertainty; and the introduction of competition, while positive to customers and markets, can affect ongoing revenue and the asset base.
- **Economic conditions:** Macro events can have multiple financial implications, including: lower revenue; increased bad debt; increased operational cost; increased cost of borrowing; and a reduction in the Regulatory Capital Value. The events can also impact the wider supply chain with knock-on effects to our service delivery and cost to serve.
- **Asset health:** General use, exposure to natural hazards, pressure and load all contribute to the deterioration of assets. In addition, other factors such as technological obsolescence and operating assets beyond their optimal capacity to cope with increased demand (population growth and/or climate change) also affect asset health. Ageing assets, therefore, provide an underlying and cross-business risk and uncertainty both to efficiency and for the long-term resilience of asset integrity and the associated service capability.
- **Culture:** Embedded through processes, reward mechanisms, values and behaviours, corporate culture is important to maintain high performance and cuts across the majority of risks in the profile. In an increasingly challenging business environment, our focus is to continue to embed a culture of innovation, customer service and behaving in a responsible manner at the same time as being open and transparent.

### Common consequence themes

Each consequence is analysed for the financial and reputational implications relative to multiple stakeholders. Categorisation of the consequences illustrates four common impact themes:

- **Customers:** Customers are impacted through our service offering, the quality of their experience when dealing with us, and how our operational and capital schemes affect them in the community.
- **Environment:** Our assets, operations and capital programmes can have a significant impact on the environment in both rural and urban settings. As a major land owner and operator of a large fleet of vehicles, the way we manage these also has environmental implications.
- **Investors:** The vast majority of risks in the profile have financial implications that could affect shareholder investment in the short and long term. Reputational impact associated with ethics, environmental protection and efficiency is also relevant for investors' interest in the company.
- **Employees:** Our employees are fundamental to delivering our service requirements as well as our strategic objectives. Equally, our employees can be affected by multiple risks across the business, but primarily in relation to employment and health, safety and wellbeing risks.

## Strategic report

# Our principal risks

### 1 Water service

#### Strategic theme

The best service to customers

#### Sponsor(s)

Water, wastewater and digital services director

#### Principal risk description

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.

#### Causal factors themes (Drivers/influences of risk)

- Climate change
- Demographic change
- Legal and regulatory change
- Asset health

#### Consequence themes and stakeholder groups

- Customers
- Environment
- Investors

#### Appetite and tolerance

Water - Averse

#### Control/mitigation

- Strict quality controls and sampling regime
- Physical and chemical treatment with automation
- Cleaning, maintenance and replacement of assets
- Water resources and production planning
- Pressure/flow management and leak detection
- Integrated network and response capability

#### Top five event-based business risks (\*most significant group risks)

- Failure of Haweswater Aqueduct\*
- Water sufficiency\*
- Failure to treat water
- Failure of the distribution system (leakage)
- Dam failure\*

## Strategic report

### 2 Wastewater service

#### Strategic theme

The best service to customers

#### Sponsor(s)

Water, wastewater and digital services director

#### Principal risk description

The failure to remove, treat and return water to the environment and recycle sludge to land

#### Causal factors themes (Drivers/influences of risk)

- Climate change
- Demographic change
- Legal and regulatory change
- Asset health

#### Consequence themes and stakeholder groups

- Customers
- Environment
- Investors

#### Appetite and tolerance

Wastewater - Prudent

Bioresources - Moderate

#### Control/mitigation

- Physical and chemical treatment
- Odour management systems
- Drainage and wastewater management plans
- Wastewater network operating model
- Cleaning, maintenance and replacement of assets
- Customer campaigns

#### Top five event-based business risks (\*most significant group risks)

- Wastewater network failure (sewer flooding)\*
- Failure to treat sludge\*
- Recycling biosolids to agriculture\*
- Wastewater treatment (permits)
- Mersey Valley Sludge Pipeline

## Strategic report

### 3 Retail and commercial

#### Strategic theme

At the lowest sustainable cost

#### Sponsor(s)

- Customer and people director
- General counsel and company secretary

#### Principal risk description

Failing to provide good and fair service to domestic customers and third-party retailers or a failure of or issue in relation to non-regulated interests

#### Causal factors themes (Drivers/influences of risk)

- Legal and regulatory change
- Economic conditions
- Asset health
- Culture

#### Consequence themes and stakeholder groups

- Customers
- Investors

#### Appetite and tolerance

Retail - Prudent

Commercial - Moderate

#### Control/mitigation

- Customer-focused initiatives
- Best practice collection techniques
- Customer segmentation
- Priority Services scheme
- Data management and data sharing
- Non-regulated operation governance

#### Top five event-based business risks (\*most significant group risks)

- Customer experience
- Cash collection
- Billing accuracy
- Wholesale revenue collection
- Developer services

## Strategic report

### 4 Supply chain and programme delivery

#### Strategic theme

At the lowest sustainable cost

#### Sponsor(s)

Commercial, capital delivery and engineering director

#### Principal risk description

The potential ineffective delivery of capital, operational or functional processes/programmes including change.

#### Causal factors themes (Drivers/influences of risk)

- Legal and regulatory change
- Economic conditions
- Culture

#### Consequence themes and stakeholder groups

- Communities
- Customers
- Environment
- Investors
- Suppliers

#### Appetite and tolerance

Supply chain - Prudent

Programme delivery - Moderate

#### Control/mitigation

- Category management
- Supplier relationship management
- Capital, change and operational programme management
- Portfolio, programme and project risk management

#### Top five event-based business risks (\*most significant group risks)

- Price volatility\*
- Unfunded developer programmes
- Security of the supply chain
- Dispute with supplier
- Capital delivery programme

## Strategic report

### 5 Resource

#### Strategic theme

At the lowest sustainable cost

#### Sponsor(s)

- Customer and people director
- Health, safety and wellbeing and estate services director
- Water, wastewater and digital services director

#### Principal risk description

The potential failure to provide appropriate resources (human, technological or physical) required to support business activity.

#### Causal factors themes (Drivers/influences of risk)

- Climate change
- Legal and regulatory change
- Economic conditions
- Asset health
- Culture

#### Consequence themes and stakeholder groups

- Customers
- Employees
- Investors

#### Appetite and tolerance

Resource - Moderate

#### Control/mitigation

- Adoption of effective technology
- Multiple communication channels
- Training and personal development
- Talent, apprentice and graduate schemes
- Change programmes and innovative strategies
- Maintenance, replacement or renovation of assets

#### Top five event-based business risks (\*most significant group risks)

- Land management
- IT asset support
- Loss or failure of NIS systems
- Business critical data
- Employee relations

## Strategic report

### 6 Finance

#### Strategic theme

At the lowest sustainable cost

#### Sponsor(s)

Chief financial officer

#### Principal risk description

The potential inability to finance the business appropriately.

#### Causal factors themes (Drivers/influences of risk)

- Demographic change
- Legal and regulatory change
- Economic conditions
- Asset health

#### Consequence themes and stakeholder groups

- Customers
- Employees
- Investors

#### Appetite and tolerance

Finance - Prudent

#### Control/mitigation

- Long-term refinancing
- Liquidity reserves
- Counterparty credit exposure and settlement limits
- Hedging strategies
- Sensitivity analysis
- Monitoring of the markets

#### Top five event-based business risks (\*most significant group risks)

- Credit ratings\*
- Pension scheme funding deficit\*
- Financial outperformance\*
- Tax efficiency/fair share\*
- Totex efficiency challenge\*

## Strategic report

### 7 Health, safety and environmental

#### Strategic theme

In a responsible manner

#### Sponsor(s)

- Environment, planning and innovation director
- Health, safety and wellbeing and estate services director

#### Principal risk description

The potential harm to employees, contractors, the public or the environment.

#### Causal factors themes (Drivers/influences of risk)

- Climate change
- Asset health
- Culture

#### Consequence themes and stakeholder groups

- Communities
- Employees
- Environment
- Investors

#### Appetite and tolerance

Health, safety and wellbeing - Averse

Environment - Averse

#### Control/mitigation

- Strong governance and management systems
- Certification to ISO 45001 and ISO 14001
- Benchmarking, auditing and inspections
- Targeted engagement and improvement programmes
- Carbon reduction initiatives
- Self-generation of energy

#### Top five event-based business risks (\*most significant group risks)

- Carbon commitments\*
- Disease pandemic\*
- Occupational health exposure
- Minor injuries
- Process safety (bioresources and wastewater)

## Strategic report

### 8 Security

#### Strategic theme

In a responsible manner

#### Sponsor(s)

General counsel and company secretary

#### Principal risk description

The potential for malicious activity (physical or technological) against people, assets or operations.

#### Causal factors themes (Drivers/influences of risk)

- Economic conditions
- Asset health
- Culture

#### Consequence themes and stakeholder groups

- Communities
- Customers
- Employees
- Investors

#### Appetite and tolerance

CNI and SEMD - Averse

Other - Prudent

#### Control/mitigation

- Physical and technological security measures
- Strong governance, inspections and audits
- Security authority liaison and NIS compliance
- System and network integration
- Business continuity and disaster recovery
- Insurance

#### Top five event-based business risks (\*most significant group risks)

- Cyber\*
- Terrorism\*
- Criminality
- Fraud
- Data protection

## Strategic report

### 9 Conduct and compliance

#### Strategic theme

In a responsible manner

#### Sponsor(s)

- Corporate affairs director
- General counsel and company secretary

#### Principal risk description

The failure to adopt or apply ethical standards, or to comply with legal and regulatory obligations and responsibilities.

#### Causal factors themes (Drivers/influences of risk)

- Climate change
- Demographic change
- Legal and regulatory change
- Economic conditions
- Asset health
- Culture

#### Consequence themes and stakeholder groups

- Communities
- Customers
- Employees
- Environment
- Investors
- Suppliers

#### Appetite and tolerance

Legislation - Averse

Other - Prudent

#### Control/mitigation

- Ethical supply chain, diversity and inclusivity policies
- Data classification and levels of authorisation
- Stakeholder engagement activities
- Audits and peer reviews
- Governance, risk assessment and horizon scanning
- Brand comparisons and dashboard of culture metrics

#### Top five event-based business risks (\*most significant group risks)

- Water Plus
- Bribery
- Non-regulated assets

## Strategic report

- Procurement compliance
- Corporate governance and listing rules compliance

### 10 Political and regulatory

#### Strategic theme

The best service to customers

#### Sponsor(s)

- Corporate affairs director
- General counsel and company secretary
- Strategy, policy and regulation director

#### Principal risk description

Developments connected with the political, regulatory and legislative environment

#### Causal factors themes (Drivers/influences of risk)

- Legal and regulatory change
- Economic conditions

#### Consequence themes and stakeholder groups

- Customers
- Employees
- Environment
- Investors

#### Appetite and tolerance

Appetite or tolerance cannot be determined due to no genuine choice or control

#### Control/mitigation

- Consultation with government and regulators
- Communication with customers

#### Top five event-based business risks (\*most significant group risks)

- Price Review 2024 outcome\*
- Upstream competition (bioresources)
- DPC exit – HARP
- ASHE index
- Upstream competition (water resource)

## Strategic report

### Notes

1. Principal risks: Based on the value chain of the company, principal risks represent inherent areas where value can be gained, preserved or lost. Water, wastewater (including biosources) and retail and commercial areas are the primary activities, with all other areas as supportive/contributing activities.
2. Appetite and tolerance: Averse: A strong opposition to accept risk within business strategy or operational activity. Prudent: A reluctance to accept risk within business strategy or operational activity, but careful acceptance within tight boundaries. Moderate: Willingness to accept risk with regard to business strategy or operational activity provided this is within reasonable limits. Accepting: Willingness to accept risk with regard to business strategy or operational activity. (NB As a regulated company providing essential public services none of the principal risks have risk accepting as a strategic direction or approach).

## The company's most significant event-based risks

The most significant event-based risks represent the ten highest-ranked risks by exposure (likelihood of occurrence of the event multiplied by the most likely financial impact) and those risks which have been assessed as having a significantly high impact, but low likelihood. Depending on the circumstances, financial impacts will include loss of revenue, additional or extra cost, fines, regulatory penalties and compensation. Reputational impact relative to our multiple stakeholders is also assessed, reported and considered as part of the mitigation.

Summarised below are the top ten ranking risks (1–10), and those assessed as having high impact, but low likelihood (A–F):

### 1. Price Review 2024 outcome

**Risk exposure:** This risk focuses on the capacity and capability to develop a business plan that creates value for customers, communities, and the environment that is sustainable and resilient for the long term relative to the unique characteristics of the region we serve, in light of multiple influencing factors – notably changing demographics, climate change and asset health.

**Control/mitigation:** We have established cross-cutting work streams and theme owners to identify the products and evidence required for the submission and we will maintain a close dialogue with Ofwat throughout the process.

**Assurance:** Extensive customer research and several external providers have been commissioned for technical optioneering. Second line assurance is provided through a dedicated price review team and a PR24 programme board. An internal audit is scheduled and external assurance is currently under procurement.

### 2. Failure of the Haweswater Aqueduct

**Risk exposure:** The Haweswater Aqueduct is a key asset with current low resilience due to deterioration, with failure potentially resulting in water quality issues and/or supply interruptions to a large proportion of the United Utilities customer base.

**Control/mitigation:** A capital project to replace the tunnel sections of the aqueduct has already commenced with the completion in November 2020 of one section. The remaining sections are due to be replaced as part of Haweswater Aqueduct Resilience Programme (HARP) by 2029.

**Assurance:** Technical and geological advice and modelling have been sought throughout the programme development, with second line assurance including engineering technical governance. Independent assurance is provided by cyclical internal audits and external assurance over the competitively appointed provider.

### 3. Wastewater network failure (sewer flooding)

**Risk exposure:** Equipment failure, collapses/bursts or inadequate hydraulic/operational capacity to cope with extreme weather and population growth, resulting in sewer flooding.

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**Control/mitigation:** Preventative maintenance and inspection regimes, customer campaigns and sewer rehabilitation programmes.

**Assurance:** Second line assurance provided by wholesale assurance, engineering technical governance and flood review panel. Subject to regular internal audits and external assurance of regulatory reporting.

### 4. Cyber

**Risk exposure:** Data and technology assets compromised due to malicious or accidental activity, leading to a major impact to key business processes and operations.

**Control/mitigation:** Multiple layers of control, including a secure perimeter, segmented internal network zones, access controls, constant monitoring and forensic response capability.

**Assurance:** Security stance reflects multiple sources of threat intelligence. The security steering group provides second line assurance, with independent assurance provided by cyclical internal audits and various technical audits by external specialists.

### 5. Water sufficiency

**Risk exposure:** Water sufficiency is one of the most sensitive risks to climate, with the frequency of recent periods of extended hot, dry weather being evidence of changing circumstance and the potential for implementation of water use restrictions on customers.

**Control/mitigation:** We produce a Water Resources Management Plan (WRMP) every five years, which forecasts future demand and water availability under repeats of historic droughts, adjusted for climate change. A statutory Drought Plan is also developed every five years, setting out the actions we will take in a drought situation.

**Assurance:** The WRMP and Drought Plan are subject to various second and third line assurance activities prior to publication.

### 6. Carbon commitments

**Risk exposure:** This risk focuses on the capacity and capability to decarbonise water and wastewater activity relevant to the Public Interest Commitments (PIC) to achieve net zero by 2030 in light of the growth pressures, lack of technological advances or innovation and the fundamental change of approach required.

**Control/mitigation:** We will continue to develop near-term initiatives to address process and energy emissions, and create woodland and restore peatland, while responding to an evolving policy and technological landscape. We are also developing a long-term strategy to reduce emissions and to fully understand and optimise potential decarbonisation initiatives and pathways.

**Assurance:** Water industry research and technical support combined with a climate change mitigation steering group provides second line assurance. An internal audit is scheduled and external assurance of emissions, regulatory reporting lines and science-based targets has been established.

### 7. Failure to treat sludge

**Risk exposure:** This risk relates to the interdependency between wastewater and bioresource treatment activity in light of changing demographics, asset health and legislative/regulatory change. Industrial Emissions Directive (IED) now applying to biological treatment of sewage sludge within AMP 7, with no investment assigned to this requirement is a key factor.

**Control/mitigation:** The Throughput, Reliability, Availability, and Maintainability (T-RAM) of our facilities is a key area of mitigation, with formal service level agreements between the two core activities. In relation to IEDs, discussions at national level are being held to move the high capital cost improvements into PR24.

## Strategic report

**Assurance:** Wholesale assurance and engineering technical governance provide second line assurance. Subject to cyclical internal audit and ad-hoc external strategic reviews.

### 8. Recycling of biosolids to agriculture

**Risk exposure:** This risk represents various impact scenarios including operational failures, increased restrictions or total ban of recycling biosolids to agriculture. Referencing the EA's interpretation of the Farming Rules for Water (FRfW) regulations and the increasing threat to recycling a large proportion of biosolids.

**Control/mitigation:** United Utilities is accredited to the UK Biosolids Assurance Scheme (BAS), which certifies that our treatment and recycling activities meet regulatory requirements and best practice. We also work closely with farmers and landowners and have robust standard operating procedures established with contractors.

**Assurance:** Wholesale assurance and engineering technical governance provide second line assurance. Subject to both cyclical internal and external audit.

### 9. Price volatility

**Risk exposure:** This risk reflects the inflationary pressures across all commodities, notably energy, associated with the post COVID-19 economic bounce back which have been exacerbated further by the conflict in Ukraine.

**Control/mitigation:** Contract provision with suppliers, hedging policy and supply agreements manage volatility and minimise vulnerability in the contract and price risk with the suppliers including periods of agreed fixed pricing and negotiation of CPI/H uplift on an annual basis.

**Assurance:** Market analysis and supplier engagement, combined with quarterly business reviews provide second line assurance. Due to the scale of procurement an energy governance panel has oversight over procurement and use.

### 10. Credit rating

**Risk exposure:** Credit ratings below internal targets, due to deterioration in financial and/ or operational performance and/or external factors (such as inflation) resulting in more expensive funding.

**Control/mitigation:** Continuous monitoring of markets, and the management of key financial risks within defined policy parameters

**Assurance:** Second line assurance provided by financial control and quarterly business reviews, with oversight provided by the treasury committee. The treasury function is subject to regular internal audits.

#### A. Pension deficit

**Risk exposure:** The potential for the pension scheme funding deficit to increase because of life expectancy rates leading to additional contributions.

**Control/mitigation:** Constant monitoring combined with hedging against interest rates, inflation and growth asset risk.

**Assurance:** Policy and oversight is led by the pensions review management group, taking into account advice from accountancy and law firms. Pension governance is subject to periodic internal audits.

#### B. Financial outperformance

**Risk exposure:** Failure to achieve financial outperformance due to macro economic conditions and efficiency challenges, impacting the cost of debt and delivery of the company business plan.

**Control/mitigation:** Interest rate and inflation management, ongoing monitoring of markets and regulatory developments, and company business planning.

## Strategic report

**Assurance:** Second line assurance and oversight is provided by the board and treasury committee in addition to executive quarterly business reviews. Subject to cyclical internal audit reviews.

### C. Dam failure

**Risk exposure:** Uncontrolled release of a significant volume of water from reservoirs due to flood damage, overtopping, earthquake or erosion leading to catastrophic impacts downstream.

**Control/mitigation:** Each reservoir is regularly inspected by engineers. Where appropriate, risk reduction interventions are implemented through a prioritised investment programme.

**Assurance:** Various sources of second line assurance, including supervising engineers, dam safety group, wholesale assurance and regular board reviews. Independent assurance is provided by panel engineers and internal audit.

### D. Fair payment of tax

**Risk exposure:** Failure to maximise the available tax efficiencies and reliefs due to changing mechanisms.

**Control/mitigation:** Tax policies and objectives cover: efficient structuring of commercial activities; maintaining a robust governance and risk management framework; and an open and transparent relationship with tax authorities.

**Assurance:** Tax policies are based on advice from multiple sources, including accountancy firms. Third-party assurance is provided by internal audit and accountancy firms.

### E. Disease pandemic

**Risk exposure:** Serious illness in a large proportion of the UK population and consequences to our workforce, the wider supply chain and macro economy.

**Control/mitigation:** The incident management process would be invoked, supported by the Pandemic Response Plan. This includes the implementation of multi-channel communication with non-pharmaceutical interventions as per government guidance.

**Assurance:** Wholesale assurance provides second line assurance, with internal audit undertaking various reviews.

### F. Terrorism

**Risk exposure:** A significant asset to be compromised by terrorist activity leading to loss of supply, contamination and/or pollution.

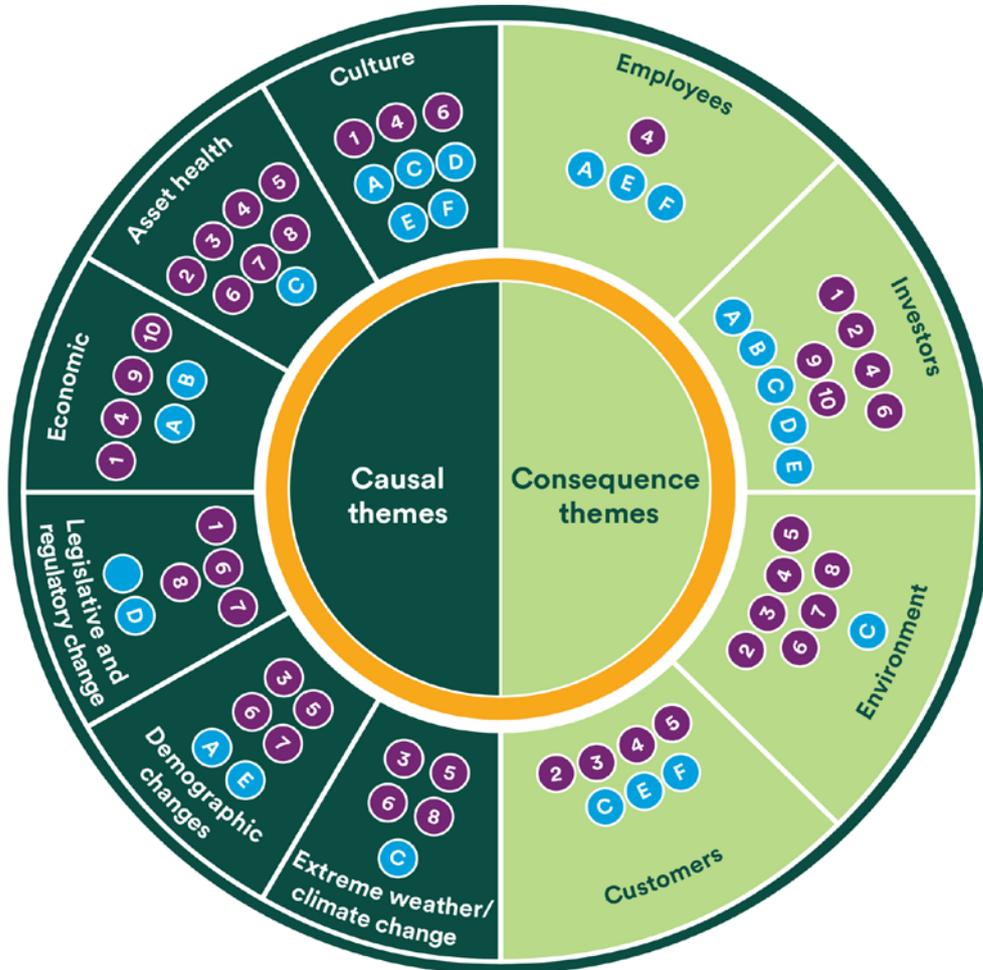
**Control/mitigation:** A risk-based protection of assets in line with the Security and Emergency Measures Direction (SEMD) and close liaison with the Centre for the Protection of National Infrastructure (CPNI), regional counter terrorist units, local agencies and emergency services.

**Assurance:** Security posture is based on various threat advisors. Second line assurance is provided by the security steering group. In addition, internal audit undertakes cyclical audits with external technical assurance being delivered by specialists.

# Strategic report

## Mapping of common themes to the most significant group risks

The diagram below illustrates how the common themes (causal and consequence) relate to the company’s most significant event-based risks, demonstrating how new and emerging circumstances can not only influence the risk exposure, but also focus attention for control and mitigation.



**Most significant event-based risks**

- 1 Price Review 2024 outcome
- 2 Failure of Haweswater Aqueduct
- 3 Wastewater network failure (sewer flooding)
- 4 Cyber
- 5 Water sufficiency
- 6 Carbon commitments
- 7 Failure to treat sludge
- 8 Recycling of biosolids to agriculture

- 9 Price volatility
- 10 Credit rating
- A Pension deficit
- B Financial outperformance
- C Dam failure
- D Fair payment of tax
- E Disease pandemic
- F Terrorism

**Key:**

- Top ten ranking risks relative to likelihood and impact
- High impact, low likelihood risks

## Strategic report

### New and emerging risks

Following horizon scanning activity undertaken by the business, a watching brief is held over risks/issues which are worthy of note due to their new, emerging or reputational status, and typically have too high levels of uncertainty or complexity to quantify.

- **Plastics:** Attention on single-use plastic and microplastic (plastics less than 5 mm) pollution is ongoing, with their presence in the environment being linked to the water cycle. We are responding proactively and have formed a two pillar approach to addressing plastics, focusing on operational plastic waste and plastic in the water cycle.
- **Perfluoroalkyl and polyfluoroalkyl substances (PFAS):** There is a growing focus on PFAS chemicals including from our public liability insurers who are looking to exclude related liability claims. PFAS are manufactured chemicals used in everyday products. Known as ‘forever chemicals’, they are persistent, bioaccumulate and may be toxic even at low levels. We have completed an assessment of the likely presence of PFAS in raw water sources, the results of which are incorporated into the Drinking Water Safety Plan and aligned to the requirements set out by the Drinking Water Inspectorate.

### 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.

In relation to the Manchester Ship Canal Company matter reported in previous years, a hearing was held in the Court of Appeal at the end of March 2022. A decision is expected during summer 2022, which may provide further clarity in relation to the rights and remedies afforded to the parties and others in relation to discharges by water companies into the canal and other watercourses.

Beyond this, there is nothing to report regarding material litigation, including in respect of the Argentina multiparty ‘class action’ reported on in previous years, and to which there have been no material developments.

### Conflict in Ukraine

The conflict in Ukraine has led to a number of risks emerging (growing, developing or becoming more prominent) from a security and economic perspective.

- **Cyber:** The likelihood of the cyber risk has been increased to reflect the rising tensions between Russia and the west, while taking into account the adoption of increased security measures which include security operations teams on extended high alert and the rapid deployment of technical blocking of critical indicators of compromise.
- **Price volatility:** This risk reflects inflationary uplift across multiple commodities with energy the most volatile.
- **Security of the supply chain:** This risk reflects the knock on impact of inflationary pressure on manufacturing output with some production facilities reducing operations. It also reflects sanctions imposed against Russia and Belarus and the restriction or prevention of access to certain goods.
- **Cash collection:** Inflationary pressure is having a significant impact on the cost of living, affecting customers’ ability to pay bills.
- **Supplier viability:** This risk reflects the impact the unprecedented price increases are having on suppliers who cannot honour locked prices in contracts and the threat of suppliers going into administration with a knock-on effect to operations and the capital delivery programme.

## Strategic report

- **Credit rating:** Whilst underlying credit quality is not a concern, the impact of high inflation on finance expense results in the potential for Credit Agency thresholds to be breached when combined with other factors such as additional investment spend to meet environmental and service improvements over and above price review allowances.

### Legislative/regulatory change

In addition to the emerging economic conditions exacerbated by the conflict in Ukraine, legislative and regulatory change is also a prominent emerging theme which impacts a number of event-based risks.

Relatively recent developments include uncertainty associated with the Environment Agency's interpretation of the Industrial Emissions Directive (IED) and Farming Rules for Water (FRfW) and implications for ongoing compliance, process and investment across wastewater and bioresources risk.

As a responsible company, United Utilities is committed to the protection and enhancement of the environment and can demonstrate many previous and current initiatives, the most recent being the road map to 'better river health' including a pledge to invest £230 million into 184 kilometres of rivers by 2025. We will continue to work closely with all our regulators and partners to deliver better solutions including full cooperation with the ongoing industry wide investigation by Ofwat and the Environment Agency into possible unpermitted sewage discharges into rivers and watercourses.

The Environment Act, which was enacted in November 2021, has potentially far more significant implications for the water sector, due to it being the UK's new framework of environmental protection. Depending on how the new legislation will be interpreted and applied, meeting its requirements may demand a fundamental shift in the water industry's approach to environmental risks, requiring significant investment across multiple AMPs.

## Corporate governance report

### Biographical details of the board of directors

#### Sir David Higgins

Chair

**Responsibilities:** Responsible for the leadership of the board, setting its agenda and ensuring its effectiveness on all aspects of its role.

**Qualifications:** BEng Civil Engineering, Diploma Securities Institute of Australia, Fellow of the Institute of Civil Engineers and the Royal Academy of Engineering.

**Appointment to the board:** May 2019; appointed as Chairman in January 2020.

**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.

**Career experience:** Sir David was previously 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. In December 2019 he stepped down as non-executive director and chair of the remuneration committee at Commonwealth Bank of Australia.

**Current directorships/business interests:** Chair of Gatwick Airport Limited and a member of the Council at the London School of Economics. He is also Chair of United Utilities Group PLC.

**Independence:** Sir David met the 2018 UK Corporate Governance Code's independence criteria (provision 10) on his appointment as a non-executive director and chair designate.

**Specific contribution to the company's long-term success:** Sir David's experience of major infrastructure projects and his knowledge and understanding of the role of regulators will be invaluable in meeting the challenges of the next regulatory period and beyond. As chairman of the nomination committee he is responsible for ensuring the succession plans for the board and senior management identify the right skillsets to face the challenges of the business.

#### Steve Mogford

Chief Executive Officer (CEO)

**Responsibilities:** To manage the company'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.

**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:** Steve was 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. He is a former non-executive director of G4S plc.

**Current directorships/business interests:** He is Chief Executive Officer of United Utilities Group PLC and a non-executive director of Water Plus, a joint venture between United Utilities and Severn Trent serving business customers. With effect from 1 August 2022, he will join the board of QinetiQ Group plc as a non-executive director.

## Corporate governance report

**Specific contribution to the company's long-term success:** As the Chief Executive Officer, Steve has driven a step change in the company's operational performance, and has implemented a Systems Thinking approach to underpin future operational activities and improved performance.

### Phil Aspin

Chief Financial Officer (CFO)

**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) Mathematics, Chartered Accounting (ACA), Fellow of the Association of Corporate Treasurers (FCT).

**Appointment to the board:** July 2020.

**Skills and experience:** Phil has extensive experience of financial and corporate reporting, having qualified as a chartered accountant with KPMG and more latterly through his role as group controller. He has a comprehensive knowledge of capital markets and corporate finance underpinned through his previous role as group treasurer and his FCT qualification. Having been actively engaged in the last four regulatory price reviews he has a strong understanding of the economic regulatory environment.

**Career experience:** Phil has over 25 years' experience working for United Utilities. Prior to his appointment as CFO in July 2020, he was group controller with responsibility for the group's financial reporting and prior to that he was group treasurer with responsibility for funding and financial risk management. He has been a member of EFRAG TEG and chaired the EFRAG Rate Regulated Activities Working Group.

**Current directorships/business interests:** Phil was appointed as a member of the UK Accounting Standards Endorsement Board in March 2021. He is chair of the 100 Group pensions committee and a member of both the 100 Group main committee and the stakeholder communications and reporting committee. He is Chief Financial Officer of United Utilities Group PLC and a non-executive director of Water Plus, a joint venture between United Utilities and Severn Trent serving business customers.

**Specific contribution to the company's long-term success:** Phil has driven forward the financial performance of the group and delivered the group's competitive advantage in financial risk management and excellence in corporate reporting.

### Louise Beardmore

Chief Executive Officer designate (CEO designate)

**Responsibilities:** To work with, and support, the Chief Executive Officer in managing the group's business and to lead the creation of the company's PR24 business plan, covering the next five-year regulatory period..

**Qualifications:** BSc (Hons) Business Management, Fellow of the Chartered Institute of Personnel Development, Vice-President of the Institute of Customer Services.

**Appointment to the board:** May 2022.

**Skills and experience:** Louise has extensive experience working in utility companies both in the UK and internationally and she consistently demonstrates the ability to successfully design, drive and implement organisational strategy in different operating environments. She has a strong strategic mind set and a track record of delivering major transformational change within regulated utility and service structures, improving performance for all stakeholders.

**Career experience:** Louise joined United Utilities on its graduate programme and has comprehensive experience of the company, its customers and its regulators. She was appointed as customer service

## Corporate governance report

and people director in 2016, prior to which she held a number of senior positions across the United Utilities group. She has led teams in business transformation, water operations, electricity and telecoms as well as customer service and people capabilities both in the UK and internationally. She has recently completed the corporate director programme at Harvard Business School.

**Current directorships/business interests:** Louise is also Chief Executive Officer designate of United Utilities Group PLC. She is a non-executive director of Engage for Success and named on the Northern Power Women's 'Power List' in recognition of her contribution to diversity, inclusion and talent, paving the way for female leaders in business.

**Specific contribution to the company's long-term success:** Louise's strategic vision and constant customer focus will continue to build on the group's significant performance and delivery for customers, communities and the environment.

### Mark Clare

Senior independent non-executive director

**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 Chair or Chief Executive Officer.

**Qualifications:** Chartered Management Accountant (FCMA).

**Appointment to the board:** November 2013.

**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:** Mark was previously chief executive Barratt Developments plc. He is a former trustee of the Building Research Establishment and the UK Green Building Council. Mark held senior executive roles held in Centrica plc and British Gas. He is a former non-executive director of BAA plc, Ladbrokes Coral PLC and Aggreko plc.

**Current directorships/business interests:** Mark was appointed as senior independent non-executive director at Wickes Group plc and as chair of the remuneration committee in April 2021. He is non-executive chair at Grainger plc and a non-executive director at Premier Marinas Holdings Limited. He is also senior independent non-executive director of United Utilities Group PLC.

**Specific contribution to the company's long-term success:** As senior independent non-executive director, Mark applies his own considerable board experience gained during his career to United Utilities and provides a sounding board to the executive in many areas.

### Liam Butterworth

Independent non-executive director

**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:** MBA Business Administration and Management, CIM Marketing, HND Mechanical Production Engineering.

**Appointment to the board:** January 2022

**Skills and experience:** As a serving CEO, Liam brings strong engineering and industrial technology experience to the board, with a track record of managing performance and enhancing corporate culture.

## Corporate governance report

**Career experience:** Liam has over 30 years' experience in the automotive industry. He started his career at Lucas Industries as an apprentice toolmaker, before moving into marketing, sales and purchasing at FCI Automotive. Joining Delphi Technologies plc in 2012, he became CEO in December 2017. He joined GKN Automotive Limited, owned by Melrose plc, as CEO in 2018.

**Current directorships/business interests:** Liam is CEO of GKN Automotive Limited. He is also a non-executive director of United Utilities Group PLC.

**Specific contribution to the company's long-term success:** Liam's operational experience contributes to the board's continuing focus on the performance of the business via the Systems Thinking approach.

### Stephen Carter CBE

Independent non-executive director

**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.

**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:** Stephen 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. He stepped down as a non-executive director at the Department for Business Energy and Industrial Strategy in December 2020. He is a former chair of Ashridge Business School. A Life Peer since 2008.

**Current directorships/business interests:** Stephen is group chief executive of Informa plc. He is also an independent non-executive director of United Utilities Group PLC.

**Specific contribution to the company's long-term success:** Stephen's experience as a current chief executive and his previous work in the public sector and government provides valuable insight for board discussions on regulatory matters.

### Kath Cates

Independent non-executive director

**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:** Solicitor of England and Wales

**Appointment to the board:** September 2020.

**Skills and experience:** Kath has spent most of her career working in a regulated environment in the financial services industry. Since 2014, she has focused on her non-executive roles, chairing all the main board committees and undertaking the role of senior independent director.

**Career experience:** Kath previously was chief operating officer at Standard Chartered plc before which she held a number of roles at UBS Limited over a 22-year period, prior to which she qualified as a solicitor. She is a former non-executive director at Brewin Dolphin Holdings plc and RSA Insurance Group plc, where she chaired the remuneration committee.

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**Current directorships/business interests:** Kath is a non-executive director at Columbia Threadneedle Investments where she chairs the TPEN audit committee. She is a non-executive director of TP ICAP Group Plc and Brown Shipley. She is an independent non-executive director of United Utilities Group PLC.

**Specific contribution to the company's long-term success:** Kath's broad board experience and knowledge of different regulated sectors enables her to contribute to board governance and risk management at United Utilities.

### Alison Goligher

Independent non-executive director

**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 lead the board's activities concerning directors' remuneration.

**Qualifications:** BSc (Hons) Mathematical Physics, MEng Petroleum Engineering.

**Appointment to the board:** August 2016.

**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:** Alison is a non-executive director and chair of the remuneration committee at Meggitt PLC and a part-time executive chair at Silixa Ltd. In February 2021 she was appointed as a non-executive director of Technip Energies NV. She is also an independent non-executive director of United Utilities Group PLC.

**Specific contribution to the company's long-term success:** Alison's understanding of the operational challenges of large capital projects and the benefit of deploying technology provides valuable insight into the longer-term strategic risks faced by the business. Her role as the designated non-executive director for workforce engagement provides the board with a better understanding of the views of employees and greater clarity on the culture of the company.

### Paulette Rowe

Independent non-executive director

**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 + Man (Hons), MBA.

**Appointment to the board:** July 2017.

**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 senior executive roles in banking and technology at Facebook, Barclays and the Royal Bank of Scotland/NatWest. Former trustee and chair of children's charity The Mayor's Fund for London.

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**Current directorships/business interests:** CEO of Integrated and Ecommerce Solutions and member of the Paysafe Group executive since January 2020. Paysafe, a former FTSE 250 company, is now privately owned by PE firms CVC and Blackstone. She is also an independent non-executive director of United Utilities Group PLC.

**Specific contribution to the company's long-term success:** Paulette's wide-ranging experience in regulated sectors, profit and loss management, technology and innovation enables her to provide a first-hand contribution to many board topics of discussion. In her current executive role she often faces many of the same issues, and has been able to provide support to senior management at United Utilities.

### Doug Webb

Independent non-executive director

**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 and treasury committees.

**Qualifications:** MA Geography and Management Science, Chartered Accountant (FCA).

**Appointment to the board:** September 2020.

**Skills and experience:** Doug has extensive career experience in finance from qualifying as a chartered accountant with Price Waterhouse, his executive roles as CFO of major listed companies and more recently through his non-executive positions and focus on audit committee activities.

**Career experience:** Doug was previously chief financial officer at Meggitt PLC from 2013 to 2018 and prior to that, he was chief financial officer at both the London Stock Exchange Group plc and QinetiQ Group plc. He is a former non-executive director and audit committee chair at SEGRO plc, having stepped down in 2019.

**Current directorships/business interests:** Doug currently serves as a non-executive director and audit committee chair at Johnson Matthey plc, BMT Group Ltd and the Manufacturing Technology Centre Ltd. He is an independent non-executive director of United Utilities Group PLC.

**Specific contribution to the company's long-term success:** Doug's financial capabilities and his experience as an audit committee chair strengthen the board's financial expertise.

### Changes to board directors:

Brian May left the board at the end of the company's AGM in July 2021, he ceased to be a director of United Utilities Group PLC at that time.

Neither Mark Clare nor Stephen Carter are seeking reappointment at the AGM in July 2022 having served on the board for nearly nine and nearly eight years respectively. As a result, at that time both will cease to be directors of United Utilities Group PLC.

Louise Beardmore was appointed after the year-end as a director and CEO designate on 1 May 2022 and, at that time, as a director of United Utilities Group PLC.

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### Letter from the Chair, Sir David Higgins:

#### Dear Shareholder

As I write, and cast my thoughts back to the early part of the year, our way of life and world of work was still very much dominated by restrictions associated with the pandemic. By the end of our financial year, we have transitioned at pace in some respects to the normality of our working lives before COVID-19. Virtual board meetings became a necessity during the pandemic, and, notwithstanding the usual electronic hiccups that we are all now so familiar with, provided an efficient alternative enabling us to ensure the usual governance mechanisms were adhered to. Still, it is good now to be again sitting alongside colleagues in meetings – and to be joined by Liam Butterworth, who was appointed as an independent non-executive director in January 2022. More detail on his appointment can be found on page 133 of the UUG 2022 Annual Report.

#### Governance

The past year has challenged the normal interaction of both the board and management. The board were kept fully apprised of management's actions and changes to normal business practices in the early stages of the pandemic. A combination of physical meetings where possible, in conjunction with virtual board and committee meetings, have been held to maintain the integrity of our governance structure. Induction programmes for Kath Cates and Doug Webb were undertaken virtually, and I know, in due course, Kath and Doug will welcome the opportunity to visit some of the company's principal operational sites and important capital projects, as will all board members. Informal virtual meetings have been held the evening before board meetings, as a substitute for our usual informal pre-board dinners. The annual board evaluation was externally facilitated this year, by virtual means by Independent Audit Limited (see page 135 of the UUG 2022 Annual report and financial statements).

Additionally, we have held a number of virtual workshops on key topics, including: leakage; digital strategy; diversity and inclusion and, as a direct consequence of the pandemic, considering the options for new ways of working for employees across appropriate parts of our business. These in-depth sessions have provided board members with a greater understanding of these particular challenges and initiatives, and how they are being addressed by management. We held a strategy day in November 2020, enabling the board to spend time debating a number of strategic and long-term business priorities, an action which was identified in the 2019/20 board evaluation. A particular focus for the day, was understanding the plans for the Haweswater Aqueduct Resilience Programme and Ofwat's 'direct procurement for customers' approach, through which the programme will be delivered.

In the following pages of this corporate governance report we have set out how we have met and delivered against the objectives of Ofwat's board leadership, transparency and governance framework (BLTG), which since 1 August 2019 are contained within the company's Licence as a provider of water and wastewater services\*. Furthermore, we set out how we have adopted the guiding provisions in the course of meeting the objectives of the BLTG. A copy of Ofwat's BLTG can be found at:

<https://www.ofwat.gov.uk/wp-content/uploads/2019/01/Board-leadership-transparency-and-governance-principles-2019-updated-July-2019.pdf>

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The company's ultimate holding company, United Utilities Group PLC (UUG), has a premium listing on the London Stock Exchange. An explanation of how UUG has applied the principles and reported against the provisions of the 2018 UK Corporate Governance Code can be found in the UUG Annual report and financial statements on pages 118 to 191. The group operates a structure that allows directors to be members of the boards of both UUW and UUG. These arrangements have been in place since March 2011 and were in place throughout the year ended 31 March 2022.

The boards of both UUW and UUG fully support Ofwat's drive for the highest standards of board leadership, transparency and governance in the industry. We are satisfied that current practices and the application of the 2018 Code at the holding company levels is entirely consistent with the Ofwat principles.

\*United Utilities Water Limited is regulated under the Water Industry Act 1991, the Water Act 2003, the Water Act 2014 and its Conditions of Appointment ('Licence').

### Risk

The board has an agreed framework for managing strategic and operational risks in accordance with the agreed risk appetite. The board regularly reviews the position to ensure that management are managing and mitigating risk in accordance with the board's agreed risk appetite. These risks include succession planning for senior management and asset resilience, with particular consideration for the impacts of climate change. The board is directly supported in this by the internal audit and risk management team and indirectly by KPMG during the course of their audit of the financial statements.

### Looking ahead

With the second year of the 2020–25 asset management period behind us, the board is beginning to focus on the early stages of the next price review process for the 2025–30 asset management period. Louise Beardmore will take the lead in the creation of the company's PR24 business plan, following her appointment as CEO designate with effect from 1 May 2022. Further information on the CEO designate appointment process can be found on page 130 of the UUG 2022 Annual Report.

After 12 years, and leading the transformation of the group into one of the top performing water and wastewater businesses, Steve Mogford has expressed his wish to step down from the board and retire in early 2023. Until that time, he will continue to lead the business and in doing so provide a transition period for the leadership to pass to Louise.

In my time as Chair, I have found Steve to be a remarkable individual, and I look forward to continue working with him over the coming months. Both Mark Clare and Stephen Carter will step down on 21 July 2022, on behalf of the board I wish to thank them both for their valuable support and wish them well for the future.

**Sir David Higgins**

**Chair**

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### Board statement: Ofwat's board leadership, transparency and governance framework

Ofwat's revised board leadership, transparency and governance (BLTG) principles came into effect from 1 April 2019 and were embedded into the licence on 1 August 2019. These require U UW to meet the objectives of the principles and to explain in an effective, accessible and clear manner how this has been achieved.

This statement demonstrates how United Utilities Water Limited's board of directors (the board), has met the BLTG objectives during 2021/22. It references the provisions set out within the guidance when explaining how we are delivering against these objectives.

This statement briefly summarises how, by implementing this approach, the company is delivering for its customers and other stakeholders. Further detail to support this statement is set out within the U UW Annual Performance Report, this United Utilities Water Limited Annual Report and Financial Statements and the United Utilities Group PLC Annual Report and Financial Statements. We provide references to this material below.

#### **A) The regulated company board establishes the company's purpose, strategy and values, and is satisfied that these and its culture reflect the needs of all those it serves.**

The board, supported by the executive team, is committed to achieving the very best results for the company, the customers it serves and its wider stakeholders.

We believe our purpose, strategy, vision and values will promote the long-term sustainable success of the company, further customers' interests, and create value for shareholders and other stakeholders. Our intention is to hand over the business to our successors in a better and more resilient position for the future. The structure of our purpose, strategy, vision and values is set out on pages 16 and 17 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements. 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, and in doing so have regard (amongst other matters) to S172(1) (a-f) of the Companies Act 2006.

#### **Provisions:**

##### **i. The board develops and promotes the company's purpose in consultation with a wide range of stakeholders and reflecting its role as a provider of an essential public service.**

As a provider of an essential service in our region, our purpose is to provide great water and more for the North West. Our three core values – customer focused, innovative and trustworthy – provide the cultural framework through which we operate. Behaving responsibly has been part of the United Utilities ethos for many years and aligns with our purpose. The corporate responsibility committee has a principal role in the group's governance structure. It leads, on behalf of the board, in the review and challenge process to ensure management's activities in the increasingly broad area of environmental, social and governance matters, are consistent with that of a business behaving in a responsible manner. The report of this committee, which includes a look forward in to the next year can be found on pages 156 to 159 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements.

We work to deliver our vision to be the best UK water and wastewater company through three strategic themes of providing the best service to customers, at the lowest sustainable cost and in a responsible manner. In defining the company's purpose, the board took into account information and views from stakeholders through utilising research and engagement – including that which contributed to our AMP7

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business plan – and the other feedback and intelligence obtained from customers through both programmatic research and day to day interactions. It is a standing item for the board’s corporate responsibility committee to discuss engagement with national and regional stakeholders each time it meets. For the year ended 31 March 2022, the board is satisfied that the formulation of our aspirations in terms of our purpose, vision, values and culture have been informed by our stakeholders and we operate our business in such a way that will create long-term value for all. We believe the company has played its part in contributing to the North West and has demonstrated the ‘more’ of its purpose for our customers, employees, shareholders and other stakeholders.

### ii. The board makes sure that the company’s strategy, values and culture are consistent with its purpose.

Our vision is to be the best UK water and wastewater company. To ensure that we deliver our purpose and work towards our vision, we have three strategic themes - which define the way we operate - and three core values - which provide the cultural framework within which we operate.

- **The best service to customers** – We put customers at the heart of everything we do. As well as delivering a reliable service of great-tasting water and removing wastewater, we proactively keep customers informed about any work we are doing in their area and communicate with them in ways that meet their individual needs; for example, we now use ‘push texts’ to send updates and alerts to customers within a specified location. The best service to customers means being available for them when they need to contact us, always interacting in a friendly and helpful manner, and offering tailored support and assistance for customers when they need it. As well as these day-to-day interactions, it means consulting and understanding more broadly what matters to them about the service we deliver. This shapes what we do across our range of activity. For example, we redesigned our bills based on customer research and feedback so that they were more helpful for customers, whilst on the wastewater network our Dynamic Network Management programme is installing digital sensors to help us proactively understand when the system is not performing as it should. The sensors send an alert back to a central system, meaning we can better respond in real time to deviations in performance, identifying and resolving issues before they impact on customers or the environment.
- **At the lowest sustainable cost** – To run a resilient business, it is important to ensure cost reductions are sustainable so that we can keep them down without compromising on resilience or the quality of service we deliver. When we develop our plans and assess different options for consideration, we look to minimise the whole-life cost. This fits with the total expenditure (totex) model, because the most cost-effective option can vary between traditional operating expenditure (opex) or capital expenditure (capex) solutions. Our Systems Thinking approach helps us look holistically at all options, and operating our entire network as a system rather than discrete assets opens up new avenues that would otherwise not have been available.
- **In a responsible manner** – We will only deliver our purpose and create and maintain value for our stakeholders if we act in a responsible manner. This means protecting and enhancing the natural environment, using natural solutions where possible, and reducing our carbon footprint and waste. It means promoting a safe, healthy and engaging workplace for our employees, supporting their physical and mental health. It drives us to support local communities on issues that matter to them, and to work with local schools and training facilities to promote skills for the future. Above all it means we are open, honest and transparent in our dealings and in reporting our performance. As part of our Catchment Systems Thinking (CaST) Fund, we provided funding to community groups across the North West to deliver elements of our catchment management approach, focused in particular on community engagement with nature or helping shape and promote natural capital markets. One of the first projects to receive funding is led by the Mersey Rivers Trust and focuses on establishing community participation in the lower catchment area of the River Bollin. It aims to

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increase the number of people connecting with nature and accessing local blue-green space for health and wellbeing. The project will engage volunteers and landowners in restoring the reed bed habitat at Tatton Mere, a popular recreational site in Cheshire.

### **Our core values and culture are:**

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

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

**Trustworthy** – We make promises knowingly and keep them, behaving responsibly and with integrity towards all of our stakeholders.

**Culture** – As well as our purpose, strategy and core values, we monitor our culture against key categories relating to our people, such as engagement, health and wellbeing, diversity, and development.

The United Utilities Group PLC Annual Report and Financial Statement sets out additional information about these strategic themes and how they run through everything we do. For further information and explanation of our approach, we would refer in particular to the 2021/22 Strategic Report (pages 16 to 109.)

### **iii. The board monitors and assesses values and culture to satisfy itself that behaviour throughout the business is aligned with the company's purpose. Where it finds misalignment it takes corrective action.**

Our values demonstrate how we behave individually and collectively as the board and how we ask our employees to behave. Our employees are fundamental to delivering our strategy and achieving our purpose.

Our core values of being customer focused, trustworthy and innovative underpin our culture of behaving as a responsible business in the way we interact with all the stakeholders we serve. We must continually reinforce these values so that the right behaviours cascade throughout the organisation, ensuring our culture of behaving responsibly drives what we do. Key to this is taking action to address any issues where there is misalignment with the company's values. As well as our engagement survey we run regular employee barometers to ask employees what they are seeing, hearing and feeling. This approach allows us to act quickly if there are any areas of misalignment and take immediate actions.

In addition to the existing reporting presented to the board, management has developed the United Utilities cultural model and a dashboard of cultural metrics to provide a comprehensive overview to support the board in fulfilling its role in monitoring and assessing culture. The model reflects our people, our value and our purpose. The dashboard comprises relevant metrics derived from the annual employee engagement survey; human resources policies in relation to diversity and inclusion and training; whistleblowing reporting; health, safety and wellbeing policies and practices; and other measures underpinning our purpose of 'providing great water and more for the North West'.

We are pleased to have received external validation of our approach to monitoring culture, featuring as a best practice case study with the Financial Reporting Council 'Creating Positive Culture Opportunities and Challenges Report', December 2021. A recent independent audit found our approach to be a "pragmatic and effective model" for supporting the board in its role of monitoring and assessing culture and a useful framework for driving improvements and interventions"(PwC, February 2021).

Our employees are at the heart of the culture of our business and their 'lived experience', is a key part of the board's assessment and monitoring of culture. Alison Goligher, the current designated non-executive

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director for engagement with the workforce, facilitates two-way dialogue between the board and employees. Alison chairs the Employee Voice panel (the panel) formed from representatives of a number of employee groups and employee networks from within the business and with representatives drawn from across the geographical region. There is an open invitation to all board members to attend meetings of the panel and during this year, Sir David and Kath Cates have participated and answered questions from panel members on board strategy.

Alison has met the panel virtually four times throughout the year. In order to ensure two-way communication, Alison provides updates to the panel from the perspective of the board and its committees, and similarly she provides feedback to the board on the work of the panel. Alison has regular meetings with senior trade union representatives as part of the agreed panel approach.

The panel has adapted its approach during the pandemic and moved from face to face and site meetings to virtual meetings. These have proved popular with panel members, particularly field based operational staff who find it much easier to attend virtually than travel from their operational sites. There are 30 members of the panel and membership rotates approximately every two years.

The panel have been provided with business updates and information sessions to broaden their knowledge of how board and corporate governance and have three key sub groups focused on continual improvement of the employee opinion survey, supporting our employee networks to promote support and inclusion across the company and to explore in more detail the drivers and measures of organisation culture. The culture sub-group has focused its energies on obtaining a grass-roots view of the changes to ways of working during the pandemic and contributing to the 'next ways of working' project and on the discussion of topical issues relating to culture, such as the focus on racial inequality.

Employees' views are measured annually through the employee engagement survey with the objective of taking any required action to improve how permanent employees feel about the company and understand its direction. Employees are provided with information through briefings and access to online materials, to enable them to understand the financial and economic factors affecting the group's performance. Along with our employee relations team, our CEO holds regular face-to-face meetings with senior trade union representatives to facilitate two-way communication and engagement with the views of employees' representatives.

The group has a commercial arrangement with a third party for the provision of agency staff and contractors. Engagement and communication in relation to these members of the wider workforce is managed directly by the third party via a dedicated third party account manager who liaises directly with the company's human resources team. If there is any significant change activity, a representative of the third party joins the project team, thereby ensuring consistency when communicating key information to employees, agency staff and contractors.

The board remains committed to embedding a health and safety culture to ensure employees go home safe and well, and regularly receives updates on health, safety and wellbeing activities and health and safety incidents of employees and contractors. The implementation of employee wellbeing policies and activities continued to be a major focus throughout the year. From an external perspective, the board reviewed the approach and progress of work to identify areas where there is any risk of modern slavery occurring in our supply chain and it approved the 2022/23 slavery and human trafficking statement.

Taken together, the board is satisfied that policies, practices and behaviours within the business are aligned with the company's purpose, vision, values and strategy. Further information about how the board monitors culture and employee engagement are set out on pages 125 to 126 of the 2021/22 United Utilities Group PLC Annual Report and Financial statements.

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### **B) The regulated company has an effective board with full responsibility for all aspects of the regulated company's business for the long term.**

The group operates a structure that allows directors to be members of the boards of both U UW and its ultimate holding company, United Utilities Group PLC (UUG). These arrangements have been in place since March 2011 and were in place throughout the year ended 31 March 2022.

As a listed company UUG has applied the principles and reported against the provisions of the 2018 UK Corporate Governance Code (the code), for the year ended 31 March 2022.

Further detail on the reporting on the application of the principles and against the provisions of the 2018 UK Corporate Governance Code is provided on pages 116-199 of the 2021/22 United Utilities Group PLC Annual Report and Financial statements.

The boards of both UUG and U UW fully support Ofwat's drive for the highest standards of board leadership, transparency and governance in the industry. We are satisfied that current practices and the application of the code at both holding company and regulated company levels are entirely consistent with the Ofwat principles.

On pages 46 to 49 of the 2021/22 United Utilities Group PLC Annual Report and Financial statements we set out our planning for the short, medium and long term. The board has full visibility as plans are presented to the board throughout the year.

#### **Provisions:**

- i. The regulated company sets out any matters that are reserved for shareholders or parent companies (where applicable); and explains how these are consistent with the board of the regulated company having full responsibility for all aspects of the regulated company's business, including the freedom to set, and accountability for, all aspects of the regulated company's strategy.**

The U UW board has full responsibility for all aspects of its business as an appointee. Furthermore there are no items/topics relating to the regulated activities of U UW contained within UUG board's schedule of matters reserved for its own decision.

U UW and UUG are distinct legal entities and are operated as such. Notwithstanding that the same individuals are directors for both companies and scheduled board meetings of each company are held on the same day, they are held as separate meetings with board packs and agendas being prepared for each company's meeting, thereby creating distinction between meetings. Given that U UW represents approximately 99 per cent of UUG's revenues, decisions taken for U UW are unlikely to be in conflict with those of UUG. Were that to be the case, the directors would be responsible for taking decisions on behalf of each entity in accordance with S172 of the Companies Act 2006, and acting 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. The company secretary would advise on any potential conflict of interest, and the board would seek independent advice on any matter if thought necessary.

Matters that have been reserved for decision by the UUG board can be found on our website at

[www.unitedutilities.com/globalassets/documents/pdf/03---schedule-of-matters-reserved-for-decision-by-the-board.pdf](http://www.unitedutilities.com/globalassets/documents/pdf/03---schedule-of-matters-reserved-for-decision-by-the-board.pdf)

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- ii. Board committees, including but not limited to audit, remuneration and nomination committees, report into the board of the regulated company, with final decisions made at the level of the regulated company.**

The U UW board has delegated specific powers, subject to certain limits, relating to the capital investment programme to the U UW capital investment committee and in relation to financing, by way of power of attorney, to the Chief Financial Officer and/or the Treasurer. U UW does not duplicate board committees already in operation at the UUG level (the board committees). The activities of the board committees, as required in accordance with the code, whose members are made up entirely of independent non-executive directors (in accordance with provisions 9 and 10 of the code who are directors of the company) are necessarily targeted towards U UW matters, given that U UW represents approximately 99 per cent of UUG's revenues. The alignment of the interests of U UW and UUG ensures that the interests of U UW and its customers are safeguarded, and avoids unnecessary duplication. The group has operated in this manner since 2011.

Further information about the UUG committees and approach to Board governance can be found in the 2021/22 United Utilities Annual Report and Financial Statements on pages 112 – 198. This includes reports from the Nomination committee (pages 130-139), the Treasury committee (page 155), the Audit committee (pages 143-154), the Corporate responsibility committee (pages 156-159) as well as the Annual statement from the remuneration committee chair (pages 160-163).

- iii. The board of the regulated company is fully focused on the activities of the regulated company; takes action to identify and manage conflicts of interest, including those resulting from significant shareholdings; and ensures that the influence of third parties does not compromise or override independent judgement.**

Meetings of the board are fully focused on the company's regulated obligations and activities as an appointee in accordance with its licence as a provider of water and wastewater services and the board is supported by the director of strategy, policy and regulation. Typically, board meetings receive the following standing items: operational activities and incidents; review of performance against operational and financial KPIs; regulatory updates and customer updates.

The board, whose directors' biographies can be found on pages 112 to 115 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements, includes a strong independent non-executive representation with a diverse range of backgrounds, skills and experience. As part of the director recruitment process, potential conflicts of interest would be assessed to ensure the suitability of the candidate in this respect (amongst others). A register of directors' interests is maintained and directors are asked to identify any potential conflicts of interest on any subject matter on the board's agenda at each meeting.

### **C) The board's leadership and approach to transparency and governance engenders trust in the regulated company and ensures accountability for their actions.**

Excellent governance is part of who we are and United Utilities was delighted to be accredited with the Fair Tax Mark for the past two years. We participate in a range of global Environment, Social and Governance (ESG) ratings, indices and frameworks to benchmark our approach against best practice and emerging sustainability challenges. We target being "upper quartile across a suite of investor indices" to demonstrate our performance. We adhere to the highest levels of corporate governance. Fairness and transparency is key to the way we report, the way we operate, and the way we interact with all our stakeholders. In the last reporting year, the board has reviewed the effectiveness of the whistleblowing policies and processes and incidents under investigation and noted the activities within the business to prevent and detect fraud. It concluded that the whistleblowing policies and processes were effective and noted the activities within the business to protect and detect fraud, the latter having been reviewed by

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the audit committee. During the year, the audit committee asked management to commission an independent review of the group's fraud risk management framework to assess its maturity and identify any enhancements required given the evolving nature of business processes and the working environment. This was felt to be timely, particularly in light of the need for remote working during the pandemic and the subsequent move to hybrid working in some areas of the business. An action plan to strengthen the approach to fraud risk assessment has been implemented, overseen in the first instance by the security steering group forum and with the final report presented to the committee.

Our human rights policy can be found on our website,

**[www.unitedutilities.com/corporate/responsibility/our-approach/human-rights/](http://www.unitedutilities.com/corporate/responsibility/our-approach/human-rights/)**

with links to other related policies including our modern slavery policy and our approach to sustainable supply chain called United Supply Chain. We work with suppliers and contractors whose business principles, conduct and standards align with our own. 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 fully comply with rules on reporting payments to suppliers.

In recent years the UK water sector has faced challenges to its legitimacy, and questions raised about the ownership structure of the sector. We have been open and transparent in reporting our equity and debt financing arrangements and do not use offshore financing vehicles. Throughout AMP6 we developed a sound approach to assurance which is a key enabler to providing high quality data provision. We are maintaining, and where appropriate evolving, our approach to assurance into AMP7 to build further on the trust we have earned, making improvements where shortcomings are identified and to enhance the confidence that customers, regulators and other stakeholders can have in our performance reporting.

Each year the board reviews and discusses the evaluation of the board, its committees and individual directors and conflicts of interest. Once every three years this process is undertaken by an external organisation and in the intervening years the evaluation is facilitated by the company secretary. An external review was last undertaken in February 2021, the review this year was facilitated by the company secretary in February 2022. This process identified action points and any ongoing training needs. Further details can be found on pages 135 to 138 of the 2021/22 United Utilities Group Annual Report and Financial Statements. As part of its annual governance processes, the terms of reference for the audit, remuneration, treasury and corporate responsibility committees were reviewed by each committee and the board received post-meeting reports from the chairs of each committee summarising discussions and actions. It implemented matters arising from its biannual updates on changes and developments in corporate governance as thought fit. Further details of the company's approach to transparency and governance can be found in the corporate governance report contained within pages 110-199 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements.

### Provisions:

- i. A detailed explanation of the structure of the United Utilities group is set out on page 124.**
- ii. An explanation of dividend policies and dividends paid, and how these take account of delivery for customers and other obligations (including to employees).**

In May 2020 the U UW Board determined that in the context of the COVID-19 pandemic and the level of uncertainty at that time, no dividend payments would be made by U UW during 2020/21. In the 2020/21 Annual Performance Report we explained that the deferral of the 2020/21 base dividend payment was to be kept under review by the U UW Board, with a view to reinstating the dividend later in the AMP7 period at such time as there is more certainty in relation to the prevailing economic conditions following the pandemic, and the financial position had become more clear.

During 2021/22 the Board further reviewed the position and determined that there was sufficient certainty about the impact of the pandemic on the business and on the economy more generally such that dividend payments could be reinstated. Further detail on the dividend policies and dividends paid,

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and how these take account of delivery for customers and other obligations is provided in section 2.4 of the Annual Performance Report.

**iii. An explanation of the principal risks to the future success of the business, and how these risks have been considered and addressed.**

The principal risks and uncertainties to the success of the business and the ways in which these risks are managed, monitored and mitigated are set out on pages 104 to 109 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements.

**iv. The annual report includes details of board and committee membership, number of times met, attendance at each meeting and where relevant, the outcome of votes cast.**

The table below sets out, for the year ended 31 March 2022, the number of scheduled meetings of the United Utilities Water Limited Board that were attended and the maximum number of scheduled meetings that could have been attended.

Sir David Higgins	8/8
Steve Mogford	8/8
Phil Aspin	8/8
Mark Clare	8/8
Liam Butterworth <sup>(1)</sup>	1/1
Stephen Carter	8/8
Kath Cates	8/8
Brian May <sup>(2)</sup>	3/4
Alison Goligher	8/8
Paulette Rowe	8/8
Doug Webb	8/8

1. Liam Butterworth was appointed as a non-executive director on 1 January 2022.

2. Brian May stepped down from the board on 23 July 2021

Memberships of board committees and attendance at these is set out in the Governance section of the 2021/22 United Utilities Group PLC Annual Report (pages 111 to 198.)

**v. An explanation of the company's executive pay policy and how the criteria for awarding short and long-term performance related elements are substantially linked to stretching delivery for customers and are rigorously applied. Where directors' responsibilities are substantially focused on the regulated company and they receive remuneration for these responsibilities from elsewhere in the group, policies relating to this pay are fully disclosed at the regulated company level.**

A detailed explanation of the group's directors' remuneration policy and its application during 2021/22 is set out on pages 169 to 176 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements. Details of remuneration for the directors of U UW is set out within Section 2.5 of the Annual Performance Report and page 125 to 127 of the United Utilities Water Limited Annual Report and Financial Statements. The criteria for awarding short and long-term performance related elements are

## Corporate governance report

substantially linked to stretching delivery for customers and are rigorously applied, with executive pay arrangements aligned to our purpose, vision, values and strategy, thereby incentivising great customer service and the creation of long-term value for all.

As set out in these disclosures, for AMP7 the company has committed to ensuring that performance pay for executive directors is aligned to delivery for customers, embeds stretching targets and is being rigorously applied. We will continue to provide transparent reporting on executive pay each year.

### **D) Boards and their committees are competent, well run, and have sufficient independent membership, ensuring they can make high quality decisions that address diverse customer and stakeholder needs.**

As detailed above, the group operates a structure with the same directors sitting on the boards of both UUW and UUG, thereby increasing the efficiency and effectiveness of the corporate governance structure. As a result and given that UUW represents approximately 99 per cent of UUG's revenues, the company does not duplicate the board committees already operating at the UUG level. Full details of the UUG board and board committees are set out within the Governance section of the 2021/22 United Utilities Group PLC Annual Report and financial statements (pages 111 to 198).

#### **Provisions:**

- i. Boards and board committees have the appropriate balance of skills, experience, independence and knowledge of the company. Boards identify which customer and stakeholder expertise is needed in the boardroom and how this need is addressed.**

The board and the board committees have an appropriate combination of skills, experience and knowledge, biographies of the directors are set out on pages 112-115 and the skills matrix of directors is set out on page 134 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements. Consideration is given to the length of service of the board as a whole and membership is regularly refreshed, non-executive directors would normally only serve a term of up to nine years in accordance with the code (the tenure of board directors is set out on page 132 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements). Appointments to the board are subject to a formal, rigorous and transparent procedure. The board diversity policy (see page 134 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements) is taken into account during the recruitment process. The policy incorporates targets for gender and ethnic diversity, which are to maintain at least 40 per cent female representation and to have at least one director from a minority ethnic background\* and to have at least one of the positions of: chair, CEO, senior independent director or CFO held by a female. These targets will be met as of the end of July 2022. An effective succession plan is maintained for board and senior management. Improving diversity and inclusion within the group has been high on the board agenda. Further detail is set out on pages 134 to 135 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements.

\*Defined by reference to categories recommended by the Office for National Statistics (ONS) excluding those listed by ONS as coming from a white ethnic background

- ii. Independent non-executive directors are the largest single group on the board.**

There are currently seven independent non-executive directors on the board out of a total of eleven (at May 2022). Their biographies can be found on pages 112 to 115 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements. Independence is tested against the criteria set out in the code.

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- iii. The chair is independent of management and investors on appointment and demonstrates objective judgement throughout their tenure. There is an explicit division of responsibilities between running the board and executive responsibility for running the business.**

Sir David Higgins was appointed to the board in May 2019 as chair designate and in line with the BLTG provisions, he was independent on appointment when assessed against the circumstances set out in the code. He was appointed as Chair of the board on 1 January 2020. The roles and responsibilities of the Chair are set out as part of the group's governance framework.

- iv. There is an annual evaluation of the performance of the board. This considers the balance of skills, experience, independence and knowledge, its diversity, how stakeholder needs are addressed and how the overarching objectives are met. The approach is reported in the annual report and any weaknesses are acted on and explained.**

A board evaluation is conducted annually, with an independent assessment every third year, as has been the case for a number of years. This year the evaluation was facilitated internally by the company secretary, in consultation with the Chair and the board committee chairs. The most recent external audit was conducted during 2020/21. Full details, can be found on page 135 of the 2021/22 United Utilities Group PLC Annual Report and Financial Statements.

- v. There is a formal, rigorous and transparent procedure for new appointments which is led by the nomination committee and supports the overarching objective**

Details of the approach to board succession can be found on pages 133 to 135 of the 2021/22 United Utilities Group PLC Annual Report and financial Statements.

- vi. To ensure there is a clear understanding of the responsibilities attached to being a non-executive director in this sector, companies arrange for the proposed, final candidate for new non-executive appointments to the regulated company board to meet Ofwat ahead of a formal appointment being made.**

Liam Butterworth was appointed to the board in January 2022 and met (via video call) with representatives of Ofwat prior to his appointment to the board on 1 December 2021, as have all non-executive directors since April 2016

- vii. There is a majority of independent members on the audit, nomination and remuneration committees and the audit and remuneration committees are independently led.**

Independent non-executive directors form the members of the board committees and chair the audit, remuneration, treasury and corporate responsibility committees.

### E) Delivering for customers and stakeholders

We believe that we are delivering a strong performance for customers and stakeholders and have described this in section 1.1 of the company's Annual Performance Report and in the strategic report in pages 16-109 of the 2021/22 United Utilities Group PLC Annual Report.

Examples of delivery include helping over 200,000 households currently struggling with their bills through our extensive range of affordability schemes, including leading the utility sector in implementing Open Banking, which has helped us deliver even better customer service. It takes a process that

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previously could have taken weeks down to just a few minutes, allowing us to find the most suitable support scheme for customers quickly. There is always more we would like to be able to do though, and we are a leading supporter of the Consumer Council for Water's drive to introduce a national social tariff. This would help to deliver a fairer sharing of support across the country, as we believe the right support should be provided to those who need it regardless of where they live in the country.

Our focus is on investing in and delivering sustainable operational performance. In 2021/22 we achieved over 78% of our performance commitments.

In wastewater, the benefits of our Pollution Incident Reduction Plan are being realised. We are sector frontier on pollution incidents, having reduced overall pollution by a third since the start of the AMP. Our treatment works compliance remains strong and we expect to remain green on this measure in the Environment Agency's annual performance assessment for 2021.

In water, we are investing £100 million in our water network to reduce incidences of discolouration experienced by customers. Progress to date has been good with a more than 30% reduction in discolouration reports by customers in the first three months of 2022 when compared to 2021. We outperformed our leakage target for the 16th consecutive year.

Our focus and targeted investment is helping us to deliver great service to customers and this year we have continued to perform well against C-MeX and D-MeX. We have again achieved the BSI accreditation for customer vulnerability for providing services for our most vulnerable customers.

We are on track to deliver our AMP7 environmental improvement programme, which will improve river and bathing water quality in the North West, and have made good progress against our carbon pledges. We are upper quartile across a suite of environmental, social and governance (ESG) indices, and our robust balance sheet provides long-term financial resilience.

We are achieving higher outperformance payments thanks to strong operational performance against customer outcome delivery incentives as well as financial outperformance. As a responsible company we are sharing this success with customers, as we did in AMP6, by investing £765 million to help accelerate further enhancements for customers and the environment.

Remuneration arrangements for executive directors are aligned to our purpose, vision and strategy helping to incentivise great customer service and the creation of long-term value for customers and other stakeholders, including the environment. The table on page 166 of the UUG 2022 Annual report summarises how our incentive arrangements are aligned to our business strategy. During the year our remuneration arrangements were thoroughly reviewed, with a key area of focus being on how we could strengthen the extent to which environmental, social and governance matters are reflected going forward. Additional information and context is available in the remuneration committee report on pages 160 to 191 of the 2021/22 United Utilities Group PLC Annual Report.

In respect of our long-term incentives (LTIs), performance is measured over at least a three-year period but outcomes only become available to the directors after at least five years from grant. Since 2020, half of the overall outcome available for our LTI is based on key performance indicators including operational, service resilience, and from 2022 will reflect our performance on specific carbon measures, all of which capture the stretching delivery of performance in the interests of customers and the environment. The other half is related to our performance against return on regulated equity targets, where performance is influenced by the extent to which we deliver for customers. Overall, since 2020 at least 50 per cent of our LTI is based on customer and environmental objectives, including 10 per cent specifically related to carbon reduction initiatives.

Page 179 of the 2021/22 United Utilities Group PLC Annual Report provides details about the outcome of the LTI that was granted in 2019 and had a performance period that ended on 31 March 2022. This 2019 LTI had different performance measures than those which have applied since 2020 as outlined above. Overall, one-third of the 2019 LTI was based directly on our customer service performance (C-MeX contacts and written complaints). Whilst the final outcome will only be confirmed in the summer of 2022 when the complaints performance of all other water companies is known, we believe we have

## Corporate governance report

performed very well in this area and will have reached our stretch target in full. The other two-thirds of the 2019 LTI is based on our performance against return on regulated equity and shareholder return targets, where our performance has also been strong. Overall, we expect that the vesting outcome for the 2019 LTI will be 100 per cent once the customer service performance component is confirmed.

In respect of the annual bonus scheme, performance is measured over a one-year period but half of the outcome is deferred in to shares and only become available to the directors three years after the cash bonus is paid.

For a number of years the measures used in our annual bonus arrangements for executive directors incentivise stretching performance delivery for customers, including on our environmental commitments and obligations, with an overall weighting of 75 per cent. In respect of the performance year 2021/22, customer satisfaction and employee engagement remain high, we have achieved our best ever performance against customer outcome delivery incentives (ODIs), we are on track to deliver our AMP7 environmental improvement programme, and we have again achieved the maximum 4 star “industry leading company” status against the Environment Agency’s annual performance assessment. Details about how this performance has impacted the executives directors’ bonuses are shown on page 178 of the 2021/22 United Utilities Group PLC Annual Report.

Following a review during the year we have introduced two new performance measures to our 2022/23 annual bonus scorecard, one focussing on improving the appearance of drinking water, and the other one delivering on our Better Rivers commitments (further details of which are available on page 67 of the 2021/22 United Utilities Group PLC Annual Report). We have revised our existing Time, Cost, Quality index measure to place renewed emphasis on the efficiency of our capital delivery programme and to reflect the carbon impact of enhancement projects. Details of our performance against these measures will be included in our 2022/23 Annual Performance Report.

For all incentive outcomes, legally enforceable mechanisms are in place to enable the company to withhold amounts due, or recover amounts already paid, in circumstances if relevant information becomes known at a later point.

## Corporate governance report

### Providing great water and more for the North West

#### Embedding our purpose

Board members, individually and collectively, are cognisant of their statutory duties as set out in the Companies Act 2006 (the Act). In accordance with section 172 of the Act, directors are individually required to act 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. In doing so, the directors must have regard to the likely consequences of any decision in the long term and the interests of, among other matters, employees, customers, suppliers, the community and the environment, and on the company's reputation. By virtue of the long-term nature of the water and wastewater industry, thinking about our stakeholders is an integral part of our decision-making process and underpinned by our regulatory contract. The board's 2021/22 S172(1) Statement can be found on page 13 of the UUG 2022 Annual Report, and provides examples of how our purpose is embedded in board decisions.

#### Incorporating sustainability in our stewardship alongside creating value

Long-term sustainability is a key component of the way in which the board manages the business. With many parts of the water and wastewater network across the North West built over 100 years ago, the board continues to apply the ethos of sustainability and building assets that last, and, crucially, operate efficiently and effectively to serve customers' needs. The group's planning horizons can be found on pages 46 to 49 of the UUG 2022 Annual Report. During the year, the board held deep-dive sessions to consider the group's Water Resources Management Plan and its Drainage and Wastewater Management Plan. Sustainability and environmental protection drivers underpin both these plans.

Set out on page 22 of the UUG 2022 Annual Report, as part of our business model, is how value is created for our shareholders and other stakeholders in a sustainable manner. The board's governance approach, its culture and the way it operates the business is to behave responsibly towards all of the group's stakeholders.

#### Being a guardian for future generations

Environmental issues are high on the list of matters considered by the board. The corporate responsibility committee takes the lead in overseeing management's development of our climate change mitigation strategy, and reports regularly to the board on the matter.

Plans are progressing to drive the group's transition to a low carbon future by minimising our contribution to global warming through a reduction in our carbon emissions. Carbon has been incorporated as a factor to be considered in:

- our investment appraisal and decision-making processes;
- our land management practices to enhance/ improve natural capital;
- the innovation that we encourage both within our operations and through working with our partners and suppliers; and
- our implementation of a 'circular' mindset.

The board is kept fully informed by management on the impacts of climate change from an operational perspective. Extreme weather events impacting our region and our operations in recent years are increasingly common. When such incidents occur, the CEO keeps board members fully apprised of the impact on operations via virtual meetings and other forms of communication. The board would be informed of any material points of learning identified in the post-incident review process, and progress with the implementation of material actions. Our reporting against TCFD can be found on pages 41 to 57 of the UUG Annual Report.

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### Improving river health and recreation

During the year, the board has been fully engaged in considering the criticism aimed at the group for its part in the health of some of the rivers in our region. This criticism has also been widely made in relation to a number of other companies operating in the wastewater sector. The sewerage network in the North West carries sewage and rainwater. Storm overflows are incorporated into the wastewater network to help to prevent the flooding of streets, homes and businesses during periods of heavy rainfall.

When sewers and treatment plants are operating at full capacity they can spill storm water (including diluted sewage) into rivers via the storm overflow. The board has committed to £230m in environmental improvements, supporting at least a one third sustainable reduction in the number of spills recorded from our storm overflows by 2025 compared to the 2020 baseline.

### Working with our regulators

Ofwat has introduced a new approach for major capital construction projects, namely Direct Procurement for Customers (DPC). The group's first project that has been approved for procurement via the DPC method is the Haweswater Aqueduct Resilience Programme (HARP), which the board considered during the year.

The information currently available suggests that the DPC route has the potential to offer the best value for customers and therefore supports the position that this should be tested by progressing HARP through a DPC procurement process. Given the importance of this asset to the business, this decision is included in the statement by the directors in performance of their statutory duties in accordance with S172(1) of the Act and set out on page 13 of the UUG 2022 Annual Report.

### Diversity, equality and inclusion

The board recognises the need to recruit and retain fantastic people to enable the delivery of a great service as part of the long-term sustainable success of the business. Good progress has been made on the journey to drive forward diversity, equality and inclusion within the business, as evidenced by the findings of the specialist inclusion partner who conducted a progress review during the year, observing that there was now much greater recognition of the strategic importance of diversity, equality and inclusion within the business with 'great progress in all audited areas', since their initial engagement in October 2020. Further information on diversity, equality and inclusion can be found on pages 44 to 45 of the UUG 2022 Annual Report. Furthermore, as part of the board diversity policy (see page 134 of the UUG 2022 Annual Report) the 'tone from the top' by the Chair has been set, by including the requirement for an inclusive and belonging environment being fostered in the boardroom encouraging open and frank contributions from all board members.

### Delivering against our regulatory contract

Under the current regulatory model, we are a monopoly supplier of water and wastewater services to our domestic customers. Simplistically, the opportunities for improving our financial performance are based on outperforming our five-year contract. Underlying this is a complex set of regulatory key performance indicators, including total expenditure (totex) outperformance, the outcome delivery incentive (ODI) mechanism, customer measure of experience (C-MeX) and financing expenditure (see pages 50 to 83 of the UUG 2022 Annual Report) which are managed and monitored by the business.

### Risk management and internal control

The principal risks and uncertainties to the success of the business, which are agreed by the board, and the ways in which these risks are managed, monitored and mitigated are set out on pages 72 to 88.

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### UW board activity in 2020/21

#### Customer

- Considered and approved the publication and submission to Ofwat of 2022/23 charges for wholesale water, wholesale wastewater and household and new connections services;
- Reviewed updates on activities within customer services including: C-Mex; D-Mex; business market services; complaints; digital initiatives and support for customers in relation to affordability and those in vulnerable circumstances and approved the extension and consolidation of the interim social tariff arrangements used for 2021/22 into future years;
- Regular review and monitoring of the company's operational response and performance in relation to the 2021/22 extreme weather events, particularly the water resources challenges in the summer of 2021;
- Met with representatives of YourVoice, the company's customer challenge group, discussing the ongoing work with the company, YourVoice's assurance on the 2021 annual performance report;
- Reviewed and discussed developments in cyber crime and the activities undertaken to enhance the effectiveness of the company's security controls; and
- Reviewed and delivered developments in the company's technology and digital services.

#### Business as usual

- Received updates on the Security and Emergency Measures Directive;
- Regular updates and discussion of the progress of the Haweswater Aqueduct Resilience Programme (HARP) and approval of the Outline Business Case to Ofwat under the Direct Procurement for Customers approach;
- Received an annual briefing on dam and reservoir safety and the company's risk based approach;
- Reviewed monthly updates on health and safety performance and the annual health and safety report and continued focus on the 'home safe and well' programme embedding a health and safety culture within the business, with added focus being placed on process safety improvements at operational sites;
- Discussed the results of the annual employee engagement survey and updates on the activities of the employee voice panel and links to employee network groups, including the panel's contribution to the work on diversity and inclusion and the next ways of working project; and
- Discussed the company's dashboard of cultural metrics and associated analysis and concluded culture and behaviour are consistent and remain aligned with the company's business purpose, strategy and values;
- Reviewed and monitored the progress against the climate change mitigation/carbon reduction strategy; and
- In-depth review sessions on the Price Review process for the next AMP, the Drainage and Waste Water Management Plan, and the Water Resource Management Plan.

#### Regulatory

- Considered and discussed the independent assurance supporting the 2020 annual performance report, including the risk and compliance statement and the board statement which were approved for submission to Ofwat and publication;
- Received quarterly updates and the annual report on UW's DWI water quality performance;
- Received updates on the Environment Agency's performance assessment;
- Reviewed and accepted modifications to Licence Conditions;
- Reviewed and discussed communications received from Ofwat, the Environment Agency and the Drinking Water Inspectorate;

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- Discussed the Ofwat/Environment Agency investigation, and considered the company's response, into storm overflows; and
- Approval of Water Trading gateway 1 submission to the Regulatory Alliance for Progressing Infrastructure Development (RAPID) and held a deep-dive session to consider water trading.

### Governance

- Granted powers of attorney to senior managers in relation to treasury, commercial and property related matters;
- Approved the appointment of Louise Beardmore as Chief Executive Officer designate with effect from 1 May 2022 and Liam Butterworth as an independent non-executive director with effect from 1 January 2022;
- Reviewed and discussed the external evaluation of the board; and
- Reviewed and approved the slavery and human trafficking statement.

### Financial

- Reviewed and approved UUW's proposed treasury activities for 2021/22;
- Approved the interim dividend;
- Approved the company's annual report and financial statements;
- Approved the company's business plan for 2022/23;
- Reviewed, discussed and approved proposals in relation to pensions in general and endorsed the preferred methodology for Guaranteed Minimum Pension equalisation;
- Received regular updates on financial measures: cash collection, revenue and ODI performance;
- Approved the sustainable finance report for publication;
- Regular review of the progress of Water Plus Group Limited, the joint venture with Severn Trent serving commercial customers and considered and approved the consolidation of credit support in the form of guarantees to Water Plus to align with the requirements of the Wholesale-Retail Code alongside those provided by the joint venture partner; and
- Considered and approved the final capital sanction to close out the West Cumbria Supplies project to provide a long-term sustainable water supply to customers on the West Coast of Cumbria.

### Purpose, vision, values and culture

Our purpose is to provide great water and more for the North West. Our vision is to be the best UK water and wastewater company through providing the best service to customers, at the lowest sustainable cost and in a responsible manner. In setting the company's purpose, the board took into account information and views from stakeholders, utilising much of the research and engagement that contributed to our 2020–25 business plan submission and feedback obtained from customers as part of the company's brand refresh undertaken during 2019/20. For the year ended 31 March 2022, the board is satisfied that the formulation of our aspirations in terms of our purpose, values and culture have been informed by our stakeholders and we operate our business in such a way that will create long-term value for all.

Our values demonstrate how we behave individually and collectively as the board and how we ask our employees to behave. Our employees are fundamental to delivering our strategy and achieving our purpose. Our values of being customer focused, trustworthy and innovative underpin our culture of behaving as a responsible business in the way we interact with all the stakeholders we serve. We must continually reinforce these values so that the right behaviours cascade throughout the organisation, ensuring our culture of behaving responsibly drives what we do

### Monitoring our culture

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Throughout the organisation, our culture is monitored to ensure behaving responsibly drives what we do. Key to this is taking action to address any issues where there is misalignment with the company’s culture. We are pleased to have received external validation of our approach to monitoring culture, featuring as a best practice case study with the Financial Reporting Council ‘Creating Positive Culture Opportunities and Challenges Report’, December 2021. A recent independent audit found our approach to be a “pragmatic and effective model” for supporting the board in their role of monitoring and assessing culture and a “useful framework for driving improvements and interventions” (PwC, February 2021).

### Listening to our employees



Our employees are at the heart of the culture of our business and their ‘lived experience’, is a key part of the board’s assessment and monitoring of culture. Alison Goligher, the current designated non-executive director for engagement with the workforce, facilitates two-way dialogue between the board and employees. There is an open invite to all board members to attend meetings of the panel and during this year, Sir David and Kath Cates have participated and answered questions from panel members on board strategy. Alison chairs the Employee Voice panel (the panel) formed from representatives of a number of employee groups and employee networks from within the business and with representatives drawn from across the geographical region. Alison has met the panel virtually four times throughout the year. In order to ensure two-way communication, Alison provides updates to the panel from the perspective of the board and its committees, and similarly she provides feedback to the board on the work of the panel. Alison also has regular meetings with senior trade union representatives as part of the agreed panel approach. The panel has adapted its approach during the pandemic and moved from face-to-face and site meetings to virtual meetings. These have proved popular with panel members, particularly field-based operational staff who find it much easier to attend virtually than travel from their operational sites. There are 30 members of the panel and membership rotates approximately every two years.

The panel has been provided with business updates and information sessions to broaden their knowledge of the board and corporate governance. The three key sub-groups have focused on the continual improvement of the employee opinion survey, supporting our employee networks to promote diversity and inclusion across the company, and to explore in more detail the drivers and measures of organisation culture. The culture sub-group has focused its energies on obtaining a grass-roots view of the changes to the ways of working during the pandemic and contributed to the ‘next ways of working’ project. It also contributed to discussions on topical issues relating to culture, such as the focus on racial inequality. Employees’ views are measured annually through the employee engagement survey with the objective of taking any required action to improve how permanent employees feel about the company and understand its direction. Employees are provided with information through briefings and access to online materials, to enable them to understand the financial and economic factors affecting the group’s

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performance. Along with our employee relations team, our CEO holds regular face-to-face meetings with senior trade union representatives to facilitate two-way communication and engagement with the views of employees' representatives.

The group has a commercial arrangement with a third party for the provision of agency staff and contractors. Engagement and communication in relation to these members of the wider workforce is managed directly by the third party via a dedicated third party account manager who liaises directly with the company's human resources team. If there is any significant change activity, a representative of the third party joins the project team, thereby ensuring consistency when communicating key information to employees, agency staff and contractors.

Set out on pages 30 to 32 of the UUG 2022 Annual Report is the company's approach to our engagement with and creating value for employees, with health, safety and wellbeing a priority. Furthermore, an explanation of the company's approach to rewarding the workforce can be found in the report of the remuneration committee on page 183 of the UUG Annual Report and Financial Statements.

### Whistleblowing policy

As part of our two-way communication the board has responsibility for reviewing the group's arrangements for individuals to raise matters of concern and the arrangements for the investigation of such matters. The group's whistleblowing policy (the policy) supports the culture within the group where genuine concerns may be reported and investigated without reprisals for whistleblowers. A confidential telephone helpline and a web portal are available to enable employees (including agency workers and contractors) to raise matters of concern in relation to possible incidents of 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 that have caused or may cause damage to the environment, such as pollution or other contamination. Both the helpline and web portal are operated by a third party, enabling any concerns to be reported anonymously. The policy states that no employee will be victimised for raising a matter in accordance with the policy. Matters raised with the helpline/portal are in the first instance raised with the relevant director and investigated by senior managers independent of any involvement of the issues being considered. Details of the findings of the investigation and proposed solution are considered by the whistleblowing committee (whose membership comprises the company secretary, the customer services and people director, the strategy, policy and regulation director, the head of internal audit and the commercial, engineering and capital delivery director) and which meets quarterly. The board routinely reviews matters considered by the whistleblowing committee, the outcome of the investigation and the ways in which the matters were brought to a conclusion, thus ensuring that the core value of integrity is upheld and fostering an environment where employees feel it is 'safe to speak up' and to do so without fear of reprisal.

### Our stakeholders

The board has direct contact with various stakeholder representatives, including: Ofwat and YourVoice (the independent customer challenge group). The chair of YourVoice attends a UUG board meeting to provide an opportunity for discussion, in-depth customer insight and the sharing of views.

Engagement with representatives of all our stakeholder groups occurs widely across many aspects of the business, and more information can be found on pages 30 to 32 of the United Utilities Group PLC Annual Report.

Further information on stakeholder engagement can be found in the report of the United Utilities Group PLC corporate responsibility committee on pages 156 to 159 and in the measures reported on pages 52 to 74 of the United Utilities Group PLC Annual Report for the year ended 31 March 2022.

### 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 funding to build and improve our water and wastewater treatment works and associated network of pipes for each five-year cycle and beyond. We

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are heavily reliant on successfully raising 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 debt capital markets (with maturities typically ranging from seven years to up to 50 years at issue). Debt finance is primarily raised via the group's London listed multi-issuer Medium Term Note Programme (the programme limit was increased and redenominated from EUR7 billion to £10 billion in November 2021), 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), remains a significant lender to United Utilities Water, currently providing around £1.1 billion of loan funding supporting past capital investment programmes, with our existing EIB loan portfolio expected to 'run-off' in line with the scheduled maturities of each loan.

A greater proportion of the group's term finance is therefore likely to come from the debt capital markets, including funding raised under the group's sustainable finance framework that was established in November 2020. In July 2021, the group published its inaugural sustainable finance framework allocation and impact report, which provides credit investors with details on the use of proceeds of our debut sustainable bond issue, along with the selected case studies on eligible projects funded.

The group currently has gross borrowings of circa £7,979.8 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 to keep credit investors informed of significant events. The treasury team has regular dialogue with the group's relationship banks, the EIB and the credit rating agencies. More information can be found on our website at [unitedutilities.com/corporate/investors/credit-investors](https://unitedutilities.com/corporate/investors/credit-investors)

Rating agency services continue to be provided to the group by Moody's Investors Service Limited, Fitch Ratings Ltd and S&P Ratings UK Limited under contracts signed at the beginning of 2020 for an initial three-year term. Debt capital markets issuance by the group has therefore been made on a solicited basis by all three rating agencies during the 2021/22 financial year.

### Chair of the board

The role and behaviour of the Chair is fundamental to the effective operation and decision-making of the board and in creating an atmosphere where open and frank discussion is facilitated and encouraged. The roles and responsibilities of the Chair are set out as part of the company's governance framework. Sir David was independent on appointment when assessed against the circumstances set out in provision 10 of the code.

It is the role of the Chair, supported by the company secretary, to drive forward the business agenda of board meetings to ensure that the board is kept abreast of the regulatory drivers and strategic needs of the business, and to ensure that the directors receive accurate, timely and clear information. The Chair and company secretary hold regular meetings to discuss agenda items and board materials. Board packs are distributed electronically five days before the meeting. Ensuring board materials are of an appropriate length, on what can be particularly complex and technical issues, is a constant challenge, and progress has been made during the year by the introduction of a revised board paper template.

### 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 Chair of any potential conflict or potential new

## Corporate governance report

appointment or directorship. Additionally, the board reviews the position of each director annually. No changes were recorded that would impact the independence of any of the directors. No conflicts of interest had arisen during the year.

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 is overcommitted and unable to fulfil their responsibilities as a board director for United Utilities. 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 Chair would be responsible for discussing the matter with them and agreeing a course of action.

During the year, permission was sought from the board to take on additional non-executive responsibilities by: Kath Cates as a non-executive director of Brown Shipley, and by Steve Mogford who will join the board of QinetiQ Group plc as a non-executive director with effect from 1 August 2022.

Executive directors are not normally allowed to take on more than one non-executive position, a non-executive role is considered to be beneficial from a developmental perspective.

### Ongoing board development and training

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 director's element of the board evaluation exercise, directors are asked to identify any skills or knowledge gaps they would like to address. Directors made a number of suggestions, as set out on page 136 of the UUG 2022 Annual Report.

Consideration of ESG 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 UUG Annual Report pages 121 to 123 of the UUG 2022 Annual Report and pages 110 to 112 of this Annual Report, and the report of the corporate responsibility committee on pages 156 to 159 of the UUG 2022 Annual Report). The board's approach to these matters is reflected in our strategic themes, 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, whose role is predicated on protecting customer interests in how the group goes about its business, the board is kept informed of customer, in-region environmental affairs and social matters.

In addition to this less formal approach to board development, during the year the board 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. Non-executive directors completed an in-house online training course on water quality awareness. A number of board members attended events organised by Ofwat for non-executive directors.

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, Alison Goligher has again chaired the Employee Voice panel as part of the ongoing work to ensure the board has a direct link to understanding the views of employees (see page 126 of the UUG 2022 Annual Report) of the business. Paulette Rowe has contributed to the work on diversity, equality and inclusion (see pages 44 to 45 of the UUG 2022 Annual Report).

### Induction of new non-executive directors

An induction programme is arranged for new non-executive directors. The programme for Liam Butterworth is set out on page 135 of the UUG 2022 Annual Report. On joining the board, non-executive directors would 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.

## Corporate governance report

New directors receive information on the key duties of being a director of a regulated water company. They are required to meet with representatives of Ofwat prior to appointment.

### Wider succession pipeline and talent management

For a number of years, the group has had a written succession plan for the executive directors and other members of the executive team, which includes outline timescales. The plan was developed further during the year and a more structured approach adopted towards the executive succession pipeline. The 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 board appointments, in aiming 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/or participating in an executive business school programme, as appropriate. 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. The 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, and is a way of gaining valuable experience that may be applied at United Utilities so long as no conflicts of interest occur.

During the year, board directors had a number of opportunities to meet with members of the executive team, both formally when senior managers were required to present at board meetings on matters related to their responsibilities, and on more informal occasions.

Our graduate and apprentice programmes are thriving and from time to time, board members have the opportunity to attend events and meet with members of these programmes and other employees identified as potential talent within the business.

Historically, our industry has been male dominated, but measures are in place to increase diversity in broad terms among our employees (see pages 44 to 45 of the UUG Annual Report and Financial Statements). At present fifty per cent of our executive team (excluding the CEO and CFO) is female, as yet there is no ethnic diversity among the team. The gender balance of the direct reports of the executive team is 65 per cent male and 35 per cent female, representation of ethnic minorities is 3 per cent. Gender pay data can be found on page 44 of the UUG Annual Report and Financial Statements.

Along with the wider employee population, we continue to work towards improving the diversity of our succession pipeline as part of our ongoing diversity and inclusion plans.

### Oversight of financial aspects of ESG

ESG, and behaving responsibly, has been a long-term commitment and part of the board ethos for many years and is embedded throughout the business. It naturally flows through into the board's approach to the integrity of the group's financial reporting. Recognising that climate change is a key risk to the group's provision of water and wastewater services (see page 70), 2021/22 is the third year that the group has reported against the TCFD recommendations. As part of the processes supporting the provision of the 'fair, balanced and understandable' statement, the board took into account the existing processes of review and assurance of the TCFD and wider narrative reporting. Management reviewed the assurance processes relating to narrative reporting and ESG matters, particularly those relating to TCFD reporting, and determined that the levels of assurance provided by the combination of the work by internal audit and of the various third parties was satisfactory at this time – a stance endorsed by the

## Corporate governance report

audit committee. The TCFD report addresses the TCFD recommendations and includes, for the second year, scenario analysis (see pages 46 to 50). Inclusion of climate-related information in accordance with the TCFD is mandatory for the company in its 31 March 2023 annual report.

### **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 (see page 67) 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 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 risk profile is reviewed in conjunction with the full and half-year reporting cycle alongside deep dives and routine performance reviews.

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. Climate change is a causal risk theme that underpins our core operations and provision of water and wastewater services to customers (see page 70).

### **Going concern and long-term viability**

The directors considered it appropriate to prepare the financial statements on the going concern basis, as explained in the basis of preparation note to the accounts on page 151.

#### **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 2029.**

#### ***Basis of assessment***

This viability statement is based on the fundamental assumption that the current regulatory and statutory framework does not substantively change. The long-term planning detailed on pages 18 to 19 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 5 to 21.

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. Specifically, risks associated with current levels of economic uncertainty and climate change have been incorporated into the baseline position and factored into the various scenarios modelled as part of the group's assessment. 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 72 to 88. This approach considers the full range of categories of risk that could impact the company, such as financial, operational and regulatory risks. In addition, consideration is given to the adequacy of workforce policies and practices, all liabilities including pension liabilities, any exposure to

## Corporate governance report

revenue variations, and expectations of future performance taking account of past performance in delivering for customers.

Within the context of this long-term planning and management of risks, the group's principal business operates within five-year regulatory price control cycles. Medium-term planning considers the current price control period, over which there is typically a high degree of certainty, and looks beyond this in order to facilitate smooth transitions between price control periods. This results in the board concluding a recurring period of seven years to be an appropriate period over which to perform a robust assessment of the group's long-term viability.

### ***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 £657 million of available liquidity at March 2022 providing 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 circa 65 per cent, a robust pension position and current credit ratings of A3/BBB+/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; and
- The current regulatory framework within which the group operates – which provides a high degree of cashflow 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 finance in most market conditions, and expects to continue to do so into the future. This is despite the group no longer having access to future EIB funding following the UK's exit from the EU.

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 88. The baseline plan against which the viability assessment has been performed incorporates the estimated impact of current high levels of inflation which are expected to endure in the near term before falling to more normal levels. This baseline plan is then subject to further stress scenarios and reverse stress testing that takes into account the potential impact of the group's principal risks. Such risks include: environmental risks such as the occurrence of extreme weather events and other impacts of climate change, further details of which are included in the group's TCFD disclosures on pages 41 to 57; political and regulatory risks; the risk of critical asset failure; significant cyber security breaches; current economic uncertainties including high levels of inflation and a squeeze on the cost of living impacting the group's customer base; and the potential for a restriction to the availability of financing resulting from a capital markets crisis.

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The scenarios considered are underpinned by the group’s established risk management processes, taking into account those risks with a greater than 10 per cent (1 in 10) cumulative likelihood of occurrence. Risks associated with current economic conditions are reflected within the baseline position, with further potential downside risks (most notably in relation to bad debt and low inflation) covered by the individual scenarios modelled, and collectively within a combined scenario.

Based on these risks, the following six largest impacting scenarios were identified and applied as downside stress scenarios to UUW’s baseline plan:

Scenario modelled	Link to risk factors
<b>Scenario 1:</b> Totex £500m one-off impact in 2022/23	Broadly representing the largest ‘severe but reasonable’ risk which is a critical asset failure, all assumed to be operating costs
<b>Scenario 2:</b> Totex underperformance of 10% (c£120m–c£140m) per annum for 2022/23–2028/29	Representing more than the cumulative total expected NPV totex impact of the remaining top 10 ‘severe but reasonable’ risks (including environmental, cyber security and network failure risks)
<b>Scenario 3:</b> CPIH inflation of 2.0% below baseline plan for 2022/23 and 2023/24, and 1.0% below baseline plan for 2024/25–2028/29	Consistent with quantum of inflation impacts modelled within top 10 severe but reasonable risks
<b>Scenario 4:</b> An increase in bad debt of £15m per annum from 2022/23 to 2028/29	Aligned to internal risk factor on debt collection.
<b>Scenario 5:</b> Additional ODI penalty of c£50m per annum	Assumes mid-point of UUW’s baseline and FD P90 ODI position
<b>Scenario 6:</b> Combined scenario – 50% of scenarios 2-5	50% of scenarios 2-5
<p>Example mitigations (of which none are required to remain viable under the scenarios modelled):</p> <ul style="list-style-type: none"> <li>• Issuing of new finance</li> <li>• Reduction in discretionary totex spend</li> <li>• Capital programme deferral</li> <li>• Closing out of derivative asset position</li> <li>• Restriction of dividend</li> <li>• Raising of new equity</li> </ul>	

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.

The most extreme of the severe but reasonable scenarios modelled, without any mitigating action, resulted in: UUW comfortably retaining investment grade credit ratings and no projected breaches of financial debt covenants.

## Corporate governance report

As part of the assessment, reverse stress testing of two extreme theoretical scenarios focusing on totex overspend and persisting low inflation have been performed to understand the extent to which the group could further absorb financial stress before it reaches a sub-investment grade credit rating. This reverse stress testing demonstrated that these extreme conditions would have to be significantly outside what would be considered 'severe but reasonable' scenarios before the group's long-term viability would be at risk.

### ***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, including hybrid debt; capital programme deferral; reduction in other discretionary totex spend; the closeout of derivative asset positions; the restriction of dividend payments; and access to additional equity.

Consideration of the mitigating actions that could be applied would take account of the specific circumstances arising under different extreme scenarios. For example, to mitigate against a large one-off impact (such as scenario 1 - £500m one-off totex impact), liquidity could be quickly enhanced by issuing new finance, accessing additional equity or closing out derivative asset positions. Where longer-term persisting impacts were expected (such as in scenario 2-6) mitigations such as the restriction of dividend payments or a reduction in discretionary totex spend are viable alternative options. However, it should be stressed that no specific mitigating actions are required under any of the six scenarios modelled above.

### ***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 note to the accounts.

## **Significant issues considered in relation to the financial statements**

With regard to the UUG financial statements the UUG audit committee and the UUG board reviewed a number of principal areas of judgement. These are disclosed on pages 151 to 152 of the UUG 2022 annual report and are all applicable to UUG with the exception of accounting for the proposed sale of United Utilities Renewable Energy Limited (UURE).

### **External auditor**

KPMG are appointed as statutory auditor to all wholly owned companies in the United Utilities group. The company adheres to the UUG policy on non-audit services provided by the external auditor and in relation to auditor independence (see pages 149 to 150 of the UUG 2022 annual report). The company's licence requires the preparation of audited regulatory accounts, therefore there are many advantages and efficiencies if KPMG also audits the regulatory accounts. Information on the assessment of the effectiveness of the external audit process can be found on pages 148 to 149 of the UUG 2022 annual report.

The appointment of statutory auditor is the responsibility of the UUG audit committee, as is the responsibility for agreeing the audit fee and the appointment of the audit engagement partner.

## Corporate governance report

### Licence obligations

The board receives reports about the performance of the company, and during the year approved the 2021 Annual Performance Report and the associated Risk and Compliance Statement (the 'Statement'). The Statement sets out how the board pays particular regard to, and awareness of and how, it meets the obligations of its Licence.

### Assessing the effectiveness of the internal audit function

Details of the main features of the United Utilities group's internal audit function can be found on page 153 of the UUG 2022 Annual Report.

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 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 in 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.

### Risk management systems

The group designs its risk management activities to manage rather than eliminate the risk of failure to achieve its strategic objectives. 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. A diagram and explanation of the risk management governance and reporting process can be found on page 101 of the UUG 2022 Annual Report. 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 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 in order to maintain an up to date view of the assessment of risk. 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 against the key elements of ISO 31000:2018 Risk Management

## Corporate governance report

Standard. 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 2017/18.

### **Anti-fraud and anti-bribery**

The audit committee is responsible for reviewing the group's procedures for detecting fraud, and the systems and controls for preventing other inappropriate behaviour. 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, the customer services and people director, the strategy, policy and regulation director, the commercial, engineering and capital delivery director and the 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 apprised in regular updates on the progress and findings of investigations of cases of alleged fraud and any remedial actions taken.

In line with the group's anti-fraud culture and zero-tolerance attitude towards fraud, a fraud incident forum has been established to identify and understand potential threats, and optimise the group's response and mitigation and ensure consistency across the business.

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. Employees in certain roles are required to complete anti-bribery training materials. As part of the anti-bribery programme, employees must comply with the group's hospitality policy. The hospitality policy permits employees to accept proportionate and reasonable hospitality for legitimate business purposes only and all hospitality (and gifts) offered and accepted has to be logged, and approved when accepted. Employees and representatives of the group's suppliers must comply with the group's responsible sourcing principles and United Supply Chain approach. The group will not tolerate corruption, bribery and anti-competitive actions and suppliers are expected 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 UUG audit committee.

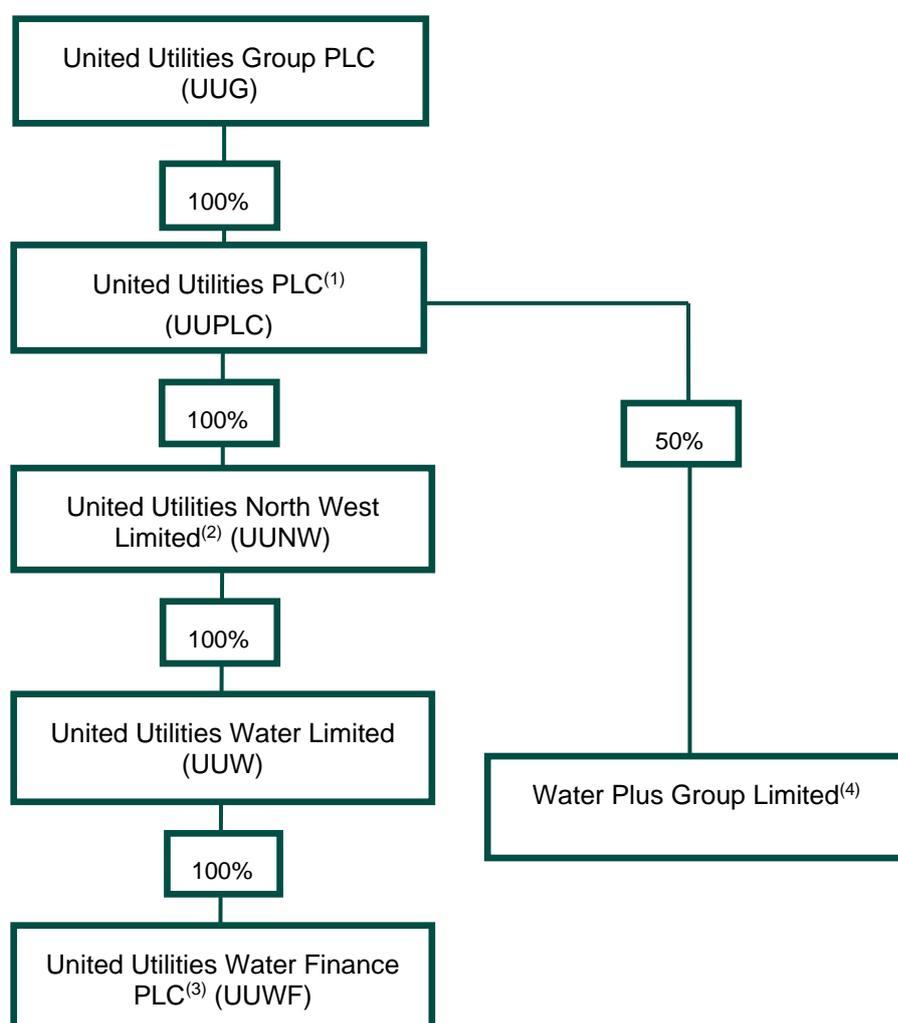
## Corporate governance report

### United Utilities group structure

As a group, United Utilities has a simple corporate structure. UUG has a primary listing on the London Stock Exchange with a stock code of 'UU'; it has around 70,000 registered shareholders. Below UUG, there are two intermediate holding companies, United Utilities PLC (UUPLC)<sup>(1)</sup> (which is also the holding company for a number of non-regulated and legacy/dormant companies) and United Utilities North West Limited (UUNW)<sup>(2)</sup>. The regulated company UUW is a direct subsidiary of UUNW which in turn is a direct subsidiary of UUPLC. Neither UUPLC nor UUNW are operational entities.

All companies are registered in England and Wales and copies of their accounts are available at Companies House.

### United Utilities group structure chart



<sup>(1)</sup>United Utilities PLC – was the listed ultimate holding company prior to July 2008, when the United Utilities group of companies underwent a scheme of arrangement as part of the return of value to shareholders from the proceeds of the sale of the electricity distribution business. This company is used from time to time to raise debt financing.

<sup>(2)</sup>United Utilities North West Limited – previously held the electricity distribution business prior to its disposal in 2007 and is retained for legal purposes.

<sup>(3)</sup>United Utilities Water Finance PLC is used to raise debt finance in support of UUW.

<sup>(4)</sup>Water Plus Group Limited – 50 per cent joint venture with Severn Trent serving customers in the non-household (business) water and wastewater retail market.

## Corporate governance report

### Directors' remuneration report

This report should be read in conjunction with note 3 to the financial statements, which provides information in respect of the total directors' remuneration.

All directors of United Utilities Water Limited (Uuw) are also directors of United Utilities Group PLC (UUG). Further remuneration details including the policy can be found in the annual report and accounts of UUG.

For the purposes of this disclosure, the company's directors can be split into two categories:

- executive directors of Uuw; and
- non-executive directors of Uuw.

#### Non-executive directors

As outlined in the annual report and accounts of United Utilities Group PLC, the non-executive Chairman and non-executive directors do not participate in the company's incentive arrangements (i.e. annual bonus or share schemes) and were paid no remuneration linked to water service standards.

#### Executive directors' remuneration in 2021/22 (audited information)

	Base salary £'000	Benefits £'000	Cash allowance in lieu of pension £'000	Bonus £'000	Long-term incentives <sup>(2)</sup> £'000	Total £'000
Steve Mogford	784	23	173	727 <sup>(1)</sup>	1,471	3,178
Phil Aspin	405	21	49	452	113	1,040

Note:

<sup>(1)</sup> Steve Mogford informed the committee that he wished to unconditionally waive £150,000 of his 2021/22 bonus. This is reflected in the details shown.

<sup>(2)</sup> The long-term incentive is in respect of the Long Term Plan (LTP) award which was granted in June 2019 for which the outcome is based on performance over the three-year period from 1 April 2019 to 31 March 2022. The LTP amount is estimated as the vesting percentage for the one-third relating to customer service excellence will not be known until later in 2022, and the award for Steve Mogford will not vest until the end of an additional holding period. Phil Aspin's award was granted prior to his appointment to the board and so no holding period applies. For the purpose of this table the value of LTP awards has been calculated using an average share price over the three-month period from 1 January 2022 to 31 March 2022 of 1,064.4 pence per share. This is greater than the share price at the time these awards were made to participants and accordingly some of the value shown is attributable to share price appreciation. See page 179 of the UUG 2022 Annual Report for further details.

A recharge of £231,000 during the year ended 31 March 2022 (2021: £221,000) was charged to other companies in the United Utilities group in relation to the provision of executive director services (£177,000 (2021: £168,000) and non-executive director services (£55,000 (2021: £53,000)).

## Corporate governance report

### Directors' remuneration report (continued)

#### 2021/22 annual bonus (audited information)

Measure	Steve Mogford		Phil Aspin	
	Max. %	Actual %	Max. %	Actual %
<b>Underlying operating profit</b>	25.0	25.0	25.0	25.0
C-MeX ranking versus the other WASCs	10.0	3.8	10.0	3.8
Written complaints	10.0	10.0	10.0	10.0
Outcome delivery incentive (ODI) composite	35.0	27.2	35.0	27.2
Time, cost and quality of capital programme (TCQI)	20.0	20.0	20.0	20.0
<b>Total as % bonus maximum</b>	<b>100.0</b>	<b>71.3<sup>(1)</sup></b>	<b>100.0</b>	<b>86.0</b>
<b>Total as % base salary</b>	<b>130.0</b>	<b>92.7</b>	<b>130.0</b>	<b>111.7</b>
<b>Total £'000</b>		<b>727</b>		<b>452</b>

<sup>(1)</sup> Steve Mogford informed the committee that he wished to unconditionally waive £150,000 of his 2021/22 bonus. This is reflected in the details shown.

For each of these bonus measures there was a threshold level of performance which triggered a partial payment of bonus with a sliding scale providing for achievement of up to 100 per cent of the relevant element of bonus.

#### Long-term incentives

For 2021/22 the performance measures, and achievement against those measures for UUG shares previously granted to UUG executive directors which vested in 2021/22, or whose performance period ended in 2021/22 are summarised below:

Performance measure	Weighting	Achievement
<b>Relative total shareholder return (TSR)</b> versus the median TSR of FTSE 100 companies (excluding financial services, oil and gas and mining companies)	33.3%	33.3% out of 33.3% (Actual)
<b>Return on Regulated Equity (RoRE)</b> . Average RoRE compared to the average allowed return set by the regulator across the three year performance period	33.3%	33.3% out of 33.3% (Actual)
<b>Customer service excellence</b> . Ranking for the year ended 31 March 2022 out of the 11 water and wastewater companies using a combined customer service measure comprising C-MeX performance and customer complaints	33.3%	33.3% out of 33.3% (Estimated) <sup>1</sup>
<b>Total vesting</b>		<b>100.0%</b>

<sup>(1)</sup> This is an estimate as the final outcome will not be known until the volume of written complaints received by other companies are available later in 2022.

## Corporate governance report

### Directors' remuneration report (continued)

Details of the number of UUG shares vesting and value of these shares which vested in 2021/22, or whose performance period ended in 2021/22, are as follows:

Director	Number of shares vesting	Value of shares vesting £'000
	2019 LTP <sup>1</sup>	2019 LTP <sup>2</sup>
Steve Mogford	138,222	1,471
Phil Aspin	10,597	113

<sup>(1)</sup> The 2019 Long Term Plan (LTP) awards were granted in June 2019 and performance was measured over the three-year period from 1 April 2019 to 31 March 2022. As Steve Mogford was an executive director when his award was granted in 2019 it will normally vest following an additional holding period so that the overall vesting period is at least five years from the grant date, and the unvested shares will remain subject to withholding provisions during this holding period. Phil Aspin was not an executive director when his award was granted and so in line with the remuneration policy this historic award will vest once the final outcome is confirmed. Under the shareholding guidelines he will be required to hold the vesting shares (on a net of tax basis).

<sup>(2)</sup> The value of the 2019 LTP awards has been calculated by multiplying the number of shares vesting by the average UUG share price over the three month period 1 January 2022 to 31 March 2022 (1,064.4 pence per share).

## Corporate governance report

### UK Tax policies and objectives

Consistent with our wider business objectives, we are committed to acting in a responsible manner in relation to our tax affairs.

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 and always seek to declare profits in the place where their economic substance arises;
- 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 adhere fully 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 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 to actively manage any such risk.

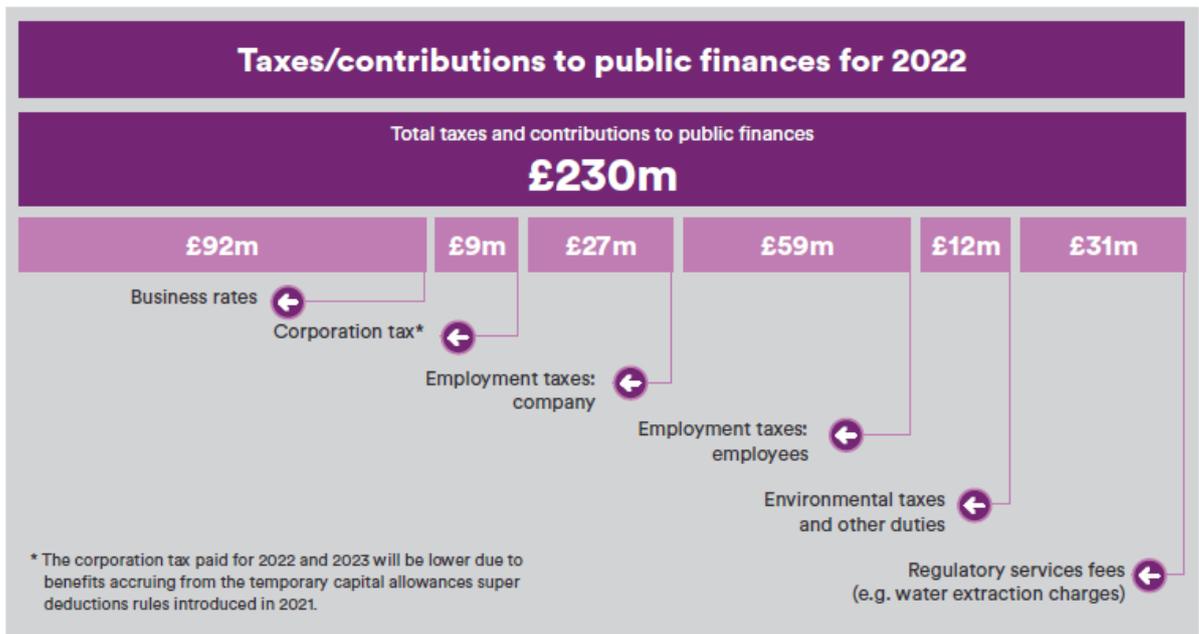
In any given year, the group's effective cash tax rate on underlying profits may fluctuate from the standard UK rate mainly due to the available tax deductions on capital investment. These deductions are achieved as a result of utilising tax incentives, which have been explicitly put in place by successive governments precisely to encourage such investment. This reflects responsible corporate behaviour in relation to tax.

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 2021/22, the impact of tax deductions on capital investment alone reduced average household bills by around £20.

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.

Every year, the group pays significant contributions to the public finances on its own behalf as well as collecting and paying further amounts for its 5,000 strong workforce. Details of the total payments for 2022 of around £230 million are set out below.

## Corporate governance report



The above tax policy disclosure meets the group's statutory requirement under Paragraph 16 (2) of Schedule 19 of Finance Act 2016 to publish its UK tax strategy for the year ended 31 March 2022.

See our website for our latest separate annual tax report, which includes further details in relation to the following key areas:

- How much tax we pay;
- How we ensure that we the right tax at the right time; and
- How we ensure our tax affairs are transparent for all our stakeholders.

Recognising the United Utilities group's ongoing commitment to paying its fair share of tax and acting in an open and transparent manner in relation to its tax affairs, we were delighted to have retained the Fair Tax Mark independent certification for a third year, with UUG having been only the second FTSE 100 company to be awarded the Fair Tax Mark in July 2019.

## Directors' report

Our directors present their management report, including the strategic report, on pages 3 to 88 and the audited financial statements of United Utilities Water Limited (the company) and its subsidiaries (together referred to as the group) for the year ended 31 March 2022.

### Business model

United Utilities Water Limited ("Uuw") is a subsidiary of United Utilities North West Limited. The ultimate parent company of Uuw is United Utilities Group PLC ("UUG").

A description of the company's business model can be found within the strategic report on pages 20 to 51 of the UUG 2022 Annual Report.

### Profit and dividends

The results for the year, set out in the consolidated income statement on page 146 show that loss for the year after tax was £76.7 million (2021: profit after tax of £410.1 million).

The directors have not recommended a final ordinary dividend (2020: £nil). Interim ordinary dividends totalling £339.2 million have been declared and paid during the year (2020: no interim ordinary dividends declared or paid during the year).

### Corporate governance statement

The corporate governance report on pages 89 to 129 is hereby incorporated by reference into this directors' report and includes details of our compliance with Ofwat's board leadership, transparency and governance framework (BLTG), which since 1 August 2019 is contained within the company's Licence as a provider of water and wastewater services. Furthermore, we set out how we have adopted the guiding provisions in the course of meeting the objectives of the BLTG. A copy of Ofwat's BLTG can be found at:

<https://www.ofwat.gov.uk/wp-content/uploads/2019/01/Board-leadership-transparency-and-governance-principles-2019-updated-July-2019.pdf>

### Risk management and internal control

A description of the main features of our risk management and internal control systems in relation to the financial reporting process which forms part of this directors' report are set out on pages 66 to 71.

### Share capital

At 31 March 2022, the issued ordinary share capital of the company was £230.0 million (2021: £230.0 million) divided into 230,000,000 ordinary shares of £1.00 each. Details of our share capital and movements in our issued share capital are shown in note 20 to the financial statements on page 183

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.

### 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 maintains an appropriate level of directors' and officers' liability insurance.

## Directors' report

### Political and charitable donations

It is the company's policy position that 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 can include promoting United Utilities' activities at the main political parties' annual conferences, and occasional stakeholder engagement in Westminster. The group incurred expenditure during the year of £15,834 (2021: £5,801; 2020: £23,627) as part of this process. At the 2021 UUG AGM, an authority was taken to cover such expenditure. A similar resolution will be put to UUG shareholders at the 2022 UUG AGM to authorise such expenditure.

As the provider of services to 7 million people across the North West, customers can sometimes contact their constituency MP and ask that they raise an issue with the company on their behalf. In 2021/22, we received 378 such contacts from MPs' offices covering topics, including flooding, water supply and land management. As part of our work to build constructive relationships with all our stakeholders, we encourage MPs and members of their offices to work closely with us to address constituency concerns and arrange case worker events to discuss such issues in detail. Throughout the year, when COVID-19 guidelines allowed, we held face-to-face meetings with key MPs to discuss a number of topics, including river water quality, storm overflows and recreational land management.

We engage regularly with the two devolved administrations in the North West – the Greater Manchester Combined Authority (GMCA) and the Liverpool City Region (LCR) – as well as the region's local authorities, on a range of topics of shared interest, such as tackling flooding risk and enhancing the North West's natural capital. Our sponsorship of the All-party Political Groups for GMCA and LCR helps bring MPs and peers of all parties together with key leaders to help maximise future investment in these areas for the benefit of local communities.

In addition, the company's activities to engage with political stakeholders on matters relevant to the water industry and its operating footprint in the North West extend to its membership of trade associations. This is described in the section below.

### 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, and the Confederation of British Industry. 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 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 wellbeing of the North West. Our total contribution to these associations in 2021/22 was £408,441 (2020/21: £420,403).

Through Water UK, the company has supported efforts to interact with parliamentary bodies, such as Select Committees and Chairs of specific committees, provide information on topics such as the performance of storm overflows in relation to river water quality. The company supported Water UK in its effort to engage the Government as the Environment Bill passed through its parliamentary stages, including preparation of the 21<sup>st</sup> century rivers report.

Through our membership with both the CBI, in particular as a member of its North West regional council, and the North West Business Leadership Team, we have engaged with regional MPs and political stakeholders, such as local authorities and metro mayors, to explore how the business community can work more effectively with the public sector to drive economic growth in the region and tackle some of the North West's pressing social issues. For example, we have participated in discussions as part of the unlocking regional growth/levelling up agenda, and employee resilience and wellbeing.

## Directors' report

### Employees

Our policies on employee consultation and on equal opportunities for all employees can be found on pages 22 and 24 of the UUG 2022 Annual Report. 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 and where it is safe and practical to do so. Importance is placed on strengthening employees' engagement (see page 30 of the UUG annual report). 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 13. Employees are encouraged to own shares in UUG 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 158.

### Environmental, social and community matters

Details of our approach, as a responsible business, is set out in the Strategic Report, in particular where we describe our approach to purpose and stakeholder value on pages 10 to 11 and 23. Further information is available on our website at [www.unitedutilities.com/corporate/responsibility/](http://www.unitedutilities.com/corporate/responsibility/). Our approach to engagement with our environmental stakeholders and those in the communities we serve can be found on pages 13 to 17. 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 13.

### Customers and suppliers and key stakeholders

Our approach to engagement with customers, suppliers, regulators and other key stakeholders can be found on pages 13 to 17. 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 13. Our United Supply Chain approach sets out how we work with our suppliers, which can be found on our website at: [unitedutilities.com/corporate/about-us/governance/suppliers/delivering-value/united-supplychain/](http://unitedutilities.com/corporate/about-us/governance/suppliers/delivering-value/united-supplychain/); we are 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 2022, our average time taken to pay invoices was 13 days; in the previous six months it was 13 days.

### Energy and Carbon

Our TCFD reporting includes our energy and carbon report on pages 41 to 63 and is hereby incorporated by reference into this directors' report.

### 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 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 A5.

### Events occurring after the reporting period

Details of events after the reporting period are included in note 22.

## Directors' report

### Slavery and human trafficking statement

Our slavery and human trafficking statement can be found on our website at: [unitedutilities.com/human-rights](https://unitedutilities.com/human-rights)

### Going concern basis of accounting

The directors' considerations in preparing these financial statements on a going concern basis of accounting are set out in the corporate governance report and in the basis of preparation and accounting policies note to the financial statements (see page 158).

### Directors

The names of our directors who served during the financial year ended 31 March 2022 can be found on pages 89 to 94.

#### *Non-executive directors*

Sir David Higgins  
Liam Butterworth (appointed 1 January 2022)  
Stephen Carter  
Kath Cates  
Mark Clare  
Alison Goligher  
Brian May (resigned 23 July 2021)  
Paulette Rowe  
Doug Webb

#### *Executive directors*

Phil Aspin  
Louise Beardmore (appointed 1 May 2022)  
Steve Mogford

#### *Secretary*

Simon Gardiner

At no time in the year did any director have a material interest in any contract or arrangement which was significant in relation to the group's business.

### Disclosure of information to the auditor

Each of the persons who is a director at the date of approval of this report confirms that:

1. so far as they are aware, there is no relevant audit information of which the group's auditor is unaware; and
2. they have taken all the steps that he/she ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the group's auditor is aware of that information.

This confirmation is given, and should be interpreted, in accordance with the provisions of section 418 of the Companies Act 2006.

## Directors' report

### Auditor

Pursuant to Section 487 of the Companies Act 2006, the auditor will be deemed to be reappointed and KPMG LLP will therefore continue in office. The remuneration of the auditor will be agreed by the UUG audit committee.

Approved by the board on 28 June 2022 and signed on its behalf by:

**Phil Aspin**

**Chief Financial Officer**

## 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 UK-adopted international accounting standards 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 the group's 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 UK-adopted international accounting standards;
- 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 and a Directors' Report that complies 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.

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.

### 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

## Statement of directors' responsibilities in respect of the annual report and the financial statements

- the strategic and directors' reports include 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 28 June 2022 and signed on its behalf by:

**Phil Aspin**

**Chief Financial Officer**

## Independent auditor's report

to the members of United Utilities Water Limited

### 1. Our opinion is unmodified

We have audited the financial statements of United Utilities Water Limited ("the Company") for the year ended 31 March 2022 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 158 to 163.

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 2022 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with UK-adopted international accounting standards;
- the parent Company financial statements have been properly prepared in accordance with UK-adopted international accounting standards 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.

### 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 board.

We were first appointed as auditor by the shareholders on 22 July 2011. The period of total uninterrupted engagement is for the 11 financial years ended 31 March 2022. 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 public interest entities. No non-audit services prohibited by that standard were provided.

### 2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, 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 decreasing order of audit significance, 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.

## Independent auditor's report

to the members of United Utilities Water Limited

<p><b>Revenue recognition and allowance for household customer debt</b>  Revenue not recognised: £26.6 million (2021: £27.1 million)  Provision for customer debts: £78.3 million (2021: £74.9 million)  Refer to pages 160 to 161 and 216 (accounting policies), and notes 2 and 11 (financial disclosures)</p>	
<p><b>The Risk</b></p> <p><b>Subjective estimate:</b></p> <p>At each balance sheet date:</p> <ul style="list-style-type: none"> <li>- judgment 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</li> <li>- assumptions involving a high degree of estimation uncertainty are required to assess the recoverability of trade receivables.</li> </ul> <p>The effect of these matters is that, as part of our risk assessment, we determined that recognition of revenue and 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 accounting policies on pages 152 to 154) disclose the sensitivity estimated by the group.</p> <p>The risk has increased in the current year due to the likelihood of cash collection profiles changing as a result of the COVID-19 pandemic, particularly when government assistance is withdrawn. This will introduce further uncertainty into the estimation.</p>	<p><b>Our Response</b></p> <p>We performed the tests below rather than seeking to rely on the group's controls because the nature of the balance is such that we would expect to obtain audit evidence primarily through the detailed procedures described.</p> <p><b>Our procedures included:</b></p> <p><b>Accounting analysis:</b> assessed the derecognition of revenue for compliance with relevant accounting standards where the collection of consideration is not probable on the date of initial recognition;</p> <p><b>Methodology choice:</b> assessed the appropriateness of the customer debt provisioning policy based on historical cash collections, credits, re-bills and write-off information, and estimates of future economic scenarios and their impact on credit losses;</p> <p><b>Sensitivity analysis:</b> considered the sensitivity of the key assumptions; and</p> <p><b>Assessing transparency:</b> assessed the adequacy of the group's disclosures of its revenue recognition and customer debt provisioning policies, including the judgement involved in recording revenue and estimation uncertainty of the doubtful debts provision.</p> <p><b>Our results</b></p> <p>We found the amount of the revenue recognised to be acceptable (2021: acceptable);</p> <p>We considered the level of doubtful debt provisioning to be acceptable (2021: acceptable).</p>

## Independent auditor's report

to the members of United Utilities Water Limited

### Capitalisation of costs relating to the capital programme

Property, plant and equipment additions: £728.5 million (2021: £677.5 million)

Refer to pages 162 and 217 to 219 (accounting policies) and note 9 (financial disclosures)

#### The Risk

##### 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 in-year project costs as capital or operating expenditure is inherently judgemental. 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 accounting policies on pages 197 to 203) disclose the sensitivities estimated by the group.

#### Our Response

We performed the detailed tests below rather than seeking to rely on any of the group's controls because our knowledge of the design of these controls indicated that we would not be able to obtain the required evidence to support reliance on controls.

##### Our procedures included:

**Accounting analysis:** assessed the group's capitalisation policy for compliance with relevant accounting standards;

**Tests of details:** critically assessed the capital nature of a sample of projects against the capitalisation policy focusing on new projects approved, project overspend, forecast cost to complete;

**Assessing transparency:** assessed the adequacy of the group's disclosures of its capitalisation policy including the judgement involved in assessing expenditure as capital.

##### Our results:

We found the group's classification of expenditure as capital or operating to be acceptable (2021: acceptable).

## Independent auditor's report

to the members of United Utilities Water Limited

### Valuation of retirement benefit obligations

£2,232.6 million (2021: £2,435.3 million)

Refer to pages 162 and 222 (accounting policies) and notes 15 and A6 (financial disclosures)

#### The Risk

##### 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 to 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 accounting policies on pages 197 to 203) disclose the sensitivities estimated by the group.

#### Our Response

We performed the tests below rather than seeking to rely on the group's controls because the nature of the balance is such that we would expect to obtain audit evidence primarily through the detailed procedures described.

##### Our procedures included:

**Our actuarial expertise:** used our own actuarial specialists to challenge key assumptions and estimates used in the calculation of the retirement benefit obligations; and perform 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;

**Methodology assessment:** we use our own actuarial specialists to assess the appropriateness and consistency of the methodology applied by management in setting the key assumptions;

**Assessing external actuary's credentials:** we assess competence and independence of the external actuary engaged by the group; and

**Assessing transparency:** we consider 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 notes 15 and A6 to the financial statements.

##### Our results

We found the resulting estimate of the retirement benefit obligations to be acceptable (2021: acceptable).

In the previous year the capitalisation of overheads was included in the Capitalisation of costs relating to the capital programme key audit matter. We continue to perform procedures over the capitalisation of overheads but we've excluded it from the key audit matter as the size of the balance is less significant than the judgement around the capitalisation of project costs.

## Independent auditor's report

to the members of United Utilities Water Limited

### 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 £15.9 million (2021: £17.5 million), determined with reference to a benchmark of group profit before tax of £282.8 million, normalised to exclude net fair value gains or losses on debt and derivative instruments disclosed in note 6, of which it represents 5.6% (2021: 4.0%).

Materiality for the parent company financial statements as a whole was set at £15.8 million (2021: £17.0 million), determined with reference to a benchmark of company profit before tax normalised to exclude net fair value gains or losses on debt and derivative instruments disclosed in note 6, of which it represents 5.6% (2021: 3.9%).

In line with our audit methodology, our procedures on individual account balances and disclosures were performed to a lower threshold, performance materiality, so as to reduce to an acceptable level the risk that individually immaterial misstatements in individual account balances add up to a material amount across the financial statements as a whole.

Performance materiality was set at 75% (2021: 75%) of materiality for the financial statements as a whole, which equates to £11.9m (2021: £13.1m) for the group and £11.8m (2021: £12.7m) for the parent company. We applied this percentage in our determination of performance materiality because we did not identify any factors indicating an elevated level of risk.

We agreed to report to the Board any corrected or uncorrected identified misstatements exceeding £0.5 million (2021: £0.5 million), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Of the group's two (2021: two) reporting components, we subjected two (2021: two) to full scope audits for group purposes.

The group team approved the component materialities, which ranged from £6.0 million to £15.8 million (2021: £8.0 million to £17.0 million) having regard to the mix of size and risk profile of the group across the components. The work on all components, including the audit of the parent company, was performed by the group team.

The scope of the audit work performed was predominantly substantive as we placed limited reliance upon the group's internal control over financial reporting.

### 4. Going concern

The directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the group or the company or to cease their operations, and as they have concluded that the group's and the company'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").

We used our knowledge of the group, its industry, and the general economic environment to identify the inherent risks to its business model and analysed how those risks might affect the group's and company's financial resources or ability to continue operations over the going concern period. The risk that we considered most likely to adversely affect the group's and company's available financial resources and metrics related to a one-off total expenditure impact.

## Independent auditor's report

### to the members of United Utilities Water Limited

We considered whether these risks could plausibly affect the liquidity or covenant compliance in the going concern period by assessing the directors' sensitivities over the level of available financial resources and covenant thresholds indicated by the group's financial forecasts taking account of severe, but plausible, adverse effects that could arise from these risks individually and collectively.

Our procedures included:

**Assessing key assumptions in the forecasts:** critically assessing assumptions in base case and downside scenarios relevant to liquidity and covenant metrics such as inflation rate growth compared to market forecasts, forecast bonus payments compared to historical bonus payments and forecast dividend payments compared to group dividend policy. This included assessing whether downside scenarios applied assumptions which are mutually consistent, using our assessment of the possible range of each key assumption and our knowledge of inter-dependencies;

**Funding assessment:** considering the availability of existing debt arrangements and committed loan facilities, including testing compliance with covenants and expected maturity dates;

**Historical accuracy of managements forecasts:** comparing historical budgets to actual results to assess the directors' track record of budgeting accurately;

**Evaluating directors' intent:** evaluating the achievability of the actions the directors consider they would take to improve the position should the risks materialise, including assessment of mitigating actions within their control;

**Assessing the completeness and accuracy of the matters covered in the going concern disclosure:** considering whether the going concern disclosure in the basis of preparation note to the financial statements gives a full and accurate description of the directors' assessment of going concern, including the identified risks and related sensitivities.

Our conclusions based on this work:

- we consider that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate;
- we have not identified, and concur with the directors' assessment that there is not, a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the group's or company's ability to continue as a going concern for the going concern period; and
- we found the going concern disclosure in the basis of preparation note to the financial statements to be acceptable.

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 above conclusions are not a guarantee that the group or the company will continue in operation.

## 5. Fraud and breaches of laws and regulations – ability to detect

### *Identifying and responding to risks of material misstatement due to fraud*

To identify risks of material misstatement due to fraud ("fraud risks") we assessed events or conditions that could indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud. Our risk assessment procedures included:

- enquiring of directors, the audit committee, internal audit and inspection of policy documentation relating to the ultimate parent, United Utilities Group PLC, as to the group's high level policies and procedures to prevent and detect fraud, including the internal audit function,

## Independent auditor's report

### to the members of United Utilities Water Limited

and the group's channel for "whistleblowing", as well as whether they have knowledge of any actual, suspected or alleged fraud.

- reading Board and Audit Committee meeting minutes relating to the ultimate parent, United Utilities Group PLC; and
- considering remuneration incentive schemes and performance targets for directors.

We communicated identified fraud risks throughout the audit team and remained alert to any indications of fraud throughout the audit.

As required by auditing standards, and taking into account possible pressures to meet profit targets and our overall knowledge of the control environment, we perform procedures to address the risk of management override of controls and the risk of fraudulent revenue recognition, the risk that group management may be in a position to make inappropriate accounting entries, and the risk of bias in accounting estimates and judgements such as revenue recognition and provisions for household customer debt and capitalisation of costs relating to the capital programme.

Further detail in respect of the above accounting estimates and judgements is set out in the key audit matter disclosures in section 2 of this report.

We also performed procedures including:

- identifying journal entries to test based on risk criteria and comparing the identified entries to supporting documentation. These included journals relating to revenue, capitalised costs and treasury posted to unexpected or unrelated accounts; and
- assessing significant accounting estimates for bias.

#### ***Identifying and responding to risks of material misstatement due to non-compliance with laws and regulations***

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, through discussion with the directors and other management (as required by auditing standards), 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.

As the group is regulated, our assessment of risks involved gaining an understanding of the control environment including the entity's procedures for complying with regulatory requirements.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

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, pension 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, Environment 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 its legal form. Auditing standards limit the required audit procedures to identify non-compliance with these laws and

## Independent auditor's report

to the members of United Utilities Water Limited

regulations to enquiry of the directors and inspection of regulatory and legal correspondence, if any. Therefore if a breach of operational regulations is not disclosed to us or evident from relevant correspondence, an audit will not detect that breach.

### ***Context of the ability of the audit to detect fraud or breaches of law or regulation***

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 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 fraud, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. Our audit procedures are designed to detect material misstatement. We are not responsible for preventing non-compliance or fraud and cannot be expected to detect non-compliance with all laws and regulations.

### **6. 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 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 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.

### **7. 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.

## Independent auditor's report

to the members of United Utilities Water Limited

### 8. Respective responsibilities

#### *Directors' responsibilities*

As explained more fully in their statement set out on pages 142 to 143, 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 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 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](http://www.frc.org.uk/auditorsresponsibilities).

### 9. 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.

#### **Ian Griffiths (Senior Statutory Auditor)**

for and on behalf of KPMG LLP, Statutory Auditor  
*Chartered Accountants*  
1 St Peter's Square, Manchester M2 3AE  
28 June 2022

## Consolidated income statement

for the years ended 31 March

	Note	2022 £m	2021 £m
Revenue	2	1,844.6	1,797.6
Staff costs	3	(181.7)	(170.0)
Other operating costs	4	(456.6)	(416.8)
Allowance for expected credit losses – trade and other receivables	4	(23.4)	(28.7)
Other income	4	3.6	3.7
Depreciation and amortisation expense	4	(415.6)	(419.3)
Infrastructure renewals expenditure		(169.5)	(164.8)
<b>Total operating expenses</b>		<b>(1,243.2)</b>	<b>(1,195.9)</b>
<b>Operating profit</b>		<b>601.4</b>	<b>601.7</b>
Investment income	5	12.2	18.6
Finance expense	6	(188.0)	(114.6)
<b>Investment income and finance expense</b>		<b>(175.8)</b>	<b>(96.0)</b>
<b>Profit before tax</b>		<b>425.6</b>	<b>505.7</b>
Current tax charge	7	82.0	(78.2)
Deferred tax charge	7	(584.3)	(17.4)
<b>Tax</b>	7	<b>(502.3)</b>	<b>(95.6)</b>
<b>Loss/(profit) after tax</b>		<b>(76.7)</b>	<b>410.1</b>

All of the results shown above relate to continuing operations.

## Consolidated statement of comprehensive income

for the years ended 31 March

	Note	2022 £m	2021 £m
<b>Loss/(profit) after tax</b>		<u>(76.7)</u>	<u>410.1</u>
<b>Other comprehensive income</b>			
<i>Items that may be reclassified to profit or loss in subsequent periods:</i>			
Cash flow hedge effectiveness		106.7	9.3
Tax on items taken directly to equity	7	<u>(1.8)</u>	<u>(1.8)</u>
<b>Other comprehensive income that may be reclassified to profit or loss</b>		<u>104.9</u>	<u>7.5</u>
<i>Items that will not be reclassified to profit or loss in subsequent periods:</i>			
Remeasurement gains/(losses) on defined benefit pension schemes	15	228.7	(62.3)
Change in credit assumptions for debt reported at fair value through profit or loss		(4.1)	(43.3)
Cost of hedging – cross-currency basis spread adjustment		-	(12.7)
Tax on items taken directly to equity	7	<u>(104.7)</u>	<u>30.3</u>
<b>Other comprehensive income that will not be reclassified to profit or loss</b>		<u>119.9</u>	<u>(88.0)</u>
<b>Total comprehensive income</b>		<u><u>148.1</u></u>	<u><u>329.6</u></u>

## Consolidated and company statement of financial position

at 31 March

### Group and company

	Note	2022 £m	2021 £m
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	9	12,082.2	11,732.3
Intangible assets	10	160.8	181.1
Investments	A1	0.1	0.1
Inventories		0.4	-
Retirement benefit surplus	15	771.2	531.0
Derivative financial instruments	A5	399.4	410.3
		<u>13,414.1</u>	<u>12,854.8</u>
<b>Current assets</b>			
Inventories		16.4	16.0
Trade and other receivables	11	227.5	224.8
Current tax asset		98.8	-
Cash and short-term deposits	12	181.9	648.6
Derivative financial instruments	A5	58.1	14.4
		<u>582.7</u>	<u>903.8</u>
<b>Total assets</b>		<u>13,996.8</u>	<u>13,758.6</u>
<b>LIABILITIES</b>			
<b>Non-current liabilities</b>			
Trade and other payables	18	(835.2)	(796.7)
Borrowings	13	(7,897.5)	(7,998.4)
Deferred tax liabilities	16	(2,075.4)	(1,384.6)
Derivative financial instruments	A5	(136.7)	(107.8)
		<u>(10,944.8)</u>	<u>(10,287.5)</u>
<b>Current liabilities</b>			
Trade and other payables	18	(359.2)	(318.3)
Borrowings	13	(473.0)	(717.1)
Current tax liabilities		-	(20.7)
Provisions	17	(13.5)	(11.1)
Derivative financial instruments	A5	(0.4)	(6.9)
		<u>(846.1)</u>	<u>(1,074.1)</u>
<b>Total liabilities</b>		<u>(11,790.9)</u>	<u>(11,361.6)</u>
<b>Total net assets</b>		<u>2,205.9</u>	<u>2,397.0</u>
<b>EQUITY</b>			
<b>Capital and reserves attributable to equity holders of the company</b>			
Share capital	20	230.0	230.0
Other reserves	19	86.5	6.6
Retained earnings		1,889.4	2,160.4
<b>Shareholder's equity</b>		<u>2,205.9</u>	<u>2,397.0</u>

These financial statements for the group and United Utilities Water Limited (company number: 2366678) were approved by the board of directors and authorised for issue on 28 June 2022, and signed on its behalf by:

Phil Aspin  
Chief Financial Officer

## Consolidated and company statement of changes in equity

for the years ended 31 March

### Group and company

	Share capital £m	Other reserves* £m	Retained earnings £m	Total £m
At 1 April 2021	230.0	6.6	2,160.4	2,397.0
Loss after tax	-	-	(76.7)	(76.7)
<b>Other comprehensive income</b>				
Remeasurement gains on defined benefit pension schemes (see note 15)	-	-	228.7	228.7
Change in credit assumptions for debt reported at fair value through profit or loss	-	-	(4.1)	(4.1)
Cash flow hedge effectiveness	-	106.7	-	106.7
Tax on items taken directly to equity (see note 7)	-	(26.8)	(79.7)	(106.5)
<b>Total comprehensive income</b>	-	79.9	68.2	148.1
Dividends (see note 8)	-	-	(339.2)	(339.2)
<b>At 31 March 2022</b>	<u>230.0</u>	<u>86.5</u>	<u>1,889.4</u>	<u>2,205.9</u>

### Group and company

	Share capital £m	Other reserves* £m	Retained earnings £m	Total £m
At 1 April 2020	100.0	9.4	1,958.0	2,067.4
Profit after tax	-	-	410.1	410.1
<b>Other comprehensive income</b>				
Remeasurement gains on defined benefit pension schemes (see note 15)	-	-	(62.3)	(62.3)
Change in credit assumptions for debt reported at fair value through profit or loss	-	-	(43.3)	(43.3)
Cash flow hedge effectiveness	-	9.3	-	9.3
Cost of hedging – cross-currency basis spread adjustment	-	(12.7)	-	(12.7)
Tax on items taken directly to equity (see note 7)	-	0.6	27.9	28.5
<b>Total comprehensive income</b>	-	(2.8)	332.4	329.6
Redemption of preference shares	-	130.0	(130.0)	-
Capitalisation of capital redemption reserve and issue of ordinary shares (see note 20)	130.0	(130.0)	-	-
Dividends (see note 8)	-	-	-	-
<b>At 31 March 2021</b>	<u>230.0</u>	<u>6.6</u>	<u>2,160.4</u>	<u>2,397.0</u>

\* Other reserves comprise the capital redemption reserve, cost of hedging reserve and cash flow hedging reserve. Further detail of movements in these reserves is included in note 19.

As permitted by section 408 of the Companies Act 2006, the company has not presented its own income statement. The results of the company are not materially different from the group.

## Consolidated and company statement of cash flows

for the years ended 31 March

### Group and company

	Note	2022 £m	2021 £m
<b>Operating activities</b>			
Cash generated from operations	A2	1,025.8	1,122.8
Interest paid		(121.2)	(142.5)
Interest received and similar income		1.2	6.3
Tax paid		(37.4)	(72.6)
Tax received		-	26.9
<b>Net cash generated from operating activities</b>		<u>868.4</u>	<u>940.9</u>
<b>Investing activities</b>			
Purchase of property, plant and equipment		(608.8)	(604.5)
Purchase of intangible assets		(19.5)	(33.6)
Grants and contributions received	18	1.8	5.0
Repayment of loans to joint ventures	A7	-	-
<b>Net cash used in investing activities</b>		<u>(626.5)</u>	<u>(633.1)</u>
<b>Financing activities</b>			
Proceeds from borrowings net of issuance costs		343.6	1,605.1
Repayment of borrowings		(723.7)	(1,762.1)
Dividends paid to equity holders of the company	8	(339.2)	-
<b>Net (used in)/cash from financing activities</b>		<u>(719.3)</u>	<u>(157.0)</u>
<b>Net decrease in cash equivalents</b>		<u>(477.4)</u>	<u>150.8</u>
Cash and cash equivalents at beginning of the year		638.5	487.7
Cash and cash equivalents at end of the year	12	<u>161.1</u>	<u>638.5</u>

### 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 A8.

#### **Basis of preparation**

The financial statements have been prepared in accordance with the requirements of the Companies Act 2006, and with UK-adopted international accounting standards. 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 entity 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 entity in the form of cash and committed facilities as well as consideration of the group's capital adequacy, along with a baseline plan that incorporates latest views of the current economic climate, including high levels of inflation in the near term. The directors have considered the magnitude of potential impacts resulting from uncertain future events or changes in conditions, and the likely effectiveness of mitigating actions that the directors would consider undertaking. The baseline position has been subjected to a number of severe but reasonable downside scenarios in order to assess the entity's ability to operate within the amounts and terms (including relevant covenants) of existing facilities. These scenarios consider: the potential impacts of increased totex costs, including a significant one-off totex impact arising in the assessment period; lower CPIH inflation; elevated levels of bad debt; outcome delivery incentive penalties; and the impact of these factors materialising on a combined basis. Mitigating actions were considered to include deferral of capital expenditure; a reduction in other discretionary totex spend; the close out of derivative asset balances; and the deferral or suspension of dividend payments.

Consequently, the directors are satisfied that the entity will have sufficient funds to continue to meet its liabilities as they fall due for at least 12 months from the date of approval of the financial statements, and that the severe but reasonable downside scenarios indicate that the entity will be able to operate within the amounts and terms (including relevant covenants) of existing facilities. The financial statements have therefore been prepared on a going concern basis.

#### **Adoption of new and revised standards**

There were no new standards, interpretations and amendments, effective for the year ended 31 March 2022, that were relevant to the group or would have a material impact on the entity's financial statements, or that were not early adopted in previous years.

#### ***'Phase II' – IBOR reform***

In January 2021, the Secretary of State for BEIS and the EU endorsed the IASB-published amendments to IFRS 9 'Financial Instruments', and IFRS 7 'Financial Instruments: Disclosures' in respect of interest rate benchmark reform, effective for annual periods beginning on or after 1 January 2021 with early adoption permitted ('Phase II' IBOR Reform). The entity chose to early adopt the Phase II reforms for the year ended 31 March 2021, though this has had no impact on the financial statements for the year then ended.

## Accounting policies

The entity also subscribed to the ISDA 2020 IBOR fallbacks protocol in the previous financial year, with these protocols embedding fallback provisions into the group's interest rate derivative contracts enabling a contractual replacement of LIBOR as a benchmark with SONIA. All of the entity's derivative counterparties subscribed to the protocol and from 1 January 2022 the entity's derivative portfolio transitioned from referencing LIBOR to referencing SONIA as the underlying floating interest rate.

As part of the transition, where applicable, the entity has applied the relevant practical expedients from certain requirements in IFRS 9 and IFRS 7 relating to changes in the basis for determining contractual cash flows of financial assets, financial liabilities and hedge accounting.

On 31 December 2021, the group had a balance of £501.6 million loan instruments, along with an additional £555.0 million of undrawn committed facilities that transitioned away from referencing LIBOR as the floating benchmark rate.

Derivatives with a notional value of £5,166.0 million also transitioned on this date, with this figure being inclusive of £2,117.8 million notional value of derivatives designated within fair value hedge relationships. Immaterial hedge effectiveness was recorded in the entity's income statement through the transition as a result of maintaining economic equivalence within the fair value hedge relationships.

Detail on the derivation of this net balance can be found in note A5, along with further information on the entity's transition to alternative benchmarks.

### **Critical accounting judgements and key sources of estimation uncertainty**

In the process of applying its accounting policies set out in note A8, 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. As estimates carry with them an inherent level of uncertainty, the group performs sensitivity analysis where this is practicable and where, in management's opinion, it provides useful and meaningful information. This sensitivity analysis is performed to understand a range of outcomes that could be considered reasonably possible based on experience and the facts and circumstances associated with individual areas of the financial statements that are subject to estimates. 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.

As part of the evaluation of critical accounting judgements and key sources of estimation uncertainty, the group has considered the implications of climate change on its operations and activities, further details of which are set out below.

The following paragraphs detail the estimates and judgements the group believes to have the most significant impact on the annual results as reported in accordance with IFRS, including specific considerations in light of current economic circumstances such as the cost of living experienced by customers.

#### ***Revenue recognition and allowance for doubtful receivables***

*Accounting estimate* – The group recognises revenue generally at the time of delivery and when collection of the resulting receivable has been deemed probable. In estimating the amount of revenue to recognise, where 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 deemed probable. There are two different criteria whereby management does not recognise revenue for amounts which have been billed to those customers on the basis that collectability is not probable. These are as follows:

## Accounting policies

- 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, but has previously had bills de-recognised and has more than their current year debt outstanding.

This two-criteria approach resulted in a £26.6 million reduction in revenue compared with what would have been recognised had no adjustment been made for amounts where collectability is not probable. 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 probable (i.e. the second criteria were disapplied), the required adjustment to revenue would have been £12.4 million lower.

*Accounting estimate* – At each reporting date, the company and each of its subsidiaries evaluate the estimated recoverability of trade receivables and record allowances for expected credit losses based on experience. Estimates 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 2022, an allowance for expected credit losses relating to household customer debt of £78.3 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 increased by £1.1 million or reduced by £0.5 million respectively.

Since early 2020, the group's expected credit loss assessment in respect of trade receivables has been significantly impacted by the economic uncertainty brought about as a result of the COVID-19 pandemic. Whilst economic uncertainty linked to the COVID-19 pandemic has receded somewhat during the year ended 31 March 2022, with households and businesses adjusting to a new post-pandemic norm, a high level of economic uncertainty remains due largely to increases in the cost of living during the year and that are forecast to continue in the near future. This could have a significant impact on many of the group's customers that could in turn affect the ability of some customers to pay their bills.

In recognition of this ongoing future uncertainty, the basis on which the allowance for expected credit losses covering the group's household customer base is assessed has been updated during the year. Whereas in the prior year the allowance for expected credit losses was determined based on the assumption that cash collection experienced over the last two years continues into the future, this would no longer be expected to give a reasonable view of cash collection risk. This is because cash collection for the year has performed strongly and therefore may overstate future cash collection forecasts when considering the current economic climate, while cash collection for the year ended 31 March 2021 was impacted by the COVID-19 pandemic and resulted in much lower levels of cash collection than might be expected on an ongoing basis.

In light of this, a longer run four-year average of cash collection has been modelled and is deemed to give a more realistic forecast for future collection taking into account all of the above factors, including expected increases in the cost of living. This assumption supports the reported household bad debt charge of 1.8 per cent of household revenue. Had future cash collection been assessed based on the average cash collection during the current year only, the bad debt charge would have been 1.6 per cent of household revenue resulting in a reduction in the charge of £2.7 million, with similar results based on using average cash collection from the last two or last three years. If average cash collection from the prior year only was used the bad debt charge would have been 2.0 per cent of household revenue resulting in an increase in the charge of £3.4 million. Consideration of this range of reasonably possible scenarios indicates that, based on current levels of economic uncertainty, the allowance for expected credit losses is within a reasonable range, and that a longer run four year average results in a balanced position in light of current levels of uncertainty.

*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 household 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 dates of

### Accounting policies

the last water 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 2022 was £145.8 million. Had actual consumption been 5 per cent higher or lower than the estimate of units supplied, this would have resulted in revenue recognised for unbilled amounts being £5.0 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 (PP&E) 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 as incurred. Determining enhancement from maintenance expenditure requires an accounting judgement, particularly when projects have both elements within them. Enhancement spend was 57 per cent of total spend in relation to infrastructure assets during the year. A change of +/- 1 per cent would have resulted in £3.9 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 PP&E represent 40 per cent of total support costs. A change in allocation of +/- 5 per cent would have resulted in £2.3 million less/more expenditure being charged to the income statement during the period.

*Accounting estimate* – The estimated useful economic lives of PP&E 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 PP&E 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. The depreciation and amortisation expense for the year was £415.6 million. A 10 per cent increase in average asset lives would have resulted in a £37.8 million reduction in this figure and a 10 per cent decrease in average asset lives would have resulted in a £41.5 million increase in this figure.

#### ***Retirement benefits***

*Accounting estimate* - the group operates two defined benefit 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 A6.

*Accounting estimate* – Included within the group's defined benefit pension scheme assets are assets with a fair value estimated to be £271.7 million that are categorised as 'level 3' assets within the IFRS 13 'Fair value measurement' hierarchy, meaning that the value of the assets is not observable at 31 March 2022. Estimates of the fair value of these assets have been performed by the investment managers' valuation specialists using the latest available statements of each of the funds that make up the total level 3 asset balance, updated for any subsequent cash movements between the statement date and the year end reporting date.

## Accounting policies

### *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 A5.

### **Climate Change**

The group is continually developing its assessment of the impact that climate change has on the assets and liabilities recognised and presented in its financial statements.

The natural environment within which the group operates is constantly changing, and this influences how its water and wastewater services are to be delivered in the future. In addition, the group has embedded ambitious climate-related targets within its own operations, with this affecting the portfolio of assets required to deliver such services.

The impact of climate change has been considered in the preparation of these financial statements across a number of areas, predominantly in respect of the valuation of the property, plant and equipment held by the group.

Asset life reviews are undertaken regularly for facilities impacted by climate change, environmental legislation or the group's decarbonisation measures. This can result in the acceleration of depreciation of assets that are deemed to be commercially obsolete or for which no further use is planned, in part as a result of the group's decarbonisation strategy. In recent years this has resulted in material accelerations in respect of bioresources facilities impacted by changes in environmental legislative requirements. No further material accelerations were required in the current financial year, however this is subject to continuous assessment.

The group is exposed to potential asset write-downs following flooding resulting from extreme weather events, the frequency of which are expected to increase as the effects of climate change become more apparent. Following large-scale flooding, items are identified that have been damaged beyond repair and require immediate accounting write-downs. No such charges were required in the current financial year.

In addition to the risks posed by an increased likelihood of large-scale flooding events in future years, climate change also presents challenges relating to prolonged periods of hot and dry weather, the frequency of which is expected to increase. This could potentially impact the viability of certain types of assets in future years such as those associated with the intake of water from the natural environment, or require a strategic reconfiguration of assets to respond to such challenges. It is expected that if any such impact were to materialise this would be over a longer period of time rather than within a single financial year, and no financial impact has been identified in the current year.

In recent years the group has sought to further enhance the accuracy of its useful life assessments through the introduction of more forward-looking information in asset life reviews. This includes the use of disposal data to identify trends that may inform the group's view of useful lives into the future. This information is used alongside other decommissioning data and data from strategic asset planning systems to inform useful asset lives.

The group mitigates the exposure that the carrying value of its book asset base has to climate-related risks through strategic planning activities that incorporate defined climate scenarios, climate change mitigation pledges, and long-term climate projections. The group installs permanent flood defences and other resilience measures at the most vulnerable facilities to protect its assets.

## Notes to the financial statements

### 1. Segmental reporting

The group operates and is managed as one class of business, which is the provision of water and wastewater services, therefore no segmental information is required to be disclosed.

### 2. Revenue

The group's revenue arises from the provision of services within the United Kingdom.

	2022	2021
	£m	£m
Wholesale water charges	776.5	751.0
Wholesale wastewater charges	946.3	941.5
Household retail charges	68.9	64.1
Other	52.9	41.0
	<u>1,844.6</u>	<u>1,797.6</u>

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.

Wholesale water and wastewater charges relate to services provided to household customers and non-household retailers. Household retail charges relate solely to the margin applied to the wholesale amounts charged to residential customers. These wholesale charges and the applicable retail margin are combined in arriving at the total revenues relating to water and wastewater services provided to household customers. No margin is applied to wholesale water and wastewater services provided to non-household retailers.

Other revenues comprise a number of smaller non-core income streams including 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

	2022	2021
	£m	£m
Fees to non-executive directors	0.8	0.8
Salaries	1.2	1.2
Benefits	0.3	0.2
Bonus	0.7	0.7
Share-based payment charge	1.8	1.7
	<u>4.8</u>	<u>4.6</u>

Included within the above are aggregate emoluments of £2.7 million (2021: £2.5 million) in respect of the highest paid director.

## Notes to the financial statements

### 3. Directors and employees (continued)

A recharge of £0.2 million during the year ended 31 March 2022 (2021: £0.2 million) was charged to other companies in the United Utilities group in relation to the provision of director services. No executive directors accrued benefits under defined benefit schemes, and all executive directors opted for a cash allowance in lieu of their defined contribution pension entitlement during the current and prior year.

Two directors (2021: two directors) received shares in United Utilities Group PLC in respect of qualifying services. Two directors (2021: three directors) had long-term incentive plans which vested during the year. Aggregate amounts receivable relating to long-term incentive plans of £1.6 million (2021: £1.8 million) were recognised during the year. Further details on amounts receivable in relation to long-term incentive plans are included in the directors' remuneration reporting on pages 132 to 134.

#### Remuneration of key management personnel

	2022 £m	2021 £m
Salaries and short-term employee benefits	6.2	6.3
Share-based payment charge	2.6	3.0
	<u>8.8</u>	<u>9.3</u>

Key management personnel comprises all directors and certain senior managers who are members of the executive team.

#### Staff costs (including directors)

	2022 £m	2021 £m
Wages and salaries <sup>(1)(2)</sup>	302.6	274.8
Employee-related taxes and levies	28.2	25.2
Severance	0.4	1.3
Post-employment benefits:		
Defined benefit pension expense (see note 15)	8.1	7.0
Defined contribution pension expense (see note 15)	26.1	23.4
Employee benefits expense before recharges	<u>365.</u>	<u>331.7</u>
Amounts recharged to parent and fellow subsidiary companies	(1.0)	(1.7)
Charged to other areas including regulatory capital schemes	<u>(182.7)</u>	<u>(160.0)</u>
Staff costs	<u>181.7</u>	<u>170.0</u>

#### Notes:

<sup>(1)</sup> Wages and salaries excluding non-permanent staff was £260.3 million (2021: £240.4 million).

<sup>(2)</sup> In order to give a clearer view of the group's total staff costs, wages and salaries and amounts charged to other areas including regulatory capital schemes now include the costs of non-permanent staff who have worked for the group, whose costs were previously included within hired and contracted services presented within other operating costs. Accordingly, these amounts for the year ended 31 March 2021 have been re-presented to show information on a consistent basis, which has resulted in an increase in staff costs and a reduction in the costs of hired and contracted services of £11.6 million compared with what was presented in the financial statements published for that year.

Included within employee benefits expense there were £0.4 million (2021: £1.7 million) of restructuring costs.

## Notes to the financial statements

### 3. Directors and employees (continued)

A recharge of £1.0 million during the year ended 31 March 2022 (2021: £1.7 million) was charged to other companies in the UUG group in relation to the provision of employee services.

Conditional share awards in relation to shares of the ultimate parent undertaking, United Utilities Group PLC, have been granted to employees of the group under various schemes. Details of the terms and conditions of each scheme are given in the 2022 UUG annual report and financial statements. Included within wages and salaries is an expense of £4.6 million (2021: £3.4 million) relating to a recharge of share-based payment costs from the ultimate parent undertaking (see note A7).

#### Average number of staff employed by the group during the year (full time equivalent including directors)

	2022 number	2021 number
Average number of staff employed by the group during the year	5,558	5,158

The 2022 total employee benefits expense, before recharges, of £365.4 million (2021: £331.5 million) includes the employee costs relating to the persons employed during the year noted above in addition to costs of £15.9 million (2021: £17.8 million) in relation to services provided by employees of United Utilities PLC who support UUW. These costs have been incurred directly by UUW throughout the year but relate to employees of United Utilities PLC. The average number of employees of United Utilities PLC providing services to the company during the year was 170 (2021: 196).

### 4. Operating profit

	2022 £m	2021 £m
<b>Other operating costs</b>		
Power	104.4	88.2
Hired and contracted services <sup>(1)</sup>	94.2	84.3
Property rates	90.3	89.4
Materials	90.2	81.8
Regulatory fees	28.4	28.0
Insurance	16.9	13.0
Accrued innovation costs	5.9	6.2
Loss on disposal of property, plant and equipment and intangibles	3.8	8.4
Other expenses	22.5	17.4
	<u>456.6</u>	<u>416.8</u>
<b>Allowance for expected credit losses – trade and other receivables</b>		
Allowance for expected credit losses – trade and other receivables (see note 11)	23.4	28.7
	<u>23.4</u>	<u>28.7</u>
<b>Other income</b>		
Other income	(3.6)	(3.7)
	<u>(3.6)</u>	<u>(3.7)</u>
<b>Depreciation and amortisation expense</b>		
Depreciation of property, plant and equipment (see note 9)	374.4	376.8
Amortisation of intangible assets (see note 10)	41.2	42.5
	<u>415.6</u>	<u>419.3</u>

## Notes to the financial statements

### 4. Operating profit (continued)

Note:

<sup>(1)</sup> As explained in note 3, costs associated with non-permanent staff that were previously included within hired and contracted services are now included within staff costs. Accordingly, the prior year non-permanent staff costs included within hired and contracted services presented within other operating costs in the prior year have also been re-presented. This resulted in an increase in staff costs and a reduction in the costs of hired and contracted services of £11.6 million compared with what was presented in the financial statements published for that year.

During the year ended 31 March 2022, the group experienced inflationary pressures across much of its operating cost base. This was most notable in relation to power costs, which increased by £16.2 million compared with the prior year, largely due to price increases. Through its progressive hedging policy the group was able to lock in the commodity price on the majority of its consumption for the year ended 31 March 2022 before the most recent energy price rises, and therefore secured an average rate over the year of £78 per MWh. This compares favourably with the market rate of over £200 per MWh as at the year-end reporting date and has been fundamental to the group's ability to minimise the impact of price rises on its cost base.

Incremental costs totalling £5.8 million have been incurred during the year in relation to the implementation of Software as a Service (SaaS) arrangements, which are increasingly expected to be recognised within operating costs in accordance with clarifications on the appropriate accounting treatment issued by the IFRS Interpretations Committee (IFRIC) during the year. The majority of SaaS implementation costs in previous years have been accounted for as intangible asset additions. These prior year amounts have not been restated to reflect the group's updated approach as they have not been material.

Research and development expenditure for the year ended 31 March 2022 was £1.2 million (2021: £1.0 million). In addition, £5.9 million (2021: £6.2 million) of costs have been accrued by United Utilities Water Limited in relation to the Innovation in Water Challenge scheme operated by Ofwat for AMP7. These expenses directly offset amounts recognised in revenue during each year intended to fund innovation projects across England and Wales as part of an industry-wide scheme to promote innovation in the sector. The amounts accrued will either be spent on innovation projects that the group successfully bids for or will be transferred to other successful water companies in accordance with the scheme rules.

During the year, the group obtained the following services from its auditor, with a total value of £443,000 (2021: £468,000), which are broken down as follows:

	2022 £'000	2021 £'000
<b>Audit services</b>		
Statutory audit – group and company	310	304
Statutory audit – subsidiary	25	34
	<u>335</u>	<u>338</u>
<b>Non-audit services</b>		
Regulatory audit services provided by the statutory auditor	64	71
Other non-audit services	44	59
	<u>443</u>	<u>468</u>

## Notes to the financial statements

### 5. Investment income

	2022 £m	2021 £m
Interest receivable on short-term bank deposits held at amortised cost	1.1	1.1
Interest receivable on loans to joint ventures of the UUG group held at amortised cost (see note A7)	-	2.4
Net pension interest income (see note 15)	11.1	13.4
Other interest receivable	-	1.7
	<u>12.2</u>	<u>18.6</u>

### 6. Finance expense

	2022 £m	2021 £m
<b>Interest payable</b>		
Interest payable on borrowings held at amortised cost <sup>(1)</sup>	329.9	180.0
Interest payable on borrowings from intermediate parent undertakings	0.9	1.4
Preference share dividends (see note 8)	-	4.6
	<u>330.8</u>	<u>186.0</u>

#### Fair value losses on debt and derivative instruments

Fair value hedge relationships:

Borrowings <sup>(2)</sup>	(199.4)	(155.1)
Designated swaps <sup>(2) (3)</sup>	194.0	132.8
	<u>(5.4)</u>	<u>(22.3)</u>

#### Financial instruments at fair value through profit or loss

Borrowings designated at fair value through profit or loss <sup>(4)</sup>	(7.9)	(67.3)
Associated swaps <sup>(5)</sup>	9.7	67.8
	<u>1.8</u>	<u>0.5</u>

Fixed interest rate swaps <sup>(5)</sup>	(139.7)	(36.0)
Net payments on derivatives and debt under fair value option	(31.5)	(17.6)
Inflation swaps <sup>(5)</sup>	29.7	3.4
Other	2.3	0.6
	<u>(139.2)</u>	<u>(49.6)</u>
<b>Net fair value (gains)/losses on debt and derivative instruments<sup>(6)</sup></b>	<u>(142.8)</u>	<u>(71.4)</u>
	<u>188.0</u>	<u>114.6</u>

Notes:

<sup>(1)</sup> Includes a £227.9 million (2021: £52.6 million) non-cash inflation uplift expense in relation to the group's index-linked debt and £1.5 million (2021: £1.7 million) interest expense on lease liabilities, representing the unwinding of discounting applied to future lease payments.

<sup>(2)</sup> Includes foreign exchange gains of £4.4 million (2021: £43.9 million gains), excluding those on instruments measured at fair value through profit or loss. These losses are largely offset by fair value gains on derivatives.

<sup>(3)</sup> Under the provisions of IFRS 9 'Financial instruments', changes in fair value resulting from changes to the foreign currency basis spread are recognised in other comprehensive income rather than profit or loss as they relate to items designated in an accounting hedge relationship. There was no overall gain or loss recognised in other comprehensive income during the year in relation to these items (2021: £12.7 million loss).

<sup>(4)</sup> Under the provisions of IFRS 9 'Financial instruments', a £4.1 million fair value loss (2021: £43.3 million loss) due to changes in the group's own credit risk is recognised in other comprehensive income rather than within profit or loss.

## Notes to the financial statements

### 6. Finance expense (continued)

<sup>(5)</sup> These swap contracts are not designated within an IFRS 9 hedge relationship and are, as a result, 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.

<sup>(6)</sup> Includes £33.2 million income (2021: £21.4 million) due to net interest on derivatives and debt under fair value option and £28.3 million expense (2021: £1.3 million expense) due to non-cash inflation changes on index-linked derivatives.

Interest payable is stated net of £52.7 million (2021: £30.4 million) borrowing costs capitalised in the cost of qualifying assets, with £52.1 million (2021: £30.3 million) capitalised within property, plant and equipment and £0.6 million (2021: £0.1 million) capitalised within intangible assets during the year. This has been calculated by applying an average capitalisation rate of 4.2 per cent (2021: 2.3 per cent) to expenditure on such assets as prescribed by IAS 23 'Borrowing Costs'.

### 7. Tax

	2022 £m	2021 £m
<b>Current tax</b>		
UK corporation tax	-	78.1
Adjustments in respect of prior years	(82.0)	0.1
Total current tax (credit)/charge for the year	<u>(82.0)</u>	<u>78.2</u>
<b>Deferred tax</b>		
Current year	97.8	19.6
Adjustments in respect of prior years	82.3	(2.2)
	<u>180.1</u>	<u>17.4</u>
Change in tax rate	404.2	-
Total deferred tax charge for the year	<u>584.3</u>	<u>17.4</u>
Total tax charge for the year	<u><u>502.3</u></u>	<u><u>95.6</u></u>

The deferred tax charge of £404.2 million (2021: £nil) reflects the Government's planned increase in the rate of corporation tax from 19 per cent to 25 per cent from 1 April 2023.

The adjustments in respect of prior years mainly relate to optimising the available research and development UK tax allowances on the group's innovation-related expenditure, for multiple prior years.

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:

	2022 £m	2022 %	2021 £m	2021 %
Profit before tax	<u>425.6</u>		<u>505.7</u>	
Tax at the UK corporation tax rate	80.9	19.0	96.1	19.0
Deferred tax rate adjustment	23.5	5.5	-	-
Adjustments in respect of prior years	0.3	0.1	(2.1)	(0.4)
Change in tax rate	404.2	94.9	-	-
Net (income not taxable)/expense not deductible for tax	<u>(6.6)</u>	<u>(1.5)</u>	<u>1.6</u>	<u>0.3</u>
Total tax charge and effective tax rate for the year	<u><u>502.3</u></u>	<u><u>118.0</u></u>	<u><u>95.6</u></u>	<u><u>18.9</u></u>

## Notes to the financial statements

### 7. Tax (continued)

The deferred tax rate adjustment reflects the fact that the current year deferred tax charge is at the future rate of 25 per cent, rather than the 19 per cent current year rate.

The movement from expenses not deductible in the prior year to income not taxable is mainly due to the additional 30 per cent element of the temporary capital allowances super-deductions introduced in 2021.

The table below reconciles the notional tax charge at the UK corporation tax rate to the total current tax charge for the year:

	2022	2021
	£m	£m
Profit before tax	425.6	505.7
Profit before tax multiplied by the standard rate of UK corporation tax of 19 per cent	80.9	96.1
Relief for capital allowances in place of depreciation	(107.7)	(78.6)
Disallowance of depreciation charged in the accounts	68.8	70.0
Financial transactions timing differences	(26.9)	(7.8)
Pension timing differences	(2.8)	-
Relief for capitalised interest	(10.0)	(5.8)
Other timing differences	2.0	2.6
Adjustments to tax charge in respect of prior years	(82.0)	0.1
Income not taxable	(9.0)	(0.7)
Depreciation charged on non-qualifying assets	2.5	2.3
Tax losses carried forward	2.2	-
Current tax charge for the year	<u>(82.0)</u>	<u>78.2</u>

The Group's current tax charge is lower than the UK headline rate of 19 per cent primarily due to a range of adjustments which are simply timing differences between recognition of the income or expense in the accounts and in the related tax computations submitted to HMRC. These include deductions in relation to capital spend, pension timing differences, unrealised profits or losses in relation to financing and related treasury derivatives and capitalised interest.

The current year net timing differences in relation to capital spend, i.e. capital allowances less depreciation, was more than the prior year mainly due to the temporary super-deductions introduced in 2021.

The adjustment to tax charge in respect of prior years of £82.0 million mainly relates to optimising the available research and development UK tax allowances on the group's innovation-related expenditure, for multiple prior years.

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 current year pension timing differences was lower than the prior year mainly due to the required accounting reallocation to equity of £2.7 million in the prior year, due to there being a prior year actuarial loss.

The relief for capitalised interest relates to amounts which are immediately deductible under the UK tax rules notwithstanding the amounts being capitalised for accounting purposes. The year on year amount will depend on the amount capitalised.

## Notes to the financial statements

### 7. Tax (continued)

Other timing differences include a range of small value items where there is a timing difference between the accounting and tax recognition.

The increase in income not taxable is mainly due to the additional 30 per cent element of the temporary capital allowances super-deductions introduced in 2021.

Depreciation charged on non-qualifying assets relates to accounting depreciation where there is no corresponding tax deduction.

Where permitted under HMRC rules, any available UK tax losses will be carried forward and utilised in future periods, when the tax rate is at 25 per cent.

#### Tax on items recorded within other comprehensive income

	2022 £m	2021 £m
<b>Current tax</b>		
Relating to other pension movements	-	(2.7)
<b>Deferred tax (see note 16)</b>		
On remeasurement (losses)/gains on defined benefit pension schemes	81.5	(19.7)
Relating to other pension movements	-	2.7
Share-based payments	(1.0)	-
On net fair value (losses)/gains recognised in other comprehensive income	26.0	(8.8)
	<u>106.5</u>	<u>(28.5)</u>
Total tax charge/(credit) on items recorded within other comprehensive income	<u>106.5</u>	<u>(28.5)</u>

The prior year current tax amount of £2.7 million relating to other pension movements is the contributions in excess of the amounts in the profit and loss account which has to be allocated against the actuarial loss. No adjustment is required in the current year due to the actuarial gain. The tax adjustments taken to other comprehensive income primarily relate to remeasurement movements on the group's defined benefit pension schemes. Management consider that the most likely method of realisation would be through a refund, which would be taxed at the rate applicable to refunds from a trust (currently 35 per cent).

### 8. Dividends

Amounts recognised as distributions to equity holders of the company in the year comprise:

	2022 £m	2021 £m
<b>Ordinary shares</b>		
Interim dividend for the year ended 31 March 2022 at 0.49 pence per share (2021: 0.0 pence)	112.2	-
Interim dividend for the year ended 31 March 2022 at 0.25 pence per share (2021: 0.0 pence)	57.7	-
Interim dividend for the year ended 31 March 2022 at 0.74 pence per share (2021: 0.0 pence)	169.3	-
	<u>339.2</u>	<u>-</u>

The directors have not recommended a final ordinary dividend (2021: £nil).

## Notes to the financial statements

### 9. Property, plant and equipment

Property, plant and equipment comprises owned and leased assets.

	2022 £m	2021 £m
Property, plant and equipment – owned	12,026.1	11,676.1
Right of use assets – leased	56.1	56.2
<b>Net book value</b>	<u>12,080.2</u>	<u>11,732.3</u>

#### Property, plant and equipment – owned

Group and company	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
<b>Cost</b>						
At 1 April 2020	355.5	5,730.5	7,615.1	562.8	1,548.6	15,812.5
Additions	1.8	100.9	134.9	8.4	425.9	671.9
Transfers	9.7	66.5	416.4	(3.9)	(490.7)	(2.0)
Disposals	(1.6)	-	(164.0)	(47.6)	-	(213.2)
At 31 March 2021	<u>365.4</u>	<u>5,897.9</u>	<u>8,002.4</u>	<u>519.7</u>	<u>1,483.8</u>	<u>16,269.2</u>
Additions	2.5	84.8	182.6	6.3	452.4	728.6
Transfers	6.3	48.7	235.1	6.2	(296.4)	(0.1)
Disposals	(0.3)	(0.1)	(136.0)	(14.5)	-	(150.9)
At 31 March 2022	<u>373.9</u>	<u>6,031.3</u>	<u>8,284.1</u>	<u>517.7</u>	<u>1,639.8</u>	<u>16,846.8</u>
<b>Accumulated depreciation</b>						
At 1 April 2020	122.5	434.5	3,441.5	423.3	-	4,421.8
Charge for the year	8.2	42.6	296.0	29.1	-	375.9
Transfers	-	-	-	(1.0)	-	(1.0)
Disposals	(1.6)	-	(155.0)	(47.0)	-	(203.6)
At 31 March 2021	<u>129.1</u>	<u>477.1</u>	<u>3,582.5</u>	<u>404.4</u>	<u>-</u>	<u>4,593.1</u>
Charge for the year	8.6	44.9	294.1	26.8	-	374.4
Transfers	-	0.2	(0.1)	-	-	0.1
Disposals	(0.1)	-	(132.7)	(14.1)	-	(146.9)
At 31 March 2022	<u>137.6</u>	<u>522.2</u>	<u>3,743.8</u>	<u>417.1</u>	<u>-</u>	<u>4,820.7</u>
<b>Net book value</b>						
At 31 March 2021	<u>236.3</u>	<u>5,420.8</u>	<u>4,419.9</u>	<u>115.3</u>	<u>1,483.8</u>	<u>11,676.1</u>
At 31 March 2022	<u>236.3</u>	<u>5,509.1</u>	<u>4,540.3</u>	<u>100.6</u>	<u>1,639.8</u>	<u>12,026.1</u>

## Notes to the financial statements

### 9. Property, plant and equipment (continued)

During the year, there was a transfer of £0.9 million cost from intangible assets to property, plant and equipment following a data cleanse exercise in respect of the fixed assets register. The overall impact of these reclassifications on the purchase of property, plant and equipment and intangible assets in the statement of cash flows (note A2) is nil.

#### Property, plant and equipment – leased

Group and company	Land and buildings £m	Operational assets £m	Fixtures, fittings, tools and equipment £m	Total £m
<b>Cost</b>				
At 1 April 2020	49.4	6.5	-	55.9
Additions	2.3	1.5	0.2	4.0
Disposals	(0.1)	(0.2)	-	(0.3)
At 31 March 2021	51.6	7.8	0.2	59.6
Additions	1.1	0.8	-	1.9
Disposals	(0.4)	(1.4)	-	(1.8)
At 31 March 2022	52.3	7.2	0.2	59.7
<b>Accumulated depreciation</b>				
At 1 April 2020	0.8	1.0	-	1.8
Charge for the year	1.0	0.9	-	1.9
Disposals	(0.1)	(0.2)	-	(0.3)
At 31 March 2021	1.7	1.7	-	3.4
Charge for the year	1.1	1.0	-	2.1
Disposals	(0.5)	(1.4)	-	(1.9)
At 31 March 2022	2.3	1.3	-	3.6
<b>Net book value</b>				
At 31 March 2021	49.9	6.1	0.2	56.2
At 31 March 2022	50.0	5.9	0.2	56.1

Note:

To carry out its activities, the group enters into leases of assets from time to time, typically in relation to items such as land, buildings and vehicles. Due to the nature of the group's operations, many of the group's leases have extremely long terms, ranging from one year to 999 years. The group does not typically lease assets on a short-term basis or enter into leases for low value asset and therefore no material costs were incurred during the year, either individually or in aggregate, in relation to lease contracts with a duration of less than 12 months or for low-value assets.

At 31 March 2022, the group and company had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £280.8 million (2021: £335.5 million).

In addition to these commitments, the group and company have long-term expenditure plans which include investments to achieve improvements in performance required by regulators and to provide for future growth.

## Notes to the financial statements

### 10. Intangible assets

<b>Group and company</b>	Total £m
<b>Cost</b>	
At 1 April 2020	440.8
Additions	32.7
Disposals	(51.0)
Transfers	2.0
At 31 March 2021	424.5
Additions	20.1
Disposals	(13.2)
Transfers	0.9
At 31 March 2022	432.3
<b>Accumulated amortisation</b>	
At 1 April 2020	251.8
Charge for the year	41.5
Disposals	(50.9)
Transfers	1.0
At 31 March 2021	243.4
Charge for the year	41.2
Disposals	(13.1)
Transfers	-
At 31 March 2022	271.5
Net book value at 31 March 2021	181.1
Net book value at 31 March 2022	160.8

The group and company's intangible assets relate mainly to computer software.

At 31 March 2022, the group and company had entered into contractual commitments for the acquisition of intangible assets amounting to £1.8 million (2021: £0.9 million).

### 11. Trade and other receivables

<b>Group and company</b>	2022 £m	2021 £m
Trade receivables	61.8	61.4
Amounts owed by intermediate parent and fellow subsidiary undertakings (see note A7):		
Trading balances	2.5	1.0
In relation to guarantees	-	-
Floating rate loan	-	-
Amounts owed by other related parties (see note A7)	28.5	27.1
Other debtors and prepayments	48.6	34.1
Accrued income	86.1	101.2
	227.5	224.8

## Notes to the financial statements

### 11. Trade and other receivables (continued)

The carrying amounts of trade and other receivables approximate their fair value.

Trade receivables do not carry interest and are stated net of allowances for expected credit losses, an analysis of which is as follows:

<b>Group and company</b>	2022 £m	2021 £m
At the start of the year	80.3	71.3
Amounts charged to operating expenses (see note 4)	23.4	28.7
Trade receivables written off	(19.2)	(20.2)
Amounts charged to deferred income	-	0.5
At the end of the year	<u>84.5</u>	<u>80.3</u>

Amounts charged to deferred income relate to amounts invoiced for which revenue had not yet been recognised in the income statement.

At each reporting date, the group evaluates the recoverability of trade receivables and records allowances for expected credit losses which are measured in a way that reflects an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes and considers past events, current conditions and forecasts of future conditions.

At 31 March 2022 and 31 March 2021, the group and company 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:

<b>Group and company</b>	Aged less than one year £m	Aged between one year and two years £m	Aged greater than two years £m	Carrying value £m
<b>At 31 March 2022</b>				
Gross trade receivables	68.9	26.1	51.4	146.3
Allowance for expected credit losses	(20.3)	(13.1)	(51.2)	(84.5)
Net trade receivables	<u>48.6</u>	<u>13.0</u>	<u>0.2</u>	<u>61.8</u>
		Aged		
		between		
		one year		
		and		
		two years		
		£m		
<b>At 31 March 2021</b>				
Gross trade receivables	62.0	35.3	44.4	141.7
Allowance for expected credit losses	(20.0)	(16.5)	(43.8)	(80.3)
Net trade receivables	<u>42.0</u>	<u>18.8</u>	<u>0.6</u>	<u>61.4</u>

At 31 March 2022, the group and company had no trade receivables that were not past due (2021: £nil).

## Notes to the financial statements

### 11. Trade and other receivables (continued)

The majority of accrued income balances represent contract assets arising from timing differences between the billing cycle and the usage of water by customers. They therefore typically reverse in subsequent months, with all amounts held in relation to these contract assets at the beginning of the reporting period having subsequently reversed into the income statement during the year. At 31 March 2022 and 31 March 2021, the group had no accrued income that was past due. In instances where the collection of consideration is not considered probable at the point services are delivered, no accrued income balance is recognised, as the criteria to recognise revenue in accordance with IFRS 15 has not been met.

### 12. Cash and cash equivalents

	2022 £m	2021 £m
<b>Group and company</b>		
Cash at bank and in hand	8.3	2.4
Short-term bank deposits	173.6	646.2
<b>Cash and short-term deposits</b>	<u>181.9</u>	<u>648.6</u>
Book overdrafts (included in borrowings, see note 13)	(20.8)	(10.1)
<b>Cash and cash equivalents in the statement of cash flows</b>	<u><u>161.1</u></u>	<u><u>638.5</u></u>

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 cash management practices, represent the value of cheques issued and payments initiated that had not cleared as at the reporting date.

### 13. Borrowings

	2022 £m	2021 £m
<b>Group and company</b>		
<b>Non-current liabilities</b>		
Bonds <sup>(1)</sup>	5,798.5	5,656.3
Bank and other term borrowings	1,445.0	1,710.3
Lease liabilities (see note 14)	54.1	54.1
Amounts owed to intermediate parent undertaking (see note A7)	599.9	577.6
	<u>7,897.5</u>	<u>7,998.4</u>
<b>Current liabilities</b>		
Bonds	-	388.5
Bank and other term borrowings	284.7	152.4
Book overdrafts (see note 12)	20.8	10.1
Lease liabilities (see note 14)	3.0	3.0
Amounts owed to intermediate parent undertaking (see note A7) <sup>(2)</sup>	164.5	163.0
	<u>473.0</u>	<u>717.0</u>
	<u><u>8,370.5</u></u>	<u><u>8,715.4</u></u>

Note:

<sup>(1)</sup> For the company, bonds includes £3,148.5 million (2021: £3,064.8 million) of amounts owed to subsidiary undertakings.

<sup>(2)</sup> For the company, £0.2 million (2021: £0.4 million) of amounts is owed to subsidiary undertakings.

For further details of the principal economic terms and conditions of outstanding borrowings see note A4.

## Notes to the financial statements

### 14. Leases

As part of its activities, the group typically leases items such as land, buildings and vehicles. The group does not typically lease assets on a short-term basis or enter into leases for low value assets and therefore no material costs were incurred during the year, either individually or in aggregate, in relation to lease contracts with a duration of less than 12 months or for low value assets.

Lease terms range from one year to 999 years. Due to the nature of the group's operations, many of the group's leases have extremely long terms.

The maturity profile of lease liabilities recognised at the balance sheet date is:

	2022	2021
<b>Group and company</b>	£m	£m
Less than 1 year	2.6	3.0
1 to 5 years	8.2	9.4
5 to 10 years	6.7	6.7
10 to 25 years	25.0	24.8
35 to 50 years	41.3	41.0
50 to 100 years	81.5	81.0
100 to 500 years	106.9	107.6
Longer than 500 years	3.2	3.2
<b>Total undiscounted cash payments</b>	<u>275.4</u>	<u>276.7</u>
Effect of discounting	<u>(218.3)</u>	<u>(219.6)</u>
<b>Present value of cash payments</b>	<u><u>57.1</u></u>	<u><u>57.1</u></u>

During the year ending 31 March 2022, £1.6 million (2021: £1.7 million) of interest expense on lease liabilities was recognised, representing the unwinding of the discounting applied to future lease payments (see note 6).

The total cash outflow for leases for the year ended 31 March 2022 was £3.0 million (2021: £3.2 million), of this £1.6 million (2021: £1.7 million) was payment of interest and £1.4 million (2021: £1.5 million) payment of principal.

Payment of interest forms part of cash flows from operating activities and payment of principal is included within repayment of borrowings, which forms part of cash flows from financing activities in the statement of cash flows.

### 15. Retirement benefit surplus

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) – as well as a defined contribution scheme which is part of the UUPS, and a series of historic unfunded, unregistered retirement benefit schemes operated for the benefit of certain former employees.

Both defined benefit schemes are closed to new employees, and since 1 April 2018 the majority of active members in the defined benefit section of the UUPS have been part of a hybrid section comprising both defined benefit and defined contribution elements in order to reduce the overall costs and risk to the group resulting from increases in future service costs, while balancing the interests of employees by maintaining an element of defined benefit pension provision.

Information about the pension arrangements for executive directors is contained in the directors' remuneration report.

## Notes to the financial statements

### 15. Retirement benefit surplus (continued)

#### Defined benefit schemes

As similar financial and demographic assumptions are used in accounting for both of the group's defined benefit pension schemes, and given they have similar risk profiles, the information below and further detail provided in note A5 is presented on an aggregated basis unless otherwise stated.

The net pension income before tax recognised in the income statement in respect of the defined benefit pension schemes is summarised as follows:

	2022	2021
	£m	£m
<b>Group and company</b>		
Current service cost	7.1	4.6
Curtailments/settlements	-	0.4
Administrative expenses	1.0	2.0
<b>Pension expense charged to operating profit</b>	<u>8.1</u>	<u>7.0</u>
Net pension interest income credited to investment income (see note 5)	(11.1)	(13.4)
<b>Net pension income credited before tax</b>	<u>(3.0)</u>	<u>(6.4)</u>

Defined benefit pension costs excluding curtailments/settlements included within employee benefit expense were £8.1 million (2021: £6.6 million) comprising current service costs and administrative expenses.

Total post-employment benefits expense excluding curtailments/settlements charged to operating profit of £34.3 million (2021: £30.0 million) comprise the defined benefit costs described above of £8.1 million (2021: £6.6 million) and defined contribution pension costs of £26.1 million (2021: £23.4 million) (see note 3).

Included within curtailments/settlements is £nil (2021: £0.3 million) relating to the equalisation of GMP benefits (see note A6 for further details).

The reconciliation of the opening and closing net pension surplus included in the statement of financial position is as follows:

	2022	2021
	£m	£m
<b>Group and company</b>		
At the start of the year	531.0	579.1
Income recognised in the income statement	3.0	6.4
Contributions	8.5	7.8
Remeasurement gains/(losses) gross of tax	228.7	(62.3)
<b>At the end of the year</b>	<u>771.2</u>	<u>531.0</u>

Included in the contributions paid of £8.5 million (2021: £7.8 million), which are included as cash outflows in arriving at net cash generated from operations in the consolidated statement of cash flows, enhancements to benefits provided on redundancy of £0.2 million (2021: £0.6 million), payments in relation to historic unfunded, unregistered retirement benefit schemes of £2.5 million (2021: £0.9 million), and administration expenses of £0.2 million (2021: £0.2 million). Contributions in relation to current service cost remained broadly stable at £5.6 million (2021: £6.1 million).

## Notes to the financial statements

### 15. Retirement benefit surplus (continued)

Remeasurement gains and losses are recognised directly in the statement of comprehensive income.

<b>Group and company</b>	2022 £m	2021 £m
The return on plan assets, excluding amounts included in interest	78.5	185.4
Actuarial gains /(losses) arising from changes in financial assumptions	122.7	(323.5)
Actuarial gains arising from changes in demographic assumptions	39.2	60.5
Actuarial (losses)/gains arising from experience	(11.7)	15.3
Remeasurement gains/(losses) on defined benefit pension schemes	<u>228.7</u>	<u>(62.3)</u>

Deferred tax on the movement in the defined benefit surplus during the year has been recognised at a rate of 35 per cent, being the rate applicable to refunds from a trust, reflecting the most likely method by which the defined benefit surplus would be realised (see notes 7 and 19).

For more information in relation to the group's and company's defined benefit pension schemes see note A6.

#### Defined contribution schemes

During the year, the group made £26.1 million (2021: £23.4 million) of contributions to defined contribution schemes which are included in employee benefits expense in the consolidated income statement (see note 3), and as cash outflows in arriving at net cash generated from operating activities in the consolidated statement of cash flows.

### 16. Deferred tax liabilities

The following are the major deferred tax liabilities and assets recognised by the group and company, and the movements thereon, during the current and prior year:

<b>Group and company</b>	Accelerated tax depreciation £m	Retirement benefit obligations £m	Other £m	Total £m
At 1 April 2020	1,213.2	202.7	(22.9)	1,393.0
Charged/(credited) to the income statement	8.6	-	8.8	17.4
Credited to equity (see note 7)	-	(17.0)	(8.8)	(25.8)
	<u>1,221.8</u>	<u>185.7</u>	<u>(22.9)</u>	<u>1,384.6</u>
At 31 March 2021	1,221.8	185.7	(22.9)	1,384.6
Charged to the income statement	150.5	2.8	26.8	180.1
Change in tax rate	413.7	-	(9.5)	404.2
Charged to other comprehensive income (see note 7)	-	81.5	25.0	106.5
	<u>1,786.0</u>	<u>270.0</u>	<u>19.4</u>	<u>2,075.4</u>
At 31 March 2022	<u>1,786.0</u>	<u>270.0</u>	<u>19.4</u>	<u>2,075.4</u>

Certain deferred tax assets and liabilities have been offset in accordance with IAS 12 'Income Taxes'.

## Notes to the financial statements

### 16. Deferred tax liabilities (continued)

The deferred tax charge of £404.2 million (2021: £nil) reflects the Government's planned increase in the rate of corporation tax from 19 per cent to 25 per cent from 1 April 2023.

The accelerated tax depreciation represents the difference between capital allowances and accounting depreciation on the group's property, plant and equipment. Capital allowances are tax reliefs provided in law and spread the tax relief due over a pre-determined standard number of years. This contrasts with the accounting treatment, where the expenditure is treated as an asset with the cost being depreciated over the useful life of the asset, or impaired if the value of such assets is considered to have reduced materially. Due to the group's continued significant annual capital expenditure, the deductions for capital allowances are expected to exceed depreciation for the medium term and continue to impact future corporation tax payments.

Given the fully funded nature of the group's defined benefit pension schemes, the retirement benefit obligations primarily relates to deferred taxation on the pensions schemes surplus position. This amount is significantly impacted by financial market conditions and long-term inflation expectations and therefore it is difficult to forecast future movements. However, these movements have no impact on medium-term future corporation tax payments as they only impact year-on-year deferred tax movement.

Deferred tax on retirement benefit obligations can arise where there are year-on-year differences between the contributions paid and the associated amounts charged to the profit and loss account. However, given the fully funded nature of our pension schemes, any such deferred tax movements, together with the associated impact on future corporation tax payments, is not expected to be significant for the medium term.

The other short-term temporary differences of £19.4 million includes £10.4 million relating to tax losses which have been carried forward, where permitted under HMRC rules, to be utilised in future periods when the tax rate is at 25 per cent. Also included are other short-term timing differences in relation to the year on year movement in financial transactions which are sensitive to fair value movement on treasury derivatives and can therefore fluctuate significantly from year to year. However, these fair value movements have no impact on future corporation tax payments as they only impact the year on year deferred tax movement.

### 17. Provisions

<b>Group and company</b>	Restructuring £m	Other £m	Total £m
At 1 April 2020	4.9	11.5	16.4
Charged/(credited) to the income statement	1.3	(0.9)	0.4
Utilised in the year	(4.6)	(1.1)	(5.7)
At 31 March 2021	1.6	9.5	11.1
Charged/(credited) to the income statement	0.3	4.7	5.0
Utilised in the year	(0.7)	(1.9)	(2.6)
At 31 March 2022	1.2	12.3	13.5

The group and company had no provisions classed as non-current at 31 March 2022 or 31 March 2021.

The restructuring provision as at 31 March 2022 and 31 March 2021 relates to severance costs as a result of group reorganisation.

Other provisions principally relate to contractual, legal and environmental claims against the group and company and represent management's best estimate of the value of settlement, the timing of which is dependent on the resolution of the relevant claims.

## Notes to the financial statements

### 18. Trade and other payables

	2022 £m	2021 £m
<b>Group and company</b>		
<b>Non-current</b>		
Deferred grants and contributions	818.2	780.4
Other creditors	17.0	16.3
	<u>835.2</u>	<u>796.7</u>
<b>Current</b>		
Trade payables	27.5	32.7
Amounts owed to parent and fellow subsidiary undertakings (see note A7)	2.6	4.7
Amounts owed to other related parties (see note A7)	-	1.3
Other tax and social security	6.6	5.9
Deferred grants and contributions	16.0	15.4
Accruals and other creditors	258.5	207.4
Deferred income	48.0	50.9
	<u>359.2</u>	<u>318.3</u>
	<u>1,194.4</u>	<u>1,115.0</u>

Included within accruals and other creditors as at 31 March 2022 was £19.2 million (2021: £17.9 million) of accrued interest, which at the company level was owed to subsidiary undertakings.

The average credit period taken for trade purchases is 13 days (2021: 13 days).

The carrying amounts of trade and other payables approximates to their fair value at 31 March 2022 and 31 March 2021.

The majority of deferred income balances represent contract liabilities arising from timing differences between customer payments, the billing cycle, and the usage of water by customers. They therefore typically reverse in subsequent months, with all amounts held in relation to these contract liabilities at the beginning of the reporting period having subsequently reversed into the income statement during the year.

#### *Deferred grants and contributions*

	2022 £m	2021 £m
<b>Group and company</b>		
At the start of the year	795.8	751.3
Amounts capitalised during the year	1.8	5.0
Transfer of assets from customers	52.4	55.0
Credited to the income statement – revenue	(15.4)	(14.6)
Credited to the income statement – other operating costs	(0.4)	(0.4)
Credited to allowance for bad and doubtful receivables	-	(0.5)
	<u>834.2</u>	<u>795.8</u>

## Notes to the financial statements

## 19. Other Reserves

	Capital redemption reserve £m	Cost of hedging reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2021	-	0.4	6.2	6.6
<b>Other comprehensive income</b>				
Change in fair value recognised in other Comprehensive income	-	-	108.0	108.0
Amounts reclassified from other comprehensive income to profit or loss			(1.3)	(1.3)
Tax on items taken directly to equity	-	-	(26.8)	(26.8)
<b>Total comprehensive income at 31 March 2022</b>	<u>-</u>	<u>0.4</u>	<u>86.1</u>	<u>86.5</u>
		Cost of hedging reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2020	-	10.7	(1.3)	9.4
<b>Other comprehensive income</b>				
Change in fair value recognised in other Comprehensive income	-	(12.7)	9.3	(3.4)
Tax on items taken directly to equity	-	2.4	(1.8)	0.6
<b>Total comprehensive income</b>	<u>-</u>	<u>(10.3)</u>	<u>7.5</u>	<u>(2.8)</u>
Redemption of preference shares	(130.0)	-	-	(130.0)
Elimination of capital redemption reserve on allotment of ordinary shares	130.0	-	-	130.0
<b>At 31 March 2021</b>	<u>-</u>	<u>0.4</u>	<u>6.2</u>	<u>6.6</u>

The group recognises the cost of hedging reserve as a component of equity. 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.

The group designates 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.

## 20. Share capital

Group and company	2022 £m	2021 £m
<b>Issued, called up and fully paid</b>		
230,000,000 (2021: 230,000,000) ordinary shares of £1.00 each	230.0	230.0
	<u>230.0</u>	<u>230.0</u>

## Notes to the financial statements

### 20. Share capital (continued)

On 30 September 2020 the company redeemed its 130,000,000 redeemable preference shares, resulting in a reduction in retained earnings and the creation of a capital redemption reserve. In order to simplify its reserves position following this redemption, on the same date the company effected a bonus issue of 130,000,000 of ordinary shares of £1.00 each for nil consideration, which were allotted to its immediate parent as fully paid share capital and resulted in the elimination of the capital redemption reserve.

Preference shareholders were not entitled to receive notice of, attend or vote at, any general meeting of the group. However, preference shareholders received priority to other classes of shareholders on a winding up, liquidation or other return of capital to shareholders of the company.

In accordance with IAS 32 'Financial Instruments: Presentation', prior to their redemption the 130,000,000 7 per cent preference shares of £1.00 each were recognised as financial liabilities.

### 21. Contingent liabilities

Since 2016, the group has received indications from a number of groups of property search companies (PSCs) that they intend to claim compensation for amounts paid in respect of CON29DW water and drainage search reports, which they allege should have been provided to them either free of charge or for a nominal fee in accordance with the Environmental Information Regulations. In April 2020, a group of over 100 PSCs, comprising companies within the groups that had previously issued notice of intended claims, served proceedings on all of the water and sewerage undertakers in England and Wales, including United Utilities Water Limited, for an unspecified amount of compensation. This is an industry-wide issue, and while the litigation has progressed during the year it remains in its early stages. The litigation's likely direction and the quantum of any compensation being claimed is uncertain at this stage; however, based on the information currently available, the likelihood of the claim's success is considered to be low, and any potential outflow is not expected to be material.

No performance guarantees have been entered into as at 31 March 2022 by either the group or the company (2021: none).

### 22. Events after the reporting period

In April 2022 the group took out a £100 million term loan facility provided by Export Development Canada due April 2030, and entered into a further undrawn committed borrowing facilities with a total amount available of £40 million.

### 23. Ultimate parent undertaking

The company's immediate parent undertaking is United Utilities North West Limited, a company incorporated in England and Wales.

The company's ultimate parent undertaking and controlling party is United Utilities Group PLC, a company incorporated in England and Wales.

The smallest group in which the results of the company are consolidated is that headed by United Utilities Water Limited.

The largest group in which the results of the company are consolidated is that headed by United Utilities Group PLC. The consolidated accounts of this group are available to the public and may be obtained from: The Company Secretary, United Utilities Group PLC, Haweswater House, Lingley Mere Business Park, Lingley Green Avenue, Great Sankey, Warrington, WA5 3LP.

## Notes to the financial statements

### A1 Subsidiaries and other group undertakings

Details of the company's subsidiary undertakings and significant holdings in undertakings other than subsidiary undertakings, all of which are unlisted, are set out below. The registered address for each entity is Haweswater House, Lingley Mere Business Park, Lingley Green Avenue, Great Sankey, Warrington, WA5 3LP, United Kingdom.

	Class of share capital held	Proportion of share capital owned %	Nature of business
<b><i>Subsidiary undertakings</i></b>			
<b>England and Wales</b>			
United Utilities Water Finance PLC	Ordinary	100.00	Financing company
Lingley Mere Management Company Limited	Ordinary	74.78	Property management

The control of Lingley Mere Management Company Limited (LMMC) is split between UUW and United Utilities Property Services (UUPS), who respectively hold a 74.78 per cent and 10.85 per cent stake in LMMC. The non-controlling interest in LMMC is not considered to be material for either the UUW or United Utilities groups (see note A8).

The company does not hold any interests in joint ventures or associated undertakings. All other investments are held at fair value.

## Notes to the financial statements

### A2 Consolidated and group statement of cash flows – further analysis

#### *Cash generated from operations*

	2022 £m	2021 £m
Profit before tax	425.6	505.7
Adjustment for investment income (see note 5) and finance expense (see note 6)	175.8	96.0
<b>Operating profit</b>	<b>601.4</b>	<b>601.7</b>
Adjustments for:		
Depreciation of property, plant and equipment (see note 9)	374.4	376.8
Amortisation of intangible assets (see note 10)	41.2	42.5
Loss on disposal of property, plant and equipment (see note 4)	3.8	8.4
Amortisation of deferred grants and contributions (see note 18)	(15.8)	(15.0)
Changes in working capital:		
Increase in inventories	(0.8)	(3.6)
(Increase)/decrease in trade and other receivables	(4.5)	112.5
Increase in trade and other payables	24.1	5.6
Increase/(decrease) in provisions (see note 17)	2.4	(5.3)
Pension contributions paid less pension expense charged to operating profit	(0.4)	(0.8)
<b>Cash generated from operations</b>	<b>1,025.8</b>	<b>1,122.8</b>

The group and company have received property, plant and equipment of £52.4 million (2021: £55.0 million) in exchange for the provision of future goods and services (see notes 18 and A8).

#### *Reconciliation of fixed asset purchases to fixed asset additions*

#### **Owned property, plant and equipment<sup>(1)</sup>**

	2022 £m	2021 £m
<b>Group and company</b>		
<b>Purchase of property, plant and equipment in statement of cash flows</b>	<b>608.8</b>	<b>604.5</b>
Non-cash additions:		
Transfers of assets from customers (see note 18)	52.4	55.0
IAS 23 capitalised borrowing costs (see note 6)	52.1	30.3
Net book value transfers to intangible assets	-	1.0
Timing differences on cash paid <sup>(2)</sup>	15.3	(18.9)
<b>Property, plant and equipment additions</b>	<b>728.6</b>	<b>671.9</b>

<sup>(1)</sup> This reconciliation relates to property, plant and equipment owned by the group and therefore excludes right-of-use assets recognised in accordance with IFRS 16 'Leases', for which cash flows relating to the associated lease liabilities are included within repayment of borrowings and interest paid in the statement of cash flows.

<sup>(2)</sup> Timing differences arise and reverse when additions are recognised in the statement of financial position in a different period to when cash payments for capital expenditure are made. Capital accruals recognised in relation to these timing differences are included in 'Accruals and other creditors' within trade and other payables (note 18).

## Notes to the financial statements

### A2 Consolidated and group statement of cash flows – further analysis (continued)

Intangible assets	2022 £m	2021 £m
<b>Purchase of intangibles assets in statement of cash flows</b>	<b>19.5</b>	<b>33.6</b>
IAS 23 capitalised borrowing costs (see note 6)	0.6	0.1
Net book value transfers to intangible assets	-	(1.0)
<b>Intangible asset additions</b>	<b>20.1</b>	<b>32.7</b>

### A3 Net debt

In the below tables, where derivatives are in an economic hedge of borrowings, derivative cash flows are shown netted with the net payment or receipt being reported against the underlying borrowing cash flow to provide a more faithful representation of the substance of the transaction.

The fair value of the derivatives reported in financing liabilities that are not hedging specific debt instruments are removed in calculating the group's net debt position. These derivatives correspond to the group's fixed interest rate swaps and inflation swaps, neither of which are designated within an IFRS 9 hedging relationship and both of which are classified as 'held for trading' under the accounting standard. The fair value movements on those derivatives that are not excluded from the revised definition of net debt (being derivatives in a fair value hedge relationship) are expected to be materially equal and opposite in value to the fair value movement included in borrowings, resulting in materially all fair value movements being excluded.

Fair value movements includes the indexation expense relating to the group's inflation swap portfolio of £28.3 million (2021: £1.3 million). The remaining fair value and foreign exchange movements in the year on the group's bond and bank borrowings are materially hedged by the fair value swap portfolio.

Movements in net debt during the year are impacted by changes in liabilities from financing activities as detailed in the tables below. The tables below should therefore be read in conjunction with the consolidated statement of cash flows.

Notes to the financial statements

**A3 Net debt  
(continued)**

					Borrowings		Derivatives		Total liabilities from financing activities	Loan receivable	Cash and cash equivalents	Adjustments in calculating net debt	Net debt
	Bonds	Bank and other term borrowings	Lease liabilities	Amounts owed to intermediate parent undertaking	Redeemable Preference shares	in a fair value hedge	at fair value through profit or loss						
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
At 31 March 2021	(6,044.8)	(1,862.8)	(57.1)	(740.5)	-	263.0	40.5	<b>(8,401.7)</b>	-	638.5	98.4	<b>(7,664.8)</b>	
<b>Non-cash movements</b>													
Inflation uplift on index-linked debt	(150.4)	(78.2)	-	-	-	-	-	<b>(228.6)</b>	-	-	-	<b>(228.6)</b>	
Fair value movements	199.6	5.1	-	3.7	-	(194.1)	99.8	<b>114.1</b>	-	-	(138.5)	<b>(24.4)</b>	
Foreign exchange	(5.6)	1.3	-	-	-	-	-	<b>(4.3)</b>	-	-	-	<b>(4.3)</b>	
Other	1.4	-	(3.0)	-	-	-	-	<b>(1.6)</b>	-	-	-	<b>(1.6)</b>	
<b>Cash flows used in financing activities:</b>													
Receipts in respect of borrowings and derivatives	(173.7)	-	-	(170.0)	-	-	-	<b>(343.7)</b>	-	343.7	-	-	
Payments in respect of borrowings and derivatives <sup>(1)</sup>	375.0	204.8	1.5	142.5	-	-	-	<b>723.8</b>	-	(723.8)	-	-	
Payment in respect of loan receivable	-	-	-	-	-	-	-	-	-	-	-	-	
Dividends paid	-	-	-	-	-	-	-	-	-	(339.2)	-	<b>(339.2)</b>	
<b>Changes arising from financing activities</b>	<b>246.3</b>	<b>133.0</b>	<b>(1.5)</b>	<b>(23.8)</b>	<b>-</b>	<b>(194.1)</b>	<b>99.8</b>	<b>259.7</b>	<b>-</b>	<b>(719.3)</b>	<b>(138.5)</b>	<b>(598.1)</b>	
Cash flows used in investing activities	-	-	-	-	-	-	-	-	-	(626.5)	-	<b>(626.5)</b>	
Cash flows generated from operating activities	-	-	1.5	-	-	-	-	<b>1.5</b>	-	868.4	-	<b>869.9</b>	
At 31 March 2022	(5,798.5)	(1,729.8)	(57.1)	(764.3)	-	68.9	140.3	<b>(8,140.5)</b>	-	161.1	(40.1)	<b>(8,019.5)</b>	

Notes to the financial statements

A3 Net debt (continued)

					Borrowings		Derivatives		Total liabilities from financing activities	Loan receivable	Cash and cash equivalents	Adjustments in calculating net debt	Net debt
	Bonds	Bank and other term borrowings	Lease liabilities	Amounts owed to intermediate parent undertaking	Redeemable Preference shares	in a fair value hedge	at fair value through profit or loss						
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	
At 31 March 2020	(5,251.0)	(2,522.1)	(54.4)	(1,057.3)	(130.0)	395.7	80.6	(8,538.5)	40.0	487.7	131.7	(7,879.1)	
<b>Non-cash movements</b>													
Inflation uplift on index-linked debt	(32.4)	(20.2)	-	-	-	-	-	(52.6)	-	-	-	(52.6)	
Fair value movements	100.0	11.4	-	24.0	-	(140.7)	(40.1)	(45.4)	-	-	(33.3)	(78.7)	
Foreign exchange	38.7	5.2	-	-	-	-	-	43.9	-	-	-	43.9	
Other	0.7	-	(5.9)	-	-	-	-	(5.2)	-	-	-	(5.2)	
<b>Cash flows used in financing activities:</b>													
Receipts in respect of borrowings and derivatives	(900.7)	(6.1)	-	(658.0)	-	(2.9)	-	(1,567.7)	-	1,565.1	-	(2.6)	
Payments in respect of borrowings and derivatives <sup>(1)</sup>	-	669.0	1.5	950.8	130.0	10.8	-	1,762.1	-	(1,762.1)	-	-	
Payment in respect of loan receivable	-	-	-	-	-	-	-	-	(40.0)	40.0	-	-	
Dividends paid	-	-	-	-	-	-	-	-	-	-	-	-	
<b>Changes arising from financing activities</b>	<b>(793.7)</b>	<b>659.4</b>	<b>(4.4)</b>	<b>316.8</b>	<b>130.0</b>	<b>(132.7)</b>	<b>(40.1)</b>	<b>135.1</b>	<b>(40.0)</b>	<b>(157.0)</b>	<b>(33.3)</b>	<b>(95.2)</b>	
Cash flows used in investing activities	-	-	-	-	-	-	-	-	-	(633.1)	-	(633.1)	
Cash flows generated from operating activities	-	-	1.7	-	-	-	-	1.7	-	940.9	-	942.6	
<b>At 31 March 2021</b>	<b>(6,044.8)</b>	<b>(1,862.8)</b>	<b>(57.1)</b>	<b>(740.5)</b>	<b>-</b>	<b>263.0</b>	<b>40.5</b>	<b>(8,401.7)</b>	<b>-</b>	<b>638.5</b>	<b>98.4</b>	<b>(7,664.8)</b>	

## Notes to the financial statements

### A4 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:

Group and company	Currency	Year of final repayment	Fair value 2022 £m	Carrying value 2022 £m	Fair value 2021 £m	Carrying value 2021 £m
<b>Borrowings in fair value hedge relationships</b>			<b>2,551.5</b>	<b>2,494.0</b>	<b>2,913.5</b>	<b>2,895.4</b>
5.75% 375m bond	GBP	2022	-	-	394.5	388.5
2.0% 450m bond <sup>(1)</sup>	GBP	2025	450.1	441.2	470.6	465.3
2.867% 320m bond <sup>(1)</sup>	HKD	2026	30.8	31.3	31.7	32.0
2.92% 739m bond <sup>(1)</sup>	HKD	2026	71.0	72.4	73.2	74.1
1.129% 52m bond <sup>(1)</sup>	EUR	2027	43.4	43.2	46.9	46.6
2.37% 830m bond <sup>(1)</sup>	HKD	2027	77.0	80.4	79.6	81.9
5.625% 300m bond	GBP	2027	356.4	347.6	388.0	380.4
			95.4	94.1	-	-
5.02% JPY 10bn dual currency loan	JPY/USD	2029	80.9	83.9	87.2	90.2
0.875% 300m bond <sup>(1)</sup>	GBP	2029	269.0	274.6	284.8	295.8
2.058% 30m bond <sup>(1)</sup>	EUR	2030	26.4	25.7	28.9	28.6
			64.5	67.6		
2.625% 350m bond <sup>(1)</sup>	GBP	2031	428.5	407.8	460.8	440.5
1.641% 30m bond <sup>(1)</sup>	EUR	2031	25.6	24.5	28.0	27.4
2.9% 600m bond <sup>(1)</sup>	HKD	2031	58.4	55.1	60.4	56.4
1.474% 35m bond <sup>(1)</sup>	USD	2031	22.4	22.8	23.5	22.7
1.707% 28m bond <sup>(1)</sup>	EUR	2032	23.8	24.0	26.1	27.0
1.653% 26m bond <sup>(1)</sup>	EUR	2032	21.0	21.9	24.0	24.7
1.70% 30m bond <sup>(1)</sup>	EUR	2033	25.3	25.7	27.8	29.0
2.0% 50m bond <sup>(1)</sup>	GBP	2033	94.8	91.7	103.8	98.4
5.0% 200m bond	GBP	2035	246.8	258.5	273.7	285.9
<b>Borrowings designated at fair value through profit or loss</b>			<b>369.9</b>	<b>369.9</b>	<b>373.6</b>	<b>373.6</b>
6.875% 400m bond (owed to intermediate parent)	USD	2028	369.9	369.9	373.6	373.6
<b>Borrowings measured at amortised cost</b>			<b>6,674.4</b>	<b>5,506.6</b>	<b>6,832.4</b>	<b>5,446.5</b>
Short-term bank borrowings - fixed	GBP	2022	49.2	42.9	50.7	50.7
0.80% + LIBOR 100m loan <sup>(2)</sup>	GBP	2022	-	-	101.1	100.0
0.47% + RPI 100m IL loan	GBP	2023	132.3	129.1	125.2	119.7
0.49% + RPI 100m IL loan	GBP	2025	134.3	124.2	126.6	115.2
0.013% + RPI 25m IL bond <sup>(1)</sup>	GBP	2025	33.2	31.0	30.7	28.7
0.1275% + RPI 100m IL loan	GBP	2026	133.3	122.5	125.0	113.6
0.01% + RPI 20m IL bond <sup>(1)</sup>	GBP	2028	26.6	25.3	25.0	23.7
1.23% + RPI 50m EIB (amortising) IL loan	GBP	2029	37.6	34.7	40.5	36.8
0.288% + CPI 100m IL loan	GBP	2029	117.0	107.6	113.9	102.1
1.29% + RPI 50m EIB (amortising) IL loan	GBP	2029	40.2	36.9	42.9	38.8
1.12% + RPI 50m EIB (amortising) IL loan	GBP	2029	39.7	36.6	42.4	38.5
1.10% + RPI 50m EIB (amortising) IL loan	GBP	2029	39.7	36.6	42.3	38.5
0.75% + RPI 50m EIB (amortising) IL loan	GBP	2029	41.2	38.2	43.6	39.8
0.76% + RPI 50m EIB (amortising) IL loan	GBP	2030	41.1	38.1	43.6	39.7
1.15% + RPI 50m EIB (amortising) IL loan	GBP	2030	41.5	37.9	44.1	39.6
1.11% + RPI 50m EIB (amortising) IL loan	GBP	2030	41.6	38.0	44.2	39.7
0.178% + RPI 35m IL bond <sup>(1)</sup>	GBP	2030	49.7	43.3	46.1	40.2

Notes to the financial statements

A4 Borrowings (continued)

Borrowings measured at amortised cost (continued)	Currency	Year of final repayment	Fair value 2022	Carrying value 2022	Fair value 2021	Carrying value 2021
0.245% + CPI 20m IL bond <sup>(1)</sup>	GBP	2031	24.5	22.7	24.0	21.5
0.01% + RPI 38m IL bond <sup>(1)</sup>	GBP	2031	50.8	47.6	48.6	44.5
3.375% + RPI 50m IL bond	GBP	2032	142.2	86.4	140.2	83.1
0.986% + SONIA 100m EIB (amortising) loan <sup>(3)</sup>	GBP	2032	61.6	62.5	68.7	68.8
0.968% + SONIA 150m EIB (amortising) loan <sup>(3)</sup>	GBP	2032	96.8	98.4	107.6	107.8
0.850% + SONIA 100m EIB (amortising) loan <sup>(3)</sup>	GBP	2033	67.1	68.8	74.2	75.0
0.788% + SONIA 150m EIB (amortising) loan <sup>(3)</sup>	GBP	2033	104.9	107.8	115.7	117.2
2.0% 250m bond <sup>(1)</sup>	GBP	2033	236.9	245.6	259.4	245.7
0.01% + RPI 100m EIB (amortising) IL loan	GBP	2033	97.6	91.8	100.3	92.2
0.01% + RPI 75m EIB (amortising) IL loan	GBP	2034	73.2	68.8	75.3	69.1
0.01% + RPI 75m EIB (amortising) IL loan	GBP	2034	76.0	71.3	77.9	71.4
0.01% + RPI 75m EIB (amortising) IL loan	GBP	2034	75.9	71.3	77.9	71.4
1.9799% + RPI 100m IL bond	GBP	2035	242.4	161.1	243.9	155.2
1.150% + SONIA 100m EIB (amortising) loan <sup>(3)</sup>	GBP	2035	83.5	84.4	91.6	90.6
1.117% + SONIA 75m EIB (amortising) loan <sup>(3)</sup>	GBP	2035	66.6	65.6	71.2	70.3
0.01% + RPI 26.5m IL bond <sup>(1)</sup>	GBP	2036	36.3	35.1	35.7	33.0
0.379% + CPI 20m IL bond <sup>(1)</sup>	GBP	2036	25.4	22.7	25.6	21.5
0.01% + RPI 29m IL bond <sup>(1)</sup>	GBP	2036	39.5	36.6	38.9	34.2
0.093% + CPI 60m IL bond <sup>(1)</sup>	GBP	2037	73.2	67.6	73.7	64.1
1.66% + RPI 35m IL bond	GBP	2037	70.6	53.5	68.2	49.6
1.75% 250m bond <sup>(1)</sup>	GBP	2038	215.0	248.2	236.7	248.1
2.40% + RPI 70m IL bond	GBP	2039	152.2	104.4	148.8	96.8
1.7829% + RPI 100m IL bond	GBP	2040	255.2	159.4	237.4	153.5
0.01% + CPI 125m IL bond <sup>(1)</sup>	GBP	2040	143.9	151.3	144.5	145.6
1.3258% + RPI 50m IL bond	GBP	2041	120.1	79.6	117.8	76.6
1.5802% + RPI 100m IL bond	GBP	2042	248.9	158.9	205.1	153.1
1.875% 300m bond <sup>(1)</sup>	GBP	2042	257.1	295.5	287.7	295.3
1.5366% + RPI 50m IL bond	GBP	2043	51.1	31.7	49.6	30.6
1.397% + RPI 50m IL bond	GBP	2046	126.0	79.5	113.6	76.5
0.359% + CPI 32m IL bond <sup>(1)</sup>	GBP	2048	40.7	35.6	41.0	33.8
1.7937% + RPI 50m IL bond	GBP	2049	143.8	79.1	122.4	76.2
Commission for New Towns (amortising) loan – fixed	GBP	2053	46.3	25.5	52.6	26.2
1.847% + RPI 100m IL bond	GBP	2056	252.7	161.5	255.0	149.8
1.815% + RPI 100m IL bond	GBP	2056	250.8	160.8	251.9	149.1
1.662% + RPI 100m IL bond	GBP	2056	244.6	160.5	241.6	148.8
1.5865% + RPI 50m IL bond	GBP	2056	120.1	80.2	122.0	74.4
1.591% + RPI 25m IL bond	GBP	2056	60.7	40.0	60.5	37.1
1.556% + RPI 50m IL bond	GBP	2056	122.2	79.8	121.6	74.0
1.435% + RPI 50m IL bond	GBP	2056	119.1	79.5	119.4	73.7
1.3805% + RPI 35m IL bond	GBP	2056	81.7	55.7	82.4	51.6
1.585% + RPI 100m IL bond	GBP	2057	241.2	154.5	311.2	143.2
0.387% + CPI 33m IL bond <sup>(1)</sup>	GBP	2057	42.6	36.4	44.4	34.5
1.702% + RPI 50m IL bond	GBP	2057	122.8	77.9	124.5	72.2
Amounts owed to intermediate parent undertaking	GBP	Various	394.5	394.5	367.9	367.0
Book overdrafts (see note 12)	GBP	2022	20.8	20.8	10.1	10.1
Lease liabilities	GBP	Various	57.1	57.1	57.1	57.1
			<b>9,555.8</b>	<b>8,370.5</b>	<b>10,119.5</b>	<b>8,715.4</b>

## Notes to the financial statements

### A4 Borrowings (continued)

(1) For the company these borrowings relate to amounts owed to subsidiary undertakings on terms identical to those of the bonds held by United Utilities Water Finance PLC.

(2) Loan repaid in October 2021. As such the floating reference rate through to repayment was LIBOR.

(3) Rates on these loans have been affected by the IBOR transition. The LIBOR/SONIA credit adjustment spread, finalised as a spread adjustment at 27.66bps in each instance, has been added to the fixed rate component referenced in the table to reflect the underlying fixed interest payable post IBOR-reform.

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 the 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 table are unsecured. Funding raised in foreign currencies is swapped to sterling to match funding costs to income and assets.

### A5 Financial risk management

#### *Risk management*

The board (or as appropriate the UUG board) is responsible for treasury strategy and governance, which is reviewed on an annual basis.

The UUG treasury committee, a subcommittee of the UUG 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. As well as managing our exposure to these risks, these policies help the group to maintain compliance with relevant financial covenants, which are in place primarily in relation to borrowings from the European Investment Bank (EIB) and include interest cover and gearing metrics. These policies are reviewed by the UUG 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 UUG treasury committee, which details the status of the group's compliance with treasury policies and highlights the level of risk against the appropriate risk limits in place.

The 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 set with reference to overall UUG policy parameters. Liquidity is actively monitored by the treasury function and is reported monthly to the UUG treasury committee through the operational compliance report.

At 31 March 2022, the group and company had £736.9 million (2021: £1,203.6 million) of available liquidity, which comprised £181.9 million cash and short-term deposits (2021: £648.6 million) and £555.0 million (2021: £555.0 million) of undrawn committed borrowing facilities. Short-term deposits mature within three months and bank overdrafts are repayable on demand.

## Notes to the financial statements

### A5 Financial Risk Management (continued)

The group and company had available committed borrowing facilities as follows:

	2022 £m	2021 £m
<b>Group and company</b>		
Expiring within one year	80.0	80.0
Expiring after one year but in less than two years	115.0	80.0
Expiring after more than two years	360.0	395.0
<b>Total borrowing facilities</b>	<b>555.0</b>	<b>555.0</b>
Facilities drawn	-	-
<b>Undrawn borrowing facilities</b>	<b>555.0</b>	<b>555.0</b>

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.

#### *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 and company'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. This table does not include the impact of lease liabilities for which the maturity profile on an undiscounted basis has been disclosed in note 14.

Group and company	Total <sup>(1)</sup>	Adjustment <sup>(2)</sup>	1 year or less	1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years
At 31 March 2022	£m	£m	£m	£m	£m	£m	£m	£m
Bonds	6,988.0		114.3	66.2	67.4	68.6	69.9	6,601.6
Bonds – UUWF	3,923.3		51.6	51.6	501.6	178.0	39.7	3,100.8
Bank and other term borrowings	1,970.2		261.3	133.4	268.9	269.5	131.4	905.7
Parent borrowings	654.3		187.6	81.3	20.7	20.5	20.4	323.8
Adjustment to carrying value <sup>(2)</sup>	(5,222.4)	(5,222.4)						
Borrowings	8,313.4	(5,222.4)	614.8	332.5	858.6	536.6	261.4	10,931.9
Derivatives:								
Payable	1,209.5		42.5	59.5	58.9	146.3	41.1	861.2
Receivable	(1,756.0)		(123.0)	(141.7)	(122.2)	(193.5)	(86.5)	(1,089.1)
Adjustment to carrying value <sup>(2)</sup>	226.1	226.1						
Derivatives – net assets	(320.4)	226.1	(80.5)	(82.2)	(63.3)	(47.2)	(45.4)	(227.9)

## Notes to the financial statements

### A5 Financial Risk Management (continued)

Group and company	Total <sup>(1)</sup>	Adjustment <sup>(2)</sup>	1 year or less	1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years
At 31 March 2021	£m	£m	£m	£m	£m	£m	£m	£m
Bonds	7,228.7		509.2	63.0	64.1	65.2	66.4	6,460.8
Bonds – UUWF	3,768.3		49.7	49.7	49.7	499.7	169.7	2,949.8
Bank and other term borrowings	2,113.3		118.9	348.7	122.4	254.3	257.3	1,011.7
Parent borrowings	790.4		184.0	164.0	80.0	19.7	19.6	323.1
Adjustment to carrying value <sup>(2)</sup>	(5,242.4)	(5,242.4)						
<b>Borrowings</b>	<b>8,658.3</b>	<b>(5, 242.4)</b>	<b>861.8</b>	<b>625.4</b>	<b>316.2</b>	<b>838.9</b>	<b>513.0</b>	<b>10,745.4</b>
Derivatives:								
Payable	917.1		49.3	43.1	38.0	36.0	129.2	621.5
Receivable	(1,415.7)		(102.0)	(125.6)	(92.0)	(99.7)	(202.3)	(794.1)
Adjustment to carrying value <sup>(2)</sup>	188.6	188.6						
<b>Derivatives – net assets</b>	<b>(310.0)</b>	<b>188.6</b>	<b>(52.7)</b>	<b>(82.5)</b>	<b>(54.0)</b>	<b>(63.7)</b>	<b>(73.1)</b>	<b>(172.6)</b>

Notes:

<sup>(1)</sup> 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.

<sup>(2)</sup> 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, excluding £57.1 million (2021: £57.1 million) of lease liabilities.

For the company, those bonds with United Utilities Water Finance PLC represent amounts owed to subsidiary undertakings.

#### 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 from household customers are limited due to the customer base being comprised of a large number of unrelated households. However, collection can be challenging as 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 credit terms for the group's retail customers are set out in market codes.

## Notes to the financial statements

### A5 Financial Risk Management (continued)

In reaction to the impact of the COVID-19 pandemic, changes were made to the payment terms set out within the market codes. These changes provided the option for extended credit terms for retailers. However, this has now ended and all outstanding payments have been made. As at 31 March 2022, Water Plus was the group's single largest debtor, with amounts outstanding in relation to wholesale services of £28.6 million (2021: £27.7 million). During the year, sales to Water Plus in relation to wholesale services were £363.1 million (2021: £362.9 million). Details of transactions with Water Plus can be found in note A7.

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 11).

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 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 2022 and 31 March 2021, 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:

	2022	2021
	£m	£m
<b>Group and company</b>		
Cash and short-term deposits (see note 12)	181.9	648.6
Trade and other receivables (see note 11)	227.5	224.8
Derivative financial instruments	457.4	424.7
	866.8	1,298.1
	866.8	1,298.1

The credit exposure on derivatives is disclosed gross of any collateral held. At 31 March 2022, the group and company held £49.2 million (2021: £50.7 million) as collateral in relation to derivative financial instruments (included within short-term bank borrowings - fixed in note A4).

#### Market risk

The group and company'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. For the 2020-2025 regulatory period, from 1 April 2020 the group's RCV is 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.

## Notes to the financial statements

### A5 Financial risk management (continued)

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 currently weighted towards RPI-linked form, with circa 75 per cent of the hedge linked to RPI and circa 25 per cent linked to CPI and/or CPIH. These weightings are consistent with the prior financial year.

The group believes this is an appropriate inflation hedging policy taking into account a balanced assessment of the following factors: economic hedge of the company's 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 the increase in the CPI/CPIH-linked hedge proportion over the past few years. Inflation risk is reported monthly to the UU group's treasury committee in the operational compliance report.

The carrying value of index-linked debt held by the group, including the carrying value of the nominal debt swapped to CPI, was £4,220.4 million at 31 March 2022 (2021: £4,094.3 million).

#### 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 impact of inflation on revenues and other income statement costs as well as the hedging aspect of the group's regulatory assets and post-retirement obligations.

#### Increase/(decrease) in profit before tax and equity

	2022	2021
Group and company	£m	£m
1 per cent increase in RPI/CPI	(37.0)	(35.4)
1 per cent decrease in RPI/CPI	37.0	35.4

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.

#### 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).

## Notes to the financial statements

### A5 Financial risk management (continued)

From 1 April 2020 for the regulatory period to 2025, Ofwat has continued to set a fixed real cost of debt in relation to embedded debt (80 per cent of net debt), but has introduced a debt indexation mechanism in relation to new debt (20 per cent of net debt), where the allowed rate on new debt will vary in line with specific debt indices. The debt indexation mechanism will be settled as an end of regulatory period adjustment.

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. As such, at the start of each regulatory period, a proportion of the projected nominal net debt representing new debt for that regulatory period, will remain floating until it is fixed via the above 10-year reducing balance basis, which should approximate 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 UU group's treasury committee through the operational compliance report.

#### Sensitivity analysis

The following table details the sensitivity of 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.

#### Increase/(decrease) in profit before tax and equity

	2022	2021
<b>Group and company</b>	£m	£m
1 per cent increase in interest rate	85.0	124.2
1 per cent decrease in interest rate	(89.9)	(128.3)

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

### A5 Financial risk management (continued)

#### Hedge accounting

Details regarding the interest rate swaps designated as hedging instruments to manage interest rate risk are summarised below:

	1 year or less	1 to 2 years	2 to 5 years	Over 5 years
Notional principal amount £m	-	-	450.0	1,425.0
Average contracted fixed interest rate %	-	-	1.00	2.15

This table represents the derivatives that are held in fair value hedging relationships, with the weighted average net fixed rate receivable across both legs to the swap disclosed. The SONIA/LIBOR credit adjustment spread has been assumed to form part of the fixed rate element of the payable leg which is to be netted off against the fixed rate receivable leg for the purposes of the rates shown.

Further detail on the fair value hedging relationships is provided below:

Risk exposure	Interest rate risk on borrowings	
Nominal amount of hedging instruments	£m	1,875.0
Carrying amount of hedging instruments	£m	45.8
Accumulated fair value (gains)/losses on hedged items	£m	33.9
<b>Fair value (gains)/losses used for calculating hedge ineffectiveness for the year ended 31 March 2022<sup>(1)</sup>:</b>		
Hedged items	£m	(164.6)
Hedging instruments	£m	162.7
Hedge ineffectiveness recognised in the income statement	£m	(1.9)
Nominal amount of hedging instruments directly impacted by the IBOR reform	£m	1,675.0

Note:

<sup>(1)</sup> The change in fair value of the hedging instruments used to measure hedge ineffectiveness exclude interest accruals and changes in credit spread adjustments. The full impact of fair value movements on the income statement is disclosed in note 6.

#### 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.

## Notes to the financial statements

### A5 Financial risk management (continued)

#### Hedge accounting

Details regarding the cross-currency interest rate swaps designated as hedging instruments to manage currency and interest rate risk are summarised below:

	1 year or less	1 to 2 years	2 to 5 years	Over 5 years
Notional principal amount £m	-	-	99.9	442.9
Average contracted fixed interest rate %	-	-	1.92	0.96

This table represents the derivatives that are held in fair value hedging relationships, with only the weighted average net receivable for the fixed interest rate elements of the swap disclosed. The SONIA/LIBOR credit adjustment spread has been assumed to form part of the fixed rate payable which is to be netted off against the fixed rate receivable for the purposes of the rates shown here. Further detail on the fair value hedging relationships is provided below:

Risk exposure	Foreign currency and interest rate risk on borrowings	
Nominal amount of hedging instruments	£m	542.8
Carrying amount of hedging instruments	£m	23.0
Accumulated fair value (gains)/losses on hedged items	£m	31.8
<b>Fair value (gains)/losses used for calculating hedge ineffectiveness for the year ended 31 March 2022<sup>(1)</sup>:</b>		
Hedged items	£m	(34.8)
Hedging instruments	£m	36.7
Hedge ineffectiveness recognised in the income statement	£m	1.9
Nominal amount of hedging instruments directly impacted by the IBOR reform	£m	442.8

Note:

<sup>(1)</sup> The change in fair value of the hedging instruments used to measure hedge ineffectiveness exclude interest accruals and changes in credit spread adjustments. The full impact of fair value movements on the income statement is disclosed in note 6.

#### Interest rate benchmark reform

Globally, financial regulators are requiring that market participants cease using certain financial market benchmark reference rates (i.e. interbank offered rates, IBORs), and transition to the use of alternative nearly risk-free rates (RFRs).

The only benchmark reference rate that the group was exposed to was GBP LIBOR, which ceased on 31 December 2021. In the run up to 31 December 2021, the group fully transitioned all of its financial instruments away from GBP LIBOR.

## Notes to the financial statements

### A5 Financial risk management (continued)

Floating rate loans payable were re-documented to replace references to GBP LIBOR with appropriate sterling risk free rates or, where the maturity date was sufficiently short, repaid early to avoid re-documentation. Derivatives were transitioned away from GBP LIBOR by the group and all of its counterparties adhering to the ISDA 2020 IBOR fall-backs protocol, which has automatically replaced references in derivatives to GBP LIBOR with risk free rates, and systems were upgraded to enable accurate recording and valuation of transitioned financial instruments. Inter-company loans and loans receivable with the group's principal joint venture have also been restructured to reference the Bank of England Base Rate.

The group is not exposed to any other benchmark reference rate and so its activities in relation to interest rate benchmark reform are now complete.

In August 2020, the IASB issued Interest Rate Benchmark Reform Phase II, Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 (the Phase II Amendments), and the group has applied all relevant amendments when accounting for the impact of the IBOR transition in the year.

Applying the ISDA fall-back provisions in transitioning the group's derivative portfolio has maintained economic equivalence across the financial instruments held in fair value hedges and, as a result, immaterial hedge ineffectiveness was recorded in the group's income statement in the year.

The amount of financial instruments that transitioned to alternative benchmarks is set out below. Non-derivative financial instruments are presented at their carrying value, with the derivatives at their nominal value, in order to give the fairest representation of the magnitude of instruments that transitioned to RFRs. In addition to the below, the group held £555.0 million of undrawn committed facilities as at 31 December 2021 that transitioned away from referencing LIBOR to reference sterling risk free rates.

Type of financial instrument	Amounts transitioned to RFR (£m)
Non-derivative financial liabilities (pay GBP LIBOR)	£501.6
Derivative instruments (pay GBP LIBOR)	£2,343.9
Derivative instruments (receive GBP LIBOR)	£(2,822.1)
Net position	£23.4

#### **Repricing analysis**

The following tables categorise the group and company's borrowings, derivatives and cash deposits on the basis of when they reprice or, if earlier, mature.

The repricing analysis demonstrates the group and company'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.

## Notes to the financial statements

## A5 Financial risk management (continued)

Group and company	Total	1 year	1-2	2-3	3-4	4-5	More
At 31 March 2022	£m	or less	years	years	years	years	than 5
		£m	£m	£m	£m	£m	£m
<b>Borrowings in fair value hedge relationships</b>							
Fixed rate instruments	2,494.0	-	-	441.2	103.7	-	1,949.1
Effect of swaps	-	2,494.0	-	(441.2)	(103.7)	-	(1,949.1)
	<u>2,494.0</u>	<u>2,494.0</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Borrowings designated at fair value through profit or loss</b>							
Fixed rate instruments	369.9	-	-	-	-	-	369.9
Effect of swaps	-	(369.9)	-	-	-	-	(369.9)
	<u>369.9</u>	<u>(369.9)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Borrowings measured at amortised cost</b>							
Fixed rate instruments	921.1	50.1	1.1	1.9	3.2	1.4	863.4
Floating rate instruments	902.8	902.8	-	-	-	-	-
Index-linked instruments	3,682.7	3,682.7	-	-	-	-	-
	<u>5,506.6</u>	<u>4,635.6</u>	<u>1.1</u>	<u>1.9</u>	<u>3.2</u>	<u>1.4</u>	<u>863.4</u>
Effect of fixed interest rate swaps	-	(2,267.8)	575.0	350.0	200.0	-	1,142.8
<b>Total borrowings</b>	<u>8,370.5</u>	<u>5,231.7</u>	<u>576.1</u>	<u>351.9</u>	<u>203.2</u>	<u>1.4</u>	<u>2,006.2</u>
Cash and short-term deposits	(181.9)	(181.9)	-	-	-	-	-
<b>Net borrowings</b>	<u>8,188.6</u>	<u>5,049.8</u>	<u>576.1</u>	<u>351.9</u>	<u>203.2</u>	<u>1.4</u>	<u>2,006.2</u>

## Notes to the financial statements

## A5 Financial risk management (continued)

Group and company	Total	1 year	1-2	2-3	3-4	4-5	than 5
At 31 March 2021	£m	or less	years	years	years	years	years
		£m	£m	£m	£m	£m	£m
<b>Borrowings in fair value hedge relationships</b>							
Fixed rate instruments	2,895.5	388.6	-	-	465.3	106.1	1,935.5
Effect of swaps	-	2,590.5	-	-	(465.3)	(106.1)	(1,935.5)
	<u>2,590.5</u>	<u>2,895.5</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Borrowings designated at fair value through profit or loss</b>							
Fixed rate instruments	373.6	-	-	-	-	-	373.6
Effect of swaps	-	373.6	-	-	-	-	(373.6)
	<u>373.6</u>	<u>373.6</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Borrowings measured at amortised cost</b>							
Fixed rate instruments	923.1	51.2	1.0	1.1	0.9	3.7	865.1
Floating rate instruments	1,006.7	1,006.7	-	-	-	-	-
Index-linked instruments	3,516.5	3,516.5	-	-	-	-	-
	<u>5,446.3</u>	<u>4,574.4</u>	<u>1.0</u>	<u>1.1</u>	<u>0.9</u>	<u>3.7</u>	<u>865.1</u>
Effect of fixed interest rate swaps	-	(2,332.3)	164.5	575.0	350.0	200.0	1,042.8
	<u>-</u>	<u>(2,332.3)</u>	<u>164.5</u>	<u>575.0</u>	<u>350.0</u>	<u>200.0</u>	<u>1,042.8</u>
<b>Total borrowings</b>	<u>8,715.4</u>	<u>5,511.2</u>	<u>165.5</u>	<u>576.1</u>	<u>350.9</u>	<u>203.7</u>	<u>1,907.9</u>
Cash and short-term deposits	(648.6)	(648.6)	-	-	-	-	-
	<u>(648.6)</u>	<u>(648.6)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Net borrowings</b>	<u>8,066.8</u>	<u>4,862.6</u>	<u>165.5</u>	<u>576.1</u>	<u>350.9</u>	<u>203.7</u>	<u>1,907.9</u>

**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 proportion of its anticipated net electricity usage out to the end of the regulatory period from 2020 to 2025, partially through entering into electricity swap contracts.

## Notes to the financial statements

### A5 Financial risk management (continued)

#### Hedge accounting

Details of electricity swaps designated as hedging instruments to manage electricity price risk are summarised below:

	1 year or less	1 to 2 years	2 to 5 years	Over 5 years
Notional amount MWh	306,480	329,400	350,280	-
Average contracted fixed interest rate %	46.52	46.35	45.95	-

Electricity swaps have been designated in 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 in the effective portion of the hedge being recognised in other comprehensive income.

Risk exposure	Electricity price risk	
Nominal amount of hedging instruments	£m	45.6
Carrying amount of hedging instruments	£m	111.1
Fair value (gains)/losses used for calculating hedge ineffectiveness for the year ended 31 March 2022 <sup>(1)</sup> :	£m	106.7
Hedge ineffectiveness recognised in the income statement	£m	-
Cash flow hedge reserve	£m	86.3
Amount reclassified from the cash flow hedge reserve to the income statement	£m	(1.3)

Note:

<sup>(1)</sup> The change in fair value of the hedging instruments used to measure hedge ineffectiveness exclude interest accruals and changes in credit spread adjustments. The full impact of fair value movements on the income statement is disclosed in note 6.

#### Capital risk management

The group's objective when managing capital is to maintain efficient access to debt capital markets throughout the economic cycle.

Assuming no significant changes to existing rating agencies' methodologies or sector risk assessments, the group aims to maintain long-term issuer credit ratings for U UW of at least A3 with Moody's Investors Service (Moody's) and BBB+ with S&P Global (S&P) and a senior unsecured debt rating for U UW of at least A- with Fitch Ratings (Fitch). Debt issued by U UW's financing subsidiary, United Utilities Water Finance PLC, is guaranteed by U UW and is therefore rated in line with U UW.

## Notes to the financial statements

### A5 Financial risk management (continued)

In order to maintain its targeted credit ratings, the group needs to manage its capital structure with reference to the ratings methodology and measures used by Moody's, S&P and Fitch. The ratings methodology is normally based on a number of key ratios (such as RCV gearing, adjusted interest cover, post maintenance interest cover (PMICR), Funds from Operations (FFO) to debt, and debt to EBITDA) and threshold levels as updated and published from time to time by Moody's, S&P and Fitch. The group looks to manage its risk by maintaining the relevant key financial ratios used by the credit ratings agencies to determine a corporate's credit rating, within the thresholds approved by the board.

Capital risk is reported monthly to the UU group's 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.

#### 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 and company

At 31 March 2022	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
<b>Financial assets at fair value through profit or loss</b>				
Derivative financial assets – fair value hedge	-	156.1	-	156.1
Derivative financial assets – held for trading <sup>(1)</sup>	-	190.1	-	190.1
Derivative financial assets – cash flow hedge	-	111.0	-	111.0
Investments	-	0.1	-	0.1
<b>Financial liabilities at fair value through profit or loss</b>				
Derivative financial liabilities – fair value hedge	-	(87.2)	-	(87.2)
Derivative financial liabilities – held for trading <sup>(1)</sup>	-	(49.8)	-	(49.8)
Derivative financial liabilities – cash flow hedge	-	-	-	-
Financial liabilities designated as fair value through profit or loss	-	(369.9)	-	(369.9)
<b>Financial liabilities for which fair value has been disclosed</b>				
Financial liabilities in fair value hedge relationships	(2,206.6)	(304.9)	-	(2,511.5)
Other financial liabilities at amortised cost	(2,383.8)	(4,290.6)	-	(6,674.4)
	<u>(4,590.4)</u>	<u>(4,645.1)</u>	<u>-</u>	<u>(9,235.5)</u>

## Notes to the financial statements

### A5 Financial risk management (continued)

At 31 March 2021	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
<b>Financial assets at fair value through profit or loss</b>				
Derivative financial assets – fair value hedge	-	272.8	-	272.8
Derivative financial assets – held for trading <sup>(1)</sup>	-	142.6	-	142.6
Derivative financial assets – cash flow hedge	-	6.9	-	6.9
Investments	-	0.1	-	0.1
<b>Financial liabilities at fair value through profit or loss</b>				
Derivative financial liabilities – fair value hedge	-	(12.6)	-	(12.6)
Derivative financial liabilities – held for trading <sup>(1)</sup>	-	(100.3)	-	(100.3)
Derivative financial liabilities – cash flow hedge	-	-	-	-
Financial liabilities designated as fair value through profit or loss	-	(373.6)	-	(373.6)
<b>Financial liabilities for which fair value has been disclosed</b>				
Financial liabilities in fair value hedge relationships	(2,766.0)	(147.5)	-	(2,913.5)
Other financial liabilities at amortised cost	(1,863.4)	(4,969.0)	-	(6,832.4)
	<u>(4,629.4)</u>	<u>(5,180.6)</u>	<u>-</u>	<u>(9,810.0)</u>

Notes:

<sup>(1)</sup> 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 £130.1 million (2021: £146.3 million).

- 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 £4,590.4 million (2021: £4,629.4 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 £39.0 million decrease (2021: £2,448.0 million increase) in level 1 fair value measurements primarily reflects the maturity of the 5.75 per cent £375 million bond in March 2022, which was classified as a level 1 fair value measurement in the prior financial year, and a reduction in the number of observable quoted bond prices in active markets at 31 March 2022.

During the year, changes in the fair value of financial liabilities designated at fair value through profit or loss resulted in a £0.4 million loss (2021: £23.9 million loss). Included within this was a £4.2 million gain (2021: £43.3 million loss) attributable to changes in own credit risk, recognised in other comprehensive income. The cumulative amount due to changes in credit spread was £39.9 million profit (2021: £35.7 million profit). The carrying amount is £143.8 million (2021: £147.5 million) higher than the amount contracted to settle on maturity.

## Notes to the financial statements

### A6 Retirement benefits

#### Defined benefit schemes

Under the group's defined benefit pension schemes – the United Utilities Pension Scheme (UUPS) and the United Utilities PLC group of the Electricity Supply Pension Scheme (ESPS) – employees are entitled to annual pensions on retirement. Benefits are payable on death and following other events such as withdrawing from active service. No other post-retirement benefits are provided to these 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, who are required by law to act in the interests of all relevant beneficiaries and are responsible for the investment policy with regards to the assets plus the day-to-day administration of the benefits.

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.

Since 1 April 2018, the majority of active members in the defined benefit sections of the UUPS have been part of a hybrid section comprising both defined benefit and defined contribution elements. Pension benefits relating to pensionable service before 1 April 2018 have not been affected by the transition to this hybrid section, which was introduced as a consequence of increases in future service costs 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 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.

Under the group's defined benefit pension schemes, employees are entitled to annual pensions on retirement. Benefits are payable on death and following other events such as withdrawing from active service. No other post-retirement benefits are provided to these employees.

Information about the pension arrangements for executive directors is contained in the directors' remuneration report.

As at 31 March, the total fair value of the schemes' assets, and the present value of the defined benefit obligations, and therefore the value of the net retirement benefit surplus included in the consolidated statement of financial position, was as follows:

	2022	2021
	£m	£m
<b>Group and company</b>		
Total fair value of schemes' assets	3,003.8	2,966.4
Present value of defined benefit obligations	(2,232.6)	(2,435.4)
<b>Net retirement benefit surplus</b>	<u>771.2</u>	<u>531.0</u>

## Notes to the financial statements

### A6 Retirement benefits (continued)

The defined benefit obligation includes benefits for current employees, former employees and current pensioners as analysed in the table below:

Group and company	2022 £m	2021 £m
Total value of current employees benefits	461.9	717.1
Deferred members benefits	335.4	320.0
Pensioner members benefits	1,435.3	1,398.3
<b>Total defined benefit obligation</b>	<u>2,232.6</u>	<u>2,435.4</u>

Movements in the present value of the defined benefit obligations are as follows:

	2022 £m	2021 £m
At the start of the year	(2,435.4)	(2,256.5)
Interest cost on schemes' obligations	(49.3)	(50.5)
Actuarial gains/(losses) arising from changes in financial assumptions	122.7	(323.5)
Actuarial gains arising from changes in demographic assumptions	39.2	60.5
Actuarial (losses)/gains arising from experience	(11.7)	15.3
Curtailments/settlements	-	(0.4)
Member contributions	(2.2)	(2.3)
Benefits paid	111.2	126.6
Current service cost	(7.1)	(4.6)
At the end of the year	<u>(2,232.6)</u>	<u>(2,435.4)</u>

The duration of the combined schemes is around 17 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 of future benefits payable

Under UK legislation there is a requirement that pension schemes are funded prudently, and that funding plans are agreed by pension scheme trustees. The defined benefit schemes are subject to funding valuations carried out by independent qualified actuaries, in conjunction with the schemes' trustees, on a triennial basis. These valuations inform the level of future contributions to be made by the group in order to ensure that the schemes are appropriately funded and therefore that benefits can be paid. The latest finalised funding valuation was carried out as at 31 March 2021, and determined that the schemes were fully funded on a low-dependency basis without any funding deficit that requires additional contributions from the company over and above those related to current service and expenses.

The schemes' funding plans are reviewed regularly, including between funding valuations. The group expects to make further contributions of £8.2 million in the year ending 31 March 2023, £7.5 million in respect of current service contributions and £0.7 million in respect of expenses. Annual contributions are expected to be broadly similar to this until at least the point at which the next triennial valuation (due as at 31 March 2024), is finalised, which is expected to be towards the end of the year ending 31 March 2025. At this point a detailed re-evaluation of the level of annual contributions, and the basis on which these are made, will take place.

## Notes to the financial statements

### A6 Retirement benefits (continued)

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. Both the UUPS and ESPS schemes are fully hedged for inflation exposure through external market swaps and gilts. Further details of the derivatives used in reducing investment risk are disclosed in the 'Schemes' assets' section of this appendix.

In addition to the strategies implemented to date, the group and trustees are committed to exploring further de-risking options that may be implemented in the future, including in relation to longevity risk.

The basis on which scheme liabilities are valued for funding purposes differs from the basis required under IAS 19 'Employee Benefits', 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 in the consolidated statement of financial position at both 31 March 2022 and 31 March 2021 as, under both the UUPS and ESPS scheme rules, the group has an unconditional right to a refund of the surplus assuming the gradual settlement of plan liabilities over time until all members have left the plans.

#### 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 using 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 future inflation. Both UUPS and ESPS fully hedge RPI inflation exposure along with underlying interest rates through external market swaps and gilts (including gilt repurchase instruments), the value of which is included in the schemes' assets (net of associated derivative liabilities).

Consequently, the reported statement of financial position under IAS 19 remains volatile due to changes in credit spread and changes in mortality, neither of which have been hedged at the current time.

Changes in credit spreads have not been hedged primarily due to difficulties in doing so over long durations. In contrast, the schemes' specific funding bases are unlikely to suffer from significant volatility due to credit spread, because a prudent, fixed credit spread assumption is applied.

Changes in mortality have not been hedged due to this exposure being subject to lower volatility in the short term and relatively high hedging costs, though the group and scheme trustees are committed to exploring options to de-risk changes in mortality, or pension longevity, in future periods, as outlined above.

Pension benefits under the defined benefit element of the UUPS hybrid section, which represents a relatively small proportion of total defined benefit obligations, are linked to CPI rather than RPI.

## Notes to the financial statements

### A6 Retirement benefits (continued)

In the year ended 31 March 2022, the discount rate increased by 0.75 per cent (2021: 0.25 per cent decrease), which includes a 0.35 per cent increase in credit spreads and a 0.4 per cent increase in gilt yields over the year. The IAS 19 remeasurement gain of £228.7 million (2021: £62.3 million loss) reported in note 18 has largely resulted from an increase in credit spreads during the year partially offset by an RPI inflation assumption increase of 0.4 per cent (2021: 0.55 per cent increase). The impact of movements in credit spreads is less pronounced on a scheme funding basis compared with the remeasurement loss recognised on an IAS 19 accounting basis as the discount rate used for valuing obligations utilises a fixed credit spread assumption.

#### Reporting and assumptions

The results of the latest funding valuation at 31 March 2021 have been used to inform the group's best estimate assumptions to use in calculating the defined benefit pension position reported on an IAS 19 basis at 31 March 2022. The results of the funding valuation have been adjusted to take 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 2021 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:

	2022 % p.a.	2021 % p.a.
Discount rate	2.80	2.05
Pension increases	3.75	3.35
Pensionable salary growth (pre-2018 service):		
ESPS	3.75	3.35
UUPS	3.75	3.35
Pensionable salary growth (post-2018 service):		
ESPS	3.75	3.35
UUPS	3.20	2.75
Price inflation - RPI	3.75	3.35
Price inflation - CPI <sup>(1)</sup>	3.20	2.75

Note:

<sup>(1)</sup> The CPI price inflation assumption represents a single weighted average rate derived from an assumption of 2.85 per cent pre-2030 and 3.65 per cent post-2030 (31 March 2021: 2.45 per cent pre-2030 and 3.25 per cent post-2030).

The discount rate is consistent with a high-quality corporate bond rate, with 2.80 per cent being equivalent to gilts plus 1.10 basis points (31 March 2021: 2.05 per cent being equivalent to gilts plus 75 basis points). The corporate bond population used in deriving this rate comprises corporate bonds rated at least AA by one or more credit rating agencies.

In accordance with the scheme rules, pensionable salary growth is linked to RPI for UUPS for service pre-2018 and CPI for service post-2018, for ESPS the growth is linked to RPI.

Assumed pension increases are aligned to the RPI price inflation assumption as the vast majority of benefits across the schemes have a direct RPI linkage.

## Notes to the financial statements

### A6 Retirement benefits (continued)

In September 2019, the Chancellor of the Exchequer highlighted the UK Statistic Authority's proposals to change RPI to align with CPIH (Consumer Prices Index, including housing costs). Plans to reform RPI and bring it in line with CPIH from 2030 were confirmed on 25 November 2020, though this is subject to judicial review. Broadly CPIH increases are expected to average around 1 per cent per annum below RPI in the long-term (about the same as CPI), so this change could have a significant impact on many pension schemes.

#### *Demographic assumptions*

At 31 March 2022, the base tables used for the mortality in retirement assumption are the Continuous Mortality Investigation's (CMI) S3PA (2021:S2PA) year of birth tables, with a scaling factor of 109 per cent (2021: 106 per cent) and 115 per cent (2021: 109 per cent) for male pensioners and non-pensioners respectively and 110 per cent (2021: 104 per cent) and 111 per cent (2021: 105 per cent) for female pensioners and non-pensioners respectively, reflecting the profile of the membership. At 31 March 2022, future improvements in mortality are based on the extended CMI 2021 (2021: CMI 2020) projection model, with a long-term annual rate of improvement of 1.25 per cent (2021: 1.25 per cent). To adjust for the impact of circumstances arising as a result of the COVID-19 pandemic on future mortality trends for the schemes' membership, an adjustment has been made to reflect an expectation that the direct and indirect consequences of the pandemic will have an adverse impact on longevity in the short to medium term. Accordingly, in arriving at the mortality assumptions for the current year, the group has included a w2021 parameter of 10 per cent within the CMI 2021 projections, which is a subjective estimate that has an impact of circa £22 million decrease in the defined benefit obligation. All other parameters within the future improvements model are consistent with the prior year.

The current life expectancies at age 60 underlying the value of the accrued liabilities for the schemes are:

	2022 years	2021 years
Retired member – male	25.9	26.0
Non-retired member – male	26.5	26.9
Retired member – female	27.9	28.4
Non-retired member – female	29.0	29.5

#### **Sensitivity of the key scheme assumptions**

The assumptions used in measuring the group's defined benefit surplus reflect management's best estimates as at the reporting date. These estimates inherently involve judgement, and the measurement of the defined benefit surplus is sensitive to changes in these key assumptions. These sensitivities, together with further information on the judgements involved and level of estimation uncertainty, are presented below. Sensitivity calculations 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, however it demonstrates how reasonably possible changes could impact on the measurement of the defined benefit surplus.

#### *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.

## Notes to the financial statements

### A6 Retirement benefits (continued)

#### *Discount rate*

An increase/decrease in the discount rate of 0.25 per cent would have resulted in a £95.9/£89.9 million (2021: £106.7/£114.2 million) decrease/increase in the schemes' liabilities at 31 March 2022, 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. High quality corporate bonds are considered to be those that have a credit rating of AA or above with at least one rating agency. An alternative approach could be taken whereby only those bonds rated AA or higher by at least two rating agencies are used. While this alternative approach may provide additional comfort around the quality of these corporate bonds, management believes that the wider population of corporate bonds under a 'single agency' approach gives a more representative indication of high quality corporate bonds that are aligned to the schemes' liabilities, and therefore provides a more robust estimate.

#### *Price inflation*

An increase/decrease in the inflation assumption of 0.25 per cent would have resulted in a £84.2/79.4 million (2021: £108.6/£102.3 million) increase/decrease in the schemes' liabilities at 31 March 2022, 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 2022, meaning that this sensitivity is likely to be insignificant as a result. The sensitivity to price inflation allows for the impact of changes to pensionable salary growth and pension increases, which are both assumed to be linked to price inflation. While inflation may be volatile in the near term, as has been the case during the year ended 31 March 2022, the value of the schemes' liabilities is based on inflation assumptions that reflect the full profile of the liabilities, in particular the long-term nature.

- Consistent with market practice, and reflecting the possibility that inflation may rise or fall more than expected in the future, in arriving at the company's best estimate for RPI, an inflation risk premium of 0.2 per cent (2021: 0.2 per cent) has been deducted from the breakeven inflation rate for the year ended 31 March 2022. The impact of this is a decrease in the defined benefit obligation of around £70 million and therefore an increase in the net defined benefit surplus compared with no inflation risk premium being deducted. There is no allowance for any further change in the inflation risk premium post-2030 as a result of RPI reform. A reduction in expected RPI will result in a reduction to the value of pension scheme liabilities; however, as our pension schemes are hedged for RPI inflation movements, this will result in a comparable reduction to the value of pension scheme assets.
- The assumption for CPI is set by deducting a 'wedge' from the RPI inflation assumption to reflect structural differences. For pre-2030 inflation this wedge has been estimated at 0.9 per cent per annum, reducing to 0.1 per cent per annum post-2030 given that RPI and CPI are expected to converge. The impact of this reduction in the post-2030 wedge as a result of RPI reform is a circa £6 million increase to the defined benefit obligation and therefore a decrease in the net defined benefit surplus compared with the wedge remaining at 0.9 per cent per annum after 2030.

#### *Mortality long-term improvement rate*

An increase in the mortality long-term improvement rate from 1.25 per cent to 1.50 per cent would have resulted in a £22.0 million decrease in the schemes' liabilities at 31 March 2022 (2021: £25.0 million decrease in the schemes' liabilities).

#### *Life expectancy*

An increase/decrease in life expectancy of one year would have resulted in a £98.7 million (2021: £113.1 million) increase/decrease in the schemes' liabilities at 31 March 2022. 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.

## Notes to the financial statements

### A6 Retirement benefits (continued)

#### Further reporting analysis

The fair value derivatives included within pension scheme asset classification are analysed as follows:

Group and company	Underlying Fair value of Schemes' assets			
	assets £m	derivatives £m	Combined £m	assets %
At 31 March 2022				
Non-equity growth assets	472.8	-	472.8	15.7
Gilts	2,214.3	(1,372.8)	841.5	28.0
Bonds	1,265.4	(1.6)	1,263.8	42.1
Other	341.0	84.7	425.7	14.2
<b>Total fair value of schemes' assets</b>	<u>4,293.5</u>	<u>(1,289.7)</u>	<u>3,003.8</u>	<u>100.0</u>
At 31 March 2021				
Non-equity growth assets	307.5	-	307.5	10.4
Gilts	2,188.8	(1,163.2)	1,025.6	34.6
Bonds	1,378.5	(6.9)	1,371.6	46.2
Other	280.2	(18.5)	261.7	8.8
<b>Total fair value of schemes' assets</b>	<u>4,155.0</u>	<u>(1,188.6)</u>	<u>2,966.4</u>	<u>100.0</u>

Included within the group's defined benefit pension scheme assets are assets with a fair value estimated to be £223.8 million that are categorised as 'level 3' assets within the IFRS 13 'Fair value measurement' hierarchy, meaning that the value of the assets is not observable at 31 March 2022. Estimates of the fair value of these assets have been performed by the investment managers' valuation specialists using the latest available statements of each of the funds that make up the total level 3 asset balance, updated for any subsequent cash movements between the statement date and the year end reporting date.

The UUPS has entered into a variety of derivative transactions to change the return characteristics of the assets held to reduce undesirable market and liability risks. As such, the above breakdown 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. The collateral portfolio, comprising cash and eligible securities readily convertible to cash, provides sufficient liquidity to manage exposure relating to the derivative transactions and is expected to achieve a return in excess of SONIA (Sterling Overnight Index Average).

The derivative values in the tables above represent the net market value of derivatives held within each of these asset categories as follows:

## Notes to the financial statements

### A6 Retirement benefits (continued)

<b>Group and company</b>	2022 Total £m	2021 Total £m
<b>Gilts</b>		
Repurchase agreements	(1,372.8)	(1,163.2)
	<u>(1,372.8)</u>	<u>(1,163.2)</u>
<b>Bond – hedging non-sterling exposure back to sterling</b>		
Currency forwards	(1.2)	(7.4)
Interest rate swaps	(0.4)	0.5
	<u>(1.6)</u>	<u>(6.9)</u>
<b>Other – managing liability risks targeting a high level of interest rate and inflation hedging</b>		
Asset swaps	(26.9)	(22.0)
Interest rate swaps	14.9	19.2
RPI inflation swaps	96.6	(15.5)
Total return swaps	0.1	(0.2)
	<u>84.7</u>	<u>(18.5)</u>
Total fair value of derivatives	<u>(1,289.7)</u>	<u>(1,188.6)</u>

The derivatives shown in the tables only cover those expressly held for the purpose of reducing certain undesirable asset and liability risks. The schemes 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 other pooled funds, as they are not held expressly for the purpose of managing risk. The total fair value of pooled funds held within the schemes' assets was £514.3 million (2021: £522.5 million).

The intention is that the schemes' assets provide a full economic hedge of interest rates and RPI inflation of the schemes' liabilities on a scheme funding basis. As the scheme funding basis is more prudent than the IAS 19 measurement basis for the defined benefit obligation, the schemes are more than 100 per cent hedged on an accounting basis.

Movements in the fair value of the schemes' assets were as follows:

	2022 £m	2021 £m
At the start of the year	2,966.4	2,835.6
Interest income on schemes' assets	60.4	63.9
The return on plan assets, excluding amounts included in interest	78.5	185.4
Member contributions	2.2	2.3
Benefits paid	(111.2)	(126.6)
Administrative expenses	(1.0)	(2.0)
Group contributions	8.5	7.8
At the end of the year	<u>3,003.8</u>	<u>2,966.4</u>

The group's actual return on the schemes' assets was a gain of £138.9 million (2021: £249.3 million), principally due to losses on derivatives hedging the schemes' liabilities.

## Notes to the financial statements

### A7 Related party transactions

The aggregate disclosable transactions between the UUG group and company and the related parties in the wider UUG group of companies were as follows:

Group	Sales of goods and services		Purchase of goods and services		Recharge of costs to/(by) related parties at nil margin	
	2022 £m	2021 £m	2022 £m	2021 £m	2022 £m	2021 £m
Ultimate parent undertaking	-	-	-	-	(4.6)	(3.5)
Intermediate parent undertaking	-	-	-	-	0.2	0.2
Fellow subsidiaries	-	-	4.9	4.8	1.3	2.0
Joint ventures of the UUG group	363.1	362.0	-	-	(0.7)	(0.7)
	<u>363.1</u>	<u>362.0</u>	<u>4.9</u>	<u>4.8</u>	<u>(3.8)</u>	<u>(2.0)</u>

Sales of services to related parties during the year mainly represent non-household wholesale charges to Water Plus that were billed during the period. These transactions were on the market credit terms in respect of non-household wholesale charges, which are governed by the wholesale charging rules issued by Ofwat.

There was no termination payment (2021: £2.7 million) made to a fellow subsidiary during the year. The termination payment made in the year ended 31 March 2021 was in accordance with the terms of an agreement between the two parties and related to the early removal of a solar array to facilitate the completion of capital projects. There were also £0.1 million (2021: £nil million) of charitable contributions advanced 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.

Details of transactions with key management are disclosed in note 3.

No interest income (2021: £1.6 million) was recognised on loans to joint ventures of the UUG group during the year following the transfer of a revolving credit facility extended to Water Plus from UUG to United Utilities PLC in the year ended 31 March 2021.

#### Company

In addition to the above amounts, the company incurred interest charges of £79.9 million (2021: £48.7 million) in relation to the amounts owed to its subsidiary, United Utilities Water Finance PLC (UUWF), which represent external borrowings held by UUWF that are on-lent to the company on identical terms to those borrowings owed by UUWF to external parties (see below). The company also incurred a management fee of £0.1 million (2021: £0.1 million) in relation to the services provided by UUWF.

The following amounts were outstanding at the reporting date:

Group	Amounts owed by related parties		Amounts owed to related parties	
	2022 £m	2021 £m	2022 £m	2021 £m
Ultimate parent undertaking	-	-	2.2	2.0
Intermediate parent undertaking	0.6	0.5	789.9	745.5
Immediate parent undertaking	-	-	-	-
Fellow subsidiaries	1.9	0.5	0.2	2.7
Joint ventures of the UUG group	28.5	27.1	-	1.3
	<u>31.0</u>	<u>28.1</u>	<u>792.3</u>	<u>751.5</u>

## Notes to the financial statements

### A7 Related party transactions (continued)

At 31 March 2022, amounts owed by related parties were £31.0 million (2021: £28.1 million), comprised entirely of trade balances. Trade balances are unsecured and will be settled in accordance with normal credit terms. Included within these balances was £28.5 million (2021: £27.1 million) owed by Water Plus and £2.5 million (2021: £1.0 million) owed by the group's intermediate parent company and fellow subsidiaries of the UUG group.

No expense or allowance has been recognised for bad and doubtful receivables in respect of the amounts owed by related parties (2021: £nil).

At 31 March 2022, amounts owed to related parties were £792.1 million (2021: £751.5 million), comprising £0.2 million (2021: £6.0 million) of trade balances, £764.4 million (2021: £740.5 million) of borrowings (see note 13) and its associated accrued interest of £0.2 million (2021: £0.1 million) owed to United Utilities PLC. Included within these trade balances were £nil million (2021: £1.3 million) owed to Water Plus and £2.2 million (2021: £2.0 million) owed to United Utilities Group PLC.

In addition to the above, the group's £98.8 million current tax asset (2021: £20.7 million current tax liability) included £25.5 million (2021: £4.9 million) owed to United Utilities PLC as intercompany group relief payable.

During the year, guarantees with an aggregate limit of £32.1 million (2021: £32.1 million) have been provided to the company by United Utilities PLC in respect of amounts owed by Water Plus in relation to wholesale charges.

#### Company

In addition to the amounts outstanding above, the company owed £3,232.0 million (2021: £3,024.1 million) in respect of borrowings (see note 13), and £19.2 million (2021: £17.9 million) in respect of associated accrued interest, to its subsidiary, UUWF. These amounts represent external borrowings held by UUWF, which are on-lent to the company on identical terms to those of the amounts owed to external parties. The company has guaranteed these external borrowings held by UUWF. Furthermore, the company owed £0.1 million (2020: £0.3 million) in respect of cash pooling arrangements to its intermediate parent company United Utilities PLC.

### A8 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 160 to 165.

#### Basis of consolidation

The group financial statements consolidate the financial statements of the company and entities controlled by the company (its subsidiaries). The results of subsidiaries 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.

## Notes to the financial statements

### A8 Accounting policies (continued)

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.

#### Revenue recognition

Revenue from the sale of water, wastewater and other services represents the fair value of the consideration receivable in the ordinary course of business for the 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.

There are two main areas of the group's activities considered to result in revenue being recognised:

- the provision of core water and wastewater services, accounting for more than 97 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 core water and wastewater services, which are deemed to be a distinct performance obligation under the contracts with customers, follow the same pattern of transfer to the customer who simultaneously receive and consumes both of these services over time.

Revenue is generally recognised at the time of delivery, with consideration given as to whether collection of the full amount under the contract is considered probable. Should the group consider that the criteria for revenue recognition has not been met for a transaction, revenue recognition would be delayed until such time as collectability is deemed probable.

Payments received in advance of revenue recognition are recorded as deferred income. This includes the revenue in respect of connection activities, itself a distinct performance obligation. The revenue in respect of these activities is 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.

## Notes to the financial statements

### A8 Accounting policies (continued)

#### 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, UK tax authorities. 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, 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.

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.

## Notes to the financial statements

### A8 Accounting policies (continued)

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 75 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.

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 to the operating capability and/or resilience of the network is treated as additions. Amounts incurred in maintaining the operating capability and/or resilience of the network in accordance with current standards 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.

## Notes to the financial statements

### A8 Accounting policies (continued)

#### *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 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 interpretation 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 generally amortised over a period of three to ten years.

United Utilities Water Limited expenses costs incurred in the implementation and ongoing operation of computing systems built and delivered on a 'software as a service' (SaaS) basis and hosted in an external cloud environment. These do not generally give rise to an identifiable intangible asset that the entity controls. In limited circumstances, costs incurred in association with the implementation and customisation of a SaaS system may enhance the group's existing digital infrastructure and would be expected to generate broader future economic benefit. Where this results in an identifiable intangible asset that the group controls, the costs are capitalised in accordance with IAS 38 and subsequently 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. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. 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.

## Notes to the financial statements

### A8 Accounting policies (continued)

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.

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.

#### **Capitalisation of costs associated with regulatory price review programmes**

As a regulated business, United Utilities Water Limited is required to submit business plans to its regulator, Ofwat, on a cyclical basis. The costs to develop these business plans, which can be significant, largely relate to the development of material capital programmes to be delivered over the next five-year price control period. As such, the majority of these costs are considered to be directly attributable to bringing capital solutions into working condition, giving rise to future economic benefit in the form of reduced project costs as the capital programme is delivered, and supporting the enhancement of the company's infrastructure network as a whole. Such costs are therefore capitalised within property, plant and equipment where appropriate, and depreciated over a period of five years as the economic benefit is realised through the delivery of the capital programme.

#### **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 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.

## Notes to the financial statements

### A8 Accounting policies (continued)

#### *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.

## Notes to the financial statements

### A8 Accounting policies (continued)

#### *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 A5).

#### *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.

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.

## Notes to the financial statements

### A8 Accounting policies (continued)

#### 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.

#### 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.

In order to hedge its exposure to certain foreign exchange risks, the group enters into derivative instruments (see note A5).

## Notes to the financial statements

### A8 Accounting policies (continued)

#### Grants and contributions

Grants and contributions receivable in respect of property, plant and equipment arise from a number of sources including contributions from developers towards the expansion of the water and wastewater network and connection of properties to the network. These grants and contributions are treated as deferred income, which is credited to the income statement over the estimated useful economic lives of the related assets.

#### Leases

At inception of a contract, the group assesses whether a contract is or contains a lease. Where a lease is present, a right-of-use asset and lease liability is recognised at the commencement date. The lease liability is measured at the present value of future lease payments due over the term of the lease, with the right-of-use asset recognised as property, plant and equipment at cost. This is generally equivalent to the initial measurement of the lease liability.

The group has elected to apply a practical expedient permitted by IFRS 16 whereby for the fixtures, fittings, tools and equipment asset class of leases the lease and non-lease components of the contracts are not separated, and are instead both accounted for as if they were a single lease component. Where non-lease components exist they are embedded within the lease payments, and the group deems that separation of such contracts into their constituent parts for this asset class would generally not be practicable nor have a material effect on the financial statements. IFRS 16 requires that where this practical expedient is applied, it is applied to the entire class of similar assets. The group has not applied this expedient to the remaining lease asset classes. Non-lease components include service charges, maintenance charges, and monitoring charges. For lease asset classes where the expedient has not been applied, non-lease components are excluded from the projection of future lease payments and are recorded separately within operating costs on a straight-line basis.

The lease payments are discounted using the group's incremental rate of borrowing if the interest rate implicit in the lease cannot be readily determined. For materially all of the group's leases, the group's incremental rate of borrowing is used. This rate is calculated using a number of inputs, being observable risk-free gilt rates, specific data based on bonds already in circulation for the relevant group company as well as data from the wider utility sector. Further adjustments for payment profile and the term of the lease are made.

After the commencement date, the lease liability is increased for the accretion of interest (being the unwinding of the discounting applied to future lease payments) and reduced by lease payments made. In addition to this, the carrying amount is updated to reflect any remeasurement or lease modifications. Remeasurements are typically required as a result of rent reviews or changes to the lease term. In these cases a corresponding adjustment to the right-of-use asset is made.

Depreciation of right-of-use assets is charged on a straight-line basis over the term of the lease. Lease payments are instead charged to the income statement on a straight-line basis over the period of the lease.

Where leases have a term of less than 12 months from the commencement date and do not have a purchase option, the group applies the short-term lease recognition exemption available under IFRS 16. The group applies the low value recognition exemption permitted by the standard to leases of assets with a value of less than £2,500. Payments for short-term and low value leases are instead charged to operating costs on a straight-line basis over the period of the lease.

## Notes to the financial statements

### A8 Accounting policies (continued)

#### Statement of cash flows

##### *Grants and contributions received*

Grants and contributions received arise from transactions with customers, typically property developers, that result in the expansion of the group's water and wastewater network and therefore its fixed asset base. Given that these grants and contributions are used to fund expenditure that results in the enhancement of the group's network assets, the cash inflows are classified within investing activities in the period.

##### *Interest payments and receipts*

IFRS allows interest payments and interest receipts to be classified within operating activities or financing activities/investing activities. The group classifies interest payments and interest receipts within operating activities, with management viewing these in conjunction with other operating cash flows in assessing the ability of the group to maintain its operating capability.

##### *Support costs*

Costs of time and resources incurred by the group's support functions that is capitalised in the period (see page 162) is included in purchase of property, plant and equipment within investing activities. These cash flows represent expenditures that have been made for resources intended to generate future income and cash flows, and the group deem these to therefore meet the definition of an investing activity.

##### *Cash flows on derivatives*

The cash flows on derivatives as a result of the group's hedging activities are presented together with the cash flows relating to the underlying hedged item to provide a more faithful representation of the substance of the transaction.

##### *Taxes paid*

Taxes paid by the group are presented as cash flows from operating activities. The group deem it impracticable to identify the tax cash flows with respect to individual transactions, which may themselves be presented in investing activities or financing activities, and instead present total tax cash flows as operating activities.

##### *Dividend receipts*

Dividends received from joint ventures have been presented in investing activities, with these cash receipts deemed to represent a return on investments previously made by the group.